THE LENDER WITH TWO MORTGAGES ON THE SAME PROPERTY
Risks and Strategies

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The Fall 2009 issue, Vol. 44, Issue No. 3, of the *Real Property, Trust and Estate Law Journal* will include an article entitled *The Lender With Two Mortgages on the Same Property: Risks and Strategies*, by Brian D. Hulse. The article will explore some difficult and little-known issues facing lenders holding two or more mortgages or deeds of trust on the same property. The most fundamental of these issues is the risk that, by foreclosing one of the two mortgages, a court will deem the debt secured by both mortgages to have been satisfied. If the lender does not anticipate these issues in planning its realization strategy, it can severely impair its rights.

The case law in this area is inconsistent and has created unpredictability and unnecessary variations in outcomes from state to state. This is an undesirable situation in the modern world of real estate finance where lenders and the secondary markets deal with a national lending market and unnecessary local variations only add additional costs to the lending process, which are ultimately passed on to borrowers.

Most cases hold that, if the lender forecloses the more senior mortgage, while that foreclosure will wipe out the junior mortgage as a lien on the property, that foreclosure will generally not operate to extinguish the debt secured by the junior mortgage. *See, e.g., Urbach v. Monchamp Corporation*, 110 Or. App. 275, 821 P.2d 1116 (1991); *United Bank of Lakewood National Association v. One Center Joint Venture*, 773 P.2d 637 (Colo. App. 1989). Notwithstanding this general rule, there are situations and states in which such a foreclosure will be held to have extinguished the junior debt. *See, e.g., Iwan Renovations, Inc. v. North Atlanta National Bank*, 296 Ga. App. 125, 673 S.E. 2d 632 (2009); and *Simon v. Superior Court*, 4 Cal. App. 4th 63, 5 Cal. Rptr. 2d 428 (1992).

Oregon recently retreated somewhat from the ruling in *Urbach* in the case of residential foreclosures by a 2009 amendment to its trust deed statute. The amendment amends the state's antideficiency law, to provide that, where a residential trust deed is foreclosed judicially or nonjudicially, no deficiency or other judgment may be entered on any "other note, bond or other obligation" where that other obligation is secured by another residential trust deed or mortgage on the same property if (i) the two obligations were "created at the same time" and (ii) the other obligation is "owed to the beneficiary in the residential trust deed that was subject to the trustee's sale or the foreclosure."

The law is somewhat different where the junior mortgage is foreclosed. In that case, "if the holder of both a junior and senior mortgage forecloses the junior and buys at the foreclosure sale it is generally held that, in the absence of an agreement to the

contrary, the mortgagor's personal liability for the debt secured by the first mortgage, or for a deficiency, is extinguished." *See*, 1 NELSON AND WHITMAN, REAL ESTATE FINANCE LAW § 6.16 (5th ed. 2007) and cases cited therein. The cases have reached this result by a variety of theories, some of which are of questionable merit. Further, courts have too often applied technical legal theories, such as the doctrine of merger, in mechanical ways that do not address the underlying equities of the case.

The article will explore all of these issues in detail, will discuss state variations in the law and will propose strategies for the secured creditor to employ, at both the documentation stage and at the foreclosure stage, to minimize the risks. These issues have heightened importance in the current environment of greatly increased numbers of foreclosures after a long period of a buoyant real estate market with a very low foreclosure rate.

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