My Updated Wish List for New York Real Estate Law

By Joshua Stein

About 12 years ago, I wrote an article for this *Journal*, consisting of a "wish list" of 12 changes I wanted to see in New York real estate law. The 12 changes I wished for would have simplified and streamlined the law and practice of real estate in New York, without substantively benefiting or hurting any particular group.

Today, 12 years later, not one of my wishes has been granted. In some ways, New York law has changed in ways that were the opposite of what I wanted.

Given my impressive batting average and impressively consistent results to date, I thought it would be a good idea to update and expand my wish list.

Each item in my original (and now expanded) wish list would remove complexity and unnecessary issues, excitement, or risks from New York real estate law. Some items are minor, such as eliminating documents in real estate closings. Few should be controversial. Of course, almost any proposal for change, however minor, may offend someone somehow or have unintended consequences that I have not considered. In that case, or if I have missed some compelling reason that existing law is terrific and requires no change, I apologize. When I next republish my wish list, I will fix my misguided comments.

New York real estate practitioners take for granted many of the existing headaches and gratuitous complexities of New York real estate law, as described in this article. New York real estate law does not have to be this way. But it probably will continue to be this way.

My wish list reflects only my own opinions, or perhaps fantasies, and only at the moment of writing—and, in the case of everything on my original wish list, without interruption for the 12 years since publication. My wish list is in no way tempered by considerations of practicality or how much interest and excitement my great suggestions may elicit in the Legislature.

If I were appointed tomorrow as grand commissioner to improve New York real estate law, here are the first changes I would make, ranked by importance:

1. Foreclosures

New York's nonjudicial foreclosure statute for commercial properties lapsed in 2009.[1] Legislative efforts to revive it have failed. It was an excellent statute while it lasted, with ample borrower protections and no application at all to residential foreclosures. The Legislature should have extended it. But it fell victim to bad timing. During the financial crisis, the Legislature did not want to touch anything that might speed up any foreclosure, commercial or residential. Nothing in the Legislature's views seems to have changed in the many years since the statute lapsed and the financial crisis ended. That leaves judicial foreclosure as the sole remedy in New York for a defaulted loan, even if the foreclosure is uncontested or consensual. Even in these latter cases, judicial foreclosure in New York often takes years to accomplish for no good reason.

If the Legislature reinstates nonjudicial foreclosure, as it should, then it should nevertheless adjust the previous statute in two ways.

First, the lapsed nonjudicial foreclosure statute did not apply to any commercial building where residential renters occupy more than about two-thirds of the units.[2] But what if the mortgagee has no interest in terminating residential leases, or does not have the option thanks to rent regulation? There, it is hard to see why a defaulting owner of an apartment building should be any more immune from nonjudicial foreclosure than a defaulting owner of an office building or a shopping center. Any reinstated nonjudicial foreclosure law should eliminate any exclusion for apartment buildings with more than four units, as long as the mortgagee does not try to terminate any residential leases by foreclosure. This change would, among other things, almost always help residential tenants by replacing a financially stressed landlord with one who probably paid less and borrowed less, and hence is under less stress and likely to better maintain and operate the building.

Second, the lapsed nonjudicial foreclosure statute allowed a court to set aside a sale of the property within a year, even after resale to a bona fide purchaser.[3] Although such a purchaser might be entitled to restitution, this provision caused legitimate concern for purchasers and their title insurance companies, which often refused to insure title on foreclosed properties until the full year had lapsed. In the face of that risk, purchasers hesitated to acquire those properties and invest in necessary improvements. So lenders had to take title to foreclosed properties and maintain and carry them for a year before selling them. But the former nonjudicial foreclosure statute gave borrowers and all other interested parties generous protections, including the right to require any foreclosing lender to proceed judicially. An extra one-year right to set aside a sale was just counterproductive and unnecessary. If the Legislature revives nonjudicial foreclosure, it should eliminate any possibility of setting aside a sale, to encourage lenders to place foreclosed commercial real estate back into the marketplace as soon as possible.

On the residential side, the Legislature has made the judicial foreclosure process even slower and more complicated by enacting multiple layers of borrower protections and procedural requirements. Those requirements, combined with an already overburdened court system, have produced extraordinarily slow timelines for foreclosures, even if uncontested. During that excruciatingly slow process, no one really knows who owns the property in foreclosure. Hence no one has much incen-

tive to maintain it. This helps produce so-called "zombie houses" and hurts neighborhoods. The Legislature should look hard at what it can do to speed up residential foreclosures while giving residential borrowers reasonable, but not excessive, protections.

2. Yellowstone Injunctions

New York commercial lease disputes often quickly become high-intensity full-blown litigations as a result of glitches in the Real Property Actions and Proceedings Law that artificially increase the stakes in the early stages of any landlord-tenant litigation. These glitches have existed for about five decades, long enough to have been fixed.

A commercial tenant will often seek a so-called Yellowstone injunction to try to prevent the landlord from terminating the lease for a nonmonetary default or sometimes even monetary disputes, because the landlord might be wrong.[4] This process often takes place on an emergency basis, late some Friday afternoon. In seeking a Yellowstone injunction, a tenant need not demonstrate a likelihood of success on the merits, a typical hurdle to injunctive relief.[5]

Courts grant these injunctions readily but then take their time—often lots of time—to decide the merits of the case. So tenants in default often use the process to delay for years the landlord's legitimate lease enforcement. A procedural protection becomes a substantive protection just because it takes so long.

The Legislature could readily eliminate all the Yellowstone excitement and some of the opportunities for delay by saying that if a court ultimately decides a tenant was in fact in default under its lease, then the tenant will have a last clear chance to cure the default to prevent termination, regardless of what the lease says. Any such rule would need to be accompanied by an absolute requirement for the tenant to continue paying fixed rent, perform any undisputed obligations, and perhaps deliver security for disputed obligations, while the court decides the dispute. Faster courts would help, too.

3. Mortgage Consolidations

Every New York commercial refinancing forces the parties to perpetrate a complex series of assignment, consolidation, and amendment documents, to say nothing of occasional splitters, spreaders, and lost note documentation, all to mitigate mortgage recording tax. This massive accumulation of complex paperwork (and potential spurious legal issues) could and should be replaced by a simple affidavit that discloses the tax already paid on the existing mortgage debt that encumbers the property. The borrower would then pay any incremental tax on new debt resulting from the current transaction. Lenders would have the same incentives they already do to assure payment of the right tax. With this change, though, we could eliminate mortgage chains, most lost note documentation, and the tedious task of drafting documents whose sole purpose is the continuation and manipulation of old mortgages.

4. Revolving Loans

New York theoretically imposes its mortgage recording tax on every re-advance of a substantial commercial revolving loan.[6] That position simply prevents New York real property from securing such loans. The Legislature should solve this problem, as well as some other similar problems that the mortgage recording tax creates for substantial modern multistate transactions. By making it possible for New York real property to secure a broader range of modern finance transactions, the Legislature would increase tax revenue.

5. Lien Law

New York law on mechanics' liens and construction loans is absolutely incomprehensible and unnecessarily complex. It creates a regime about which a famous lawyer for mechanic's lien claimants once bragged that for any construction loan he could always find some way the construction lender had violated the Lien Law. The Legislature should clarify and simplify this statute—translate it into English without changing its essential substantive concepts and requirements. Along the way, I would also make at least one substantive change: the Lien Law should make it possible for landlords to know with certainty that they can avoid exposure to liens resulting from a tenant's construction work. This might require a mechanism like the "notices of non-responsibility" seen in other states.

6. Single-Member Entities

The rating agencies and securitization industry have decided that New York law makes New York single-member limited liability companies less reliable and less issue-free than Delaware entities of the same type. This concern has moved much entity formation business to Delaware and created the need to involve Delaware counsel in major transactions. Whatever problems the rating agencies and the securitization industry have identified could presumably be fixed by thoughtful New York legislation that reproduces the benefits of Delaware statutory and case law on limited liability companies. The Legislature should also repair anything else that makes New York less hospitable than Delaware for forming routine entities for real property transactions.

7. Scaffold Law

The Scaffold Law is unique to New York State. Labor Law Sections 240 and 241 impose liability on contractors and property owners for gravity-related injuries that workers sustain regardless of their conduct on the job.[7] Many insurance policies exclude coverage for this liability. The law applies to both private actors and the City of New York. In a bizarre twist, the law shifts liability away from the people who can best manage it, the contractors who actually oversee work on the site, as opposed to owners. The law has produced huge amounts of litigation, much of it against the City. The typical lawsuit can be charac-

terized as spear fishing by the plaintiffs' bar. The law to some degree discourages public and private investment. It increases construction costs and clogs courts. At least one reform group estimates that the law's statewide cost exceeds that of major infrastructure projects. New York's Scaffold Law should be abolished or revised to: (a) establish minimum standards for safety equipment and training, with immunity for an owner that meets those standards; (b) adopt a comparative negligence standard to take into account a worker's negligence; and (c) make it easier for owners to shift these risks to the contractors that actually oversee the work being done.

8. Conditional Limitations

If a lease ends ten days after a landlord gives notice of termination for default, the landlord qualifies to bring a summary proceeding to recover possession. New York's common law calls this a "conditional limitation."[8] On the other hand, if the lease ends automatically when the landlord gives notice of termination for default, the landlord does not qualify to bring a summary proceeding and must bring a plenary action in Supreme Court. That is because the termination is considered to have arisen from a "condition subsequent," which does not qualify for a summary proceeding.[9] The distinction makes no sense. Legislation should eliminate it, to allow summary proceedings in both circumstances and to prevent a possible glitch in lease drafting.

9. LLC Publication

A New York limited liability company must publish notice of its formation in two newspapers for six weeks.[10] Failure to publish precludes access to the court system or at least constitutes grounds for dismissal of an action brought by the LLC that failed to publish—and embarrassment for counsel. The law ostensibly protects the public by letting people know information that might help them decide whether to do business with an LLC. In 2017, though, we now have this cool new thing called the internet. And the New York Secretary of State has a reasonably good website with information on LLCs. So New York's publication law serves no purpose beyond subsidizing some newspapers. New York is one of only a handful of states that still require publication. The Legislature should get rid of it.

10. Insured Closing Letters

Abstract companies and title agents often hold escrows for transactions where they will write title insurance. The parties to those escrows sometimes worry about possible malfeasance or loss of funds. So they ask a national title insurance company to backstop performance by the abstract company or title agent. In most states, national title insurance companies often issue "insured closing service letters" or "closing protection letters," to protect parties to the transaction from these risks. In New York, however, the Department of Financial Services (formerly the Insurance Department) says any such letters can relate only to issuance of a title insurance policy. For mix-ups in, e.g., handling of funds or documents, New York buyers and sellers just have a claim against an abstract company or title agent—neither of which typically has a substantial balance sheet. New York should eliminate this minor headache for closings by allowing national title insurance companies to backstop abstract companies and title agents in a meaningful way. (New York did recently enact a title agent licensing law designed in part to raise standards in that business,[11] but the concern remains.).

11. Online Information

New York City, primarily under the Bloomberg Administration, has done a great job of making real property information available online. Most real estate lawyers especially appreciate ACRIS, the Automated City Register Information System. Vast amounts and categories of other real property information are also available online, both through the City's website (www.nyc.gov) and elsewhere. Resources include www.oasisnyc.net and other websites that consolidate data. A few categories of information, such as building loan agreements, still cannot be viewed online but should be made available. And, ideally, the City would organize all the various City-operated online data sources so a single search would give the user access to all municipal information on a particular property.

12. Opaque Disclosure Law

Whatever may be the merits or wisdom of the State's Property Condition Disclosure Act, the text of the act is hardly a model of transparency and clear disclosure. The Act would probably flunk New York's Plain English Law, which imposes a fine of $50 for using incomprehensible language in a consumer contract.[12] The PCDA and similar statutes should be rewritten in Plain English to help serve the Legislature's goal of achieving broad and effective communication of useful information.

13. Simpler Mortgage Documents

The New York Real Property Law on its face seems to create two great tools to simplify New York mortgage documents. First, anyone can incorporate by reference a statutory form of mortgage defined in the Real Property Law, thus creating a one-page mortgage.[13] Second, anyone has the statutory right to record a master mortgage.[14] Future mortgages can incorporate that master mortgage by reference, again creating one-page mortgages. No one uses either tool.

The statutory mortgage deserves not to be used, because it is woefully deficient and does not meet elementary requirements of New York law. It is an embarrassment but no one cares. The master mortgage makes much more sense. A similar tool is widely used in, for example, California.

The Legislature should update New York's statutory form of mortgage to reflect current law, and should consider taking steps to encourage use of master mortgages. On the other hand, because longer mortgages create more recording fees, neither of these changes seems likely

to happen anytime soon. One may need to placate the county clerks by establishing a special high fee to record a master mortgage.

14. Assignments of Rents for Mortgage Loans

Why must a mortgage lender obtain a separate assignment of rents, beyond the assignment already in the mortgage? The answer: New York law does not really require a separate assignment. The law gives lenders a secondary security interest in the rents if the mortgage—which often includes an assignment of rents—is somehow invalidated. Lenders' lawyers use a separate assignment to preserve their remedies during a foreclosure and as a backup measure in case something goes wrong in the mortgage. How often does something go wrong in a mortgage? Not very often or at all, in my experience. And how often does a foreclosing lender actually exercise its rights under an assignment of rents, rather than have a receiver appointed? Again, not very often or at all.

The Legislature should adopt the Uniform Assignments of Rents Act proposed by the Uniform Law Commission many years ago, or similar legislation, to make it clear that a mortgagee does not need a separate assignment of rents, and can, if it wants, enforce an assignment of rents built into a mortgage as soon as a foreclosure begins. The model act also eliminates the legal fiction that a lender licenses back to the borrower the right to receive rents. This minor change would eliminate an entire spurious body of law.

15. Assignment of Leases on Conveyance

When a seller conveys income-producing real property to a buyer, the seller ordinarily delivers both a deed and a separate assignment of the seller's interest in leases. Though routine, the assignment of leases does not accomplish much. It is difficult to imagine any set of facts where the landlord's interest in a lease would not travel with the property to its new owners. Buyers demand a separate assignment in part because they know goal-oriented landlord-tenant courts may require an owner to allege and prove how it obtained an interest in the property and leases (if the lease was signed by the previous landlord), but somehow a deed is not enough. The Legislature should amend New York law to say: (a) a deed automatically conveys the grantor's interest in leases, including rent arrearages, except to the extent the deed expressly says it does not in a particular case; (b) ownership of record establishes prima facie standing and chain of title in lease enforcement actions; and (c) the tenant has the burden to raise a genuine issue about whether the landlord holds record title or is, perhaps, just some stranger trying to have some fun enforcing a lease in which the plaintiff does not actually have any interest.

16. Wicks Law

The Wicks Law generally requires New York municipalities to hire separate contractors for HVAC, plumbing, and electrical work. Each contract must be awarded to the lowest "responsible bidder," whatever that means.[15] The Wicks Law supposedly promotes competition and prevents corruption in awarding public work contracts. If that were true, then why does it not apply to other trades? Modern projects certainly need superstructures, ironwork, paving, asphalt, and carpentry. Most private owners find it efficient to hire a general contractor or single construction manager for substantial building projects. New York government entities, on the other hand, must solicit and evaluate separate bids and hire internal staff to manage construction. All of this drives up the cost of administration, management, and coordination efforts; causes cost overruns and delays in governmental construction projects, and makes it hard to implement best practices in construction. The Wicks Law should be repealed.

17. Leasehold Condominiums

New York law says a condominium cannot be created on a leasehold—unless the project is located in a handful of favored areas and involves a quasi-public agency.[16] Although this law presumably tries to protect consumers, it in fact hurts consumers by relegating sponsors to the use of cooperatives, a truly wretched form of ownership, rather than condominiums for the rare leasehold project that includes for-sale apartments. New York should figure out a way to allow leasehold condominiums in a way that adequately protects consumers. Other states seem to do it.

18. Landlord Liability for Negligence

The New York General Obligations Law says a tenant cannot release a landlord from liability for negligence.[17] Some New York leasing practitioners argue that if a tenant promises to pay any "deductible" amount under a liability insurance policy that otherwise benefits the landlord, that agreement violates the General Obligations Law and is invalid. This argument then implies that the tenant should maintain the lowest possible deductible amounts, regardless of the tenant's risk management program company-wide. A low deductible requirement seems inappropriate, at least in a commercial transaction where the choice of a deductible amount simply represents a business decision in the parties' risk management program. The Legislature should remove this possible issue, at least for substantial commercial leases.

19. Memorandum of Contract

A recorded memorandum of contract is enforceable against third parties for 30 days after the stated closing date.[18] After that, it is presumably a nullity. But the statute does not expressly say that. And New York courts sometimes are quite open to creative theories and claims, such as an argument that: (a) the statute is not clear enough; (b) even if the contract memo expired, a later buyer still knows about the earlier contract so remains subject to it; or (c) in the interests of equity, a contract memo should remain effective longer than the statute says. Therefore, a careful seller may hesitate to record a contract memo. A careful buyer may hesitate to proceed in the face of a contract memo, even if it expired. A careful title insurance company may raise an exception for an expired contract memo when it really should not. The Legislature should make contract memos a practical

and reliable mechanism by revising the law to unequivocally say an expired contract memo does not put anyone on notice of anything. That proposition works well for expired UCC-1 financing statements. It should work just as well for expired contract memos.

20. Attorney Escrow Accounts

Attorneys sometimes steal escrowed money. It does not happen much, but it does happen. It usually happens because an attorney is struggling with addiction or some other problem. An escrow account gives a troubled attorney unrestricted access to a tempting pot of someone else's money to use to fund or hide those problems. Attorney escrow accounts should be subject to reasonable controls to protect clients, such as requiring: (a) banks to send monthly statements to everyone with an interest in the account; (b) online access to account information for lawyers and their clients; or, (c) signatures from more than one person to release an escrow. Any of this could be accomplished just by changing New York's rules on attorney escrows. The change would not need to affect New York's rules about interest on Lawyers' Accounts, by which interest on small escrows is used as a funding mechanism for legal services for the poor.

21. Premature Brokerage Claims

New York law allows a licensed broker to assert a claim without a written brokerage agreement if the broker procures a ready, willing, and able buyer or tenant, whether or not a transaction actually closes.[19] Careful sellers and landlords protect themselves from unexpected brokerage claims by appropriate documentation and dealing with reputable brokers who want repeat business. But the law still allows claims when a seller or landlord would not intuitively "expect" to face them. The Legislature should fix that.

That concludes my list of changes I would like to see in New York statutes and common law.

I have stayed away from suggesting reductions in taxes on real estate transactions, as these are obvious suggestions and not particularly creative. Although it goes against my personal views on these issues, I also note that New York's high taxes do not seem to have prevented New York real estate from doing quite well for investors for quite a long time.

The continued success of New York real estate investment has produced some of the highest rents and property values in the country or the world, making it difficult or impossible for nonwealthy people to find a place to live at reasonable cost. State and city governments are trying to solve this problem by promoting affordable housing construction, often at great hidden cost.

As a supplement to my wish list, I would suggest that if the state and city governments want to promote affordable housing, they should look critically at government programs that constrict and complicate production of new rental housing. Of course, all that constriction and complication helps preserve the high values of existing properties. Thus, it has its own constituency that will oppose any change.

Each of those constrictive and complex programs originally arose for a good, or at least politically appealing, reason. Each grew over time. Today one can reasonably argue they make it harder than necessary to build new housing and hence they merit a critical look. Those programs are: zoning; building and other codes; rent regulation; unusually high real estate taxes on multifamily rental property; environmental review; and finally, landmark preservation. I would gladly sacrifice all my earlier wish list items in exchange for cutting back (not eliminating) these six programs with an eye toward making it easier to build in New York City.

That gives me a total of 27 wishes that will not be granted.

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Endnotes

1. N.Y. Real Prop. Acts. Law Art. 14 (Repealed July 1, 2009).
2. N.Y. Real Prop. Acts. Law § 1401 (Repealed July 1, 2009).
3. N.Y. Real Prop. Acts. Law § 1410 (Repealed July 1, 2009).
4. *See Graubard Mollen Horowitz Pomeranz & Shapiro v. 600 Third Ave. Assocs.*, 93 N.Y.2d 508, 693 N.Y.S.2d 91, 715 N.E.2d 117 (1999).
5. *See generally*, *Garland v. Titan W. Assocs*., 147 A.D.2d 304, 308, 543 N.Y.S.2d 56, 59 (1989); *Continental Towers Garage Corp. v. Contowers Assocs. Ltd. Partnership*, 141 A.D.2d 390, 394, 529 N.Y.S.2d 322, 324-35 (1988); *Herzfeld & Stern v. Ironwood Realty Corp.*, 102 A.D.2d 737, 738, 477 N.Y.S.2d 7, 8 (1984).
6. N.Y. Tax Law § 250(2)(b).
7. N.Y. Lab. Law § 240, §241.
8. N.Y. Real Prop. Acts. Law § 711.
9. *Id.*
10. N.Y. Ltd. Liab. Co. Law § 206(a) (McKinney 2017).
11. N.Y. Ins. Law § 2139 (McKinney 2017) (adopted 2014).
12. N.Y. Gen. Oblig. Law § 5-702 (McKinney 2017).
13. N.Y. Real Prop. Law § 291-d(3) (McKinney 2017).
14. N.Y. Real Prop. Law § 291-d(1) (McKinney 2017).
15. N.Y. Gen. Mun. Law § 101 (McKinney 2017).
16. N.Y. Real Prop. Law § 339-e (McKinney 2017).
17. N.Y. Gen. Oblig. Law § 5-321(McKinney 2017).
18. N.Y. Real Prop. Law § 294(5) (McKinney 2017).
19. *See Realty Investors of USA Inc. v. Bhaidaswala*, 254 A.D.2d 603, 604, 679 N.Y.S.2d 179, 181 (3rd Dep't 1998); *see also Prime City Real Estate Co. v. Hardy*, 256 A.D.2d 80, 81, 681 N.Y.S.2d 245, 245-46 (1st Dep't 1998).