

Zombie Properties May Haunt Lenders in Wisconsin Foreclosures

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A recent Wisconsin Supreme Court case holds that a foreclosure court can require a foreclosing lender to sell an abandoned or "zombie" property at a sheriff's sale within a court-determined reasonable time after the expiration of the 5-week redemption period applicable in such cases.

In *The Bank of New York v. Carson*, the lender foreclosed on Carson's residence in the City of Milwaukee. More than 16 months after the judgment of foreclosure was entered, the lender still had not sold the property through a sheriff's sale. Carson filed a motion to amend the judgment to include a specific finding under § 846.102(2) that the property was abandoned, and asked that the lender be ordered to sell the property promptly after the expiration of 5 weeks from entry of the amended judgment. The circuit court concluded that it lacked authority to compel a lender to sell an abandoned property and denied the motion.

Carson appealed and the Court of Appeals agreed with Carson, reversing the circuit court and determining that the plain language of the statute "directs the court to ensure that an abandoned property is sold without delay, and it logically follows that if a party to a foreclosure moves the court to order a sale, the court may use its contempt authority to do so." The lender then appealed to the Wisconsin Supreme Court, arguing that the use of the word "shall" in the statute was "permissive" and not mandatory, and that instead the lender had 5 years to conclude a sheriff's sale based on a different statute.

The Supreme Court affirmed the Court of Appeals, holding that the trial court has authority to order a lender to sell an abandoned property after expiration of the redemption period because § 846.102(1) states that:

the sale of such mortgaged premises *shall be made* upon the expiration of 5 weeks from the date when such judgment is entered.

Carson also holds that the trial court can require a lender to sell the abandoned property within a "reasonable" time after the expiration of the redemption period, but does not provide any criteria for determining what a reasonable time is. The decision discussed the challenges posed by abandoned properties and reasoned that the legislature intended a prompt sale of abandoned properties to address such problems.

Carson contrasts with another recent Court of Appeals case not involving an abandoned property, but also involving whether a foreclosing lender can be required to sell a foreclosed property upon the expiration of the applicable redemption period. In the consolidated case of *Bank of America, N.A. v. Prissel* and *Bank of America, N.A. v. Gerlach* ("Gerlach") the lender elected to waive its right to a deficiency judgment thereby shortening the residential redemption period from 12 to 6 months. The lender did not promptly proceed with sheriff's sales and the borrowers then moved to vacate the foreclosure judgments on the grounds that since the lender did not publish notice of the sales prior to the expiration of the redemption period, valid sales could not be conducted without such publication and therefore the foreclosure judgments could not be satisfied. This argument was based on subsection (2) of § 846.101 which provides that:

the sale of such mortgaged premises *shall* be made upon the expiration of 6 months from the date when such judgment is entered.

and that

[n]otice of the time and place of sale *shall* be given... within such 6-month period...

The *Gerlach* court affirmed the circuit court's decision denying the motions, holding that the use of the word "shall" in § 846.101(2) is "directory" and not mandatory. In other words, the statute *allowed* for the publication of the sale notice prior to the expiration of the redemption period to ensure that a sale can occur immediately upon the expiration of the period, but did not *require* such publication. A lender's decision not to so publish is not fatal to its ability to publish and direct the sheriff to conduct a sale at a later date.

The *Gerlach* court noted that the borrowers were in no worse a position due to the lender's decision not to sell the properties. The *Gerlach* decision also opined that in a hypothetical situation a borrower would benefit from a lender's decision against immediately publishing a sale notice (a prerequisite to a Sheriff's sale) by continuing to occupy a home without having to pay the mortgage and knowing (in these cases) there was no liability for any deficiency. Such extra time would also afford the borrower an opportunity to redeem or work out a loan modification with the lender.

Are Carson and Gerlach Contradictory?

Carson and *Gerlach* both involved appellate court interpretation of the word "shall" in the applicable statute governing the deficiency election and applicable redemption period, and each addressed the issue of whether a lender can be compelled to sell a property after the redemption period. However, the cases are differentiated by the nature of the property being foreclosed; *Carson* involved an abandoned home and *Gerlach* did not. In fact, the *Carson* decision (from the Supreme Court, and decided after *Gerlach*) was careful to limit its holding to abandoned homes. Therefore, the holdings are not contradictory.

Practical Implications of the Decisions

Although *Carson* permits a circuit court to require a lender to sell an abandoned property within a reasonable time after the redemption period expires, the case does not require the lender to *buy* the property. Foreclosing lenders are often the first and only bidders for their collateral at sheriffs' sales, but there is no law requiring the lender to bid. However, if the lender does not bid, anybody else (including the owner) could attend the sale and win the bidding for the property with a very small bid. If that did not happen and there are no bids at the sale, further court involvement may be necessary to address the limbo status of the unsold abandoned property. This would lead to further delay in the ultimate disposition of the zombie property, which *Carson* was trying to avoid.

Other takeaways for lenders from *Carson* are:

1. Lenders should recognize before starting a foreclosure if they may be dealing with an abandoned property. The statutory criteria that will evidence abandonment include:
 - Boarded, closed, or damaged windows or doors.
 - Missing, unhinged, or continuously unlocked doors.
 - Terminated utility accounts.
 - Accumulation of trash or debris.
 - Reports to law enforcement officials of trespassing, vandalism, or other illegal acts.
 - Conditions that make the premises unsafe or unsanitary.
2. If some or all of those factors are present in the lender's pre-foreclosure due diligence, an early informed decision should be made as to whether the lender really wants to own the property through foreclosure.
3. Some municipalities (notably the City of Milwaukee) have ordinances that put registration and maintenance obligations on the lender after just *starting* a foreclosure action, which should also be considered prior to filing.
4. Lenders should consider just suing the borrower on the note and not foreclosing on the property if there is a risk that it is abandoned and the lender does not want to own the property or let it be sold at a sheriff's sale for a minimal amount. More money judgments against borrowers who abandon their properties may be an unintended consequence of *Carson* because in a foreclosure on residential property, the deficiency is usually waived.
5. If the facts permit, lenders should seek a finding in the foreclosure judgment (a final judgment for purposes of appeal) that the property is *not* abandoned, thereby increasing the procedural burden on the borrower to seek a different finding post-judgment.

Carson should encourage lenders to make an earlier decision as to whether they really want to own an abandoned property at the end of the foreclosure process. If not, then the lender still has the option to just sue on the note.

Gerlach confirms the current practice as to properties that are not abandoned, so its impact may be minimal. Borrowers frequently lack creditworthiness for post-foreclosure refinancing or modification of their mortgage loans, and therefore there is generally little incentive for lenders to delay a sheriff's sale of unabandoned foreclosed property after the expiration of the redemption period to allow additional time for such negotiations. As a result, the perceived benefit of additional time being afforded to borrowers by not compelling a sale at the conclusion of the redemption period (which is the holding in *Gerlach*) may be limited.

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