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New York Legislature Gives Lenders A New Way To Screw Up Foreclosures

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Between Christmas and New Year's Day of 2022, New York's Governor signed legislation designed to correct an alleged potential for "abuse" of the foreclosure process by mortgage lenders. The context for that "abuse" is relatively exotic and unusual. It had nevertheless spawned a series of New York cases. The Legislature's solution to the "abuse" creates a new pitfall for mortgage lenders when they try to recover their defaulted loans through the foreclosure process.

The legal issues start when a mortgage lender accelerates a loan, which is to say, requires the borrower to repay the entire loan because the borrower defaults in making monthly payments or in complying with other obligations under the loan documents. Once the lender accelerates the loan, New York law gives the lender six years in which to start a foreclosure action. Amazingly, lenders miss that deadline with some frequency.

Sometimes, a lender accelerates the loan as part of commencing the foreclosure litigation. Later, the lender might voluntarily stop the

foreclosure. In a recent New York case, the state's highest court decided that, in that circumstance, the voluntary termination cancels the acceleration. After that cancellation, the lender can stop worrying about the six-year period in which to start a foreclosure action. Instead, the lender can hold off and accelerate again later, starting a new six-year period.

The Legislature didn't like the idea that lenders could start to foreclose, stop their foreclosure action, and then wait as long as they wanted to accelerate again. This was considered to be abusive, a cruel way of tormenting the borrower. That was true even though at all points in the process the loan remained in default. The borrower had borrowed the loan, had the full benefit of the loan proceeds, wasn't performing its obligations under the loan documents, and could have ended its torment at any time by bringing the loan current or selling the mortgaged property.

In response, the state enacted a new law saying that once a lender accelerates a loan, nothing the lender unilaterally says or does can cancel or reverse the acceleration. After accelerating, the lender has only six years to start a foreclosure action. Voluntary termination of a foreclosure action doesn't restart the clock.

It doesn't seem horribly burdensome to require a mortgage lender to successfully start a foreclosure action, no matter what, within six years after accelerating a loan. On the other hand, the New York foreclosure process is extraordinarily complex and slow. Every foreclosure involves a judge and a series of filings and motions, which the courts often process at a snail's pace. Lenders are in no hurry to endure and pay for that process if they can avoid or postpone it. Most lenders don't really want to foreclose—they just want to be repaid—so they optimistically try to work with borrowers to give them more time. That sometimes involves voluntarily terminating a foreclosure proceeding.

In the bizarre case where a lender has accelerated a loan but years go by without a foreclosure action, the new law could effectively force the lender to start an action, rather than keep working with the borrower. Of course, a lender could probably solve the problem by making a bilateral agreement with the borrower to extend time, but the courts might not look kindly on that. Lenders worry about being too cute and creative. The new law should assure that lenders won't wait six years before starting their foreclosure actions. Thus, borrowers in default should no longer be tormented by facing uncertainty for more than six years.

Stepping back a bit, the legal developments described in this article take place against a backdrop in which New York mortgage loans can remain in default for the better part of a decade without a resolution. There's something very wrong with that picture. If New York foreclosures move that slowly, why would any sane mortgage lender accept a New York mortgage?

According to news reports, a sponsor of the new law, State Senator James Sanders, lives in a house that has been in foreclosure for 10 years. How can that be? And does it give him a conflict of interest?

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I help buyers, sellers, borrowers, lenders, tenants, property owners, and other commercial real estate market participants identify and achieve their business goals. To do that, I need to understand risk, security, numbers, value, financeability,

flexibility, and exit strategy. Some legal issues matter a lot and many don't. It's important to know the difference. I write extensively on commercial real estate law and practice – over 300 articles and five books on leasing, lending, and other areas, with some emphasis on ground leases. I occasionally serve as an arbitrator or expert witness in complex real estate disputes. That lets me see how transactions go wrong. Often, the problems could have been avoided by keeping it simple and following the money, but everyone got sidetracked. As a Forbes contributor, I try to tell stories that teach worthwhile lessons for real estate deals. **Read Less**