LENDER LIABLE FOR FIRE DEATH AT MORTGAGED PREMISES!

*by Bruce J. Bergman

Since when does a mortgage foreclosure beget a negligence action? For mortgage lenders it is assuredly a Kafkaesque scenario, perilous and startlingly scary: people die in a fire at mortgaged premises and a court rules that the lender can be liable for damages to the estate of the deceased. It certainly doesn't sound like a creature of real estate law or practice – not in the traditional sense that most practitioners would perceive, but it is. A new ruling says so, *Lezama v. Cedano*, 119 A.D.3d 479, 991 N.Y.S.2d 32 (1st Dept. 2014).

How this came about, why it is possible, and why lenders would aver that it should not be so is the focus that follows.

THE NEW CASE

This was a *negligence* action arising from a fire that killed a twelve year old boy and his mother (and another person not involved in the action), all residents of a multiple dwelling. The estate administrator of the deceased initiated suit against the owner of the building – which is standard and expected – *and* the mortgage holder (not standard), alleging that had the premises been adequately maintained, the deaths would not have occurred.

*Bruce J. Bergman, a partner with Berkman, Henoch, Peterson, Peddy & Fenchel, P.C. of Garden City, is the author of "Bergman on New York Mortgage Foreclosures" (four vols., LexisNexis Matthew Bender, rev. 2014).

The mortgagee was foreclosing on the building and had obtained a judgment of foreclosure and sale but was not a mortgagee-in-possession and did not own the property[1]; the mortgagor did. Equitable title is conveyed only when the property is struck down at the foreclosure auction sale[2], followed, when a deed is delivered, by legal title.

An important aspect of the complaint in the negligence action was the assertion that the mortgagor (owner) had abandoned the building, that the mortgagee knew the building was abandoned, that no one had been appointed to inspect or maintain the property and that it was occupied by several tenants.

The mortgagee moved to dismiss for failure to state a cause of action, based upon documentary evidence showing that the property was not abandoned and it therefore had no obligation to maintain (without which there could be no liability as to it).

Procedurally, the holding was that the mortgagee had failed to conclusively establish that the property was not abandoned and accordingly the motion to dismiss the complaint was denied. This invoked discussion of 3211(a) motion standards not relevant to this evaluation. Rather, the portent of the holding is that the confluence of a judgment of foreclosure, abandonment by the owner and the presence of tenant(s) imposes a maintenance obligation upon the mortgagee who is then liable in tort.

The potential liability to the lender in this case – and for others in the future is staggering, critically in an amount which can never be assessed in advance.

STATUTE CREATING REPAIR OBLIGATION

At common law, a mortgagee not in possession of mortgaged property and without control over it could not be liable in negligence for its condition.[3] Were a mortgagee in possession, however, then it would be liable to secure and protect the property.[4] (This is one reason why becoming a mortgagee in possession is so rarely pursued.)

The mortgage crisis of the late 2000's, however, enticed the legislature to implement a host of borrower friendly provisions relating to mortgage foreclosures. But one in particular had the effect of protecting tenants – not borrowers. Enforceable as of April 14, 2010, this was RPAPL §1307, entitled "Duty to Maintain Foreclosed Property".[5]

RPAPL §1307(1) provides in essence that when a plaintiff in a residential real property mortgage foreclosure action obtains the judgment of foreclosure and sale, 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. This, of course, changed the common law and shifted the duty to maintain from the owner/borrower to the foreclosing plaintiff, albeit commencing at the stage of judgment of foreclosure and sale.

It was immediately and readily predictable without mantic powers that the statute would create unexpected tort liability, although there is no indication such was the intent or that it was even considered. (That it likely was not foreseen by the solons is part of the problem.)

ADDITIONAL PERILS AND AMBIGUITY

When a residential mortgage loan is made, a lender cannot know if or when it might go into default, or when it will arrive at the judgment plateau and if the other conditions which trigger the maintenance imperative will be fulfilled, much less divine whether a claimed dangerous condition could exist and result in harm. But if the stars are in parlous alignment, the lender could face not only unpredictable expense for an undefinable period, but catastrophic unforeseeable liability.

This peril is compounded by confusion – uncertainties – in the statute itself which make consequences still more arduous to plan for. Among many examples, *duration* of the maintenance period, and thus the time of exposure to tort liability, is ultimately immeasurable.

One demarcation is that the maintenance obligation will arise if the property is vacant. Because a mixed-use building is covered by the statute, it is not clear if the commercial establishments must be vacant as well, or only the residential portions.

Another point invoking repair occurs when property becomes vacant after *issuance* of the foreclosure judgment. This presents two immediate problems. How is

the foreclosing party to know precisely if the property *becomes* vacant and how often do they have to look to assess that determination?

As part of that dilemma, all begins with “issuance” if a judgment – but that is not a term of art. A judgment is first signed and thereafter entered. The time between the two events can be days, weeks or more. Thus, precisely when the obligation might begin, and when the lender must be on the alert, is unclear; it is certainly imprecise.

The next defining moment recited by the statute is “abandoned by the mortgagor but occupied by a tenant.” The definition of residential property for the purpose of this section does not require owner occupied. So if the mortgagor never resided at the property, entirely conceivable, it may be impossible to measure “abandonment”. If a tenant is present, maintenance is required only if abandoned by the mortgagor so this will typically be extraordinarily difficult to determine. Even if the mortgagor did live at the premises, knowing if he departed, with the intention never to return, is always a murky question of fact. Even assuming that was determinable, it is not clear whether abandonment means merely the mortgagor’s physical departure or abandonment of his responsibilities as the owner.

Further indistinction emerges because the mortgagor and the owner are not necessarily the same person. A mortgagor who owns the property can (and sometimes does) sell the mortgaged premises. So measuring anything by referring solely to the mortgagor is pointedly indeterminate.

Because entry of a judgment of foreclosure and sale is the last step in a foreclosure action prior to the auction sale, the drafters likely assumed that duration of the maintenance period imposed upon foreclosing lenders was, if not finite, of limited length. The real world actuality, however, is that it is certainly *not* finite and duration from judgment to recordation of the referee's deed can be remarkably lengthy for a host of reasons recognized by practitioners.[6]

Another serious, although possibly obscure, matter surrounds ending a foreclosure action to halt the maintenance imposition. Lenders sometimes realize as a foreclosure nears its conclusion that proceeding to a sale has no value. They initiated the action hoping that some favorable resolution would arrive, an approach everyone would encourage. It may be, though, that outstanding taxes are greater than the value of the property, or that a declining market or physical deterioration has too greatly eroded the equity. In such instances (and there are of course others) a lender might sagely elect to avoid futility, spend no more and not proceed to sale. But if the lender is saddled with the repair obligation, the term of the obligation becomes unending should the sale never be consummated. Likewise, the period of tort liability becomes eternal. Thus, the option not to proceed is effectively removed unless this evaluation can be made much earlier in the case, something lenders find difficult for the very reason that encouraging or eliciting a more amenable conclusion so often requires prosecution of the foreclosure action.

CONCLUSIONS AND FINAL INCONGRUITIES

Critically, as a matter of law, a mortgage is a *lien* on real estate. It is not an ownership interest.[7] If a lender deemed it advisable as a matter of business judgment to become a mortgagee in possession to collect rents and maintain the property, it is free to do so pursuant to the mortgage documents and case law – but for all the reasons mentioned here invariably does not so elect. Nor is it obliged to. Alternatively, again purely a matter of choice, the lender can have a receiver appointed for that purpose, but may refrain if the income is insufficient, lest the lender be constrained to pay the receiver – precisely what it might not want to do.

Not only is it revolutionary to require a party with only a lien interest (the mortgagee) to be liable for property maintenance, there is also a startling incongruity in making a mortgagee responsible for anything once the property is struck down at a foreclosure auction sale. From that moment, and until conveyance of the deed when the bidder becomes the legal owner, the *bidder* is the equitable owner of the property.[8] The mortgage is gone and the mortgagee has no interest in the property. Still, the statute demands responsibility when even the lender's lien interest has vanished. Indeed, it is questionable how a lender with neither title nor a lien could have an insurable interest to serve as a basis to maintain insurance coverage – which it assuredly must have if it will be liable for injury and death at the mortgaged premises.

It seems markedly irreconcilable that a mortgagor could default, forcing a lender to institute a foreclosure action and face expense and loss, then compelling the lender

to attend to the defaulter's own property at the lender's expense and peril, inclusive of claimed negligence liability. That, however, is what the statute so indecorously does.

As a final disconcerting inconsistency, worthy of reemphasizing, the maintenance mandate is an event lenders did not bargain for and could never accurately calculate in advance. The life of the repair obligation is uncertain (potentially much longer than the statute imagined) and the monies to be expended for the indefinable period are likewise not predictable. What repairs and maintenance any building might need would depend upon the extent of owners' neglect and how long the property suffered that neglect. Nor could the cost of supplying heat and utilities for any size building for an immeasurable period be capable of prior contemplation. But the new case – ineluctably arising from the statute - adds much more and confirms the easy prediction that lenders will become defendants in negligence actions by virtue of initiating foreclosures.

Why lenders had to be made the gatekeepers to relieve defaulting borrowers of their responsibilities to tenants is an especially troubling inquiry, particularly when adding to it the wonderment as to why lenders would want to make mortgage loans in New York if they might unpredictability be exposed to such enormous liability.

---

[1] A judgment of foreclosure and sale does not grant ownership and does not extinguish the right to redeem. *See, Mosello v. Ali, Inc.*, 193 B.R.147 (S.D.N.Y. 1996), citing *Barnard v. Onderdonik*, 98 N.Y.158 (1885). Also see discussion and citation at 1 *Bergman on New York Mortgage Foreclosures,* §2.21(3), LexisNexis Matthew Bender (rev. 2014).

[2] *See, Hepworth v. Manetto Holding Corp.*, 262 A.D.877, 28 N.Y.S.2d 526 (2d Dept. 1941); *Norwest Mortgage, Inc. v. Brown*, 35 A.D.3d 682, 830 N.Y.S.2d 158 (2d Dept. 2006); for further discussion and citation, 1 *Bergman on New York Mortgage Foreclosures,* §2.24(3), LexisNexis Matthew Bender (rev. 2014).

[3] *Town of Huntington v. Lagone*, 29 Misc.3d 779, 908 N.Y.S.2d 320 (Dist. Ct. 2010), citing *Bowles v. City of New York*, 154 A.D.2d 324, 545 N.Y.S.2d 799 (2d Dept. 1989); *Moran v. Regency Sav. Bank,* 20 A.D.3d 305, 799 N.Y.S.2d 29 (1st Dept. 2005). Also, see discussion at 1 *Bergman on New York Mortgage Foreclosures* §2.24[9], LexisNexis Matthew Bender (rev. 2014).

[4] *Town of Huntington v. Lagone*, *supra.*, at note 3, citing *Trusto Bank v. Eakin,* 256 A.D.2d 778, 681 N.Y.S.2d 410 (3d Dept. 1998).

[5] The title is a misnomer because the obligation to maintain is imposed not when the property has been foreclosed (although it continues through that time) but, instead, during a foreclosure action wherein a judgment of foreclosure and sale has "issued".

[6] See delineation at 2 *Bergman on New York Mortgage Foreclosures*, §27.12, LexisNexis Matthew Bender (rev. 2014).

[7] *The Prudence Co. v. 160 West Seventy-Third Street Corp.,* 260 N.Y.205 (1932); *Holmes v. Gravenhorst*, 263 N.Y.148, 188 N.E. 285 (1933); *Colter Realty v. Primer Realty Corporation*, 262 A.D. 77, 27 N.Y.S.2d 850 (1st Dept. 1941); *Title Guar & Trust Co. v. Feldon Realty Corporation*, 149 Misc. 206, 267 N.Y.S. 48 (Sup. Ct. 1933); *Goodell v. Silver Creek Nat. Bank*, 48 N.Y.S.2d 572 (Sup. Ct. 1944). For an expanded discussion of this subject see 1 *Bergman on New York Mortgage Foreclosures* §2.05(1) and 2 *Bergman on New York Mortgage Foreclosures* §27.01[2] and [5]; §27.02[2], LexisNexis Matthew Bender (rev. 2014).

[8] Hepworth v. Manetto Holding Corp., 262 A.D. 877, 28 N.Y.S.2d 526 (2d Dept. 1941). For further discussion and case law citation see 2 *Bergman on New York Mortgage Foreclosures* §2.24[3], LexisNexis Matthew Bender (rev. 2014).