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Locke Lord QuickStudy: New York's Court of Appeals Issues Groundbreaking Ruling on Foreclosure Statute of ?Limitations

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After several years of inconsistent decisions involving New York's six-year statute of limitations for mortgage foreclosure actions, the New York Court of Appeals took the bull by the horns and issued a groundbreaking decision that establishes two clear rules: (1) a lender's voluntary discontinuance of a foreclosure action revokes the acceleration of a mortgage loan and stops the running of the statute of limitations, and (2) the "unequivocal overt act" for acceleration of a mortgage debt does not include default letters that state that the lender "will" accelerate upon the borrower's failure to cure the default. Both rules will likely be welcome clarifications to mortgage lenders in New York, who found themselves defending against increasing statute of limitations claims that were caused by the filing and dismissal of foreclosure actions shortly after the 2008 financial crisis.

In coming to its decision, the Court considered "the intersection of two areas of law where the need for clarity and consistency are at their zenith: contracts affecting real property ownership and the application of the statute of limitations." The Court also noted there had been "few occasions to address how a lender may effectuate an acceleration of the maturity of a debt secured on real property."

While the Court reaffirmed the long standing principle that "acceleration occur[s] by virtue of the filing of a complaint in a foreclosure action," it re-examined decisions reached by the Appellate Division, Second Department in *Freedom Mtge. Corp. v. Engel*, 163 A.D.3d 631 (2d Dept. 2018) and *Ditech, v. Naidu*, 175 A.D.3d 1387 (2d Dept. 2018) where that Court found that a voluntary discontinuance, in and of itself, did not constitute a sufficiently "affirmative act of revocation of the acceleration." In reversing, the Court of Appeals found this approach "harmful to the parties [and] incompatible with the policy underlying the statute of limitations."

With its decision in *Engel*, the Court of Appeals issued a clear rule that "the noteholder's voluntary discontinuance of [the] action constitutes an affirmative act of revocation of that acceleration as a matter of law, absent an express, contemporaneous statement to the contrary by the noteholder." The Court of Appeals noted that recent decisions by the Second Department had "suggested that the revocation inquiry turns on an exploration into the bank's intent, accomplished through an exhaustive examination of post-discontinuance acts." In analyzing the Appellate Division decisions, the Court found that "[s]uch an approach leads to inconsistent and unpredictable results and, critically, renders it impossible for parties to know whether, or when, a valid revocation has occurred, inviting costly and time-consuming litigation to determine timeliness." The Court reasoned that "the impact of the noteholder's voluntary discontinuance of the action should be evident at the moment it occurs." Moreover, the Court played out the impact of its holding by reasoning that "[a] clear rule that a voluntary discontinuance evinces

revocation of acceleration (absent a noteholder's contemporaneous statement to the contrary) makes it possible for attorneys to counsel their clients accordingly, allowing borrowers to take advantage of the opportunity afforded by the de-acceleration—reinstatement of the right to pay arrears and make installment payments, eliminating the obligation to immediately pay the entire outstanding principal amount in order to avoid losing their home."

Providing its second clear rule, the Court held in *Vargas v. Deutsche* that the Appellate Division, First Department erred when it concluded that a default letter stating that the noteholder "will" accelerate upon the borrower's failure to cure the default constituted clear and unequivocal notice of an acceleration. The Court disagreed with the First Department because "the letter did not seek immediate payment of the entire, outstanding loan, but referred to acceleration only as a future event, indicating the debt was not accelerated at the time the letter was written." Further, the Court noted that the facts of *Vargas* "demonstrate" why acceleration should not be deemed to occur absent an overt, unequivocal act. Noteholders should be free to accurately inform borrowers of their default, the steps required for a cure and the practical consequences if the borrower fails to act, without running the risk of being deemed to have taken the drastic step of accelerating the loan. Even in the event of a continuing default, default notices provide an opportunity for pre-acceleration negotiation—giving both parties the breathing room to discuss loan modification or otherwise devise a plan to help the borrower achieve payment currency, without diminishing the noteholder's time to commence an action to foreclose on the real property, which should be a last resort."

The Court of Appeals' decision will no doubt have a tremendous impact on countless cases in New York State where, at one time, a case may have been discontinued for a variety of reasons. By setting forth a pair of bright-line rules, the Court of Appeals will likely save countless litigants from fighting over what a lender intended with its discontinuance of a prior foreclosure or its default letter prior to a foreclosure filing.

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