

Commercial and Residential Foreclosure (AZ)

A Practical Guidance® Practice Note by Lawrence E. Wilk and Corrinne R. Viola, Jaburg Wilk



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This practice note discusses the commercial and residential foreclosure process in Arizona, addressing both the lender's rights under the Arizona Judicial Foreclosure Statutes (Ariz. Rev. Stat. § 33-701 through Ariz. Rev. Stat. § 33-730), and, if applicable, under the Deeds of Trust Statutes (Ariz. Rev. Stat. § 33-801 through Ariz. Rev. Stat. § 33-821). Although foreclosure is a lender-driven process, this practice note provides guidance to counsel for both lenders and borrowers in Arizona.

The scope of this practice note is limited to these two alternatives for foreclosure of real property. It does not address the remedies available under the statutory framework for Agreements for Sale (Ariz. Rev. Stat. § 33-741 through Ariz. Rev. Stat. § 33-750). (Agreements for Sale are a form of secured transaction that exists statutorily, has specific documentation, and is infrequently used by lenders in Arizona. The statute is informative and provides forms and procedures for enforcing a lender's rights by way of forfeiture.) Finally, this practice note does not address

the many tangential issues that may arise as a result of a foreclosure, such as a receivership and bankruptcy. Recent recessions have resulted in a plethora of new case law and legislative action. The law in this area continues to evolve, but the processes addressed herein remain in place.

For general guidance on owning and financing commercial real estate in Arizona, see [Commercial Real Estate Ownership \(AZ\)](#) and [Commercial Real Estate Financing \(AZ\)](#).

Security Documents – Mortgage or Deed of Trust

Prior to 1971, the majority of secured loans issued by lenders in Arizona were documented with a debt instrument, generally a promissory note, and real estate mortgage. The mortgage would be recorded with the county recorder where the property was located and establish the priority of the lender's interest in the real property. The procedural requirements for foreclosing the lender's interest in the real property are delineated in the statutory framework of Ariz. Rev. Stat. § 33-701 et seq.

The process requires the filing of a complaint for foreclosure in a court of competent jurisdiction (the Superior Court of Arizona), in the county where the property is located, and requires the lender to obtain a judgment for foreclosure resulting in the eventual sale of the property by the county sheriff. The sale is not deemed complete until it is held by the sheriff and the required redemption period expires. This process is not only costly, but results in significant delay to the lender.

In response to the concerns of lenders, in 1971 the Arizona legislature enacted the Deeds of Trust Statutes contained in Ariz. Rev. Stat. § 33-801 et seq. In enacting

this statutory framework, the legislature sought to expedite the foreclosure process, eliminate significant expense, allow the process to move forward without (or with limited) court intervention, and alleviate the long delays resulting from the existence of the redemption periods available under the judicial foreclosure process. While the statute significantly benefited lenders, the legislation also considered borrowers' interests by providing safeguards to ensure that, despite expediting the process, the rights of borrowers would not be trampled.

Depending on the type of security instrument and/or method of foreclosure at hand, this practice note alternatively refers to a borrower as a "mortgagor," "defendant," or "trustor" and a lender as a "mortgagee," "plaintiff," or "beneficiary."

Deciding between Judicial vs. Nonjudicial Foreclosure

While the Deeds of Trust statutory provisions have been almost exclusively used by lenders since 1971, the judicial foreclosure process remains relevant. For instance, a deed of trust may be foreclosed as if it were a mortgage. Ariz. Rev. Stat. § 33-805. In that case, the statutory language of Ariz. Rev. Stat. § 33-701 et seq. is applicable. Certain factual scenarios illustrate why the ability to foreclose a deed of trust as a mortgage is still relevant today.

Availability of Deficiency Judgment

Under Ariz. Rev. Stat. § 33-807(A), a deed of trust may be foreclosed in the same manner as mortgage, in which case the provisions of Ariz. Rev. Stat. § 33-701 et seq. apply. A factor to consider in determining whether to exercise the power of sale under the trustee sale statute or to foreclose through the judicial foreclosure process is the beneficiary's rights under a residential loan to seek a deficiency judgment.

A trustee sale of residential property that qualifies under Ariz. Rev. Stat. § 33-814 precludes any recovery of a deficiency. On the other hand, a judicial foreclosure only precludes recovery of a deficiency of a purchase money secured loan. The distinction is important. While a significant number of loans are purchase money loans (in which case the mode of foreclosure is irrelevant), a large number of residential loans secure non-purchase money obligations (home equity, home improvement, and other secured transactions not involving the purchase of the property). These types of loans routinely appear as junior liens or encumbrances against the real property and are

subject to being terminated upon foreclosure by a senior lienholder. To the extent that there is equity in a parcel of real property to cover a portion of a non-purchase money debt secured in a junior lien position, and the beneficiary of that debt makes a business decision that a foreclosure will provide a significant return on its obligation (even if the interests of a senior lien will need to be addressed), then the judicial foreclosure route may be the appropriate method for preserving the lender's deficiency rights. Ariz. Rev. Stat. § 33-807 affords the beneficiary the ability to pursue this course of action.

What rights does a junior lienholder beneficiary have if a senior lienholder forecloses and the junior lienholder does not cure the senior lienholders trustee sale to protect its secured interest, nor attempt a judicial foreclosure to preserve a deficiency? Under this scenario, the beneficiary's secured interest is extinguished. This very issue was addressed in *Baker v. Gardner*, 770 P.2d 766 (1989).

In *Baker*, the lender, who was secured in a junior lien position, sought to waive its security and sue directly on its note. The note that was the basis of the suit represented the deferred balance of the purchase price of a parcel of residential property. The lender argued that it had a right to sue on the note, and waive its security under Ariz. Rev. Stat. § 33-722. In their defense, the defendants argued that the security for the loan was a deed of trust and that Ariz. Rev. Stat. § 33-814(E) (which precludes a deficiency claim) supersedes the lender's rights under Ariz. Rev. Stat. § 33-722 and limits the lender's right to recovery to proceeds from a forced sale of the property. The court concluded that the intent behind Ariz. Rev. Stat. § 33-814(E) was to abolish the personal liability of those who give trust deeds encumbering properties of two and one-half acres or less and used for a single one- or two-family dwellings. The court's initial decision was premised on the facts of the case. Specifically, the loan in question was purchase money in nature. In rendering its broadly worded opinion, the court failed to clarify the effect of its decision if the loan in question was non-purchase money in nature. In issuing its supplemental decision, the court considered the effect of its prior decision on a non-purchase money loan and concluded that if a lender is entitled to a deficiency judgment, it can also waive the security under Ariz. Rev. Stat. § 33-722 and sue on the note. The effect of this decision is to allow a lender with a non-purchase money loan to waive its security, forego having to judicially foreclose on its loan and obtain a deficiency judgment. The lender can proceed directly on its note to obtain a judgment for the amounts owed.

Ability to Accelerate the Loan

In addition to preserving certain deficiency rights, there are at least two other reasons for a lender to judicially foreclose rather than exercise its rights under the trustee's sale statutes.

The first is to accelerate the note, making all amounts due and payable, without the ability to reinstate. As discussed below, under a power of sale, the trustor or junior lienholder has the right to reinstate the loan by curing the defaulted payments. The loan only is all due and payable after 5 p.m. the last business day before the sale. In situations where a beneficiary has a repetitive defaulting borrower who ultimately cures each trustee's sale, the lender has the ability to call the note and alleviate further issues with the borrower. To the extent that the lender is an asset-based lender, the acceleration of the loan offers that lender a greater opportunity to obtain ownership of the property.

Issues with Loan Documentation

The second reason arises where there may be issues with the documentation or there may be existing claims that may be subject to litigation. A judicial foreclosure allows the lender to have any issues resolved in an orderly manner, and, ultimately, obtain an order authorizing a judicial foreclosure and the forced liquidation of the lender's security.

Judicial Foreclosure Overview

Prior to initiating any foreclosure proceeding, counsel for the lender must examine the loan documents and confirm they comply with Arizona law. The review should include confirmation that the mortgage contains a correct legal description, the parties are correctly named, and the document is recorded in the appropriate county. Counsel should also determine whether there is any language that might affect the choice of law or limit recovery.

In addition to the mortgage, the lender should review the note, or debt instrument, to determine if there is an acceleration clause and what, if any, notice is required to initiate the proceeding. Since a foreclosure under either statute is an equitable action, the lender is well advised to provide notice prior to accelerating the outstanding indebtedness. See *Harbel Oil Co. v. Steele*, 318 P.2d 359 (1957). In the event of a nonmonetary default, most documentation requires notice and an opportunity to cure.

Examples of residential security instruments commonly used in Arizona can be accessed on the [Fannie Mae website](#).

Preparation of the Foreclosure Complaint

Title Report

Prior to drafting the judicial foreclosure complaint, counsel for the mortgagee should obtain a title search, referred to as a judicial foreclosure report and/or litigation guarantee, from an Arizona title company. The report identifies all parties that should be named as parties in the complaint as either the plaintiff or a defendant interest holder with a claim junior to that of the lender. The report will provide information, and documentation to support the named defendants status as an owner, a tenant with a recorded interest in the property, a subordinate lienholder, or other interest recorded against the property, all of which hold an interest that appears subordinate to that of the mortgagee. The report also identifies senior claims, including, but not limited to taxes; assessments; covenants, conditions, and restrictions (CC&Rs); homeowner association claims; and senior lienholders.

The report will provide a form of caption for the foreclosure complaint and, for the purpose of service, the addresses of parties to be named as defendants. The report should also provide title insurance, insuring the lender (and counsel) from liability if the report is inaccurate and the inaccuracy results in any claim being asserted against the mortgagee or counsel.

Contents of the Complaint

Necessary Parties and Other Basic Information

The complaint will be captioned in conformity with the information provided in the title report. Jurisdiction for the complaint is the Superior Court in the county where the property is located. The necessary parties to the complaint include the current holder of the obligation, as plaintiff and the owner of the property, the original obligor (if different from the owner), and junior interest holders as defendants. Failure to name these parties will negate the lender's ability to terminate that party's interest in the property upon completion of the process.

The complaint should include a description of the plaintiff(s) and defendant(s), confirm jurisdiction over that parties, and describe the nature of the interests claimed. Recorded copies of the documents relied upon by the plaintiff in asserting its claim should be included, as well as the

recorded documents of the defendants. The property must be accurately described by its legal description in the complaint and an allegation included, in accordance with the terms of the mortgage, to confirm the right of the plaintiff to execute against the property in partial or full satisfaction of the indebtedness.

Information regarding the Default

The nature of the default should be clearly set forth, and if the note is to be accelerated, supporting language included. The body of the complaint should include a detailed statement regarding the amounts requested pursuant to the note and mortgage. This should include the outstanding principal amount, interest, late charges, default interest (if provided for), and any advancement made to protect the interest of the mortgagee. A thorough examination of the note will disclose any further damages that should be included in the claim. The claim for relief shall include a request for a judgment for the amounts requested.

Attorney's Fees

The mortgagee may be entitled to reasonable attorney's fees as a matter of contract. To the extent that the contract may not provide for such fees and costs, Arizona has a savings statute which may allow for attorney's fees and costs, within the discretion of the court, in any contested matter. Ariz. Rev. Stat. § 12-341 and Ariz. Rev. Stat. § 12-341.01. Whether the claim for attorney's fees is a matter of contract or statute, the claim should be clearly set forth in not only the body of the complaint, but also the claim for relief.

Deficiency Claim

Under the note and Ariz. Rev. Stat. § 33-729, the plaintiff may be entitled to a deficiency claim should the fair market value of the property not fully satisfy the lienholder's claim. To the extent that the plaintiff is not prohibited from seeking a deficiency by statute or by contract, an allegation as to the entitlement must be included in not only the body of the complaint, but also the request for relief. Failure to do so will preclude recovery of a deficiency. *Greater Ariz. Sav. & Loan Ass'n v. Gleeson*, 429 P.2d 464 (Ariz. Ct. App. 1967).

Claim for Relief

The claim for relief should include a request that the interest of each defendant be determined to be junior and subordinate to the interest of the plaintiff. It should also include a request that upon the sale of the property by the sheriff, the interests of the defendants shall be terminated, subject only to their right to redeem the property, or right

to distribution if the sale procures funds in excess of the plaintiff's claim. To facilitate the sale of the property by the sheriff, the relief requested should include a request that upon entry of a judgment for foreclosure, a writ of special execution will issue commanding the sheriff of that county to sell the property after appropriate notice and to disburse any proceeds of sale (after reimbursement of his or her expenses) in accordance with the judgment and priority of claims.

Right to Redemption

Upon the sheriff calling the sale and determining a successful bidder, a statutory redemption period commences, allowing those parties whose interests are adversely affected to provide full payment of the bid amount plus costs within the statutory time frame and thereby protect its interest. The sheriff will issue the successful bidder a sheriff's certificate which acknowledges the successful bid. Legal title to the property does not pass to the purchaser until the expiration of the operable redemption period and execution and delivery of the sheriff's deed. In accordance with Ariz. Rev. Stat. § 12-1282, the complaint must include language setting forth the appropriate redemption period. Ariz. Rev. Stat. § 12-1282(A) provides for a 30-day redemption period, running from the date of the sale if the property is both abandoned and not used for agricultural or grazing purposes. If the property is used for either purpose, Ariz. Rev. Stat. § 12-1282(B) provides for a redemption period of six months after the sale.

The complaint should be verified by a representative of the plaintiff and filed in the appropriate court. Summonses should be issued.

Lis Pendens

As part of the foreclosure process, the lender should prepare and record in public records of the county recorder in the county in which the property is located a notice of lis pendens. The lis pendens should be recorded immediately upon receipt of the court filing number. The purpose of the lis pendens is to provide notice to all subsequent interest holders in the property of the pendency of an action that may affect the title to real property. It does not establish any substantive rights to the property, which can only be determined by the court in the pending litigation. See *Evergreen W., Inc. v. Boyd*, 810 P.2d 612 (Ct. App. 1991).

A lis pendens prevents any subsequent lienholder from becoming a bona fide purchaser and alleviates the need for the plaintiff to amend the complaint if subsequent claims are recorded. An important practice pointer is to ensure

that when the complaint is filed, no new interests have been recorded. Since a judicial foreclosure report may have been provided several days prior to filing and/or the title search information may be several days behind, the title company should be contacted prior to filing or shortly after filing to ensure all required parties have been named.

For a sample form of *lis pendens*, see [Notice of Lis Pendens \(Judicial Foreclosure\) \(AZ\)](#).

The Court Process in a Judicial Foreclosure

For purposes of the foreclosure of the property and recovery of the property, the action is considered an *in rem* proceeding. Once the steps described above are complete, service must be commenced against the named defendants. This is particularly significant given due process considerations.

Due process becomes an issue if the lender seeks a deficiency. To seek monetary recourse, the action requires actual service on the party against whom the relief is requested. Absent actual service, or a court order authorizing alternative service, failure to serve the recourse party will negate the recovery of a deficiency. However, to aid the flow of commerce and to allow property to be readily alienable, the inability to serve a defendant will not preclude service by publication which will allow the property to be sold in an execution sale.

Once service is accomplished, and the time for answering has expired, the proceeding moves forward in accordance with the rules of civil procedure, applicable to any form of litigation in Arizona. In Arizona, a defendant or third-party defendant must file and serve an answer or other responsive pleading within 20 days after being served with the summons and complaint. *Ariz. R. Civ. P. 12(a)(1)(A)* (*Ariz. R. Civ. P. 4.2(E)(3)* gives out-of-state defendants 30 days instead of 20 to file an answer or other responsive pleading.). If timely answers are not filed, the plaintiff may seek to declare the defendant(s) in default. That entry of default does not become effective for 10 business days following written Application for Default. *Ariz. R. Civ. P. 55(a)*. Provided a response is still not received, the plaintiff may apply for default and a judgment may issue.

As to any parties that file an answer or other responsive pleading, in all likelihood, their claims will be subject to a motion for summary judgment which will establish (1) the default under the terms of the promissory note, (2) the amount owed, and (3) the priority of the plaintiff's

interest. Each of these items are determined by the verified complaint and a declaration from the plaintiff's representative. Absent any material issues of fact, a judgment for foreclosure can issue.

For a chart setting out the time line for the judicial foreclosure process, see [Judicial Foreclosure Timeline Chart \(AZ\)](#).

Borrower Defenses

Since foreclosure proceedings are creatures of equity, equitable defenses are available to the defendants. *Ariz. Coffee Shops v. Phx. Downtown Parking Ass'n*, 387 P.2d 801 (1963). Equitable remedies are fashioned on the facts of any given case. Under appropriate factual scenarios, defenses of laches, clean hands, waiver, or estoppel may apply and should be considered by the defendants in filing an answer. See generally *Ariz. R. Civ. P. 8(d)*.

In the limited event that the defendants raise a genuine issue of material fact, the action proceeds through the normal process which will include discovery, followed by trial.

The Judgment for Foreclosure and Sale

The judgment for foreclosure (the judgment) mirrors the language of the complaint and should:

- Establish that the interests of the defendants are junior to that of the plaintiff
- Include the amount of the judgment (including all costs and attorney's fees)
- Confirm that the property will be sold at auction to partially or fully satisfy the indebtedness
- Provide the applicable redemption period
- Order the sheriff to sell the property –and–
- Provide the sheriff with authority to execute against the other assets of the mortgagee in the event that a deficiency claim is available

Wolfswinkel v. Superior Court, 145 Ariz. 154, 700 P.2d 852 (Ct. App. 1984).

The Judicial Foreclosure Sale Process

Upon entry of the judgment, the plaintiff's counsel must prepare a writ of special execution which will then be delivered to the sheriff, who sets a date for the sale and provides appropriate notice. *Ariz. Rev. Stat. § 12-1554*. The sheriff will set the location of the sale, and on the date

of the sale, conduct an auction. It is incumbent upon the plaintiff to provide the sheriff with an opening bid. The plaintiff is entitled to a credit bid, up to the amount of the judgment. A credit bid gives the lender or the lienholder the ability to bid the amount of the debt the borrower owes, including any costs incurred as a result of the sale, without having to tender funds (except for the costs and fees incurred by the sheriff).

If the lender intends to bid a deficiency amount, that amount should reflect the actual fair market value of the property, less the amount of any senior liens, on the date of sale. The deficiency should represent the difference between the amount of the judgment and the fair market value (less the amounts owed any senior lien) of the property or the amount bid, whichever is greater. See Ariz. Rev. Stat. § 12-1566. The mortgagor must request a fair market hearing within 30 days or the right to contest the deficiency is lost. Ariz. Rev. Stat. § 12-1566(C). In the event of a timely request, the court will set a priority hearing to determine the fair market value. Pursuant to Ariz. Rev. Stat. § 12-1566(C), the court will credit the amount due on the judgment with the greater of the sales price or the fair market value of the property. Fair market value is defined in the statute as the most probable price, as of the date of the execution sale, in cash or in terms equivalent to cash, or in other precisely revealed terms, after deduction of prior liens and encumbrances with interest to the date of sale, for which the real property (or interest therein) would sell after reasonable exposure in the market under conditions requisite to a fair sale, the buyer and seller each acting prudently, knowledgeably and for self-interest, and assuming that neither is under duress. The court will hear admissible evidence, preferably by accredited appraisers, and make a determination.

Upon completion of the sheriff's sale, the sheriff will issue a sheriff's certificate, confirming that the purchaser, subject to the expiration of the redemption period set forth in the judgment, will receive a sheriff's deed. During the running of redemption period, the purchaser is not entitled to possession of the property, but is entitled to any income generated by the property. Ariz. Rev. Stat. § 12-1588.

Upon expiration of the redemption period, and assuming that no party has redeemed the property, the sheriff will issue a sheriff's deed transferring legal title and the right to possession to the purchaser.

Redemption Process

Pursuant to Ariz. Rev. Stat. § 12-1282, to redeem, a junior lienholder must file written notice of its intention to redeem with the county recorder where the property is located.

The notice must be recorded in the time frame for the redemption, as provided for in the judgment. Provided that the mortgagor does not redeem within the prescribed time frame in the judgment, each subsequent lienholder, in the priority of its lien, has a five-day period subsequent to the expiration of the time frame of the mortgagor to pay off the redemption amount of the judgment and the aggregate amount of any prior redeeming lienholder. The redemption amount includes interest at 8%. Ariz. Rev. Stat. § 12-1282 and Ariz. Rev. Stat. § 12-1285.

Commercial and Residential Judicial Foreclosure and Deficiencies

The foregoing procedures are applicable to both commercial and residential real estate foreclosures (absent any restrictive language within the contract), with one caveat. The Arizona legislature has determined that the public policy providing for deficiencies differs for residential versus commercial deficiencies. While commercial loan documents are negotiated, in most cases, between sophisticated businesspeople who are in a position to control their respective rights and liabilities, residential loans are not. Understanding the devastation of a foreclosure of a person's residence, the legislature enacted Ariz. Rev. Stat. § 33-729, commonly referred to as an anti-deficiency statute. Under the language of this statute, a judgment of foreclosure of a purchase money loan secured by a parcel of property of two and one-half acres or less, on which a single one- or two-family dwelling is located, does not extend to any other property of the judgment debtor. If the proceeds of the sale are insufficient to satisfy the indebtedness, the judgment creditor is precluded from seeking additional recovery from the judgment debtor. This statute, along with the anti-deficiency statute discussed below has been the subject of fairly recent case law and statutory changes (also discussed below).

Whether a loan is purchase money, or not, must be evaluated on the facts of each case. Some clarity was recently provided by the Arizona Supreme Court. In August of 2020, the Arizona Supreme Court in *Helvetica Servicing Inc. v. Michael S. Pasquan* reiterated that lenders are precluded from seeking a deficiency judgment against the borrower when foreclosing on residential purchase money loans. However, the court made an important distinction regarding whether a construction loan or home improvement loan constitutes a purchase money loan under the statute. While the court determined that a construction loan qualifies as purchase money, the court went on to

state that whether a loan is a construction loan or a home improvement loan is a question of fact for which the trial court must consider the totality of the circumstances. The court specifically noted that home improvement loans are not entitled to anti-deficiency protection, whereas construction loans are.

In *Helvetica*, the Pasquans defaulted on a \$3.4 million loan from Helvetica. After the default, Helvetica sued to judicially foreclose. It obtained a judgment for the amount due on the loan, completed a sheriff's sale, and obtained a deficiency judgment against the defendants for \$1,936,825.53. The Pasquans appealed, arguing they were entitled to anti-deficiency protection. Ultimately, the question resolved by the Arizona Supreme Court was the distinction between a construction loan and a home improvement loan. The court identified "five nonexclusive factors" to determine whether a loan is a construction loan for purposes of anti-deficiency protection under Section 33-729(A):

1. Whether there was a complete or substantially complete demolition of an existing structure and a new building constructed in its place
2. The intent of the parties when executing the loan documents
3. Whether the structure was inhabitable or inhabited during construction
4. Whether the structure was largely preserved and improved or substantially expanded –and–
5. Whether the project is characterized as "home improvement" or "construction" in the loan documents and in the permits or other official documents

Id.

If, after application of the above non-exhaustive test, the court finds the loan was a construction loan, the borrower is entitled to anti-deficiency protection.

Once again, as a practice pointer, the nature of the loan in question must be thoroughly analyzed to determine if it qualifies for a deficiency under the statute prior to determining if a judicial foreclosure is the appropriate means for going forward.

Nonjudicial Foreclosure (Trustee's Sale) Overview

In 1971, with the intent of expediting the foreclosure process and alleviating the significant expense by lenders and borrowers incurred in the foreclosure process, the

legislature enacted the trustee's sale procedures codified in Ariz. Rev. Stat. § 33-801 et seq.; *Steinberger v. McVey*, 318 P.3d 419 (Ct. App. 2014). The resulting statutes, while expediting the process, sought to weigh the need for expedience against the significant rights of the borrower. In doing so, the statute removed the lender's absolute right to accelerate the note (unless the note had matured prior to the initiation of the sale process) and allowed the borrower until 5 p.m. the day before the scheduled sale to reinstate the loan, thereby terminating the sale by merely tendering payments sufficient to cure the payments in default together with all costs and fees incurred and allowed by statute. For this benefit, the statute allowed the lender to initiate and conclude a sale within 91 days, without the requirement of court intervention or a redemption period, with one exception: the Internal Revenue Service (IRS) is entitled to a 120-day redemption period.

The process is accomplished by providing various notices in strict compliance with the mandates of the statutes. Unlike the initiation of a judicial foreclosure, the act of foreclosing nonjudicially is not considered a state-sanctioned activity and is not subject to the normal constraints required pursuant to due process protections. *Jackson v. Metro. Edison Co.*, 419 U.S. 345 (1974). See also, e.g., *Kenly v. Miracle Props.*, 412 F. Supp. 1072 (D. Ariz. 1976); *Teran v. Citicorp Person-to-Person Fin. Ctr.*, 706 P.2d 382 (Ct. App. 1985). So long as the trustee conducting the sale provides notice of the sale in strict compliance with the statutes, the actual receipt of notice by the party required to be notified is of no consequence. Furthermore, the lack of the due process requirement alleviates the need for the trustee to investigate additional addresses for a party if the required notice is returned unaccepted. *Transamerica Fin. Servs. v. Lafferty*, 856 P.2d 1188 (Ct. App. 1993).

Finally, the statute sought to provide finality upon completion of a sale by requiring that any defenses to the sale be raised prior to the sale. Failure to timely raise a defense terminates a party's right to contest a sale subsequent thereto. *Zubia v. Shapiro*, 243 Ariz. 412, 408 P.3d 1248 (2018).

For a chart setting forth the time line for a nonjudicial foreclosure, see [Trustee's Sale Timeline Chart \(AZ\)](#).

The Deed of Trust and Assignment of Rents

Like a mortgage, the deed of trust secures the payment of a separate contract or debt instrument. It is recorded in the county in which the real property is located, and, similar to the mortgage, its priority is determined by the timing of the recording. The principal of "first in time, first in right" will determine its priority.

The deed of trust may secure any interest in real property that may be subject to transfer; including, but not limited to fee simple title, leasehold interest, and mining claims. Ariz. Rev. Stat. § 33-801(8). To be effective, the deed of trust must include a legal description of the property by either (1) use of block, tract, or parcel number; (2) metes and bounds or course and distance survey; (3) governmental rectangular survey; (4) use of a name of an unpatented mining claim together with recording data; (5) the name of a patented mining claim with the mineral survey number; or (6) use of a homestead entry survey number. Ariz. Rev. Stat. § 33-802(A). The mailing address of each trustor, beneficiary, and trustee **shall** be specified. Ariz. Rev. Stat. § 33-802(B). The failure to list the correct legal description may require that a judicial foreclosure proceeding be initiated to allow for the reformation of the deed of trust and its eventual foreclosure.

There are three parties to a deed of trust: (1) the trustor (the borrower), (2) the beneficiary (the lender or its successor), and (3) the trustee (the third party empowered to conduct the trustee's sale).

In theory, the deed of trust is a deed executed in conformity with the statute and conveys the trust property to a qualified trustee to secure the performance of a contract(s). This fictional trust does not change the rights of the trustor to possess or enjoy the use of the property. It does not empower the beneficiary to assert an ownership interest in the property until the completion of a properly noticed trustee's sale and it limits the rights of the trustee to initiating a trustee's sale, cancelling a trustee's sale, issuing a trustee's deed upon completion of the sale, and releasing the deed of trust upon payment. Ariz. Rev. Stat. § 33-803.01.

The Trustee

Due to the role of the trustee as an independent third party to that of the trustor or the beneficiary, the statute provides specific qualifications for the trustee. Ariz. Rev. Stat. § 33-803. To qualify, the trustee must be (1) an association doing business as a bank, trust company, savings and loan, credit union, insurance company, escrow company, or consumer lender, doing business in accordance with the laws of the state of Arizona; (2) a member of the state bar of Arizona; (3) a licensed real estate broker under the laws of Arizona; (4) a person licensed as an insurance producer under the laws of Arizona; (5) an entity licensed, chartered, or regulated by the FDIC, the comptroller of

currency, the Federal Home Loan Bank, the NCUA, the Farm Credit Administration, the Federal Reserve Board, or any successors; or (6) the parent company of any of these entities. Subject to limited exceptions, the beneficiary cannot be the trustee. Ariz. Rev. Stat. § 33-803(C).

If the deed of trust fails to list a trustee, the existing trustee resigns, the deed of trust incorrectly lists a trustee, or the beneficiary decides to remove the trustee for any reason, the beneficiary is empowered to substitute another qualified person or entity as the new trustee. See Ariz. Rev. Stat. § 33-804. The notice of substitution is recorded and mailed to the trustor. A suggested form for a substitution of trustee is included in the statute. For an annotated version of this form, see [Substitution of Trustee \(Nonjudicial Foreclosure\) \(AZ\)](#).

The duties of the trustee are not necessarily the duties of a trustee in a normal trust relationship. Under Arizona law, the fiduciary duty to the trustor is limited to the foreclosure context, and only obligates the trustee to conduct the sale in accordance with statute. *Vawter v. Bank of Am. NA*, 108 F. Supp. 3d 719 (D. Ariz. 2015).

The Nonjudicial Foreclosure (Trustee's Sale) Process

By virtue of the trustee's position, a power of sale is conferred upon the trustee of a deed of trust under which the trust property may be sold. The sale must be conducted in the manner mandated by Ariz. Rev. Stat. § 33-807 et seq., after a breach or default in performance of the contract(s) for which the trust property is conveyed as security, or a breach or default of the trust deed. See Ariz. Rev. Stat. § 33-807(A).

At the option of the beneficiary, the deed of trust may be foreclosed in accordance with the notice provisions of the trustee's sale statutes or the provisions of the judicial foreclosure statutes. See Ariz. Rev. Stat. § 33-801. See also Ariz. Rev. Stat. § 33-701. If the beneficiary chooses to exercise its remedial rights under the judicial foreclosure statutory framework, the procedures required to conduct a sale will be dictated by the provisions of Ariz. Rev. Stat. § 33-701 et seq., as discussed previously. A party cannot initiate a power of sale of trust property if a separate action to judicially foreclose the property is pending. In such a case, the judicial action must first be dismissed. See Ariz. Rev. Stat. § 33-807(B).

Initiating the Sale

The beneficiary, upon the existence of a default, may initiate a nonjudicial foreclosure by notifying the trustee of the default and requesting that the trustee initiate the proceeding. No formal pre-foreclosure notice is necessary unless mandated by the loan documents or under a federally-mandated regulation applicable to residential foreclosures. However, it is always good practice to send a pre-foreclosure demand prior to incurring additional expense. A nonjudicial foreclosure, as with the judicial foreclosure, is subject to principals of equity. Sending the notice provides potential defenses to several principals of equity that might be raised by a trustor in an attempt to stop a pending action.

Upon notification from the beneficiary, the trustee, or subsequently appointed trustee, commences the nonjudicial foreclosure by ordering a trustee's sale guarantee report from a title company of his or her choosing. Similar to the judicial foreclosure report, the guarantee report provides a road map for compliance with the statutory framework. The report will set forth all interests that appear of record against the property and provide copies of the recorded documents. In addition, the report provides the names and addresses of all parties entitled to notice under the statute, as well as the appropriate places for posting and publication (setting forth addresses for posting and newspapers of general circulation in the county where the property is located). The report also provides insurance coverage to the trustee if, in reliance and compliance with the report, an action is subsequently brought against the trustee for any inaccuracy in the report. It is important to note that this policy is for the benefit of the trustee and it should not be assumed by a purchaser at sale that the title company will subsequently issue an owner's policy.

The trustee then drafts and provides the beneficiary with the initial documentation to be executed in furtherance of the sale. In accordance with the Servicemembers Civil Relief Act, an affidavit of nonmilitary service must be provided to the beneficiary for execution. 50 U.S.C. § 3901 et seq. The affidavit confirms that the trustor(s) are not currently on active duty in a military capacity. (The trustee can confirm the status of the trustor through a national registry such as the [United States Department of Defense Manpower Data Center](#).) The foreclosure cannot be initiated if the trustor is currently in military service until there has been compliance with the act. For a sample form of affidavit, see [Affidavit with Respect to Military Service \(Nonjudicial Foreclosure\) \(AZ\)](#).

The beneficiary must be provided with and execute a statement of breach or nonperformance, which establishes

the nature of the default. By signing this document, the beneficiary confirms the specific nature of the breach. The trustee can rely upon the statement, as well as any other information received from the beneficiary, and is insulated from future liability arising from any inaccuracy. Ariz. Rev. Stat. § 33-820(A). The statement also confirms the intent to commence a trustee's sale. For a sample form, see [Statement of Breach or Non-performance \(Nonjudicial Foreclosure/Trustee's Sale\) \(AZ\)](#).

As noted above, if the trustee is to be substituted, documents in compliance with Ariz. Rev. Stat. § 33-804 need to be executed and recorded. For a sample form of substitution, see [Substitution of Trustee \(Nonjudicial Foreclosure\) \(AZ\)](#).

Upon confirmation and receipt of the affidavit establishing that the trustor is not deployed on active duty, the signed statement of breach and nonperformance, and a substitution of trustee (if necessary), the trustee is then empowered to commence the trustee's sale process.

Notice of Trustee's Sale

To initiate the sale, the trustee must prepare for recording a notice of trustee's sale. The requirements for the notice are set forth, in detail, in Ariz. Rev. Stat. § 33-808. The notice must include:

- The date, time, and location for the sale, which can be no sooner than 91 days after the date of recordation of the notice of sale (The location of the sale is limited to the location of the trustee, the trust property, or an identifiable location at the county courthouse in the county where the property is located. The sale shall be set between 9 a.m. and 5 p.m. and may not occur on a weekend or holiday.)
- The street address, if any, or an identifiable location for the property, together with an accurate legal description for the property
- A county assessor's tax parcel number for the real property
- The original principal balance as shown on the deed of trust, or a statement "unspecified" if none is included in the document
- The names and addresses, as of the date of the recording of the notice, of the beneficiary and trustee, and the name and address of the original trustor, as stated in the deed of trust or subsequent request for notice which may be recorded and establish a different address (The notice is signed by the trustee and must clearly set forth the authority under which the trustee qualifies.)

- The telephone number of the trustee and a statement setting forth the licensing authority pursuant to which the trustee qualifies under Ariz. Rev. Stat. § 33-803
- Finally, the document must include, in bold print and capitalized type, the following paragraph:

NOTICE! IF YOU BELIEVE THERE IS A DEFENSE TO THE TRUSTEE SALE OR IF YOU HAVE AN OBJECTION TO THE TRUSTEE SALE, YOU MUST FILE AN ACTION AND OBTAIN A COURT ORDER PURSUANT TO RULE 65, ARIZONA RULES OF CIVIL PROCEDURE, STOPPING THE SALE NO LATER THAN 5:00 P.M. MOUNTAIN STANDARD TIME OF THE LAST BUSINESS DAY BEFORE THE SCHEDULED DATE OF THE SALE, OR YOU MAY HAVE WAIVED ANY DEFENSES OR OBJECTIONS TO THE SALE. UNLESS YOU OBTAIN AN ORDER, THE SALE WILL BE FINAL.

To aid in the preparation of the notice of trustee's sale, Ariz. Rev. Stat. § 33-808(D) provides a form to be used by the trustee. For an annotated version of the form, see [Notice of Trustee's Sale \(Nonjudicial Foreclosure\) \(AZ\)](#).

While certain errors in the notice may not invalidate the notice, an inaccuracy in the legal description or time, date, or location of the sale will invalidate the sale and require that it be cancelled and restarted. Notwithstanding this rule, a defect in the legal description may not be fatal if the document, read in its entirety, is sufficient to cure the defect.

The sale is initiated upon recordation of the notice of trustee's sale. Within five days after the recordation of the notice of trustee's sale, the trustee must provide notice, by certified or registered mail, to all parties listed in the deed of trust. Ariz. Rev. Stat. § 33-809(B). The mailing must be directed to the addresses set forth therein. The mailing includes, in addition to the notice, a copy of the statement of breach and nonperformance. The notice included in this mailing does not need to include the recording information stamp that reflects the date of recordation.

Within 30 days of recording the notice, the trustee must deliver a copy of the notice of trustee's sale, reflecting the recording information setting forth the recordation date of the notice, to each party who at the time of recording claims to have an interest in the real property. The mailing must be sent by certified or registered mail and include a copy of the statement of breach and nonperformance. The mailing must be delivered to the address of any party reflected in the recorded document establishing the interest, or at such address that may be included in a separate request for notice. If no address is included in

the recorded document reflecting a party's interest, the notice should be sent to the address where the recorded document was to be delivered after recording. No further investigation is required.

The trustee's guarantee report includes the information required to comply with the mailing requirement. Similar to the issue addressed by the judicial foreclosure report, the trustee must confirm that the report is current, through the date of recording of the notice, and that no intervening recorded interests exist. Provided the report is current through the date of recordation, any subsequently recorded interests are deemed to have been recorded with knowledge of the recorded notice and no further notice is required to be delivered to those interests.

In addition to notice through direct mailings, the notice of trustee's sale must be posted at the designated place for postings at the courthouse in the county in which the property is located, as well as a conspicuous place on the trust property, provided posting can be completed without a breach of the peace. Ariz. Rev. Stat. § 33-808(A)(3). The postings must occur at least 20 days prior to the date set for the sale of the property.

In addition to posting the property and courthouse, the notice of trustee's sale must be published in a newspaper of general circulation in the county in which the trust property is located. Ariz. Rev. Stat. § 33-808(A)(4). The notice must be published at least once a week for four consecutive weeks, with the last publication occurring more than 10 days prior to the sale.

By providing the notice of the sale in the manner explained above, the legislature deemed that sufficient notice is provided to allow the borrower and third parties the timely ability to protect their interests. While due process may not apply, strict adherence to the noticing provisions set forth above is a requirement. *Patton v. First Federal Sav. & Loan Ass'n*, 578 P.2d 152 (1978).

Bring Down Report

Thirty days prior to the sale, the trustee should request a bring down report, which will update the initial report through the date of the request of the title company.

The purpose of this additional report is to determine (1) if the IRS has filed a claim or lien subsequent to the recordation of the notice of trustee's sale, and (2) if there has been any other occurrence which may affect the trustee's ability to move forward with the sale. While as a general rule a completed trustee's sale is final and not subject to redemption, there is an exception for the IRS. "Where a sale of real estate is made to satisfy a lien prior

to that of the United States, the United States shall have one year from the date of sale within which to redeem, except that with respect to a lien arising under the internal revenue laws the period shall be 120 days or the period allowable for redemption under State law, whichever is longer . . . " 28 U.S.C. § 2410(c).

This additional notice and right to redemption does not elevate nor change the priority of the Internal Revenue claim. This period may be waived with the consent of the IRS, but it will require the trustee or purchaser to contact the IRS and establish that there is no equity to cover its claim. The trustee should request a day of sale bring down report from the title company to assure that there has not been a bankruptcy filing or other claim that will impair the trustee's ability to complete the sale.

Additional Obligations of the Trustee

At any time that the deed of trust is subject to reinstatement, but not earlier than 30 days after the recording of the notice of trustee's sale, upon written request, the trustee must provide the person requesting such information (provided the information is known by the trustee) the unpaid principal balance of the obligation, the name of the owner of the property, and a list of the liens and encumbrances upon the trust property. The trustee is not subject to liability for the information provided, except for a willful or intentional failure to provide information. Ariz. Rev. Stat. § 33-809(G).

Beginning at 9 a.m. and continuing to 5 p.m. the last business day preceding the sale, and then continuing through the date and time for sale, the trustee must make available the actual bid or a good-faith estimate of the credit bid which will be made at sale. In the event the bid is not made timely available, the sale will be continued until the trustee can comply. Ariz. Rev. Stat. § 33-809(F).

Reinstatement Prior to Sale

Prior to 5 p.m. on the last business day prior to the sale date, the trustor, trustor's successor in interest, and any person having a subordinate interest may reinstate the loan and cancel the pending sale by paying the beneficiary, the trustee, or the trustee's agent the past due amounts then due under the contract (without acceleration), together with the costs and expenses of conducting the sale. Permissible costs are:

- The cost of the title report
- The costs of mailing photocopying, recording, posting, and publishing required documents

- Any postponement fees
- Auctioneer fees
- The trustee's fees in an amount not to exceed \$600.00 or one-half of 1% of the outstanding balance (whichever is greater) –and–
- Allowable attorney's fees incurred in protecting and preserving the beneficiaries interest in the real property

Upon payment, the trustee records a cancellation of sale and the contract is deemed reinstated. Ariz. Rev. Stat. § 33-813(B). A form of cancellation of sale is incorporated in Ariz. Rev. Stat. § 33-813. For an annotated version of this form, see [Cancellation of Notice of Trustee's Sale \(Nonjudicial Foreclosure\) \(AZ\)](#).

If the note has matured prior to the initiation of the trustee's sale, the amount then due under the contract should be the full amount of the obligation together with the expenses outlined above. Failure to reinstate the contract prior to 5 p.m. the last business day prior to the sale terminates the right to reinstate the loan and results in the acceleration of the contract without any further ability to reinstate.

Sale by Public Auction

On the date and time for sale designated in the notice of sale, the trustee will offer the property for sale. The sale may be conducted by an agent for the trustee and the trustee need not be present. Only the beneficiary may make a credit bid, all other bidders are expected to tender cash if they are the successful bidder. To qualify as a bidder, anyone other than the beneficiary must provide the trustee with a cashier's check in the amount of \$10,000. Upon completion of the sale, the trustee refunds deposits to all but the successful bidder. Ariz. Rev. Stat. § 33-811(A). In the event the bidder does not perform, the deposit is forfeited and the bidder may be responsible for any additional damages incurred. Ariz. Rev. Stat. § 33-811.

The trustee may, at his or her choice or upon request of the beneficiary, postpone the sale for any reason by giving actual notice of the postponement date and time at the time and place of the existing sale. The sale cannot be extended for a period exceeding 90 days, at any given extension. The sale can be continued any number of times. No further notice is required other than the oral notice given at the time and place of the sale. Ariz. Rev. Stat. § 33-810(B), see also *Nicholson v. Nagel* (In re Nagel), 245 B.R. 657 (D. Ariz. 1999). The trustee may also change the location of the sale at the time of the postponement. The new location must comply with Ariz. Rev. Stat. § 33-808.

A sale is not complete if it is held contrary to, or in violation of federal statute or an undisclosed bankruptcy. A sale that is held in violation is considered continued to a date 28 days from the date of the sale, at the same location. If the 28th day falls on a holiday, the sale will be continued to the first business day thereafter. Ariz. Rev. Stat. § 33-810(C). The trustee must provide notice of the new sale date to all bidders who provide their name and address at the original sale.

The successful bidder, exclusive of the beneficiary, has until 5 p.m. the following business day to tender funds acceptable to the trustee sufficient to pay the accepted bid. In the event the high bidder fails to perform, the trustee in his or her sole discretion can either (1) offer the property to the second highest bidder or (2) continue the sale to reopen bidding. If the trustee reopens bidding, he or she must notify all bidders that have provided the trustee with their names and addresses by certified or registered mail of the new sale location, date, and time. If the trustee offers the property to the second highest bidder and that bidder fails to perform, the trustee may continue to offer the property to each successive bidder until a bidder performs. Ariz. Rev. Stat. § 33-811(A).

Within seven business days of payment, the trustee must record a trustee's deed transferring title to the property to the high bidder. The recording of the trustee's deed raises a presumption that the trustee has fully complied with the requirements necessary to exercise the power of sale including recording, mailing, posting, publishing, and conducting the sale. Ariz. Rev. Stat. § 33-811(B). The deed is conclusive evidence of compliance as to a third-party purchaser for value without notice thereby assuring the buyer of uncontested title. For a sample form, see [Trustee's Deed Upon Sale \(Nonjudicial Foreclosure\) \(AZ\)](#).

The trustor, its successors or assigns, and any party to whom the trustee has provided notice by mail, waives any defenses to the sale not raised prior to the sale date and the subject of injunctive relief that is issued prior to 5 p.m. the last business day before the sale. Ariz. Rev. Stat. § 33-811(C). Any order must be delivered to the trustee within 24 hours of its entry, but no later than the 5 p.m. deadline. The nature and intent of this statute is very effectively addressed in the original *BT Capital, LLC v. TD Serv. Co. of Ariz.*, 265 P.3d 370 (App. 2011) (holding that TD and PCF were not entitled to judgment as a matter of law), opinion vacated and case remanded to trial court by *BT Capital, LLC v. TD Serv. Co. of Ariz.*, 275 P.3d 598 (2012) (affirming the superior court's entry of summary judgment). To ensure that the real property can reenter the stream of commerce, the foregoing statutes provide finality

to the sale and comfort to the ultimate purchasers. The statute does not preclude a party from bringing an action that is independent of the sale. *Bank of America, NA v. Felco Business Services, Inc.*, 403 P.3d 150 (2017).

To the extent that an action is brought to enjoin the sale, or address issues involving the beneficiary, the trustee is not an appropriate party to the action. The trustee is bound by any order entered against the beneficiary. If the trustee is named, the trustee must be immediately dismissed from the action and the trustee is entitled to an award of its damages, including costs and reasonable attorney's fees. Ariz. Rev. Stat. § 33-807(E).

Determination of the Bid and Disposition of Proceeds

The opening bid should consist of the outstanding balance (principal and interest) owed to the beneficiary, together with any advancements that were made to protect the beneficiary's lien position or the property and the costs and expenses of conducting the sale (the cost of the title report, mailing and photocopying, recording, posting, publication, any postponement fees, auctioneer fees, trustee's fees, and allowable attorney's fees incurred in protecting and preserving the beneficiaries interest in the real property). Assuming the fair market value of and the equity in the property exceeds this amount, the bid should incorporate these amounts and will be a credit bid at sale.

Having determined the maximum bid pursuant to the above analysis, the beneficiary must also evaluate its bid based on the potential effect of the fair market value of the property being less than the maximum bid amount. In such event, how does the beneficiary preserve a deficiency claim?

The ability to establish a deficiency claim is set forth in Ariz. Rev. Stat. § 33-814. The considerations to be evaluated include (1) the beneficiary's right to a deficiency (do the terms of the note make it nonrecourse or is a deficiency precluded as a matter of statute?), (2) the fair market value of the real property on the date of sale, and (3) the senior liens that appear prior to the beneficiary's lien on the property. Assuming deficiency rights exist, the determination of the deficiency bid will be predicated upon the amount of equity, as established by credible appraisal evidence, that exists in the property to satisfy a portion of the claim of the beneficiary. To determine this amount, the beneficiary must deduct the senior lien amounts from the fair market value and then compare the amount owed against the remaining value. The bid should represent the available equity and the deficiency (the remaining amount of the debt after crediting the equity).

Under Ariz. Rev. Stat. § 33-814, if the beneficiary seeks a deficiency, the trustor and/or guarantor(s) are entitled to a credit for either the fair market value of the property (less the amount owed senior liens) on the date of sale or the amount bid, whichever is greater. Accordingly, the beneficiary cannot underbid and seek a greater deficiency, and in the event of an overbid, the trustor and/or guarantor are entitled to a larger credit and the deficiency claim of the beneficiary is reduced. As a practice pointer, deficiency issues should be addressed at the inception of the proceeding and appropriate action taken to verify if a deficiency exists, and if so, in what amount. Deficiency claims are discussed in further detail below.

The proceeds of the sale are disbursed in the following order:

1. The costs and fees of completing the sale
2. The amounts owed to the beneficiary under its contract
3. All other amounts that may be owed to the beneficiary

To the extent that the bid amount exceeds the amount owed to the beneficiary, and subject to available amounts, excess proceeds are distributed in the following order:

1. To any condominium or community association that are owed assessments
2. To junior lienholders based upon priority
3. To the trustor

Excess Proceeds

After payment in full of all of the expenses of sale and the amounts owed to the beneficiary, the trustee has several options available for the payment of any additional proceeds acquired as a result of the sale of the property. Within 15 days after completion of the trustee's sale, the trustee must mail notice to all junior claimants advising them of the existence of excess proceeds. The trustee may then, as one option, disburse the funds in the order of the priority listed in the title report, with each junior lienholder being paid in full in accordance with their priority prior to disbursement to the next junior lienholder. This is an ill-advised method of distribution for at least two reasons. First, the trustee must rely upon the title report as to lien priorities, which may later prove inaccurate. Second, the trustee must also rely upon the junior lienholders assertions as to the amounts that they may be owed. If either of these may be incorrect, the trustee may be exposed to potential liability.

A more appropriate way to deal with the distribution of excess proceeds is found in Ariz. Rev. Stat. § 33-812(C) through (P). Under these provisions, within 90 days of the sale, the trustee shall deposit the excess proceeds with

the county treasurer in the county in which the property is located pending an order from the Superior Court. The trustee, as the plaintiff, will then initiate a civil action naming the county treasurer as the defendant and mail a conformed copy of the complaint, by certified or registered mail, to all parties who were entitled to notice under Ariz. Rev. Stat. § 33-809 and any other person known by the trustee to claim an interest in the property. The mailing must include a copy of one of the following: (1) the trustee sale guarantee and all amendments or endorsements, (2) the title search used by the trustee, or (3) a detailed description of all liens and encumbrances used by the trustee in furtherance of the sale. The mailing must also include a list of all persons receiving notice, a detailed description of all distributions that have been made, and a narrative description of all liens and encumbrances and their priority. The trustee will not have liability for the accuracy of the narrative description. Upon completion of the mailing, the trustee is dismissed from the action without prejudice and is entitled to his or her reasonable costs and attorney's fees incurred in this process.

Any party with an interest in the excess proceeds may apply for the amount they claim and within three days of the application, must serve, by any form of mail that requires a signed acceptance, a copy of the application to the county treasurer and all parties listed in the mailing. An affidavit of mailing must be filed with the court establishing the receipt or nonreceipt by all required parties to the mailing. If a mailing is returned with a forwarding address, the applicant must send a new mailing to the forwarding address and file a subsequent affidavit.

Within 45 calendar days of receipt, any party claiming an interest in the proceeds must file a response and mail it to each applicant. Each applicant is then provided 10 days to reply. Upon expiration of the 10-day reply period, the applicant provides notice to the court, and all parties entitled to notice, that the process has been completed. The court, absent any dispute as to priority or amount, must then issue an order to the treasurer to disburse funds in accordance with the priority set forth in the order. In the event of a dispute, the court will refrain from issuing an order for 180 days, allowing the parties to request a hearing to determine the dispute. Upon resolution of the dispute, the court will issue an order to the treasurer to disburse the proceeds.

If the proceeds are not claimed within two years, the funds are deemed abandoned.

A cottage industry has evolved as a result of the rise in excess proceeds claims. Third parties have sought to purchase the rights of junior interests at a discount and

then pursue the claims for their own self-interest. To counteract the growing disparity which resulted from the uninformed junior interest selling its interest to an experienced purchaser, the legislature enacted Ariz. Rev. Stat. § 33-812(P) which limits third parties rights to purchase interests.

Deficiency Claims

A growing body of law has arisen due to the recent recessions and flattening of real property values. Again, absent language in the note or deed of trust to the contrary or a statutory provision, a beneficiary is entitled to a deficiency claim. Ariz. Rev. Stat. § 33-814 sets forth the process and procedure for establishing a deficiency amount and obtaining a deficiency judgment. Determining the amount of a deficiency bid is discussed above. Assuming a deficiency bid has been made and represents the successful bid, the beneficiary is required to initiate a formal legal proceeding within 90 days of the date of the sale of the trust property. The statute is a statute of repose, and not limitation, and the failure to timely comply will preclude any right to recovery. While the process, up to this point, has not required court intervention (except to the extent injunctive relief may be sought under Ariz. Rev. Stat. § 33-811), the recovery of a deficiency requires involvement of the superior court. A formal complaint is filed with the court, and a priority hearing is then set to determine the right to, and amount of, a deficiency judgment. At the priority hearing, the beneficiary must establish by competent evidence the amount of its debt and the fair market value of the property on the date of sale, the same requirements necessary to establish a deficiency under the judicial foreclosure statute. To the extent the debt exceeds the value—as established by the court—the beneficiary is entitled to a judgment for the difference. The borrower and/or guarantor are entitled to a credit for the greater of the amount bid at sale or the fair market value of the property (less senior liens). The process is the same whether the property is used for commercial purposes, or residential (subject to the following discussion).

As with the judicial foreclosure statutory framework, the trustee's sale statute also contains an anti-deficiency provision. Ariz. Rev. Stat. § 33-814(G). If the property is comprised of two and one-half acres or less that is limited to and utilized as a single one- or two-family dwelling and is sold pursuant to the trustee's power of sale, the beneficiary, as a matter of law, is precluded from seeking a deficiency judgment. The same policy considerations behind Ariz. Rev. Stat. § 33-729 apply to trustee's sales. However, unlike Ariz. Rev. Stat. § 33-729, Ariz. Rev. Stat. § 33-814 does not limit its application to purchase

money loans. In the event of a trustee's sale, a deficiency under this statute is precluded on any loan, regardless of whether it is a purchase money loan, or not, provided the property qualifies in size and use. Accordingly, to obtain a deficiency on a residential foreclosure under this statute, it is incumbent upon the beneficiary to establish that the property does not qualify for protection. As a result of the language contained in the statute, Arizona courts have addressed various issues regarding the qualification of the property under the statute. The following will summarize a number of relevant decisions. For this reason, it is imperative to discuss the case law which created various issues the legislature addressed in their revisions to Ariz. Rev. Stat. § 33-729 and Ariz. Rev. Stat. § 33-814.

In *M & I Marshall & Ilsley Bank v. Mueller*, 268 P.3d 1135 (Ct. App. 2011), the court was asked to determine if the borrower of a partially completed house, which would qualify under the statute if fully completed, is entitled to protection under the statute. Ignoring a normal interpretation of the term "utilized" in the statute, the court expanded the interpretation of the statute to include the borrowers "intent to utilize" as the foundation for protecting the borrower and finding that the statute precluded recovery of a deficiency after the foreclosure. But see *BMO Harris Bank, N.A. v. Wildwood Creek Ranch, LLC*, 340 P.3d 1071 (2015), which overruled *Mueller* by holding that the anti-deficiency statute did not apply until the dwelling was completed on the property.

In *Mid Kansas Fed. Sav. & Loan Ass'n v. Dynamic Dev. Corp.*, 804 P.2d 1310 (1991), the issue raised was whether a commercial developer, with no intention to utilize the spec homes he was constructing, would be entitled to the protection of the anti-deficiency statute. While the ultimate outcome of the case was reached based upon additional considerations, the court did determine that absent express limiting language in the statute or explicit evidence of legislative intent, the court could not hold that the statute excludes a residential developer from its protection. The same determination was made in *Northern Arizona Properties v. Pinetop Properties Group*, 725 P.2d 501 (App. 1986) in which the court determined that the statute protected investors in a rental property that qualified under the statute for protection from any deficiency. Based upon these decisions, as long as the real property qualifies under the statute based on its use and size, the borrower's intentions are not a consideration. The same holds true of an ownership interest in a time-share. So long as the real property qualifies, the borrower is afforded the protection of Ariz. Rev. Stat. § 33-814; see also *Independent Mortgage Co. v. Alaburda*, 281 P.3d 1049 (App. 2012).

As discussed above, the legislature enacted identical revisions to Ariz. Rev. Stat. § 33-729 and Ariz. Rev. Stat. § 33-814 to address the issues created by these rulings. The legislature codified that loans secured by real property originated after December 31, 2014, no longer qualify under the statute if (1) the borrower is engaged in the business of constructing and selling dwellings and the deed of trust was given for the purpose of construction for the sale to another person, (2) real property that contains a dwelling was never substantially completed, or (3) property that contains a dwelling has never actually been utilized as a dwelling; Ariz. Rev. Stat. § 33-814(H). For the purpose of these statutes, substantial completion means that the property has been the subject of a final inspection by the governmental entity that issued the original building permit or if a final inspection is not required, the dwelling has been completed in all material respects as prescribed in the applicable ordinances and regulations of the government entity that issued the building permit; Ariz. Rev. Stat. § 33-814(I). The intent of these statutes was to effectively codify and overrule several of the above referenced decisions.

This raises another important practice pointer. It is essential to confirm whether the deed of trust was originated before or after the applicable date of the recent enactment. Loans originated prior to the December 31, 2014, date are subject to the case law in existence prior to that date. Confirm the size of the property and use to determine if Ariz. Rev. Stat. § 33-814 applies.

Crafty lenders have sought to circumvent the language of the statutes by incorporating contract terms that provide for the waiver of the borrower's and/or guarantors rights under Ariz. Rev. Stat. § 33-814. In response, the Arizona

courts have held that in residential loan documents, language waiving the rights of the trustor violate public policy and are unenforceable. Parkway Bank & Trust Co. v. Zivkovic, 304 P.3d 1109 (App. 2013). However, courts have held that the same public policy considerations do not apply to the guarantor (who is not subject to losing his or her residence), and have held that the guarantor can waive the protections afforded to him/her under Ariz. Rev. Stat. § 33-814. Arizona Bank & Trust v. James R. Barrons Trust, 351 P.3d 1099 (2015).

Despite lender attempts to enforce waiver provisions eliminating the fair market valuation hearing, Arizona courts have determined that such provisions are oppressive and violative of public policy considerations in both commercial and residential foreclosures and are unenforceable. CSA 13-101 Loop, LLC, v. Loop 101, LLC, 341 P.3d 452 (2014).

Action for Waste

Both the judicial nonjudicial foreclosure statutes provide for a separate action to recover a loss in the value of a lender's collateral based upon a separate action for waste. The action for waste is codified in Ariz. Rev. Stat. § 33-729(B) and Ariz. Rev. Stat. § 33-806(B). The trustee or beneficiary may maintain an action against any person, including the trustor, where damage occurs to the property through physical abuse or destruction to the property, waste, or impairment of the security. The provisions of Ariz. Rev. Stat. § 33-729 and Ariz. Rev. Stat. § 33-814 do not restrict or limit this action. Accordingly, an action for waste exists despite the fact that the borrower and the property may be subject to protection under the anti-deficiency statute.

Lawrence E. Wilk, Shareholder, Jaburg Wilk

For more than three decades, Lawrence E. Wilk has represented creditors, trustees, receivers, and debtors in significant bankruptcy cases in federal, state, and bankruptcy courts. His clients include banks, insurance companies, leasing companies, and private parties with investments secured by real property, commercial equipment, accounts receivable, and intangible property. An experienced and adept negotiator, Larry has assisted in restructuring and working out non-performing loans for clients. And, if the loans cannot be restructured, he has conducted hundreds of judicial and non-judicial foreclosures.

Larry has unique expertise in both multi-level marketing and Ponzi schemes having represented court-appointed receivers to recover significant monies invested through fraudulent schemes. He has been pivotal in several of the largest fraud cases arising in Arizona, which include real estate holdings, mortgage servicing, escrow, affinity investing, and a multi-level marketing jewelry company.

Corinne R. Viola, Associate, Jaburg Wilk

Well-versed in commercial litigation, Cori has represented clients as both plaintiff and defense counsel. At previous law firms, she helped clients navigate and resolve business disputes as well as representing institutional lenders in their creditor's rights matters. She has appeared in many Arizona courts on behalf of clients.

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