A New Look at *Sanders v. Palmer* and the Multiple Mortgage Situation — Less Cause For Alarm?*

Bruce J. Bergman**
Garden City, New York

Editorial Comment: We are again fortunate in having the expertise of Bruce Bergman in the area of mortgage foreclosures. In the following piece he deals with an aspect of mortgage law deriving from multiple mortgages securing a single debt. Mortgage law must not be viewed as just a matter of paper work. How that security will be allowed to function when it is called upon to satisfy an obligation, is the critical ingredient — a matter brought to the fore in the Court of Appeals' case of Sanders v. Palmer analyzed by Bruce in the following piece.

The issuance of the Court of Appeals' decision in *Sanders v. Palmer*, 68 N.Y.2d 180, 507 N.Y.S.2d 844 (1986) caused considerable stir and consternation among mortgage lenders and their counsel. A portion of the opinion is of the view that where multiple mortgages secure a single debt, there must be separate sales of the security, with application for and fixation of a deficiency upon each sale as a prerequisite to sale of the next parcel if deficiency liability is sought. (The one saving grace is the condition that the court may order otherwise.) Because the situation of multiple mortgages securing one debt is not uncommon, the cited language presents lenders with apparently nettlesome mechanical and financial problems which are neither simply illusory nor mere fodder for pedantic law review analysis.

As to procedure, it presents the singularly convoluted mandate that after each parcel is sold, there must be a determination of the deficiency. If this means a mere mathematical computation to assess the **quantum** of the deficiency, so as to determine which parcel is best to next sell, it is perhaps a less troublesome concept. Lamentably, there exists no form of procedure to accomplish this, but astute practitioners would be able to glean some form of motion to achieve the end. Unfortunately, however, the many months this procedure grafts on to the foreclosure process increases the period during which interest will accrue and would tend, therefore, to pose some threat to the integrity of the investment. Mindful that any party potentially liable for a deficiency could quarrel with the issue of value, it is conceivable that a valuation trial would be required, suggesting still further protraction as well as further expense for expert witnesses in addition to increased noncompensible legal cost. In any event, the case is not clear in specifying whether a calculation only need be pursued or whether an actual deficiency **judgment** must be obtained.

Assuming it is the deficiency judgment which is required, one could inquire as to the mechanics attendant to its status after a subsequent parcel is sold. With the proceeds of the second parcel in hand, does that mean that the original deficiency judgment is simply reduced by the quantum of monies received? The answer may perhaps be "no," because the deficiency must be assessed anew with all the valuation aspect infirmities previously mentioned.

Although the cited burdens and confusion emanating from the case are troublesome enough, whether the offending dicta in *Sanders v. Palmer* flows appropriately from the case is another area of question. To understand the point, the law as it existed prior to the subject case is worthy of some analysis.

When a mortgagee forecloses, it is bound by the legal proposition that exclusion of a parcel from the foreclosure complaint is a waiver of any right against that piece. [*Bankers Trust Co. v. G.H. Equities, Inc.*, 57 A.D.2d 601, 394 N.Y.S.2d 30 (2nd Dept. 1977); *Bodner v. Brickner*, 29

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A.D.2d 441, 288 N.Y.S.2d 342 (1st Dept. 1968), citing *Matter of City of N.Y. (Neptune Ave.)*, 271 N.Y. 331, 3 N.E.2d 445)]. Next, pursuant to RPAPL Section 1321(1), it is within the purview of the referee appointed to compute to "...examine and report whether the mortgaged premises can be sold in parcels..."

Finally, when a mortgagee neglects to apply for a deficiency judgment, regardless of the foreclosure sale proceeds, the sum received through the foreclosure sale must be deemed full satisfaction of the mortgage debt, to the exclusion of any other pursuit of deficiency liability. [RPAPL Section 1371(3)]. Save a rarely invoked exception to the cited aphorism, which is not relevant to the point, there is a plethora of well established case law underscoring the mandate to pursue a deficiency in the foreclosure or suffer extinguishment of the right to claim such liability. [*See inter alia, Whitestone Sav. & Loan Ass'n. v. Allstate Ins. Co.*, 28 N.Y.2d 332, 270 N.E.2d 694, 321 N.Y.S.2d 862 (1971); *Bedcro Realty Corp. v. Brooklyn Trust Co.*, 290 N.Y. 520, 49 N.E.2d 992 (1943); *Corley v. Miller*, 520 N.Y.S.2d 21 (2nd Dept. 1987); *TBS Enter., Inc. v. Grobe*, 114 A.D.2d 445, 494 N.Y.S.2d 716 (2nd Dept. 1985); *Polish Nat'l. Alliance of Brooklyn v. White Eagle Hall Co.*, 98 A.D.2d 400, 470 N.Y.S.2d 642 (2nd Dept. 1983); *Sportmen's Park, Inc. v. N.Y. Property Ins. Underwriting Ass'n.*, 97 A.D.2d 893, 470 N.Y.S.2d 456 (3rd Dept. 1983), *aff'd* 63 N.Y.2d 998, 473 N.E.2d 262, 483 N.Y.S.2d 1012 (1984); *Kleet Lumber Co. v. Foley Constr. Corp.*, 91 A.D.2d 1014, 458 N.Y.S.2d 889 (2nd Dept. 1983); *Guardian Fed. Sav. & Loan Ass'n. v. Horse-Hawk Holding Corp.*, 72 A.D.2d 737, 421 N.Y.S.2d 244 (2nd Dept. 1979); *Band Realty Co. v. North Brewster, Inc.*, 59 A.D.2d 770, 398 N.Y.S.2d 724 (2nd Dept. 1977); *Statewide Sav. & Loan Ass'n. v. Canoe Hill, Inc.*, 54 A.D.2d 1018, 388 N.Y.S.2d 188 (3rd Dept. 1976), *aff'd*, 44 N.Y.2d 843, 378 N.E.2d 118, 406 N.Y.S.2d 755 (1978); *Serial Fed. Sav. & Loan Ass'n. of N.Y.C. v. Crescimanno*, 35 A.D.2d 561, 313 N.Y.S.2d 326 (2nd Dept. 1970)].

Given the accepted prior status of the law, what did *Sanders v. Palmer* conclude and why did it so provide? The facts in the case are not so peculiar. A corporate loan was secured by mortgages on three parcels owned by the mortgagor corporation. In addition to personal guarantees by certain principals of the corporation, there was an additional personal guarantee, in turn further secured by a second mortgage on the guarantor's own property.

When a default ensued, the lender instituted foreclosure on **one** of the corporate properties and a **separate** foreclosure upon the guarantor's parcel. The guarantor was named as a party defendant in the foreclosure of the corporate property. The first foreclosure proceeded to a sale, but no deficiency judgment was sought. Instead, the lender then elected to complete the foreclosure upon the guarantor's property. Ultimately, the guarantor interposed an answer in the latter foreclosure urging RPAPL Section 1371(3) as a bar on the ground that neglect to pursue a deficiency in the first foreclosure was a prohibition against any later liability on the guarantee.

Both special term and the Second Department understandably adopted the guarantor's position and proscribed prosecution of the second foreclosure. The Court of Appeals affirmed. What is curious, however, is the precise language the Court of Appeals employed in its affirmance.

When the plaintiff neglected to include **all** the parcels securing the debt in one foreclosure, it clearly waived its rights as against all excluded security. That miscue alone could have been the basis of the decision in *Sanders*. Not only did the plaintiff refrain from pursuing two corporate parcels, but it saved the guarantor's property for inclusion in a separate, unauthorized foreclosure.

Still further, when plaintiff completed the initial foreclosure, but failed to timely seek a deficiency judgment against the named guarantor, that procedural flaw could likewise have been the sole basis for an affirmance. Established precepts, as noted, would have prohibited seeking a deficiency judgment when that relief had not been pursued in the first foreclosure action.

Somehow compelled nevertheless to go further, the Court of Appeals asserted that a guarantor who provides security beyond that given by the debtor is entitled to the protection of RPAPL Section 1371(3) when no deficiency judgment is obtained. Such is a well founded view and the case could have halted there, setting forth that a guarantor cannot be liable unless a deficiency judgment is obtained. Such is an accepted maxim of long standing, phrased in terms that where a foreclosing plaintiff fails to timely move for a deficiency, no action may be maintained against a guarantor. [*TBS Enter., Inc. v. Grobe, supra.; Merchants Nat'l. Bank & Trust Co. of Syracuse v. Wagner*, 93 Misc. 2d 244, 402 N.Y.S.2d 936 (1978); *Robert v. Kidansky*, 111 App. Div. 475, 97 N.Y.S. 913 (1st Dept. 1906), *aff'd*, 188 N.Y. 638, 81 N.E. 1174 (1907); *Kings County Sav. Bank v. Fulton Sav. Bank*, 268 App. Div. 452, 52 N.Y.S.2d 47 (2nd Dept. 1944); *Scofield v. Doscher*, 72 N.Y. 491 (1878); *Suydam v. Bartle*, 9 Paige 294 (1841); *Gouldner v. Rachlin*, 177 (61) NYLJ (3-30-77), p. 10, col. 1B (Sup. N.Y., Evans, J.); *State Bank of Albany v. Amak Enter., Inc.*, 77 Misc. 2d 340, 353 N.Y.S.2d 857 (1974); *Kleet Lumber Co. v. Foley Constr. Corp., supra.; Bedcro Realty Corp. v. Brooklyn Trust Co., supra.; Statewide Sav. & Loan Ass'n. v. Canoe Hill, Inc., supra.; Band Realty Co. v. North Brewster, Inc., supra.*]. The principle has also been expressed that where plaintiff neglects to apply for a deficiency judgment, no right remains to resort to any other collateral security because the debt is deemed fully satisfied. [*Klein v. Gray*, 127 N.Y.S.2d 459 (1954)].

That several mortgages may have been given to secure one debt cannot, the Court ruled in *Sanders*, authorize a multiplicity of suits where the properties are subject to the jurisdiction of one court. That pronouncement is immune from dispute and could have been part of the already accepted basis to rule in plaintiff's behalf. It was at this juncture, however, that the Court of Appeals reached a new level of analysis and opined in dicta that in the instance of multiple mortgages for one debt, what is required is a separate sale of each portion of the security in such order as the court fixes, followed by the serial determination of deficiency — **unless the court orders otherwise**.

Offended though mortgagees may be by the noted ultimate pronouncement, the effect may not be as omi-

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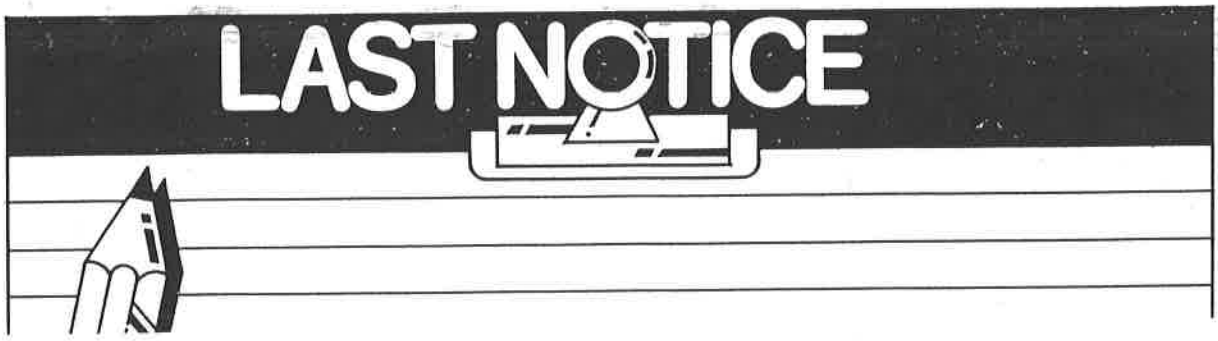
nous as it first appeared. If only a portion of the security is sold, there should not be deficiency judgment liability because unsold security could yet eliminate the deficiency. To go through the exercise of individual assessments of the deficiency quantum is the unfortunate and deleterious aspect. But then there is the exculpatory language that the court can direct otherwise.

In turn, this harkens back to the computing referee's authority to determine whether the security can be sold in parcels. As a practical matter, a foreclosing mortgagee should have some reasonable expectation of the value of its security. Appraisals in the file are typical. If stale, they can be readily updated. If non-existent, they can be solicited. Armed with value, the referee can decree, for example, that two parcels together be sold first upon the assumption that they will yield the full sum owed. The judgment can certainly confirm this sequence of sale and in so doing, in compliance with *Sanders v. Palmer*, the court has indeed otherwise ordered. If unexpectedly there is a shortfall, **then** the deficiency can be assessed and plaintiff can sell a third parcel. Where three parcels were at issue, one sale only is perhaps likely, with a possibility of two, instead of three. It might even be that full value could not be obtainable unless all three parcels are sold either in one block or in some number of immediate sales without necessity to assess deficiencies in between. At least such appears possible in light of the *Sanders* directive that the court has the authority to otherwise direct.

While all this of course depends upon the relationship between the amount due the lender and the respective value of the properties, the specter of *Sanders v. Palmer* seriously upsetting traditional notions of foreclosure practice may not be as calamitous as originally perceived.

****Mr. Bergman is a partner in the law firm of Roach & Bergman in Garden City and an adjunct associate professor of real estate with New York University's Real Estate Institute where he teaches the mortgage foreclosure course. A member of the American College of Real Estate Lawyers and past chair of the Real Property Law Committee of the Nassau County Bar Association, his text, *Bergman on New York Mortgage Foreclosures*, will be published in early 1990 by Matthew Bender & Co., Inc.**



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