SERVICING MANAGEMENT®
THE MAGAZINE FOR LOAN SERVICING PROFESSIONALS

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Lender Victimized By Negligence Suit... In A Foreclosure Action?

A recent case in New York State threatens to hold lenders liable, in some instances, if someone gets hurt or killed on a property in foreclosure.

by Bruce J. Bergman

Is it possible, or even remotely conceivable, that a mortgage holder could begin a mortgage foreclosure action and, by virtue of that, be liable for a death at the premises caused by negligence? The frightening Alice in Wonderland answer - at least in New York - is "yes."

Lenders and servicers are all too aware that legislatures in the various states have been on a crusade in recent years to implement legislation to protect borrowers and tenants who are perceived as put upon by powerful lenders. Although helping and enlightening borrowers is laudable as an overall concept, if the legislation is misguided, overreaching, overzealous or ambiguous, or any combination thereof, the result can be downright bizarre, to say nothing of dangerous, to lenders. As part of a trend, this could happen in any state. Such nostrums can have significant unintended consequences, which is precisely the point in this instance.

A recent case in New York declared that a lender may be liable for damages to the family of a deceased mother and child who died in a fire at the mortgaged premises. [Lezama v. Cedano, 119 A.D.3d 479, 991 N.Y.S.2d 32 (1st Dept. 2014).] Understand that the lender did not own the property. The borrower still owned it and was sued as well, but the court found that the lender could not demonstrate that the property had not been abandoned by the owner or the borrower. Why that mattered arises out of the New York statute and is an aspect to be mentioned.

First, this situation should not be confused with what can happen after a foreclosure sale. If a lender buys back the property, until it completes an eviction and obtains legal title, it has no care, custody and control over the property. Generally, without that requisite care, custody and control, it cannot be liable for negligent acts; it was not in a position to maintain the property so if lack of maintenance leads to injury, it cannot be liable for that reason.

In the new case cited, though, the foreclosure had not yet been completed. How, then, could there be any issue of a lender - not owning the property and not in control of the property - being liable for injuries through negligence? The answer lies in the unfortunate mandate of the New York statute entitled "Duty to Maintain Foreclosed Property." This was part of a comprehensive 2009 law regarding foreclosures that provided exten-

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sive protections to borrowers, although it was immediately apparent to some, even then, that negligence liability visited upon lenders would be an inevitable result.

The essence of that law [it happens to be Real Property Actions and Proceedings section 1307(1)] is that when a plaintiff in a mortgage foreclosure action obtains the judgment of foreclosure and sale for residential real property, and if the property is vacant or becomes vacant after issuance of the judgment, or is abandoned by the mortgagor but still occupied by a tenant, the lender is required to maintain the property until ownership is transferred through the closing after a foreclosure sale.

Thus, it became obvious that a lender proceeding through a foreclosure would now be required to determine whether all of its foreclosed properties (after judgment) were vacant or abandoned - not at all easy to do. It can be uncertain. But if there was an abandonment or if it had been vacated, then there was this maintenance responsibility that could expose the lender to a negligence claim for a period of unknown duration.

So, the option available to lenders from time immemorial to allow a foreclosure to lie fallow is gone.

That is just what happened in the cited case.

There, the lender argued that the property had not been abandoned and that it had documentary evidence to demonstrate that. Accordingly, it made a motion to dismiss the complaint in the negligence action on the ground, that the complainant could not state a cause of action. But the court found that the lender failed to adequately prove that the premises were not abandoned. That being so, the complaint was allowed to stand - and the case had to proceed.

What will happen with that particular case, for the moment, is not known. It is still possible that the lender may be able to show that the property was not abandoned, in which event the maintenance obligation never applied. If it does not, though, it may very well be liable for enormous sums for the loss of life.

The overall concern, though, is what this portends for future cases - in New York and other states that may adopt this construct. The real impetus for the statute likely was neighborhood blight seen by some municipalities as a genuine condition and a threat. Making lenders and servicers the gatekeepers to take care of borrowers' responsibilities to maintain the property was a way to assure that deeper, more responsible pockets would perform the maintenance task.

This, however, creates enormous problems, questions and burdens, including the following:

- Making lenders responsible for maintenance foists upon them the very care, custody and control - over someone else's property - which can be the foundation of a negligence claim.
- If a lender has an interest in maintaining property upon which it has a lien (the mortgage), it can do so volitionally by having a receiver appointed or becoming a mortgagee-in-possession. But that has always been a choice - not a mandate.
- Although lenders can force-place hazard insurance on a mortgaged property, whether it has an insurable interest for liability coverage is a different issue. If not, it is a self-insurer for enormous unpredictable sums.
- Whether lender maintenance is imposed at judgment or some other stage, the duration of a foreclosure can never be precisely predicted. Therefore, duration of exposure to both maintenance expense and the peril of negligence suits is simply indeterminate; how does one price that into the cost of a mortgage investment?

Lenders need to pursue foreclosures, in part, to entice borrowers to satisfy the debt, or to sell, or refinance, or modify or settle in some fashion. But if nothing helpful eventuates, and if the equity is gone (sometimes open taxes could be greater than the value of the property), the lender may wish to simply refrain from completing the foreclosure action. Once maintenance is imposed, though, it will never end if the action never ends. So, the option available to lenders from time immemorial to allow a foreclosure to lie fallow is gone.

There is more to all of this, tied in to the particular language of statute(s). But in the end, where are lenders left in deciding to make a mortgage loan when the cost to do it could be millions of dollars in negligence liability? SM

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