



## **Land Banks and Tax Sales under the Municipal Claims and Tax Lien Law**

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### ***Summary***

*Pennsylvania's Land Bank Act, Act 153 of 2012, (the Land Bank Act) was enacted in November 2012 to enable local governments to form land banks as locally controlled entities for the purpose of amassing, inventorying, managing and marketing blighted, abandoned and tax delinquent properties. The Land Bank Act gives land banks, in concert with taxing bodies, the authority to acquire properties that are tax delinquent under Pennsylvania's tax sale laws. This memo sets out the potential options available to a land bank where the Municipal Claims and Tax Lien Law (MCTLL) governs.*

*MCTLL governs delinquent property tax enforcement in Philadelphia County, Allegheny County and the municipalities and school districts within Allegheny County. MCTLL also governs the collection of municipal claims, other than real estate taxes, throughout the Commonwealth. The Real Estate Tax Sale Law (RETSL) with its tax claim bureaus governs delinquent property tax enforcement throughout the Commonwealth but not in Philadelphia and Allegheny Counties. However, municipalities in RETSL districts as well as tax claim bureaus may adopt the provisions of MCTLL for delinquent property tax enforcement. The Housing Alliance has published a similar memorandum for RETSL jurisdictions.*

*Please note that this memo provides a general introduction for municipal officials, elected representatives and community leaders to support their participation in the discussion around land banking in Pennsylvania. Delinquent property tax enforcement is a highly technical, legal proceeding. Municipal solicitors and tax collectors' counsel have the best knowledge of applicable procedures. These experts should be consulted on specifics related to the properties and processes in their local jurisdictions.*

**Land banks may acquire properties through the MCTLL tax and municipal claim enforcement process.** Section 2117(d) of the Land Bank Act, provides options for how a land bank may intervene in MCTLL collection and enforcement proceedings. One option allows for the municipality to assign and transfer tax claims and/or municipal claims to the land bank which would allow the land bank to stand in the shoes of the municipality to collect and enforce those claims. Other options occur as part of the foreclosure proceedings for failure pay taxes or municipal claims, colloquially referred to as a ‘tax sale’. Under MCTLL, the tax sale is a sheriff’s sale which is an execution of a judgment against real estate to satisfy a debt. The sheriff conducts two, different, statutory, types of tax sales, the upset sale and the judicial sale. This article will generically refer to ‘tax delinquent property’ as the subject of the foreclosure but a municipal claim may be the basis of the judgment against the property.

Notably, MCTLL amendments allow a free and clear sale on the same day of the first sale in Philadelphia and Allegheny Counties only.

Traditionally, a tax delinquent property is exposed first at an upset sale for the minimum bid, or upset price, which is the amount that satisfies the tax liens and municipal claims against the property, and the costs of the sale. If the upset price is not bid, the property may be brought to a second sale, a free and clear judicial sale. Notably, MCTLL amendments allow a free and clear sale on the same day of the first sale in Philadelphia and Allegheny Counties only.

In order to divest a person of his or her interest in a property and sell a property free and clear of any tax lien, municipal claim or privately held interests, federal constitutional law requires due process notice be provided to those with a legally protected property interest.<sup>1</sup> This constitutional mandate puts the burden on whoever is initiating the sale (i.e. the plaintiff or more specifically for our purposes, the foreclosing taxing body, or perhaps the land bank) to (1) obtain a title examination that reveals all legally protected property interests, and (2) notify all those parties with an interest in the property of the pending sale. After tax sale on an occupied, not vacant, property, MCTLL provides for a nine month redemption period during which the owner may pay to get the property back.<sup>2</sup>

**Under the Land Bank Act, an agreement between the foreclosing taxing body and the land bank is required.** The agreement sets out the protocol for the land bank to purchase at tax sale or receive transfers from the foreclosing taxing body in accordance with the Land Bank Act and MCTLL procedures more thoroughly discussed below. There is a great deal of flexibility under the Land Bank Act as to whether the foreclosing taxing body is the bidder at sale and the land bank is the transferee or the land bank is the bidder, etc. As a matter of policy, information about

<sup>1</sup> This notice requirement is based on the U.S. Supreme Court ruling in the case of *Mennonite Board of Missions v. Adams*, 462 U.S.791, 103 S. Ct. 2706 (1984). It is often referred to as ‘Mennonite notice’.

<sup>2</sup> MCTLL section 7293. Despite no redemption on vacant properties, it is very difficult to obtain title insurance before nine months expires.

the land bank as bidder or transferee pursuant to the agreement should be standard language in all of the notices to the parties.<sup>3</sup>

In Allegheny County only, the required agreement is amongst any taxing bodies as well as any municipal authorities whose claims comprise the upset price.<sup>4</sup> Each and every parcel of real estate in Pennsylvania is subject to real property taxes charged by three taxing bodies: county, municipality and school district. The unpaid charges of certain authorities, like water authorities, are municipal claims. Municipal claims act like taxes in that they run with the land, in other words, a lien and accumulating interest remains against the property until paid or divested. In order to facilitate the clearing of public liens on properties acquired by the land bank, it makes sense for land banks in all counties to do as much as possible during the formation of a land bank to establish procedures, protocols and agreements amongst the three taxing bodies and municipal authorities.

**The upset sale does not traditionally provide free and clear title.** The upset price is the amount that satisfies all the outstanding taxes and municipal claims against the property that the sheriff is made aware of, as well as the costs of enforcement. The upset sale price typically does not include private liens or mortgages attached to the property, although any party in interest may bid to protect their interest in the property. As a result, the upset sale may remove the owner's interest and possibly even public claims, but the property may be subject to outstanding privately held mortgages, liens and judgments.<sup>5</sup>

**Pursuant to the Land Bank Act, at upset sale, the land bank can obtain the property for costs only if there is no higher bid.** The sheriff deputy conducting the sale would announce: "I have a bid for minimum. Are there any other bids?" Pause. "Hearing none, the property is sold to the {land bank name} per agreement between {foreclosing taxing body} and the {land bank name} pursuant to Act 153 of 2012." Where a third party bidder bids even an additional \$1.00 above minimum upset price, the third party bidder will acquire the property at upset sale instead of the land bank.

At upset sale, there are two key considerations for a land bank:

- the land bank can obtain the property for costs only if no one bids higher than the upset price; and
- the property may retain substantial liabilities such as private mortgages and judgments that will transfer to the land bank.

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<sup>3</sup> Under the Land Bank Act provisions that relate to RETSL, the sale advertisements are required to make reference to a potential bid by the land bank but the Land Bank Act provisions that relate to MCTLL do not include this requirement.

<sup>4</sup> Land Bank Act section 2117 (e.1)

<sup>5</sup> "[A] prior-in-time mortgage will not be divested by an upset sale, but will be divested at a free and clear sale." EMC Mortgage Corp v. Lentz, 972 A.2d 112, 116 (Pa.Cmwlt. 2009).

**The judicial sale is intended to “divest the property of its claims so the property can be returned to productive use under new ownership.”**<sup>6</sup> To divest the property of its claims means to free or rid the real estate title of the interests held against the property by third parties, such as tax liens, municipal claims as well as mortgages and judgments. Where the foreclosing taxing body fails to receive the upset price, traditionally, the property may be brought to a second sale, a free and clear judicial sale. To hold a judicial sale, the foreclosing taxing body must petition the court to issue notice to all interested parties asking why the property should not be sold free and clear of all claims, mortgages, and other types of debt against the property. Assuming proper notice is provided to all owners and others with an interest in the property, the court may issue the order that the property be sold free and clear of all claims and set a sale date. At that sale, the property is wiped clean of all tax liens and municipal claims, private liens and mortgages, etc. by virtue of the free and clear court order.<sup>7</sup>

**The credit bid, or bid of costs, is available under MCTLL and Pennsylvania Rules of Civil Procedure.**<sup>8</sup> Pennsylvania court procedures allow for a credit bid at either the upset or judicial sale. The credit bid is a bid by the plaintiff for the amount that is owed to it and which is secured by the property. The plaintiff offering the credit bid is not required to pay the deposit money at the time of the sale as a condition of the sale, nor is it required to pay the balance of the purchase price, since to actually pay this amount would be to pay money owed to itself. The highest bid the plaintiff can offer is the total amount due to it and sheriff fees, called ‘poundage’, are based on that amount. One possible scenario in the required agreement between the land bank and the foreclosing taxing body may provide that the foreclosing taxing body may credit bid and then transfer the property to the land bank.

**Property owners do not receive the proceeds from a credit bid.** Typically when a property is auctioned at tax sale, the buyer pays cash for the property and this money is distributed to all parties with a property interest in order of priority defined by law. The property owner is last on the distribution list. If there is a bid above the upset price, the sheriff prepares a schedule of distribution listing the parties that will be paid from the sale proceeds. Where there is a credit bid, the property owner and all others with a claim against the property will not receive any money realized from the sale since nothing is actually paid.

**The best opportunity for a land bank to obtain a tax delinquent property is after a free and clear court order is obtained and, in accordance with the order, the property is exposed to a free and clear sale.** As described above, a title exam is obtained and notice to all those with an interest in the property is provided as part of the free and clear court order which may be obtained prior to the first sale in Philadelphia and Allegheny Counties. Again, assuming proper notice has been provided to those that hold an interest in the property, those property interests may be divested in accordance with the free and clear court order.

Under the Land Bank Act provisions that relate to MCTLL judicial sales, the foreclosing taxing body and the land bank may enter into a prior agreement to set the sale price and to “alter the

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<sup>6</sup> City of Allentown v. Kauth, 874 A.2d 164 (Pa.Cmwlt. 2005).

<sup>7</sup> See EMC Mortgage Corp in footnote 4.

<sup>8</sup> MCTLL Section 7279; PA Rules of Civil Procedure, Rule 3133.

form, substance and timing of the sales price”.<sup>9</sup> In other words, prior to the judicial sale, the foreclosing taxing body and the land bank may agree on a purchase price and on non-monetary, performance-based terms that will satisfy that purchase price. This allows, for example, an agreement that the land bank is expected to expend funds for rehabilitation, demolition, or maintenance of the property and land bank does not pay any purchase price at tax sale.

Furthermore, these Land Bank Act judicial sale provisions also say the property is “deemed sold to the land bank regardless of bids by other parties”.<sup>10</sup> This trump bid means automatic transfer to the land bank regardless of other bids if the land bank and the foreclosing taxing body have entered into a prior agreement. The sale of the property to the land bank is transacted at the judicial sale by way of an announcement by the sheriff deputy conducting the sale, that the property is “sold to the land bank per agreement between {foreclosing taxing body} and the {land bank name} pursuant to Act 153 of 2012.” The land bank acquires the property at judicial sale with free and clear title. MCTLL and the Land Bank Act provide procedures for multiple parcels to be included in one court petition for a judicial sale.

**Property owners and those with an interest in the property will not be compensated where the land bank offers a trump bid.** The Land Bank Act’s trump bid, or preemptive bid provision, at judicial sale has raised questions by Pennsylvania attorneys who view the public auction at tax sale as the opportunity to potentially obtain a high bid to satisfy property debts and to provide any remaining proceeds to the property owner. To the best of our knowledge, there is no constitutional right to a public auction since an owner or party with an interest in the property has an unconditional legal right to halt a tax sale at any time prior to the moment of sale. All of the federal constitutional law in this field deals with due process requirements of notice and hearing, not any substantive right to an auction. Further, tax sales are not considered takings under federal constitutional law because any party with an interest in the property has a right to redeem the property by paying outstanding liens and judgments prior to completion of the sale.

**A quiet title action may be needed to obtain insurable title.** It is especially critical that a title insurance policy be issued on land banked properties identified for development as opposed to permanent open or green space. Some title insurance providers will never insure a property that has been subject to a tax sale even with a free and clear order. Some may issue title insurance based on their review of the tax sale file. Some may require a quiet title action, a court action to remove clouds on title. Whether acquired through tax sale or other means, the Land Bank Act provides for ‘Expedited quiet title proceedings’<sup>11</sup> on multiple properties within a single action and under specified court time frames. Some title insurance providers are of the opinion that quiet title actions are to be used only for the removal of invalid claims against the property, but other providers will insure based on a judge’s order quieting title when the lien or claim holder fails to respond to the quiet title action. It is important for land banks to develop a working relationship with a quality title insurance provider that insures title on the type of problematic properties that tend to end up in a land bank.

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<sup>9</sup> Land Bank Act section 2117(d)(3)(1).

<sup>10</sup> Land Bank Act section 2117(d)(4)(ii).

<sup>11</sup> Land Bank Act section 2118.