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The New Rules Of Foreclosure Litigation



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Since the first loans and mortgages changed hands with cloaks and stone in Israel[1] and Greece[2] thousands of years ago,[3] never previously had mortgages caused a worldwide economic collapse of financial markets. Unfortunately, as the federal and state government as well as some judges place barriers and hurdles breaking contracts and preventing lenders from collecting monies owed to them, or foreclosing on the homes pledged as collateral, lenders may eventually run away from traditional lending, leading to a new world of lending where cash and goods are king, bartered in exchange for property. This would destroy most of the equity acquired in an owner's home. Strange judicial decisions have come down and played their part in slowing down the foreclosure process or simply eviscerating the foreclosure action.

Fortunately, our appellate courts have come to the rescue and brought the essentials for any government: law and order and predictability of law so that business people and consumers alike can prepare contracts without uncertainty. One of the worst fears of every real estate and dirt lawyer is the unknown of what a court will do if a problem arises with a contract.

Having reviewed all of the appellate foreclosure cases since January 2010, we will discuss some of the most important foreclosure cases decided in that period. Our goal is not to denounce or praise these cases but to teach the practitioner and title professional how to proceed in this new era of mortgage and foreclosure litigation. As a general rule, the courts continue to show far greater restraint against enforcing lenders' claims, but our review has shown that when lender's counsel prepares the papers meticulously in accordance with the new laws, properties do go to judgment and sale.

One interesting pattern has emerged. Although the counties of the Second Judicial Department[4] account both for roughly 50 percent of the population and 50 percent of owner-occupied housing in the state of New York, over 70 percent of foreclosures in the state were in the Second Department.[5] While we decline to speculate as to the economic or sociological reasons for the statistical discrepancy, it does mean that the Second Department is leading the way in making foreclosure law.[6]

No Sale Pending Modification

In *Aames Funding Corp. v. Houston*,[7] the Second Department stayed a foreclosure sale pending a determination on his application for a residential mortgage modification pursuant to the federal Home Affordable Mortgage Program (HAMP).[8]

The loan servicer had notified the homeowner that he might be eligible for a loan modification under HAMP, and the homeowner submitted an application to the loan servicer. While the homeowner's application was pending, the lender published a notice of foreclosure sale.

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The court cited Version 2.0 of the "Making Home Affordable Program Handbook,"[9] which was in effect at the time the lower court denied the homeowner's motion to stay the foreclosure sale. The handbook stated, in pertinent part, that "a servicer may not refer any loan to foreclosure or conduct a scheduled foreclosure sale unless and until…the borrower is evaluated for HAMP and is determined to be ineligible for the program."

Since the loan servicer was a participant in the HAMP program, it was barred from scheduling a foreclosure sale during the HAMP process.

Single Lawsuit Rule

Under New York's equitable relief doctrine, when a borrower defaults on mortgage payments, a lender seeking repayment of a loan may proceed either at law to recover a judgment for the mortgage debt, or may bring an action in equity to foreclose the mortgage, but not pursue both remedies at the same time.[10]

However, that does not deprive a foreclosure plaintiff of a money judgment. In the event the foreclosure sale is insufficient to satisfy the debt, attorney fees, and court costs and expenses, the plaintiff may move for a judgment for those sums within the context of the foreclosure action.[11] The plaintiff must move for such judgment within 90 days after the date of the consummation of the sale by the delivery of the referee's deed to the purchaser[12] at the foreclosure sale.

Generally, plaintiffs move for a deficiency judgment simultaneously with moving to confirm the sale, but the deficiency judgment motion does not enjoy the same flexibility as the confirmation motion.[13] Courts strictly enforce this 90-day period and uniformly treat it as a statute of limitations, beginning on the date that a properly executed deed is delivered, not when it is recorded.[14] Failure to serve the notice of motion within this period serves as a complete bar to the entry of a deficiency judgment.[15]

In *Aurora Loan Services v. Lopa*,[16] the Second Department held that the equitable relief doctrine does not prevent a plaintiff in a foreclosure complaint from also requesting a deficiency judgment.

In *Aurora*, a lender brought suit to foreclose on a mortgage. The lender prayed for deficiency judgment against the homeowner in the event that the amount realized by the sale was less than the amount of the mortgage debt. The court reasoned that while a lender may not simultaneously pursue both a remedy at law and a remedy in equity, a prayer for deficiency judgment within the context of an actual mortgage foreclosure complaint does not constitute a separate action for money judgment. Looking to RPAPL §1371(2), permitting a plaintiff in a foreclosure action to "make a motion in the action for leave to enter a deficiency judgment," the court allowed the prayer for deficiency judgment in the foreclosure complaint as incidental to the principal relief demanded.

Illiteracy No Defense

Although it involved a tax foreclosure and not a mortgage foreclosure *Matter of City of Rochester* (*Duvall*) shows the limits on the courts' extent of consideration and mercy, and its ruling applies not only to all species of foreclosures, but potentially to all species of New York litigation altogether.

The Third Department clearly sympathized with petitioner-homeowner's situation as an illiterate, 91-year-old man who lost his home to tax foreclosure, but found that defendant's illiteracy was not a proper basis on which to attack foreclosure papers or their predicate notices. The respondent, City of Rochester (city), sent notices of an outstanding

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tax bill and of an impending tax foreclosure action to the homeowner by ordinary mail. After receiving only a small portion of the payments from the homeowner over a two-year period, the city sold the property and the homeowner was personally served with a 10-day notice to quit.

In determining whether the notice was reasonable, the majority took into account the status and conduct of the homeowner as well as the burden placed on the city in providing reasonable notice.[18] The court determined that the city's actions in mailing the notice to the homeowner were reasonably calculated, under all the circumstances, to inform the homeowner of the impending foreclosure action and afford him an opportunity to present his objections.[19]

A two-judge dissent, without going into detail, opined that the city was or should have been aware that the homeowner was illiterate, and his illiteracy was a significant circumstance or condition that weighed against a "reasonable calculation"[20] that the usual method of mailing the foreclosure notice would inform the homeowner of the foreclosure action. Consequently, the dissent concluded that the homeowner was not provided with adequate notice of the impending taking.

The dissent further concluded that there were reasonable steps that the city could have taken to inform the homeowner of his tax delinquency but refused to set forth what those could have been. We note that a two-justice dissent in the Appellate Division, under CPLR 5601, automatically entitles the appellant to an appeal as of right to the Court of Appeals. We find ourselves wondering whether the two dissenting justices were therefore setting up the matter so as to give nature enough time to moot the most serious considerations in the case. Were *Duvall* not decided the way it was, not only in foreclosures, but in any kind of suit, anybody with any kind of inability to read English would seem automatically entitled to special considerations that would make litigation in New York impossible to pursue. The majority holding in *Duvall* therefore seems mandatory, two dissenters notwithstanding.

Due Process

In tax foreclosures, there are special considerations of due process attaching only because the government is seeking to seize property. In *Matter of Orange County Commissioner of Finance v. Helseth*,[21] the Court of Appeals held that the county was only obligated to give singular notice of the foreclosure action, as that was the underlying governmental action threatening the landowners' property interests. However, while it is generally a uniquely governmental function to lay and collect taxes, due process concerns also attach when a government is the lender and bringing a mortgage foreclosure.

The state may not deprive a person of property without due process of law, meaning giving notice "reasonably calculated, under all the circumstances," to inform the party whose rights are to be affected of the opportunity to appear and be heard.[22] Constitutional due process does not require that notice be given for each successive stage of the foreclosure proceedings.

In *Matter of Orange County Commission of Finance*, the landowners owned an unimproved piece of property, not their residence. When the landowners were informed that the county was sending their tax bills to this empty lot, they filed a change of address form with the county. Over a year later the landowners paid that year's real property taxes at the county office, directly informing them of their then-current address. Despite these attempts to inform the county of their proper address, the landowners did not receive any additional real estate property tax bills or correspondence for the property.

The next year, the landowner's failed to pay taxes on the property and the county commenced a tax lien foreclosure action. The county mailed the notice to the property in conjunction with other forms of valid service.

Following a default judgment of foreclosure, the county sent the landowners a letter by certified mail, return receipt requested, to the property's address informing the landowners that the county had acquired title to the property. The letter further advised the landowners of a local law, which afforded them a release option, permitting them to repurchase the parcel through a release of the county's interest. This letter came back to the county as "unclaimed."

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Since the release option was a discretionary, permissive remedy that was available to the landowners after the property's lawful foreclosure and conveyance to the county, the court found the landowner's property interest lawfully extinguished in spite of the sending of mail to an address the county had reason to know was bad.[23]

The Court of Appeals distinguished the U.S. Supreme Court holding in *Jones v. Flowers*,[24] because in *Jones* the public tax sale was in lieu of a foreclosure proceeding and therefore, the public tax sale constituted a governmental taking that required due process.[25] The court held that *Jones* does not expand the municipality's obligations beyond the due process required for the actual tax lien foreclosure sale.

Conclusion

While in the past two years courts have shown themselves particularly solicitous of borrowers' rights in foreclosure proceedings, we see from this brief survey that the courts are far less solicitous of taxpayers' rights. At least when it comes to foreclosure, the courts appear far more willing to give leeway to the government than to banks.

1. There are references in the Old Testament that provide evidence that there was lending among individuals in the ancient world. Both the Books of Exodus and Deuteronomy indicate that there was lending and that personal property collateral was used to assure repayment of loans. Debtors would pledge their personal property to creditors for the creditor to hold until the debtor repaid the loan. If the loan was not repaid, the creditor was able to sell the pledged property. The Books of Exodus and Deuteronomy refer to two types of collateral: cloaks and millstones. Millstones were equipment used to grind wheat into flour and were valuable possessions because an owner would use a millstone to produce a livelihood. Roger D. Billings and Frank J. Williams, "Abraham Lincoln, Esq: the Legal Career of America's Greatest President" 109-112 (2010).

2. In ancient Greece, placing a pillar or tablet on the land, inscribed with the creditor's name and the amount of the debt indicated a pledge for land. H.W. Chaplin, "The Story of Mortgage Law," 4 *Harv. L. Rev.* 1 (1890).

3. The authors wish to credit New York Law School Professor of Law and director of the Center for Real Estate Studies, Andrew R. Berman's article "Once a Mortgage, Always a Mortgage—The Use (and Misuse of) Mezzanine Loans and Preferred Equity Investments" 11 *Stan. J.L. Bus. & Fin.* 76 (2005), for leading them to authority on the history of mortgages.

4. The Second Department includes Richmond, Kings, Queens, Nassau, Suffolk, Westchester, Dutchess, Orange, Rockland and Putnam counties.

5. An analysis of http://www.RealtyTrac.com revealed that as of January 2012 there were a total of 1672 foreclosures in New York and 1185 of these foreclosures were in the Second Department.

6. Such as, for example, the Third Department's overwhelming presence in corrections law.

7. *Aames Funding Corp. v. Houston*, 85 A.D.3d 1070, 926 N.Y.S.2d 639 (2d Dept. 2011).

8. Part of the congressional response to the 2008 crisis.

9. One should not mistake the word "handbook" for implying anything less than the full force of law.

10. Real Property Actions and Proceedings Law §1301.

11. *Steuben Trust Co. v. Buono*, 254 A.D.2d 803, 677 N.Y.S.2d 882 (4th Dept. 1998).

12. Real Property Actions and Proceedings Law §1371.

13. *Seiden v. Chagnon*, 33 A.D.2d 951, 306 N.Y.S.2d 847 (3d Dept. 1970).

14. *Cicero v. Aspen Hills II,* 85 A.D.3d 1411, 1412, 926 N.Y.S.2d 680, 682 (3d Dept. 2011).

15. Id., at 1412, at 682.

16. *Aurora Loan Services v. Lopa*, 88 A.D.3d 929, 932 N.Y.S.2d 496 (2d Dept. 2011).

17. *Matter of City of Rochester (Duvall)*, 92 A.D.3d 1297, 939 N.Y.S.2d 214 (4th Dept. 2012).

18. *Matter of Harner v. County of Tioga*, 5 N.Y.3d 136, 140, 800 N.Y.S.2d 112, 833 N.E.2d 255 (2005).

19. *Mullane v. Central Hanover Bank & Trust*, 339 U.S. 306, 314, 70 S.Ct. 652, 657, 94 L.Ed. 865 (1950).

20. *Weigner v. City of New York*, 852 F.2d 646, 650, cert denied 488 U.S. 1005, 109 S.Ct. 785, 102 L.Ed.2d 777 (1994).

21. *Matter of Orange County Commission of Finance v. Helseth*, N.Y. Slip Op. 01324 (2012).

22. *Mullane*, at 314, at 657.

23. *Sheehan v. County of Suffolk*, 67 N.Y.2d 52, 59, 499 N.Y.S.2d 656, 490 N.E.2d 523 (1986).; RPTL §1123(8).

24. *Jones v. Flowers*, 547 U.S. 220, 224, 126 S.Ct. 1708, 164 L.Ed.2d 415 (2006).

25. See, Bailey & Treiman, "Despite 'Jones,' Ambiguities in Title Chain Can Be Cured," *NYLJ,* June 10, 2009.