

MINNESOTA REAL ESTATE FORECLOSURES: 21 COMMON QUESTIONS & ANSWERS

Our Creditors' Remedies attorneys answer the most asked questions from their clients.

Practice Area:

**CREDITORS' REMEDIES,
BANKRUPTCY & WORK-OUT**

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1. WHAT HAPPENS AT A REAL ESTATE FORECLOSURE SALE?

The sheriff of the county where the real estate is located reads the published Notice of Foreclosure Sale; solicits bids; and then issues to the highest bidder a Sheriff's Certificate of Sale (if foreclosure by advertisement) or a Sheriff's Report of Sale (if foreclosure by action). In foreclosure by action, following issuance of the Sheriff's Report of Sale, the court is moved to confirm the sale. If confirmed, the sheriff then issues the Sheriff's Certificate of Sale.

2. WHO CAN BID AT A FORECLOSURE SALE?

Anyone. However, because of Minnesota's redemption rules, it is rare for anyone other than the foreclosing creditor to bid at a foreclosure sale. In almost all cases, the highest bidder is the foreclosing creditor.

3. DOES THE FORECLOSING CREDITOR NEED TO BRING CASH TO THE FORECLOSURE SALE? WHAT ABOUT OTHER BIDDERS?

No. The foreclosing creditor may "credit bid" all or some of the debt secured by the mortgage. The mortgage debt is satisfied or partially satisfied by the amount of the foreclosing creditor's bid. Accordingly, the foreclosing creditor should carefully consider the value of its collateral and other potential sources of recovery (including guarantors and other collateral) before attending the sale. Any other party who bids at the sheriff's sale must bid with cash or certified funds.

4. WHAT DOES THE HIGHEST BIDDER AT A SHERIFF'S SALE ACQUIRE?

The highest bidder at the sale acquires ownership of the mortgage property, subject to: (i) existing reservations, restrictions and easements of record, if any; (ii) any prior liens (including any unpaid real estate taxes and assessments, which are always first priority liens); (iii) the owner's redemption rights; and (iv) the redemption rights of junior lienholders who timely file a notice of intention to redeem.

5. WHAT ARE THE REDEMPTION RIGHTS OF THE OWNER OF THE FORECLOSED PROPERTY?

The owner of the foreclosed property generally has two significant rights during the redemption period. First, unless a receiver is appointed over the property, the

owner retains all incidents of ownership during the redemption period, including the rights of occupancy and use, and the right to collect any rents and profits generated by the property. Second, any time during the redemption period (see answer to Question 11), the owner may “redeem” (or re acquire) full title to the foreclosed property by paying the holder of the Sheriff’s Certificate (usually, the foreclosing creditor) an amount equal to the amount bid at the sale, plus interest accruing after the date of sale, plus certain costs and expenses (including reasonable attorneys’ fees, subject to a cap in foreclosures by advertisement) accruing after the date of the sale (the “Redemption Price”).

6. WHAT HAPPENS IF THE OWNER OF THE FORECLOSED PROPERTY REDEEMS?

If the owner redeems, the rights existing under the Sheriff’s Certificate of Sale are extinguished and any junior liens against the foreclosed property are “revived” as though there had been no foreclosure sale. The owner is given a Certificate of Redemption at the time of redemption, which is filed with the real estate records and serves as record notice of the redemption.

7. WHAT HAPPENS IF THE OWNER OF THE FORECLOSED PROPERTY DOES NOT REDEEM AND THERE ARE NO JUNIOR LIENS AGAINST THE PROPERTY?

If the owner does not redeem during the owner’s redemption period, then the foreclosing creditor (or the holder of the Sheriff’s Certificate) becomes the fee owner of the foreclosed property: (i) free and clear of the foreclosed mortgage; (ii) free and clear of any interest of the mortgagor; and (iii) subject to any prior mortgages or liens. Except for certain agricultural properties, the holder of the Sheriff’s Certificate is then free to hold or dispose of the property in any manner. Generally, the foreclosing party will market and sell the property. When dealing with Torrens property, the holder of the Sheriff’s Certificate should go through a “proceeding subsequent,” a legal proceeding which causes the Registrar of Titles to cancel the existing owner’s Certificate of Title and issue a new owner’s Certificate of Title in the name of the new owner.

8. WHAT KIND OF REDEMPTION RIGHTS DOES A JUNIOR LIENHOLDER HAVE?

Any junior lienholder who wants to redeem must record and file a Notice of Intention to Redeem at least one week before the owner’s redemption period expires. If the owner does not redeem, then the highest priority junior lienholder who has timely filed a Notice of Intention to Redeem has seven days to redeem (or buy) the foreclosed property by paying the Redemption Price to the holder of the Sheriff’s Certificate. A redeeming party may redeem through the Sheriff’s Department or directly through the holder of the Sheriff’s Certificate. The redeeming party receives a Certificate of Redemption. Once the junior lienholder redeems, it becomes the fee owner of the foreclosed property: (i) free and clear of the mortgagor’s rights in the property; and (ii) free and clear of the foreclosing creditor’s rights; but (iii) subject to the redemption rights of any junior lienholders; and (iv) subject to any liens which were superior to the foreclosed mortgage.

9. HOW DO THE REDEMPTION RULES WORK IF THERE ARE MULTIPLE JUNIOR LIENHOLDERS?

Each junior lienholder’s redemption rights are determined by the priority of their liens. If it has timely filed a Notice of Intention to Redeem and the owner does not redeem, the first junior lienholder has the

first seven day option to redeem the property from the holder of the Sheriff's Certificate by paying the Redemption Price. Any subsequent junior lienholder who has timely filed a Notice of Intent to Redeem then has (in the order of their priority) successive seven day periods to redeem from the lienholder by paying the prior redeeming creditor an amount (roughly) equal to the Redemption Price, plus the amount due on any prior redeeming mortgage.

10. WHAT HAPPENS TO PRIOR MORTGAGES AND LIENS IF A JUNIOR MORTGAGE IS FORECLOSED?

Senior mortgages and liens "ride through" a foreclosure sale conducted by a junior lienholder. As a result, any party buying real estate at a foreclosure sale will acquire the property subject to the prior liens. After acquiring the property through foreclosure, the new owner may, but is not required to, pay off the prior liens. If the prior liens are not paid, then the prior lienholders would likely proceed with their own foreclosure sale.

11. HOW LONG IS THE OWNER'S REDEMPTION PERIOD?

In most cases, the owner's redemption period is six months. The owner has a longer, 12 month redemption period in certain circumstances, including where: (i) the original principal amount of the mortgage debt has been paid down by a third or more; (ii) the mortgaged property is more than 10 acres but less than 40 acres and was "in agricultural use" when the mortgage was signed (and the mortgagor did not waive the 12 month redemption period); or (iii) the land is more than 40 acres in size.

In certain limited circumstances, the redemption period can be reduced to two months or five weeks. After a mortgage has been in default for at least 30 days, the mortgagor and the lender can agree to a reduced two month redemption period under a voluntary foreclosure agreement ("VFA"), which is discussed in more detail in the answer to Question 20. In certain cases involving abandoned residential properties, the redemption period can be reduced to five weeks. (Five week redemption periods are discussed further in the answer to Question 21.)

12. DO JUNIOR LIENHOLDERS RECEIVE NOTICE OF A FORECLOSURE SALE BY A SENIOR LIENHOLDER?

If the senior lienholder forecloses by action (by starting a lawsuit), it should name any junior lienholders as defendants in the lawsuit. A junior lienholder in a foreclosure by action should receive notice that a foreclosure proceeding has started when it is served with the summons and complaint. The junior lienholder should then monitor the progress of the foreclosure proceedings and remain apprised of significant events and deadlines, including any lien priority issues, the date of the foreclosure sale, the redemption deadlines, and the deadlines for filing a Notice of Intent to Redeem.

If the senior lienholder forecloses by advertisement, it is not generally required to provide junior lienholders with notice of the foreclosure sale. As a result, a foreclosure sale could occur without the knowledge of the junior lienholder, and the junior lienholder could lose its mortgage and redemption rights. To prevent this, junior lienholders should always file a Request for Notice of a Mortgage Foreclosure by Advertisement in the appropriate county real estate offices (Torrens or Abstract) when

taking a junior lien against the property. If the Request for Notice is filed before the senior foreclosing lienholder files a Notice of Pendency, the senior lienholder must provide the junior lienholder with notice of the foreclosure by advertisement. Senior lienholders customarily provide junior lienholders with notice of a foreclosure by advertisement, even though they are not required to do so. However, a junior lienholder should always file a Request for Notice to make sure its rights are protected.

13. WHAT IS A DEFICIENCY CLAIM?

Deficiency claims come into play when the collateral is worth less than the debt secured by the mortgage. When the lender “credit bids” at the foreclosure sale, it reduces the mortgage debt by the amount bid. If the lender bids the full amount of the debt, there is no deficiency. If the lender bids less than the mortgage debt, then the “deficiency” is the difference between the amount bid and the mortgage debt. It is important to remember that the deficiency is not determined by what the lender ultimately receives on disposition of the property. By way of example, a lender who: (i) is owed \$1 million; (ii) bids \$1 million at the foreclosure sale; and (iii) after the expiration of the redemption period sells the property for \$500,000 does not have a \$500,000 deficiency claim even though the lender has experienced a \$500,000 loss. Instead, the lender in this example has no deficiency claim because it bid the full amount of the mortgage debt at the foreclosure sale.

14. DOES MINNESOTA HAVE AN ANTI-DEFICIENCY STATUTE?

Yes. Under Minnesota’s “anti deficiency statute,” the lender may not pursue a deficiency against the mortgagor if: (i) the lender forecloses by advertisement (instead of by action); and (ii) the owner’s redemption period is six months or less. So in most cases, the lender cannot recover a deficiency against the mortgagor if the lender forecloses by advertisement. Accordingly, if the mortgaged property is worth less than the mortgage debt, the foreclosing creditor will often foreclose by action in order to preserve a deficiency claim against the mortgagor, unless the mortgagor has no other assets with which to satisfy a deficiency claim.

15. DOES MINNESOTA’S ANTI-DEFICIENCY STATUTE PROTECT GUARANTORS?

Under current published case law no. Current published case law provides that a lender may foreclose by advertisement and still pursue guarantors (who are not also the mortgagor) for recovery of any deficiency claim. See, e.g., *Nat’l City Bank of Minneapolis v. Lundgren*, 435 N.W.2d 588, 591–93 (Minn. Ct. App. 1989); see also *Ed Herman & Sons v. Russell*, 535 N.W.2d 803, 806 (Minn. 1995) (“Minnesota courts have found that guarantors are not protected by anti-deficiency statutes.”).

16. WHAT ARE REINSTATEMENT RIGHTS?

When an unmaturing installment note goes into default, virtually all promissory notes or loan agreements allow the lender to “accelerate” the note, at which point the installment feature of the note goes away and the entire loan becomes immediately due and payable. Minnesota’s “reinstatement” statute, which is designed

to protect borrowers, permits borrowers to stop the foreclosure of the mortgage by “curing” defaults any time before the Sheriff’s sale. The right of reinstatement is unique to the foreclosure of real estate mortgages. Generally, borrowers do not have a right to “cure” loan defaults after they have defaulted and the lender has accelerated the loans. Reinstatement does not apply to loans which have matured.

17. WHAT IS A FORECLOSURE BY ADVERTISEMENT AND HOW LONG DOES IT TAKE?

Virtually all mortgages signed in Minnesota contain a “power of sale” clause, which entitles the mortgagee, at its option, to foreclose the mortgage by advertisement. Although there are many technical requirements and deadlines, a foreclosure by advertisement is generally conducted by publishing a notice of the time, date and place of the foreclosure sale in a legal publication for six consecutive weeks. The actual sale typically takes place about eight weeks after the Notice of Pendency is recorded. The sale is followed by a redemption period, which is usually six months. Accordingly, assuming there is no bankruptcy filing, a typical foreclosure by advertisement (including the typical six month redemption period) generally takes around eight to nine months.

18. WHAT IS A FORECLOSURE BY ACTION AND HOW LONG DOES IT TAKE?

Instead of foreclosing by advertisement, a lender may foreclose by action. To foreclose by action, the mortgagee must commence a lawsuit in the county where the mortgaged property is located, and sue everyone with a lien or interest in the property which is junior to the mortgage being foreclosed, including: (i) owners of the property; (ii) junior lienholders; and (iii) in appropriate cases, tenants and other occupants. Before a foreclosure sale can occur, the foreclosing party must obtain a decree of foreclosure from the court. To obtain a decree of foreclosure, the foreclosing party must “win” the lawsuit. Generally, a party can win a lawsuit in one of four ways: (i) by default judgment (when the defendant fails to answer the complaint or defend the lawsuit); (ii) by summary judgment (if there are no disputed issues of material fact and the lender is entitled to judgment as a matter of law); (iii) after a trial; or (iv) pursuant to a written agreement. From a timing perspective: (i) default judgments are entered relatively fast, usually within a month to six weeks after the service of the complaint; (ii) summary judgment takes longer (difficult to predict, but typically within two to five months after the service of the complaint); (iii) trials generally take a year or more to conclude; and (iv) judgments pursuant to agreements are entered under any timeline to which the parties agree.

A foreclosure by action is not completed when the court enters a decree of foreclosure. The decree of foreclosure only permits the lender to proceed with publication of the foreclosure sale, a publication process that resembles the six weeks of successive publication used in foreclosures by advertisement. Then, after the foreclosure sale is conducted, the party conducting the foreclosure sale must go back to the court and ask the court to enter an order confirming the sale. In a foreclosure by action, the redemption period does not start running until the date the court enters an order confirming the sale. Once the sale is confirmed, the sheriff will issue the Sheriff’s Certificate.

For obvious reasons, a foreclosure by action can take considerably longer than a foreclosure by advertisement and can also be considerably more expensive. A “fast” foreclosure by action (where the matter proceeds by default) will usually add only a month or two to the foreclosure process. A foreclosure by action which proceeds by summary judgment can easily add two to five months to the process. Cases which proceed to trial can add considerably more time to the process because it generally takes a year or so before a trial can occur.

19. WHY WOULD A LENDER FORECLOSE BY ACTION IF FORECLOSURE BY ADVERTISEMENT IS GENERALLY FASTER AND MORE COST EFFECTIVE?

Most residential mortgages in Minnesota are foreclosed by advertisement. However, many mortgages secured by commercial properties are foreclosed by action. There are several reasons why many commercial mortgages are foreclosed by action. First, the lender may want to maintain a deficiency against the mortgagor, which usually cannot be done in a foreclosure by advertisement. Second, there may be title issues which need to be resolved by a court order. Third, loans secured by commercial mortgages are often guaranteed by one or more guarantors and are often secured by other collateral, including non-real estate collateral. When foreclosing by advertisement, the lender cannot commence another action (such as: (i) an action for claim and delivery to acquire possession of personal property serving as collateral; or (ii) a collection suit against a guarantor to recover a deficiency) until after the foreclosure sale is conducted. Uncertainty regarding collateral values and uncertainty regarding the ability to collect from guarantors, together with a desire to bring all parties and sources of recovery into play, often cause a lender on a commercial loan to pursue foreclosure by action, unless the lender is fully secured by the real estate or the mortgaged real estate is the only real source of recovery.

20. WHEN CAN A LENDER NEGOTIATE A VOLUNTARY FORECLOSURE AGREEMENT WITH A SHORTENED TWO-MONTH REDEMPTION PERIOD?

VFAs (or voluntary foreclosure agreements) are an option if: (i) the property is neither homestead nor agricultural; (ii) at least one of the defaults has existed for at least one month; (iii) the mortgage was executed on or after August 1, 1993; (iv) the mortgagee is willing to waive a deficiency claim against the mortgagor; (v) the mortgagor is willing to give the lender possession of the property or consent to the appointment of a receiver; (vi) the mortgagor is willing to waive its right to surplus sale proceeds, to contest foreclosure, and to rents and occupancy from the date of the VFA through the redemption period; and (vii) the mortgagor is agreeable to a two month redemption period. The obvious benefit of a VFA is the two month redemption period. Also, the publication period is reduced to four weeks from six weeks, for a typical time savings of nearly five months.

21. WHEN CAN A LENDER TAKE ADVANTAGE OF THE REDUCED FIVE WEEK REDEMPTION PERIOD FOR ABANDONED RESIDENTIAL PROPERTIES?

The redemption period may be reduced by court order to five weeks if: (i) the mortgage was executed after December 31, 1989; (ii) there has been a default in the payment of money existing for at least 60 days; (iii)

the property is 10 acres or less in size; (iv) the property is improved with a residential dwelling consisting of less than five units; (v) the dwelling is not a model home; (vi) the dwelling is not under construction; (vii) the property is not used in agricultural production; and (viii) the mortgaged property has been abandoned. Prima facie evidence of abandonment may be established by an affidavit by an appropriate municipal or county official stating that the mortgaged premises are not actually occupied and any of the following:

- (1) windows or entrances to the premises are boarded up or closed off, or multiple window panes are broken and unrepaired; (2) doors to the premises are smashed through, broken off, unhinged, or continuously unlocked; (3) gas, electric, or water service to the premises has been terminated; (4) rubbish, trash, or debris has accumulated on the mortgaged premises; (5) the police or sheriff's office has received at least two reports of trespassers on the premises, or of vandalism or other illegal acts being committed on the premises; or (6) the premises are deteriorating and are either below or are in imminent danger of falling below minimum community standards for public safety and sanitation.

A certified copy of the court's order reducing the redemption period to five weeks may be, but is not required to be, recorded with the county recorder or registrar of titles, as applicable.

For more information on foreclosures and other creditors' remedies questions, contact our bankruptcy attorneys:



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