Protecting Tenants at Foreclosure Act Summary

By: Jeff Horn

On May 20, 2009, President Obama signed into law the Helping Families Save Their Homes Act of 2009. Title VII of the new legislation is entitled Protecting Tenants at Foreclosure Act (hereinafter "PTAFA") and was enacted to protect the interests of bona fide tenants occupying properties after foreclosure sales. Prior to the enactment of PTAFA, the post-foreclosure dispossessory proceedings were often mere formalities However, as a result of PTAFA, lenders and other purchasers at the foreclosure sale will face new challenges when they purchase tenant-occupied properties. Under Section 702 of PTAFA, in the case of any foreclosure on a federally-related mortgage loan or on any dwelling or residential real property after May 20, 2009, any immediate successor in interest in such property pursuant to the foreclosure shall assume such interest subject to the provision, by such successor in interest of a notice to vacate to any bona fide tenant at least 90 days before the effective date of such notice. Moreover, the immediate successor in interest in the property pursuant to a foreclosure shall also assume its interest subject to the rights of any bona fide tenant, as of the date of such notice of foreclosure, under any bona fide lease entered into before the notice of foreclosure to occupy the premises until the end of the remaining term of the lease, except that a successor in interest may terminate a lease effective on the date of sale of the unit to a purchaser who will occupy the unit as a primary residence, subject to the receipt by the tenant of a 90 day notice to vacate. For the purposes of this article, the purchaser at foreclosure sale, whether it is the lender or a third party, will be referred to as the lender. While Section 703 of PTAFA addresses the effect of foreclosure on Section 8 tenancies, this article will only cover the effect of foreclosure on general tenancies.

One of the challenges that lenders will encounter is determining whether a property is occupied by the former owner or by a tenant. In the event that the property is occupied by the former mortgagor, PTAFA is not applicable, and the lender can proceed with the eviction process under applicable state law.

However, if the property is occupied by a tenant, the lender should determine whether the tenant or lease is bona fide. According to PTAFA, a lease or tenancy shall be considered bona fide only if (1) the mortgagor or the child, spouse, or parent of the mortgagor under the contract is not the tenant; (2) the lease or tenancy was the result of an arms-length transaction; and (3) the lease or tenancy requires the receipt of rent that is not substantially less than fair market rent for the property or the unit's rent is reduced or subsidized due to a Federal, State, or local subsidy.

If the lender believes that the tenancy or lease is not bona fide, it can proceed with the eviction action under applicable state law. If the tenant files a responsive pleading in which it claims that its tenancy or lease is bona fide, then the issue will become a question of fact for the court to determine. In the event that the court agrees with the tenant, the lender's eviction action will likely be dismissed. However, even if the action is dismissed, the might find that the tenant owes rent payments to the lender. While PTAFA does not contain a provision allowing the lender to collect rent, it appears likely that lenders are entitled to rent payments during the tenant's continued occupancy of the premises. If the tenant fails to make rent payments, the lender would be able to bring an eviction action against the tenant for failure to payment rent.

If the lender believes that the tenancy or lease is bona fide, there are several ways that it can proceed. In cases where there is not a lease that would permit the tenant to stay for a longer period of time, the lender could take a conservative approach and send out a notice that the tenancy will terminate in 90 days. If the tenant does not vacate after the expiration of the 90 day notice period, the lender can proceed with an eviction under applicable state law. However, if the lender adopts this approach, it is likely foregoing its right to collect rent payments during the 90 day period.

It is often advantageous for the lender to seek rent payments from the tenant for numerous reasons whether the tenant is entitled to remain in possession of the property for 90 days or for the remaining term of a lease. In addition to the financial benefits of receiving rental payments, the lender can usually obtain possession of the property sooner if it can establish that rent payments are due and that the tenant has failed to pay. In such cases, the lender can bring a dispossessory action prior to the expiration of the 90 day notice period or prior to the expiration of the lease term based on the tenant's failure to pay rent.

Due to the enactment of PTAFA, lenders will face new challenges as they adopt new strategies to obtain possession of properties after foreclosure sales. In many cases, lenders might choose to seek rent payments from tenants as a possible vehicle to obtain possession of the properties more quickly.