

Featured Professionals

Mark W. Vyvyan

Related Services

Real Estate & Construction

Minnesota Appeals Court Clarifies Borrowers Entitled to Surplus After Foreclosure by Action

Legal Update

05.26.2021

Deficiency judgments are common occurrences in mortgage foreclosures and typically arise when the amount bid at sale is less than the amount due on the mortgage debt. It is rare, however, when the amount bid at sale exceeds the mortgage debt. When this happens, Minnesota law directs that the resulting “surplus” is paid to the borrower. Minn. Stat. § 581.06 (2020). It is important to remember that the existence of a deficiency or surplus is determined at the time of the sheriff’s sale, and not a later resale, as determined in *State Bank of Young America v. Fabel*, 530 N.W.2d 858 (Minn. Ct. App. 1995).

A recent Minnesota Court of Appeals decision considered how the parties’ stipulation as to the amounts due under the mortgage can affect the amount of surplus. *SW Partners, LLC v. Trade Center Property, LLC*, A20-0773, 2021 WL 856071 (Minn. Ct. App. 3/8/2021) (unpublished). Previous decisions have found that a stipulated judgment amount can be used to calculate a deficiency judgment. *First Minnesota Bank v. Overby Development, Inc.*, 783 N.W.2d 405 (Minn. App. 2010).

In *SW Partners*, two affiliated companies borrowed \$1.8 million, secured by mortgages on two different properties. After the borrowers defaulted, SW (the creditor) brought three different actions to obtain a judgment for the outstanding amounts and foreclose on the properties. The Court of Appeals, in its opinion, indicated that it was unclear why the lender brought three different actions for the same underlying debt and why those actions were never consolidated.

The parties then stipulated the amounts owed, and the District Court entered three separate judgments (all relating to the same underlying debt) in the amounts of \$1,983,815.63, \$1,990,012.67 and \$2,005,371.35, respectively. The properties were subsequently sold at a sheriff’s sale for \$600,000 and \$1.8 million, with the highest bids coming from SW itself. Each party was then asked to submit a number as to what the surplus would be, assuming there is one, and the District Court accepted SW’s lower submission of \$273,900.38 and awarded the surplus to the borrower.

On SW’s subsequent appeal, the Appeals Court ruled that there was “obviously” a surplus, as the two bids totaling \$2.4 million exceeded even the highest of the three stipulated amounts. The most important lesson, however, came from SW’s attempt

Minnesota Appeals Court Clarifies Borrowers Entitled to Surplus After Foreclosure by Action

at using *Overby* to its advantage. In *Overby*, the Court substituted the stipulated amount as the mortgage debt, which was less than the total outstanding mortgage debt. The lender appealed, arguing that the surplus calculation should be based on the total outstanding mortgage debt, not the lesser stipulated amount. The Court rejected that argument, ruling that the “mortgage debt” should be reduced consistent with the portion of the property actually foreclosed upon. Since only part of the property had been foreclosed upon and the stipulation reflected that, the lesser amount of the stipulation was used for calculating a surplus.

SW, in its appeal of the case at hand, attempted to cite *Overby* as evidence that the stipulated judgment should be substituted for the mortgage debt amount for the purposes of determining the surplus. The Appeals Court dismissed that argument, distinguishing this case from *Overby* by relying on the underlying policy driving both cases – preventing lenders from abusing the system by overbidding and preventing redemption, while at the same time eliminating any surplus that would otherwise belong to the borrower. Instead, the Appeals Court affirmed the District Court’s ruling, which used SW’s submission of \$273,900.38 as the surplus amount, which was based off SW’s winning bids at the sheriff’s sale and the mortgage debt.

SW Partners serves as a reminder that lenders and borrowers should be careful when stipulating as to the amounts due on a mortgage, especially when such stipulated amount is materially different from the amount of the underlying mortgage debt. Similarly, this decision reaffirms that lenders need to be careful when placing a bid at sheriff’s sale and to always be certain they fully understand the impact of their bid.