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Controller, Sacramento

E. L. SORENSEN, JR.
Executive Director

January 13, 1997

Re: Foreclosures and Trustee's Sales

Dear Mr. :

This is in response to your letter of November 7, 1996, in which you pose two questions:

1. Does one who forecloses on real property of another assume all the outstanding liabilities/liens of the real property foreclosed upon which have priority over his/her loan? Does he/she "Step into the shoes" of the person foreclosed upon?

This is not a tax question, and, thus, is outside of our bailiwick. As a consequence, we cannot respond.

2. Is one who forecloses on real property of another considered a "bona fide purchaser for value" pursuant to Section 531.2 of the Revenue and Taxation Code?

Enclosed is a copy of an earlier letter (which has been redacted for confidentiality) that specifically addresses the "purchaser for value" issue and provides the requested legal authorities. As to the term "bona fide," it is generally interpreted to mean "in good faith,...without knowledge or notice of the prior interest." (Miller & Starr, California Real Estate 2d, §8.36, p. 342.) So, whether or not a given foreclosing trust deed beneficiary is "bona fide" or not as to a forthcoming escape assessment with the meaning of section 531.2 is a question of fact that must be addressed on a case-by-case basis.

I hope the above is sufficient to satisfy your inquiry. If not, please call me at (916) 324-6593. The views expressed in this letter are, of course, advisory only and are not binding upon the assessor of any county. You may wish to consult the appropriate assessor in order to confirm his or her opinion in this matter.

Our intention is to provide courteous and helpful responses to inquiries such as yours. Suggestions that help us accomplish this objective are appreciated.

Very truly yours,

Robert W. Lambert
Senior Tax Counsel

RWL:ba
cc: Honorable Kenneth P. Hahn
Los Angeles County Assessor
Attn: Mr. Stewart Barnick

Mr. Jim Speed - MIC:63
Mr. Dick Johnson - MIC:64
Ms. Jennifer Willis - MIC:70
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Executive Director

August 9, 1996

[redacted]
Los Angeles, CA 90067-2326

Re: [redacted]

Dear [redacted]

This is in response to your letter dated March 15, 1996, in which you make inquiry into the applicability of section 531.2 of the Revenue and Taxation Code to foreclosure sales[1] .

As I understand it, the underlying facts upon which your inquiry is based are as follows:

1. In 1988, [redacted] and three partners (the taxpayers) acquired real property in [redacted]

2. The assessor erred in valuing the property in 1992, 1993, and 1994.

3. In 1994, the real property was foreclosed upon by the bank which held the first deed of trust on the property.

4. Thereafter, an escape assessment was made under section 531.2 and entered on the unsecured roll in the taxpayers' names.[2]

[1] Unless otherwise noted, all further section references will be to the Revenue and Taxation Code.
[2] You do not state whether or not there was any sale or encumbrance of the property between the date of the "foreclosure" and the date of the escape assessment. For purposes of this letter, we will assume that no such sale or encumbrance occurred during that time period.

Rather than attempt to address or explain any remarks made by [redacted] of the [redacted] or [redacted], I will simply provide my opinion on the question raised. That question, as I understand it, is as follows: Given the above facts (and only the above facts), was the [redacted] correct in entering the referenced escape assessment on the unsecured roll under the provisions of section 531.2?

In my opinion, the [redacted] was correct in so entering the escape assessment on the unsecured roll. The reasons for this opinion are set forth below:

Pursuant to subdivision (a) of section 531.2 relating to escape assessments:

> When the property is real property which subsequent to July 1 of the year of escape for purposes of this article, or subsequent to July 1 of the year in which the property should have been lawfully assessed, for purposes of Article 3 (commencing with Section 501), but prior to the date of that assessment and the showing thereof on the secured roll, with the date of entry specified thereon, has (1) been transferred or conveyed to a bona fide purchaser for value, or (2) become subject to a lien of a bona fide encumbrance for value, the escape assessment pursuant to either of these articles shall not create or impose a lien or charge on that real property, but shall be entered on the unsecured roll in the name of the person who would have been the assessee in the year in which it escaped assessment and shall thereafter be treated and collected like other taxes on that roll. The tax rate applicable shall be the secured tax rate of the year in which the property escaped assessment.

So, given the language of the above statute, the issue that arises is whether or not a foreclosing trust deed beneficiary who receives title to the foreclosed-upon real property via a trustee's deed or judicial decree can be said to be a "purchaser for value" of that property within the meaning of section 531.2.[3] By "foreclosure," we mean either a judicial foreclosure or trustee's sales.

First, is a foreclosing trust deed beneficiary a "purchaser" of the property that is foreclosed upon? In my opinion, the answer is yes. As stated in Miller & Starr, California Real Estate 2d, § 9.149, p. 492:

> Anyone can bid at the foreclosure sale. The beneficiary can purchase the property at the sale. The only distinction between the beneficiary . . . and any other bidder is that the beneficiary . . . can purchase the encumbered property at the foreclosure sale by making a "credit bid" of the amount of the secured obligation, plus accrued interest and costs, without payment of additional cash. He may bid more or less than the amount owed to him. He is not required to bid the full amount of his debt but can intentionally make an underbid in an amount less than the unpaid balance of the obligation owed to him. If he bids more than the amount of his debt, he is required to produce cash or its equivalent the same as any other bidder. [Numerous cites omitted.]

Thus, if a trust deed beneficiary elects to pursue a foreclosure, the beneficiary must bid on the property at the foreclosure or trustee's sale like any other prospective foreclosure purchaser. And if the beneficiary acquires title to the property, it will only be because the beneficiary has outbid the other prospective foreclosure purchasers, if any. The fact that all or some portion of the beneficiary's bid amount consists of a credit bid is irrelevant. A foreclosing trust deed beneficiary who happens to acquire title to the foreclosed-upon property -- as opposed to receiving payment in full of the redemption amount from another bidder -- can only have acquired such title by purchase.

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[3] Since you do not raise the issue, we assume that the foreclosing trust deed beneficiary was "bona fide" within the meaning of section 531.2.

Second, given that a foreclosing trust deed beneficiary can be a "purchaser," is a beneficiary's purchase of the foreclosed-upon property "for value" within the meaning of section 531.2? In my opinion, the answer to this question is also yes.

It is axiomatic that consideration may consist of either a benefit conferred upon one party or a detriment suffered by the other (See Witkin, Summary of California Law, Vol. 1, "Contracts," § 208, p. 217.) In the case of foreclosure sales -- even foreclosure sales that only involve credit bids -- both varieties of consideration are commonly involved. For instance, the benefit conferred upon the trustor generally consists of debt relief; and a detriment to the beneficiary may be found in the fact that the trustor may be released from personal liability to the beneficiary on a recourse debt to the extent of the credit bid. In any event, given the debt relief to the trustor that occurs in a foreclosure sale, the "for value" requirement of section 531.2 appears to be met.

In addition, for both federal and state income tax purposes, a foreclosure sale of real property is treated as a sale or exchange of the property (*Helvering v. Hammel*, 311 U.S. 504 (1941); Rev. Rul. 1.73-36, 1973-1 C.B. 372.) Even in those cases where the trustor is not personally liable on the secured note, the trustor is considered to have sold the foreclosed-upon property for value for income tax purposes. And the amount realized on the foreclosure sale includes the full amount of the nonrecourse debt. (*Tufts v. Commr.*, 461 U.S. 300 (1983).)

Thus, in my opinion, the facts that you have presented to us do not contradict the determination of the [redacted] Assessor's Office that, under section 531.2, this escape assessment should be entered on the unsecured roll "in the name of the person who would have been the assessee in the year in which it escaped assessment." As a consequence, we cannot agree with your criticism of that determination.

The views expressed in this letter are, of course, only advisory in nature. They are not binding upon you or the assessor of any county.

Very truly yours,

Robert Lambert /JD

Robert W. Lambert
Senior Tax Counsel

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cc:

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Ms. Jennifer Willis, MIC:70