

When Is A Trustee's Sale Really "Final"?

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I. Introduction

The threat of a borrower's bankruptcy always hangs over lenders' attempts to foreclose on real property. But until now, lenders have become accustomed to believing that once the gavel comes down, the threat of bankruptcy has been eliminated. A recent decision by the Bankruptcy Court for the Central District of California throws that belief into doubt.

In *In re Gonzalez*,¹ Judge Mark S. Wallace held that a borrower's bankruptcy petition can void a trustee's sale even if the petition is filed *after* the trustee's sale has been completed, as long as the borrower files before the execution of the trustee's deed upon sale. The *Gonzalez* decision is not binding precedent on any other court, but it is a wake-up call to California lenders, foreclosure sale bidders, and trustees that a trustee's deed should be recorded as quickly as possible after any sale, and that further legislative action may be needed to clarify California's trustee sale statutes.

II. The Gonzalez Decision

In *Gonzalez*, the borrower pledged a house in Riverside as collateral for a loan, and defaulted. A lender conducted a non-judicial foreclosure sale, and a third party was the successful bidder, paying \$167,000 for the house. Later that same day, the borrower filed a Chapter 7 petition. The foreclosure trustee then issued a trustee's deed in favor of the third-party purchaser, and the deed was recorded several days later. The borrower refused to vacate the residence, and the purchaser filed a motion for relief from the automatic stay in order to evict him. The purchaser took the position that the deed issued by the foreclosure trustee was valid notwithstanding the fact that the borrower filed a bankruptcy petition before the deed was recorded, because the deed "related back" to the moment of the foreclosure sale under California Civil Code §2924h(c).

The Bankruptcy Court denied the motion. Disagreeing with several earlier California bankruptcy court opinions,² the Court held that the "relation back" portion of the California statute was not sufficient to save the post-petition issuance of the trustee's deed from invalidity. The Court reasoned that the statute did not expressly abrogate California Civil Code §1091, which provides that title to real estate can pass only by deed or by operation of law.

Since no deed had been executed at the moment of the debtor's bankruptcy filing, and since the completion of the trustee's auction did not pass title to the purchaser by operation of law, title remained in the hands of the debtor. Therefore, the post-petition trustee's deed was void.

III. The Impact on Secured Lenders and Foreclosure Sale Bidders

Commentators have quickly lined up to argue that the *Gonzalez* case was wrongly decided, and the decision is not binding precedent on any other court. However, the Court's holding should give lenders and bidders pause. A borrower who files a bankruptcy petition after a foreclosure sale has been completed, but before a trustee's deed has been executed and recorded, now has a colorable argument that the sale is void, although the weight of authority is to the contrary. The *Gonzalez* decision should create an added incentive for foreclosure trustees to issue and record a trustee's deed as quickly as possible after a sale to protect the successful bidder from an intervening bankruptcy to the extent reasonably possible.

In the long run, California lenders may need to seek legislative clarification of the statutes involved in the *Gonzalez* decision to ensure that other courts do not reach the same conclusion. California Civil Code §2924h already provides that "the trustee's sale shall be deemed final upon the acceptance of the last and highest bid, and shall be deemed perfected as of 8 a.m. on the actual date of sale if the trustee's deed is recorded within 15 calendar days after the sale." But the Court in *Gonzalez* held that Section 2924h refers only to finality of the "agreement for sale," and that the transaction is not actually complete until it is closed by the recordation of the trustee's deed. Ultimately, the legislature may need to step in to clarify the language of Section 2924h so that a trustee's sale is actually treated as "final" upon the acceptance of the last and highest bid in all courts of competent jurisdiction in this state. In the meantime, *Gonzalez* creates uncertainty in this important area of law, which may have the undesirable effect of chilling bidding at foreclosure sales.



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¹ *In re Gonzalez*, No. 6:11-bk-15665-MW, , --- B.R.--, 2011 WL 3328508 (Bankr. C.D.Cal. Aug. 1, 2011).

² See *In re Garner*, 208 B.R. 698 (Bankr. N.D.Cal. 1997); *In re Engles*, 193 B.R. 23 (Bankr. S.D.Cal. 1996).