MISSTATEMENT ON MORTGAGE APPLICATIONS AS BASIS TO FORECLOSURE

by Bruce J. Bergman

Readers hardly need be reminded that from time to time, less than candid information is supplied on a mortgage application by a borrower. How meaningful that could be depends upon a number of factors, but a few quick examples make the point. For lenders who sell their paper, they may nevertheless be obliged to buy back a loan if it is based upon erroneous information. Then too, the interest rate on an owner-occupied house is, of course, less than when the owner resides elsewhere. In the end, then, a compelling question is, what's the remedy?

One of the places where lenders do not so often encounter unusual variety is the nature of the default which triggers acceleration and then foreclosure. Overwhelmingly, the default encountered is failure to pay. For whatever reason, the borrower missed some or many installments or failed to satisfy the mortgage upon its maturity. Although there are nuances surrounding even this most obvious and basic breach, essentially (in New York) the courts are very strict in authorizing foreclosure for neglect to pay. There isn't much room for legitimate excuse when non-payment is the issue.

Even a brief review of an acceleration clause in a mortgage, however, reveals immediately that there are other grounds to accelerate and foreclosure. In a residential mortgage, these will typically include due on sale, maintenance of insurance, keeping current a senior mortgage, failure to pay taxes, failure to repair, alterations without consent, demolition without consent, building violations and failure to issue estoppel certificate, among some others. The commercial mortgage will contain many more provisions to abide the complexities attendant to larger transactions.

Is it possible that a borrower could be maintaining payments on the mortgage while violating some other term? Although it won't occur very often, the answer is most assuredly "yes." For example, where a lender might not be escrowing for taxes, a borrower could be remitting monthly installments towards the mortgage while ignoring real estate tax bills. Or, the borrower might be making the payments but neglecting upkeep to the point where the property is precipitously declining in value.

But why the discussion? It might seem apparent that if a borrower breaches an obligation in the mortgage contract, there would be no question but that foreclosure is authorized. In New York that is not so.

This is too broad and detailed a subject to analyze in depth here. [More than sixty-five printed pages are consumed reviewing it at 1 Bergman on New York Mortgage Foreclosures, Chap. 4 (Matthew Bender & Co., Inc., Rev. 1996)—a source we heartily recommend!] The key to analysis is the type of default. More briefly than the subject deserves, for failure to pay installments, or maintain insurance, or for breach of the due on sale provision, enforcement will be unswerving. That is likely so as well for total demolition without consent and failure to issue an estoppel certificate. For almost any other variety of default, uncertainty surrounds the result and it may be highly dependent upon the facts.

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Now here is a comforting scenario which returns to the central topic. A lender sells many of its loans shortly after closing. The borrower must have a certain level of credit (there are of course other elements) and if the loan is not as represented, the lender must buy it back from the assignee.

In keeping with these procedures, a borrower's mortgage application recites his employment with an insurance company. Some time later, his employment was terminated. At the closing, the lender required a re-signing of the mortgage application to confirm the information. Even though the statement about employment was no longer true, the borrower re-signed and the loan closed. The mortgage was then assigned.

Many months later, the assignee discovered the employment misrepresentation and insisted that the original lender buy back the loan. A foreclosure was then about to begin, based upon the misrepresentation, when there was also a payment default. Nevertheless, both grounds were recited as the basis of the foreclosure.

While the borrower tried to argue that he did not mislead the lender, the court granted summary judgment, reciting plaintiff's entitlement to judgment by virtue of "the proof that defendant misrepresented his employment status... when he re-executed his mortgage application and stated therein that he was employed..." [Loan America Financial Corporation v. Talboom, 620 N.Y.S.2d 221 (1994)].

Because the borrower was clearly in default in remitting mortgage payments (although he tried to argue that he was not), it certainly made it easier for the court to support foreclosure for the employment misstatement as well. The ultimate question is whether this case stands firmly for the position that such a misleading assertion in a mortgage application is a ground to foreclosure in New York. We think it is and at the very least, this enlightened decision for the first time provides potent ammunition to make the argument should it be necessary to protect a lender.

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