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Message from the Chair

When I was growing up, I was always fascinated by roller coaster rides—whether at Coney Island, Great Adventure, Rye Playland, Great Escape or at Six Flags Amusement Park. Little did I realize that many years later, I would be taking a new type of roller coaster ride—this one involving the economy and the practice of real estate law.

For years it appeared as if the real estate market and the practice of real estate law were going up, up and up and the roller coaster would never hit the peak and begin its down run. Little did most of us know what lay ahead in the fall of 2008 when the real estate roller coaster hit the top and started a freefall downward journey.

The past 12 months or so have not exactly been fun for most real estate attorneys. Several months ago, the front page of the *New York Times* Real Estate Section showcased a lead article entitled "DON'T EVEN SAY THE WORDS." The writer of the article went on to indicate that "Real estate, that once sexy topic, is now high on the list of things people don't want to talk about." The writer lamented that "It may be that real estate is more persona non grata than public enemy no. 1."

However, over the last month or so, there have been signs of a possible recovery by the real estate industry, but the signals are still mixed. Recently, *New York Magazine* ran an article entitled "The Downturnaround Is Here." In somewhat tongue-in-cheek fashion, the article contained a number of conflicting headlines:

THE RECOVERY IS AT HAND!

NO, THE RECOVERY IS NOT AT HAND!

THE RECOVERY IS A FAKE!

THERE WILL BE NO RECOVERY!

THE RECOVERY IS ALL IN OUR MINDS!

So where does the present conundrum leave real estate attorneys and how does the present economic climate affect the practice of real estate law?

When I was recently asked by a business publication how the present recession was impacting the practice of real estate law, I told the reporter that the current economic climate has turned out to be an exceedingly mixed bag for real estate attorneys. Developers of both commercial and residential projects are finding it increasingly difficult to secure financing for new construction as well as obtaining refinancing from overly cautious lenders. As a result, very few new development proposals are being presented to planning boards and zoning boards throughout the State of New York. This obviously has a negative impact on real estate attorneys.

Insofar as existing commercial real estate, vacancy rates in office buildings and retail spaces have significantly increased as businesses retrench or go into bankruptcy. As a result, many real estate attorneys are involved in renegotiation of commercial leases, mortgage foreclosures or bankruptcy proceedings. Also, due to the financial downturn, there are considerably fewer residential real estate closings taking place throughout the State of New York.

As we are aware, the issue of subprime mortgages and other variable-rate mortgages has attracted significant attention in the media. Some homeowners, even those with prime mortgages, are losing their jobs and are defaulting on their mortgage payments. As a result, residential foreclosures are on the rise. Both the Federal Government and the State of New York have enacted legislation in order to give additional protection to homeowners from possible foreclosures. The State Bar Association has been responsive to these issues and has run a number of programs around the state for real estate attorneys who need to deal with issues involving the current mortgage crisis. Moreover, the Federal and State legislation which encourages lenders to renegotiate loans with borrowers and gives other legal protections to borrowers has resulted in more legal work for lenders' and borrowers' attorneys as they get involved in loan amendments and workouts.

Unfortunately, the possibility of mortgage foreclosures has also given rise to a number of unscrupulous companies which charge consumers anywhere from $1,000.00 to $5,000.00 to allegedly help distressed homeowners "renegotiate" their existing mortgages. Many of these companies take a significant fee upfront and do little, if any, work on behalf of homeowners. Moreover, some of these companies may well be engaged in the unlawful practice of law.

Although the practice of real estate law has definitely taken a downturn as a result of the events over the past year, there is still business for real estate attorneys as they attempt to counsel commercial and residential owners and tenants through the current financial downturn. However, and unfortunately, there are many real estate practitioners, including many who are members of our Section, whose practices have suffered greatly as a result of the current economic climate.

Although I do not have a crystal ball, it appears that the business of real estate and the practice of real estate law are finally starting to emerge from the 2008/2009 debacle. Hopefully individuals, investors and lenders will realize that both commercial and residential real estate are good solid investments and real estate practitioners in our Section will be the beneficiaries of the anticipated upswing.

To tell you the truth, I never much enjoyed roller coaster rides because of the extreme up and downs. I would much rather go on a steady and straight ride. After the past 12 months, I'm sure many of my fellow Real Property Law Section members would agree.

Joel H. Sachs

The New Federal "Protecting Tenants at Foreclosure Act"

By Dan M. Blumenthal

On May 20, 2009, President Obama signed into law the "Protecting Tenants at Foreclosure Act,"[1] (the "Act") designed to provide protections for tenants whose landlords fall into foreclosure. The new law became effective on signing,[2] but sunsets in December 2012.[3] The substantive provisions of the Act are found in 42 U.S.C.A. § 1437f (West 2009) and in notes to 12 U.S.C.A. § 5220 (West 2009).

The Act covers any dwelling or residential real property "in the case of any foreclosure . . . after the date of enactment."[4] So what properties are covered? Is a property in use as a dwelling in contravention of local building or zoning codes protected? Probably, as the language of the Act appears to use "residential" as a modifier of "rental properties."[5] Is a property covered if the legal use is residential, but it is used in some other manner? Probably not, for the reasons set forth above. However, these issues will need to be resolved by judicial interpretation or amendment.

What foreclosures are subject to the Act? It can be argued that the language "any foreclosure . . . after the date of enactment of this title" imposes the Act on any foreclosure action,[6] residential or commercial, where someone resides in the property, but limits the application of the Act to foreclosures commenced after May 20, 2009.

The Act affects "any immediate successor in interest" to unnamed parties (but presumably the borrowers).[7] At least one line of New York cases holds that the immediate successor in interest to the borrower/homeowner is the court as the typical judgment of foreclosure and sale divests the borrowers of all their "right, title and interest" in the property.[8] Even if it was determined that such an interpretation does violence to the legislative intent of the "Act,"[9] it is a defensible argument that a foreclosure sale bid (with deposit) makes the bidder the legal equivalent of a contract vendee, and "[t]he execution of a contract for the purchase of real estate and the making of a partial payment gives the contract vendee equitable title to the property."[10] If the bidder then assigns his bid, is the assignee no longer the "immediate successor"?

Presuming that the Act intends to bind the grantee of the referee's deed at a court-ordered foreclosure sale, what are the purchaser's obligations, and to whom are they owed?

The purchaser owes a bona fide tenant either recognition of an unexpired lease term or,[11] if no lease is in effect, a notice to vacate of at least 90 days duration.[12] Is this meant to supplant the predicate notice required for New York State summary proceedings[13] or the demand predicate to seeking a writ of assistance?[14] Perhaps the Act can be applied much as a Fair Debt Collection Practices Act ("FDCPA") notice.[15] A proper FDCPA is not a prerequisite to a non-payment proceeding.[16] Essentially, the FDCPA compliance is parallel relief, not part of the foreclosure process. The distinction that may mandate a different application of the notice under this new Act is that the FDCPA is self-contained, with a schedule of fines and penalties.[17] No such penalty provisions are found in this new legislation.

So what interests are entitled to notice under the Act? The holders of bona fide leaseholds, including statutory (month to month) tenancies or tenancies terminable at will are protected provided the leasehold was created "before the notice of foreclosure."[18] As New York has no legal document entitled "Notice of Foreclosure," we are left to speculate as to the equivalent. Is an acceleration letter notice of foreclosure? More likely candidates are either the Notice of Pendency or Summons. By this interpretation, only parties named, or entitled to be named, in the foreclosure are entitled to the additional notice under the "Act." The Secretary of Housing would seem to require that service of notice under the Act must be made after the transfer of title pursuant to foreclosure as the burden of giving the notice is placed on "immediate successors in interest of a residential property, which is being foreclosed."[19]

For a leasehold to be "bona fide" under the Act, the transaction must have been "arms-length,"[20] and for rent "not substantially less than fair market rent" unless reduced or subsidized by a government agency.[21] Tenancies by "the child, spouse, or parent of the mortgagor" are specifically recognized as not being bona fide.[22]

The Act also closes a loophole by which a foreclosure purchaser could terminate a lease under the HUD Housing Voucher program ("Section 8"). Foreclosure purchase is specifically declared not to be "good cause" for termination.[23] However, a foreclosure purchaser may, on 90-day notice, terminate the Housing Assistance Payment ("HAP") contract and tenancy,[24] or any tenancy, for personal use.[25] Where the action foreclosed a "federally related mortgage loan,"[26] the relief afforded by the Act shall be ineffective if "any State or local law [ ] provides longer time periods or other additional protections for tenants."[27]

As can be seen from this analysis, the Act raises many questions that will be only sorted out with application followed by litigation at either the state or federal level. For practitioners, the most cautious route is to amend the 10-day notice for a summary proceeding (or demand for possession prior to moving for a writ of assistance) to 90 days. A defensible middle ground is to send a 90-day notice to any party found in possession after the foreclosure sale, then proceed in the usual fashion with each step alleging that physical removal can occur no earlier than the 91st day from the first notice.

Endnotes

1. Protecting Tenants at Foreclosure Act, Pub. L. No. 111–22, §§ 701–704, 123 Stat. 1632 (2009).
2. *See* § 702(a), 123 Stat. at 1660–61 ("In the case of any foreclosure . . . on any dwelling or residential real property after the date of enactment of this title, any immediate successor in interest in such property pursuant to the foreclosure shall assume such interest subject to [certain rights of the tenant].").
3. § 704, 123 Stat. at 1662 ("This title, and any amendments made by this title are repealed, and the requirements under this title shall terminate, on December 31, 2012.").
4. § 702(a), 123 Stat. at 1660–61.
5. *See* § 702(a), 123 Stat. at 1660 (indicating that the statute applies in any foreclosure "on a federally-related mortgage loan or on any dwelling or *residential* real property") (emphasis added).
6. *See id.* at § 702(a), 123 Stat. at 1660–61.
7. *Id.*
8. *See Green Point Sav. Bank v. Barbagallo*, 247 A.D.2d 442, 443, 668 N.Y.S.2d 678, 679 (2d Dep't 1998) ("Upon entry of the judgment of foreclosure and sale . . . , the mortgagors no longer had any title through which they could convey a leasehold interest." (citing *SRF Builders Capital Corp. v. Ventura*, 224 A.D.2d 678, 639 N.Y.S.2d 59 (2d Dep't 1996))).
9. *See Pultz v. Economakis,* 10 N.Y.3d 542, 547, 890 N.E.2d 880, 882, 860 N.Y.S.2d 765, 767 (2008) ("It is fundamental that a court, in interpreting a statute, should attempt to effectuate the intent of the Legislature." (quoting *State v. Patricia II*., 6 NY.3d 160, 162, 844 N.E.2d 743, 745, 811 N.Y.S.2d 289, 291 (2006))).
10. *Carnavalla v. Ferraro,* 281 A.D.2d 443, 443, 722 N.Y.S.2d 47, 48 (2d Dep't 2001) (finding that a contract vendee holds "an equitable interest in the property derived from the mortgagor" and therefore possesses "a common law right to redeem the mortgage" prior to a foreclosure sale) (citing *Polish Nat'l Alliance of Brooklyn v. White Eagle Hall Co*., 98 A.D.2d 400, 405, 470 N.Y.S.2d 642, 647 (2d Dep't 1983)).
11. Protecting Tenants at Foreclosure Act, Pub. L. No. 111–22, § 702(a)(2)(A), 123 Stat. 1632, 1661 (2009) ("[A]ny immediate successor . . . shall assume such interest subject to—the rights of any bona fide tenant, as of the date of such notice of foreclosure— under any bona fide lease entered into before the notice of foreclosure to occupy the premises until the end of the remaining term of the lease. . . .").
12. § 702(a)(2)(B), 123 Stat. at 1661 ("[A]ny immediate successor . . . shall assume such interest subject to—the rights of any bona fide tenant, as of the date of such notice of foreclosure— without a lease or with a lease terminable at will under state law, subject to the receipt by the tenant of the 90 day notice under subsection (1). . . .").
13. *See* N.Y. Real Prop. Acts. § 713(5) (McKinney 2006) ("The property has been sold in foreclosure and either the deed delivered pursuant to such sale, or a copy of such deed, certified as provided in the civil practice law and rules, has been exhibited to him.").
14. *See Kilpatrick v. Argyle Co*., 199 A.D. 753, 758, 192 N.Y.S. 98, 101 (1st Dep't 1922) ("A writ of assistance is, in ordinary cases, the process for giving possession of land under an adjudication and will be granted upon the sale being confirmed, and proof that the purchaser has received a deed of conveyance from the master, which has been shown to the party in possession accompanied by a demand of possession, which has been refused.").
15. *See* 15 U.S.C. §§ 1692–1692p (2006).
16. *See Dearie v. Hunter*, 183 Misc. 2d 336, 337, 705 N.Y.S.2d 519, 520 (Sup. Ct. App. T. 1st Dep't 2000) (citing *Wilson Han Ass'n v. Arthur,* 27 HCR 374A, N.Y. L.J., July 6, 1999, at 29, col. 4 (Sup. Ct. App. T. 2d Dep't)); *Barstow Rd. Owners, Inc. v. Billing,* 179 Misc. 2d 958, 966–67, 687 N.Y.S.2d 845, 852 (Dist. Ct. Nassau County 1998) ("[T]he FDCPA does not provide for or compel dismissal of state court special proceedings commenced by landlords because of alleged unauthorized 'debt collection' practices. . . .").
17. *See* 15 U.S.C. § 1692k(a) (2006) (explaining what civil liability a debt collector is subject to for failing to comply with the statute).
18. Protecting Tenants at Foreclosure Act, Pub. L. No. 111–22, § 702(a)(2)(A), 123 Stat. 1632, 1661 (2009) ("[A]ny immediate successor . . . shall assume such interest subject to . . . the rights of a bona fide tenant, as of the date of such notice of foreclosure . . . under any bona fide lease entered *before the notice of foreclosure*.") (emphasis added).
19. Protecting Tenants at Foreclosure: Notice of Responsibilities Placed on Immediate Successors in Interest Pursuant to Foreclosure of Residential Property, 74 Fed. Reg. 30106 (June 24, 2009) (noting that the notice is intended to alert HUD program participants of the obligation "imposed on immediate successors of interest in any residential property pursuant to foreclosure" to provide tenants "with at least 90 days' advance notice of the need to vacate").
20. Protecting Tenants at Foreclosure Act, Pub. L. No. 111–22, § 702(b)(2), 123 Stat. at 1661 (stating that for a lease or tenancy to be considered "bona fide" it must have been the "result of an arms–length transaction").
21. § 702(b)(3), 123 Stat. at 1661 (indicating that for a lease or tenancy to be considered "bona fide" it "requires the receipt of rent that is not substantially less than fair market rent or the unit's rent is reduced or subsidized due to a [government] subsidy").
22. § 702(b)(1), 123 Stat. at 1661 (exempting from "bona fide" tenancies those tenancies held by the "mortgagor or the child, spouse, or parent of the mortgagor").
23. § 703(1), 123 Stat. at 1661; *see also* 42 U.S.C.A. § 1437f(o)(7)(C) (West 2009) ("Each housing assistance payment contract entered into by the public housing agency and the owner of a dwelling unit . . . shall provide that during the term of the lease, the owner shall not terminate the tenancy except . . . for other good cause. . . .").
24. *See* Protecting Tenants at Foreclosure Act, Pub. L. No. 111–22, § 703(1), 123 Stat. 1632, 1661 (2009) ("[An] owner may terminate the tenancy effective on the date of transfer of the unit to the owner if the owner—will occupy the unit as a primary residence and has provided the tenant a notice to vacate at least 90 days before the effective date of such notice.").
25. *Id.*
26. 12 U.S.C. § 2602(1) (2006) (defining a federally related mortgage loan).
27. Protecting Tenants at Foreclosure Act, Pub. L. No. 111–22, § 702(a)(2), 123 Stat. at 1661–62 ("[A]ny immediate successor . . . shall assume such interest subject to . . . the rights of any bona fide tenant, as of the date of such notice of foreclosure . . . without a lease or with a lease terminable at will under state law."); *see also* 42 U.S.C. § 1437f(o)(7)(F) (2009) (providing that the statute shall not upset any state or local law that grants tenants with additional protections).

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Excluding High-Cost and Subprime Home Loans from Title Insurance Coverage

By Christopher W. Burdick

As the New York Real Estate Bar knows all too well, the meltdown in the financial markets has had far-reaching consequences, including changes in the legal framework for lenders and title insurers. Areas that New York's legislators targeted have included subprime lending practices deemed to be abusive. The title insurance industry responded with changes in certain endorsements to the loan policy to make it clear that coverage does not extend to lack of compliance with such consumer protection provisions. This article briefly outlines the relevant sections of New York Banking Law, the rationale behind the title industry response, the changes in title insurance coverage, and whether further changes may be appropriate.

I. New York Banking Law §§ 6–*l* (High-Cost Home Loans) and 6–m (Subprime Home Loans)

In June 2008, the New York State Legislature acted to amend section 6–*l* and adopt a new section 6–m to the Banking Law.[1] The Governor's August 5, 2008 press release, issued with his signing of the legislation, stated that the new law is intended to address the "foreclosure crisis" with the Banking Law changes aimed at "attacking flaws in New York's banking regulations to prevent such a crisis from happening again."[2]

a. Section 6–*l* (High-Cost Home Loans)

Banking Law § 6–*l* first was enacted in 2002 as an anti-predatory lending law regulating home loans exceeding certain specified thresholds,[3] including excessively high interest rates, points, and fees.[4] Together with additional provisions added under the 2008 law, the law imposes a wide array of limitations and prohibited practices on high-cost home loans: "[n]o call provisions,"[5] "[n]o balloon payments,"[6] "[n]o negative amortization,"[7] no post default increased interest rate,[8] limitation on advance monthly payments paid out of loan proceeds,[9] limitation on modification or deferral fees,[10] "[n]o oppressive mandatory arbitration clauses,"[11] "[n]o financing of insurance or other products sold in connection with the loan,"[12] "[n]o 'loan flipping,'"[13] "[n]o refinancing of special mortgages,"[14] "[n]o lending without due regard to repayment ability,"[15] "[n]o lending without counseling disclosure and list of counselors,"[16] limitation on financing of points and fees,[17] "[r]estrictions on home improvement contracts,"[18] "[n]o encouragement of default,"[19] "[p]rohibited payments to mortgage brokers,"[20] "[n]o points and fees when a lender refinances its own high-cost home loan with a new high-cost home loan,"[21] "[n]o prepayment penalties,"[22] "[n]o abusive yield spread premiums,"[23] "[m]andatory escrow of taxes and insurance,"[24] "[m]andatory disclosure of taxes and insurance payments,"[25] and "[n]o teaser rates" with a duration of six months or less.[26]

Remedies for violation of such limitations and prohibitions may be sought through enforcement rights vested in the superintendent of the Department of Banking and the Attorney General[27] as well as through private actions.[28] Any person found by a preponderance of the evidence to have violated the law shall be liable to the borrower for, among other things, actual damages (including consequential and incidental damages);[29] statutory damages;[30] court-awarded reasonable attorneys' fees;[31] injunctive, declarative and such other equitable relief as the court deems appropriate;[32] voiding of the loan by the court upon a finding of intentional violation,[33] and rescission.[34] The aforementioned remedies are not intended to be exclusive,[35] and the borrower may assert claims in recoupment and defenses to payment against the original lender and any assignee.[36]

"[T]he meltdown in the financial markets has had far-reaching consequences, including changes in the legal framework for lenders and title insurers."

b. Section 6–m (Subprime Home Loans)

Before launching into the summary of this new section of the Banking Law, it may be useful to explain that the term "subprime," in common parlance, refers to the lender's evaluation of the creditworthiness of the borrower. The term gained currency during the 2007 credit crunch and refers to a borrower who does not meet the lender's highest underwriting standards. The term also refers to a security (e.g., a pool of subprime mortgage loans) with a subprime rating, also known as "C paper." The rate, points, and other loan costs that a lender charges to subprime borrowers were higher than to prime borrowers, corresponding to the higher risk that the lender believed it was undertaking. As the subprime lending market developed, regulators and legislators came to believe that many of the lenders were offering loans whose terms could trap borrowers, particularly low-income borrowers, into loans which they could not repay. The legislative response reflects the state government's belief that the lenders themselves bear significant, if not primary, responsibility for the problem and that their lending practices should be further regulated.[37]

Section 6–m establishes prohibitions and limitations effective September 1, 2008 on "subprime home loans," the definition of which is based upon the extent to which its fully indexed annual percentage rate exceeds certain benchmark rates, but excludes home equity lines of credit, loans for initial construction of a dwelling, and temporary or "bridge loans" with a term of 12 months or less.[38] The Superintendent of Banking has the authority to set different thresholds in certain instances.[39] The prohibitions and limitations generally parallel those contained in section 6–*l*.[40] Though the remedies differ somewhat, the borrower and state authorities are provided ample tools to attack and overturn a subprime loan violating the law.

The lender (or mortgage broker) is required to determine the borrower's ability to repay and may not extend a subprime home loan absent such determination.[41] As under section 6–*l*, the Superintendent of the Department of Banking or the Attorney General may enforce section 6–m.[42] Any person found by a preponderance of the evidence to have violated the law shall be liable to the borrower for actual damages,[43] court-awarded reasonable attorneys' fees,[44] and injunctive, declaratory, and such other equitable relief as the court deems appropriate.[45] The aforementioned remedies are not intended to be exclusive,[46] and a borrower in default more than 60 days or in foreclosure may assert violation of the law as a defense.[47]

II. Title Industry Response

A cursory reading of these sections of the Banking Law clearly points to the fact that the title insurance industry cannot and should not extend coverage to loans that do not comply with such laws. Further, it would not be reasonable to expect that underwriters can determine whether the practices of the lenders, so much of which occurs outside the four corners of the loan documents, violate such laws. Given the inclusion of rescission in the remedies under these Banking Law provisions, a title insurer could face a complete failure of title, resulting in the need to pay the entire policy amount to the insured lender.

Accordingly, the 2008 law prompted the New York title insurance industry through its statutorily recognized Title Insurance Rate Service Association ("TIRSA") to take action consistent with the new law.[48] On October 21, 2008, TIRSA submitted to the New York State Insurance Department proposed changes to (1) the Standard New York Loan Endorsement (Loan Policy), (2) the Fannie Mae Balloon Mortgage Endorsement, (3) the Variable Rate Mortgage Endorsement, (4) the Variable Rate Mortgage Endorsement (Fixed Rate) and (5) the Variable Rate Mortgage Endorsement (Negative Amortization).[49]

In its transmittal letter to the Insurance Department, TIRSA explained that these sections of the Banking Law, as amended by the 2008 law, impose penalties on lenders who violate them, and the title insurance policy does not cover such violations:

> Since these violations are caused by a lender's failure to comply with the Banking Law, there is no insurance coverage under the Loan Policy.[50] However, to avoid any uncertainty as to the scope of the policy coverage, it is believed that this exclusion [the new Exclusion Number 8] is necessary to make this abundantly clear.[51]

III. Changes in Endorsements

As to the Standard New York Loan Endorsement, which invariably is appended to every loan policy issued in New York, TIRSA proposed a new "Exclusion From Coverage Numbered 8" to the pre-printed exclusions from the coverage set out in the loan policy jacket.[52] The new exclusion reads: "Any consumer protection law including, without limitation, New York Banking Law sections 6–*l* ('High-Cost Loans') and 6–m ('Subprime Home Loans'), relating to a mortgage on land improved or to be improved by a structure intended principally for occupancy by one-to-four families."[53]

Each of the other four endorsements contains a simple conforming change consisting of the addition of a clause to the last "subject to" paragraph in each such endorsement, "including without limitation Section 8 of the Exclusions From Coverage, as added by the Standard New York Endorsement (Loan Policy)."[54] The purpose of adding the clause is to make it clear that the endorsement is not intended to upend the new exclusion.

The Insurance Department approved the changes effective December 1, 2008.[55] Both the revised Standard New York Endorsement (Loan Policy) and, as an example of the other four revised endorsements, the Variable Rate Endorsement (Negative Amortization) are at the foot of this article, each marked against its respective predecessor.

IV. Further Changes May Be Appropriate

While in this writer's opinion as a title insurance attorney, the title industry response is appropriate and consistent with the new law, it also should be noted that attorneys in and familiar with the title industry note that such response may be incomplete and expose the industry to unaddressed risks.[56] Just as the loan policy now excludes coverage to a lender violating the provisions in the Banking Law discussed above, similarly, the owner's policy may need to exclude coverage to an owner who acquires title through foreclosure of a high-cost or subprime loan. The exclusions in the owner's policy differ from those in the loan policy and are unlikely to spare the title insurer from covering such abuses.[57] An exclusion added to the Standard New York Endorsement (Owner's Policy) may be appropriate. Further, it would be imprudent for the title industry to be exposed to potential significant losses resulting from lack of compliance with these new provisions of the Banking Law regardless of whether it is under a loan policy or an owner's policy.

To remain competitive, but at the same time, financially sound, title insurers must balance evolving coverage needs of their customers against taking on undue risk. Over the years, there has been a decline in the risks that the title industry insures as they relate to usury, truth-in-lending and other consumer protection laws.[58] This decline corresponds to an increase in enforcement of, and prohibitions and limitations contained in, such laws.[59] Like any other financial or insurance product, title insurance must adapt quickly to the changing business and regulatory landscape without losing its core value in the marketplace.

Endnotes

1. N.Y. Banking Law §§ 6–*l* to 6–m (McKinney Supp. 2009). *See generally* Kirsten Keefe & Elizabeth Hasper, *New State Law Addresses Mortgage Foreclosure Crisis and Subprime Lending Abuses*, Legal Servs. J. (Empire Justice Center, Albany, NY) Aug. 1, 2008, *available at* http://www.empirejustice.org/issue-areas/consumer-community-development/subprime-mortgage-lending/state-legislature-addresses.html?print=t (summarizing the Foreclosure Prevention and Responsible Lending Act).
2. Press Release, Office of Governor David A. Paterson, Governor Paterson Signs Comprehensive Reforms to Address Foreclosure Crisis (Aug. 5, 2008) (on file with author), *available at* www.ny.gov/governor/press/press_0805081.html ("The new law will immediately help protect people from losing their homes and mandates reforms to help avoid a similar crisis in the future. The bill also takes into consideration the importance of striking the right balance between consumer protection and the availability of affordable credit.").
3. *See* N.Y. Banking Law § 6–*l* (McKinney Supp. 2009) (defining a high–cost home loan, providing the limitations placed upon terms of such loans, and prohibiting certain solicitation practices in regard to such loans).
4. *Id.* at § 6–*l*(1)(g)(ii) (indicating upper limit of points and fees for valid "high-cost home loan").
5. *Id.* at § 6–*l*(2)(a) ("No high-cost home loan may contain a provision that permits the lender, in its sole discretion, to accelerate the indebtedness. This provision does not prohibit acceleration of the loan in good faith due to the borrower's failure to abide by the material terms of the loan.").
6. *Id.* at § 6–*l*(2)(b) ("No high-cost home loan may contain a scheduled payment that is more than twice as large as the average of earlier scheduled payments, unless such balloon payment becomes due and payable at least fifteen years after the loan's origination.").
7. *Id.* at § 6–*l*(2)(c) ("No high–cost home loan may contain a payment schedule with regular periodic payments that cause the principal balance to increase.").
8. *Id.* at § 6–*l*(2)(d) ("No high–cost home loan may contain a provision which increases the interest rate after default.").
9. *Id.* at § 6–*l*(2)(e) ("No high–cost home loan may include terms under which more than two periodic payments required under the loan are consolidated and paid in advance from the loan proceeds provided to the borrower.").
10. *Id.* at § 6–*l*(2)(f) ("A lender may not charge a borrower any fees to modify, renew, extend, or amend a high–cost home loan or to defer any payment due under the terms of a high–cost home loan if, after modification, renewal, extension or amendment, the loan is still a high-cost loan or, if no longer a high-cost home loan, the annual percentage rate has not been decreased by at least two percentage points.").
11. *Id.* at § 6–*l*(2)(g) ("No high–cost home loan may be subject to a mandatory arbitration clause that is oppressive, unfair, unconscionable, or substantially in derogation of the rights of consumers.").
12. *Id.* at § 6–*l*(2)(h) ("No high–cost home loan shall finance, directly or indirectly, any credit life, credit disability, credit unemployment, or credit property insurance, or any other life or health insurance premiums, or any payments directly or indirectly for any debt cancellation or suspension agreement or contract or any product or service that is not necessary or related to the high-cost home loan. . . .").
13. *Id.* at § 6–*l*(2)(i) ("No lender or mortgage broker making or arranging a high-cost home loan may engage in the unfair act or practice of 'loan flipping.'").
14. *Id.* at § 6–*l*(2)(j) ("No lender or mortgage broker making or arranging a high-cost home loan may refinance an existing home loan that is a special mortgage originated, subsidized or guaranteed by or through a state, tribal or local government, or nonprofit organization. . . .").
15. *Id.* at § 6–*l*(2)(k) ("A lender or mortgage broker shall not make or arrange a high–cost home loan without due regard to repayment ability, based upon consideration of the resident borrower or borrowers' current and expected income, current obligations, employment status, and other financial resources. . . .").
16. *Id.* at § 6–*l*(2)(l) (mandating lenders to provide borrowers upon application a required notice encouraging borrowers to seek financial counseling prior to signing loan documents).
17. *Id.* at § 6–*l*(2)(m) (explaining that when making a high–cost home loan, a lender may not, directly or indirectly, finance points and fees greater than three percent of the principal loan amount).
18. *Id.* at § 6–*l*(2)(n) ("A lender shall not pay a contractor under a home improvement contract from the proceeds of a high–cost loan. . . .").
19. *Id.* at § 6–*l*(2)(o) ("In making or arranging a high-cost home loan, a lender or mortgage broker shall not recommend or encourage default on an existing loan or other debt prior to and in connection with the closing or planned closing of a high-cost home loan that refinances all or any portion of such existing loan or debt.").
20. *Id.* at § 6–*l*(2)(p) ("[N]o lender or mortgage broker shall accept or give any fee, kickback, thing of value, portion, split or percentage of charges, other than as payment for goods or facilities that were actually furnished or services that were actually performed.").
21. *Id.* at § 6–*l*(2)(q) ("A lender shall not charge a borrower points and fees in connection with a high–cost home loan if the proceeds of the high–cost home loan are used to refinance an existing high–cost loan held by the lender or an affiliate of the lender.").
22. *Id.* at § 6–*l*(2)(r) ("No prepayment penalties or fees shall be charged or collected on a high-cost home loan. A prepayment penalty in a high-cost home loan shall be unenforceable.").
23. *Id.* at § 6–*l*(2)(s) ("[T]he mortgage broker shall, at the time of application, disclose the exact amount and methodology of total compensation that the broker will receive.").
24. *Id.* at § 6–*l*(2)(t) (explaining that, with certain exceptions, a lender under a high–cost home loan made after July 1, 2010 is required to collect monthly

escrows for property taxes and hazard insurance, provided that a borrower may waive the escrow requirements after one year).

25. *Id.* at § 6–*l*(2)(u) ("[T]he lender or mortgage broker shall inform the borrower that an additional amount will be due for taxes and insurance and shall disclose to the borrower as soon as reasonably possible the approximate amount of the initial periodic payment for property taxes and hazard insurance.").

26. *Id.* at § 6–*l*(2)(v) ("No lender or mortgage broker shall make or arrange a high–cost home loan which has an initial or introductory rate with a duration of less than six months.").

27. *Id.* at § 6–*l*(5) ("The attorney general, the superintendent, or any party to a high–cost home loan may enforce the provisions of this section.").

28. *Id.*

29. *Id.* at § 6–*l*(7)(a) ("Any person found by a preponderance of the evidence to have violated this section shall be liable to the borrower for . . . actual damages, including consequential and incidental damages.").

30. *Id.* at § 6–*l*(7)(b) ("Any person found by a preponderance of the evidence to have violated this section shall be liable to the borrower for . . . statutory damages. . . .").

31. *Id.* at § 6–*l*(8) ("A court may also award reasonable attorneys' fees to a prevailing borrower.").

32. *Id.* at § 6–*l*(9) ("A borrower may be granted injunctive, declaratory and such other equitable relief as the court deems appropriate in an action to enforce compliance with this section.").

33. *Id.* at § 6–*l*(10) ("Upon a finding . . . of an intentional violation by the lender . . . , the home loan agreement shall be rendered void. . . .").

34. *Id.* at § 6–*l*(11) ("Upon a judicial finding that a high–cost home loan violates any provision of this section, whether such violation is raised as an affirmative claim or as a defense, the loan transaction may be rescinded.").

35. *Id.* at § 6–*l*(12) ("The remedies provided in this section are not intended to be the exclusive remedies available to a borrower of a high–cost home loan.").

36. *Id.* at § 6–*l*(13) ("In any action by an assignee to enforce a loan against a borrower in default more than sixty days or in foreclosure, a borrower may assert any claims in recoupment and defenses to payment under the provisions of this section and with respect to the loan . . . that the borrower could assert against the original lender of the loan.").

37. *Cf.* Sandra Phillips, *Reducing Home Mortgage Foreclosures in a Predatory Lending Environment: A Case Study of a Mid–Sized City in Central New York,* 36 FORDHAM URB. L.J. 489, 504 (2009) (noting federal government's response to "the devastation caused by subprime lending" included the passage of the "Housing and Economic Recovery Act of 2008").

38. N.Y. BANKING LAW § 6–m(1)(c) (McKinney Supp. 2009) ("A subprime home loan excludes a transaction to finance the initial construction of a dwelling, a temporary or "bridge" loan with a term of twelve months or less . . . , or a home equity line of credit.").

39. *Id.* at § 6–m(1)(ii) ("[T]he superintendent may from time to time designate such other threshold rates as may be necessary to achieve parity between . . . nationally chartered institutions and banking organizations, mortgage banks and mortgage brokers in this state or to alleviate such unduly negative effects.").

40. *Compare* N.Y. BANKING LAW § 6–m(2) (McKinney Supp. 2009), *with* N.Y. Banking Law § 6-l(2) (McKinney Supp. 2009) (defining similar restrictions upon the terms of subprime home loans and proscribing similar solicitation practices).

41. N.Y. BANKING LAW § 6–m(4) (McKinney Supp. 2009) ("No lender or mortgage broker shall make or arrange a subprime home loan unless the lender or mortgage broker reasonably and in good faith believes at the time the loan is consummated that [the borrowers] ha[ve] the ability to repay the loan according to its terms.").

42. *Id.* at § 6–m(8) ("The attorney general or the superintendent may enforce the provisions of this section.").

43. *Id.* at § 6–m(9) ("Any person found by a preponderance of the evidence to have violated this section shall be liable to the borrower of a subprime home loan for actual damages.").

44. *Id.* at § 6–m(10) ("A court may also award reasonable attorneys' fees to a prevailing borrower in a foreclosure action.").

45. *Id.* at § 6–m(11) ("A borrower may be granted injunctive, declaratory and such other equitable relief as the court deems appropriate in an action to enforce compliance with this section.").

46. *Id.* at § 6–m(12) ("The remedies provided in this section are not intended to be the exclusive remedies available to a borrower of a subprime home loan.").

47. *Id.* at § 6–m(13) ("In any action by a lender or assignee to enforce a loan against a borrower in default more than sixty days or in foreclosure, a borrower may assert as a defense, any violation of this section.").

48. *See* Michael J. Berey, First American Title Insurance Company of New York, Underwriting Bulletin No. 53–2008: Revised TIRSA Endorsements: Subprime & High–Cost Home Loans (Nov. 18, 2008), http://www.advantagetitle.com/news-and-updates/underwriter-pdf/fa_53-2008.pdf (describing TIRSA's response to amendment of N.Y. BANKING LAW § 6–*l* and passage of N.Y. BANKING LAW § 6–m).

49. *See* Berey, *supra* note 48, at 1.

50. Letter from Title Insurance Rate Service Association to the New York State Insurance Department (Oct. 2008) (on file with author).

51. *Id.*

52. Berey, *supra* note 48, at 1 ("The Standard New York Endorsement (Loan Policy) has been amended to add new Exclusion From Coverage numbered 8. . . .").

53. *See id.*

54. *See id.*

55. *See id.* at 2.

56. *See, e.g.*, Melvyn Mitzner, Senior Counsel, Keane & Beane, P.C., Title Insurance Industry Response to Subprime Crisis at the New York State Bar Association Annual Meeting (Jan. 29, 2009) (transcript available from New York State Bar Association).

57. *See* Berey, *supra* note 48.

58. *Cf.* Dennis R. Casale & Travis P. Nelson, The Decline of the Subprime Mortgage Market, PRINCETON UPDATE (Pepper Hamilton LLP 4th Quarter 2007), *available at* http://www.pepperlaw.com/pdfs/PrincetonQ42007.pdf (predicting similar trends based on increased governmental regulations).

59. *See id.* at 4 ("[W]hat is likely to result is a correction on the part of legislators, regulators, the courts, and the marketplace to make the subprime mortgage lending environment more transparent and more informed.").

Christopher W. Burdick is Senior Vice President and Underwriting Counsel of Stewart Title Insurance Company.

BLANK TITLE INSURANCE COMPANY

STANDARD NEW YORK ENDORSEMENT

(Loan Policy)

1. Exclusion Number 7 is deleted, and the following is substituted:

   7. Any lien on the Title for real estate taxes, assessments, water charges or sewer rents imposed by governmental authority and created or attaching between Date of Policy and the date of recording of the Insured Mortgage in the Public Records. This Exclusion does not modify or limit the coverage provided under Covered Risk 11(b).

2. Exclusions From Coverage is amended by adding a new Exclusion Number 8:

   8. Any consumer protection law including, without limitation, New York Banking Law Sections 6-l ("High-Cost Loans") and 6-m ("Subprime Home Loans"), relating to a mortgage on Land improved or to be improved by a structure or structures principally for occupancy by one-to-four families.

This endorsement is issued as part of the policy. Except as it expressly states, it does not (i) modify any of the terms and provisions of the policy, (ii) modify any prior endorsements, (iii) extend the Date of Policy, or (iv) increase the Amount of Insurance. To the extent a provision of the policy or a previous endorsement is inconsistent with an express provision of this endorsement, this endorsement controls. Otherwise, this endorsement is subject to all of the terms and provisions of the policy and of any prior endorsements.

DATE: **BLANK TITLE INSURANCE COMPANY**

By:

BLANK TITLE INSURANCE COMPANY

VARIABLE RATE MORTGAGE ENDORSEMENT NEGATIVE AMORTIZATION

—NEW YORK—

Attached to and made a part of Policy Number ____

The Company insures the owner of the indebtedness secured by the insured mortgage against loss or damage sustained by reason of:

1. The invalidity or unenforceability of the lien of the insured mortgage resulting from the provisions therein which provide for: (a) changes in the rate of interest; or (b) the addition of unpaid interest to the principal balance of the loan.

2. Loss of priority of the lien of the insured mortgage as security for the principal balance of the loan, including any unpaid interest which was added to principal in accordance with the provisions of the insured mortgage, which loss of priority is caused by (a) changes in the rate of interest; (b) increases in the unpaid principal balance of the loan resulting from the addition of unpaid interest.

"Changes in the rate of Interest," as used in this endorsement, shall mean only those changes in the rate of interest calculated pursuant to the formula provided in the insured mortgage at Date of Policy.

This endorsement does not insure against loss or damage based upon (a) usury, or (b) any consumer credit protection or truth-in-lending law.

This endorsement is made a part of the policy and is subject to all of the terms and provisions thereof, including, without limitation, Section 8 of the Exclusions From Coverage, as added by the Standard New York Endorsement (Loan Policy), and of any prior endorsement thereto, except that the insurance afforded by this endorsement is not subject to Section 3(d) of the Exclusions From Coverage. Except to the extent expressly stated, it neither modifies any of the terms and provisions of the policy and any prior endorsements, nor does it extend the Date of Policy and any prior endorsements, nor does it increase the Amount of Insurance.

DATE: **BLANK TITLE INSURANCE COMPANY**

By:

Update on Marketable Title in New York

By Marvin N. Bagwell

"These are the times that try men's souls."

—Thomas Paine, "The Crisis,"
December 23, 1776

People employed in the title industry, at least those of us still remaining, know what Thomas Paine must have felt. With the bankruptcy of LandAmerica, the holding company of Commonwealth and Lawyer's Title, two of the largest and most prominent title underwriters, the subsequent acquisition of both by Fidelity, questions raised by the bar regarding the solvency of the other major and minor title underwriters, massive layoffs by underwriters and agents alike of many individuals who were long employed in the industry, the retirement of several of the industry's leading lights, and the paucity of new real estate transactions requiring title insurance, it is a wonder that title people even bother to get up in the morning. However, two-and-a-half centuries after the Founding Fathers endured their time in the wilderness, those of us still treading water look to another patron saint, Gloria Gaynor, for words to inspire us while we are bailing water: "I will survive!"—Hopefully.

When in survival mode, we tend to cast aside that which is secondary and would weigh us down. When one is hoarding every nickel and dime to pay the mortgage, the number of angels dancing on the head of a pin loses its relevance. But the wheels of justice move on. The courts continue to issue decisions that have relevance for the title industry. The following is an attempt to gather some of those cases in one place, so that when normalcy returns, we can once again have heated debates over commas, semicolons and how the courts could have gotten "it" that wrong. Just pretend we have selected "Potpourri" on *Jeopardy* and Alex Trebek tells us that all the correct answers begin with the letter "M." This "M" is for Marketability of title.

In 2007 and 2008, everyone in the New York title industry was so busy that few noticed that the courts issued three opinions on marketability of title, two of which involved successful bidders out-of-foreclosures sales motioning the courts to set aside their purchase contracts, and one of which involved a street widening setback line. Exceptions to title raised in title reports were at issue in these cases as well. Despite the similarities in the foreclosure cases, the courts reached diametrically opposite holdings. All three cases arose because a title company raised an exception to title over which the title company refused to insure or "omit." That fact, in and of itself, makes the cases notable.

". . . it is a wonder that title people even bother to get up in the morning."

In the first case, *R.J. Alan Co. v. Fusco*,[1] Jacob Selechnik, Jason Joseph and Louis Zazzarino were the eventual successful bidders for property foreclosed upon by R.J. Alan Co.[2] The bidders deposited $121,000 with the referee to secure their purchase. Subsequently, the bidders brought suit to set aside the contract because the title company raised three exceptions to title: (1) the adequacy of the notice of sale; (2) a gap in the time between the recording of the first and second notices of pendency; and (3) the legal sufficiency of the service of papers on all parties to the foreclosure action. The bidders argued that foregoing exceptions raised by the title company rendered title unmarketable. In the context of this analysis, the basis for the title exceptions is not all that relevant. In any event, after reviewing the allegations, the court held that the location of sale and the advertising methods used by the foreclosing party complied with the statutes, that no liens were recorded within the gap in time between the two notices of pendency (no foul, no harm), and, finally, that the bidders failed to demonstrate in what way the alleged lack of legal sufficiency impaired the marketability of title. The court held title to be marketable despite the exceptions raised by the title company in its title report. Hence, the bidders lost their attempt to void their contract of purchase. The court gave the bidders 30 days to close title or they would forfeit their deposit.[3]

In the second case, *NYCTL 1998-1 Trust v. Mayfield*,[4] NYCTL, a trust that held New York City tax liens ("Trust"), sold 1105 Dumont Avenue in Brooklyn at foreclosure sale to ZZ Management LLC ("ZZ").[5] ZZ bid $310,000 for the property and deposited $37,000 with the referee. ZZ then assigned its bid to Brooklyn Organization LLC ("Brooklyn"). Brooklyn ordered a title report which revealed that the deed from The City of New York (the "City") to the foreclosed borrower contained a reverter clause. The clause provided that if the borrower, the defendant Mary Mayfield, failed to renovate the property and to pay for the property's upkeep, then "at the option of the City title to the Disposition Area shall revert to and revest in the City."[6] Two title companies declined to issue a title policy free of an exception to title for the reverter. Further, the City declined the bidders' request to release the reverter from the property. Brooklyn brought suit to set aside the foreclosure sale and for the return of its deposit. The Trust argued that the terms of sale provided that the property was being sold subject to all covenants and restrictions of record and that since the reverter was a matter of public record, ZZ and Brooklyn could have discovered the reverter before they bid. In effect, the Trust's position was that the bidders were bound by the terms and conditions of their contract.[7]

The court found that "as a general rule, a purchaser . . . [out of] foreclosure . . . is entitled to . . . good, marketable title."[8] Ergo, Brooklyn should win. Then, the court spent a great deal of time in its opinion explaining why Brooklyn should lose. After all, Brooklyn executed the contract, and it could have discovered the right of reverter before bidding on the property. Then the court explained that, even though it lacked the power to toss the contract, even under the contract, Brooklyn should prevail because the Trust's inability to provide title insurance as specifically required by one paragraph in the contract overrode the bidder's general obligation to accept title subject to covenants and restrictions of record. Finally, the whipsawing came to an end when the court noted that courts have previously held that the City's right of reverter rendered title unmarketable.[9] Finally, the court held that because the Trust was unable to convey marketable title or to provide title insurance to insure over the reverter, the Trust was in violation of the terms of sale itself. The court vacated the foreclosure sale and directed the Trust to return the deposit to Brooklyn.[10] Whew!

The third case also involved an interest in the subject property held by the City of New York. In *Rasul v. O'Brien,*[11] Rasul entered into a contract to purchase 660 Targee Street on Staten Island from O'Brien for $285,000.[12] To bind the contract, Rasul deposited $10,000 into escrow. Rasul then ordered a title report, which revealed that a 30-foot setback line affected the property along its entire street frontage. Although the court indicated that no definitive evidence had been presented to it to show when the setback line was established, it was clear that the line had been established by New York City for purposes of possible street widening. The survey showed that if the City chose to widen the street, the new street would run through about 15 feet of the structure for its entire length. Based on this encumbrance to title, Rasul sought to cancel the contract on the grounds that the property's title was "uninsurable and unmarketable."[13] He demanded the return of his deposit. O'Brien countered that he could produce a title company willing to insure the sale and refused to return the deposit.[14]

According to the court, the general rule in cases such as this is that if the City decided to widen the street, it would compensate Rasul through a condemnation proceeding. However, Rasul said that if the premises were damaged by fire, the City might not permit him to rebuild. The court responded that he could apply for a variance. This was not the end of the story for Rasul. The court said further that "[c]ase law indicates that the restrictive use imposed by [the City Code] would not render title unmarketable unless a substantial portion of the property lies within the bed of the street and the property would be rendered useless thereby."[15] The court held that Rasul was entitled to cancel the contract and it ordered O'Brien to return Rasul's deposit:

> Under the definition of "marketable title" it is apparent that the setback line renders this title unmarketable. No reasonably intelligent person would want to purchase a home with the potential legal problems this premise has, resulting from the existence of the setback line. . . . Clearly the fact that 30 feet of a 46 foot wide lot would be lost should the City widen the street renders the property useless.[16]

Although the holdings appear to be all over the lot, all of the holdings, within the classic interpretation of the law of marketability of title, are correct.

Classical jurisprudence in New York regarding which defects render title marketable or unmarketable rests upon three often-quoted holdings. The first leg of the tripod is *Norwegian Evangelical Free Church v. Milhauser*,[17] where the sainted Justice Cardozo wrote, "The law assures to a buyer a title free from reasonable doubt, but not from every doubt."[18] A decade-and-a-half later, the First Department, in the case of *Whittier Estates v. Manhattan Savings Bank*,[19] established the second leg when it wrote, "[t]he test of [marketability] is not the hazard of possible litigation, for, as has been pointed out, 'it seems to be the inalienable right of any person to start a lawsuit'. . . . The test is rather the chance of successful attack."[20] Finally, at a time which most of us can still remember, the third and final leg steadied the doctrine when the court wrote in *Voorheesville Rod & Gun Club, Inc. v. E. W. Tomkins Co.*,[21]

> A marketable title is "a title free from reasonable doubt, but not from every doubt."[22] We have said that a "purchaser ought not to be compelled to take property, the possession or title of which he may be obliged to defend by litigation. He should have a title which will enable him to hold his land free from probable claim by another, and one which, if he wishes to sell, would be reasonably free from any doubt which would interfere with its market value."[23]

Read together, the foregoing three cases force any counsel contemplating an action asserting that title is unmarketable to ask her or himself two questions. Given my fact situation, once my client acquires title, will a third party bring an action to set aside my client's title? If the likely answer to this first question is "Yes," then counsel must ask, "Will the action to set aside my client's title be successful?" If the answer to the second question is "No," then title is marketable. Those of you who were quick to raise your hands in first year property class already see a problem here, but please keep reading.

In regard to the first case that we considered above, *R.J. Alan Co. v. Fusco*, it was quite obvious to the court that the exceptions to title raised by the purchasers-out-of the foreclosure action would not lead to a divesture of title.[24] The notice of sale was statutorily correct, no liens arose in the gap period between the filings of the notices of pendency, and the purchaser failed to identify any deficiency in the service of papers upon the parties sufficient for the court to opine upon whether such deficiency adversely affected marketability. Since there was no possibility that the title would be subjected to successful litigation, title was marketable. The narrative was different in the second case, *NYCTL 1998-1 Trust v. Mayfield*.[25] There, because the City had declined to release its right of reverter, it was patently obvious that had the purchaser taken title, it would be subject to litigation. Second, the litigation would have been successful because other courts had already held that a reverter in favor of the City of New York rendered title unmarketable. Hence, though it tried mightily to bind the purchaser to its contract, when that failed, the court had little choice but to find that the title indeed was unmarketable. The third case, *Rasul v. O'Brien*, follows the same pattern.[26] The court found it obvious that had he taken title, Rasul might have found himself facing litigation from the City in the form of a condemnation action or even having to file for a variance. However, it should be noted that the court in *O.W. Siebert Co. v. Kramer* reached a different conclusion by holding that a title was marketable because the five feet easement did not render "the property unusable in part or in whole."[27]

Here is the catch. There is a bit of circular reasoning, a catch-22 if you will, involved in this analysis. The courts have ruled that a title must be subject to successful litigation if the title is to be determined as being unmarketable.[28] For the tried and true questions as to title marketability, this works well. All counsel has to do is to undertake the legal research and determine whether a court, in the past, has ruled upon a particular fact situation. However, counsel does not know whether a new fact situation has led to an unmarketable title until counsel litigates the question. Which comes first, the successful litigation or the unmarketable title? Metaphorically, the court rulings in this particular area of the law leave us with a chicken or egg question.[29]

> *"The title industry, like much of our world economy, undoubtedly is living through hard financial times."*

This is one area of the law where the past dictates the future. Precedence is king (or queen, if you prefer). The diligent counsel has to turn to Warren's Weed to see which issues have been and which issues have not been litigated. In the service of his or her client, counsel, facing a new and un-ruled-upon fact pattern involving marketability of title, must be prepared to become an advocate and to make arguments by analogy to the past as best as she or he can. In other words, being just a counsel is not sufficient; in this area, one must also become a lawyer with the persuasive ability, work ethic and willingness to make new law.[30]

Speaking of being a lawyer, there is a lesson to be gleaned from our subject cases. The bidders in these cases could have avoided a great deal of agony, legal fees and expenses, and saved precious time had they obtained a title report prior to bidding on the properties and executing a contract of sale. The defects would have become known and the purchasers would have known not to bid because of the exceptions to title. In matters and cases such as this, title insurance proves its relevance even in a down market.

The title industry, like much of our world economy, undoubtedly is living through hard financial times. But as all of the foregoing cases illustrate, real property transactions do not go ahead until exceptions raised by the title company are resolved. The wheels of commerce grind to a halt without the industry. Title will be back. If anyone asks how you know, just tell him or her that Thomas Paine and Gloria Gaynor told you so.

Endnotes

1. N.Y. L.J., Apr. 4, 2007, at 26, col. 3 (Sup. Ct. Westchester County Mar. 21, 2007).
2. *See R.J. Alan Co. v. Fusco*, N.Y. L.J., Apr. 4, 2007, at 26, col. 3 (Sup. Ct. Westchester County Mar. 21, 2007).
3. *See id.*
4. N.Y. L.J., Aug. 22, 2007, at 27, col. 1 (Sup. Ct. Kings County July 20, 2007).
5. *See* NYCTL 1998–1 *Trust v. Mayfield*, N.Y. L.J., Aug. 22, 2007, at 27, col. 1 (Sup. Ct. Kings County July 20, 2007).
6. *Id.* (quoting Deed from the City of New York to Mary Mayfield, Art. 4 (June 19, 1986)).
7. *See id.*
8. *Id.* (quoting *Jorgensen v. Endicott Trust Co.*, 100 A.D.2d 647, 648, 473 N.Y.S.2d 275, 276 (3d Dep't 1984)).
9. *See id.* (citing *Van Vliet & Place v. Gaines*, 249 N.Y. 106, 109, 162 N.E. 600, 601 (1928); *Bloom v. Kernan*, 146 A.D.2d 916, 917, 536 N.Y.S.2d 897, 898 (3d Dep't 1989); *McAndrew v. Lanphear*, 280 A.D. 6, 9, 111 N.Y.S.2d 238, 242 (4th Dep't 1952)).
10. *See id.* ("Brooklyn is entitled to an order vacating the foreclosure sale in its entirety and directing the return of the deposit.").

11. No. 24896/07, 2008 WL 2276004 (N.Y. Civ. Ct. Richmond County May 19, 2008).

12. *See Rasul v. O'Brien*, No. 24896/07, 2008 WL 2276004, at *1 (N.Y. Civ. Ct. Richmond County May 19, 2008).

13. *Id.* at *2.

14. *See id.*

15. *Id.* at *3 (quoting *O.W. Siebert Co. v. Kramer*, 107 Misc. 2d 520, 521, 435 N.Y.S.2d 476, 477 (Sup. Ct. Queens County 1980)).

16. *Id.* at *3–*4.

17. 252 N.Y. 186, 169 N.E. 134 (1929).

18. *Norwegian Evangelical Free Church v. Milhauser*, 252 N.Y. 186, 190, 169 N.E. 134, 135 (1929) (Cardozo, J.) (citing *Crocker Point Ass'n v. Gouraud*, 224 N.Y. 343, 349, 120 N.E. 737, 738 (1918)).

19. *Whittier Estates, Inc. v. Manhattan Sav. Bank*, 181 Misc. 662, 48 N.Y.S.2d 111 (Sup. Ct. App. T. 1st Dep't 1944).

20. *Id.* at 666, 48 N.Y.S.2d at 114 (quoting *Reformed Prot. Dutch Church in Garden St. v. Madison Ave. Bldg. Co.*, 214 N.Y. 268, 279, 108 N.E. 444, 447 (1915)).

21. 82 N.Y.2d 564, 626 N.E.2d 917, 606 N.Y.S.2d 132 (1993).

22. *Voorheesville Rod & Gun Club v. E.W. Tomkins Co.*, 82 N.Y.2d 564, 571, 626 N.E.2d 917, 920, 606 N.Y.S.2d 132, 135 (1993) (quoting *Regan v. Lanze*, 40 N.Y.2d 475, 482, 354 N.E.2d 818, 822, 387 N.Y.S.2d 79, 83 (1976)).

23. *Id.* (quoting *Dyker Meadow Land & Improvement Co. v. Cook*, 159 N.Y. 6, 15, 53 N.E. 690, 692 (1899)).

24. *See R.J. Alan Co. v. Fusco*, N.Y. L.J., Apr. 4, 2007, at 26, col. 3 (Sup. Ct. Westchester County Mar. 21, 2007).

25. *See* NYCTL 1998–1 *Trust v. Mayfield*, N.Y. L.J., Aug. 22, 2007, at 27, col. 1 (Sup. Ct. Kings County July 20, 2007).

26. *See Rasul*, No. 24896/07, 2008 WL 2276004, at *1 (N.Y. Civ. Ct. Richmond County May 19, 2008).

27. *See O.W. Siebert Co. v. Kramer*, 107 Misc. 2d 520, 522, 435 N.Y.S.2d 476, 478 (Sup. Ct. Queens County 1980).

28. *See Weiss v. Cord Helmer Realty Corp.*, 140 N.Y.S.2d 95, 98–99 (Sup. Ct. Kings County 1955).

29. *See* Marvin N. Bagwell, AXYS, L.L.C. v. Ng*: A Close Encounter of the Marketable Title Kind*, 33 N.Y. Real Prop. L.J. 3 (2005). *See generally AXYS, L.L.C. v. Ng*, N.Y. L.J., Jun. 16, 2004, at 18, col. 1 (Sup. Ct. N.Y. County).

30. By no means does this article cover the entire marketable title landscape. Entire pine forests in Maine have been decimated to produce the paper on which musings regarding marketable title have been printed. This author admittedly has contributed more than his share to the carbon footprint. *See, e.g.*, Marvin N. Bagwell, *Marketability–The Legislature (and Title Insurers, of Course) Save the Day*, N.Y. L.J., May 8, 2002, at 5; Marvin N. Bagwell, *What Is Marketability?*, N.Y. L.J., Mar. 13, 2002, at 5.

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The Section 8 Program: Voluntary Participation Is a Thing of the Past

By Jeffrey R. Metz

In the past 18 months, the judiciary and the City Council have carved out protections for tenants qualifying for what is commonly known as the Section 8 Program.[1]

Complaints that these new protections require owners, large and small, to lose a significant amount of control over those to whom they rent, or have previously rented to on a non-Section 8 basis, and to face difficulties with the bureaucracies that administer the program on the local level have fallen on deaf ears. In getting to this state of affairs, the question thus arises: Have the judicial and legislative branches been guided by sound legal principles, or, more pragmatically, have they been guided by the notion that the societal burden of housing the less fortunate should be shifted to the property owner whom they believe can best bear the burden? Predictably, as with most issues, the answer rests with what side of the ideological fence you are on.

The Section 8 Program

Section 8 of the United States Housing Act of 1937 was enacted "[f]or the purpose of aiding low-income families [to] obtain decent and affordable housing."[2] Under the program, tenants make rental payments based upon their income and ability to pay;[3] any shortfall is covered by the Department of Housing and Urban Development ("HUD") in the form of "assistance payments."[4] To effectuate such payments, HUD enters into contribution contracts with local housing authorities (PHAs)[5] who, in turn, make the assistance payments to the owner.[6]

As the Court of Appeals explained:

> The Section 8 system (Tenant Based Assistance: Housing Choice Voucher Program) is a federal program that provides housing assistance to eligible low-income families by giving subsidies to landlords who rent apartments to them (see 42 USC §1 437f). Once NYCHA has issued a Section 8 voucher to an eligible family, and the family has found a landlord willing to accept it, the landlord and NYCHA must sign a Housing Assistance Payments (HAP) contract (see 24 CFR § 982.451). The HAP contract specifies the terms of the landlord's participation in the Section 8 program. Section 8 tenants make rental payments based on their ability to pay, and NYCHA issues subsidy payments to the landlords to cover the balance of the agreed rent.[7]

Thus, the Section 8 relationship is not merely a bilateral landlord-tenant relationship but rather a tripartite relation of (i) landlord-tenant/federal program, (ii) tenant-federal program, and (iii) landlord-federal program. The tenant and landlord enter into a lease agreement; the tenant and the agency administering the Section 8 program enter into a contract, and the landlord and the administering agency enter into a Housing Assistance Payments (HAP) Contract.[8]

The HAP contract consists of three parts.[9] As is relevant here, part B of the HAP contract specifically provides that it is a separate contract between the PHA and the owner.[10] It runs concurrently with the lease between the landlord and the tenant.[11] Significantly, it "terminates automatically if the lease is terminated by the owner or the tenant."[12] Underscoring that it is separate and distinct from the lease agreement between the owner and the tenant, the HAP contract provides:

> The family is not a party to or a third party beneficiary of Part B of the HAP Contract. The family may not enforce any provision of Part B, and may not exercise any right or remedy against the owner or PHA under Part B.[13]

Part C of the HAP contract contains a tenancy addendum that must be attached to the lease if any tenant participates in the program.[14] It sets forth the duties and obligations of the landlord and tenant with respect to the other provisions of the HAP contract.[15] It states that "[t]he tenant shall have the right to enforce the tenancy addendum against the owner."[16] It also provides that Federal Law is controlling:

> Conflict with Other Provisions of Lease
>
> a. The terms of the tenancy addendum are prescribed by HUD in accordance with Federal law and regulation, as a condition for Federal assistance to the tenant and tenant's family under the Section 8 voucher program.
>
> b. In case of any conflict between the provisions of the tenancy addendum as required by HUD, and any other provisions of the lease or any other agreement between the owner and the tenant, the requirements of the HUD-required tenancy addendum shall control.[17]

Thus, "[t]he tenant and the owner may not make any changes in the tenancy addendum,"[18] and "[i]f there is any conflict between the tenancy addendum and any other provisions of this lease, the language of the tenancy addendum shall control."[19] *Critically, there is no language in the HAP contract or the addendum that restricts an owner's right to opt out of the Section 8 program at the expiration of a term of a HAP contract*.

The Heretofore Voluntary Nature of the Section Program

The intent of the U.S. Congress in enacting the Section 8 program was to make landlord participation voluntary.[20] As one Court put it: "That 42 U.S.C. § 14237f does not mandate landlord participation in the Section 8 program is undisputed."[21] Another Court observed: "Since its inception, a hallmark of the Section 8 program has been its voluntary aspect . . . [where] . . . [n]o landlord is required to participate . . . or to take a Section 8 tenant."[22]

In that regard, 42 U.S.C. § 1437f(1)(A) states that "the selection of tenants shall be the function of the owner."[23] The implementing Code of Federal Regulations further provides at 24 CFR § 982.302(b) in pertinent part: "If the family finds a unit, and the owner is willing to lease the unit under the program, the family may request PHA approval of the tenancy."[24]

Similarly, 24 CFR § 982.452(b) provides that an owner is responsible for "(1) [p]erforming all management and rental functions for the assisted unit, including selecting a voucher-holder to lease the unit, and deciding if the family is suitable for tenancy of the unit."[25]

That Congress views the program as a voluntary one for owners is illustrated by its 1998 express repeal of two provisions it had enacted in 1987.[26] The first was known as the "take one, take all" provision.[27] As the name implies, if an owner chose to rent to one Section 8 tenant, he then had to accept all subsequent Section 8 applicants.[28] Thus, by removing the owner's choice to limit his participation in the program (after he had accepted the first Section 8 tenant), the "take one, take all" provision so conflicted with normal market practices that it was discouraging owners from accepting their first Section 8 tenant.[29]

The second provision was known as the "endless lease" provision.[30] It provided that at the end of a lease term, the landlord could not refuse to renew a Section 8 lease "except for serious or repeated violations of the terms and conditions of the lease, for violation of applicable Federal, State or local law, or for other good cause."[31]

This provision, in particular, had owners up in arms. As the Senate Report from the Committee on Banking Housing and Urban Affairs noted:

> The Committee bill recognizes that the lease conditions under the current section 8 programs have deterred private owners from participating in the programs because they require owners to treat assisted residents differently from unassisted residents. The Committee bill reforms the lease conditions to make the new voucher program operate as much like the unassisted market as possible.[32]
>
> * * *
>
> Some program requirements have constrained the ability of owners to make rational business decisions. . . . The Committee bill reforms section 8 to make the program operate like the unassisted market as much as possible. . . .[33]

The sole purpose and effect of the repeal, one Court instructed, "was to clarify the seminal issue of who will participate in the program itself—that is, to specify that a landlord may, at the end of the lease term, decide to forego the burdens and benefits of its Section 8 participation, just as a tenant may make a similar decision."[34]

Rosario v. Diagonal Realty, L.L.C.

In light of this background, can an owner in New York City opt out of the Section 8 program if a tenancy is subject to the Rent Stabilization Law?[35] In *Rosario v. Diagonal Realty, L.L.C.* ("*Rosario*"),[36] the Court of Appeals answered in the negative.

In that case, the tenant entered into possession on an ordinary rent-stabilized basis. Approximately twelve years into the long term (30 years) tenancy, the tenant obtained Section 8 benefits and the landlord agreed to participate in the program. The owner was also receiving what are commonly known as "J-51" benefits.[37] The J-51 law contains a broad anti-discriminatory provision prohibiting owners from declining to rent to a prospective tenant because of his or her receipt of Section 8 benefits. N.Y.C. Admin. Code § 11-243(k) states in pertinent part:

> No owner of a dwelling to which the benefits of this section shall be applied . . . shall directly or indirectly deny . . . the use of, participation in, or being eligible for a governmentally funded housing assistance program, including, but not limited to, the section 8 housing voucher program and the section 8 housing certificate program . . . of any of the dwelling accommodations in such property. . . .[38]

In 2003, the landlord informed NYCHA that it was electing to opt out of the Section 8 program with respect to Rosario. Further, it refused to accept a subsidy payment and then sued Rosario for nonpayment of rent.

Rosario, and others, commenced a declaratory judgment action against certain owners for a declaration that the owners could not opt out of the Section 8 program.

Arguing before the Supreme Court, the tenants asserted that (i) the

Section 8 subsidy was a material term of a rent-stabilized lease, and that under the Rent Stabilization Code, they must be offered a renewal lease on the same terms and conditions as the prior lease which contained the Section 8 subsidy, and (ii) that because the landlords were receiving J-51 benefits, they were prohibited from engaging in discriminatory practices against the tenants and, therefore, were required to accept the subsidy.

The owners countered by arguing that the renewal provisions of the Rent Stabilization Law conflicted with and were pre-empted by the federal repeal of the endless lease provision. Moreover, they contended that the J-51 anti-discrimination provision applied solely to initial rentals, not to existing tenancies.

The Supreme Court found for the tenants, and the Appellate Division affirmed.[39] The Court of Appeals similarly affirmed, finding in the main that "a landlord's prior acceptance of a Section 8 subsidy is a term of a lease that must be continued on a renewed lease."[40] That Rosario was not a Section 8 beneficiary when she first signed her lease was, according to the Court, of no legal moment. The Court wrote:

> But 9 NYCRR 2522.5(g)(1) [New York City's Rent Stabilization Code] makes no mention of a tenant's initial lease. It requires that a renewal lease "be on the same terms and conditions as the expired lease"—not necessarily the original lease. "Expired lease" means the lease that will have just expired when the renewal lease is to become effective.[41]

The high court then went on to give decidedly short shrift to the owners' preemption argument, finding that there was no express or implied preemption of federal law and ruling: "We conclude that it was not the intent of Congress, when it created the so-called endless lease rule, to remove state and local law protections afforded to Section 8 recipients."[42]

To be sure, the Court of Appeals soundly rebuffed the owners' position, and the U.S. Supreme Court has declined to entertain the case.[43] The tenor of the Court's opinion appears to indicate that the bundle of property rights which accompanies ownership must give way to house the less fortunate, especially when considering that "assistance payments" will always make up a given shortfall.

Kosoglyadov v. 3130 Brighton Seventh, L.L.C.

If *Rosario* left open any question regarding the enforceability of the anti-discrimination provisions of the "J-51" law, it was put to rest in *Kosoglyadov v. 3130 Brighton Seventh, LLC* ("*Kosoglyadov*").[44] There, the tenants entered into possession without Section 8 benefits and became eligible for a voucher 13 years into the tenancy.[45] The owner had obtained J-51 benefits in the interim. When the tenants demanded that the landlord accept their Section 8 voucher, and the landlord declined, the tenants brought a suit alleging, *inter alia,* that the landlord's refusal to accept her Section 8 subsidy violated the anti-discrimination provisions of the J-51 law.[46]

In opposition to the tenants' motion for summary judgment, the owner indicated that the program was voluntary and that it chose not to volunteer because it would incur the following burdens (quoting from Appellant's brief)**:**

- doubling of the managing company's workload by having to prepare both tenants' renewal leases each term and having to prepare and file additional paperwork with NYCHA for the same event;
- in the event that a tenant fails to submit documents to NYCHA, having to wait for the tenant to correct this situation before NYCHA will tender the rent subsidy, which could take months;
- subjecting the Owner to substantial additional delay and paperwork when commencing nonpayment proceedings against tenants;
- having to keep separate accounting books for both the tenant and NYCHA;
- submitting to annual inspections by NYCHA and being forced to supply tenants with services and maintenance above and beyond state and local housing and building codes; and
- paying for the additional administrative fees, legal fees, and apartment maintenance costs associated with these additional burdens.[47]

Among several other arguments, the landlord also contended that transforming Section 8 from a voluntary to a mandatory program would act as serious disincentive to owners to participate in the J-51 program, the purpose of which is to provide incentives to upgrade premises, not to subject owners to the loss of control over whom they accept as tenants and the concomitant burdens of dealing with the PHA.[48]

Equally, if not more important, the owner argued that the anti-discriminatory provision of the J-51 law applied only to initial rentals, and since the tenants had already been living in their unit for 13 years, the owner never deprived the tenants of any dwelling accommodations.[49]

As in *Rosario*, the owner's complaints fell on deaf ears. Citing to *Rosario*, the Appellate Division found that:

> Despite the voluntary nature of the Section 8 program at the federal level, state and local law may

> properly provide additional protections for recipients of Section 8 rent subsidies even *if these protections could limit an owner's ability to refuse to participate in the otherwise voluntary program*.[50] (emphasis added)

Therefore, the Court found that the tenants "established, prima facie, that the defendants discriminated against them in violation of the anti-discrimination provision of the J-51 tax abatement law by refusing to accept the means of payment proffered by them solely because these means are obtained through a federal housing program."[51]

Both in *Rosario* and *Kosoglyadov*, the owners' concerns over the loss of control of their tenant populations and their disdain for another layer of bureaucracy found no traction whatsoever.[52] Hence, it appears clear that the judiciary has determined that owners are better equipped to, and should, therefore, bear the societal burden of dealing with housing for the less fortunate. This sentiment has now been expanded upon by the City Council, which has enacted a significant amendment to the New York City Human Rights Law that leaves owners with no control over Section 8 recipients, regardless of whether a tenant is stabilized or the owner receives J-51 benefits.[53]

N.Y.C. Admin. Code § 8-101, *et seq.*

In 2008, the City Council enacted Local Law 10, which amended the New York City Administrative Code § 8-101, *et seq*. (the "N.Y.C. Human Rights Law") to prohibit owners from rejecting or discriminating against present or potential tenants based upon any "lawful source of income," i.e., Section 8 vouchers.[54]

In so doing, the City Council overrode Mayor Bloomberg's veto of the bill. The Mayor's veto message forcefully stated in pertinent part:

> The City Council's effort to protect tenants from "source of income discrimination" while well-intentioned, would force private landlords to participate in a public program even at a cost to their bottom lines and has the potential to result in increased rents in our most affordable housing stock. Intro. 61-A fails to recognize that the onus should be on the government to make the program more attractive for private sector participation, not the other way around. Furthermore, Intro. 61-A fails to address the City's housing crisis; it is a solution in search of a problem.[55]

The Mayor further noted that Section 8 participation often results in business losses for owners:

> While we are seeing improvements to the Section 8 program, we must recognize that landlords participating in the program may incur costs for which they are not compensated. Even with the improvements that my administration is implementing, once a landlord agrees to a Section 8 voucher for a particular unit, the unit is taken off of the market while the necessary inspections and paperwork are completed. While HPD and NYCHA have made great efforts to reduce this time period, it is still an average of three months. Rent is not collected on the unit during this time. The City must respect a landlord's decision not to forsake multiple months of rent by participating in the Section 8 program. In addition, once in the program, housing units are subject to annual inspections and subsidy payments may be suspended until violations are rectified.[56]

The Mayor also reflected on the loss of control issue: "The Section 8 program should work for both tenants and landlords . . . Intro. 61-A prohibits private owners from making sound business decisions regarding the disposition of their own property and mandates them to enter into a contract with a government agency they would otherwise never had to engage."[57]

The Mayor concluded by stating that Intro. 61-A essentially "makes a voluntary government program involuntary. . . ."[58] But like the owners' arguments before the Courts, the Mayor's concerns regarding the costs and burdens to the landlords were overridden by the perceived benefits poor tenants would receive.[59]

Section I of Local Law 10 contains the City Council's legislative intent. It could not be any clearer:

> The Council hereby finds that some landlords refuse to offer available units because of the source of income tenants, including current tenants, plan to use to pay the rent. In particular, studies have shown that landlords discriminate against holders of section 8 vouchers because of prejudices they hold about voucher holders. This bill would make it illegal to discriminate on that basis.[60]

In a press release issued on the override, Council Speaker Quinn noted that the legislation "will not only increase access for people eligible for Section 8 vouchers to affordable housing, it will fully protect an individual's right to housing, regardless of their financial circumstances."[61] The press release also stated, almost as an afterthought, that:

> [Because] small landlords may have difficulty with the administrative burden that can come to the Section 8 program, the legislation exempts landlords who own five or fewer units. However, rent con-

trolled tenants who reside in these small properties would come under the protection of the law. The law applies to all housing accommodations, regardless of number of units in each, of anyone who owns at lease one property of six or more units.[62]

Local Law 10 has had an immediate impact on the judiciary.

Rizzuti Issacs v. Hazel Towers, Co.

In *Rizzuti Issacs v. Hazel Towers, Co.* ("*Rizzuti*"),[63] the tenants commenced an action to compel the owner to accept their Section 8 vouchers. The owner was subject to J-51 benefits, and according to the Court, the "tenants rely on the provision of J-51, Administrative Code § 11-243, which prohibits landlord recipients of this subsidy to property owners from discriminating on the basis of Section 8."[64] The owner countered by arguing that the J-51 anti-discrimination provision "does not apply to tenants already in possession in contrast to incoming applicants."[65]

The Court never addressed this issue as it applied, apparently *sua sponte*, Local Law 10, and held that "the new protection [accorded by Local Law 10] expressly extends to tenants such as the plaintiffs herein, already in residence as well as incoming, potential tenants."[66]

Thus, by virtue of Local Law 10, a Section 8 recipient, regardless of whether he or she is rent regulated or not, and regardless of whether he or she is first applying for an apartment, or has previously occupied a unit as a non-Section 8 tenant, can dictate that the owner participate in, and not opt out of, the Section 8 program.[67]

Given this state of affairs, certain owners believe that the treatment accorded to Section 8 tenants is as unfair as it is a violation of federal law.

This is especially true in light of a recent decision of the Appellate Division, First Department, as well as one decided by the Supreme Court.

Mother Zion Tenant Association v. Donovan

Mother Zion Tenant Ass'n v. Donovan ("*Mother Zion*")[68] dealt with another aspect of the Section 8 program, which the Appellate Division explained in the following manner:

> In order to entice owners to develop Section 8 housing, in the 1960s Congress enacted legislation offering developers below-market interest rates and mortgage insurance for 40-year mortgages. However, owners had a right to prepay the federal mortgages and exit the Section 8 program after 20 years. Subsequent legislation required owners opting out of the Section 8 program to give one year's notice to the United States Department of Housing and Urban Development (HUD), the appropriate state and local agencies, and the affected tenants, and provided for "enhanced voucher assistance" for tenants and other incentives, including restructuring of mortgage debt and increased rents, to induce owners to remain in the Section 8 program or to enable tenants to remain in their apartments after an owner exits the program.[69]

Thus, the Court pointedly observed that "the federal Section 8 program is a voluntary one, based on incentives."[70]

The Court next explained that Local Law 79 (N.Y.C. Admin. Code § 26-801 *et seq.*), which the City Council passed over mayoral veto on August 2005, provides:

> *inter alia*, that owners of "assisted rental housing," including Section 8 and Mitchell Lama programs, must provide tenants and HPD with one year's notice of intent to withdraw from such an assisted housing program, and grants the tenants, through a tenant association or qualified entity approved by HPD, a right of first opportunity to purchase the building at an "appraised value" set by a three-member "advisory panel" or a right of first refusal to purchase at the price offered by a bona fide purchaser approved by HPD.[71]

Thus, the Local Law "forces an owner to choose between remaining in Section 8 [and] offering to sell the building at a rate determined by appraisers."[72]

The owner qualified and invoked the opt-out provision as of March 2007. The tenants formed an association and notified HPD and the owner that they sought to invoke the right of first refusal. Both HPD and the owner contended the Local Law 79 was preempted by federal and state laws. The tenants then brought an action to declare that the owner must follow Local Law 79.

The Supreme Court rejected the tenants' position, and the Appellate Division affirmed, finding that Local Law 79 "actually conflicts with the federal regime of an entirely voluntary program. . . ."[73] The Court further observed that "[L]ocal [L]aw 79 was enacted, in part, with the aim of nullifying the federal provision allowing for an owner's voluntary withdrawal."[74] And, for good measure, the Court found that "[p]etitioners' characterization of the Local Law affording 'additional protections' does not disguise that actual conflict with the federal laws."[75]

The Appellate Division cited to *Rosario* for the proposition that the repeal of the "endless lease" provision did not preempt application of state rent regulation laws requiring renewals on the same conditions[76] "because legislative and regulatory language expressly contemplated that state and local laws would continue such protections."[77] Yet, in the next breath, it went on to forcefully reject the notion that states have "an unfettered ability to impose restrictions greater than those imposed by federal law. . . ."[78]

Prior to *Mother Zion*, the Supreme Court decided *Real Estate Board of New York, Inc. v. City Council* ("*Real Estate Board*"),[79] which, in addressing Local Law 79, "reluctantly conclude[d] that to the extent that it applies to federal housing programs, Local Law 79 is preempted by federal housing law."[80]

Whether *Mother Zion* and *Real Estate Board* can be reconciled with *Rosario* and *Kosoglyadov,* and whether these more recent cases foreshadow a viable challenge to Local Law 10, remains to be seen.

The Ideological Divide

For low income tenants and their advocates, the recent judicial decisions and the amendments to the New York City Human Rights Law are welcome developments that allow for greater freedom in the renting of apartments in New York City.

But for certain owners, who reject the notion that they should be required to bear the societal burden or housing the less fortunate, this recent turn of events is highly disturbing. These owners believe that a tenant's impecuniousness should not wield a sword so mighty that they are forced to participate *in a voluntary program* against their wishes. Further, they believe that the judiciary and the City Council have no business dictating to whom they rent.

But, of course, as with most housing issues, the true state of events depends upon your point of view.

Endnotes

1. *See* 42 U.S.C. § 1437f (2009) (outlining the Low Income Housing Assistance Program, commonly known as Section 8).
2. *Mother Zion Tenant Ass'n v. Donovan*, 55 A.D.3d 333, 334, 865 N.Y.S.2d 64, 66 (1st Dep't 2008) (explaining that Section 8 "provides for rent subsidies to owners of multiple dwelling rental properties, either through vouchers issued to individual tenants or through project-based programs"); 42 U.S.C. § 1437f(a)(1) (2009).
3. *See Rosario v. Diagonal Realty*, L.L.C., 8 N.Y.3d 755, 761, 872 N.E.2d 860, 862, 840 N.Y.S.2d 748, 750 (2008).
4. *See* 42 U.S.C. § 1437f(a) (2009) ("For the purpose of aiding low-income families in obtaining a decent place to live and of promoting economically mixed housing, assistance payments may be made with respect to existing housing in accordance with the provisions of . . . [section 1437f].").
5. The public housing agencies (PHAs) that administer the program in New York City are: (i) the New York City Housing Authority ("NYCHA") (*see, e.g., German v. Fed. Home Loan Mortgage Corp.*, 885 F.Supp. 537, 573 (S.D.N.Y 1995); (ii) New York City Department of Housing Preservation & Development ("HPD") (*see, e.g., Manhattan Plaza Assoc., L.P. v. Dep't of Hous. Pres.*, 3 Misc.3d 717, 717-18, 779 N.Y.S.2d 740, 740-41 (N.Y. Sup. Ct. 2004); and (iii) the State Div. of Hous. & Cmty. Renewal ("DHCR") (*see, e.g., Rizzo v. N.Y. State Div. of Hous. and Cmty. Renewal*, 16 A.D.3d 72, 79-80, 789 N.Y.S.2d 139, 146 (1st Dep't 2005).
6. *See* U.S. Dep't of Hous. and Urban Dev., Form HUD–52641, Housing Assistance Payments Contract, 4 (2007), *available at* http://www.hud.gov/offices/adm/hudclips/forms/files/52641.pdf (stating that the PHA is responsible for making payments to the owner).
7. *Rosario*, at 760–61, 872 N.E.2d at 862, 840 N.Y.S.2d at 750 (citing 42 U.S.C. § 1437f; 24 C.F.R. § 982.451 (2009)).
8. *See Seminara Pelham, L.L.C. v. Formisano*, 5 Misc. 3d 695, 700-01, 782 N.Y.S.2d 898, 902 (New Rochelle City Ct. 2004) (stating that landlords accepting Section 8 were in a tripartite relationship of landlord-tenant/federal program).
9. *See* U.S. Dep't of Hous. and Urban Dev., s*upra* note 6 at i (asserting that the HAP has three parts: Contract Information, Body of Contract, and Tendency Addendum).
10. *See id.* at 3, Part B.1.c ("During the HAP contract term, the PHA will pay housing assistance payments to the owner in accordance with the HAP contract.").
11. *See id.*, Part B.4.a.
12. *Id.*, Part B.4.b.1.
13. *Id.* at 5, Part B.12.a.
14. *See* U.S. Dep't of Hous. & Urban Dev., Form HUD–52641–A, Tenancy Addendum (2007), *available at* http://www.hud.gov/offices/adm/hudclips/forms/files/52641–a.pdf.
15. *See id.* at 1–5 (setting forth such duties and obligations, such as the lease, the use of the contract unit, the rent to the owner, family payment to the owner, other fees and charges, maintenance, utilities, and other services, the termination of the tenancy by the owner, the lease in relation to the HAP contract, PHA termination of assistance, a family moves out, the security deposit, prohibition and discrimination, conflict with other provisions of the lease, changes in the lease or the rent, and notices).
16. *Id.* at 1, Part 2.b (describing the rights of the tenant in a lease).
17. *Id.* at 4, Part 14.b.
18. *Id*. Part 15.a.
19. *Id.* at 1, Part 2.b.
20. *See Salute v. Stratford Greens Garden Apts.*, 136 F.3d 293, 296, 300-01 (2d Cir. 1998) (honoring owners' refusal to rent to Section 8 certificate holders).
21. *Franklin Tower One, L.L.C. v. N.M.*, 725 A.D.2d 1104, 1113, 157 N.J. 602, 619 (1999) (noting that, even though landlord participation is voluntary, "the voluntary nature of the Section 8 program is not at the heart of the federal scheme.").
22. 30 *Eastchester, L.L.C. v. Healy*, No. SP–2002–77, 2002 WL 553709, at *3 (N.Y. City Ct. Mar. 28, 2002).
23. 42 U.S.C. § 1437f(c), (d) (2009).
24. 24 C.F.R. § 982.302(b) (1999).
25. 24 C.F.R. § 982.452(b) (2008).
26. *See Salute v. Stratford Greens Garden Apts.*, 136 F.3d 293, 300 (2d Cir. 1998) (noting that the voluntariness was adopted when the two provisions were part of the statute, but holding that "[t]he repeal of the . . . provisions does not affect the voluntariness of the Section 8 program.").
27. *See id.* (indicating that "[t]he 'take one, take all' . . . provision[] [was] part of the statute when the voluntariness provision was adopted").
28. *See id.* at 295.
29. *Id.* at 297-98 (quoting *Salute v. Stratford Greens Garden Apts.*, 918 F.Supp. 660, 664 (E.D.N.Y. 1996)) (observing that the "take one, take all" provision would create an incentive for landlords to evict tenants who later become indigent and eligible for Section 8, so that the landlord does not have to become a full–fledged participant).
30. *See id.* at 300.
31. *Id.* at 300 n.5.
32. S. Rep. No. 105–21, at 36 (1997).
33. *Id.*
34. *Seminara Pelham, L.L.C. v. Formisano*, 5 Misc. 3d 695, 698, 782 N.Y.S.2d 898, 901 (New Rochelle City Ct. 2004).
35. *See* New York, N.Y., Admin. Code Tit. 26, ch. 4, § 26–501 (2008) (defining how an emergency is found and then declared).
36. 8 N.Y.3d 755, 872 N.E.2d 860, 840 N.Y.S.2d 748 (2007), *cert. denied*, 128 S.Ct. 1069, 169 L. Ed. 2 808 (2008).
37. *See* New York, N.Y., Admin. Code Tit. 11, ch. 2, § 11–243 (2008) (reextending the exemption and tax abatament when

improvements are made to substandard dwellings).

38. New York, N.Y., Admin. Code tit. 11, ch. 2, § 11-243(k) (2008) (explaining that denial cannot be "because of race, color, creed, national origin, gender, sexual orientation, disability, marital status, age, religion, alienage or citizenship status").
39. *See Rosario v. Diagonal Realty, L.L.C.*, 9 Misc. 3d 681, 699, 803 N.Y.S.2d 343, 357 (Sup. Ct., N.Y. County 2005), *aff'd*, 32 A.D.3d 739, 821 N.Y.S.2d 71 (1st Dep't 2006) (finding rent–stabilized tenants are entitled to an automatic renewal lease).
40. *Rosario v. Diagonal Realty*, 8 N.Y.3d 755, 761, 872 N.E.2d 860, 863, 840 N.Y.S.2d 751, 751 (2007), *cert. denied*, 128 S. Ct. 1069, 169 L. Ed. 2d 808 (2008).
41. *Id*. at 762, 872 N.E.2d at 863, 840 N.Y.S.2d at 751 (contrasting 9 N.Y.C.R.R. 2522.5(g)(1) to Diagonal's argument that this section of the Rent Stabilization Code does not apply as a result of when Rosario initially signed the lease, she did not have the status of "a Section 8 beneficiary").
42. *Id*. at 764, 872 N.E.2d at 865, 840 N.Y.S.2d at 753 (holding that Congress intended to terminate "state and local protections" that the Section 8 recipients were receiving prior to the termination of the endless lease rule).
43. *See Rosario*, 128 S.Ct. 1069, 169 L. Ed. 2d 808 (2008) (denying petition for writ of certiorari to the Court of Appeals of New York).
44. 54 A.D.3d 822, 863 N.Y.S.2d 777 (2d Dep't 2008).
45. See *Kosoglyadov v. 3130 Brighton Seventh*, 54 A.D.3d 822, 823, 863 N.Y.S.2d 777, 779 (2d Dep't 2008) (stating that the New York City Housing Authority issued the plaintiffs a voucher under Section 8 in 2006, when the plaintiffs had initially applied for such voucher in 1992).
46. *Id.* at 824, 863 N.Y.S.2d at 780.
47. Brief of Defendants–Appellants at 16–17, *Kosoglyadov v. 3130 Brighton Seventh*, L.L.C., 54 A.D.3d 822, 863 N.Y.S.2d 777, No. 2007-10431 (2d Dep't 2008).
48. *See id.* at 20–21 ("[t]he Order's compulsory proscriptions—forcing an owner of an *existing long–term rent stabilized tenancy* to also (13 years into the tenancy) accept a Section 8 voucher and enter into additional regulatory burdens via a HAP contract, simply because it receives J–51 tax benefits for building improvements—are contrary to the express language and intent of the Section 8 law and the judicial precedent.").
49. *See id.* at 4 (arguing that the tenants were not deprived of ability to remain in possession because tenants had resided in there for over thirteen years with no apparent economic hardship).
50. *Kosoglyadov*, at 824, 863 N.Y.S.2d at 779 (citing *Rosario v. Diagonal Realty, L.L.C.*, 8 N.Y.3d 755, 764 n.5, 872 N.E.2d 860, 865 n.5, 840 N.Y.S.2d 748, 753 n.5 (2007), *cert. denied*, 128 S. Ct. 1069, 169 L. Ed. 2 808 (2008); 24 C.F.R. § 982.53(d) (2008)).
51. *Kosoglyadov v. 3130 Brighton Seventh*, 54 A.D.3d 822,824, 863 N.Y.S.2d 777, 779 (2d Dep't 2008) (citing New York, N.Y., Admin. Code tit. 11, ch. 2, § 11–243(k) (2008)); *Cosmopolitan Assoc., L.L.C. v. Fuentes*, 11 Misc. 3d 37, 38–39, 812 N.Y.S.2d 738, 740 (Sup. Ct. App. T. 2d Dep't 2006).
52. *See, e.g.*, *Rosario v. Diagonal Realty, L.L.C.*, 8 N.Y.3d 755, 761, 872 N.E.2d 860, 863, 840 N.Y.S.2d 751, 751 (2007) (holding that a tenancy cannot opt out of Section 8 if it is subject to rent stabilization laws); *Kosoglyadov*, at 824, 863 N.Y.S.2d at 779 (stating that although Section 8 is voluntary, state and local laws may delimit an owner's ability to refuse to participate).
53. *See* New York City Commission on Human Rights, *Chapter 1. Commission on Human Rights § 8–101*, http://www.nyc.gov/html/cchr/html/ch1.html#1 (creating a city agency which has general jurisdiction over matters of discrimination over housing and other real estate).
54. *See id.*
55. Letter from Mayor Bloomberg to Hector L. Diaz (Feb. 29, 2008) (on file with author) (criticizing the effort of the City Council "to protect tenants from 'source of income discrimination'").
56. *Id.* (recognizing the costs that landlords face when participating in the Section 8 program).
57. *Id.* (noting the business decisions that private owners would have to engage in when participating in the Section 8 program).
58. *Id.* (concluding that the Mayor believes that Intro. 61–A transforms a voluntary program into an involuntary one).
59. *Id.* (acknowledging that the concerns of the Mayor were ultimately disregarded).
60. N.Y.C. Commission on Human Rights, *To Amend the Administrative Code of the New York, in Relation to Prohibiting Landlords from Discriminating Against Tenants Based on Lawful Source of Income*, http://www.nyc.gov/html/cchr/html/ammend08.html.
61. Press Release, N.Y.C Council, Preserving Access to Affordable Housing (Mar. 26, 2008), *available at* http://council.nyc.gov/html/releases/024_032608_prestated_sec8override.shtml ("Members of the City Council will vote to override Mayor Bloomberg's veto of legislation to prohibit discrimination against prospective tenants based on lawful source of income.").
62. *Id*.
63. No. 406514/07, 2008 N.Y. Misc. LEXIS 2176 (Sup. Ct. N.Y. County Mar. 27, 2008).
64. *Rizzuti Issacs v. Hazel Towers Co*., No. 406514/07, 2008 N.Y. Misc. LEXIS 2176, at *2–3 (Sup. Ct. N.Y. County Mar. 27, 2008) (arguing that the provisions of J-51 applies to tenants already in possession).
65. *Id.* at *3.
66. *Id.* at *5.
67. *See, e.g.*, *Rizzuti*, 2008 N.Y. Misc. LEXIS 2176 (granting the motion for summary judgment made by the plaintiffs for a declaration and an injunction).
68. 55 A.D.3d 333, 865 N.Y.S.2d 64 (1st Dep't 2008).
69. *Mother Zion Tenant Ass'n v. Donovan*, 55 A.D.3d 333, 334, 865 N.Y.S.2d 64, 65–66 (1st Dep't 2008) (citing 42 U.S.C. § 1437f(c)(8) (2009); 42 U.S.C. § 1437f(t) (2009); 12 USC § 1715l (2007); 12 U.S.C. § 1715z-1 (2000); 12 U.S.C. § 4106 (1992); *Forest Park II v. Hadley*, 336 F.3d 724 (8th Cir. 2003)).
70. *Mother Zion Tenant Ass'n*, at 334, 865 N.Y.S.2d at 66.
71. *Id*. at 334–35, 865 N.Y.S.2d at 66 (citing New York, N.Y., Admin. Code tit. 26, ch. 9, §§ 26–801(f), (k), (n), (o) (2008), New York, N.Y., Admin. Code tit. 26, ch. 9, § 26–802(a) (2008), New York, N.Y., Admin. Code tit. 26, ch. 9, §§ 26–804(a)-(d) (2008); New York, N.Y., Admin. Code tit. 26, ch. 9, §§ 26–805(a), (c), (e) (2008); New York, N.Y., Admin. Code tit. 26, ch. 9, §§ 26–806(a), (b), (d) (2008)).
72. *Mother Zion*, *Tenant Ass'n*, at 335, 865 N.Y.S.2d at 66 (stating that Local Law 79 "does not specify whether the appraised value is to be based on the building's worth as assisted rental housing or unencumbered property that can be let at market rates or otherwise developed.").
73. *Id*. at 336, 865 N.Y.S.2d at 67 (citing *Forest Park II*, 336 F.3d at 731–34).
74. *Id*. (stating Local Law 79 "requires owners to either remain in Section 8 or sell their property to the tenants at a rate set by a panel of appraisers").
75. *Mother Zion Tenant Ass'n v. Donovan*, 55 A.D.3d 333, 336, 865 N.Y.S.2d 64, 67 (1st Dep't 2008) (examining the Petitioners' argument that the Local Law provides "additional protections").
76. *See id*.
77. *Mother Zion Tenant Ass'n*, at 336–37, 865 N.Y.S.2d at 67 (explaining the reasoning of the Court of Appeals in *Rosario*).
78. *Id*. at 337, 865 N.Y.S.2d at 68 (holding that the court would follow the reasoning from the Eighth Circuit in *Forest Park II*).
79. 16 Misc. 3d 530, 842 N.Y.S.2d 218 (Sup. Ct., N.Y. County 2007).
80. *Real Estate Bd. of N.Y. v. City Council of City of N.Y.*, 16 Misc. 3d 530, 541, 842 N.Y.S.2d 226 (Sup. Ct., N.Y. County 2007).

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Contract of Sale: Environmental Provisions

By James P. Rigano

A contract of sale must have specific provisions that address environmental issues if the property is contaminated. The basic issue is which party will be responsible for the cleanup. However, the negotiation does not end with the simple conclusion that a buyer, seller, or perhaps some third party that was responsible for causing the contamination will address the problem. There are several contractual matters to be considered which are discussed in the following paragraphs.

Environmental Assessment

Typically, the buyer will perform a Phase I, and possibly a Phase II environmental assessment of the premises. While Phase Is are customary and are not usually subject to an objection from a seller, a seller may want some control over the Phase II process. The following is language that the parties may want to consider.

> Buyer, at its sole cost and expense, may perform an environmental assessment of the Premises that must be completed within 60 days of the execution of this contract. Such assessment may include review of relevant documents and interviews of knowledgeable employees and officers of Seller, review of files of governmental authorities and other work associated with a Phase I environmental assessment. To the extent that the Buyer wants to perform a Phase II investigation involving a sampling and analysis of soil, groundwater, or other items ("Phase II work"), Buyer shall provide a detailed work plan to Seller. Seller shall have the right to approve the work plan and the contractor selected by Buyer to perform the Phase II work. Buyer's contractor shall execute an access agreement prepared by Buyer prior to performing Phase II work. The Phase II work must be completed within the 60-day period described above.
>
> Within 60 days after the execution of this contract, Buyer may, at its election, notify Seller in writing that, based upon the results of the environmental assessment, Buyer elects to terminate this Agreement, in which event no party has any liability to another, except as expressly reserved in this Agreement. If Seller does not receive such notification within 60 days of execution of this contract, Buyer may not terminate this agreement based on the environmental assessment performed by Buyer.

Definitions

There are several definitions that are unique to the environmental provisions of the contract. The contractual provisions will flow more readily with a definition section provided as part of the environmental language to the contract. The following are definitions that the parties should consider:

> "Environmental Claim" means any summons, complaint, demand, order, accusatory instrument, judicial decree, consent order, hearing notice, administrative order, notice of violation, subpoena, discovery request, cost recovery action, proceeding or investigation, whether administrative, civil or criminal, including any claims alleging common law claims brought by any governmental authority or any individual, group of individuals or private organization, in connection with an Environmental Condition.
>
> "Environmental Condition" means the (i) Release or threatened release of a Hazardous Substance at, in, under or otherwise affecting the Premises; (ii) actual, potential, alleged or threatened violation of any Environmental Law; (iii) the commencement or threatened commencement of an Environmental Claim; or (iv) presence of any other condition or event which could give rise to or serve as the basis for an Environmental Claim.
>
> "Environmental Laws" means any and all laws, statutes, ordinances, rules, regulations, common law theories or doctrines relating to (i) human health or protection of the environment, or (ii) the generation, storage, possession, use, handling, transportation, treatment, disposal or Release of Hazardous Substances. The term "Environmental Laws" shall include, but not be limited to, the Comprehensive Environmental Response, Compensation, and Liabil-

ity Act (42 U.S.C. § 9601 *et seq*.), the Hazardous Material Transportation Act (49 U.S.C. § 6901 *et seq*.), the Federal Water Pollution Control Act (33 U.S.C. § 1251 *et seq*.), the Oil Pollution Act of 1990 (P.L. 101-380), the Safe Drinking Water Act (42 U.S.C. § 300(f) *et seq*.), the Clean Air Act (42 U.S.C. § 7401 *et seq*.), the Toxic Substances Control Act (15 U.S.C. § 2601 *et seq*.), the Federal Insecticide, Fungicide, and Rodenticide Act (7 U.S.C. § 136 *et seq*.), and the New York Navigation Law, as such laws have been and hereafter may be amended or supplemented; Environmental Laws excludes requirements related to human health or worker safety under the Occupational Safety and Health Act (29 U.S.C. § 651 *et seq*.) or other occupational safety laws or requirements.

"Hazardous Substance" means any pollutant, contaminant, chemical, waste, substance or material, whether or not defined or regulated as such in any Environmental Law, including (without limitation) asbestos, petroleum (including crude oil or any fraction), radioactive substances and polychlorinated biphenyls, or material which has the potential to become a Hazardous Substance; provided, to the extent that the applicable laws of any state establish a meaning for "hazardous material," "hazardous substance," "hazardous waste," "solid waste" or "toxic substance," which is broader than that specified here or in any Environmental Law, such broader meaning shall apply.

"Release" means any past, current or future act, omission or event, whether on or off the Premises, which resulted or results in the accidental or intentional spilling, leaking, pumping, pouring, emitting, emptying, discarding, injecting, escaping, leaching, dumping or disposing, whether past, present or future, of a Hazardous Substance on, at, or in the Premises or the soil and groundwater underlying the Premises.

"Indemnified Expenses" means all damages, losses (foreseen and unforeseen), liabilities (tort and contract, strict and otherwise), obligations, penalties, claims (matured and contingent), sums paid in settlement of claims, litigation, demands, defenses, judgments, suits, proceedings, costs, disbursements and expenses (including all costs of defense and settlement and the fees and disbursements of attorneys, consultants and experts of any kind asserted against or incurred by Seller or Seller's officers, trustees, directors, shareholders, employees, partners, agents, subsidiaries or affiliates and arising directly or indirectly out of or in connection with any Environmental Condition involving the Premises. Indemnified Expenses will include (to the extent permitted by law), without limitation, all of the following: (1) costs incurred in the removal of Hazardous Substances, costs incurred in investigation, monitoring cleanup, and containment of Hazardous Substances, and costs incurred for remediation and restoration; (2) costs incurred to cure any violations of Environmental Law; (3) civil and criminal fines and penalties; (4) costs incurred to remove any liens imposed by law in favor of the federal or any state or local government or governmental agency or authority in connection with an Environmental Condition; (5) attorneys', accountants', consultants', and experts' fees and disbursements, administrative costs, and other out-of-pocket expenses; (6) diminution in the market value of the premises and/or any adjacent property; (7) damages or injury to, destruction of, or loss of, natural resources; (8) sums paid to tenants and other third parties (or offset against rents or other sums payable by such tenants and other third parties) pursuant to leases or other agreements wherein such tenants or other third parties are entitled to indemnification or payment on account of Environmental Conditions; (9) consequential damages; (10) sums paid by governmental authority or any other person or entity for any costs described above; and (11) all other costs and expenses of any kind or nature.

As-Is and Assumption of Liabilities Clause

Typically, in a real estate transaction, the contract will include an as-is clause. Most contracts do not go any further in terms of allocating possible liabilities associated with the premises. An as-is clause probably only bars a warranty claim against a seller and is not a complete defense to a statutory or common law claim for contamination. As a result, if a contract only has an as-is clause, the seller may be left with the burden of the environmental hazards at the property. Nevertheless, an as-is clause should be incorporated in the contract of sale.

The parties to the transaction should negotiate who will be responsible for any necessary cleanup. The contract should identify the party and state that the party assumes responsibility for the remediation activity. Contractual language to consider is as follows:

> Purchaser agrees to purchase the Premises in an "as-is" condition and to assume, upon closing of this transaction, any and all liabilities and obligations that currently exist or may arise, either directly or indirectly, from the presence of those known and unknown Environmental Conditions at the Premises. Purchaser's assumption of liability under this paragraph specifically extends to any and all costs, damages, penalties, assessments, judgments, suits, investigation, and remediation, no matter by whom sustained or levied, which may be sought in connection with the known and unknown Environmental Conditions at the premises.

Representations

A seller may be liable for fraud where he or she intentionally deceives a buyer regarding property conditions. However, under the doctrine of caveat emptor, silence by the seller is not regarded as fraud, and unless the seller intentionally provides false information, there may be no fraudulent activity. In New York State, there has been some erosion of the doctrine of caveat emptor, particularly regarding environmental matters, and a seller who intentionally does not disclose a known contamination problem may well be defending a fraud action by a buyer. As a result, the production of all existing environmental documentation regarding the premises between the parties is sound practice. While a seller may want to avoid specific representations regarding the character of the property, the seller should strongly consider identifying all environmental documents in its possession and providing those documents along with an itemized list to the purchaser.

Release

Parties to the transaction will want to consider a release of liability. For example, if the purchaser receives a discount for contamination and is assuming the responsibility for the cleanup, the seller may want to demand that the purchaser provide a release so that the purchaser would be agreeing that it could not sue the seller in the future for environmental issues. Release language to be considered is as follows:

> Buyer covenants not to commence any action, suit or proceeding or bring any claim, judgment or assessment against Seller, including any claim or suit based on common law doctrines, CERCLA or other federal or state environmental statutes currently in effect or hereinafter enacted, in connection with known and presently unknown Environmental Conditions at the Premises or alleged violations of the applicable federal and state laws, rules and regulations. With regard to Environmental Conditions at, in, on, or near the Property, including: (a) the Environmental Conditions identified in Purchaser's environmental assessment of the property; (b) Environmental Conditions which may exist whether presently known or unknown to the parties; and (c) Environmental Conditions which may hereafter be detected or discovered, Buyer releases Seller and Seller's tenants from any and all liabilities, obligations, costs, damages, claims, actions, suits, demands, judgments, penalties, fines and attorney's fees and expert-related expenses, to the extent the same arise, either directly or indirectly, from or in connection with said Environmental Conditions.

Indemnification

Perhaps the most critical clause in the environmental provisions to the contract of sale is the indemnity. Indemnities are often difficult to negotiate and parties are typically reluctant to provide indemnities. For example, a seller is interested in selling the property and walking away without future exposure or responsibility. However, a purchaser may want a seller to provide an indemnity if there are remaining environmental concerns at the property. In contrast, a seller may demand an indemnity from a purchaser where the seller has discounted the price for environmental conditions and the purchaser is assuming responsibility for the problem. Often, indemnity clauses are complex and difficult to understand. However, with the definition sections presented earlier, the indemnification language can be straightforward. The following is language to consider:

> Buyer will, at its sole cost and expense, indemnify, defend, protect, and hold harmless Seller and Seller's officers, trustees, directors, shareholders, employees, partners, agents, subsidiaries and affiliates from any and all Indemnified Expenses.

Finally, it is important that these provisions survive closing. A clause should be included at the end of the environmental section to the contract that these provisions survive closing.

The above contractual provisions will provide a solid legal basis for allocating environmental responsibilities. However, these legal provisions cannot replace commitments by respectable, well-financed parties to the transaction. For example, where a purchaser is assuming responsibility and providing a release and indemnity to a seller, the seller wants to be confident that the purchaser is committed to implementing the work, and has the financial ability to perform the work and fulfill any future indemnity demands from the seller.

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Notices of Pendency: Protecting Sellers in Contracts for the Sale and Purchase of Real Property

By William W. Weisner and Amy Carper Mena

I. Introduction

You represent an elderly client selling a commercial property that is the most valuable asset in her estate. She is in poor health and needs the money to pay medical bills and living expenses. She receives a good offer from a buyer who has a reputation for being litigious. She has not received any other acceptable offers and does not want to lose this offer. She also fears that the property's value will decline in the near future. She asks you to draft a sales contract that will prevent the buyer from tying up the property if a dispute arises (or is invented by the buyer to gain negotiating leverage) before closing, because tying up the property until a dispute is resolved would cause her severe financial distress. You draft a firm contract with limited seller representations. Among other things, you also include a provision stating that the buyer covenants not to file a notice of pendency if a dispute arises. Is the provision enforceable? Should the buyer accept it? Is it necessary? This article provides guidance to real estate attorneys pondering these issues, and includes sample provisions to be used in appropriate circumstances.

II. Background

A. What Is a Notice of Pendency and When Is It Available?

Section 6501 of the N.Y. Civil Practice Law and Rules ("CPLR") provides that a notice of pendency is a notice filed in an action "in which the judgment demanded would affect the title to, or the possession, use or enjoyment of, real property, except in a summary proceeding brought to recover the possession of real property."[1] The filing gives constructive notice that an action concerning such real property is pending, and binds any person "whose conveyance or incumbrance is recorded after the filing . . . [to] all proceedings taken in the action after such filing to the same extent as a party."[2] A notice of pendency does not create a lien, although the effect from a conveyance standpoint is similar in some respects.[3] "A notice of pendency is a statutory device, superseding the harsher common law doctrine of *lis pendens*."[4]

The right to file a notice of pendency is absolute if the statutory prerequisites are met; the right to file is not subject to judicial discretion or prior judicial review.[5] A notice of pendency may not be filed in a summary proceeding brought to recover the possession of real property.[6] If the prerequisites are met, a notice of pendency may be filed in any action in a state or federal court.[7] The United States Court of Appeals for the Second Circuit recently rejected a due process challenge to the notice of pendency statute.[8]

B. How Do You File a Notice of Pendency?

The notice of pendency must be filed in the office of the clerk of any county where property affected is situated.[9] In an action to recover a judgment affecting the title to real property, the notice must state the names of the parties and the object of the action, and contain a description of the property affected.[10] Additional filing requirements are listed in CPLR 6511. Strict compliance with the statutory requirements is a condition precedent to a valid notice of pendency.[11]

A complaint must already be on file or be filed simultaneously with the notice of pendency.[12] A plaintiff and a cross-claiming or counterclaiming defendant may file a notice of pendency in actions where notices of pendency may be filed under CPLR 6501.[13] "A notice of pendency is effective only if, within 30 days after [its] filing, a summons is served upon the defendant or first publication of the summons against the defendant is made pursuant to an order and publication is subsequently completed."[14]

Typically, no bond or other security is required to file a notice of pendency.[15] This distinction from other provisional remedies creates the potential for a purchaser to tie up a property by filing a notice of pendency without incurring any additional expense other than the cost of commencing an action and filing the notice. Although a property owner may bring a tort claim for the malicious filing of a notice of pendency,[16] such a remedy may involve difficult issues of proof, and provide little relief to an owner who does not have the means to litigate or where the notice filer has no assets.

C. How Long Is a Notice of Pendency Valid?

A notice of pendency is valid for three years.[17] Before the notice expires, a court may extend the notice for another three years upon plaintiff's motion, providing such notice as the court may require, and making a showing of good cause.[18]

D. What if the Property Is Sold to a Third Party While Title or Possession Is Subject to Litigation but No Notice of Pendency Has Been Filed?

If no notice of pendency has been filed, a purchaser cannot be charged with *constructive* notice of the litigation under Article 65 of the CLPR and, hence, will not be bound by proceedings taken in the action absent actual knowledge of the litigation.[19]

Pursuant to common law, a purchaser of real property will generally be bound by the consequences of a lawsuit of which he or she has *actual* knowledge.[20]

E. What if the Property Is Sold to a Good-Faith Purchaser for Value, but Between the Closing and Recording of the Deed, a Notice of Pendency Concerning the Property Is Filed by a Prior Contract Vendee?

Courts have interpreted N.Y. Real Property Law ("RPL") §§ 291 and 294(3) (the race-to-record statutes for good faith purchasers for value) as providing exceptions to the general rule of CPLR 6501 that a person whose conveyance or encumbrance is recorded after the filing of the notice of pendency is bound by all proceedings taken in the action after such filing to the same extent as a party.[21] These courts have done so on the premise that a notice of pendency "does not create rights that did not already exist."[22] In *2386 Creston Avenue Realty v. M-P-M Management Corp.*,[23] the Appellate Division, First Department, held that plaintiff's filing a notice of pendency for a specific-performance action was fruitless where defendant had deeded the property to a third-party good faith purchaser for value before the notice of pendency was filed, but the deed was recorded after the notice was filed, on the grounds that plaintiff had failed first to record its contract and that "[t]he filing of a notice of pendency does not substitute for the recording of the contract of sale or conveyance."[24]

F. Practical Consequences

Generally speaking, a purchase of real property may proceed, not impacted by litigation concerning the real property, if the purchaser did not have actual or constructive notice of the litigation.[25] In other words, a court generally will not unwind a sale to a bona fide purchaser for value. Only an injunction would conclusively prevent a property owner from selling or mortgaging its property to a bona fide purchaser.

But, effectively, a notice of pendency is tantamount to an injunction in many respects. In *In re Sakow*, the N.Y. Court of Appeals observed:

> [W]e have referred to a litigant's ability to file a notice of pendency as an "extraordinary" privilege because of the relative ease by which it can be obtained and its powerful effect on the alienability of real property. The notice of pendency is a unique provisional remedy, in that "the statutory scheme permits a party to effectively retard the alienability of real property without any prior judicial review." Critically, the filing of a notice of pendency requires no showing of the likelihood of success on the merits of the cause of action. Thus, "a plaintiff can cloud a defendant's title merely by serving a summons and filing a proper complaint and notice of pendency stating the names of the parties, the object of the action, and a description of the property."[26]

Most potential purchasers will not contract to buy a property if a notice of pendency has been filed with respect to the property, or at least will not close on the purchase of a property until the notice, and perhaps the litigation, is discharged. Lenders, too, are unlikely to close a loan secured by such a property, because consummating the transaction would subject their mortgage to the litigation's result.

Unlike a party who files for a preliminary injunction, a notice-filer need not show a probability of success in the litigation to obtain a notice of pendency.[27] Compare this with a *lis pendens* filed under Connecticut law, which does require such a showing,[28] or compare this with New Jersey's requirement to show "a probability that final judgment will be entered in favor of the plaintiff."[29] In fact, the Second Circuit, in *Diaz v. Paterson*, noted that New York's "mere good-faith standard . . . does not afford the most meaningful process to a property holder burdened by a notice of pendency filed in conjunction with a patently meritless law suit."[30]

Judge Joseph M. McLaughlin has commented that "the notice of pendency is the one provisional remedy a plaintiff is free to employ without posting an undertaking to indemnify the defendant in the event the plaintiff loses the action,"[31] and that this right "lends itself to abuse at the hands of unscrupulous plaintiffs who may tie up the defendant's property during the lawsuit."[32]

Even where a seller prevails in the lower court, the notice of pendency may stay in place during an appeal if the purchaser receives a discretionary stay under CPLR 5519(c),[33] which would deter a title insurance company from insuring title unless the seller posts a large deposit with the insurer covering potential defense costs. Indeed, under New York case law, a title insurer has good reason to be wary of insuring title even after a notice of pendency has been dismissed.[34]

Before exploring possible remedies for this problem, we will first examine how and when a notice of pendency may be cancelled.

G. How May an Owner Cancel a Notice of Pendency?

The CPLR distinguishes between mandatory and discretionary cancellation of a notice of pendency.[35]

First, mandatory cancellation is called for under CPLR 6514(a) if (1) the summons has not been served within the 30-day time limit of CPLR 6512, (2) the action has been settled, discontinued, or abated, (3) the time to appeal from a final judgment against the plaintiff has expired, or (4) enforcement of a final judgment against the plaintiff has not been stayed under CPLR 5519.[36]

Second, the court has discretion under CPLR 6514(b) to cancel a notice of pendency, upon motion of any person aggrieved and upon notice, if the plaintiff has not commenced or prosecuted the action in good faith.[37] According to the N.Y. Court of Appeals in *5303 Realty Corp. v. O & Y Equity Corp.*, a court's scope of review under CPLR 6514(b) is "circumscribed," and "[o]ne of the important factors in this regard is that the likelihood of success on the merits is irrelevant to determining the validity of the notice of pendency."[38]

CPLR 6515 also provides a court with discretion to cancel a notice of pendency. Under this provision, a court, upon motion of any aggrieved person in any action other than a foreclosure action as defined in CPLR 6516(b) or an action for partition or dower, and upon such notice as the court requires, may cancel a notice of pendency rightfully filed upon "terms as are just," even where the judgment demanded would affect specific real property, if the moving party (i.e., seller) provides:

> [A]n undertaking in an amount to be fixed by the court, *and* if:
>
> 1. the court finds that adequate relief can be secured to the plaintiff [i.e., the notice filer] by the giving of such an undertaking; *or*
> 2. in such an action, the plaintiff fails to give an undertaking, in an amount to be fixed by the court, that the plaintiff will indemnify the moving party for the damages that he or she may incur if the notice is not cancelled.[39] (emphasis added)

Courts generally have interpreted CPLR 6515 to call for cancellation of a notice of pendency, upon the property owner/seller's motion, if the property owner/seller provides an undertaking but the notice filer does not; however, where the notice filer provides an undertaking, courts have not cancelled the notice of pendency.[40] Notwithstanding the disjunctive word "or" connecting subsections (1) and (2) of CPLR 6515, thereby making either subsection applicable where "judgment demanded would affect specific real property," New York courts prefer to "double-bond" in actions for specific performance even when the notice filer's likelihood of success is doubtful,[41] thereby requiring the property owner/seller to post an undertaking to have the notice cancelled, but permitting the notice to remain in place if the notice filer also posts an undertaking. Query whether a property owner/seller should be required to maintain in place the undertaking that it posted to have the notice of pendency cancelled, where ultimately the notice is not cancelled because the notice filer also posted a bond under subsection (2) of CPLR 6515.

H. Amount of Undertakings

As briefly touched upon in the preceding section, the tortured language of CPLR 6515 has led to varying interpretations concerning who must post an undertaking, and, also, what the amount of such undertakings should be.[42] Courts usually focus on the damages that the other party would suffer if the notice of pendency is or is not cancelled, and a court's discretion is guided by the pleadings, the parties' acts, and the circumstances set forth in the affidavits, as well as the question of good faith, the probability of success, and the uniqueness of the property as revealed in the papers submitted.[43]

In *Weiss v. Alard*, the court held that the proper amount of the undertakings was the amount of the "benefit of the bargain" for each party.[44] The undertaking that the property owner/seller had to post was held to be the difference between the amount that the notice filer contended the property was worth ($1,750,000) over the contract price ($925,000), for an undertaking of $825,000; the notice filer's undertaking was held to be the property owner's prima facie benefit of the bargain, i.e., the contract price ($925,000).[45] But, in an older case, *Ansonia Realty Co. v. Ansonia Associates*, the Appellate Division, First Department, found that requiring the purchaser to post an undertaking representing the balance of the purchase price was disproportionate to any damages that defendants might suffer as a result of the continuance of the notice of pendency.[46]

In *Weksler v. Yaffe*, the court held that the notice of pendency should be cancelled if seller posted a bond equal to purchaser's lost profits and brokerage commission ($180,000), and if the purchaser failed also to post a bond in the amount of seller's potential damages if the notice of pendency were not lifted (measured as the cost of maintaining the property—$13,000).[47]

I. Permitted Forms of Undertakings

Undertakings under CPLR 6515 must comply with CPLR 2501, which defines an undertaking as either (1) an obligation containing a covenant by a surety to pay the required amount if any required condition is not fulfilled, or (2) any deposit, made subject to the required condition, of the required amount in legal tender of the United States or in the face value of unregistered bonds of the United States or of the state.[48] CPLR 2502 further provides that a surety must be:

> (1) an insurance company authorized to execute the undertaking within the state, or (2) a natural person, except an attorney, who executes with the undertaking his affidavit setting forth his full name and address and that he is domiciled within the state and worth at least the amount specified in the undertaking exclusive of liabilities of property exempt from application

> to the satisfaction of a judgment.[49]

For undertakings of more than $1,000, which are not deposits of legal tender of the United States or bonds, and upon which a natural person is a surety, CPLR 2503 provides that such undertakings must be secured by real property located in the state that is worth the amount specified in the undertaking exclusive of encumbrances.[50] This undertaking will create a lien on the real property when recorded in the individual-surety-bond-liens docket where the real property is located.[51]

III. Protecting the Seller

A. Suggestions

Given the potential difficulty and cost in having a notice of pendency cancelled, a purchaser may effectively tie up a seller's property regardless of the merits of purchaser's claims.[52] A seller who cannot afford to have the property tied up until the dispute is resolved will be anxious to remove the lien quickly. The uncertain requirements of CPLR 6515 do not promise a quick resolution unless the seller is prepared to post a potentially significant undertaking and the purchaser does not, in turn, post its own undertaking. The purchaser has little to lose by filing a notice of pendency, and by making such a filing it gains substantial leverage to demand the return of some or all of its contract deposit.

Accordingly, it may be advisable under certain circumstances (such as the circumstances in which our elderly client found herself) for a property owner to address this problem by seeking an express waiver in the sale/purchase agreement of the purchaser's right to file a notice of pendency in the event of a dispute under the contract. Here is sample waiver language:

> Purchaser acknowledges and represents that it is purchasing the Premises solely for investment purposes and that from Purchaser's perspective there is nothing particularly unique about the Premises. Purchaser hereby irrevocably waives the right to file a notice of pendency (under Section 6501 of the New York Civil Practice Law and Rules or otherwise) in connection with any dispute, claims, actions, or proceedings arising under or related to this Agreement and the transactions contemplated hereby. Purchaser's filing a notice of pendency shall constitute a material breach by Purchaser entitling Seller to (a) terminate this Agreement, (b) demand and receive the Deposit from the Escrow Agent as liquidated damages for such breach (Purchaser agreeing that the amount of Seller's damages from the filing of such notice of pendency may be material and are difficult to quantify, and that the amount of the Deposit is a reasonable estimate of the possible damages that Seller may suffer therefrom), (c) obtain a dismissal of Purchaser's action, and (d) obtain a court order canceling the notice of pendency without posting any undertaking that might otherwise be required under Section 6515 of the New York Civil Practice Law and Rules or otherwise. If Purchaser files a notice of pendency for any reason, Escrow Agent may rely on this waiver and shall have no liability whatsoever if Escrow Agent releases the Deposit to Seller, and Purchaser shall be deemed to have waived (x) any and all claims that Purchaser may have against Seller and Escrow Agent, and (y) any right to receive a return of the Deposit.

Alternatively, the seller could permit the purchaser to file a notice of pendency if a dispute arises but only if the purchaser posts an additional contract deposit with the escrow agent under the contract at the time of filing a notice of pendency. This forces the purchaser to "put its money where its mouth is," discouraging a purchaser with a weak claim from filing a notice of pendency. Here is sample language for such a provision:

> If any dispute arises and litigation ensues between Purchaser and Seller in connection with this Agreement, Purchaser shall deposit with Escrow Agent an additional deposit of $________ before and as a condition to Purchaser's filing a notice of pendency (in addition to all conditions provided by applicable law). Such additional deposit shall be added to and become a part of the Deposit for all purposes hereunder and shall constitute a reasonable estimate of the possible damages that Seller may suffer as a result of the additional period of time that the property may become unmarketable while a notice of pendency is in place, such damages being material and difficult to quantify. Purchaser's failure to provide the additional deposit described in this paragraph before filing a notice of pendency shall constitute a material breach by Purchaser entitling Seller to (a) terminate this Agreement, (b) demand and receive the Deposit from the Escrow Agent as

liquidated damages for such breach, (c) obtain a dismissal of Purchaser's action, and (d) obtain a court order canceling the notice of pendency without posting any undertaking that might otherwise be required under Section 6515 of the New York Civil Practice Law and Rules or otherwise. If Purchaser files a notice of pendency without providing such additional deposit, Escrow Agent may rely on this provision and shall have no liability whatsoever if Escrow Agent accordingly releases the Deposit to Seller, and Purchaser shall be deemed to have waived (x) any and all claims that Purchaser may have against Seller and Escrow Agent, and (y) any right to receive a return of the Deposit.

This requirement could be coupled with an additional provision that would require the purchaser to pay the seller's legal fees for litigation concerning the notice of pendency. If the purchaser believes that it has a valid claim, and the purchaser has the funds available, this is a reasonable position for the parties to take in appropriate circumstances.

As another alternative, the parties may consider contractually agreeing to the amount of the seller's undertaking under CPLR 6515(1), upon which posting the parties agree that a court should cancel a notice of pendency, along the lines of the following: "Seller's providing an undertaking of $________ shall constitute adequate relief securing Purchaser within the meaning of section 6515(1) of the N.Y. Civil Practice Law and Rules. Upon Seller's providing such an undertaking, a court should cancel any notice of pendency that purchaser may have filed in connection with the real property."

Of course, the purchaser's readiness to agree to any of these options will be a function of its negotiating leverage.

B. Enforceability of Suggested Provisions

What if the purchaser files a notice of pendency despite the purchaser's waiver of its right to do so or the purchaser's failure to provide an additional deposit as required in the sale/purchase agreement? It is unclear whether or how a court will enforce these contractual provisions because there are no reported cases on point. Presumably, the parties are free to contract on these issues. The suggested provisions, including the provision concerning an agreed-upon amount of undertaking for cancellation of the notice of pendency, might also provide a factual basis for the court's consideration in cancelling the notice of pendency or requiring an additional deposit in light of the equities of the case, under a view that the purchaser would not have waived its rights under Article 65 of the CPLR if the purchaser considered the property specifically unique or that the purchaser's failure to abide by its agreement demonstrates bad faith.

The purchaser's counsel should note that by waiving the purchaser's right to file a notice of pendency, the purchaser may effectively relinquish its right to obtain specific performance of the seller's obligation to sell to the purchaser. No constructive notice of the purchaser's legal action would have been provided pursuant to CPLR Article 65, so a subsequent good faith purchaser/mortgagee for value may take free of the consequences of the litigation.[53] The purchaser may still be able to obtain specific performance if it can prove that the subsequent purchaser/mortgagee had actual notice.[54] Even where the purchaser cannot obtain an order of specific performance, if its claim in the action is meritorious, it may recover damages against the seller (assuming that the purchaser did not expressly waive its right to recover damages in the sale/purchase agreement).[55]

IV. Conclusion

Where does this leave our elderly client who needs to sell her property? Absent proper counseling and planning, she will be exposed to risk if confronted with an aggressive buyer who decides after signing (or perhaps before) that he does not wish to proceed with the transaction at the contracted price. The suggested contract provisions should eliminate or at least reduce her exposure.

Endnotes

1. N.Y. CPLR 6501 (McKinney Supp. 2009).
2. *Id.* (indicating that "[t]he pendency of such an action is constructive notice, from the time of filing of the notice only, to a purchaser from, or incumbrancer against, any defendant named in a notice of pendency indexed in a block index against a block in which property affected is situated or any defendant against whose name a notice of pendency is indexed"); *see, e.g.*, *Grid Realty Corp. v. Winokur*, 43 N.Y.2d 956, 957, 375 N.E.2d 376, 376, 404 N.Y.S.2d 315, 315 (1978) (concluding that a filed notice of pendency gave plaintiffs constructive notice of a foreclosure action and bound plaintiffs to the same extent as if they had been parties to the action).
3. *See Colombo v. Caiati*, 129 Misc. 2d 338, 340, 493 N.Y.S.2d 244, 246 (Sup. Ct. Rockland County 1985) (stating that a notice of pendency does not create a lien and does not restrain the conveyance of land, though an adverse judgment may affect title to the land).
4. *In re Sakow*, 97 N.Y.2d 436, 440–41, 767 N.E.2d 666, 669–70, 741 N.Y.S.2d 175, 178–79 (2002):

   > [T]he common–law lis pendens doctrine was replaced in most states by statutes requiring the filing of a notice of pendency before a would–be purchaser or encumbrancer would be charged with notice of the prior interest. This substantially reduced the harshness of the common–law rule because the notice of pendency was filed with the records pertaining to the real property itself, and third persons were charged with knowledge only of what appeared in those records. The

statutory filing requirement first appeared in New York in 1823, and continues in its current statutory expression in CPLR article 65.

See e.g., *Da Silva v. Musso*, 76 N.Y.2d 436, 440 n.1, 559 N.E.2d 1268, 1269 n.1, 560 N.Y.S.2d 109, 110 n.1 (1990) ("This filing procedure [of CPLR article 65] was adopted to mitigate the harshness of the former common–law rule, which bound the purchaser to the outcome of litigation pending at the time of the purchase, regardless of whether the purchaser had actual knowledge of, or even the practical means to discover, the existence of the pending action.").

5. *See Da Silva*, 76 N.Y.2d at 442, 559 N.E.2d at 1271, 560 N.Y.S.2d at 112 (stating that "CPLR 6501 permits a plaintiff who has commenced an action potentially affecting title to or the use and enjoyment of real property to file a notice of pendency, and thereby impair its marketability, *as a matter of right*").

6. *See* N.Y. CPLR 6501 (McKinney Supp 2009) (stating that "[a] notice of pendency may be filed in any action in a court of the state or of the United States . . . except in a summary proceeding brought to recover the possession of real property").

7. *See id.* (recognizing that "[a] notice of pendency may be filed in any action in a court of the state or of the United States . . . .").

8. *See Diaz v. Paterson*, 547 F.3d 88, 99–100 (2d Cir. 2008), *cert. denied*, 129 S. Ct. 2789 (2009) (stating that a "mere good–faith standard" used by the CPLR does not constitute a violation of due process).

9. *See* N.Y. CPLR 6511(a) (McKinney Supp. 2009) (noting that "[i]n a case specified in section 6501, the notice of pendency shall be filed in the office of the clerk of any county where property affected is situated, before or after service of summons and any time prior to judgment").

10. *See* N.Y. CPLR 6511(b) (McKinney Supp. 2009).

11. *See In re Sakow*, 97 N.Y.2d 436, 441, 767 N.E.2d 666, 670, 741 N.Y.S.2d 175, 179 (2002) (indicating that the New York Court of Appeals "require[s] strict compliance with the statutory procedural requirements [of CPLR article 65]").

12. *See* N.Y. CPLR 6511(a) (McKinney Supp. 2009).

13. *See* N.Y. CPLR 3019(d) (McKinney Supp. 2009) (providing that a cause of action contained in a counterclaim or a cross–claim must be treated as if it were contained in a complaint).

14. N.Y. CPLR 6512 (McKinney Supp. 2009) (defining when a notice of pendency is effective in relation to the summons being served); *see Israelson v. Bradley*, 308 N.Y. 511, 515–16, 127 N.E.2d 313, 315 (1955) (holding that the plaintiff could not file a second notice of pendency for the same cause of action, where a court had already canceled the same cause of action first filed by the plaintiff and the notice of pendency for a lack of service of summons).

15. *See Diaz v. Paterson*, 547 F.3d 88, 99–100 (2d Cir. 2008), *cert. denied*, 129 S. Ct. 2789 (2009) (analyzing the constitutionality of CPLR 6514(b) and its lack of a bond requirement).

16. *See Chappelle v. Gross*, 26 A.D.2d 340, 343, 274 N.Y.S.2d 555, 559 (1st Dep't 1966) (citing *Hauser v. Bartow*, 273 N.Y. 370, 7 N.E.2d 268 (1937)) (acknowledging the tort of malicious prosecution, where a person uses a notice of pendency not for its legislatively intended purpose, but for a collateral object to damage another party). A discussion of a property owner's potential recourse against a notice filer for damages incurred as a result of the filing of a notice of pendency where the notice filer is ultimately unsuccessful in the litigation or chooses ultimately to default under the sales contract after filing a notice of pendency is beyond the scope of this article.

17. *See* N.Y. CPLR 6513 (McKinney 1980).

18. *See id.* (noting that "[b]efore expiration of a period or extended period, the court, upon motion of the plaintiff and upon such notice as it may require, for good cause shown, may grant an extension for a like additional period"); *In re Sakow*, 97 N.Y.2d 436, 442, 767 N.E.2d 666, 670–71, 741 N.Y.S.2d 175, 179–80 (2002) ("A notice of pendency is valid for three years from the date of filing and may be extended for additional three-year periods upon a showing of good cause."); *see also MCK Bldg. Assocs. v. St. Lawrence Univ.*, 5 A.D.3d 911, 912, 773 N.Y.S.2d 475, 476 (3d Dep't 2004) (holding that a mechanic's lien and the notice of pendency that extends it, expire if the plaintiff fails to obtain an extension of the notice pursuant to CPLR section 6513). *But see* N.Y. CPLR 6516 (McKinney Supp. 2009) (permitting successive notices of pendency in foreclosure actions defined therein); *Campbell v. Smith*, 309 A.D.2d 581, 582, 768 N.Y.S.2d 182, 183 (1st Dep't 2003) (permitting successive notices of pendency for prosecuting mortgage foreclosure action).

19. *See Grid Realty Corp. v. Winokur*, 43 N.Y.2d 956, 957, 375 N.E.2d 376, 376, 404 N.Y.S.2d 315, 315 (1978) (holding that the defendant was bound by a foreclosure action because the notice of pendency gave him constructive notice).

20. *See Patterson v. Brown*, 32 N.Y. 81, 96 (1865) ("Courts of equity do not relieve a party from the consequences of risks that he thus voluntarily assumes."). But note that the N.Y. Court of Appeals has found an exception to the general rule that a purchaser of real property will be bound by litigation of which the purchaser has actual knowledge at the time of the conveyance. *See Da Silva v. Musso*, 76 N.Y.2d 436, 438, 559 N.E.2d 1268, 1268–69, 560 N.Y.S.2d 109, 109–10 (1990) (holding that a purchaser of real property with actual knowledge of a pending (ultimately successful) appeal against the real property did not take subject to such litigation, where the original complaint in such litigation had been dismissed earlier on the merits and no notice of pendency or stay was in place). *But cf. Marcus Dairy v. Jacene Realty Corp.*, 298 A.D.2d 366, 368, 751 N.Y.S.2d 237, 239 (2d Dep't 2002) (holding that, where a notice of pendency had been vacated, but where the first mortgagee ultimately had been successful on appeal, a first mortgagee would have priority over a second mortgagee after weighing the fact that the first mortgagee had sought a stay, but the stay was denied and the first mortgagee, otherwise, would have no remedy). The *Da Silva* court's holding further underscores the fact that the common–law *lis pendens* doctrine has been replaced by the statutory notice–of–pendency framework. *Cf. Gaugert v. Duve*, 628 N.W.2d 861, 873, 244 Wis.2d 691, 713 (Wis. 2001) (rejecting the *Da Silva* court's reasoning on the basis of the lack of "any intent [in Wisconsin's statutory lis pendens] to abandon the application of common law principles of lis pendens").

21. *See, e.g.*, *2386 Creston Ave. Realty v. M-P-M Mgmt. Corp.*, 58 A.D.3d 158, 160–61, 867 N.Y.S.2d 416, 418–19 (1st Dep't 2008) (holding that "[a]lthough New York is a 'race-notice' state, plaintiff's failure to avail itself of the protection of either § 291 or § 294 deprives it of the right to substitute a notice of pendency for the recording of a conveyance or a contract") (citing *Avila v. Arsada Corp.*, 34 A.D.3d 609, 610, 826 N.Y.S.2d 322, 323 (2d Dep't 2006); *Finkleman v. Wood*, 203 A.D.2d 236, 238, 609 N.Y.S.2d 655, 657 (2d Dep't 1994)); *LaMarche v. Rosenblum*, 50 A.D.2d 636, 636–37, 374 N.Y.S.2d 443, 444–45 (3d Dep't 1975) (holding that a sale of real property to third parties would not be disturbed where the plaintiff filed an action for specific performance and a notice of pendency after the defendant contracted to sell the property to the third parties but before the third parties recorded their contract of sale, on the grounds that the plaintiff would "not now be heard to argue that his filing of a notice of pendency serves as a substitute [for recording his purchase contract under subdivision 3 of section 294 of the Real Property Law] and affords him the same protection since such notices have as their general object the preservation of existing property rights during litigation").

22. *2386 Creston Ave.*, 58 A.D.3d at 161, 867 N.Y.S.2d at 419 (citing *Varon v. Annino*, 170 A.D.2d 445, 445, 565 N.Y.S.2d 540, 541 (2d Dep't 1991)).

23. 58 A.D.3d 158, 867 N.Y.S.2d 416 (1st Dep't 2008).

24. *Id.* at 160, 867 N.Y.S.2d at 419 (citing 11 Warren's Weed New York Real Property § 115.04 (5th ed. 2004)).

25. *See* N.Y. CPLR 5523 (McKinney 1995) (providing that the court may not order restitution of property or rights lost by a prior court order ultimately reversed or modified if the title of such property of a purchaser in good faith and for value would be affected; in that case, the court may order only that the value or the purchase price be restored or deposited in court). *But cf. Da Silva*, 76 N.Y.2d at 442, 559 N.E.2d at 1271, 560 N.Y.S.2d at 112 (noting that "the 'good faith' [under CPLR 5523] of a purchaser who has acquired the property for value during the pendency of claimant's appeal is not vitiated by the purchaser's actual knowledge of the appeal," where the notice of pendency had been cancelled).

26. *In re Sakow*, 97 N.Y.2d, 436 441, 767 N.E.2d, 666 670, 741 N.Y.S.2d 175 179 (quoting *Da Silva*, 76 N.Y.2d at 442, 559 N.E.2d at 1268, 560 N.Y.S.2d 109, *5303 Realty Corp. v. O & Y Equity Corp*., 64 N.Y.2d 313, 476 N.E.2d 276 (1984), and *Israelson v. Bradley*, 308 N.Y. 511, 516, 127 N.E.2d 313, 315 (1955)).

27. *See Da Silva v. Musso*, 76 N.Y.2d 436, 442, 559 N.E.2d 1268, 1271, 560 N.Y.S.2d 109, 112 ("[T]he claim on which the notice of pendency is based need not necessarily be a meritorious one.") (referencing Joseph M. McLaughlin, McKinney Practice Commentary, N.Y. CPLR 6501 (McKinney 1987)).

28. Conn. Gen. Stat. § 52–325b(a) (2005) (requiring that the notice filer "establish that there is probable cause to sustain the validity of his claim").

29. N.J. Stat. Ann. § 2A:15–7(b) (West 2000).

30. *Diaz v. Paterson*, 547 F.3d 88, 99–100 (2d. Cir 2008).

31. Joseph M. McLaughlin, McKinney Practice Commentary, N.Y. CPLR 6515 (McKinney 1980).

32. *Id.*

33. *See* N.Y. CPLR 5519(c) (McKinney 1995) (providing that "[t]he court from or to which an appeal is taken or the court of original instance may stay all proceedings . . . .").

34. *See, e.g.*, *Marcus Dairy v. Jacene Realty Corp*., 298 A.D.2d 366, 368, 751 N.Y.S.2d 237, 239 (2d Dep't 2002). The Second Department held that a first mortgagee had priority over a second mortgagee, even though the second mortgage had been entered into after the dismissal of a notice of pendency filed by the first mortgagee, in part based upon the fact that the ultimately successful appellant first mortgagee would have had no effective remedy if it were to lose its priority, whereas the second mortgagee had a claim against its title insurance company. The court so held, even though, similar to the facts of *Da Silva*, the lower court had vacated the first mortgagee's notice of pendency, and further directed that the first mortgage be cancelled and discharged of record, and no CPLR 5519 stay of the lower court's judgment was in place during the first mortgagee's ultimately successful appeal of the case—but a stay had been sought, unlike in *Da Silva*. The lower court's judgment had been entered into the county clerk's office and the notice of pendency had been cancelled, but the judgment was never actually recorded in the land records, and, consequently, the first mortgage was never discharged of record. Interestingly, when the title company insured the second mortgage, it had discovered that the first mortgage still existed as an open item in the land records, but insured title without excepting the first mortgage in light of (1) the canceled notice of pendency, and (2) the holding of the N.Y. Court of Appeals in *Da Silva*, that actual knowledge did not vitiate the good faith of a purchaser acquiring property for value during a pending appeal where the notice of pendency had been cancelled because no CPLR 5519 stay was in place during the appeal. [Editor's Note: This case is also discussed in Bruce J. Bergman, "Oh, Do Lenders Need Title Insurance!", which appears on page 42 of this *Journal*.]

35. *See* N.Y. CPLR 6514(a), (b) (McKinney 1980) (defining mandatory cancellation in section 6514(a), and defining discretionary cancellation in section 6514(b)).

36. *See* N.Y. CPLR 6514(a) (McKinney 1980).

37. N.Y. CPLR 6514(b); *see also*, *e.g.*, *Israelson v. Bradley*, 308 N.Y. 511, 516, 127 N.E.2d 313, 315 (1955) (canceling a second notice of pendency filed for the same cause of action brought in Supreme Court, where the County Court had already canceled the plaintiff's first filed action and notice of pendency for failure to serve summons and complaint).

38. *5303 Realty Corp. v. O & Y Equity Corp*., 64 N.Y.2d 313, 320, 476 N.E.2d 276, 280, 486 N.Y.S.2d 887, 881 (1984) (citing I*nterboro Operating Corp. v. Commonwealth Sec. & Mortgage Corp*., 269 N.Y. 56, 59, 198 N.E. 665, 666 (1935); *Keating v. Hammerstein*, 196 A.D. 18, 21, 187 N.Y.S. 446, 448 (1st Dep't 1921); *J. Henry Small Realty Co. v. Barnett Strauss*, 162 A.D. 658, 659, 147 N.Y.S. 478, 478 (2d Dep't 1914); *Brox v. Rike*r, 56 A.D. 388, 391, 67 N.Y.S. 772, 774 (1st Dep't 1900)); *see also Interboro Operating Corp.*, 269 N.Y. at 59, 198 N.E. at 666 ("[N]otice of pendency may not be canceled for the reason that a court, looking into the future, may conclude that plaintiff will not on the merits finally prevail. So long as this action is pending, the notice may not be canceled.") (citing *Schomacker v. Michaels*, 189 N.Y. 61, 65, 81 N.E. 555, 556 (1907); *Beman v. Todd*, 124 N.Y. 114, 116, 26 N.E. 326, 327 (1891); *Mills v. Bliss*, 55 N.Y. 139, 141 (1873); *St. Regis Paper Co. v. Santa Clara Lumber Co.*, 62 A.D. 538, 538, 71 N.Y.S. 82, 82 (3d Dep't 1901)).

39. N.Y. CPLR 6515 (McKinney Supp. 2009).

40. *See*, *e.g.*, *Weiss v. Alard*, 150 F. Supp. 2d 577, 583–84 (S.D.N.Y. 2001) (maintaining a notice of pendency under CPLR 6515(2) because the notice filer offered to post undertaking, but noting that the notice filer need not post an undertaking, and notice of pendency will stay in place, if property owner fails to post undertaking); *Ansonia Realty Co. v. Ansonia Assocs*., 117 A.D.2d 527, 527–28, 498 N.Y.S.2d 141, 142 (1st Dep't 1986) (affirming the cancellation of the notice of pendency if property owner posts bond and notice filer does not "opt to retain the notice" by filing undertaking); *Weksler v. Yaffe*, 129 Misc. 2d 633, 637–38, 493 N.Y.S.2d 682, 686 (Sup. Ct. Kings County 1985) (stating that notice filer may maintain notice by posting undertaking, and if notice filer does not post undertaking, notice will be canceled upon property owner's posting of undertaking because property was not unique). *See also* Joseph M. McLaughlin, McKinney Practice Commentary N.Y. CPLR 6515, at 1 (McKinney 1980) (questioning whether every notice filer should be required to post an undertaking to indemnify the property owner/seller without first requiring the property owner/seller to put up an undertaking). In fact, a four–member plurality of the Supreme Court reached the (non–precedential) conclusion that the absence of a bond requirement in Connecticut's prejudgment attachment statute violated due process, *see Connecticut v. Doehr*, 501 U.S. 1, 1–3, 111 S.Ct. 2105, 2107–08, 115 L. Ed. 2d 1, 2 (1991). *But see Diaz v. Paterson*, 547 F.3d 88, 100 (2d Cir. 2008) (rejecting the property owners' claim that due process required that the notice filer post a bond in every case).

41. *See Weiss*, 150 F. Supp. 2d at 583 (S.D.N.Y. 2001) ("New York courts have held that 'double–bonding' is '[p]referable even when plaintiff's likelihood of success is doubtful.'") (quoting *Andesco v. Page*, 137 A.D.2d 349, 357, 530 N.Y.S.2d 111 (1st Dep't 1988)).

42. *See, e.g.*, *id*.

43. *See, e.g.*, *Ansonia Realty*, 117 A.D.2d at 527–28, 498 N.Y.S.2d at 142 (holding that the amount of undertaking should be the amount of damages that each party would suffer); *Weklser*, 129 Misc.2d at

638, 493 N.Y.S.2d at 686 (holding that undertakings should be the amount of damages in light of the weakness of defendant's case).

44. 150 F. Supp. 2d 577, 583 (S.D.N.Y. 2001) ("The amount of the respective undertakings is a matter of discretion to be informed by the pleadings, the acts of the parties and the circumstances set forth in their affidavits.") (quoting *Ronga v. Alpern*, 45 Misc. 2d 1029, 1031, 258 N.Y.S.2d 731 (Sup. Ct. Bronx County 1964)).

45. *See Weiss,* at 584.

46. *See Ansonia Realty*, 117 A.D.2d at 527–28, 498 N.Y.S.2d at 142 (holding that seller's undertaking would be $2.5 million as the amount of the purchaser's potential damages, and purchaser's undertaking would be $4 million rather than the $38.5 million balance of the purchase price).

47. 129 Misc. 2d 633, 638, 493 N.Y.S.2d, 682 686 (Sup. Ct. Kings County 1985).

48. *See Weksler v. Yaffe*, 129 Misc. 2d 633, 637, 493 N.Y.S.2d 682, 686 (Sup. Ct. Kings County 1985) (quoting N.Y. CPLR 2501); *see also* N.Y. CPLR 2501 (McKinney 1991).

49. N.Y. CPLR 2502 (a) (McKinney 1991) (defining surety).

50. *See* N.Y. CPLR 2503(a) (McKinney 1991) (defining an undertaking of more than one thousand dollars).

51. *See id.*

52. *See, e.g.*, *Da Silva v. Musso*, 76 N.Y.2d 436, 442, 559 N.E.2d 1271, 1271, 560 N.Y.S.2d 109, 112 (1990) (stating that a claim for a notice of pendency need not be meritorious).

53. *See* N.Y. Real Prop. Law §§ 291, 294(3) (McKinney 2006) (stating that any conveyance of real property not recorded is void against any subsequent good faith purchaser who duly first records the conveyance); N.Y. CPLR 5523 (McKinney 1995) (stating that a court reversing a final judgment of lost property rights may order restitution except where the title of a good faith purchaser may be affected); *2386 Creston Ave. Realty v. M–P–M Mgmt. Corp.*, 58 A.D.3d 158, 160, 867 N.Y.S.2d 416, 418–19 (1st Dep't 2008) (arguing that "[w]hen two or more prospective buyers contract for a certain property, pursuant to Real Property Law §§ 291 and 294, priority is given to the buyer whose conveyance or contract is first duly recorded.").

54. *See, e.g.*, *Da Silva*, 76 N.Y.2d at 439, 559 N.E.2d at 1270, 560 N.Y.S.2d at 110 (holding that "a purchaser of real property is bound by the consequences of a lawsuit of which he has actual knowledge," and that a notice of pendency can be filed to bind a subsequent purchaser to the extent as if he were a party to the action).

55. *See* N.Y. CPLR 5523 (stating that "A court reversing or modifying a final judgment or order or affirming such a reversal or modification may order restitution of property or rights lost by the judgment or order, except that where the title of a purchaser in good faith and for value would be affected, the court may order the value or the purchase price restored or deposited in court."); *see also Da Silva*, 76 N.Y.2d at 440-41, 559 N.E.2d at 1270, 560 N.Y.S.2d at 111 (noting that a plaintiff may obtain only "monetary relief in cases where the owner has exercised his rights under the unstayed judgments and transferred the property to a 'good faith' purchaser for value.").

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Top Ten Reasons Closings Are Adjourned

By Peter Brogan

You can almost hear the cheers when a real estate closing is scheduled. For starters, there aren't that many of them these days, but more importantly a closing is usually a happy occasion for all involved.

But what happens when things go wrong, so gravely wrong that the closing must be adjourned?

The buyers and sellers leave the conference room in confusion and disbelief, and the domino effect of an aborted buy-sell can affect closings from Westchester to California.

Identifying the problems in advance can avert these tragedies.

Quite often the causes for these adjournments are practical rather than legal. The buyer does not bring homeowners insurance; or the seller neglects to obtain a payoff letter for his mortgage. Hopefully, we don't sink to a seller bringing a Derek Jeter baseball card as photo ID.

In this scholarly forum, we will focus primarily on the statutory and case law authority that can bring a closing to a grinding halt.

With that said, let's examine the "Top Ten Reasons Closings are Adjourned."

Reason Number Ten

An executor or administrator gives a power of attorney to a third party. No! Fiduciaries cannot delegate their authority.

"The duty of a fiduciary is Personal and cannot be divested by delegation."[1]

A decedent, for example, has placed his trust in the appointed executor.

An executor, guardian, or other person acting in a fiduciary capacity can delegate the performance of mere mechanical or ministerial acts to others by power of attorney.

So, a title company will not accept a deed executed by the attorney-in-fact of an executor, but will accept a transfer tax return, as a ministerial act, when signed by that same attorney-in-fact.

A fiduciary who can't or won't act should resign.[2]

A corollary to this reason for adjournments, and equally as devastating, is situations when a fiduciary cannot act at all.

A deed which conveys directly to the trust rather than to "John Smith as trustee of the Brown Qualified Personal Residence Trust" has conveyed nothing. Title remains in the grantor (who, invariably, is now deceased).[3]

Can this closing be saved? Unless the fiduciary or grantor to the trust is in close proximity to the closing, this will be adjourned.

Reason Number Nine

Seller does not come to closing with certified funds for transfer taxes. No! Title companies will not take a personal check for transfer taxes unless authorized prior to closing.

Under the contract, the party charged by statute is required to pay the transfer taxes by "certified or official bank check."

As a result, the seller is required to pay both the New York City transfer tax,[4] and the New York State transfer tax.[5]

Unfortunately, these are not the only transfer taxes the practicing real estate attorney must be aware of these days.

New York State also imposes a "mansion tax" of one percent on certain residential properties having a consideration of one million dollars or more.

The statute calls for the purchaser to pay the mansion tax.[6]

In this area, two other municipalities impose transfer tax on the seller, Yonkers[7] and Mount Vernon.[8]

Another nasty surprise may await the attorney who does not regularly practice in certain areas of Suffolk County. It is known as the "Peconic Bay Region" transfer tax. This is a two percent tax (with small allowances) and is payable by the buyer.

As an example, a three million dollar cottage in East Hampton will result in a tax of fifty-five thousand dollars. Not a small number, even for someone with the wherewithal to afford a three million dollar summer house.

The burden of payment of all transfer taxes can be completely shifted, or shared, by negotiation between the parties. No such negotiation can take place if the parties are not made aware of the taxes by their attorneys.

Can this closing be saved?

Possibly. The party responsible for paying the tax could use a credit card, or the title closer might be able to verify the funds with the bank.

Reason Number Eight

The buyer (and his attorney) is not aware that the lending institution will deduct the buyer's closing costs of $10,017.60 from the mortgage proceeds of $200,000. Instead of having the full mortgage proceeds available to the seller, the buyer puts a personal check for $10,017.60 on the table. No! The contract calls for the balance of the purchase price to be in certified funds. This is the "Net Proceeds Trap."

The solution, of course, is for the buyer's attorney to obtain from the bank the exact amount that will be available to buyer at closing.

With mortgage documents often being emailed to the lender's attorney ten minutes after the closing starts, it is difficult for the buyer to get to his bank in advance to obtain the correct certified checks.

And that is all that has really changed. The buyer still owes the seller the same amount. It is the form in which it is delivered at closing. Even if the seller likes the pictures on the buyer's checks, it could be malpractice for the seller's attorney to accept a personal check in that amount.

With the help of a "Truth in Lending" statement and the title company, the buyer's attorney should be able to calculate the net proceeds available.

The "seller's concession" is an adjunct to this problem concerning certified funds.

The contract price is inflated to include a credit of $20,000 for repairs (the concession). The repairs are almost always imaginary, but the result is 100 percent financing or more.

If the concession is fully disclosed to the bank, all appears to be well. If, however, the bank was not made aware of the concession then the lender's attorney will be looking for the amount of the concession in the form of certified funds in order to bridge the gap between the mortgage and contract price, and will not disburse until he sees it.

The collapse of the sub-prime mortgage market will, in all likelihood, put an end to most seller's concessions.

An alarming trend in ethics opinions began in New Jersey. In 2006, a New Jersey Ethics Opinion disciplined the Buyer's and Seller's attorneys for participating in a real estate transaction which had a "Seller's Concession" built into the purchase price. Despite the fact that full disclosure was made to the originating bank, the NJ Committee on Professional Ethics held that a lender acquiring the loan in the secondary market could be deceived. See N.J. Opinion 710.

New York has now (11-2-07) issued a similar opinion. See Opinion 817. "Participation in residential real estate transactions that include a "seller's concession" and "grossed up" sales price is prohibited unless the transaction is entirely lawful, the gross-up is disclosed in the transaction documents, and no parties are misled to their detriment:" NY Opinion 817.

There is much room for interpretation in the opinion. What is meant by "transaction documents?" Must the deed contain a recital concerning the concession so that there is record notice? Would a bank relying on an appraisal, which, in turn, relied on a grossed-up purchase price of an adjoining property, be considered as a party misled to their detriment? What has always been a slippery slope is now a sheet of ice. In a market looking for solutions this could be a serious roadblock.

Can this closing be saved? In the case of the net proceeds trap, the best thing that can happen is that the parties and attorneys agree to have a cup of coffee while the buyer goes to his bank to get certified or bank checks, if not the closing will be adjourned with attendant adjournment fees charged to the buyer.

If a seller's concession is not disclosed to the bank, the closing will almost certainly be adjourned. And in light of the recent ethics opinion lawyers who practice in this field must reflect on their ethical obligations.

Reason Number Seven

The executor of an unprobated will arrives at closing to execute the deed. No! Without Letters Testamentary this person has no standing.

The authority of an executor to convey real property originates in EPTL 11-1.1, Fiduciaries' Powers, and more specifically EPTL 11-1.1(b)5(B). "With respect to any property or any estate therein owned by an estate or trust, except where such property or any estate therein is specifically disposed of: B. to sell the same at public or private sale. . . "A fiduciary is a personal representative, that is, a person who has *received letters* to administer the estate of a decedent. A preliminary executor also has the authority to convey real property. "An executor named in a will has no power to dispose of any part of the estate of the testator before letters testamentary or preliminary letters testamentary are granted . . ."[9]

Can this closing be saved? Only if luck brings all the heirs of the testator to the closing. They could then convey, pursuant to an affidavit of heirship. The proceeds could be held in escrow until letters are obtained, or to guarantee compliance with any of the terms of the will.

Reason Number Six

A Religious Corporation arrives at closing without a Supreme Court order authorizing the sale. No! Without such an order, the conveyance is void.

A religious corporation is more heavily regulated than a Not-for-Profit. So the organizational documents of the entity must be examined in order to determine the requirements placed on the property owner. Never rely on the client for this information. Since September 1, 1972, the Not-for-Profit Corporation law applies to religious corporations. In addition to court approval, the consent of two-thirds of the directors to the sale must be obtained.

"A religious corporation shall not sell, mortgage or lease for a term exceeding five years any of its real property without applying for and obtaining leave of the Court."[10]

The intent, of course, is to protect the congregation from the dissipation of church assets. This requirement extends to *all* property owned by the religious corporation, not merely the property used as a place of worship.

A mortgage also requires a court order. Without an authorizing order, the mortgage cannot be foreclosed. A purchase money mortgage does not require a court order.

The lack of a comma in the correct place in the statute has caused the erroneous belief that a mortgage for a term of less than five years does not require a court order. This is not true.

All mortgages of real property owned by a religious corporation require a court order except purchase money mortgages.

Strict compliance with the order approving the transaction is required. If the contract or mortgage terms are amended, so must be the court order.[11]

A title company will not insure a mortgage or conveyance by a religious corporation absent a court order. This is something you cannot throw money at to make it go away in order to close.

So closely related are Not-for-Profit corporations that the requirements for conveyances or their real property should be examined.

Although there are four types of Not-for-Profit corporations, only Type B and C require court orders for the sale of all or substantially all of the assets of those types of Not-for-Profits.[12] Mortgages made by Not-for-Profit corporations, even upon all or substantially all of their assets, do not require a court order.

Can this closing be saved? No! If a court order is required, the closing will be adjourned.

Reason Number Five

Seller arrives at closing with a payoff letter showing legal fees due. No! This means seller is in default of his mortgage and must act in compliance with the Home Equity Theft Protection Act.

Effective February 1, 2007, the Act amends Section 595-a of the Banking Law, Section 295-a of the Real property law, and adds new section 1303 to the Real Property Actions and Proceedings Law.

The Act requires among many other things:

- notice in the contract that the equity seller can cancel the contract within five business days.
- provision of a form to cancel the contract.
- a complete description of the payments that will be given to the 'equity seller' in return for his home.
- a description of the services the 'equity purchaser' will provide.
- the terms of any lease, if the 'equity seller' may remain in the house.
- the term of any buy back agreement.
- if Spanish is the "equity seller's" primary language, the contract must be in Spanish.
- contract must be in 12 point print.

The Act is triggered by a default in the "equity seller's" mortgage or taxes if it is two months in arrears.

Title companies are strictly construing these transactions due to the fact that any "equity seller" can cancel a transfer that is in material violation of the Act for two years after the recording of the deed.

Purchasers who will use the house as their primary residence are exempt from the Act. There are a number of other exemptions.

Can this closing be saved? No, at this point in time such titles are insurable.

Reason Number Four

The intestate decedent owner's daughter, who lives in the house, arrives at closing to execute the deed. No.! Either an administrator or* all *the heirs must convey the property.

It has happened that at closing the daughter admits that she has a brother, but that he has no interest in the property. Of course, legally, he certainly has a fifty percent interest in the property. His sister means he is 'not interested' in the property.

Notwithstanding, the legal interest of all intestate heirs must be disposed of at closing by execution of the deed.

Where a decedent leaves no will he dies intestate. A fiduciary known as an administrator can be appointed to handle the decedent's affairs.[13]

Where an administrator is the seller of the property, a bond in the amount of the purchase price must be posted to protect the other heirs.[14]

If there are no heirs, the People of the State of New York become the owners, and only the Public Administrator can convey.[15]

Title companies do not put simple estates through the expense and time of an administration proceeding, but will accept an affidavit of heirship. After all, an administration proceeding is little more than a formal affidavit of heirship.

In the *Matter of Connolly*, a 1988 Nassau County surrogates court case, the Court stated that it would not entertain an administration proceeding in these simple single asset cases, "In intestacy, decedent's real property devolved by operation of law to her distributes at the time of her death . . . ," the distributees may act "without the necessity of subjecting the estate to the burden" of an administration proceeding.

Can this closing be saved? No! All the heirs must be present at closing, and execute the deed.

Reason Number Three

A seller with a docketed judgment against him, who has been discharged in bankruptcy, believes he can sell his real property free of that judgment. No! There are two parts to a judgment, debt and lien. Bankruptcy only discharges the debt portion.

Bankruptcy is federal in nature.

Bankruptcy rules require the filing of the petition in the country clerk's office in order to put a purchaser on notice.

This is almost never done. The title company is not responsible if that filing is not done. However, the title company, by running independent searches in the Eastern and Southern districts, has extended its liability and must deal with the findings. The issue here is judgments against a discharged debtor. This is one of the most difficult phone calls title counsel can take because at first blush the title company position seems to make no sense. If the judgment has been discharged in bankruptcy how can it remain a lien on real property?

It is settled law that a discharge in bankruptcy only relieves a debtor from his personal obligation to repay the discharged debts. When a debt has been reduced to a judgment, a mere discharge does *not* remove the judgment as a lien against the debtor's real property.[16]

The *Carman* case states that "A qualified discharge serves as notice to third parties that despite debtor-owner's discharge in bankruptcy, property may still be burdened by liens," and further "Despite homestead exemptions, a lien against the exempt realty remains valid unless the debtor takes affirmative steps to avoid the lien by making an appropriate application under federal bankruptcy law."[17]

Experienced bankruptcy practitioners believe that it could be malpractice when this extra step is not taken by the attorney for the debtor.

The *Bank of New York* case is instructive as to the history and meaning of section 150 of NY Debtor and Creditor Law.[18] Section 150 is a post bankruptcy discharge proceeding in state supreme court to remove the lien against debtor's property. It supplies a corrective remedy for failure to avoid the lien in the original bankruptcy proceeding. Standing under 150 is broad and includes the purchaser from the discharged debtor.

To omit the judgment the title company will require:

- An Order Avoiding Lien in the original bankruptcy proceeding.
- An Order pursuant to section 150 of the Debtor and Creditor law directing the clerk to mark the judgment discharged (as opposed to "qualified discharge").

The Bank of New York case also affirms the fresh start philosophy of the Bankruptcy Act by establishing that a judgment against a discharged debtor is not a lien against new real property acquired by the debtor after the discharge, if the judgment was discharged in the bankruptcy proceeding, As the Court said, the discharged debtor may purchase new real property "unhampered by the pressure and discouragement of preexisting debt." A nice sentiment, not shared by most creditors.

Reason Number Two

A probated will results in Letters Testamentary issued to two executors, but only one attends the closing to execute the deed. No! Where there are only two executors appointed, both must execute the deed.

The statute is clear. Where there are two fiduciaries their actions must be unanimous, where there are three or more a majority is required.[19]

If there are more than two executors appointed, a majority must act.

As we know from Reason Ten, a fiduciary cannot delegate his authority, so where two executors are appointed, a power of attorney from one to the other will not enable the deed to be signed. Both executors must sign the deed—it is not a ministerial act.

There is a saving statute. A deed executed by one or more but not all of the executors who have been appointed will become valid ten years after the deed has been recorded.[20]

Can this closing be saved? Not unless the other executor is readily available.

Reason Number One

A probated will names a specific devisee, but the executor attends the closing to execute the deed. No! The executor has lost the power of sale, only the specific devisee can convey the real property.

As previously discussed, the authority of an executor to convey stems from EPTL 11-1.1(b)5(B):

> With respect to any property or any estate therein owned by an estate or trust, except where such property or any estate therein is specifically disposed of: . . . (B) To sell the same at public or private sale . . .

As the statute gives the executor power to sell real property, so it takes it away with the phrase "except where such property or any estate therein is specifically disposed of . . ."

Where a will reads "I give my house at 123 Fifth Avenue to Mary Brown," a specific devise has been established, and only Mary Brown can convey the real property.

If the specific devisee is also the executor, the deed must be clear that the conveyance is made in an individual capacity, it would be ineffective to convey by using an Executor's Deed.

A residuary devisee is not a specific devisee. A specific devise is a "disposition of a specified or identified item of the testator's property."[21]

Can this closing be saved? No, unless the executor also happens to be the specific devisee.

Unfortunately, these are not the only time bombs ticking out there. Constant vigilance will help to avoid the troubling consequences associated with the adjournment of a real estate closing.

Endnotes

1. 41 NY Jur. 2d. Decedents' Estates. Sec 1479.
2. SCPA 715.
3. EPTL 7-2.1.
4. NYC Admin Code Title 11 Chap 21.
5. NYS Tax Law 1402.
6. NYS Tax Law 1402.
7. City of Yonkers Transfer Tax. Chapter 15 Taxes, Article V. General Ordinance 8-1973 as amended by G.O.10-1989, G.O. 3-1998.
8. City of Mt. Vernon Real Property Transfer Tax Chapter 234 of the code of the City of Mt. Vernon NYS Tax Law 1205.
9. EPTL 11-1.3.
10. Religious Corporation Law Sec. 12.
11. *Greek Orthodox Archdiocese of North and South America V. Abrams*, 505 N.Y.S. 2d 327, 1994.
12. NPCL Sec. 510 (3).
13. SCPA 1001.
14. SCPA 805-3.
15. Abandoned Property Law Sec. 200.
16. *Fred D. Carmen v. European American Bank & Trust Company*, 576 N.Y.S. 2d (1991).
17. 11 U.S.C.A. Sec. 522 (b)(2)(A). 11 U.S.C.A. Sec. 522(F)(1).
18. *Bank of New York v. Michael J. Nies et al*, 468 N.Y.S. 2d 278 (1983).
19. EPTL 10-10.7.
20. EPTL 11-1.4; EPTL 11-1.2.
21. EPTL 1-2.17.

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RPS Green Real Estate Committee Conducts CLE Program at the New York Mets' Citi Field

By Nicholas M. Ward-Willis

Speaker Nicholas M. Ward-Willis, Co-Chair, Committee on Green Real Estate.

On August 18, 2009, the Real Property Law Section's newly formed Committee on Green Real Estate held its inaugural event, a Continuing Legal Education Seminar entitled "The Greening of America's Favorite Pastime—Discussion of Green Building Techniques Applied to the New York Mets' Construction of Citi Field." The CLE program was attended by approximately 70 attorneys and held in an auditorium within Citi Field. After the seminar, the attendees attended the New York Mets game versus the Atlanta Braves, which the Mets won in exciting fashion and scored eight (8) runs in a single inning, a franchise record.

The Green Real Estate Committee was established to educate members of the Bar and the public in general as to the emerging field of Green Real Estate. There has been a growing recognition in the real estate industry that "Green Construction" has a benefit, not only to the environment, but to the marketing of property, the prestige of the building to future owners and tenants, resale value and also in reducing operating costs. Green Construction is being encouraged by federal and state governments by the use of tax credits and local governments are considering ways to encourage or mandate "Green Construction" for new building activity and refurbishment or expansion of existing buildings. With the onset of Green Building and associated legislation, there will undoubtedly be "Green Litigation."

The CLE program at Citi Field included a presentation by the author, the Committee's Co-Chair, providing an overview of Green Real Estate and why the practicing Bar should be concerned. The author focused on how Green Real Estate and Green Construction impacts various practice areas including co-ops and condominiums, general real estate, municipal law and construction law. The author also reviewed provisions of the standard AIA Contract that requires modification on projects that incorporate Green Construction techniques.

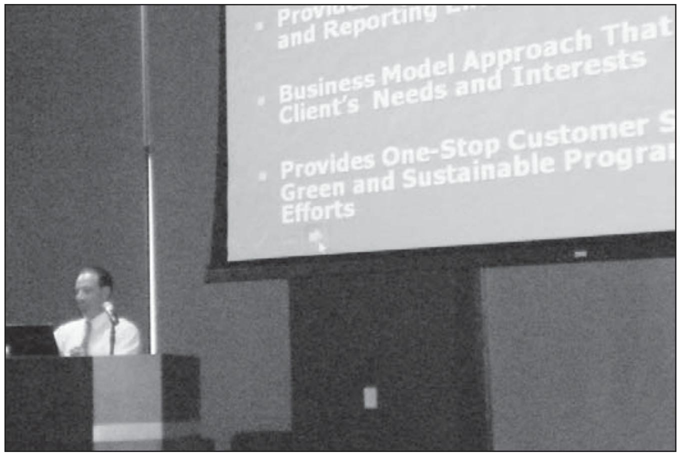
The program also included presentations by Patrick McGovern and Jeff Wolter of the New York Mets' Organization. Mr. McGovern, Vice President of Ballpark Operations for Citi Field, provided an overview of the Memorandum of Understanding entered into between the New York Mets Queen Ballpark Company and the United States Environmental Protection Agency concerning the use of sustainable development techniques for the construction of Citi Field and demolition of Shea Stadium. Mr. McGovern noted that approximately 95% of the 12,500 tons of structural steel used to construct Citi Field was made from recycled steel and in order to save

Attendees outside the auditorium at Citi Field, where the program was held.

Speaker Patrick McGovern, Vice President of Ballpark Operations for Citi Field.

CO_2 emissions, landfill space and energy, over 2 million pounds of a coal combustion product, namely fly ash, was mixed into Citi Field's concrete. It was also noted that in addition to the saving of Shea Stadium's seats, signage and other memorabilia, large quantities of materials were salvaged and recycled from the demolition of Shea Stadium. The New York Mets were able to reuse approximately 14,000 tons of steel and scrap metal and approximately 10,000 yards of concrete for Citi Field's construction.

Jeff Wolter of the Queens Ballpark Company Project Management Team, and a third-year law student at Hofstra Law School, discussed his involvement with negotiating the Memorandum of Agreement with EPA and supervising and coordinating the procurement and installation of Citi Fields' Green Roof. Citi Field has an approximately 10,000 square foot green roof over its administrative



Speaker Andrew Bellina, P.E.,
EPA Region 2 Senior Policy Advisor.

buildings and Mr. Wolter advised the attendees as to how the Green Roof was constructed. Mr. McGovern and Mr. Wolter then took the attendees on a tour of the Citi Field Green Roof, which is not open to the public.

The seminar also included a presentation from Andrew Bellina, P.E., Senior Policy Advisor for the United State Environmental Protection Agency Region 2 Office and a founder and leader of the Region 2 Green Team. Mr. Bellina provided an overview of various green construction projects and operations and how green technique can be incorporated into sustainable developments. Mr. Bellina provided a nuts and bolts explanation of green construction and the various measures that can be implemented.

The Green Real Estate Committee is pleased with the success of its first event and looks forward to furthering the Bar's understanding of Green Construction and associated issues. Individuals interested in joining the Real Property Law Section Green Real Estate Committee can contact its Co-Chairs, Nicholas M. Ward-Willis at nwardwillis@kblaw.com or Sujata Yalamanchili at syalaman@hodgsonruss.com. Information regarding the Green Real Estate Committee can also be viewed at the New York State Bar Association website at www.nysba.org/realprop.

Bergman on Mortgage Foreclosures: Oh, Do Lenders Need Title Insurance!

By Bruce J. Bergman

This missive may be too obvious—but we don't really think so. And it may even be more relevant to mortgage originators and underwriters than foreclosing mortgagees, but it still makes a very practical and dramatic point which enlightens most of us. [It all arises out of a rather bizarre late 2002 case: *Marcus Dairy v. Jacene Realty Corp.*, 298 A.D.2d 366, 751 N.Y.S.2d 237 (2d Dept. 2002)].

Certainly in New York, when a borrower seeks a mortgage it is usual that the lender will insist upon a title policy to protect the mortgagee. (The borrower, of course, purchases a fee policy for himself and the lender simultaneously requires issuance of a mortgage policy.) Because a title (or abstract) company has performed a search of the public records, the initiated might assume there is little room for defects which could surface to harm the lender. But, as we know, such is not at all the case in the real world. There are hidden title flaws that the title company might never find. Or, their readers could simply make mistakes; they are human after all and some may not do their jobs as well as others. And then there are judgment calls the title company makes which might just prove to be wrong. The latter category is the one which created a mess for a lender in the noted case (with worse consequences to the title company).

Here are the facts. Jacene gave a mortgage to the Dairy, later defaulted, with the Dairy responding by instituting a mortgage foreclosure action. The borrower defended, resulting in dismissal of the complaint, vacating of the *lis pendens* and a directive that the mortgage be cancelled and discharged of record. Although the resultant judgment was entered

in the county clerk's office, it was never recorded in the Division of Land Records and so the mortgage was not cancelled of record. The plaintiff Dairy appealed from the unpalatable judgment and sought a stay of the mortgage discharge but the motion was denied.

Jacene later conveyed the property to one Melissa Thomas, who then went and obtained a mortgage from a new lender. The title insurance company for the new lender found the Dairy's mortgage open in the Division of Land Records, but was willing to insure because of the combination of the supreme court judgment directing that the mortgage be discharged and some sage case law in New York ruling that knowledge of an appeal does not take away the bona fide status of a purchaser of property.

As you might expect, on appeal the court reversed the initial judgment and reinstated the earlier mortgage which then engendered a new mortgage foreclosure action in which the new lender was named as a party defendant.

Unfortunately for the new lender (and again more so for its title company), the transfer of the property from Jacene to Thomas was for no consideration. Moreover, Thomas made material misrepresentations in her mortgage application. (You've heard of those things before.) So the court concluded that the new mortgage lender knew or should have known of what the court found to be a fraudulent transfer of property. Based on those facts, the court decided that the new lender could not get the protection of a bona fide purchaser and could not avail itself of the helpful case law in New York previously mentioned.

In the end (and in short) the court found that the original mortgagee would have no remedy if its mortgage was not found to be senior, while the new lender could turn to its title insurance company, which should have known better, and collect from them. (Because the first mortgage lender would still have had an action on the debt even if its mortgage was junior, we are not so sure the court was entirely correct here but that is an academic point.)

An ultimate lesson of all of this—for lenders at least: title insurance is critical. That later mortgage loan here was iffy. The title company took a business risk and it turned out not to be a good one. The second lender, however, won't suffer by having taken a mortgage under what were apparently questionable circumstances. The title company was there to respond in damages.

Mr. Bergman is the author of the three-volume treatise, *Bergman on New York Mortgage Foreclosures*, LexisNexis Matthew Bender & Co., Inc. (rev. 2009) and is a member of Berkman, Henoch, Peterson & Peddy, P.C., Garden City, New York. He is also a member of the USFN and the American College of Real Estate Lawyers, and a Fellow of the American College of Mortgage Attorneys.

Scenes from the Real Property Law Section

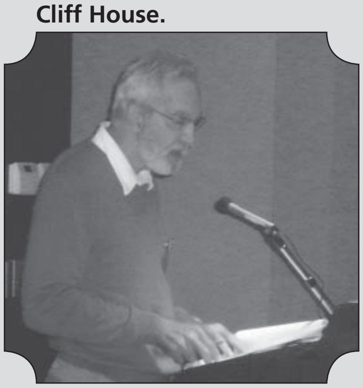
Summer Meeting

July 15-18, 2009

The Cliff House
Ogunquit, ME

Section Chair Joel H. Sachs "on the rocks" at the Cliff House.

Meeting attendees enjoy cocktails at sunset on the Ocean Terrace.



Left: NYSBA President Michael Getnick opens the MCLE Session.

Right: Barry Mills, President of Bowdoin College, addresses the dinner meeting.

John Blyth heads a panel with John Privitera, Mary McDonald and John Jones discussing natural gas deposits in upstate New York.

Program Chair Anne Copps and Nicholas Ward-Willis, Co-Chair of the Green Real Estate Committee, listen to a presentation by Dennis Greenstein, Co-Chair of the Condominiums and Cooperatives Committee.

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For ease of publication, articles should be submitted via e-mail to any one of the Co-Editors, or if e-mail is not available, on a disk or CD, preferably in Microsoft Word or WordPerfect (pdfs are NOT acceptable). Accepted articles fall generally in the range of 7-18 typewritten, double-spaced pages. Please use endnotes in lieu of footnotes. The Co-Editors request that all submissions for consideration to be published in this *Journal* use gender-neutral terms where appropriate or, alternatively, the masculine and feminine forms may both be used. Please contact the Co-Editors regarding further requirements for the submission of articles.

Unless stated to the contrary, all published articles represent the viewpoint of the author and should not be regarded as representing the views of the Co-Editors, Board of Editors or the Section or substantive approval of the contents therein.

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