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HETPA Contains Land Mines For Unwary Attorneys, Buyers

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In February of 2007 the Home Equity Theft Prevention Act (HETPA) passed the New York State Legislature, attempting to stop scam artists from stealing or tapping the equity of victims' homes. HETPA had two principal areas of concern: the substance of transactions involving persons in distressed circumstances selling their homes and the inadequacy of foreclosure procedures to inform defendants of their rights and remedies. The substantive portion of the statute1 principally allows homeowners at distressed sale conditions to rescind the sale within two years thereafter. The procedural portion of the enactment,2 calls for foreclosure pleadings to have attached to them precisely worded notices setting forth some options the defendant might have.

Despite its good intentions, HETPA's anti-consumer effect easily makes it the worst real estate statute currently on the books.3 Initially a best friend to debtors, HETPA became anachronistic the date lenders began diligently examining whether borrowers could afford the loan and tightening their credit standards. However, HETPA continues to endanger sales to investors who may be forced to relinquish the home if the seller opts for rescission. Investors now seeking to invest in distressed properties, must do so without title insurance or with a policy that excepts HETPA from the coverage. For those who forego title insurance on these deals or for those title companies that insure these sales, the monetary losses could be enormous. For a significant proportion of deals, HETPA can be keeping investors out of the market. By keeping investor-purchasers off the market, HETPA significantly curtails the number of buyers distressed sellers can turn to for relief, severely harming their chances for relief from deals they can no longer afford. On the procedural side, HETPA keeps defaulting borrowers ringing up charges they can ill afford. That notwithstanding, until HETPA is repealed, transactional attorneys need to know the common law that has developed under it.

Few Reported Decisions

HETPA has generated very few reported decisions, four substantive and six

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procedural. Two appellate cases have come down, one each for procedure and substance, both from the Secon Department. Our firm's experience and that of other real estate professionals suggests that there is so little substantive litigation because the industry has adjusted to HETPA in ways that the suspect transactions rarely actually take place.

However, in Lucia v. Goldman,4 the Second Department held that documentary evidence was insufficient to defeat a cause of action for rescission of a mortgage under HETPA. In Lucia, it was alleged that representatives of the mortgagee-bank were present at mortgage rescue scheme closing where conversations about the nature of the transaction allegedly took place in front of the bank representatives, putting the bank on notice and making it susceptible to HETPA rescission. Moreover, the decision continued that HETPA "is a remedial statute, designed to stem an anticipated rise in so-called 'mortgage rescue' schemes, and its provisions should be liberally construed in favor of equity sellers." The decision does not reveal who ultimately won the case.

Washington Mutual Bank v. Sholomov,5 was an action in Nassau County Supreme Court to rescind a mortgage entered to elude foreclosure on an earlier mortgage. In a bizarre story, the seller was driven hither and thither as various fraudulent acts and forgeries took place at different places. In the end the seller received a small payment for her house and gave title to somebody else. The court allowed the case to proceed to trial. Most importantly, the court held that the papers themselves were so irregular on their face as to put the bank on notice that this was a sale that could be violating HETPA. Thus, the bank under Sholomov, was held not only to examine the regularity of its own mortgage papers, but also the underlying conveyance documents, including the contract of
sale.

U.S. Bank v. Mar,6 present another enormously convoluted set of facts endemic to mortgage rescue scams. The case looked at three pending lawsuits, including the foreclosure before it and a pending criminal proceeding and decided to stay the foreclosure until it could be determined whether or not HETPA applies.

Deutsche Bank v. Miele, recites no facts at all except that the defendant sought to open his default in the foreclosure proceeding because the mortgage had been tainted by HETPA in some manner, without specifying how. Yet this is one of only four cases in the past three years to discuss substantive HETPA at all. The others citing the statute merely mention it, saying that it does not apply.7

Procedural HETPA

With eight lower court decisions on both its substance and its procedure coming down in the three years of HETPA, this year, procedural HETPA made its appellate debut with First National Bank of Chicago v. Silver.8

Just what is the procedure HETPA enacted? That one bringing a foreclosure on residential property of fewer than five units serves with the summons and complaint a separate notice in large type on contrasting colored paper explaining certain alternatives to the Defendant. The statute mandates the exact 270 some odd words the notice must contain.

Silver would have been a completely garden variety case. The bank brought a foreclosure by filing a notice of pendency and filing and serving a summons and complaint. On motion for summary judgment, however, the defendants cross-moved for dismissal on the basis of the newly raised ground of non-service of the HETPA notice. The narrow issue before the court was whether such a defense could be raised for the first time on summary judgment or had to be preserved first in the answer. The court, answering more than it was asked, said that this HETPA procedural defense

could be raised "at any time" and dismissed the case.

Noncompliant Notices

Silver reveals two major themes regarding these notices—that the failure to include the statutory notice is a defect in the proceeding that is beyond the power of amendment to cure and that the defect may be raised at any time in the course of the proceedings so as to strike the proceedings down.

These two features may erroneously call to mind the doctrine of subject matter jurisdiction,9 typified by the fact that the defect in question is unamendable and that it may be raised at any time. However, not all unamendable defects impair subject matter jurisdiction.10 Silver itself implies that failure to adhere to §1303 is not one of subject matter jurisdiction and may therefore be waived.

This is important because had it been a question of subject matter jurisdiction, no matter what the parties stipulated to, it would remain a cloud on title forever thereafter, even decades down the road. Since the HETPA notice does not impact subject matter jurisdiction, the defendant has the power to waive the defect in the law suit and allow it to go forward in exchange for favorable settlement terms.

Pre-'Silver' Cases

Silver does not disapprove of any of the trial court decisions that preceded it except the one it reverses. These lower cases show several trends.

The first trend—that the mere fact that the statute was only recently enacted is no excuse to fail to comply with it11—is of fairly little importance now.

Second, the burden of proof is on the plaintiff to prove that it did serve §1303 compliant notice.12 The defendant has no burden of proof either that the plaintiff failed to serve the notice or that the defendant failed to receive it.13

Third, the failure to serve a compliant notice makes the proceeding unamendably defective.14

One rogue decision in all of this is Trustco Bank v. Alexander,15 which held that because the defendant was himself a sophisticated businessman with knowledge of mortgage foreclosure scams, the deficiency of the notice was nonprejudicial and therefore nonfatal. Silver would not uphold such a finding.

'Silver's' Unknown Meaning

Silver begins:

In this matter we are asked to determine an issue of first impression at the appellate level, that is, whether the failure to comply with notice requirements of the Home Equity Theft Prevention Act (Real Property Law §265-a; hereinafter HETPA) must be raised as an affirmative defense or whether it can be raised at any time during an action. We hold that it can be raised at any time…

It asks one question: "whether the failure to comply…can be raised at any time during an action" and answers another: "We hold that it can be raised at any time." Does "any time" mean "any time during an action" or does it mean "any time during or even subsequent to an action?" If the propriety of the service of a §1303 notice can only be raised "during an action," then the notice is subject to challenge only until a final unappealable judgment.

If "any time" means any time, then theoretically there could be a property subject to a foreclosure proceeding lacking the proper §1303 notice in the chain of title. Is this something that the defendant in the foreclosure could raise even after the foreclosure auction or later?

Neither Silver nor any other case answers that.

However, it should be noted that Silver cites to W 54-7 LLC v. Schick16 wherein the court discussed an earlier case and wrote in essence that where the respondent in that case had failed to object to the lack of a preliminary notice until after judgment, the entry of the judgment effected a waiver of that lack in the petitioner's prima facie case.17 This is a reasonable reading of "any time" so as to mean "any time prior to judgment" with regard to objections to the form and sufficiency of §1303 notices and is likely Silver's intent.

Practical Advice

Under substantive HETPA, title companies must ascertain whether the seller is in arrears in taxes or mortgage payments and if so, whether the buyer is going to use the home as a primary residence. If not, HETPA must be excepted from the policy.

Buyers' attorneys must advise investor-purchasers that if they enter an HETPA-affected deal, the entire thing may unravel within two years if the seller chooses to rescind.

Under procedural HETPA, foreclosure plaintiffs' counsel, should not only serve the statutory notice precisely as described in the statute, but also make an exact copy of the notice that they serve and attach it to the affidavit of service of the summons and complaint along with an affirmation that this exact copy precisely matches the form that was given to the process server as to all the statutory specifications.

For attorneys who are defending a foreclosure action, they should move for dismissal on the basis that there is no proof in the file that the plaintiff served a §1303 compliant notice.

For title insurers, they should except from the policy any state of facts showing that §1303 was not complied with, regardless of whether the property went through to judgment and sale.

For seller's attorneys where there is a foreclosure in the chain of title, they should contact the attorneys who handled the foreclosure and procure from them an affirmation that the foreclosure adhered to §1303, including an affidavit from the process server that the only papers handed to the defendant were those actually received from plaintiff's attorney in the foreclosure and an affirmation from the attorney that the papers given the process server met the requirements of §1303.

Conclusion

The judicial procedural section of HETPA is, for good or bad, straightforward. Attorneys bringing foreclosure proceedings must both comply with the statute and prove it. Defense counsel must put their adversaries to their proof.

For title companies, there is nothing really extraordinary to be found here except that they are going to want to make sure that their copies of court papers are in color. But on the substantive side, everyone has to be on the alert.

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Endnotes:

1.Principally RPL §265-a.

2. Principally RPAPL §1303.

3. HETPA became delinquent mortgagors' best friend by keeping them in their homes long past default. According to the June 1, 2010 New York Times, citing LPS Applied Analytics, more than 650,000 United States households have not paid their mortgage in 18 months and average borrowers remain in their homes 438 days before being evicted. The article cites a lawyer's form letter stating "Even if you have 'no defenses' you may be able to keep living in your home for weeks, months or even years without paying your mortgage."

4. 68 A.D.3d 1064 (2009).

5. 20 Misc.3d 773 (2008).

6. 2008 WL 3243821.

7. Deutsche Bank Nat. Trust Co. v. McRae, 27 Misc.3d 247; Wells Fargo Bank, N.A. v. Reid, 2008 WL 293023; Deutsche Bank Nat. Trust Co. v. Fitzworme, 22 Misc.3d 1134; Wells Fargo Bank, NA v. Edsall, 22 Misc.3d 1113; Deutsche Bank Nat. Trust Co. v. Jituboh, 23 Misc.3d 1102; Phillips-Thomas v. Ellison, 27 Misc.3d 1213.

8. 2010 NY Slip Op 02511.

9. See generally, Treiman, "Subject Matter Jurisdiction in Summary Proceedings," NYLJ 3/2/90, p.1.

10 See, Treiman, "Summary Proceedings: FUBAR and Subject Matter Jurisdiction," LTPR Vol 2, Issue 12 (December 2001).

11. WMC Mortgage Corp. v. Thompson, 24 Misc.3d 738 (Sup NY 2009).

12. Countrywide Home Loans Inc. v. Taylor, 17 Misc3d 595 (Sup NY Co. 2007).
13. Butler Capital Corporation v. Cannistra, 891 N.Y.S.2d 238 (Sup. Suffolk 2009).
14. WMC Mortgage Corp. v. Thompson, 24 Misc.3d 738 (Sup NY 2009).
15. 23 Misc.3d 1129 (Sup Saratoga 2009).
16. 14 Misc.3d 49 (App Term 1st Dept 2006).
17. Actually the court inaccurately described its earlier holding in Priel v. Priel, 21 HCR 93A, NYLJ 3/5/93, 25:3. The court in Priel ruled that after litigating the case for two years, it was too late to bring up the question of the adequacy of the notice, even before judgment. However, one would be hard pressed to find the real holding of Priel would accurately predict a holding in Silver.