

REPORT OF THE NEW JERSEY JUDICIARY WORKING GROUP ON TAX SALE FORECLOSURES

Introduction

The United States Supreme Court in Tyler v. Hennepin Cnty., 598 U.S. 631, 143 S. Ct. 1369 (2023), held that local government’s retention of the excess value of the home above the plaintiff’s tax debt in a tax foreclosure was plausibly alleged as a violation of the Takings Clause of the U.S. Constitution. Like the Minnesota process, New Jersey statutes (N.J.S.A. 54:5-86 et seq.) and Court Rules permit a municipality or a private investor to obtain title to a property subject to unpaid taxes without a public sale and without any process for the property owner to retain the surplus equity beyond the amount of unpaid taxes.

In response to the Court’s decision in Tyler, Chief Justice Stuart Rabner established the Judiciary Working Group on Tax Foreclosures (“Working Group”) to critically reexamine the tax foreclosure process in New Jersey and, to the extent applicable, identify issues for consideration by the Legislative and Executive branches to ensure alignment with constitutional requirements.

As an initial response to the Tyler Court decision, even before the establishment of the Working Group, the New Jersey Supreme Court issued a July 10, 2023 Order that temporarily suspended Office of Foreclosure recommendations of final judgment in tax sale certificate cases pending as of May 25, 2023. The Court in that July 10, 2023 Order also relaxed certain Court Rules governing in rem and in personam tax foreclosures. Those actions, however, only address procedural requirements within the purview of the Court and do not touch on the underlying issues that may be implicated by Tyler.

The Working Group brought together governmental representatives¹, as well as representatives from the League of Municipalities, the New Jersey Association of Counties, Legal Services of New Jersey, Center for Social Justice at Seton Hall, county counsel, sheriffs, the Superior Court Clerk, and

¹ Designees of legislative members attended the meetings but were non-voting participants.

private attorneys including designees of specialty bar associations. Administrative Director of the Courts Glenn A. Grant chaired this broad-based working group which operated with the understanding that the Judiciary plays a secondary, supportive role in this process. Any substantive resolution of the issues raised in Tyler will be achieved by the Legislative and Executive branches, with conforming Court Rules and updated forms to follow.

Accordingly, the Working Group respectfully offers this report to assist legislative and executive branch leaders in their review and action on these important issues that affect the interests of municipalities, which are required to address unpaid property taxes through public sales, but also the private investors who purchase tax sale certificates as an investment vehicle and, finally, property owners who may have surplus equity in the property beyond their tax debt. Until the Legislative and Executive branches address the issues that the Tyler decision implicated as to New Jersey's tax sale foreclosure process, the respective interests of those involved in that process remain uncertain.

The Working Group's brief report includes five sections: (1) an overview of the current tax sale foreclosure process in New Jersey; (2) a non-exhaustive list of stakeholder interests and concerns;² (3) proposed preliminary updates to Judiciary forms (with final versions to conform to any legislative amendments); (4) a list of statutes and Court Rules that govern tax sale foreclosures; and (5) additional questions raised in discussion.

(1) New Jersey Tax Foreclosure Overview

Property taxes constitute a continuous lien on real estate. Failure to timely pay property taxes ultimately may lead to a tax sale. At the tax sale, the municipality that is owed taxes does not sell title to the delinquent property but instead sells a tax sale certificate, which serves as a lien on the property. The successful bidder must pay the municipality the delinquent taxes, costs, and any interest accrued to that date of the tax sale in exchange for the tax sale certificate. The successful bidder must also pay delinquent subsequent taxes

² The list is limited to discussions that occurred within three Working Group meetings. There are other stakeholder interests and concerns neither raised within the Working Group nor addressed in this Report.

in order to maintain its priority position, and earns up to 18% interest on those paid taxes.

If no one bids on the tax delinquent property at the tax sale, the tax sale certificate by default is owned by the municipality which can opt to proceed with a foreclosure action after six months. In cases where the tax sale results in a tax sale certificate, after two years the holder of the certificate, as a lien holder, can begin proceedings in Superior Court to foreclose on the property. If foreclosure is perfected, then fee title to the real estate is changed to that of the lien holder who can then apply to take possession of the property.

Except for the rare cases in which the federal government has a lien on the underlying property, in these foreclosures there is no sheriff's sale and no opportunity for the property owner to recoup any portion of their surplus equity before title to the property vests in the municipality or the private lien holder who secured the tax sale certificate. When the lien holder obtains title in a tax foreclosure, the final judgment also extinguishes the interests of any mortgagee (or other lien holders) in the property.

- ***Volume of Tax Foreclosures in New Jersey***

Each year, more than 1,000 properties in New Jersey proceed through tax sale foreclosure. Many property owners lose significant surplus equity since absent redemption there is no way in the current law to protect such equity. Like the homeowner in Tyler, New Jersey property owners who owed modest tax debts lose their surplus equity since the New Jersey Tax Sale Law provides no method to preserve their surplus equity. At the same time, taxes are the lifeline of a municipality: a municipality must fund the schools and pay the county its share of taxes even if the property owner does not pay property taxes.

- ***In Rem and In Personam Actions***

A private lien holder can proceed to foreclosure following the in personam (against the person) process. Except as to abandoned properties, only a municipality can proceed to an in rem (against the property) foreclosure.

Whereas Tyler involved an in rem action in which the plaintiff failed to

timely answer or appear, the same constitutional principles could arguably also apply to an in personam foreclosure. Accordingly, the Court's July 10, 2023 Order provided temporary procedural adjustments to both types of actions.

The Appellate Division has since issued one published opinion, [257-261 20th Avenue Realty v. Alessandro Roberto](#), A-3315-21 (Dec. 4, 2023), petition for cert. pending, finding that "the application of Tyler to New Jersey's similar TSL framework establishes that the confiscation of a New Jersey property owner's equity, through a tax sale foreclosure, violates the Fifth Amendment Takings Clause." In addition, the Appellate Division has issued a handful of unpublished opinions, some of which address the potential applicability of Tyler to in personam actions. See e.g., [Reo v. Johnson](#) 2023 N.J. Super. Unpub. LEXIS 907, 2023 WL 3987453 (App. Div. 2023); [Ace Holding v. Corr](#), 2023 N.J. Super. LEXIS 1303; 2023 WL 4770872 (App. Div. 2023); [Arianna Holding Co., LLC v. Doohaluk](#), 2023 N.J. Super. Unpub. LEXIS 2095, 2023 WL 7931256 (App. Div. 2023).

- ***Initial New Jersey Supreme Court Response to Tyler***

As noted, the Court in its July 10, 2023 Order directed the Office of Foreclosure to temporarily suspend review of motions and recommendation of entry of judgment in all tax sale foreclosure actions pending as of May 25, 2023. This temporary pause was intended to allow time to develop an interim protocol that would incorporate for tax sale foreclosures certain safeguards applicable to non-tax foreclosures, i.e., multiple notices and opportunities for the property owner to answer, object, defend, or redeem. While such procedural aspects can be addressed by the Court, the broader questions of how tax sale foreclosures should be handled -- including whether, and, if so, when, a tax foreclosure should proceed to public sale -- remain for legislative and executive branch determination.

In conjunction with the pause by the Office of Foreclosure, the Supreme Court further authorized, on an interim basis, relaxation of a number of Court Rules (specifically Rules 4:64-1(c), 4:64-1(d), and 4:64-7(c)) so as to require in tax sale foreclosures that notice be provided to the property owner of all dispositive pleadings, including personal service of all prejudgment notices including the notice of motion for entry of judgment, and treatment as an answer of any claim that a party has equity in the property.

(2) Stakeholder Interests

The Working Group focused its discussions on the pre-complaint, judicial, and post-judgment processes related to tax sale foreclosures. The Working Group's main objective was to highlight issues and concerns within those processes that could be considered by the Legislature and Governor in potentially amending the current statutory framework.

As part of its review, the Working Group considered the varied interests of property owners, investors, municipalities, and attorneys. The Working Group's discussion coalesced around the following concerns:

- Property owners have an interest in retaining any surplus equity they may have in the property post-sale and should be clearly informed of the requirements for redemption;
- Property owners have an interest in being provided an opportunity to redeem a property tax sale certificate to avoid loss of housing and home equity through foreclosure. Redemption may include selling their properties on the private market prior to title transferring to another party in the foreclosure process;
- Municipalities often encourage investment in tax sale properties to help return properties to productive tax rolls, and to maintain lower property tax rates for all residents; and such municipalities also work to enable residents to remain in their homes when feasible;
- Historically, investors have had an interest in gaining equity from the foreclosed property, and may be disincentivized to invest in areas of the State where property values are low unless there is the potential to obtain certain properties without the expense of public sales; and
- Attorneys require clarity as to the law and Court Rules to properly advise their clients.

(3) Proposed Preliminary Updates to Judiciary Forms

All members of the Working Group agreed as to the importance of clear communication with parties involved in tax sale foreclosures, including

unrepresented homeowners who have fallen behind in their taxes. To that end, the Working Group reviewed and suggested revisions to certain forms and notices to improve consistency and support understanding by parties involved in the tax sale foreclosure process. The proposed revisions to court forms, as well as suggested new forms, would convey to property owners in plain language the need to respond, and the process for responding, in a tax foreclosure action. The proposed revisions would explain what equity is and encourage property owners to seek legal counsel.

These proposed new and revised draft documents are available at njcourts.gov. Final updated versions of any forms will ultimately rely on and incorporate the requirements of any new law.

(4) Relevant New Jersey Statutes and Court Rules

The Working Group respectfully suggests that the Legislature consider the following statutory provisions as part of any proposed legislative response to Tyler. If statutory changes are enacted, Court Rules and forms will be amended to implement those substantive changes.

Pre-Foreclosure	Statute(s) or Court Rule(s) Affected
<i>Statute of Limitations</i> The current timeframe to file for property tax foreclosure is 20 years, except there is no limitations period if the tax sale certificate is held by a municipality.	N.J.S.A. 54:5-79 The statute of limitations for residential mortgage foreclosures previously was reduced to six (6) years. The Working Group notes that a shorter statute of limitations for property tax foreclosures, at least for those filed by third-party investors, could preserve equity but might also result in other unintended consequences such as quicker loss of title.

<i>Notices</i> In the current process, to be eligible to recover counsel fees, counsel must give written notice 30 days before filing the complaint to the parties entitled to redeem.	N.J.S.A. 54:5-97.1 R. 4:42-9(a)(5) Counsel fees are ancillary to the issues raised in <u>Tyler</u>. For clarity, the Working Group suggests that counsel fees and costs for tax sale foreclosures should be addressed by statute and conforming Court Rules.
<i>Premiums on Judicial Sale</i> The current tax sale foreclosure process provides that a premium can be bid at tax certificate sales when the bidding drops below 0% interest.	N.J.S.A. 54:5-33 Though beyond the scope of <u>Tyler</u>, the Working Group notes without any recommendation or agreement that a premium-based (rather than interest-based) system might be one option to protect a homeowner's equity and a municipality's right to sell a property subject to unpaid taxes.

Judicial Process	Statute(s) or Court Rule(s) Affected
<i>In Rem Procedures</i> In contrast to residential foreclosures, the current tax sale foreclosure process does not provide for a sheriff's sale. Rather, individuals can use the <i>In Rem</i> foreclosure procedure (N.J.S.A. 54:5-104.32).	N.J.S.A. 54:5-104.32 The Working Group suggests that any statutory changes extend to both <i>in rem</i> and <i>in personam</i> tax sale foreclosures.

<i>Election of a Judicial Sale</i> Currently, unless the United States is a defendant, tax foreclosure final judgments act as deeds to the property that transfer title to the plaintiff (i.e., the defendant has no right to elect for a judicial sale).	N.J.S.A. 54:5-104.65 This goes to the central issue in <u>Tyler</u>, i.e., the ability of a lienholder to obtain the deed to the property without a sale and opportunity for the property owner to recoup surplus equity. The Working Group discussed that property owners should have an option to request a public sale at which such equity would be recovered.
<i>Service</i> Court Rules do not require personal service once a property owner has defaulted.	R. 4:64-7(c) Though ancillary to the core issues of <u>Tyler</u>, personal service of all dispositive pleadings could be considered.
<i>Order Setting Amount, Time, Place of Redemption (OST)</i> In the current process, after the OST procedure, the final judgment conveys the deed to property.	R. 4:64-1(f) R. 4:64-7(g) Like N.J.S.A. 54:5-104.65, this goes to the central issue in <u>Tyler</u>, i.e., the ability of a lienholder to obtain the deed to the property without a sale and opportunity for the property owner to recoup surplus equity. The Working Group discussed that property owners should have an option to request a public sale at which such equity would be recovered.

<i>Recovery of Legal Fees</i> In the current <i>in personam</i> procedure, legal fees are awarded at the OST stage or, if there is a pre-judgment redemption of the property, on the motion of counsel. In the current <i>in rem</i> procedure, legal fees are only awarded on the motion of counsel.	N.J.S.A. 54:5-97 The Working Group discussed that counsel fees and costs for tax sale foreclosures should be addressed by statute and conforming court rules. (See above)
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Post-Judgment	Statute(s) or Court Rule(s) Affected
<i>Sale of Property</i> Currently, a sheriff's sale only takes place if the United States is a party (28 U.S.C. 2410).	N.J.S.A. 54:5-104.65 If Legislative and Executive Branch leaders determine to establish a process for public sales in tax foreclosures, the Working Group discussed that the statute should set out the scope and process for such sales.
<i>Disposal of Property – No Bidder</i> Currently, unless the United States is a defendant, tax foreclosure final judgments act as deeds to the property that transfer title to the plaintiff.	N.J.S.A. 54:5-87 This goes to the central issue in <u>Tyler</u>, i.e., the ability of a lienholder to obtain the deed to the property without a sale and opportunity for the property owner to recoup surplus equity. The Working Group notes that a writ of execution process, as used in residential mortgage foreclosures, could resolve concerns about potential takings.

<i>Surplus Monies</i> As noted, unless the United States is a defendant in the case, tax foreclosure final judgments act as deeds to the property that transfer title to the plaintiff. Currently, if there are surplus funds in a tax foreclosure case that proceeds to sale, those funds are deposited with the court, and any interested parties may apply for them in accordance with R. 4:64-3.	N.J.S.A. 54:5-87 N.J.S.A. 54:5-9 R. 4:64-3 The Working Group notes that one option, again following the process used in residential mortgage foreclosures, could be to have surplus funds deposited into the Superior Court Trust Fund, subject to future applications pursuant to Court Rules.
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(5) Other Issues Discussed by the Working Group

In discussion, the Working Group identified a number of additional topics that might be considered as part of reexamination of the tax foreclosure process, as follows:

- Whether the 20-year statute of limitations for filing tax foreclosure might be reduced since a lengthier period may result in depletion of the property owner's equity;
- Whether specific notices should be provided to property owners in a tax sale foreclosure during the pre-complaint, judicial, and post-judgment processes, and whether the content of such notices should be prescribed by statute;
- Whether, if a property owner has a right to request a sale of a property subject to a tax lien, the property owner should be required to take specific action to request such a sale;
- Whether online auctions should be permitted;

- Whether all tax sale foreclosures should proceed to a public sale, or whether a sheriff's sale or analog should be conducted only if requested by the property owner to preserve equity;
- Whether sheriffs and/or special masters should be engaged to conduct post-judgment sales of properties encumbered by tax liens;
- Whether, and if so, when, an appraisal or realtor comparative market analyses (CMAs) should be required; and
- How to handle any surplus monies from post-judgment auctions (e.g., whether such funds should be deposited with the Superior Court Trust Fund).

Consistent with its charge, the Working Group takes no position on the above issues and offers the above list solely for consideration by the Legislature and Governor.

Conclusion

The Working Group thanks the Chief Justice for the opportunity to collaboratively discuss the potential implications of the United States Supreme Court's holding in Tyler. The group hopes that its efforts will be useful to the Legislature and Governor in their consideration of the various interests affected by tax sale foreclosures. In addition, members concur that the advance review and preliminary revisions to forms and notices will enable the Judiciary to promptly respond to and implement any future substantive changes in this important area.

Roster of Members

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