



What Operators Should Know About Judicial Foreclosure

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The recent financial stress on the oil and gas industry may result in the foreclosure of liens on distressed assets. This article provides a brief overview of the judicial foreclosure process and related considerations to inform oil and gas operators who may be subject to judicial foreclosure.

Lenders may seek to obtain distressed assets through various means, including by default on a mortgage, by voluntary lien (such as a deed of trust), or by an involuntary lien (such as a mechanic's lien). In Colorado, mineral assets may be encumbered by a deed of trust through a private trustee acting for the benefit of a lender. Thus, foreclosure of encumbered mineral assets is typically accomplished by judicial foreclosure.

Judicial foreclosure is a civil lawsuit and is thus subject to the Colorado Rules of Civil Procedure. C.R.C.P. 105 provides for an action to fully adjudicate the rights of all parties to real property, including mineral and leasehold interests. For strategic reasons, not all parties with an interest in the property are always named as defendants; however, judicial foreclosure does not foreclose the interests of parties unless those parties are named as defendants.

Defenses to Judicial Foreclosure

A party seeking to avoid foreclosure should examine the instrument creating the lien to determine whether it was properly executed, recorded in the county where the property is located, that it accurately describes the property covered, and that it identifies the owner. If a promissory note was given, the note should be examined for notice, and that the note was given with recourse. Because promissory notes, mortgages and other security interests are easily assignable, it is also important to determine the current holder of those instruments. No Colorado law requires the recording of assignments of encumbrances and so the actual holder of the encumbrance may be a different party than that shown in the public records.

Only parties with interests recorded after the encumbrance being foreclosed need to be named as defendants. Colorado statutes do not require a foreclosing creditor to engage in an investigation into unrecorded assignments of junior liens. Senior lienholders will not generally be affected by the foreclosure, and the title materials should be examined for the presence of senior lienholders who could initiate their own foreclosure and create issues for junior lienholders. Additional requirements are imposed if the title work indicates that the federal or state government holds a junior lien.

As in any litigation, defendants should also determine whether service of process on the defendants conforms to C.R.C.P. 4. Mineral and leasehold interests are real property interests in Colorado, and so a judicial foreclosure action affecting those interests requires the execution and recording of a lis pendens in the county where the property is located. A lender can cause problems for itself if it records a lis pendens prior to filing a complaint because, until the lawsuit is filed, there is no pending litigation.

At hearing and trial, the plaintiff must be prepared to prove that it is the owner of the lien, that there has been a default that has not been cured, and that the plaintiff has a right to an order for foreclosure. The plaintiff must be prepared to present evidence of the original indebtedness, including the promissory note and a certified copy of the recorded lien, as well as the ability to demonstrate the amount owed, including principal, interest, late charges, and any other allowable charges. All defendants are entitled to cure a monetary default and are entitled to redeem the property if done within the redemption period.

Defense of a judicial foreclosure also involves scrutinizing the proceedings for any irregularities in the judicial process. Further, C.R.C.P. 105 provides certain options for defendants to avoid costs in defending the foreclosure. Defendants may also have options if they can claim an interest in the property that is superior to the lien being foreclosed, if title insurance covers the foreclosed interest, or if there is a possibility that the statute of limitations has expired. Attorneys for the plaintiff and defendants will scrutinize the notices and deadlines for any failure to comply with statutory law and the rules of procedure, as such errors can be fatal to the finality of the sheriff's sale, notwithstanding the expiration of the redemption period.

The sheriff's procedures can vary from jurisdiction to jurisdiction, and defendants can challenge any deviations from those procedures. Defendants have further recourse, including the filing of a notice of intent to cure, claiming errors in the bid sheet, the filing for bankruptcy, or objecting to the court regarding irregularities in the conduct of the sheriff's sale. Following the foreclosure sale, the debtor can file an intent to redeem or redemption can occur by holders of junior liens recorded before the lis pendens.

For help navigating these issues, please contact [Craig Berube](#) or [Tyler Weidlich](#).