

# A Homeowner's Rights Under Foreclosure



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## Summary

Many homeowners facing foreclosure are unaware of their rights. Knowledge of the rules, regulations and laws governing Texas home foreclosures can help homeowners protect their interests from an improper or irregular foreclosure process. This report explains the foreclosure process from default on a payment through sale of the property and targets areas that a homeowner may wish to examine during or after foreclosure.

This report is limited to foreclosures under deeds of trust. It does not cover foreclosures under executory contracts, sometimes referred to as *contracts for deed* or under home equity loans, which are conducted judicially. Likewise, this report assumes no federal liens are present on the property. If so, their presence could alter the described process.

### Definition of Key Terms

**Mortgagee.** The lender or holder of the security interest in the property; the lienholder; the mortgage servicer under certain conditions.

**Mortgagor.** The debtor, borrower and grantor of the security interest in the collateral; the owner of the property.

**Mortgage Servicer.** The last person to whom the mortgagor has been instructed by the current mortgagee to send payments for the debt; the original mortgagee or lender may be the mortgage servicer, if it still receives payments from the debtor.

**Security Instrument.** The deed of trust or mortgage; the document creating the lender's lien on the collateral and giving the trustee the power of sale.

**Trustee.** The person or persons authorized in the deed of trust to exercise the power of sale under the terms of the security instrument.

**Substitute Trustee.** The person or persons appointed by the current mortgagee or mortgage servicer to exercise the power of sale in lieu of the original trustee designated in the deed of trust.

**Debtor's Last Known Address.** The debtor's residence address unless the debtor provided the mortgage servicer a written change of address before the date the mortgage servicer mailed a required notice.

### Three Elements of Foreclosure

A proper foreclosure has three elements: (1) the real estate lien note executed by the mortgagor (borrower) at closing for the balance of the purchase price, (2) the deed of trust signed by the buyer at closing giving the mortgagee (lender) a security interest in the land being purchased and (3) the pertinent Texas statutory and case law. Generally, a foreclosure is proper as long as it complies with the procedure outlined in the deed of trust. Texas law is relevant only where the deed of trust is silent on an issue or where the deed of trust conflicts with Texas law.

There is no mandatory (or promulgated) Texas deed of trust. The forms may vary from lender to lender. The deed of trust prepared by the State Bar of Texas serves as the basic guideline for this report. Other deeds of trust may contain different provisions.

Copies of executed deeds of trust may be secured from the county clerk's office in the county where the land is located. The lender records the deed of trust to secure an interest in the financed property.

To trigger a foreclosure, the borrower must, among other things, default on a periodic payment required by the real estate lien note as described in the deed of trust. The lender then has the option of accelerating the collection of the remaining balance of the note. The entire amount of remaining indebtedness, not just the periodic payment in arrears, becomes due and payable.

This provision is known as the *acceleration clause*. Without it, the lender would be forced into a series of foreclosures, foreclosing only on the amount of the installment in default and not the entire unpaid balance of the note.

If the collateral securing the note is the debtor's residence, the lender may not accelerate the note immediately following a default. Instead, the lender must give the debtor at least a 20-day written notice to cure the payments in arrears. The notice must be sent by certified mail. The notice cannot be waived and is required in all instances.

If the debtor does not make the payments in default during the 20-day period, the lender may accelerate the debt by sending notice of the acceleration to the debtor.

If the collateral serves as the debtor's residence, the lender must give the following three notices unless they are waived in the deed of trust:

- A demand notice for the installment in arrears and thereafter affording the debtor an opportunity to remedy the default
- A clear and unequivocal notice of the lender's intent to accelerate the debt after the debtor has been given a reasonable time to cure the installment in arrears
- A final notice that acceleration has in fact occurred.

The first notice regarding the demand for the payment in arrears generally is not required by the deed of trust. However, the Texas Supreme Court has suggested that the lender "bring home to the borrower that failure to cure will result in acceleration of the note and foreclosure under the power of sale." It has been held proper to combine the first notice concerning the default with the second one involving the intent to accelerate.

## Waivers of Notice for Commercial Loans

If the collateral is not the debtor's residence, it is possible for the debtor to waive the described notices in the deed of trust. Texas courts disagree somewhat on the proper language for an effective waiver. Some courts have held that certain language waives the notice of acceleration but not the notice of intent to accelerate. The majority of courts, however, have upheld the effectiveness of most waivers. In cases of doubt, the courts tend to prevent acceleration of the note without proper notices.

The lender's conduct may forfeit the right to accelerate without notice even where an effective waiver has been included in the deed of trust. The case in question involved a lender who had accepted seven consecutive late payments and then attempted to foreclose without giving notice of acceleration after the eighth default occurred. The courts held the lender's past conduct destroyed the clear and unequivocal intent to accelerate once the debtor defaulted on a payment.

If the debt has been properly accelerated, the mortgagee (lender) may proceed to foreclose on the property by a non-judicial sale. No lawsuit is required. If the foreclosure sale is conducted in accordance with the deed of trust and Texas law, the sale is effective in transferring title to the highest bidder.

## Steps in Foreclosure Process

Steps leading to the foreclosure sale are described in the deed of trust and in Section 51.002 of the Texas Property Code. First, the lender or mortgage servicer sends a residential debtor 20 days notice to cure the default. If not, the next step may be initiated.

Second, the lender or mortgage servicer requests the trustee designated in the deed of trust (or the substitute trustee, as the case may be) to sell the property.

Third, the trustee begins the process by giving a 21-day advance notice of the sale by posting, sending and filing the various notifications:

- A written or printed notice must be posted at the courthouse door in the county where the property is located. If the property is located in more than one county, posting must occur in all counties where the land is located and specify the county in which the sale will occur. The day of posting counts as the first day of the required 21. It has been held that the phrase "at the courthouse door" means near any main access door to the courthouse.
- The same written or printed notice posted at the courthouse door also must be filed with the county clerk of each county in which the property is located.

The county clerk does not file the notice in the deed records. Instead, the county clerk is required to keep all such notices in a file conveniently available to the public for examination during normal business hours and until after the date of the sale specified in the notice.

**Note.** Effective Sept. 1, 2007, special rules apply to closures. If the courthouse or county clerk's office is closed because of inclement weather, natural disasters or other acts of God, the required postings and filings may occur within 48 hours after the courthouse or county clerk's

office reopens. By doing so, the effective dates of the postings and filings relate back to the date of the closure.

- The written or printed notice likewise must be sent by certified mail, postage prepaid, to each debtor obligated on the indebtedness. The notices must be forwarded to the debtor's most recent address as shown by the lender's records. (The day the notice is postmarked counts as the first day of the required 21.)

## Contents of Notice

There is little Texas statutory law regarding the contents of the notice. Because the purpose of the notice is to alert the borrower and prospective purchasers of the sale, the notice should contain the date of the deed of trust along with the volume and page where it is recorded; the name of mortgagor, mortgagee and trustee; a statement of default and a request for the trustee to sell property; and the time, date, terms and place of sale.

However, all notices for the foreclosure for deeds of trust executed on or after Sept. 1, 2005, must include the name and street address of the trustee(s) or substitute trustee(s). Consequently, if a substitute trustee is appointed after the notice of the sale has been posted, filed and sent, this may require a postponement of the foreclosure sale to allow time for new notices to be posted, filed and sent in compliance with the statute.

The actual foreclosure sale is a public auction conducted by the trustee at or near the courthouse in the county where the land is located. The trustee conducts the auction on the first Tuesday occurring 21 days after posting, filing and sending the required notices. The sale may occur anytime between 10 a.m. and 4 p.m. but must be within three hours after the time specified in the notices.

If the Tuesday occurs on a legal holiday, the sale is still valid on that date. If the trustee fails to conduct the sale on the correct Tuesday, the entire process of posting, sending and filing the required notices must be repeated.

Effective September 1, 2005, the commissioners' court may designate a public place other than the courthouse as the place to conduct the public auction (the foreclosure sale) as long as the area is in reasonable proximity of the courthouse, and it is as easily accessible to the public as the courthouse door. The commissioners court must record the designation in the real property records. However, no sale may occur at the designated location until 90 days expire after the recording. However, the posting of notices of the sale continue at the courthouse even though the sale occurs elsewhere.

These notices are the minimum requirements necessary for a valid foreclosure sale. However, if the deed of trust requires more, the additional requirements must be strictly followed. For example, many pre-1976 deeds of trust require posting at three public places, not just at the courthouse door.

Only the debtors and guarantors (those obligated to pay the debt) must receive personal notices at their last known addresses. Junior lienholders are not required to receive notice unless a contractual agreement mandates it. As a matter of policy, all lienholders and other interested partners should be contacted to ensure spirited bidding.

## Trustees and Substitute Trustees

The trustee is the central character in the foreclosure process. The trustee has the sole authority to sell the collateral and to convey title. The debtor grants this authority to the trustee in the deed of trust.

Texas statutes restrict, to some degree, persons eligible to serve as trustees or substitute trustees. No one may serve who has any other role or duty than to sell the land. Dual functions under the security instrument disqualify an individual. Likewise, the person cannot be a debt collector. (No amplification on this restriction appears in the statute.)

Otherwise, any competent person or persons may serve. The debtor may select the trustee or trustees, but in practice, the lender designates. The trustee or trustees may be the mortgagee or his or her agents, but probably not the mortgagor.

Regardless of who serves as trustee, the trustee's sole duty is to conduct the sale in a prescribed manner to reduce the loan as much as possible by securing a fair price. The office is one of personal confidence to the debtor. However, it does not rise to the level of a fiduciary duty to either the lender or debtor.

If the designated trustee is unavailable, a substitute trustee may be appointed in strict compliance with the deed of trust. Only the party or parties designated in the deed of trust may appoint the substitute trustee.

Effective September 1, 2005, lenders may authorize a mortgage servicer to appoint a substitute trustee or trustees to serve under the deed of trust. The mortgage servicer may then authorize an attorney to appoint a substitute trustee or trustees on behalf of the lender. The appointment or authorization may be made by power of attorney, corporate resolution or other written instrument. The name and street address of the substitute trustee or trustees must be disclosed on the appointments and in the notices posted and filed at the courthouse and sent to the debtor.

The conditions contained in the deed of trust for the appointment of a substitute trustee, if any, must be strictly followed. For instance, if the deed of trust provides that a substitute trustee can be appointed only where the original trustee fails to act, or where the original trustee resigns or dies, then these conditions must occur before a valid substitute trustee may be appointed.

The wording used in the State Bar deed of trust contains no conditions or contingencies for the appointment of a substitute trustee. It simply states that the lender may appoint a substitute trustee without any formality other than that the designation must be in writing.

Unless the deed of trust provides otherwise, a trustee or trustees need not formally resign before another is appointed. If the original trustee has posted, filed and sent the required notices, the substitute trustee or trustees should postpone the sale. Because the statute requires the name and street address of the trustee or substitute trustee to be placed on the notices after 2005, new notices should be posted, filed and sent to comply with the statute. The sale may transpire on the first Tuesday occurring 21 days after the new notices have been properly posted, filed and sent.

## Valid Sale by Trustee

The trustee is the only person who can conduct a valid sale. However, agents of the trustee may sign, post, file and send the notices. Once the notice is posted, the trustee or the agents need not check the courthouse to ensure the notice remains in place.

After the necessary notices have been posted, filed and sent and the required 21-day waiting period has elapsed, the trustee may proceed with the sale on the first Tuesday of the following month anytime between 10 a.m. and 4 p.m. but within three hours after the time designated in the notices.

Generally, the sale is conducted at the courthouse. However, the county commissioners may designate another location. It must be a public place, within reasonable proximity to the courthouse and as easily accessible to the public as the courthouse door. The location must be recorded in the real property records. No sale may occur at the new location until 90 days expire after the recording occurs.

The sale begins by the trustee reading a copy of the posted notice, followed by stating the terms of the sale and then by opening the bidding.

Generally, the trustee will require cash-only sales. Section 51.002 of the Texas Property Code contains no restrictions on the type of consideration required. If the deed of trust dictates cash only, only cash bids may be received.

Effective June 15, 2007, the purchase price for the property sold at the nonjudicial foreclosure sale is, by statute, payable immediately on acceptance of the bid by the trustee or substitute trustee. This posed hardships for cash-only sales even though the trustee or substitute trustee could set reasonable conditions on the sale if announced prior to the bidding.

For this reason, the statute was amended effective Sept. 1, 2009. Now the statute provides that the purchase price is payable upon acceptance of the bid or within a reasonable time thereafter when the bidder so requests. If the bidder is unable to comply, the trustee may reopen the auction only if the all bidders were told the time the sale would resume if the funds were not forthcoming. The sale must be completed by 4 p.m. without exception. Otherwise, entire process of re-posting, advertising and waiting 21 days must be repeated.

At the sale, all parties present may bid. Third parties, the lender and even the debtor are qualified.

The trustee may bid, but it is important to ascertain for whom the bids are entered. If the trustee is the mortgagee, all bids must be for the mortgagee. If the trustee is not the mortgagee, the trustee cannot bid the property either on his or her behalf or on the account of a corporation the trustee controls. However, the trustee may purchase the property in the name of a disinterested third party.

If the mortgagee enters the highest bid, the mortgagee can acquire the property without any out-of-pocket costs as long as the bid price does not exceed the balance of the debt. The lender simply applies the purchase price as a credit against the mortgagor's debt.

As mentioned, the mortgagor (borrower) may bid at the foreclosure sale, but this is unlikely. If the borrower had sufficient funds, he or she would have paid off the installment in arrears to prevent the lender from ever accelerating the note.

After the note is accelerated, the borrower still can prevent the foreclosure sale by redeeming the entire unpaid balance of the note anytime before the actual sale begins. This is known as an *equity of redemption*.

In addition to the equity of redemption, many states give the mortgagor a right of redemption for a certain period after the sale occurs. The right of redemption enables the foreclosed borrower to repurchase the property for the price it brought at the foreclosure sale. The right of redemption attempts to ensure that the property will generate adequate revenue at the foreclosure sale. Unfortunately for foreclosed Texas homeowners, there is no right of redemption in this state.

## Foreclosure by Mortgage Servicer

The lender is not the only entity that may initiate and complete the foreclosure process. The mortgage servicer has the same authority as long as these conditions are met:

- the lender grants the current mortgage servicer the administrative authority to act on its behalf in the servicing agreement;
- all notices, filings and postings preceding the foreclosure sale show that the mortgage servicer represents the mortgagee under the service agreement between the two and
- the notices, postings and filings preceding the foreclosure contain the name and address of the mortgagee or the name and address of the mortgage servicer if the lender has granted the mortgage servicer the authority to service the mortgage.

## Possession of and Title to Land, Condition of Property

Bidders at foreclosure sales should be advised about possession, the trustee's deed and the condition of the property.

As of May 20, 2009, a new federal statute impacts the possession date of rental property purchased at foreclosure. (Public Law 111-22 entitled "Protecting Tenants at Foreclosure Act of 2009") If the foreclosure involves a federally related mortgage on a dwelling or residential property, the purchaser must give any bona fide tenant in possession at least 90 days notice to vacate. (The term *bona fide tenant* is defined as one who acquired the lease at an arms-length transaction where the rent is not substantially less than the fair market value for the area.)

As to the title to the land, the Texas Property Code provides the trustee's deed received by the successful bidder contains no warranties of title from the trustee. The deed conveys what interest, if any, the debtor (mortgagor) held in the property.

Finally, the purchaser takes the property "AS IS." Any defects, problems or conditions are accepted by the purchaser without any recourse under the Deceptive Trade Practices Act.

## Division of Proceeds

Once the sale occurs, the proceeds are divided in the following manner and in the following order:

- the expenses of advertising the sale and making the conveyance, including any trustee and attorney's fees

other than those provided in the real estate lien note (the State Bar deed of trust includes a 5 percent commission for the trustee);

- the unpaid principal, interest, attorney's fees and other charges; as provided in the real estate lien note;
- any amounts due the junior or inferior lienholders; and
- the remaining balance, if any, goes to the mortgagor.

Should the foreclosure sale not generate sufficient revenue to cover the first three categories, the borrower is still personally liable for the balance. To recover the deficiencies, the lender may institute and obtain a judgment against the borrower. This is sometimes called a *deficiency suit or deficiency judgment*.

## Deficiency Judgments

In 1991, the 72nd Texas Legislature enacted new legislation altering the way deficiency judgments are handled.

In the past, mortgagors (debtors) complained that the prices brought at foreclosure sales were below the fair market value of the collateral. When the mortgagee (lender) was the purchaser, a possible double recovery occurred. In the case of *O'Leary Savings and Loan Association v. Farmers Market of Odessa*, 764 S.W. 2d 869 (Tex. App. 1989), the lender purchased the property at the foreclosure sale for \$150,000 and immediately sold it for \$200,000. The lender then sued the debtor for a deficiency based on the foreclosure price of \$150,000, even though a \$50,000 profit had been realized in the interim.

Texas case law has held consistently that the debtor has no recourse. As long as the lender complies strictly with the procedural rules specified in the deed of trust and in Chapter 51 of the Texas Property Code, both the foreclosure sale and price will be upheld.

To remedy this situation, Texas legislators added Sections 51.003–51.005 to the Texas Property Code. Section 51.003, entitled "Deficiency Judgments," applies only to nonjudicial foreclosures. It provides:

- The lender has two years to recover a deficiency judgment after the foreclosure sale (formerly it was four years).
- If the lender seeks a deficiency judgment, the debtor may request the court to determine the fair market value of the collateral as of the date of sale.
- The fair market value shall be determined by the finder of fact after the introduction of competent evidence of value by the parties. Competent evidence of value may include but not be limited to: expert opinion testimony; comparable sales; anticipated marketing time and holding costs; cost of sale; and the necessity and amount of any discount to be applied to the future sales price or the cash flow generated by the property to arrive at a current fair market value as of the date of the foreclosure sale.
- If the debtor does not request the determination of value, the foreclosure price shall be used to compute the deficiency.

- If the court determines that the fair market value is greater than the sales price, the debtor is entitled to an offset against the deficiency for the amount.
- Any money received by the lender from a private mortgage guaranty insurer shall be credited to the debtor's account prior to the suit for a deficiency. However, the private mortgage guaranty insurer may then sue the debtor for the amount of the payment.

Sections 51.004 and 51.005 are entitled "Judicial Foreclosure–Deficiency" and "Judicial or Nonjudicial Foreclosure after Judgment Against Guarantor–Deficiency" respectively. The two sections were added primarily to protect both debtors and guarantors in the event of either a *judicial* or *nonjudicial* foreclosure. *Either party may challenge the fair market value of the collateral within 90 days after the sale or 90 days after the guarantor receives actual notice of the sale, whichever is later. The procedure for determining fair market value and the offset against the deficiency is the same as specified in Section 51.003.*

*The primary differences between Section 51.003 and Sections 51.004 and 51.005 are that the latter two sections:*

- apply to *both* judicial and nonjudicial foreclosure sales,
- provide for the debtor or guarantor to challenge the fair market value of the collateral even *before* a lender seeks a deficiency judgment and
- can be used offensively by plaintiffs while Section 51.003 can be used only defensively by a defendant.

**Note.** Although the statutes attempt to remedy an inequitable position for debtors, substantive and technical legal questions persist.

The statute may be unconstitutional. A similar law was passed in 1933. The Texas Supreme Court declared it unconstitutional because it impaired existing contract rights. *Langever v. Miller*, 76 S.W. 2d 1025 (Tex. 1934). However, similar legislation has been upheld by the U.S. Supreme Court not to be in violation of the U.S. Constitution. *Richmond Mortgage & Loan Corp. v. Wachovia Bank & Trust Co.*, 300 U.S. 124 (1937).

The lender has three choices in the event of a default: (1) to seek a judgment for the unpaid balance of the note and perhaps foreclose later on the collateral, (2) to foreclose on the collateral and then seek a deficiency judgment or (3) to seek a judgment on the note and foreclose simultaneously on the collateral. The statutes are inapplicable when the lender sues on the real estate lien note but does not foreclose on the collateral.

The phrase *fair market* value is not defined but the statutes describe five possible ways to determine it. However, the five guidelines are not inclusive.

And finally, debtors still may be losers. When the difference between the fair market value and the foreclosure price exceeds the deficiency, the debtor has no right to a refund of the excess.

## Debtors' Alternatives and Remedies

Many debtors faced with the possibility of foreclosure attempt to convey the property back to the lender. If the lender

accepts the deed in lieu of foreclosure, it saves time, the expense of conducting the sale and possible litigation costs associated with an irregular or improper foreclosure. Although the law is not conclusive on the issue, a deed in lieu of foreclosure will satisfy the entire debt held by the lender against the property. Deficiency suits will be eliminated.

If the original borrower resells the property before the existing note is retired, the new buyer may or may not be liable for a deficiency judgment. If the new buyer does not get independent financing, he or she must either assume or "take subject to" the existing note. If the note is assumed, the new buyer and the seller are mutually liable for the monthly installment payments. Likewise, both are jointly responsible for any deficiency judgments. However, if the new buyer takes "subject to" the note, he or she avoids personal liability both for the payment of the existing note and for any deficiency judgments. This leaves the original borrower solely responsible for both.

The borrower may complain that the reason the property did not bring sufficient revenue was because of an impropriety, two possible remedies are available: setting aside (rescinding) the sale or suing for damages.

The borrower may pursue only one of the two. An election to pursue one bars any action to pursue the other later.

An exceedingly low price generated at the foreclosure sale is not sufficient in itself to render a sale invalid. However, the greater the disparity between the sales price and the market value of the property, the more readily the courts will find any irregularity sufficient for the debtor to successfully challenge the sale. The irregularity, however, must have contributed to the inadequacy of the consideration (low price) received at the sale.

Further, the inadequacy of the consideration can be grounds to have the sale set aside under federal bankruptcy laws. If the sales price does not equal or exceed 70 percent of the property's fair market value, the sale can be voided as a fraudulent transfer if the debtor files for bankruptcy within one year of the sale.

If the debtor does attack the sale under Texas law because of an irregularity, the attack most likely will be for damages and not to rescind. To set aside the sale, the debtor first must repay or offer to redeem the property from the purchaser at the price brought at the foreclosure sale. If the debtor possessed such resources, the foreclosure probably would never have occurred.

## Statute of Limitations

The statute of limitations may be a barrier. *With minor exceptions, an action to set aside a sale must be initiated within four years.* And, if the property has been resold during the interim to a purchaser unaware of the irregularities, the action to rescind the sale (but not for damages) may be lost.

For these reasons, most debtors who attack a foreclosure sale seek damages. To recover damages from a wrongful foreclosure, the debtor must prove how much the property would have brought if the irregularity had not occurred. In any event, the maximum recovery is limited to the difference in the fair market value of the property and unpaid balance of the note at the time of sale. Where the conduct of the lender or trustee can be proven to have been intentional or malicious, exemplary or punitive damages also may be recovered.



Any action to recover damages must be initiated within four years of the sale. Because only one remedy may be pursued, the borrower must be careful to choose the correct one. The following example is based on an actual case.

A Texas debtor sought damages for the wrongful appointment of a substitute trustee. The irregularity, but no resulting damages, was proven at trial. Consequently, the debtor recovered nothing. However, the court stated that the irregularity was sufficient to rescind the sale if such a remedy had been pursued first. Because it was not, the debtor was without further recourse.

Foreclosure will continue to play an important role in the Texas real estate market into the 1990s. Even though the homeowner may have defaulted on an installment payment, Texas law requires that a subsequent foreclosure be conducted in strict conformity to Texas law and the deed of trust. Failure to comply with either may enable the homeowner to set aside the sale or sue for damages.

## Examining Foreclosure Procedures

Here are some of the more strategic procedural points that a homeowner may wish to examine during or after a foreclosure. The list is not comprehensive and is not a substitute for legal counsel. The appropriate remedies for an irregularity are not included.

Did the circumstances prompting the foreclosure actually occur? For instance, was there a default on an installment payment as specified and required by the deed of trust?

Did the foreclosure take place within four years of the default? The Texas statute of limitations is four years and applies only to the delinquent payments due within the four years.

If the collateral serves as the debtor's residence, did the lender give the debtor a 20-day notice to cure the payments in default before accelerating the note? (This is mandatory and nonwaivable.) If the collateral did not serve as the debtor's residence, did the lender notify the debtor of the lender's intent to accelerate the note after the debtor defaulted on the payment? Did the lender notify the debtor that acceleration of the note had actually occurred? If not, was the right to receive such notices waived by the debtor in the deed of trust? (The interpretation of an effective waiver may require the services of an attorney.)

If the notices were effectively waived (except for the 20-day notice to cure for a debtor's residence), has the lender received late payments in the past without resorting to foreclosure? If so, the right to foreclosure without giving the required notices at a later date may be deemed improper.

## Notice of Sale

Did the trustee (or substitute trustee) or the trustee's agents post notice of the intended sale on the courthouse door, file notice of the sale with the county clerk and send notices to the debtors at least 21 days in advance of the actual sale? (The day of posting, filing and sending counts as the first day of the required 21.) If a pre-1976 deed of trust requires posting at three public places 21 days in advance of sale, was this requirement met?

Did the street address of the trustee or substitute trustee who conducted the sale appear on the notices that were posted, filed and sent?

If the land was located in more than one county, was the notice posted and filed in each county? Did each notice contain information specifying the county in which the sale would be conducted and the time the sale would begin?

Were personal notices sent to each person liable on the note by certified mail to their last known address according to the lender's records? (If the husband and wife have separated, an individual notice may need to be sent to each spouse.)

Was the substitute trustee, if any, properly appointed by the rightful parties in accordance with the terms of the deed of trust? Among other things, did the deed of trust require the original trustee to resign? Did the deed of trust require the appointment of the new trustee to be recorded 21 days in advance of the sale?

Did the trustee conduct the sale in the area of the courthouse designated by the commissioners court and in accordance with the deed of trust and state law? Was the sale conducted at the courthouse? If not, had 90 days elapsed since the commissioners recorded the notice of the new location in the deed records? Among other things, was the sale conducted on the first Tuesday of the month between 10 a.m. and 4 p.m. (but within three hours after the time specified in the notices) following the expiration of the 21-day notice period?

If cash bids were required in the deed of trust, did the trustee comply? Did the trustee acknowledge and accept all bids at the sale after the notice of the sale was read? Did the trustee leave the sale before it was completed without telling the bidders when it would reconvene? Did the trustee bid and purchase the property in his or her own behalf? (If the foreclosure sale has not occurred yet, the debtor may want to videotape the sale to preserve evidence of any irregularities.)

Did the sale conclude by 4:00 pm? Case law exists that indicates the sale cannot linger beyond 4:00 pm on Tuesday the day of the sale.

Did the deed records show a chain of title between the original beneficiary (the original lender or mortgagee) named in the deed of trust and the present lienholder conducting the foreclosure sale? Basically, the lienholder "of record" must be the same lienholder in charge of the sale. Most loans are assigned or sold to another lender. There must be a copy of this assignment or transfer recorded in the deed records. Otherwise, the wrong party may be conducting the sale and/or appointing the substitute trustee. This is a prevalent problem in today's market.

Did the expenses and charges levied against the debtor's interest following the sale constitute usury? Among other things, were the interest charges calculated to the date of sale or were they calculated over the duration of the note as if there had been no default? In other words, were there charges for unearned, unaccrued interest?

## Receivorship Status

Was the property in receivorship at the time of the sale? A receiver may have been appointed for an insolvency proceeding or a divorce. If so, the trustee under the deed of trust has

no authority to sell the land unless authorized by the court in which the receivership was pending.

Was the debtor alive at the time of the foreclosure? If not, the administrator of the decedent's estate generally has the unconditional right to revoke the sale for up to four years after the debtor's death. (There are several exceptions to this rule.)

Was the debtor a minor? If so, the property may not be foreclosed except under the probate court's supervision if the deed of trust was executed by the minor's guardian on behalf of the minor.

Was the debtor in the armed services or discharged within three months of the proposed sale? If so, without a court order the foreclosure is prohibited by the Federal Soldiers' and Sailors' Civil Relief Act of 1940. See Volume 50 of the United States Code Annotated, Section 532(3). This federal statute applies only if the property was owned by the person before he or she went into the service.

## Home Foreclosure and Debt Cancellation

Update Dec. 11, 2008 — The Mortgage Forgiveness Debt Relief Act of 2007 generally allows taxpayers to exclude income from the discharge of debt on their principal residence.

Debt reduced through mortgage restructuring, as well as mortgage debt forgiven in connection with a foreclosure, qualify for this relief. This provision applies to debt forgiven in calendar years 2007 through 2010. Up to \$2 million of forgiven debt is eligible for this exclusion (\$1 million if married filing separately). The exclusion does not apply if the discharge is the result of services performed for the lender or any other reason not directly related to a decline in the home's value or the taxpayer's financial condition.

The amount excluded reduces the taxpayer's cost basis in the home. Further information, including detailed examples, can be found in IRS Publication 4681, *Canceled Debts, Foreclosures, Repossessions, and Abandonments*.

### Related publications:

"Foreclosure for Dummies," reprint 1786. Free download at <http://recenter.tamu.edu/pdf/1786.pdf>.

"DILF or No DILF: Deed in Lieu of Foreclosure," reprint 1806. Free download at <http://recenter.tamu.edu/pdf/1806.pdf>.