

Understanding Property
Tax Sales and
What Advocates Can Do to
Help Clients Avoid
Tax Lien Foreclosures

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Presenter – John Rao

- An attorney with NCLC, focuses on consumer credit and bankruptcy issues and has served as a panelist and instructor at numerous bankruptcy and consumer law trainings and conferences.
- He has served as an expert witness in court cases and has testified in Congress on consumer matters.
- Mr. Rao is a contributing author and editor of NCLC's *Consumer Bankruptcy Law and Practice*; co-author of NCLC's *Foreclosures*; *Bankruptcy Basics*; *Guide to Surviving Debt*; and NCLC Reports: *Bankruptcy and Foreclosures Edition*.
- He is also a contributing author to *Collier on Bankruptcy* and the *Collier Bankruptcy Practice Guide*.
- Mr. Rao serves as a member of the federal Judicial Conference Advisory Committee on Bankruptcy Rules, appointed by Chief Justice John Roberts in 2006.



Understanding Property Tax Sales and What Advocates Can Do to Help Clients Avoid Tax Lien Foreclosures

The Property Tax Lien

- If property taxes not paid within fixed period, tax bill becomes lien on property
 - often first day of year following year in which tax is assessed
- By statute, a tax lien almost always has first priority over all other liens, including mortgages
- Same process may apply to water and sewer bills

When Do Tax Payment Problems Occur?

- Taxes for most homeowners are paid through mortgage escrow account
- Many subprime mortgages were made without escrow accounts
- Elders and heirs often have paid off homes with no escrow account
- Elders with reverse mortgages have not had escrow accounts
- Homeowners most at risk are those incapable of handling financial affairs

The Tax Sale Process

- Tax sale procedures are complicated and not understood by homeowners
- First step in advocacy is figuring out your state's tax sale procedure
- Resources:
 - Chapter 15 of NCLC's *Foreclosures*
 - Appendix G of NCLC's *Foreclosures* – Summary of State Tax Lien Foreclosure Laws
 - “The Other Foreclosure Crisis – Property Tax Lien Sales”

The Tax Sale Process

- Most states follow these steps:
 - Nonpayment and imposition of lien
 - Notice of sale
 - Sale of tax lien or certificate
 - Period for homeowner to redeem
 - Foreclosure of right of redemption
 - Final transfer of property

Different Types of Tax Sales

- Three main types: auction, negotiated bulk sale and securitization
- Tax Sale by Auction
 - “Waiting period” before sale in some states is long, often in lieu of post-sale redemption
 - Taxing authority prepares a list of delinquent taxes, identifying taxpayer, property, and amount due
 - List is typically recorded and published in the local newspaper
 - Notice provided to homeowner and other parties
 - Sale conducted by town official – usually no court involvement at this stage

Tax Sale by Auction

- **Tax Deed Sale**
 - property itself is sold at tax sale auction
 - after sale is completed, town provides purchaser with a deed to the property
- **Tax Lien Certificate Sale**
 - purchaser gets a “certificate” that gives right at some later point to foreclose tax lien and acquire deed to property
- **Transfer Without Auction**
 - Town simply executes on its lien by taking the property

Bidding Procedure at Auctions

- Tax sales are not like ordinary auctions!
- Lien or deed is not sold to highest bidder based on value of the property
- Lien or deed is sold for the amount of unpaid taxes, interest, fees, penalties, and related costs
- Some states have devised proxy for competitive bidding

Proxy for Competitive Bidding

- **Percentage ownership method** - “highest” bidder is purchaser willing to accept smallest proportional fraction of interest in the property
- **Interest rate method** - lien sold to bidder who accepts the lowest rate of interest due upon redemption
- **Overbid method** - lien sold to bidder who pays highest additional amount after paying the unpaid taxes

Negotiated Bulk Sale

- Tax liens are pooled and sold as a package at a discount to a private entity
- Private purchaser steps in shoes of town and handles collection
- State law may provide that purchaser subject to same laws as apply to town (interest, collection fees, payment options)

Securitization

- Similar to bulk sale but done through securitization process
 - City creates a trust which purchases tax liens at a discount
 - Trust issues bonds backed by the liens
 - Servicers such as Xspand and Capital Asset Research Corp. manage pool of liens or receivables purchased by trust and handle collections
 - Cities such as Jersey City, New Haven, Atlanta, New York, Washington D.C., and Philadelphia have completed securitization transactions

Right of Redemption

- Full ownership typically not transferred at tax sale even in tax deed sale states
- Purchaser acquires interest subject to right of redemption by homeowner
- Redemption period often one to three years
- States may require that redemption amount be paid to town or purchaser
- Transfer of ownership may occur automatically at end of redemption period or only after court order entered foreclosing right of redemption

Major Problems with Tax Sales

- Homeowners often confused about process and unaware of rights
- Purchasers entitled to significant profits from interest earned upon redemption
 - often 18% and higher
 - few states have automatic rate adjuster
- If no redemption, homeowner can lose home and all equity

Poll: What describes your experience with clients who have tax lien problems?

- I have no experience
- I have clients but do not know how to help
- I have provided advice or represented a few clients
- I am very experienced in representing such clients
- Other



Questions?



Preventing Tax Lien Sales

- Challenges to assessment
- Abatement, exemption and deferral programs
- Deferred payment plans
- Payment in chapter 13 bankruptcy
- Servicemembers Civil Relief Act

Tax Relief Programs

- Abatement or exemption based on age, disability, income, or personal status (veteran, firefighter, police officer, etc.)
- Benefits are not automatic – must apply and submit proof, often annually
- Generally will not apply retroactively to existing assessment or lien
- Many eligible homeowners do not apply

Types of Tax Relief Programs

- **“Circuit Breaker”** - when tax bill exceeds a set percentage of income – may be credit against state personal tax liability
- **Fixed Amount** – owner receives credit on tax bill
- **Homestead** – certain amount of property value exempt from taxation
- **Tax Freeze** – tax bill may not increase while owner enrolled or no more than fixed percentage
- **Tax Deferral** – Town retains lien but will not enforce until some event, such as sale of property

Deferred Payment Plans

- Low-income homeowners often unable to make lump-sum payment before tax sale
- Some tax collectors willing to negotiate deferred payment plans
- Right to payment plan to cure default may be provided by statute or local ordinance
- Some towns provide owners with option to have tax payments paid monthly directly from their bank account

Post-Sale Redemption

- Town or purchaser may accept redemption in installments
- Borrowing to effectuate redemption
 - reverse mortgage
 - avoid high cost or predatory mortgages
- Redemption in chapter 13 bankruptcy
 - Purchaser has secured claim that may be modified and paid during 3 to 5 year plan
 - Bankruptcy Code provision extending redemption periods by 60 days does not limit treatment of secured claims in chapter 13

Contesting a Tax Sale

- Timing and method of challenge to tax sale dependent upon state procedure
 - may be able to assert in court proceeding brought by purchaser to acquire deed or foreclose right of redemption
 - owner may need to bring affirmative action and get injunction to prevent issuance of deed
 - in some states action may be brought within SOL to set aside transfer or tax deed
 - owner has burden to prove irregularity

Contesting a Tax Sale

- Tax liens and sales created by statute - statutory requirements must be strictly followed
- Possible defects:
 - failure to give proper notice to owners and other interested parties
 - refusal of purchaser to accept redemption payments
 - failure of purchaser to record tax deed or take action within specified time period after redemption expires
 - collusion or irregularity in bidding at sale

Due Process Challenges

- Taxing authorities are state actors - adequate notice required under Fourteenth Amendment
 - *Mennonite Bd. of Missions v. Adams*, 462 U.S. 791 (1982)
 - constructive notice by publication to mortgage holder insufficient
 - notice by mail to last known address or other means to ensure actual notice is required
 - *Jones v. Flowers*, 547 U.S. 220 (2006)
 - if mailed notice returned unclaimed, town must take additional reasonable steps to provide notice

Due Process Challenges

- Adequate notice should be provided at critical steps in sale process, before property deprivation
- In many states, pre-sale and post-sale notices fail to inform about redemption right, consequences of failure to redeem, or procedure for transfer of property
- Right of redemption is significant property interest subject to due process protection
 - *In re Pontes*, 310 F.Supp. 2d 447 (D.R.I. 2004)

Poll: Do the tax sale notices
in your state adequately describe
the owner's right of redemption?

Yes

No

I don't know



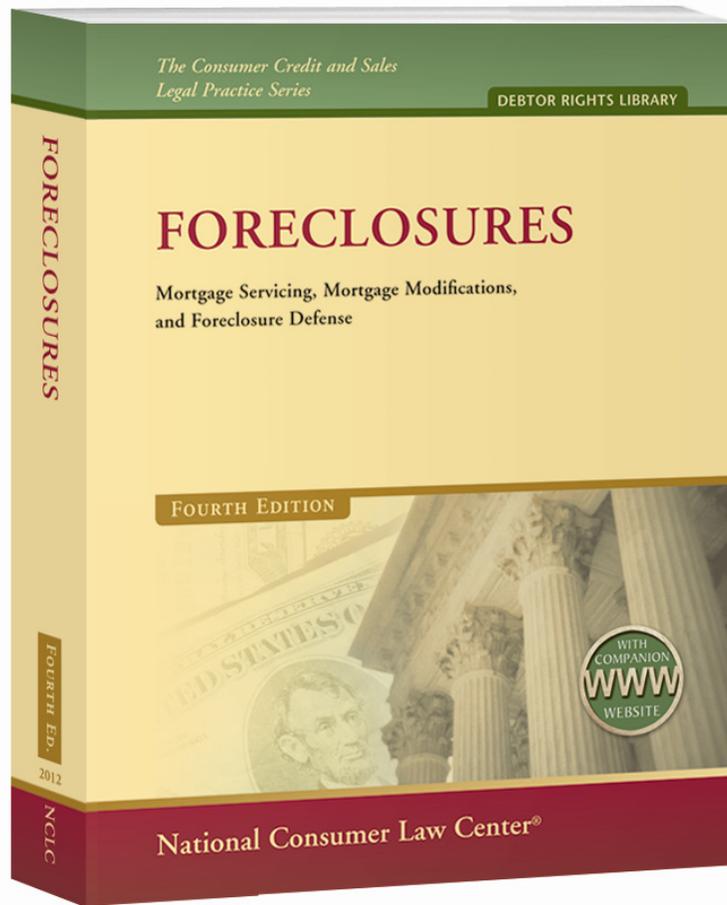
Setting Aside Tax Deed

- Inadequacy of sale price, absent fraud, is usually not enough to invalidate sale
- State fraudulent transfer statutes may not apply as purchaser not deemed creditor
- Section 548 of Bankruptcy Code may be used
 - transfer of property for less than “reasonably equivalent value” at time debtor is insolvent
 - *BFP v. Resolution Trust* not applicable because tax sale is not regularly conducted foreclosure sale under state law where no competitive bidding

Private Collection and Enforcement of Tax Liens

- Officers and employees of states and local governments are exempt from FDCPA
- Private entities may be exempt from FDCPA because taxes are not “debts,” though state collection statutes may apply
- Municipal claims for water and sewer charges considered debts under FDCPA
- Servicers for securitized trusts generally subject to state laws that apply to taxing authority

For More Information on Property Tax Sales and Avoiding Tax Lien Foreclosures: See NCLC's Foreclosures Treatise



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