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Community Associations and Corporate Newsletter

Foreclosures: What are an Association's Options?

By: Luke A. McQueen and R.A. Hurley

Foreclosure of a home or unit is an option for recovering assessments. The laws governing foreclosure options have evolved and been tweaked by legislatures over the last few years. Here is a quick survey of foreclosure options in the various jurisdictions.

Maryland: Sheriff's Sales

Maryland associations have a powerful tool for enforcing money judgments known as a sheriff's sale. Even though the sheriff's sale is inexpensive and effective, it remains one of the most underutilized options for enforcing a judgment. We often advise our clients to pursue this option when the other options have failed.

A sheriff's sale is a type of foreclosure that is available to judgment creditors. The sheriff has the power to seize a judgment debtor's property and can sell a piece of real estate owned by a judgment debtor and give the judgment creditor a share of the sale proceeds up to the amount of the judgment. Often, owners who face the threat of a sheriff's sale come forward to pay the judgment balance immediately so they can keep the property.

An association can only satisfy one judgment through the sale, even if it has more than one judgment against an owner. However, it may be able to satisfy other judgments and liens afterward, by applying to the court for any surplus proceeds of sale.

The process starts by first obtaining a writ from the court which tells the sheriff to notify the owner that a sheriff sale may be scheduled soon. Then the association coordinates the sale with the sheriff. The sale literally happens on the courthouse steps. The timeframe varies from county to county, but in general, the process takes between two to four months.

DC: The Quickly Evolving Law of Condominium Lien Foreclosure

The DC Condominium Act provides that each unit owner's obligation to pay the assessment is secured automatically by a lien that attaches to the unit.

The lien can be enforced through a lawsuit seeking the court's permission to foreclose on it, or it can be enforced by scheduling a foreclosure sale of the unit without getting the court involved.

“Superpriority” liens

A portion of the condominium lien—the last six months of the assessment—enjoys “superpriority” status over other liens on the property, even the mortgage. For years, the state of the law in DC made condominiums very powerful and put the mortgage lenders at their mercy. A line of court cases held that a foreclosure on the superpriority lien could wipe out the mortgage itself. For that reason, condominiums had no trouble attracting bidders at the foreclosure sale, and mortgage lenders would routinely pay off the condominium to cancel the sale and protect their investment.

That all changed in October 2022, when a federal court issued a decision in a case known as *M&T Bank v. Brown* in which it held that mortgages securing home loans backed by Fannie Mae and Freddie Mac could not be wiped out by a DC condominium foreclosure sale.

Even though the mortgage on a home is a public record, it can be unclear whether the loan is backed by Fannie or Freddie. But such loans constitute between 60% to 70% of all home loans nationwide, so more likely than not, any given mortgage on a DC condominium unit is protected because of the ruling in *M&T Bank v. Brown*.

Since it may not be possible to determine whether a mortgage is protected from the superpriority rule before scheduling a foreclosure sale, unit owners associations need to be prepared for two scenarios: one, the superpriority lien, if not paid before the sale, will result in extinguishment of the first

trust mortgage, or two, the foreclosure sale will be subject to the first trust, which may make it harder to sell the property.

VIRGINIA: JUDICIAL SALES ARE (almost) BACK

Virginia has a slightly different system of foreclosure from Maryland, but there are many common points. For instance, like Maryland, Virginia has sales that are auctions on the courthouse steps – however, these are usually based on statutory liens and not judgments. Judgments can be satisfied through a foreclosure in Virginia as well; however, this is most commonly done through a court approved, or judicial, sale.

Following legislative changes in 2021 that made it harder for a homeowners or unit owners association to judicially foreclose on a principal residence to satisfy a judgment, many associations pivoted to pursuing courthouse step auctions based on statutory liens. However, in this session the legislature has created an exception to exempt associations from the \$25,000 minimum judgment to conduct a judicial sale.

The General Assembly also raised the minimum lien amount for an auction in the same legislation. As of July 1, 2024, both judicial foreclosure and lien auctions must exceed \$5,000 being secured by liens or judgments, as applicable.

This is a welcome result for homeowners and condominium unit owners associations, as these statutory changes provide much more flexibility in pursuing delinquent assessments.

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COMMON RISKS

There are risks to pursuing any type of foreclosure. The owner may file suit against the association to challenge its claim, and while such a suit would be without merit, it could cost the association both time and money to resolve.

Additionally, the threat of a foreclosure may prompt an owner to file bankruptcy, which would halt the sale proceedings. After incurring the time and expense of the foreclosure process, this result is disappointing, but it is a risk of which associations need to be aware.

Finally, the property may be encumbered with significant tax debt or a large mortgage, and the association needs to be prepared in case there are no bidders at the sale. The association's options in such a scenario are to cancel the sale or to bid to try and take ownership of the property. If an association chooses to take ownership to oust the non-paying owner, it can avoid being saddled indefinitely with an owner who does not contribute to the common expenses of the association.

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