



FINANCIAL SERVICES LITIGATION BULLETIN

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Foreclosing Lenders Beware

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A new decision from recently appointed bankruptcy judge Mark S. Wallace should be of serious concern to lenders foreclosing non-judicially. Judge Wallace, who sits in the Santa Ana division of the U.S. Bankruptcy Court for the Central District of California, ruled that a pre-petition trustee's sale can be voided by a bankruptcy filed before the execution of the trustee's deed upon sale. The case, *In re Gonzalez*, 201 Bank.LEXIS 2892, was decided in August 2011.

In *Gonzalez*, the borrower was a homeowner whose house was encumbered by a loan in favor of OneWest Bank FSB. OneWest, through Quality Loan Service Corp., as trustee, conducted a non-judicial foreclosure sale. A third party called Rancho Horizon was the successful bidder. While testimony varied, it was undisputed that the sale was concluded no later than 1:27 p.m. on February 22, 2010. Gonzalez, the borrower and homeowner, filed his bankruptcy petition at 1:46 p.m. the same day. Three days later, on February 25, 2011, the trustee (Quality Loan Service) executed the trustee's deed upon sale. It was recorded with the Riverside County Recorder's office on March 2, 2011.



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The buyer, Rancho Horizon, then sought annulment of the automatic stay to complete an unlawful detainer action against Gonzalez, which had been filed without knowledge of Gonzalez's pending Chapter 7. The Bankruptcy Court denied the motion, finding that Rancho Horizon did not acquire title to the property. This was because the trustee's deed upon sale was void due to the intervening bankruptcy petition. The Court was not deterred by California Civil Code Section 2924h, which deems a trustee's sale to be "final" upon the acceptance of the last and highest bid and deems the sale perfected as of 8:00 a.m. on the actual date of the sale (i.e., before Gonzalez's bankruptcy was filed) so long as the trustee's deed upon sale is recorded within 15 days thereafter. The Court held instead that the post-petition transfer of the deed violated the automatic stay, was void *ab initio* and thus its recordation was similarly ineffective. The recordation of a void deed cannot relate back to the time and date of the sale, reasoned the Court.

At best, this decision will force lenders to hasten the recordation of trustee's deeds upon sale. At worst, this decision will introduce uncertainty into the law, disagreeing, as it does, with at least two prior published California bankruptcy court decisions - *In re Engels*, 193 B.R. 23 (Bankr.S.D.Cal. 1996) and *In re Garner*, 208 B.R. 698 (Bankr.N.D.Cal. 1997). In either event, the resulting uncertainty may affect competitive bidding at non-judicial foreclosure sales.

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