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FINANCIAL RESTRUCTURING & BANKRUPTCY

# ALERT

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## NEW JERSEY TAX LIEN FORECLOSURES SUBJECT TO CLAW BACK

By Michael Viscount

Tax lien foreclosures in New Jersey are not protected from claw back actions under standard fraudulent conveyance theories – that according to three different New Jersey bankruptcy judges who have recently considered the matter. The most recent of these rulings was made this week in a matter handled by Michael Viscount, Ray Patella and Brian Isen of the Atlantic City office of Fox Rothschild LLP in the case of *Oyster Creek Inn, Inc.*, D.N.J. Bkr. Case No. 13-22624 (GMB). In the other *Oyster Creek* ruling, Chief Bankruptcy Judge Gloria Burns followed the rationale laid out in two earlier decisions of her court mates Bankruptcy Judge Judith Wizmur in *In re Varquez*, 502 B.R. 186 (Bankr. D.N.J. 2013) and Judge Michael Kaplan in *In re Berley Associates*, 323 B.R. 433, 434 (Bankr. D.N.J. 2013). All three judges have now concluded that under the New Jersey tax lien foreclosure procedure that does not require a judicial sale of the property at public auction, the transfer of the real estate does not carry with it the protections given to title transfers by mortgage foreclosure as articulated by the 1994 ruling of the U.S. Supreme Court in *BFP v. Resolution Trust Corp.*, 511 U.S. 531, 545 (1994).

In *BFP*, the Supreme Court held that “a fair and proper price, or a ‘reasonably equivalent value,’ for foreclosed property is the price in fact received at the foreclosure sale, so long as all of the requirements of

the State’s foreclosure law have been complied with.” In New Jersey, there is one major difference between a title transfer by foreclosure of a mortgage and a title transfer by foreclosure of a real estate tax lien. Under the state’s mortgage foreclosure procedure, the final step in the foreclosure process is a judicial sale by a county sheriff who first advertises and then conducts a sale with competitive bidding where anyone with a 20 percent deposit can participate. According to the judicial analysis, this establishes a “price” for the real estate that satisfies the reasonably equivalent value test for most claw back actions. The state’s procedure for tax lien foreclosure is different. In tax lien foreclosures, there is a two-step process with the taxing authority first auctioning the tax lien for a fixed amount equal to the outstanding tax. At this “tax sale” auction, the bidders compete by bidding down the interest rate on the lien. They do not establish a price for the real estate. The foreclosure process is completed when at the end of a subsequent lawsuit, the foreclosing lien holder obtains a final judgment and gives notice to the property owner and other interested parties that they have a set number of days to redeem by paying in full the amount of the tax liability plus interest, penalties and certain costs of the foreclosure. In the absence of redemption, the judgment of the court completes the conveyance and can be recorded in the same manner that one would record a deed. There

is no judicial sale as in a mortgage foreclosure case, and therefore no action to set a “price” for the real estate.

To paraphrase Judge Wizmur (whose words were repeated this week by Chief Judge Burns), in New Jersey, tax sale foreclosures are a two-step process, neither of which involves a “price” or a “foreclosure sale,” and without a “price” and a “foreclosure sale,” *BFP* [the U.S. Supreme Court case] cannot apply. Thus, New Jersey’s tax lien foreclose procedure does

not carry with it the protections of the mortgage foreclosure process to shield the transferee from fraudulent conveyance claims by the prior owner to claw back and regain ownership of the real estate.

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