

# Real Estate Update

## The "E-Word" – E-mail

In order to provide more timely information on current real estate topics, we will soon be transitioning to an all E-mail Real Estate Update. We are sending this Update by both E-mail and snail-

mail. If you did not receive this by E-mail and would like to continue to get the Updates, please send us an E-mail at [realestate@scblaw.com](mailto:realestate@scblaw.com). Please put "Real Estate Update" in the subject line.

## The "F-Word" – Foreclosure

*Plunging stock market! Bank failures! Fannie Mae and Freddie Mac scandals! Bailout programs!*

The turmoil of the last two months has made us all very nervous, both as homeowners and also as commercial real estate investors. These are financially uncertain times. What should you do if you carried seller financing or have loaned money secured by real estate and the payments are late?

No one yet knows exactly what the Treasury Secretary will do with his new bail-out authority. Until we do, the prudent lender will keep all options open. This includes foreclosure.

### What To Do?

You need to act right away. The first thing to do is give the borrower formal notice that the failure to timely pay is a breach of the loan documents. Even if you think the borrower will eventually pay or you are negotiating a workout, sending notice preserves your rights, shortens the time to foreclosure, and gives you more flexibility.

### Alternative Remedies

Unless the property is agricultural, the loan is most likely secured by a deed of trust. A deed of trust is

a three-party contract among the beneficiary (lender), the grantor (borrower), and a trustee.

In Washington, a lender can exercise one of three remedies for a deed of trust default:

- sue the borrower on the promissory note,
- judicial foreclosure, or
- nonjudicial foreclosure.



There are pros and cons to each option.

### Judicial Foreclosure

With judicial foreclosure, the lender must file a lawsuit joining in everyone who has a lien or any other interest in the property. This litigation can take 18-24 months to complete, and the debtor can raise defenses. If successful, the court then orders the Sheriff to sell the property at auction. The title the buyer receives at the Sheriff's sale is subject to the borrower's right to redeem the property within 12 months by paying the purchase price. This makes title uncertain. On the other hand, if the sale proceeds do not fully pay the obligation, the lender can obtain a "deficiency judgment" against the borrower personally for the balance.

## Nonjudicial Foreclosure

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Nonjudicial foreclosure is a simpler and generally a quicker and cheaper process. There is no lawsuit. The beneficiary notifies the trustee that the grantor is in default and orders the trustee to sell the property at auction. There are strict procedures and time periods the trustee must follow, and the sale can occur no sooner than 190 days after the default occurred.

Once the trustee's sale has occurred, it is final – the owner cannot redeem the property.

The flip side is that the lender normally cannot obtain a deficiency judgment; *i.e.*, recovery is limited to obtaining the property or the proceeds of the sale. The beneficiary can (and nearly always will) bid in the amount

owing at the sale, so that if there are no other bidders, the lender acquires the property. However, there is an exception for certain commercial loans (*i.e.*, not owner-occupied residential property) that may permit a deficiency judgment.

In addition, a lender is not precluded from suing for a judgment for the deficiency against any guarantor of the loan.

## Suit on the Note

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If the note is secured by a second or lower priority lien and a senior lien holder forecloses, the junior lien is extinguished. In that case, the only option left is to sue on the note.

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In most cases, lenders will elect nonjudicial foreclosure. But whatever option is best in your situation, you should get advice

early in the process so that you can make well-informed decisions.



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