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Occupancies After Foreclosure in San Francisco

As a result of the downturn in our economy, many properties have been, and will continue to be, sold at foreclosure sales. The sale of bank owned properties comprises the majority of recent sales in many areas. Realtors must have some understanding of the foreclosure process and how it impacts on the rights and obligations of tenants in possession. In San Francisco, some knowledge of the rent laws, is essential.

Federal Law

Traditionally, the federal government keeps its hands off of state real property issues. But given the large number of bank failures and bailouts, and the alarming increase in property foreclosures nationwide, Washington saw it prudent to pass legislation to protect tenants in occupancy.

Congress passed the *Protecting Tenants at Foreclosure Act of 2009* in an effort to ease the impact of foreclosures on tenants. Under this law tenants after a foreclosure are entitled to 90 days notice to vacate instead of the traditional 3 day notice to quit or 30 day notice of termination of tenancy.

The Act requires immediate successors in interest at a foreclosure sale to:

(1) provide bona fide tenants with a *90 day eviction notice*, and (2) allow bona fide tenants with leases to occupy the property until the end of the lease term except leases can be terminated on 90 days notice if is purchased by an owner occupant.

Under the Act, a bona fide tenant one where the tenant isn't the foreclosed borrower or a member of his or her family, the lease is the result of an arms length transaction, and the lease requires rent that is not substantially lower than fair market value or is reduced or subsidized due to a federal, state or local subsidy.

For Section 8 tenancies, a foreclosure sale isn't considered good cause to evict. A new owner must honor existing leases, but may give a 90 day notice to quit with expiring leases. The HAP contract remains in effect as to successors in interest at the foreclosure sale.

The provisions of the Act are set to expire on December 31, 2012. However, many laws enacted to protect tenants as temporary measures end up being permanent.

State Law

The Protecting Tenants at Foreclosure Act of 2009 was designed to preempt state laws that permitted the unfettered eviction of tenants from foreclosed property. In California, the law permits the eviction of a tenant, after foreclosure, with the service of a 3 day notice to quit. However, this law is superceded by the new federal law for the time being.

While there has been talk in Sacramento about passing new laws to protect tenants in occupancy after foreclosure sales, nothing has happened. Perhaps our state lawmakers are busy with other projects, like preventing the state from going bankrupt.

State Attorney General Brown has launched an investigation into what he calls the "forgotten victims" of the collapse in the housing market. While the investigation is aimed at violations of existing laws, Attorney General Brown's investigation results could lead to a call for new legislation at the state level.

Local Law

But who needs state law where local eviction laws protect tenants. Many cities in California have eviction and rent control laws that protect tenants in occupancy. In the case of *Gross v. San Francisco Superior Court*, it was held following a foreclosure sale, a tenant in a rent controlled unit cannot be evicted without just cause. Nor can their rent be raised in violation of the San Francisco Rent Ordinance.

The San Francisco Board of Supervisors has taken the further step of protecting tenants of previously exempted units. As of April 25, 2010, any residential tenant who was in possession at the time of the foreclosure sale of certain units exempt from Rent Control, may not be evicted except for just cause. A tenant can sue for wrongful eviction for any violation of the new law.

The new law, set forth at S.F. Administrative Code Section 37.9D, provides that any tenant who has a valid lease at the time of the foreclosure sale may enforce the lease after the sale.

Within 15 days after the foreclosure sale, the person or entity that takes title must provide the tenants in the property with a notice of their rights under the new law and that advice is available from the Rent Board. The notice must be provided by posting the building and mailing by first class mail to each affected unit; or, by posting both the property and in a prominent place on each affected unit. The failure to give the notice is a defense in any eviction action.

Common Issues in San Francisco

The single most problem encountered by purchasers of foreclosed property in San Francisco is the problem of the sham lease. Because of the new protections, under federal and local law, for tenants with long term leases, there is an incentive for tenants to create fake long term leases. In addition, many of these falsified leases carry a very low monthly rent. If you see a lease that is for a term exceeding one year, or the rent is far below market value (taking rent control into consideration), you are probably looking at a falsified lease.

In some cases, the fake leases don't even contain the signature of the foreclosed borrower who would have been the landlord before the foreclosure sale. But other times, the foreclosed borrower offers a great deal to a friend or relative at the expense of the foreclosing bank. If you suspect a fake lease, talk to an attorney who specializes in these matters. Making a mistake early on can translate into a huge loss of equity.

The other common issue with tenant occupied properties relates to security deposits. The foreclosed borrower will most likely not be paying back the deposit and the tenant will be demanding that the new owner be responsible for returning the deposit.

Many times a lessee has paid deposits to the foreclosed landlord. These deposits include security deposits and the advanced payments of rent. Both are considered "security deposits" and are governed by California Civil Code §1950.5.

Within a reasonable time, the foreclosed landlord is required to transfer all security deposits to *either* the purchaser at the trustee's sale *or* to the tenant. Civil Code §1950.5(h). Foreclosed landlords rarely do either, but still remain personally liable to the tenant for the return of a deposit.

The purchaser at a trustee's sale is not immediately entitled to demand a transfer of a deposit and cannot sue to enforce a transfer. A purchaser is liable to a tenant for a return of a deposit when the trustor/landlord fails to deliver the deposit to the purchaser or lessee. If the purchaser becomes obligated to return a deposit, and no deposit was ever transferred by the foreclosed landlord, the purchaser might then be able to seek a recovery from the foreclosed landlord. The problem for the purchaser will be the lack of accounting for deposits by the trustor. Tenants may recover deposits in small claims court based upon their own testimony that a deposit was paid. The purchaser at the trustee's sale will have little or no evidence to show that the deposit should not be refunded.

Mr. Fried is a partner at Fried & Williams in San Francisco, California and can be reached at (415) 421-0100. The foregoing does not give legal advice or establish a landlord's standard of care for a specific situation. Consult an attorney for advice on particular matters. ©2010 by Fried & Williams LLP. All Rights Reserved.