

NON-JUDICIAL FORECLOSURE IN NEW YORK – WHAT’S THE STORY?

By: **Bruce J. Bergman***

Non-judicial foreclosure does indeed exist in New York – although it is not surprising that the fact is not so widely known. The immediate reason is that the procedure has no application to residential properties, which obviously diminishes its utility. But when it is available it has meaning. The procedure began in 1998 and has been extended a number of times, the latest until July 1, 2009.

First, a historical footnote: non-judicial foreclosure was a part of New York statutory law dating back before the great depression. For a number of reasons, though – due process concerns and the reluctance of title companies to insure the titles chief among them – the power was almost never used.

Meanwhile, New York attorneys well recognized that non-judicial or power of sale methods employed in almost half the states in the nation was far more efficient than the judicial version in the Empire State where actions consuming years are not unheard of. The genesis of what became the new Article 14 of the Real Property Actions and Proceedings Law was the effort of a New York State Bar Association task force intending to shortcut the time-consuming judicial foreclosure process generally in New York State. Although large commercial foreclosures in particular tended perhaps to suffer unduly from protracted delays, there was no intention to confine the prospective streamlined statute to commercial cases and exclude residential properties. When the bar association draft went through the legislative process,

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however, residential properties were excluded as subjects for non-judicial foreclosure. Although the statute is not labeled as applying essentially to non-residential properties, such is its actuality.

The statute carefully considered the infirmities of the old and intended to address them so that an efficacious, practical result could be achieved. Although its non-judicial approach clearly provides a faster method of foreclosure – to the extent the statute applies at all – it still has a number of *judicial* aspects. For example, among others, court authority must be sought when the United States holds a junior interest to be extinguished, when a receiver is desired, and to pursue either surplus monies or a deficiency judgment.

The procedures of Article 14 for power of sale foreclosure are available for a mortgage upon real property in the state so long as the mortgage contains a power of sale provision, which is defined as a provision that upon a mortgage default or a default upon a note, bond or other obligation secured thereby, the mortgagee has the right to sell the mortgaged property. Having met those preliminaries, the mortgage is entitled to be foreclosed in the matter prescribed for a non-judicial proceeding for foreclosure by power of sale pursuant to Article 14.

Four prerequisites, however, must be fulfilled. These are technical but would typically be taken care of (such as the need to record the mortgage) so need not be reviewed here. Awareness that this needs to be considered should suffice

Exception to Power of Sale Foreclosure

Exceptions to the availability of power of sale foreclosure essentially confine it to residential buildings of more than five units outside of New York City, although the foreclosure would have to leave leases intact, and commercial premises anywhere in the state. The procedure is not available for a mortgage on real property improved solely by:

- A residential building of less than six dwelling units; and

- A residential condominium unit in a residential building owned in condominium form of ownership; and
- A residential building owned by a qualified cooperative apartment corporation; and
- A building in which the number of units occupied by residential tenants equals or is greater than sixty-five percent of the total number of units in the building located in a city with a population of one million or more, which means New York City.

Power of sale foreclosure is likewise unavailable for a mortgage on property containing residential apartment units where the foreclosure would seek or would result in foreclosure, termination, modification or impairment of a tenants' interest in any lease for a residential unit in the mortgaged property or of the tenant's possessory rights pursuant thereto.

Impediments – When the Borrower Can Opt Out

Even for the narrow category of instances where power of sale foreclosure remains available, there is an ability on the borrower's part to either opt out or challenge imposition of the procedures. These opt-outs apply separately to mortgages in existence prior to the effective date of the statute and those in existence subsequent to the effective date of the statute.

Mortgages Predating 1998

If the mortgage to be foreclosed – or the extension, amendment, modification or consolidation thereof – was executed prior to the effective date of the statute, then the borrower may require that further foreclosure proceedings be conducted judicially. The borrower accomplishes this by written notice to the mortgagee delivered by registered or certified mail, or by such other method as may be specified in the mortgage, with certain time requirements and

with minimal content essentials.

Mortgages Subsequent to 1998

If the mortgage to be foreclosed non-judicially was executed after 1998, then the borrower can apply for an order directing that further proceedings be conducted judicially and for a temporary restraining order staying further proceedings pending hearing of the application. The borrower must then support the application with facts of one or more of the following allegations:

- That the mortgage does not contain a power of sale clause or some other provision permitting foreclosure in a non-judicial manner; and/or
- That the mortgage obligation is invalid or not otherwise due; and/or
- That the mortgagor is not in default under the mortgage or otherwise has a meritorious defense to the foreclosure; and/or
- That the mortgagee has not complied with the terms and conditions of Article 14; and/or
- That under the facts and circumstances presented, undue hardship to the mortgagor would result from allowing the foreclosure to proceed non-judicially.

Should the application be granted, the foreclosure must then proceed judicially unless the court subsequently orders otherwise. Should the application be denied, then the sale pursuant to Article 14 may proceed non-judicially.

Problems for Mortgagees with Opt-Out Provision

One of the problems with judicial foreclosure in New York that prompted exploration of revivifying non-judicial foreclosure was the time necessary to complete a mortgage foreclosure action. Although much of the time consumed in a judicial foreclosure involves achieving the

various plateaus, congested court calendars (particularly downstate) are a major component of burdensome durations. The provisos of the power of sale procedure greatly reduce the time, primarily by eliminating the need to invoke court involvement. (In some instances, engagement of the court becomes necessary.)

Opting out of the post-July, 1998 mortgage may not be automatic, but the legislature was generous in excavating an escape route – or at least, a time killer. Aside from the need for a power of sale provision in the mortgage, the next four grounds to argue against the abbreviated course open the door to contention and mischief.

Although ultimately proving the point is far more difficult, claiming the mortgage is invalid because of fraud in the inducement is hardly an unheard of assertion. Then there is the claim that the mortgage is not due because the mortgagee gave an extension, or was irresolute in some correspondence on the subject or erroneously rejected a remittance or misapplied a check. Then there is waiver, unconscionable conduct, bad faith, and the lower grade laches or unclean hands, among hosts of others.

And might not a mortgagor successfully argue pursuant to the “undue hardship” standard: “I can refinance this mortgage in five months. In a judicial foreclosure case, which wouldn’t conclude for twelve months, I would obtain all the funds to save the property and satisfy the mortgage. But in this rapid power of sale proceeding, the foreclosure will be over before I can get the money. I will suffer under hardship!” Maybe. Moreover, undue hardship is an ill-defined phrase. It is difficult to predict what a court might do, particularly when loss of property and a business is in the offing.

If a mortgagor’s assault on the non-judicial proceeding is successful, the hapless mortgagee endures all the time generated in starting the power of sale case and then attempting to

fend off the attack. Defeat confines the remedy solely to judicial foreclosure, and whatever time would have been saved by the non-judicial method thereby proved illusory. Even if the borrower's offensive is routed, the apparent economy of the power of sale procedure is considerably reduced.

Conclusion

This brief discussion of power of sale in New York does not explore the considerable detail of the statute; there is considerably more to it. But the details are not the point. That it exists, but does not quite live up to all expectations, is the message.

Particularly for commercial foreclosures pursued essentially on consent, power of sale is especially welcome. Beyond that, New York's reputation as a difficult state to prosecute a foreclosure remains intact.