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# My Property Was Sold At a Foreclosure Sale. Do I Still Have to Pay Back The Loan?

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Just because the lender sold the property you put up as security for a loan at a foreclosure sale doesn't mean you are no longer responsible for paying the remainder of the debt it secured after application of the foreclosure sale proceeds.

When the real estate market was enjoying steady annual increases in value, a borrower who defaulted on a loan and whose property was sold at a foreclosure sale by the lender could often rely upon the foreclosure proceeds to pay most, if not all, of the balance of the loan secured by the property. However, where the value of the secured property has experienced a significant downturn, as was the case with many properties during the recent "Great Recession," a borrower can be left with a large deficiency balance that still must be paid to the lender.

## North Carolina's Anti-Deficiency Statutes

North Carolina has anti-deficiency statutes which prevent a lender from suing a borrower for the deficiency balance remaining after application of the foreclosure proceeds to the loan balance. However, they apply only in very specific circumstances.

Section 45-21.38 of the North Carolina General Statutes provides that a holder of a note or deed of trust is not entitled to a deficiency judgment when the mortgage or deed of trust was given to the seller of the property to secure the payment of the balance of the purchase price of the real property. Thus, under § 45-21.38, a seller who takes back a mortgage on the sold property cannot, upon a default by the buyer/borrower, foreclose and sell the property and then sue the buyer/borrower for any deficiency. However, if the lender is not the seller of the property (such as a bank that lends the buyer the purchase money, the most common situation), then this statute does not apply.

Section 45-21.38A is an anti-deficiency statute that applies to: (a) "Rate Spread Home Loans" originated on or after January 1, 2005 (including loans modified after January 1, 2005, which, because of the modification, became a Rate Spread Home Loan); and (b) "Nontraditional Mortgage Loans" (including loans which became Nontraditional Mortgage Loans through modification).

A "Rate Spread Home Loan" is a loan that meets all of the following requirements:

- The borrower is a natural person;
- The debt is incurred primarily for personal, family, or household purposes;
- The principal amount of the loan is less than the highest conforming loan size limit for a single-family dwelling as established from time to time by Fannie Mae;
- The loan is secured by a security interest in a manufactured home or a mortgage or deed of trust on real estate containing a one-to-four family dwelling (existing or to be built) which will be occupied by the borrower as a principal dwelling;
- The loan is for the purpose of purchasing the dwelling; constructing, repairing, rehabilitating, remodeling, or improving the dwelling or the real property on which it is located; refinancing an existing obligation secured by the same dwelling or real property; or consolidating existing consumer debts into a new loan; and,

- The loan's annual percentage rate exceeds all three of the rate spread characteristics defined in § 24-1.1F of the North Carolina General Statutes.

A "Nontraditional Mortgage Loan" is a loan that:

- Meets the first four requirements of the Rate Spread Home Loan set out above; and,
- Contains terms that allow the borrower to defer payment of principal or interest and allow negative amortization of the loan balance, meaning the loan balance increases over time, and does not decrease as payments are made on the loan.

The § 45-21.38A anti-deficiency statute further exempts:

- Certain home equity lines of credit;
- Certain construction loans;
- Certain reverse mortgages;
- Bridge loans with a term of 12 months or less;
- Loans made by a lender who is a natural person who makes no more than one loan in a 12-month period and is not in the business of lending; and,
- Loans secured by a subordinate lien on the borrower's principal dwelling, unless the loan was made contemporaneously with a Rate Spread Home Loan or a Nontraditional Mortgage Loan, and the property is occupied by the borrower as a primary residence at the time the foreclosure proceeding is commenced.

Only if the loan falls under either of the statutes summarized above will the lender be prohibited from seeking a deficiency judgment.

### **Deficiency Action Defense - Right To Setoff Under § 45-21.36**

If a loan is not one covered by the North Carolina anti-deficiency statutes described above, the lender can sue the borrower for a deficiency after foreclosure of the secured property. However, if the purchaser at the foreclosure sale is the lender itself, which is a common occurrence because lenders tend to "credit bid" the full amount of the unpaid balance on the loan, the borrower who owned the foreclosed property may look to the defenses provided in § 45-21.36 to ensure that the loan was credited with the true value of the property and not just what the lender paid in the foreclosure.

Section 45-21.36 provides that a borrower whose property was purchased at a foreclosure sale by the lender may allege and show as a matter of defense and offset that:

- The property sold was fairly worth the amount of the debt secured by it at the time and place of sale; or,
- The amount bid by the lender at the foreclosure sale was substantially less than the property's true value.

While the North Carolina courts have not set forth specific guidelines as to how low a bid must be to qualify as "substantially less" than the property's true value, at least one court has determined that a bid of 10% below the appraised value of the property is not substantially less, while another court has determined that a bid of more than 20% below the appraised value of the property was substantially less.

### **Conclusion**

Even though a borrower may have borrowed money and put up specific property as security for the loan with the idea that the property would be used to satisfy the debt if the borrower falls into default, keep in mind that unless the loan falls under the parameters of the anti-deficiency statutes as referenced above, the borrower may still be liable for the full deficiency balance due on the loan if the sale of the property does not result in sufficient proceeds to pay off the loan in full. Both borrowers and lenders need to keep these statutes in mind in order to avoid adding a nasty surprise to the already unpleasant result of a default.

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