

Commercial Foreclosures (Non-Judicial) (CA)

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A Practice Note discussing commercial foreclosure procedures and proceedings under California law. This Note outlines the primary considerations, requirements, and processes for non-judicial foreclosures of commercial real property secured by deeds of trust. This Note also addresses the appointment of receivers, deficiency judgments, the borrower's right to reinstate the loan, and the borrower's right of redemption for commercial real property.

Foreclosure is the legal process by which a lender (beneficiary or mortgagee) liquidates secured real property to obtain payment following the borrower's (trustor's or mortgagor's) default on the underlying debt.

This Note outlines California law governing non-judicial commercial foreclosure proceedings including:

- Redemption rights.
- Deficiency judgments.

This Note also provides step-by-step guidance for conducting non-judicial commercial foreclosures under California law.

Available Methods of Foreclosure in California

Lenders in California use the following instruments to secure loans against real property:

- Deeds of trust.
- Mortgages.

Deeds of trust are the most common security instruments in California. California recognizes mortgages, but lenders rarely use them. This Note assumes the foreclosing lender is the beneficiary under a deed of trust. For more information, see [State Q&A, Real Estate Finance: California: Question 1](#).

Under California law, a lender may foreclose a loan secured by commercial real property by either:

- **Non-judicial foreclosure.** Foreclosure is authorized under a deed of trust or other contract containing a power of sale clause and is conducted at a public auction

without judicial assistance. Non-judicial foreclosures are the most commonly used form of foreclosure in California and are governed by the California Civil Code (Cal. Civ. Code §§ 2923.3 to 2944.10).

- **Judicial foreclosure.** Foreclosure of a mortgage or other contract by court order after a judgment in a lawsuit. Judicial foreclosure is rarely used with deeds of trust due to its lengthy and expensive nature and is governed by the California Code of Civil Procedure (Cal. Civ. Proc. Code §§ 725a to 730.5).

A lender may also initially choose to pursue both foreclosure processes simultaneously. This gives the lender some time to weigh the pros and cons of both processes before ultimately choosing one.

For information on judicial foreclosures, see [Practice Note, Commercial Foreclosures \(Judicial\) \(CA\)](#).

Pre-Foreclosure Requirements and Considerations

Counsel for the lender should review the terms of the note and deed of trust for any contractually required notification requirements before beginning the foreclosure process.

Most California lenders provide defaulting borrowers with a demand letter. The demand letter should include:

- The terms of the loan.
- A description of the default.
- A statement that the lender intends to strictly enforce the loan documents if the borrower does not cure the default.



Order a Title Search

Before beginning foreclosure, the lender must conduct a title search to identify liens and other encumbrances that affect title to the real property. The title search may also reveal parties that have recorded a request for notice of foreclosure.

Liens for property taxes and certain other prior liens, should be paid to protect the lender's interest in the real property.

The lender should also conduct a search of the bankruptcy court records to determine whether the borrower has filed for bankruptcy protection. If the search reveals that the borrower has filed a bankruptcy petition, the foreclosure action must stop until the lender applies for and is granted relief from the automatic stay (11 U.S.C. § 362).

Consider Appointing a Receiver

To the extent a property is in danger of waste or deterioration, a lender may move for the appointment of a receiver to protect and preserve the property. Seeking the appointment of a receiver does not constitute an action under California's "one-action" rule (Cal. Civ. Proc. Code § 564(d)). For more information on California's one-action rule see [Practice Note, Navigating the One-Action Rule in California: Overview](#).

Lenders may seek a receiver to:

- Collect rents under an assignment of leases and rents.
- Protect and preserve the property.

A receiver is responsible for paying the real estate property taxes when due and insurance premiums for the real property.

The California Code of Civil Procedure and Rules of Court govern receiverships (Cal. Civ. Proc. Code §§ 564 to 570; Cal. Rules of Court, rule 3.1175 to 3.1184). For more information on receiverships in California, see [State Q&A, Provisional Remedies: California](#).

Receiverships are an important tool to consider when the property is abandoned or is otherwise at risk if left in the hands of the borrower.

Non-Judicial Foreclosure and California's Anti-Deficiency Legislation

Non-judicial foreclosure is a contractual right arising only where the borrower expressly grants the lender a power of sale in the subject deed of trust. The power of sale

clause allows a lender to foreclose the security interest and sell the secured property if the borrower is in breach of a material obligation under the terms of the promissory note, the deed of trust, or another contract, without court proceedings. (*Biancalana v. T.D. Serv. Co.*, 56 Cal. 4th 807, 813 (2013).)

Examples of material breaches that can lead to foreclosure include:

- Failure to make timely payments on the promissory note.
- Failure to keep the secured property insured.
- Failure to pay property taxes when due.
- Transfer of title or interest in the secured property to certain parties without prior written consent of the lender.

In California:

- Deeds of trust typically contain a power of sale.
- Mortgages generally do not contain a power of sale.

California's anti-deficiency legislation prohibits the beneficiary (lender) under a deed of trust from pursuing a deficiency judgment if it forces the sale of the secured property in a nonjudicial foreclosure (Cal. Civ. Proc. Code § 580(d)).

Substitution of Trustee

The trustee named in the original deed of trust is often unqualified, unwilling, or unable to conduct the foreclosure sale. In these instances, the lender must record a substitution of trustee (SOT). In an SOT, the lender or the appointed attorney-in-fact appoints a party authorized and willing to conduct the foreclosure sale as trustee. The SOT must be:

- Signed by the current beneficiary or the beneficiary's power of attorney.
- Recorded in the county where the real property is located.

Record a Notice of Default

The first step to initiating a non-judicial foreclosure sale is for the trustee to record a notice of default.

The notice of default must include all the following:

- A statement identifying the deed of trust, including the borrower's name, recording information and legal description.

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- A statement that the borrower is in default or has breached the provisions of the deed of trust.
- A description of the breach or event of default.
- A statement that the trustee intends to sell the property if the borrower does not cure the default.
- If the default is curable, a description of the steps necessary and the deadlines for the borrower to cure the default.
- The contact information for the lender.

(Cal. Civ. Code § 2924c(b)(1).)

The trustee must mail a copy of the notice of default by certified mail to the borrower and any party that recorded a request for notice within ten days after recording the notice of default (Cal. Civ. Code § 2924b(b)). Counsel should consider obtaining a trustee sale guarantee (TSG) from a reputable title company to provide the lender with information about the names and addresses of all parties who are entitled to receive notices relating to the foreclosure. The cost of the TSG varies by the size of the loan.

The trustee must mail a copy of the notice of default, by certified mail, within one month after recording to all the following parties:

- The borrower's successor-in-interest, if any.
- The beneficiaries under any junior deeds of trust or mortgages or their assignees.
- The purchaser (vendee) under a recorded contract of sale or their successors-in-interest, if any.
- The tenant under a recorded lease or memorandum of lease.
- The Office of the State Controller if there is a recorded property tax lien.

(Cal. Civ. Code § 2924(c).)

California law prescribes the form for the notice of default (Cal. Civ. Code § 2924c(b)(1)).

Prepare the Notice of Sale

The trustee may set a sale date for the trustee's sale at least 90 days after recording the notice of default (Cal. Civ. Code § 2924c). The trustee holds a foreclosure sale between 9:00 a.m. and 5:00 p.m., Monday through Friday. After setting the sale date and time, the trustee must prepare the notice of sale for mailing and publication. The notice of sale must include:

- The time and place of the sale.
- The location where the trustee intends to conduct the sale.
- The name of the original borrower (trustor) named in the deed of trust.
- The street address, assessor's parcel number, and legal description of the real property.
- The terms of sale.
- The name, address, and telephone number of the trustee.
- The total amount of the unpaid balance of the obligation secured by the real property.
- An estimate of the costs, expenses, and advances incurred by the trustee.

(Cal. Civ. Code § 2924f(b)(1) to (b)(7).)

Common Errors in the Notice of Sale

Certain mistakes in the drafting of the notice of sale can lead to the cancellation of the sale. Those errors include:

- The wrong date, time, or place of sale.
- An incorrect legal description that makes it impossible to identify the property to be sold.

Counsel for the trustee should carefully review the notice of sale to make sure that all required information is accurate and complete.

Mail the Notice of Sale

At least 20 days before the sale date, the trustee must mail the notice of sale to:

- The trustor (borrower).
- Any party with a recorded interest in the property (see Order a Title Search).
- Any party that recorded a request for notice of sale with the county recorder for the county where the real property is located (Cal. Civ. Code § 2924b(b)(2)).

Give Notice to the IRS

Review the title report for federal tax liens. If there is a federal tax lien attached to the property, the trustee must give notice of the foreclosure sale to the IRS at least 25 days before the sale date by certified mail or personal service (26 U.S.C. § 7425(c)(1)). The foreclosure does not extinguish the tax lien if the trustee does not give notice of the sale to the IRS. The IRS has 120 days following the sale to redeem the property. (26 U.S.C. § 7425(a), (d).)

In practice, while it is rare for the IRS to redeem the property, an IRS right of redemption creates a post-foreclosure cloud on title delaying further conveyance of the foreclosed property acquired by the lender after foreclosure.

Publish, Post, and Record the Notice of Sale

The final step before conducting the sale is to publish, post, and record the notice of sale. The trustee must:

- Post the notice of sale at least 20 days before the sale date in:
 - a public place in the city where the real property is located (if in a city) or in a public place in the county seat of the county where the real property is located (if not located in a city) (usually at the courthouse) (Cal. Civ. Code § 2924f(b)(1)); and
 - a conspicuous place on the property including, if possible, on the front door of the property (Cal. Civ. Code § 2924f(b)(3)).
- Publish the notice of sale once a week for three consecutive calendar weeks, with the first publication being at least 20 days before the sale date in a newspaper of general circulation published in:
 - the public notice district where the real property is located;
 - the county where the real property is located (if no newspaper is published in the public notice district); or
 - a contiguous county with the highest population of all contiguous counties (if no newspaper is published in the public notice district or county).

(Cal. Civ. Code § 2924f(b)(2).)

- Record the notice of sale in the office of the county recorder for the county where the real property is located at least 20 days before the sale date (Cal. Civ. Code § 2924f(b)(4)).

The trustee, lender, and authorized agents of the lender or trustee have a duty to make a good faith effort to provide up-to-date information on the sale and any postponements to any person that wants the information.

Borrower's Right to Reinstate the Loan

The borrower has the right to reinstate (also known as a right to cure) the loan at any time until five business days

before the sale date. To reinstate the loan, the borrower must pay:

- The entire amount then due, other than the accelerated portion of the principal due and owing after default (all installments past due regardless of acceleration of the loan balance).
- The costs and expenses incurred by the lender resulting from enforcing its rights under the deed of trust, including:
 - insurance premiums paid by the lender, if any;
 - delinquent taxes paid by the lender, if any;
 - interest to the date of reinstatement;
 - costs of recording and publication;
 - costs of service;
 - attorneys' fees; and
 - any other expenses necessarily paid by the lender.

(Cal. Civ. Code § 2924c.)

Counsel for the lender should ensure that there is a contact person available to provide the reinstatement amount if the borrower indicates a desire and ability to reinstate.

Conducting the Sale

The trustee conducts foreclosure sales between 9:00 a.m. and 5:00 p.m. on any business day Monday through Friday. The foreclosure sale must take place:

- At the time specified in the notice of sale.
- At the location specified in the notice of sale (typically at the courthouse).
- In the county where the real property is located.

(Cal. Civ. Code §§ 2924f(c)(4) and 2924g(a)(1), (a)(2).)

The trustee or its agent conducts the sale and may schedule more than one sale for the same time and place. The trustee cannot bundle properties for sale and must sell each property separately unless, the deed of trust or mortgage requires otherwise. (Cal. Civ. Code § 2924g(a)(3), (a)(4).)

The trustee is entitled to a \$50 fee for conducting the sale, in addition to any fees permitted by statute (Cal. Civ. Code §§ 2924f(c)(5) and 2924c).

On the date of sale, the trustee must offer the property for cash sale by public auction. The beneficiary may make a full credit bid equaling the amount owed on the debt.

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The trustee has the right to require:

- Every bidder other than the beneficiary to show evidence of the bidder's ability to deposit the full amount of the final bid with the trustee and actually deposit the bid amount to be held by the trustee:
 - in cash;
 - by cashier's check drawn on a state or federal savings and loan association or national bank;
 - by a check drawn on a state or federal credit union;
 - by a check drawn by a state or federal savings and loan association, savings association, or savings bank authorized to do business in California; or
 - by cash equivalent designated in the notice of sale.
- The last and highest bidder to deposit, if not previously deposited, the full amount of the winning bid.

(Cal. Civ. Code § 2924h(b).)

If the winning bidder does not deliver the bid amount in the form designated or fails to deliver the bid amount, the bidder is:

- Liable to the trustee for all damages, including court costs and attorneys' fees.
- Guilty of a misdemeanor punishable by a fine of not more than \$2,500, where failure to deliver was willful.

(Cal. Civ. Code § 2924h(d).)

Post-Sale Requirements

The trustee, lender, and successful bidder must complete several steps after the trustee's sale to complete the foreclosure process, including:

- Executing, delivering, and recording the trustee's deed to convey title to the successful bidder.
- Taking possession of the foreclosed property.
- Disbursing the sale proceeds.

Trustee's Deed

After the foreclosure sale and payment of the bid amount, the trustee has 18 calendar days to execute and deliver a trustee's deed to the successful bidder (Cal. Civ. Code § 2924h(c)). Counsel should prepare the trustee's deed in advance of sale so that the trustee may execute and deliver it as soon as possible following payment of the sale proceeds (or application of the credit bid, as applicable).

A purchaser acquiring property by a trustee's deed acquires title that is free and clear of:

- All liens junior to the deed of trust.
- Any title, interest, or claim of:
 - the trustee;
 - the trustor;
 - the beneficiary; and
 - their respective successors in interest.

The sale is perfected if the winning bidder records the trustee's deed within 18 calendar days of the sale date.

Taking Possession of the Property

If the property is abandoned at the time of the sale, the purchaser may take possession immediately.

If the property remains occupied, the purchaser may take possession only after successfully completing an unlawful detainer action (eviction) (Cal. Civ. Code § 2924n; see [Practice Note, Landlord's Rights and Remedies \(Commercial Lease\) \(CA\): Eviction](#)).

Disbursement of Sale Proceeds

Within 30 day following the sale, the trustee must send a written notice of surplus proceeds to all parties with an interest in the property, if applicable. The interested parties have 30 days after the trustee sends the notice to submit a claim to the surplus proceeds. After reviewing the claims the trustee may:

- Distribute the sale proceeds in the order determined by California law.
- Deposit the sale proceeds with the clerk of the superior court for determination of distribution.

(Cal. Civ. Code § 2924j.)

California law prescribes the following order of priority for disbursement of the sale proceeds:

- To the costs of the sale (including trustee's fees and attorneys' fees).
- To the payment of the obligations secured by the deed of trust.
- To the payment of any junior liens or encumbrances secured by the foreclosed property.

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- The balance, if any, to the trustor or the trustor's successor in interest. If the property is sold or transferred to another, to the vested owner of record at the time of the trustee's sale.

(Cal. Civ. Code § 2924k.)

Deficiency Judgments

Deficiency judgments are not available for non-judicial foreclosures in California.

Foreclosure Comparison

	Non-Judicial Foreclosure	Judicial Foreclosure
Costs	Typically, less expensive.	Typically, more expensive.
Timeline	Minimum of approximately four months.	18 months or more, but typically several years.
Any notice requirements before commencing foreclosure	There is no statutory requirement for a pre-foreclosure demand letter. The lender must comply with any notice requirements contained within the loan documents.	There is no statutory requirement for a pre-foreclosure demand letter. The lender must comply with any notice requirements contained within the loan documents.
Publication requirements	The trustee must publish the notice of sale once each week for three consecutive weeks in a newspaper of general circulation in the public notice district or county where the real property is located. The first date of publication must occur at least twenty days before the sale date. (Cal. Civ. Code § 2924f(b)(1), (b)(2).)	Counsel for the lender must publish the summons and complaint only if alternative service is needed to provide notice of the lawsuit to a defendant (see State Q&A, Commencing an Action: California: Question 12). The sheriff must publish the notice of sale following judgment according to the same requirements for a non-judicial sale (Cal. Civ. Proc. Code § 701.540).
Declaratory judgment for loan or title defects	N/A.	The lender may include a count for a declaratory judgment to clear a title defect in a foreclosure complaint.
Deficiency judgment	No. The lender cannot sue the borrower for a deficiency after foreclosing nonjudicially (Cal. Civ. Proc. Code § 580b). A junior lienholder may sue the borrower on the debt unless the junior lien is a purchase money mortgage.	A lender may include a count for a deficiency judgment in the foreclosure complaint for non-purchase money mortgages (Cal. Civ. Proc. Code § 726(b)).

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	Non-Judicial Foreclosure	Judicial Foreclosure
Redemption period	N/A.	The redemption period is: <ul style="list-style-type: none"> • Three months after the sale date if the proceeds satisfy the debt. • One year after the sale date if the proceeds do not satisfy the debt. (Cal. Civ. Proc. Code § 729.030.)
Requirement to confirm foreclosure sale	N/A.	N/A.
One-action rule	A beneficiary (lender) under a deed of trust may only pursue one form of recovery of any debt secured by a mortgage or deed of trust (Cal. Civ. Proc. Code § 726(a)).	A beneficiary (lender) under a deed of trust may only pursue one form of recovery of any debt secured by a mortgage or deed of trust (Cal. Civ. Proc. Code § 726(a)).

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