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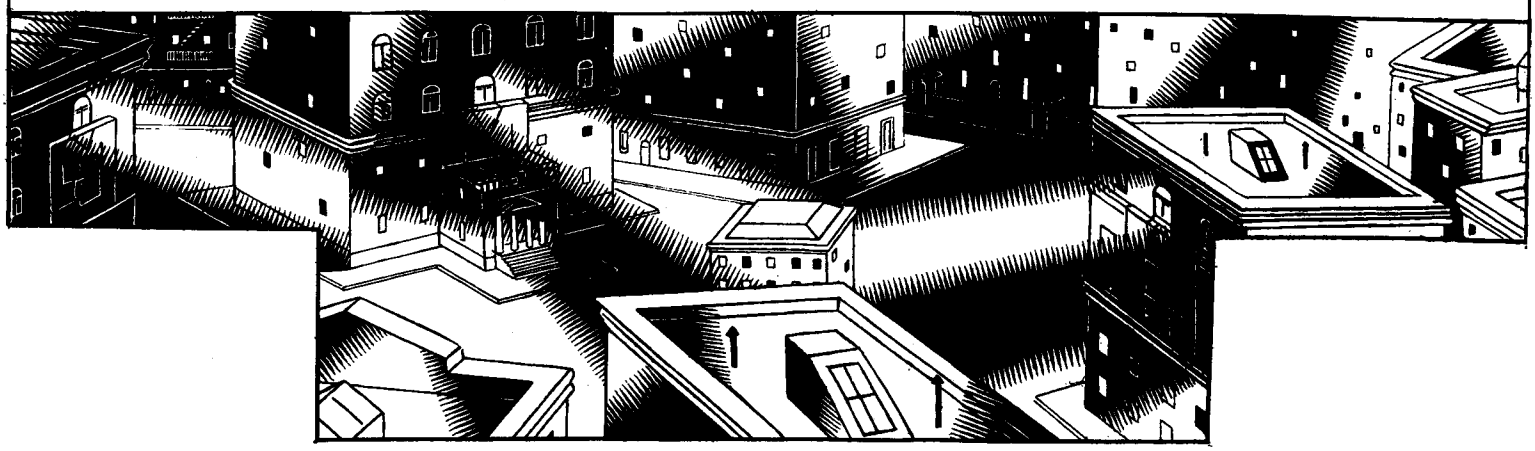
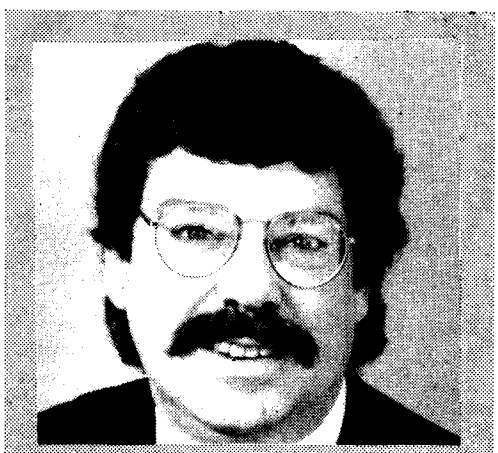
REAL ESTATE UPDATE



No Immunity From Penalty

Possible Consequences for Plaintiffs Who Delay Foreclosure



MORTGAGE FORECLOSURES

BY BRUCE J. BERGMAN

"DELAY THE FORECLOSURE" is seldom the directive of a foreclosing lender. It may very well be the borrower's goal, and often is, but the lender's or servicer's admonition is typically the opposite: "Move the case along as quickly as possible." There is, of course, compelling reason for this posture which is too obvious to dwell upon here.

Sometimes, though, a mortgagee might volitionally halt a foreclosure, for example, to accommodate a settlement. Then, there usually would be, and counsel would recommend there must be, a written stipulation or forbearance agreement, preserving a foreclosure action in place, poised to go forward the moment the mortgagor might default. (At least as between mortgagee and mortgagor, there should be no consequences of the foreclosure action remaining in place.)

Possible scenarios occasioning delay readily come to mind. Relevant documents may have been lost, misplaced or be otherwise unavailable. A foreclosing plaintiff might believe that rising, or falling, property values urge postponement of case conclusion to best serve the mortgagee's interests. Then there is inadvertence or carelessness — a file is somehow forgotten.

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Other than the instance of the settlement through forbearance or stipulation (reduced to a writing), might there be danger to a foreclosing plaintiff in allowing the action to remain pending too long? With varying degrees of peril, the answer is there may be.

Mundane Statutes

Part of the possible exposure is found in the CPLR and one area to avoid is the focus of CPLR Rule 3404 entitled "Dismissal of Abandoned Cases."[1] That rule provides that if a case is marked off or stricken from the court calendar, or unanswered upon a clerk's calendar call, and not restored within one year, it must be deemed abandoned for neglect to prosecute. As a practical matter, it is unlikely that a mortgage foreclosure would be so neglected that it would be marked off. But it could happen during a long period of performance of a settlement. The saving grace is that there is a year to restore the case to active status — unless counsel was not watchful. So, remote though it is, there is some risk.

Another hazard is secluded under the heading of "Want of prosecution," as codified in CPLR Rule 3216. There, pleadings can be dismissed by the court on its own, or upon

motion, where a party unreasonably neglects to proceed in an action, or otherwise delays in the prosecution of the case (or fails to file a note of issue, relevant in a foreclosure only in the uncommon instance of necessity for a trial.)

Such dismissal as would emerge would not be on the merits of the case; so the case could be resurrected. But the statute mandates weighty conditions precedent to dismissal. First, issue must have been joined, which is that an answer has been received. And one year must have elapsed since joinder. The major hurdle is a prerequisite that written demand be made (sent by registered or certified mail) requiring the recalcitrant party to resume prosecution and to serve and file a note of issue within 90 days after receipt of the demand, with the further proviso that default in timely compliance with the demand will be grounds for a motion to dismiss.[2]

A lender's vulnerability here is that the six-year statute of limitations might run before the foreclosure is revived — remote, but hardly impossible.

Statute of Limitations

In theory, certainly as an ideal, once a foreclosure has seasonably begun, there should be no statute of limitations issues. That is, unless the action first terminates and then runs afoul of a statute of limitations defense. An astounding, albeit aberrational, example contained these facts.[3] A mortgage was executed in November 1970. Based upon a default in remitting the mortgage installment due on March 1, 1973, the assignee of the mortgage accelerated and instituted foreclosure in May 1974. By December 1976, the action was marked off the trial calendar and (pursuant to CPLR 3404) one year thereafter the case was deemed dismissed.

In 1979 the mortgage was again assigned. Apparently it was not until 1992 that the latest assignee became aware that the mortgage had remained dormant and in default for so many years. Seeking to salvage the situation, a new foreclosure action was then instituted.

Correctly observing that acceleration had been accomplished through filing the foreclosure complaint (containing a declaration of acceleration) in 1974, the court ruled that the initial foreclosure had never been withdrawn by the lender, but rather was dismissed by the court.[4]

Deeming dismissal not to be an affirmative act by the lender, the court concluded that the acceleration had never been withdrawn. Since, therefore, the balance of the mortgage was declared due in 1974, the six-year statute of limitations expired in 1980 and was thus a bar to the new foreclosure.[5] Unusual confusion in a transferred mortgage leading to extraordinary delay sabotaged the right to foreclose.

Laches is another doctrine that should find only limited application in intercepting foreclosure.[6] The essence of laches is an estoppel against a party seeking to assert a right where exercise of the right would be inequitable after passage of a lengthy time period.[7] But as a general rule, laches is not a defense to mortgage foreclosure[8] (although there are a few unusual exceptions) based upon the paramount control of the statute of limitations. In other words, where the statute of limitations does not bar foreclosure, laches cannot preclude enforcement.[9]

The concept is highlighted by a case in which a 17-year delay in initiating a foreclosure (when the applicable period of limitation was 20 years) was held timely and not susceptible to a defense of laches.[10]

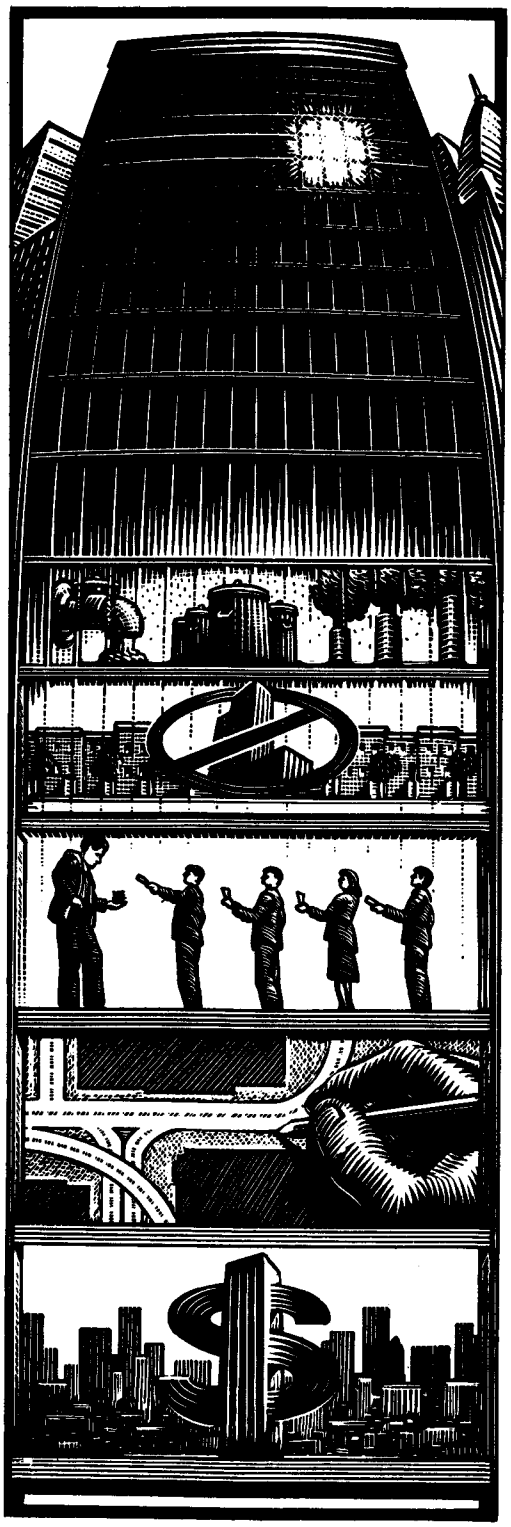

ILLUSTRATION BY JOHN MacDONALD

Comforting though all this should be to lenders, in the context of delay once a foreclosure has begun, a more recent case gives pause.[11] There, a foreclosure was dormant for 20 years until a defendant moved to dismiss pursuant to CPLR 3404 and 3216, as well as upon plaintiff's laches. (There had been a stay of the foreclosure for 20 years pending plaintiff's compliance with EPTL 13-3.5)

CPLR 3404 was rejected as a ground for dismissal because the case had not been marked off the trial calendar. Relief was also unavailable under CPLR 3216 because it could not be ascertained whether joinder of issue, a condition precedent to the 90-day demand, had occurred. As to laches, though, determination was deferred without prejudice to renewal. So, laches might yet prevail. The lesson is that the efficacy of laches is not a result to be cavalierly ignored.

Although still uncommon, probably the most likely consequence of delay to a foreclosing plaintiff is the possible loss of some interest recoupment. This is actually a basic concept, founded both upon statute and case law.

CPLR §5001(a) provides that in an equitable action — and the mortgage foreclosure case fits the category: " . . . interest and the rate and date from which it shall be computed shall be in the court's discretion." Case law concurs[12] and adds the qualification that resolution of the interest question is dependent upon the facts of each case, including the wrongful conduct of any party.[13]

Practical application of the aphorism offers some guidance and exposes areas of danger to the careless or less than sedulous mortgagee. *Dollar Fed. Sav. & Loan Association v. Kallen* stands firmly for the proposition that interest may be denied for a period of undue delay.[14]

There, although plaintiff had been awarded summary judgment, it remained aggrieved over the application of fire insurance proceeds and so appealed. Reversal issued in December 1978. For no valid reason (although some "reasons" were claimed), a proposed referee's report was not prepared until January 1980, and even then it was done only at the behest of the chagrined borrowers.

But nothing further happened, so the borrowers moved for appointment of a succesor referee. A referee's report finally emerged in September 1981, followed momentarily by the application for judgment of foreclosure and sale.

The borrowers did not quarrel with the inevitability of the foreclosure judgment. They vehemently objected, though, to the years of delay in the case which caused accrual of both interest and real estate taxes. The court agreed, finding it unconscionable to charge the borrowers with the costs of prolonged delay. Ascribing one year from the date of reversal on summary judgment as sufficient time for the referee to have prepared the report, the court halted interest on that date.[15]

Curtailment of interest was also found in a

case involving a post-foreclosure deficiency judgment motion.[16] While the judgment of foreclosure and sale issued on May 31, 1966, the sale was not conducted until March 17, 1967. No adequate explanation was advanced for this delay of almost a year.

Conceding that the lag might have been attributable to someone other than plaintiffs, the court ruled nevertheless that the burden was not to be borne by the party otherwise liable for the deficiency. Consequently, the interest component of the deficiency calculation was disallowed from the date of sale (May 31, 1966) to the date of the referee's report of sale, June 14, 1967.

A new twist with a somewhat perplexing result appears in a more recent decision, this time in Surrogate's Court.[17]

Here, the aggrieved party was a junior mortgagee suffering accrual of interest for two years while a judgment of forelcosure and sale languished with no action taken to ripen it into a sale.

The subordinate mortgagee further argued that, to its detriment, the property had declined in value during the two year hiatus, and demanded both that the court direct an immediate sale and deny interest to plaintiff from a time some two months prior to issuance of the foreclosure judgment.

In opposition, the plaintiff argued that the option to enforce its security was its own choice, so long as inequity was not visited upon a junior lienor. That proposition is supported by the protections afforded the junior party, which are either (or both) to satisfy the senior mortgage, taking an assignment of that superior lien, or foreclsoing the junior mortgage, thus capturing what equity might be available from the property.

Not only did the court find the proferred remedies to the junior more theoretical than practical, it enunciated a particularly coherent assessment of the relationship between delay after foreclosure judgment and harm to a subordiante encumbrancer:

> While the court may stay or postpone a sale for the benefit of any party, the holder of a judgment of foreclosure who unilaterally decides to refrain from selling the property until a more propitious time assumes the risk that such delay may be prejudicial to the rights of other interested parties due to a decline in property values. Even the accrual of interest caused by delaying a sale is prima facie prejudicial to subsequent lienors as any increase in the mortgage indebtedness causes a corresponding decrease in any surplus. This principle attaches even where the possibility of the sale producing a surplus is remote as otherwise the choice of whether or not to proceed with a sale despite intervening equities would rest solely with the mortgagee. Relief from a judgment which directs a sale must proceed from the court which rendered it and not the parties to the action or proceeding.

Notwithstanding the analysis, the court found that the complaining party must establish that actual injury has been sustained by virtue of the delay in plaintiff's proceeding to sale.

At the same time, the court said that damage was not ascertainable until the sale actually occurred. Thus, although the court did direct that the foreclosure sale be forthwith conducted (with interest to be denied after a date certain upon which publication was to commence), the request for interest forfeiture during the two year recess was denied without prejudice.

The subordinate mortgagee was offered a chance to renew the motion if the actual sale generated a price which would have produced a surplus but for the increase in the judgment amount attributable to the tardiness in conducting the sale.[18]

The newest and most strained peril arising from delay is imposition of fines for building violations against a mortgagee.[19] It can be suggested here that the decision is aberrational and conspicuously unfounded. But until such time as it may be reversed, it exists and requires mention. Because the case has been analyzed at length in these pages, its treatment here can be brief.[20]

Atypically, this was not an instance of an owner or junior lienors complaining of prejudically mounting senior debt, which is really the heart of this subject, but rather a case of tenants abandoned by the owner/mortgagor eliciting penalties for their suffering imposed upon a mortgagee not in possession.

However, a mortgage holder is not obligated to foreclose its mortgage. If it does foreclose, no pace of the action is mandated, although protracted delay can have monetary consequences, as previously noted. Nor is a mortgagee obliged to assume physical possession or responsibility for the mortgaged premises.

Exercise of an assignment of rents provision (which does not entail possession anyway); becoming a mortgagee in possession; obtaining the appointment of a receiver, all are options.

Indeed, for the reasons that a building may be laden with violations and could be disproportionately expensive to repair, a mortgagee might astutely elect either not to foreclose or to forsake a foreclosure action once begun.

The case at issue contained the unfortunate (for lenders) confluence of unusual delay — a 24 month interregnum between foreclosure judgment and scheduling the sale — deplorable conditons at a tenanted multiple dwelling and no one around to blame.

The image of the mortgagee bank, which could have taken control if a sale was held, was not enhanced in the court's eyes, who observed that all during the snail's pace of the action, real estate taxes and water and sewer charges were paid. Somehow, control was found on the bank's part and it was fined.

Conclusion

Certainly in reported decisions, assaults upon foreclosing plaintiffs for delay in prosecuting the actions are infrequent. But there can be consequences if a mortgagee is unduly dilatory. It would be difficult for a plaintiff to run afoul of applicable CPLR provisions because there are warning mechanisms.

The new case transmuting a mortgage holder into a controlling entity is unlikely to find favor at higher judicial levels and, while vigilance and healthy concern are recommended for the moment, a prediction that the ruling will be without significance in the future seems safe. Nor is laches a genuine practical threat, although it might be hard to banish any defense if delays mount to durations of ten, fifteen or twenty years.

Ultimately, the most viable threat to the dilatory foreclosing plaintiff is loss of interest. That point seems clear in the Second Department.

How to resolve that with the Nassau Surrogate's interpretation that actionable prejudice cannot be evaluated until a sale takes place is somewhat more difficult. Suffice to say, the mortgagee who protracts an action is not immune to penalty.

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(1) "Rule 3404. Dismissal of abandoned cases. A case in the supreme court or a county court marked "off" or struck from the calendar or unanswered on a clerk's calendar call, and not restored within one year thereafter, shall be deemed abandoned and shall be dismissed without costs for neglect to prosecute. The clerk shall make an appropriate entry without the necessity of an order."

(2) The statute is still more expansive and although the minutiae of CPLR practice dictates are not economically delineated here, careful evaluation of the full text of CPLR Rule 3216 can become important. That nuance on the subject continues is highlighted by Professor David Siegel's discussion of the rule and case law in New York State Law Digest, No. 433 (January 1996); see also *Chase* v. *Scavuzzo*, 85 NY2d 812. For an in depth review of statute of limitations as a defense in foreclosure, see 1 *Bergman on New York Mortgage Foreclousres*, §5.11 (Matthew Bender & Co., Inc., Rev. 1996).

(3) *Federal National Mort. Association* v. *Mebane*, 208 AD2d 892 (2d Dept. 1994).

(4) Id.

(5) Op cit.

(6) For a more complete discussion of laches as a defense to foreclosure, see 1 *Bergman on New York Mortgage Foreclosures*, §5.10 (Matthew Bender & Co. Inc., Rev. 1996).

(7) *Verna* v. *O'Brien*, 78 Misc.2d 288, 356 N.Y.S.2d 929 (1974).

(8) See, *inter alia*, *Cross* v. *Allen*, 141 U.S. 528, 12 S. Ct. 67, 35 L.Ed. 843 (1891); *Riordan* v. *Ferguson*, 147 F.2d 983 (2d Cir. 1945); *Wesselman* v. *Engel Co.*, 309 N.Y. 27, 127 N.E.2d 736 (1955); *Pollitz* v. *Wabash R.R. Co.*, 207 N.Y. 113, 100 N.E. 721 (1912); *New York State Mort. Loan Enforcement & Admin. Corp.* v. *North Town Phase II Houses, Inc.*, 191 AD2d 151, (1st Dept 1993); *First Fed Sav. & Loan Ass'n of Rochester* v. *Capalongo*, 152 AD2d 833, (3d Dept. 1989); *Kings County Trust Co.* v. *Derx*, 237 A.D. 548, (2d Dept. 1933); *Verna* v. *O'Brien*, 78 Misc.2d 288 (1974); *Griffo* v. *Swartz*, 61 Misc.2d 504 (1969); *Monroe County Sav. Bank* v. *Baker*, 147 Misc. 522, (1933); *Integrity Trust Co.* v. *Posch*, 13 N.Y.S.2d 973 (N.Y. City Ct. 1939).

(9) *Cross* v. *Allen*, 141 U.S. 528, 12 S.Ct. 67, 35 L.Ed. 843 (1891); See also *Brooklyn Free Kindergarten Soc'y* v. *Elbran Realty Corp.*, 255 A.D. 852, 7 NYS2d 531 (2d Dept. 1938).

(10) *Wesselman* v. *Engel Co.*, 309 N.Y. 27, 127 N.E.2d 736 (1955).

(11) *Smith* v.*Sheen*, _ A.D.2d _, 628 N.Y.S.2d 280 (1st Dept. 1995).

(12) *Sloane* v. *Gape*, _ A.D.2d _, 627 NYS2d 785 (2d Dept. 1995); *South Shore Fed. Sav. & Loan Association*, 54 AD2d 978, 389 NYS2d 29 (2d Dept. 1976); *Bosco* v. *Alicino*, 37 AD2d 552, 322 NYS2d 414 (1st Dept. 1971), citing *Shubert v. Lawrence*, 27 AD2d 292, 297, 278 NYS2d 537, 542; *Spadanuta v. Incorporated Village of Rockville Centre*, 20 AD2d 799, 800, 248 NYS2d 405, 407, affd., 15 NY2d 755, 257 NYS2d 329, 205 N.E.2d 525; CPLR 5001(a).

(13) Id.

(14) 91 AD2d 601, 456 NYS2d 430 (2d Dept. 1982).

(15) *Dollar Fed. Sav. & Loan Assocation* v. *Kallan*, 91 AD2d 601, 456 NYS2d 430 (2d Dept. 1982).

(16) *Griffo* v. *Swartz*, 61 Misc.2d 504, 306 NYS2d 64 (1969).

(17) *Galasso* v. *Zacarria*, *NYLJ.*, Mar. 24, 1994, p. 35, col. 5 (Surrogate's Ct., Nass. Co., Radigan, J.).

(18) Id.

(19) *Dept. of Housing Preservation and Development* v. *Greenpoint Sav. Bank*, N.Y.L.J., Mar. 13, 1996, p. 29, col. 2 (Civil Ct., Housing Part, George J.).

(20) See Rasmussen, "When a Landlord Disappears," *NYLJ*, Ap. 17, 1996, p. 5, col. 2.