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Wake-up Call: Snoozing Lender Loses Lien Rights

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For years, it seems mortgage lenders have paid little to no attention when condominium associations judicially foreclose on their assessment liens. Perhaps believing they were fully secure in their position as first position lien holder but for the association's super-priority as to six months' of regular assessments,¹ many mortgage lenders have barely participated in assessment foreclosure lawsuits where they were named a defendant—and in some cases, they have participated not at all. A recent case out of the Court of Appeals shows the dangers of that approach.

The case is *Summerhill Village Homeowners Association v. Roughley*.² The main takeaway from *Summerhill*—for both mortgage lenders and condominium associations—is that mortgage lenders risk losing their entire security if the association forecloses on its assessment lien. *And*, in a somewhat surprising part of the decision, the Court of Appeals held that the mortgage lender did not qualify as a redemptioner.

The relevant facts of *Summerhill* were as follows: The condominium association filed an action to

judicially foreclose its assessment lien. In addition to the unit owner, the association also included the mortgage lender as one of the defendants. The mortgage lender was secured by a deed of trust in favor of Mortgage Electronic Registrations Systems (MERS). MERS was served with the Summons and Complaint, which it forwarded to GMAC, which was the servicer of the mortgage loan. However, GMAC did not respond to the lawsuit. The association obtained a default judgment and proceeded with a sheriff's sale. A third party purchased the unit at the sale (for \$100 more than the default judgment).

After the sheriff's sale, GMAC moved to intervene in the association's foreclosure action.³ GMAC asked the court to either vacate the default judgment/decree in favor of the association, or to allow GMAC to redeem the unit.

The Court of Appeals began its analysis by looking to RCW 64.34.364(3), which creates an exception to the general rule of priorities; "first in time, first in right". Under RCW 64.34.364(3), assessment liens are afforded superior priority over previously-recorded mortgages and deeds of

trust to the extent of six months' of regular assessments. The *Summerhill* court also looked to the official comments to RCW 64.34.364, which state:

"As a practical matter, mortgage lenders will most likely pay the assessments demanded by the association which are prior to its mortgage rather than having the association foreclose on the unit and eliminate the lender's mortgage lien."

The *Summerhill* court noted that the mortgage lender in *Summerhill* had precisely that opportunity. MERS was served with the lawsuit and forwarded the pleadings to GMAC, the loan servicer. The problem was that for whatever reason GMAC failed to facilitate payment of the assessment lien before the sheriff's sale. That sale therefore extinguished the lender's deed of trust according to the *Summerhill* court.

That led to the second question: whether the mortgage lender could redeem. The *Summerhill* court answered that in the negative.

The court again looked to the relevant statute, this time RCW 6.23.010. That statute identifies

qualified redemptioners, and according to the *Summerhill* court, a first-position mortgage lender does not qualify, at least not under these circumstances. The *Summerhill* court noted that only lienors who acquired their liens *after* the foreclosed interest qualify as a redemptioner. A first-position mortgage lender, like the mortgage lender in *Summerhill*, will have acquired its lien *before* the assessment lien arose⁴ and therefore does not qualify as a redemptioner according to the *Summerhill* court.

This decision certainly has support in the statutes it relied

on. The *Summerhill* court's analysis of the relevant statutes is consistent with applicable standards of statutory construction.

However, the decision does raise a number of questions related to fairness. Is it fair to deny mortgage lenders the opportunity to redeem collateral they have lost in an assessment foreclosure? Did the legislature even consider the interplay between the statute that identifies qualified redemptioners (RCW 6.23.010) and the statute that establishes the relative priority between assessment liens and mortgage liens (RCW 64.34.364) when it

drafted those two statutes? If it did not, which seems likely, is it then fair to strictly adhere to canons of statutory construction when the practical result is a forfeiture, which the law is supposed to abhor?

Fair or not, this decision is now on the books. It will be interesting to see how this decision is received by other courts, the legislature, and of course mortgage lenders and their counsel. Until then, mortgage lenders would be well advised to do whatever is necessary to make sure they are able to fully participate in future condominium assessment foreclosures.

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Magnus R. Andersson's practice focuses on real estate, construction and banking. He has over 10 years' experience handling property transactions, financing, construction, and leasing matters. Magnus has also resolved numerous disputes on behalf of property owners, contractors, banks and other businesses over the years. Many of Magnus' clients are small to mid-sized companies based in the Puget Sound region of Washington State, but he also works with publicly-traded companies as well as individuals who own real estate.



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¹ The six month super-priority for regular assessments is not available in non-judicial foreclosures of assessment liens. RCW 64.34.364(5).

² 166 Wn. App. 625, 270 P.3d 639 (2012).

³ It is not clear from the Court of Appeals' decision why GMAC was not named a party to the proceedings originally—or whether GMAC should have been named a party instead of or in addition to MERS.

⁴ Under RCW 64.35.364(1), associations have an assessment lien from the time an unpaid assessment is due.