

Rhode Island Supreme Court Rules That Condominium Assessment Liens Could Extinguish First-Priority Mortgages

First mortgage holders in Rhode Island beware: in a 4-1 decision handed down on December 4, 2015, the Rhode Island Supreme Court has ruled that pursuant to the Rhode Island Condominium Act, RIGL § 34-36.1-1.01 et seq., liens for six months of unpaid common fees prior to the foreclosure have super-priority status, and can extinguish first-priority mortgages under certain circumstances. In *Twenty-Eleven, LLC v. Michael J. Botelho, et al.*, the Court, interpreting § 34-36.1-3.16 of the Rhode Island General Laws, held that a first mortgage had been extinguished where the holder failed to either (i) pay the assessments, or (ii) exercise its right of redemption pursuant to § 34-36.1-3.21(c).

Plaintiff Twenty-Eleven purchased a condominium unit at a condominium lien foreclosure sale. PNC Bank, N.A. held a prior first mortgage on the condominium. Subsequent to the association's foreclosure sale, PNC sought to foreclose its mortgage. In response, Twenty-Eleven filed suit, seeking to quiet title, a permanent injunction enjoining PNC's foreclosure, and a declaration that PNC's interest was extinguished by the condominium lien foreclosure. PNC argued that the Rhode Island Condominium Act, as written, could not extinguish a first mortgage, and thus Twenty-Eleven purchased the unit subject to its lien. The Superior Court agreed with PNC, and determined that "nothing in the plain and unambiguous language of the statute * * * would extinguish a first mortgage's priority position with respect to a subsequent condominium lien foreclosure deed." On appeal, the Rhode Island Supreme Court reversed and remanded the matter for further proceedings.

In its decision, the Supreme Court reviewed the language of § 34-36.1-3.16(b), which defines the priority of lien an association receives for its assessments. Section 34-36.1-3.16(b)(1) states that a condominium lien for assessments is given priority over all other liens, with three exceptions: (i) any lien recorded prior to the condominium declaration; (ii) a first-priority mortgage recorded before the assessments sought to be enforced became delinquent; (iii) and any municipal tax liens.

However, § 34-36.1-3.16(b)(2) states that the association's lien will have priority over a first priority mortgage to the extent of the assessments due for the six months prior to the foreclosure, plus \$2,500 in reasonable attorneys' fees and \$5,000 in foreclosure costs. The Supreme Court ruled that this provision means that a condominium foreclosure sale involves two separate liens for assessments: a lien for assessments more than six months old that is second to a first-priority mortgage, and a super-priority lien which extinguishes all subsequent liens — including a prior recorded mortgage — for assessments due within the last six months of the foreclosure sale plus reasonable attorneys' fees (\$2,500) and costs (\$5,000).

The Supreme Court further ruled that nothing in the statute's language overturns the legal principal that foreclosing on a lien extinguishes junior liens. Therefore, PNC's lien was extinguished by the association's foreclosure, leaving only the statutory right of redemption created by § 34-36.1-3.21(c) as potential relief for PNC. This gives former first priority mortgage holders thirty days from a post-foreclosure sale notice to pay the assessments owed as well as the fees and costs associated with the foreclosure. Unfortunately for PNC, it missed the statutory redemption deadline, and so the Supreme Court ruled its interest in the unit was wholly extinguished.

The decision carries enormous consequences for first mortgage holders where the collateral is a condominium. Such mortgagees are now on notice in Rhode Island that notices of delinquent condominium fees and of condominium lien foreclosure sales should be acknowledged upon receipt. Advancing the condominium fees upon receipt of notice of delinquency, or exercising the right of redemption if there has been a condominium lien foreclosure are now the only ways to protect their first mortgage interests. Mortgagees

may also consider, as the Court suggested, requiring condominium assessments to be paid into an escrow account, along with insurance premiums and municipal taxes.

Massachusetts first mortgage holders breathe easy: under these facts, the result would be different, as the Massachusetts condominium lien law grants the same super-priority lien on six months of condo fees, but first requires condominium associations to bring lawsuits to enforce those liens.

It remains to be seen whether the Rhode Island General Assembly will be looking at the Supreme Court's decision in *Twenty-Eleven, LLC v. Michael J. Botelho, et al.*, during its 2016 legislative season.

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