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ALERT

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Impact of Tennessee's New Foreclosure - Deficiency Judgment Statute

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We are beginning to see Tennessee courts addressing questions that arise under Tennessee's recent foreclosure deficiency judgment statute.

The new law, which went into effect in September 2010, affects the amount of a deficiency judgment a lender can obtain when a lender has foreclosed on real estate securing its loan. The statute limits the amount of a deficiency that a lender can recover from a borrower or guarantor if the real estate was sold at foreclosure for a price that was "materially less" than the "fair market value" of the property on the date of foreclosure. If the court determines that the sale price at foreclosure was materially less than the property's fair market value, then the lender can only obtain a judgment for the difference between the amount of the loan indebtedness and the fair market value of the property.

Borrowers and guarantors are relying on the new law in negotiating restructure of loans with lenders and cases where lenders sue to obtain a deficiency judgment.

In determining the amount of the deficiency judgment that a borrower or guarantor is obligated to pay, the courts – and lenders – are faced with answering several questions which were left unanswered in the new law:

What definition of "fair market value" should be used? The Uniform Standards of Professional Appraisal Practice (USPAP) uses the term "fair value," not "fair market value." What difference is there, if any, between these terms since the Tennessee statute does not define "fair market value" and Tennessee case law provides various definitions of "fair market value?"

Is the owner's opinion of "fair market value" to be given any consideration? If so, to what extent? Can the court rely upon an appraisal obtained by a lender prior to foreclosure, particularly when most appraisals base valuations on a marketing period and are not based upon a value as of the date of foreclosure?

If the lender purchases the property at foreclosure, can a lender include cost of carry, insurance, taxes, etc., as part of the balance of the loan owed in determining the amount of the deficiency? If so, over what period of time?

Strategies are available to improve a lender's position in negotiating workouts with borrowers and guarantors, both before and after foreclosure, and in litigating the amount of a deficiency judgment a lender is entitled.

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