

LOS ANGELES COUNTY BAR ASSOCIATION
PROFESSIONAL RESPONSIBILITY AND ETHICS COMMITTEE

FORMAL OPINION NO. 455

PURCHASE OF PROPERTY AT A FORECLOSURE/JUDICIAL SALE--
An attorney who only represents a mortgage company in bankruptcy court solely to obtain relief from the automatic stay is not prohibited from purchasing the property at a foreclosure sale provided that the mortgage company gives informed consent.

AUTHORITIES CITED:

Rule 4-300, Rule 3-300, Rule 3-310
(California Rules of Professional
Conduct); LACBA Ethics Opinion No.
283; LACBA Ethics Opinion No. 317;
Marlowe v. State Bar (1965) 63
Cal.2d 304, 46 Cal.Rptr. 326.

This Committee's opinion has been requested concerning the following circumstances. An attorney represents a mortgage company that has a loan on real property which has gone into foreclosure because of delinquent payments on the loan by the homeowner. The homeowner/trustor files a bankruptcy proceeding to forestall the pending foreclosure by the mortgage company. The mortgage company requests the attorney to obtain relief from the bankruptcy stay in order to allow the mortgage company to put the property back into foreclosure. The attorney files an action in the bankruptcy court to obtain relief from the bankruptcy stay and this enables the mortgage company eventually to put the property back into foreclosure proceedings. The mortgage company then proceeds with a foreclosure sale where it offers to

sell the property to the public pursuant to the foreclosure laws set forth in Civil Code §2924 et seq. The attorney requesting our opinion represents that the property can be sold to anyone interested in obtaining the property and is a public sale with all proper legal requirements taken. We are also asked to assume that the mortgage company has no opposition to the attorney working with other parties to purchase the property at the foreclosure sale and the attorney has not acted as a trustee or counsel to the mortgage company as to the foreclosure or subsequent sale.

Based on these facts, the following issues have been presented to us: First, can an attorney purchase property at a foreclosure sale with or without the informed consent of the mortgage company? Second, assuming that the attorney must obtain the informed consent of the clients, what type of disclosure is required to establish an "informed consent?"

With regard to the first issue, the Committee is of the opinion that an attorney may purchase property at a probate, foreclosure or judicial sale provided he or she does not violate Rule 4-300 of the California Rules of Professional Conduct which provides:

"A member of the state bar shall not directly or indirectly purchase property at a probate, foreclosure, receiver's, trustee's, or judicial sale in an action or proceeding in

which such member or any member affiliated by reason of personal, business, or professional relationship with that member or with that member's law firm is an attorney for a party or is acting as executor, trustee, administrator, guardian or conservator.

Rule 4-300, which became effective May 27, 1989 as part of the recently revised Rules of Professional Conduct, continues the longstanding prohibition found in prior rule 5-103 of the old Rules of Professional Conduct and prior to that Rule 8. Pursuant to these rules, and now embodied in 4-300, an attorney is prohibited from purchasing property at a probate, foreclosure, or judicial sale in which the attorney also appears as counsel for the party.

Rule 4-300 has been the focus of two prior Los Angeles County Bar Association opinions when the rule was previously set forth as Rule 8.

In Los Angeles County Bar Association Opinion No. 317 it was stated that an attorney who negotiated a sale of real property at an estate sale for an executor may not accept a finder's fee from the buyers of the property at the estate sale. Citing Rule 8 (now Rule 4-300), it was found that if the buyers of the property are willing to pay a finder's fee, they would presumably be willing to pay such additional sum for the purchase of the property. Therefore, in receiving a finder's fee, the attorney put himself in a conflict with the beneficiaries of the

estate since the additional sum that would be paid would have gone to the attorney's client. For this reason it was found in Opinion No. 317 that the attorney's conduct was unethical in representing both parties.

In Ethics Opinion No. 283 The Los Angeles County Bar Association stated that if an attorney appears for a client in a lawsuit to foreclose trust deeds on real property, he or she may not subsequently participate as a member of a group seeking to purchase the same property. In that opinion the attorney, as a purchaser, had an interest in seeking the lowest possible price on the property and put himself in a potential conflict with his client. Moreover, the facts indicated the attorney was responsible for establishing the foreclosure sale and had the client's information indicating the value of the property. The attorney also had the client's information of what he or she would be willing to accept as payment. Thus, it was found that even though the attorney disclosed his intent to purchase the property this would not dispel the attorney's interest in seeking the lowest possible price for the property while the client would want the highest possible price. Finally, in Ethics Opinion No. 283, the mortgage company's attorney participated in preparing the rules for the competitive bidding, and was also involved in conducting the advertising and notifying potential buyers of the property. Thus, not only did the attorney have a potential conflict with his client, his interest in purchasing the property

put the attorney in a conflict with the public at large. For these reasons it was concluded that even though the judicial sale would be open to competitive bidding, the dangers inherent in the conflict of interest cannot be eliminated because of the participation in preparing the rules for the competitive bidding.

Although the latter two opinions flatly prohibit the participation of attorneys in judicial foreclosure sales, we do not believe that it would be improper for an attorney to participate in a foreclosure sale in the facts presented to us in the present situation. In the present case the attorney does not appear as an attorney or trustee for the party (mortgage company) at the foreclosure sale. Nor does the attorney have any involvement in the scheduling of the sale of the property, conducting advertising on the sale, or notifying potential buyers. In the present case the attorney has only represented the mortgage company in the bankruptcy proceedings and we are of the belief that the bankruptcy action is not the "same action or proceeding" which would contemplate a complete ban on the attorney's subsequent interest in purchasing the property. The mortgage company would be represented by a trustee and may even have separate counsel that would safeguard the interest of the mortgage company. The company would also be protected by the provisions in Civil Code §2927 in assuring that the mortgage company receives a fair price for the property. Thus, we believe that Rule 4-300 does not prohibit the attorney from

participating in the purchase of the property.

However, this Committee is mindful of the considerations behind Rule 4-300 and is of the opinion that an attorney who participates, directly or indirectly, in the purchase of property at a foreclosure or judicial sale, in which a client retains an interest, does so fraught with peril. Marlowe v. State Bar (1965) 63 Cal.2d 304, 46 Cal.Rptr. 326. As the Supreme Court noted in Marlowe, any attorney challenged for violating Rule 4-300 would bear the burden of proof in such a transaction that counsel acted fairly in dealing with the client. Marlowe v. State Bar, 63 Cal.2d at 309, 46 Cal.Rptr. at 326.

Moreover, because of the various circumstances in which an attorney owes a fiduciary duty to a client, Rule 3-300 and Rule 3-310 would necessarily apply. These rules should be strictly adhered to in the type of situation presented to this Committee, and would require written informed consent from the party prior to the sale.

Rule 3-300 (former rule 5-101) regulates the conduct of attorneys entering into business transactions with their clients or acquiring certain interests adverse to their client.

In a similar fashion, Rule 3-310 (former Rules 5-102, 4-101) provides that an attorney shall avoid the representation of interests adverse to his or her client. In particular, an attorney is prohibited from representing a new client if the attorney obtains confidential information from a former client and uses such information without the client's consent. See also Business and Profession Code Section 6068(e).

Because of the application of Rules 3-300 and 3-310, informed consent must be given by the mortgage company allowing the attorney to participate at the foreclosure sale in the factual situation presented. Should the attorney obtain any information relating to the value of the property sought to be purchased, or other information that may be germane to the purchase price of the property, then this information must be provided to the client in order for the client to give effective informed consent under Rule 3-300.

Likewise, should the attorney obtain from the mortgage company any confidential information about the value of the property sought to be purchased, that information cannot be passed on to another client or used at the bidding by the attorney unless the mortgage company consents in writing to such information being used by another party.

Finally, the Committee is mindful that in certain transactions other than those presented here, parties may not have the same degree of knowledge about foreclosure or judicial sales as a mortgage company. Thus, the risks in participating in foreclosure sales by attorneys should be carefully evaluated where existing or previous clients may have had an interest in the property sought to be purchased.

This opinion is advisory only. The Committee acts on specific questions submitted ex parte and its opinion is based on such facts only as are set forth in the inquiry submitted.