New York Law Journal
SERVING THE BENCH AND BAR SINCE 1888
WWW.NYLJ.COM
An ALM Publication
VOLUME 245—NO. 38
MONDAY, FEBRUARY 28, 2011

Outside Counsel

Aggressive Defense Is Now An Option in Foreclosure Actions

By **Russell L. Penzer**

And **Giuseppe Franzella**

Historically, property owners and their counsel have failed to seek meaningful discovery from lenders in mortgage foreclosure actions, treating such actions more like special proceedings than the full plenary actions that they are. In the current environment, however, in which attorneys and judges are acknowledging more bona fide defenses to foreclosure than were historically upheld, property owners and their counsel would be well advised to take advantage of the disclosure devices provided for by the CPLR to uncover and establish potential defenses that may exist in their cases. Recent developments in the law have provided some guideposts as to some of the types of issues that should be explored through discovery.

Historical Defenses

Liberal and broad discovery is the rule in both New York and the federal court systems. However, counsel representing property owners in foreclosure actions have generally appeared less likely than they would be in any other type of case to take advantage of the availability of such discovery. The practice of forgoing discovery or seeking only limited discovery in foreclosure actions is likely tied to the fact that historically there were few defenses recognized by courts as viable in such actions.

In the past, the commonly recognized defenses to mortgage foreclosure actions were "waiver, estoppel, bad faith, fraud, or oppressive or unconscionable conduct by the mortgagee."[1] Given that these defenses, if they existed in an individual case, would likely have been apparent from the outset to the property owner, or undiscoverable absent engaging in a fishing expedition, counsel for property owners may have believed that seeking discovery in an effort to uncover the existence of such a defense would be a waste of time and resources.

> Issues such as 'robo-signing,' among others, which have recently surfaced, are fertile ground for discovery.

Recognition of New Defenses

In approaching defense of foreclosure actions now, property owners and their counsel must recognize the changes that have occurred both in the mortgage marketplace and in the political and judicial attitude toward foreclosures, and the potential legal ramifications of those changes. With the vast securitization of mortgages and the heavy trade in existing mortgages through sale and assignment, plaintiffs in mortgage foreclosure actions often have additional threshold burdens to establish entitlement to foreclosure. In a given case, these prerequisites to foreclosure may include such things as demonstrating the propriety of past assignments of the mortgage sought to be foreclosed and showing the plaintiff has proper standing to seek foreclosure.

Recently, courts and lenders alike have recognized lenders' widespread failure to properly clear these hurdles. In fact, this past October, Chief Judge Jonathan Lippman established a new filing requirement for all residential foreclosure actions. The new attorney affirmation form that must be filed in all such actions, specifically bears the notation N.B. to signify its official nature:

> N.B.: During and after August 2010, numerous widespread insufficiencies in foreclosure filings in various courts around the nation were reported by major mortgage lenders and other authorities, including failure to review documents and files to establish standing and other foreclosure requisites; filing of notarized affidavits which falsely attest to such review and to other critical facts in the foreclosure process; and "robosignature" of documents.

RUSSELL L. PENZER *is a partner and* GIUSEPPE FRANZELLA *is an associate with Lazer, Aptheker, Rosella & Yedid in Melville.*

Several of the largest lenders, including Bank of America and JPMorgan Chase, responded by placing a temporary moratorium on residential mortgage foreclosures to investigate their procedures in an effort to avoid repeating past defects in their foreclosure filings. This garnered the support of many in the federal government, some of whom have challenged Washington to issue a nationwide moratorium on residential foreclosures.

Issues such as "robo-signing," among others, which have recently surfaced, are fertile ground for discovery. Counsel for property owners should be cognizant of industry wide practices that may create defenses to foreclosure actions, and should seek discovery to see if such defenses exist in their clients' cases.

For example, in *Onewest Bank, FSB v. Covan*, the court dismissed a bank's foreclosure action without prejudice, directing that, should the bank recommence the action, in order to prevail it would have to "get to the bottom" of the employment status of a "robo-signer" who had signed assignment documents in connection with the underlying mortgage in an executive capacity on behalf of three different entities. In its decision, the court relied heavily upon testimony from a deposition the "robo-signer" gave in an unrelated Florida action.[2]

The proliferation of "robo-signers" has made depositions of a lender's officers or employees, oftentimes in the past considered to be a waste of resources, a useful tool for uncovering potential defenses.

The prevalence of "robo-signing" and the propriety (or impropriety) of assignments of mortgages present viable avenues for exploration to counsel for property owners seeking discovery from mortgagees. However, other defenses are equally ripe for discovery in the changed landscape of foreclosure litigation. Specifically, violations of federal consumer protection laws, such as the Real Estate Settlement Procedures Act (RESPA) and Truth in Lending Act (TILA), have become an increasing concern for courts.

Although RESPA was first enacted in 1974, its import as a safeguard for consumers has never been more apparent. RESPA requires that a home mortgage lender provide a borrower with certain disclosures, including lender servicing agreements, escrow account practices and financial relationships between service providers. Given the frequency with which mortgages have been securitized, assigned and otherwise transferred in the secondary market in the recent past, these disclosures are often incomplete or, worse yet, incorrect.

Lender servicing agreements are often complex and tangled, and lenders may neglect to provide borrowers with the voluminous documents memorializing these arrangements. Counsel for defendant property owners in residential mortgage foreclosure cases would be well-served to request production of such disclosures.

Although the TILA, as enacted in 1968, was initially intended to protect consumers in credit card transactions, it has been amended several times since to include provisions for disclosures of loans secured by real estate, special disclosures for adjustable rate mortgages and restrictions for high-cost, high-interest mortgages and subprime mortgages. As most mortgages currently in foreclosure fall into one or more of these categories, it is critical for borrowers and their counsel to ascertain whether the risks involved in these loan transactions were properly disclosed to borrowers. The failure by a lender to do so could lead to claims by the borrower against the lender for TILA violations.[3]

From a practical perspective, uncovering the existence of, and raising such defenses can potentially defeat the dreaded summary judgment motion which has often been insurmountable for property owners. For example, in *Downey Savings and Loan Association, F.A. v. Pinto-Bedoya*, the court denied summary judgment to a lender plaintiff to allow the defendants discovery as to the fraud and misrepresentations alleged in connection with the subject mortgage transaction.[4]

Being equipped with such defenses and being able to defeat a lender's motion for summary judgment would certainly place any property owner facing foreclosure in a better posture than he or she otherwise would have been, whether his or her ultimate goal is to litigate and defeat the foreclosure action or to negotiate a loan modification or other settlement with the lender.

Conclusion

The change in the foreclosure litigation climate has resulted in a court system that increasingly sympathizes with borrowers and frowns upon lending institutions' sloppy and, in some instances, outright fraudulent conduct. Although historically, counsel for property owners have eschewed broad discovery as a costly or fruitless practice, the shift in the foreclosure landscape and the success of various defenses warrants a more aggressive approach to pre-trial disclosure in defending such actions.

1. *EBC Amro Asset Management Ltd. v. Kaiser*, 256 A.D.2d 161, 681 N.Y.S. 539 (1st Dept. 1998).
2. 910 N.Y.S.2d 857 (Sup. Ct. Kings Co. 2010).
3. Defenses based on violations of RESPA or TILA will most likely be present in actions stemming from loan refinances, where borrowers are less likely to be represented by counsel than they would be in connection original financing of a home purchase.
4. 897 N.Y.S.2d 669 (Sup. Ct. Westchester Co. 2009).