Strict Foreclosure To The Rescue!

What To Do When You Mistakenly Fail To Name And Serve A Junior Interest

BY BRUCE J. BERGMAN

Foreclosure can be a nerve-wracking business, particularly in judicial foreclosure states. New York, for example, tends to be near the top in time-consuming litigation.

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One additional problem beyond time generally is that the consequences of a mistake can be so critical. If, for example, a foreclosure might last a year, an error at the inception could push the foreclosing party right back to that beginning stage - certainly a bungle of some distasteful significance.

So it is apparent that avoidance of miscues is always a worthy goal for lenders and servicers. But obviously we are all human and subject to frailties now and again. Included as occasionally flawed are the lender or servicer, counsel, the abstract or title company (which performed the foreclosure search), the process server - and anyone or everyone involved in the convoluted system.

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A major misstep

Among the most upsetting missteps is failing to name and serve a party with a junior interest.

The underlying goal of a mortgage foreclosure is to cause the secured property to be sold in the same legal condition it was when the mortgage was given. That is why lenders and servicers are not especially concerned about interests which later attach to the property, such as judgments or junior mortgages. If those are made defendants in the foreclosure case, as typically they would be, their interest will be cut off and the property is then presumably attractive for purchase at the foreclosure sale.

But if a party who could (and should) have been named and included in the case was omitted, an obvious problem survives. The property is now burdened by an interest (a mortgage, judgment, mechanics lien or tenancy) which should not be there. A $25 parking ticket judgment won't mean much, but a $100,000 mortgage will, so - depending upon the circumstances - this can be a genuinely troublesome incident.

How this can happen is not so difficult to imagine. Lender's counsel could misread a search and neglect to include a necessary party. Perhaps a secretary will inadvertently omit a name which had properly been included by the drafter. Or, the process server might not observe the presence of a tenant who could have been named.

Most likely, though, the fault would lie with the foreclosure search where an interest of record was overlooked.

Help is available

Although the ideal solution is to simply make the problem evaporate, because that can't happen the new owner of the property (probably the lender) will suffer some detainment. But help is in the offing.

First, let's look at a purely practical remedy.

Suppose that the missed party was a judgment creditor for $12,000. The sum due upon the foreclosed mortgage was $200,000. If the duration of a strict foreclosure case (in New York for example) is about six months (which will be discussed in a moment), because the interest during that time (at 10%) would aggregate $10,000, offering the judgment creditor perhaps $6,000 or $8,000 to release the lien is probably a good deal for both parties.

If pursued, the strict foreclosure

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Protect And Preserve The Attorney-Client Privilege

In this age of heightened litigation awareness, servicers must understand and preserve the attorney-client privilege.

Confidential, oral and written communications between clients and their attorney are privileged. The client, as holder of the privilege, can prevent other persons, including his attorney, from disclosing any confidential communications which are not made for the purpose of committing a crime or fraud.

The client can be an individual, partnership, corporation or other form of business entity. The attorney also includes in-house counsel employed by a corporation or outside counsel.

What's so important?

The basic reason why attorney-client communications must remain privileged is that if certain communications are disclosed, the opposing side will obtain critical information that might have a detrimental effect on the party making the disclosure. In essence, the communications may act as a "road map" to your defenses and weaknesses.

The attorney-client privilege is to ensure a frank and open disclosure between attorney and client of all facts, both positive and negative, which are germane to the subject matter or the litigation or potential litigation. If the privilege did not exist, this would have a chilling effect on what a client would disclose to their attorney. This could result in the client withholding information that would be beneficial to the case.

How is the privilege lost?

The attorney-client privilege can be waived, resulting in confidential communication being disclosed. Generally, this can be done when the client:

- discloses a significant part of the communication,
- consents to the disclosure by a third person, or
- fails to claim the privilege in a legal proceeding.

Both the attorney and the client should employ common sense in taking all reasonable steps to make sure that the written and oral communications between them are made in confidence and not waived. Loose lips not only sink ships, but can torpedo one's case.

Protecting the privilege

A corporation can only speak through a director, officer, employee or agent. Therefore, it is very important that the corporation authorizes and designates an officer, manager or supervisor who, under all circumstances, would be the person speaking for the corporation.

All correspondence concerning the litigation or potential litigation between the attorney and corporate clients should be sent to or emanate from the "designated litigation officer." In addition, at the top of all written communications it should state: attorney-client communication. The envelopes addressed by the attorney to the corporation client should to be addressed to or directed to the attention of the designated litigation officer.

At the pre- and post-litigation stages, internal investigations and prepared reports are commonly done. Any investigation or the preparation of any reports internally by the corporation concerning the subject matter of the litigation should only be done per the instruction of the attorney and coordinated through the designated litigation officer.

In order to ensure confidentiality, the designated litigation officer should maintain control of all correspondence, documents, investigative reports, etc., relating to the litigation. These documents should be maintained under the watchful eye and control of this officer.

The walls have ears

All telephone calls between the attorney and the corporate client should be between the designated litigation officer and the attorney when practical. In face-to-face meetings between the attorney and the corporation, the designated litigation officer should also be present when possible.

Remember to close the door and use the speaker phone sparingly (the walls have ears) when discussing the litigation. Third parties not directly or indirectly related to the litigation should be absent when any conversation, either by telephone or face-to-face, takes place.

Remember only confidential communications between attorney and client are privileged. One can hardly be considered to be speaking in confidence if he or she is yelling, or can be heard through the walls.

In summary, by using the designated litigation officer, common sense and treating all contacts between attorney and clients in a confidential and formal manner, the attorney-client privilege will not be waived.

In addition, the secrecy employed will help the client control the dissemination of information concerning the litigation and keep a lid on embarrassing rumors and leaks being spread to the detriment of the client.

-John C. Saginaw and Robert C. Harvey, Cameron & Dreyfuss

will extinguish the judgment against the property, thereby banishing the judgment creditor solely to chasing the defaulting mortgagor. Since the latter was unable to pay the mortgage, ability to satisfy the judgment is remote. All this will be highly dependent upon the circumstances - who holds the interest and how much it is, among others - but the concept should be clear. Settlement in this fashion is something to consider.

A strict foreclosure

If the purely practical route is unavailable, we arrive then at the remedy of strict foreclosure.

For our purposes, we can refrain from exploring the highly technical nuances of the process and note instead that the essence of a strict foreclosure (again in New York by way of example) is a short version of a foreclosure action, designed not to have the property sold, but to extinguish the interests of a party who could have been named in the action, but was not.

In essence, that omitted party is given by the court a right to redeem the mortgage; that is, pay all that was due upon the mortgage together with interest and any improvements made to the property in good faith. A narrow time frame in which to manifest that redemption is given, usually 30 days, but it can be up to 60 or even 90 days.

If the redemption is not accomplished, then the judgment which issues forever forecloses the right of redemption of the party who had previously been omitted. The result then is the same as if the party had been included in the original foreclosure action.

A safety net

None of this is to suggest that the strict foreclosure action is an off-handed or casual calling. It necessitates a summons and complaint, service of process, and, if an answer is received, a motion for summary judgment, among other steps.

There is some finesse required in preparing the pleadings properly and it does require an understanding of the concept and procedures. Nevertheless, it is an uncommonly sure way of solving what would otherwise be a very thorny dilemma.

Knowing that the solution exists can and should be a source of considerable comfort. It is to be hoped that you will not avail yourself of it very often, but it is there if needed. SM