

ARTICLE:**A NEW CLASS OF REDEMPTIONERS: THE ENHANCED POSITION OF TENANTS, PROSPECTIVE OWNER OCCUPANTS, AND NONPROFIT OR GOVERNMENTAL ENTITIES IN RESIDENTIAL FORECLOSURES**

*By Karl E. Geier**

The borrower has no post-sale redemption right in California's nonjudicial foreclosure process. This redemption bar has long been justified as a trade-off for the lender's post-sale deficiency bar under Civ. Proc. Code, § 580d. The secured creditor has the option of foreclosing judicially and pursuing a deficiency, which gives the borrower the right to redeem from the sale and preserve the property. Alternately, the secured creditor can foreclose nonjudicially, thereby waiving the right to a deficiency and allowing the purchaser in foreclosure to take possession and control of the property without risk of losing it if the debtor exercises its right of redemption.

Two recent statutory enactments discussed in this article have created rights for tenants, prospective owner occupants, nonprofit entities, and governmental organizations to preemptively purchase or at least have an exclusive period to offer to buy out the position of the prevailing bidder at a nonjudicial sale of one-to-four-unit residential property. While not the same as a redemption right for the borrower, and not as long in duration as the borrower's redemption right following a judicial foreclosure, these provisions undercut the position of a prevailing bidder in the trustee's sale auction, and potentially alter the dynamics of the trustee's sale process for most residential properties. Whether they will affect the lender's calculus in pursuing nonjudicial or judicial foreclosure remains to be seen, but they signal a monumental shift in policy objectives of the statutory scheme—which is no longer focused on assuring the efficacy of secured creditors' remedies but rather on promotion of public or nonprofit control of single-family dwellings in foreclosure.

A. Policy Objectives of the Power of Sale Foreclosure under Prior Law

The California Supreme Court has indicated repeatedly that the overall

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purposes of the nonjudicial foreclosure process are (a) to provide the beneficiary with a quick, inexpensive, and efficient remedy against a defaulting trustor; (b) to protect the trustor from the wrongful loss of the property; and (c) to ensure that a properly conducted sale is final between the parties and conclusive as to a bona fide purchaser.¹ As the Court suggested in *Roseleaf v. Chierighino*, the legislature could have given the debtor a right to redeem from the power of sale foreclosure while preserving the creditor's right to recover a deficiency based on the difference between the amount owed and the amount bid at the sale. Instead, the legislature chose to bar a deficiency altogether while preserving the creditor's right to a prompt recovery on the real property security.²

The net effect of the power of sale foreclosure, it has long been claimed, is to enhance the availability of mortgage financing, due to the relative speed, minimal cost, and finality of the nonjudicial foreclosure process, as well as the prospect for a better price in the event the lender has to foreclose. As a result, there are very few judicial foreclosures in the State of California, especially for single family residential loans. Also, ever since the 2012-2013 amendments to Civ. Proc. Code, § 580b, extended purchase money antideficiency protection to refinances of purchase money loans on one-to-four-unit owner-occupied properties, there has been even less of an incentive for lenders to consider judicial foreclosure of residential loans.

Aside from the implicit trade-off of no deficiency exposure for the borrower and no redemption exposure for the purchaser in foreclosure, there are other presumptive advantages in the real estate mortgage market from the lack of redemption rights for power of sale foreclosures. In a judicial foreclosure, the buyer does not receive clear title until the redemption period has passed, while the borrower has as much as a year to redeem simply by paying the amount of the purchase price, with interest at the legal rate.³ This leaves the foreclosure sale purchaser with potentially a limited return on its investment and a delay in any alternate uses or sale of the property, which reduces the number of willing purchasers in foreclosure and probably depresses the price any such purchaser is willing to pay. By contrast, in a non-judicial foreclosure, the absence of the post-sale right of redemption means the purchaser in foreclosure exercises full ownership, dominion, and control of the property from the time the trustee's deed is recorded, and is assured that it eventually will realize the benefit of its investment. This should, at least in theory, increase the attractiveness of the property for prospective purchasers and increase the price such a purchaser will

be willing to bid at the sale, which should, in turn, encourage lenders to make loans secured by such properties.

As should be clear from the foregoing description, the overall policy objectives and benefits of the power of sale foreclosure process as articulated in the case law is to facilitate mortgage lending and thereby enhance the availability of mortgage loans for residential and nonresidential borrowers. Until recently, there has been essentially no effort to advance a particular public policy agenda through governmental or nonprofit participation in the foreclosure process or to specifically address the interests of residential tenants in foreclosure.

Several legislative measures enacted in response to the residential mortgage crisis of 2007-2008 have already undermined one of the presumed benefits of the power of sale foreclosure process—that it is a quick and efficient remedy for the lender that also encourages third party bidders to bid at the sale. The Homeowner Bill of Rights and related federal and state mortgage modification programs imposed a pre-foreclosure process for lenders to discuss “foreclosure prevention alternatives” for residential borrowers in default, including a series of notifications, meetings, and opportunities for delay before the lender could record or pursue a notice of default or notice of sale for such loans.⁴ Along the way, the legislature also created new tenant protections that effectively delayed the right of a trustee’s sale purchaser to take possession of residential property and evict a tenant under a lease executed by the trustor, substantially altering the usual rule that the title of the purchaser in foreclosure relates back to the priority of the deed of trust and “wipes out” intervening interests, including junior leasehold estates.⁵ This was coupled with a requirement that tenants be given notice that property was in foreclosure,⁶ presumably to prevent “rent skimming” by the borrower-trustor who was about to be ousted from ownership of the property and to encourage tenants to exercise their rights to continued possession under their leases.

B. The New Post-Sale Preemptive Purchase Statutes

The previous changes in residential real property foreclosure law stopped short of creating a post-sale redemption right for the borrower and at least preserved the notion that the trustee’s sale purchaser could expect to immediately succeed to title and ownership of the property. While they delayed recovery of possession if the property was occupied by a bona fide tenant, they did not compel the purchaser in foreclosure to risk a loss of ownership, reduced

options for resale or use of the property, and minimal return on investment resulting from the unavoidable statutory redemption period after the sale. Nor did they inject a direct transactional role for governmental or quasi-public nonprofit entities in the foreclosure process or discourage the acquisition of ownership and operation of rental properties by private business entities or investors.

In the past few legislative sessions, however, the legislature for the first time has imposed post-sale limitations on the rights of ownership and control acquired by the prevailing bidder in a trustee's sale with respect to residential property in foreclosure. It has done so by imposing something tantamount to post-sale redemption rights (albeit styled as a preemptive right to purchase for tenants or other prospective "owner occupants" or designated nonprofit organizations or public entities). Two related provisions of law enacted since 2020 allow a favored class of persons to repurchase the property at the prevailing bidder's cost after the foreclosure sale purchaser has "won" the trustee's sale auction by submitting the highest and best cash bid at the sale. These statutes reflect a coordinated effort to shift the emphasis of residential foreclosure from the private financing and ownership of foreclosure properties to public or quasi-public nonprofit acquisition of one-to-four-unit residential properties, despite a stated intention to preserve individual owner-occupancy of such properties.

1. Civil Code Section 2924m—Preemptive Right to Match the Prevailing Bidder's Offer Within Up to 45 Days after the Trustee's Sale

The first new law is Civil Code section 2924m, which initially was adopted in 2020 and has been amended significantly and extended in 2021 and 2022.⁷ This provision allows any tenant of a one-to-four-unit residential property who wishes to purchase and continue occupying the property to bid at the sale, and if that person is the prevailing bidder, to complete the purchase and take title, with the sale being final within one business day of the sale provided the tenant purchaser supplies an affidavit of intended owner occupancy.⁸

But the statute goes much further than giving a tenant occupant the right to bid at the sale. No third party bidder who makes the highest and best bid at the trustee's sale can assume the sale is final until a period of 15 days has elapsed, during which *any prospective owner occupant*, including an eligible tenant or any other person who intends to occupy the property as a primary residence, as well as any nonprofit organization or governmental entity that meets certain standards set forth in the statute, still has an opportunity to "match" the bid of the

prevailing bidder.⁹ Moreover, if an eligible tenant purchaser or nonprofit organization representing the eligible tenant occupants and meeting other criteria specified in the statute, or any of several types of governmental entities, at any time during the 15-day period after the sale, gives notice of intent to make a post-sale preemptive bid, the 15-day period is extended to 45 days, giving the preemptive nonprofit or governmental purchaser the additional 30-day period to raise funds and complete the purchase.¹⁰

(The statute does not use the term “match the bid,” but it merely requires a representative of the eligible tenant bidders to offer a price “equal” to the full amount of the highest and best offer at the trustee’s sale.¹¹ Any other eligible bidder must offer a price that “exceeds” the prevailing bid,¹² which implies that no more than a nominal increase over the prevailing bid at the trustee’s sale will suffice, although other eligible bidders by offering more can become the prevailing purchaser during the same period of time.)

In order to make doubly certain that parties other than the prevailing bidder at the scheduled trustee’s sale have an opportunity to exercise these preemptive purchase rights, the law requires the trustee to publish notice on the trustee’s internet website the details of the prevailing bid and the timeframe and location for submitting a bid or notice of intent to bid.¹³ In other words, it is not necessary for the eligible tenant or other prospective bidder who enjoys the preemptive purchase rights created by the statute to attend or participate in the initial auction of the property at the trustee’s sale; these parties have the right to sit back and see what a prevailing bidder is willing to pay, and then to “match the offer” for 45 days thereafter. In the meantime, the title to the property remains in the original trustor, and only after the 45-day period has elapsed is the title conveyed to the trustee’s sale purchaser.¹⁴

The detailed provisions of section 2924m are clearly designed to facilitate the maintenance of the rental housing stock while substantially minimizing the ability (or desire) of for-profit investors to purchase residential property in foreclosure. In effect, when the initial prevailing bidder at the sale is a private or institutional investor that is not either an eligible tenant, an individual planning to occupy the home as a primary residence, or an eligible nonprofit tenant representative organization or prevailing entity, that prevailing bidder is required to pay the purchase price over to the trustee at the conclusion of the sale,¹⁵ but does not receive a trustee’s deed nor title or possession of the property, and is subject to a mandatory buy-out of their position for up to 45 days without

compensation for the time and expense incurred in attending and bidding at the sale, and without return on any funds deposited with the trustee at conclusion of the sale.¹⁶ In other words, such a purchaser must wait and see whether someone else will take the property off his or her hands “at cost,” with no control or possession of the property in the meantime. And while the statute seems to give priority to existing tenants or other natural persons who are prospective owner-occupants of such properties, the parties with a more realistic chance of making a cash-equivalent post-trustee’s sale bid for the foreclosed property are those nonprofit organizations or public entities that can raise capital and complete the buyout of the prevailing bidder in the relatively short timeframe allowed for such purchasers. In short, the statute may seem to encourage owner-occupancy, but more likely, it facilitates the conversion of privately-owned residential property to public or quasi-public rental housing.

As initially enacted, there was no specific provision in section 2924m that required a nonprofit organization formed to exercise the preemptive purchase rights granted to “eligible bidders” to maintain affordability of rents or resale prices after completing the purchase. That requirement was added in 2022, by the enactment of Civil Code section 2924o, which now requires such an entity (but not a governmental entity, which is excluded from the list of entities required to do so¹⁷), to record affordability covenants that restrict the property for at least 30 years, whether sold or rented; these covenants must require the property, if sold, to be at affordable housing costs for lower income residents, and if rented, to be at affordable rental rates for lower income residents.¹⁸ Whether or not so restricted, and regardless of whether the prevailing purchaser is an eligible bidder under section 2924m, the owner of the property sold in foreclosure must also comply with any applicable laws regarding eviction or displacement of tenants, including notice requirements, requirements for provision of temporary or permanent relocation assistance, the right to return to the premises, and any just cause eviction requirements.¹⁹

The 2022 amendments to the statute also create an avenue for the attorney general of the State of California to intervene in the private power of sale foreclosure process to enforce the post-sale purchase rights of non-profit organizations or governmental entities under the law, as well as those of eligible tenants and other prospective owner occupants, creating new compliance risks for lenders, trustees, and prospective purchasers in the formerly expeditious and final trustee’s sale procedure. Specifically, the state attorney general must be given no-

tice whenever the prevailing bidder, either at the conclusion of the auction or during the 45-day period allowed by the statute, is an eligible tenant purchaser or other prospective owner occupant, or one of the eligible nonprofit organizations or governmental entities listed in the statute,²⁰ and either the state attorney general or any city attorney or district attorney may bring an action to enforce the statute.²¹ Such an action may apparently be brought before or after the initial trustee's sale is conducted or completed, although the statute does not specifically so provide. This represents another departure from traditional power of sale foreclosure procedures in California, creating further opportunities for the advancement of public policy objectives that have nothing to do with the often-stated focus of existing law on the efficiency, finality, and speed of the trustee's sale process.

2. Civil Code Section 2924p—Right of First Offer Within Initial 30 Days of Listing Property for Resale, Coupled with Permanent “Anti-Bundling” Prohibition on Prevailing Bidder at Trustee’s Sale

The second major incursion on the redemption bar in residential nonjudicial foreclosures is Civ. Code, § 2924p, which became effective January 1, 2023.²² Under this statute, whenever a purchaser in foreclosure of a one-to-four-unit property is an “institution,” as defined, that has foreclosed on 175 or more residential real properties containing no more than four dwelling units in the preceding year, the institution is deemed to have acquired the property subject to a preemptive right of first offer on the part of a “prospective owner-occupant.”²³ In such cases, for a period of 30 days after the property is first listed for sale by the institution, it may only accept offers to purchase from “eligible bidders,” and must respond in writing to any “eligible bidder” who submits such an offer during that period, before considering any other offer.²⁴ There are two categories of “eligible bidders”: either the bidder must be a natural person who submits an affidavit that they will occupy the property as their primary residence within 60 days after the trustee's deed is recorded and will remain in occupancy thereafter for at least a year,²⁵ or else it must be a nonprofit entity organized to promote development of affordable rental or for-sale housing, as further specified, a community land trust, or a limited equity housing cooperative, or virtually any public entity in the state of California.²⁶

Unlike section 2924m, this statute (section 2924p) does not impose price restrictions or absolutely require the purchaser in foreclosure to accept an offer

from an “eligible bidder,” but it does prohibit any sale by the prevailing purchaser at the sale during the first 30 days other than to an “eligible bidder.” It also prohibits any “bundled sale” of such properties acquired in foreclosure.²⁷ A “bundled sale” is a sale of two or more parcels improved with one to four residential dwelling units, at least two of which have been acquired in foreclosure under a mortgage or deed of trust.²⁸

The prohibition on “bundled sales” by covered institutions applies to all one-to-four-unit residential properties acquired in foreclosure by the institution, and does not appear limited as to the time of purchase or resale by the institution.²⁹ In substance, the statute has the effect of requiring properties acquired by a higher-volume lender making a credit bid in foreclosure to be sold individually rather than in bulk to investors or other institutions that are in the business of managing portfolios of troubled properties. This is for the stated purpose of allowing owner occupants or qualifying nonprofit or governmental institutions to acquire such properties for rental or resale. (By contrast, there is no restriction in either section 2924m or section 2924p on the number of properties that may be acquired *or resold* by such nonprofit entities, but both statutes generally prohibit the trustor or the trustor’s immediate family members or persons acting for them from exercising the purchase rights as a prospective owner-occupant³⁰).

The institutions that are covered by section 2924p include all depository institutions, whether chartered under state or federal law (i.e., banks and savings institutions), all real estate licensees (i.e., mortgage brokers), and all licensed California finance lenders and licensed residential mortgage lenders, in each case, if they foreclose on 175 or more residential one-to-four-unit properties in an annual reporting period preceding a particular sale.³¹ Properties available for purchase under section 2924p would not be specifically earmarked, and there is no specific mechanism for publicizing specifically the applicability of the preemptive first offer right established by section 2924p on a property by property basis. There is also no explicit provision that would prevent a covered institution from using a nominee, subsidiary, or agent to take ownership of the loan before conducting the sale as successor beneficiary (although that course of action would seem to risk running afoul of the statute).

In any case, the identity of institutions that meet the 175 foreclosures per year threshold can be ascertained from required filings with their regulatory agencies. Likewise, the fact that a property has been acquired in foreclosure by

such an entity, or an entity controlled by or acting for such an entity, including the applicable date of the trustee's sale and identity of the buyer, would be ascertainable from the required posting of information about a trustee's sale auction under section 2924. For those "in the know," which would include, particularly, the types of nonprofit entities and governmental entities that seek to implement the rental or owner-occupied housing retention programs embodied in these laws, the two statutes together provide ample opportunity to exercise these rights. First, during the initial 15 and 45 days after the trustee's sale occurs, the eligible bidders could pursue outright preemptive purchase under section 2924m, and then, once the trustee's sale becomes "final" in the sense that no eligible bidder has exercised the preemptive purchase rights under section 2924m, there would for another 30 days to negotiate a purchase under section 2924p, once the institution who acquired the property in foreclosure, presumably by a credit bid, proceeds to list the property for resale.

C. Practical Effect, Policy Objectives, and Unintended Consequences of Creating Preemptive Rights to Buy Out the Foreclosure Sale Purchaser at Cost

Each of these statutes has been intricately drafted in much greater detail than the above summary would indicate. Since both statutes include provisions intended to preclude the original borrower-trustor from claiming the right to repurchase from the foreclosure sale purchaser, it is not strictly accurate to characterize the statutes as creating "redemption rights." For the same reason, it would not be strictly accurate to call the prospective owner-occupants or other eligible public or nonprofit bidders under either statute "redemptioners." But the practical effects of these statutes on the rights of the prevailing bidder in the initial trustee's sale are analogous to the effects of a redemption right on the part of the borrower, because they initially limit the price and expose the prevailing bidder to preemptive purchase without profit if an eligible bidder exercises its rights under section 2924m, and they further limit the ability of the foreclosing lender to liquidate a portfolio of foreclosure acquisitions in a bulk sale, due to the forced consideration of other offers for 30 days and the flat prohibition on all "bundled sales" for an indefinite period of time under section 2924p.

The policy objectives of the statutes are obvious, and stated in the preamble of section 2924p—they are to maintain availability of the housing stock for rental or owner occupancy, to discourage corporate or for-profit private investor acquisition and control of foreclosed single family homes or one-to-four-unit

residential properties, and to keep foreclosed housing available to prospective tenants and owner occupants or to nonprofit and governmental entities that will preserve availability for tenants and owner occupants.³² Perhaps less obvious, and not directly stated, but still predictable and possibly intended by the sponsors of this legislation, is an inevitable shift of emphasis from private ownership and resale of properties in foreclosure to some combination of public and quasi-public owners and operators of affordable or market-rate rental housing, with increased leverage over private participants in the foreclosure sale and resale process.

Also less obvious is the significant change of policies and legislative objectives that traditionally have been claimed as the undergirding of the power of sale foreclosure process in California. The notion that lenders are encouraged to forego a deficiency and proceed non-judicially in lieu of judicially foreclosing and subjecting themselves, as well as the foreclosure sale purchaser, to an extended redemption period, can no longer be stated as an unqualified virtue of the statutory scheme. Moreover, with the other recent changes in pre-foreclosure requirements mentioned above, the addition of the post-foreclosure preemptive purchase or first offer rights added by sections 2924m and 2924p will significantly affect the “quick, inexpensive, and efficient” attributes of the power of sale foreclosure, as well as the ability of a bona fide purchaser who bids at the foreclosure sale to rely on the absolute right to receive a trustee’s deed conveying title within 45 to 60 days after the sale. These often-recited benefits have always been implicit, and sometimes explicit, underpinnings of the legal analysis of California real property secured transactions and foreclosure jurisprudence.

The changes wrought by sections 2924m and 2924p may not be sufficient to discourage lenders from participating in the California residential mortgage market, but one can speculate there will be other unintended (or at least, unarticulated) consequences for residential foreclosure law as time goes on. Indeed, one wonders how the changes in the essential characteristics of the power of sale foreclosure process and the increased preference for public entity and non-profit organizations as purchasers and owners of foreclosure properties might affect the courts’ analysis of future cases in this area.

ENDNOTES:

¹E.g., *Yvanova v. New Century Mortgage Corp.*, 62 Cal. 4th 919, 926, 199

Cal. Rptr. 3d 66, 365 P.3d 845 (2016); *Biancalana v. T.D. Service Co.*, 56 Cal. 4th 807, 813-814, 156 Cal. Rptr. 3d 437, 300 P.3d 518 (2013).

²*Roseleaf Corp. v. Chierighino*, 59 Cal. 2d 35, 42, 27 Cal. Rptr. 873, 378 P.2d 97 (1963).

³Civ. Proc. Code, §§ 729.030, 729.050, 729.060.

⁴See discussion in 5 Miller & Starr, California Real Estate 4th, §§ 13:181 to 13:185.

⁵Civ. Proc. Code, § 1161b.

⁶Civ. Code, § 2924.8. (The initial provision requiring the trustor to provide the notice, Civ. Code, § 2924.85, lapsed in 2018, and the current provision, Civ. Code, § 2924.8, requiring the trustee to provide the notice, was enacted in 2020).

⁷See 2020 Stats., ch. 202 (SB 1079), § 7; 2021 Stats., ch. 255 (AB 175), § 2; 2022 Stats., ch. 642 (AB 1837), § 9.

⁸Civ. Code, § 2924m, subd. (c)(1).

⁹Civ. Code, § 2924m, subd. (c)(2).

¹⁰Civ. Code, § 2924m, subds. (c)(3), (c)(4).

¹¹Civ. Code, § 2924m, subd. (c)(3).

¹²Civ. Code, § 2924m, subd. (c)(4).

¹³Civ. Code, § 2924m, subd. (e).

¹⁴Civ. Code, § 2924m, subd. (f).

¹⁵See Civ. Code, § 2924h, subd. (b).

¹⁶See Civ. Code, § 2924m, subds. (f), (h).

¹⁷See Civ. Code, § 2924o, subds. (a), (b), referring only to the entities described in clauses (C) through (G), but not (H), in Civ. Code, § 2924m, subd. (a)(3); clause (H) is the list of eligible governmental entities, which include “the state, the Regents of the University of California, a county, city, district, public authority, or public agency, or any other political subdivision or public corporation in the state”.

¹⁸Civ. Code, § 2924o.

¹⁹Civ. Code, § 2924n.

²⁰Civ. Code, § 2924m, subd. (i).

²¹Civ. Code, § 2924m, subd. (j).

²²See 2022 Stats., ch. 865 (AB 2170), § 1.

²³Civ. Code, § 2924p, subds. (b)(3), (c).

²⁴Civ. Code, § 2924p, subds. (c)(1), (c)(4).

²⁵Civ. Code, § 2924p, subd. (b)(4).

²⁶Civ. Code, § 2924p, subd. (b)(2).

²⁷Civ. Code, § 2924p, subd. (c)(5).

²⁸Civ. Code, § 2924p, subd. (b)(1).

²⁹Civ. Code, § 2924p, subd. (c)(5).

³⁰Civ. Code, §§ 2924m, subd. (a)(1), 2924p, subd. (b)(4)(C).

³¹Civ. Code, § 2924p, subd. (b)(3).

³²See Civ. Code, § 2924p, subd. (a).