

Final Regulation Issued Under New York State's "Zombie Properties" Law

December 13, 2016

The New York State Department of Financial Services ("DFS") has finalized a new Part 422 to its regulations ("Final Regulation") that require banks and mortgage servicers to report and maintain vacant and abandoned properties, commonly referred to as "zombie properties." The Final Regulation expands upon legislation signed into law earlier this year. The "zombie properties" law and Final Regulation go into effect on December 20, 2016.

The "zombie properties" legislation obligates mortgage lenders and servicers to inspect, monitor, and maintain certain residential properties that are believed to be vacant and abandoned. The Final Regulation establishes reporting requirements to complement the recently passed legislation and also helps implement certain provisions.

This advisory highlights some of the differences between the proposed regulation issued by DFS in September ("Proposed Regulation") and the Final Regulation. Our advisory discussing the Proposed Regulation may be found [here](#), and the Final Regulation may be found here: <http://www.dfs.ny.gov/legal/regulations/adoptions/banking/bf422t.pdf>

Changes to Certain Definitions (Section 422.2)

The following changes were made to Section 422.2, which defines the terms used in new Part 422:

- "Mortgage" has been redefined from a "first lien upon a residential real property" to simply a "lien upon residential real property." As emphasized in Section 422's preamble, however, "Real Property and Proceedings Law ('RPAPL') Section 1308 requires certain holders of first-lien mortgages to inspect, secure and maintain vacantly and abandoned one to four family residential real property." (*Emphasis added.*)
- "Mortgagee" has been expanded to include the holder of a mortgage "and/or note" and further extended to include "... holders of credit instruments issued under a trust indenture ... to which such holders act by and through a trustee therein named."
- "Mortgage servicing," in the case of a reverse mortgage, now also means "... having been delegated by the mortgagee as responsible for oversight and maintenance of the mortgage even though payments are no longer being made by the borrower."
- "Residential real property," under the Proposed Regulation, included "... any building or structure used for both residential and commercial purposes where no more than twenty percent of the total appraised value is attributable to the commercial purpose." The Final Regulation has removed this part of the definition; only residential property is now included.

Change to Exemption Qualification (Section 422.3)

Under the Proposed Regulation, to qualify for an exemption, each mortgagee was required to “engage[] in all of the following activities during that calendar year: mortgage origination, mortgage ownership, mortgage servicing, and mortgage maintenance . . .” (Emphasis added.) This could have been interpreted to mean that a mortgagee that originated and owned a small number of loans but did not engage in mortgage servicing would not have been eligible for an exemption.

Under the Final Regulation, to qualify for an exemption, each mortgagee is now only required to “engage[] in mortgage origination and mortgage ownership during the calendar year . . .” The reference to mortgage servicing and maintenance has been removed.

Change to Deadline to Meet Burden to Prove an Exemption for 2017 (Section 422.3)

Under the Final Regulation, the deadline to meet the burden to prove an exemption has been extended from December 31, 2016, to February 28, 2017, for the 2017 calendar year. For each calendar year thereafter, the deadline will be December 31 of the preceding year (i.e., December 31, 2017, December 31, 2018, etc.). For a summary of the exemptions and the required calculations, please see our recent [advisory](#).

Addition Regarding Mortgages that Are Ninety Days or More Delinquent on December 20, 2016 (Section 422.3)

Under RPAPL Section 1308(1), “. . . within ninety days of a borrower’s delinquency, the servicer authorized to accept payment of the loan shall complete exterior inspection of the subject property to determine occupancy.” Prior to the issuance of the Final Regulation, it was unclear how much time a servicer had to conduct the initial inspection of a property subject to a delinquent loan (assuming no exemption applies). The Final Regulation includes a new provision that states:

1. Subject to subdivision (2), for all mortgages that are ninety days or more delinquent on December 20, 2016, the initial inspection required by RPAPL 1308(1) must be made on or before February 1, 2017.
2. For any residential real property that satisfies the definition of vacant and abandoned in RPAPL 1309 as of December 20, 2016, the requirements in RPAPL 1308(3) must be satisfied by February 1, 2017.

(Emphasis added.)

While the Final Regulation covers mortgages that are 90 days or more delinquent on December 20, 2016, it does not cover mortgages that are delinquent for less than 90 days on that date. It is not clear whether this was an intentional distinction or not. By not addressing mortgages that are delinquent for less than 90 days, the law appears to require inspection of these properties within RPAPL 1308(1)’s 90-day timeframe. This can be problematic under certain circumstances—for example, where a mortgage is 89 days delinquent on December 20, 2016, as drafted, the law appears to require an inspection of the subject property by December 21, 2016 (the 90th

day after delinquency). Accordingly, non-exempt institutions should arrange for the required inspections of mortgages which became delinquent recently as quickly as possible.

Changes to Vacant and Abandoned Property Reporting (Section 422.4)

The following changes were made to Section 422.4, which covers vacant and abandoned property reporting. These requirements apply for both exempt and non-exempt mortgagees and mortgage loan servicers:

- Addition of subject property's address to report.
- Addition of definition of "due diligence" a mortgagee must exhibit when determining whether a property is vacant and abandoned. "Due diligence includes but is not limited to ensuring that all timelines and requirements set forth in the law and regulation are adhered to and exercising oversight of third parties hired to inspect and investigate."
- Addition of the following provision: "For all residential real property previously reported to the Department as vacant and abandoned, the mortgagee shall provide the information required by this section by February 1, 2017."

Changes to Quarterly Reporting (Section 422.5)

The following changes were made to Section 422.5, which covers quarterly reporting (that is required for only non-exempt mortgagees):

- Addition of subject property's address to report.
- Removal of requirement to provide the identity and employer of the person who performed inspections to be named in the reports.
- Clarification that no quarterly report is required for the quarter ending December 31, 2016.
- Addition of the following provision: "Every mortgagee that is not exempt from the obligations imposed by RPAPL 1308 shall maintain for production and inspection all books and records documenting all actions to secure and maintain the subject property that have been taken, the date each action was taken, the nature of each action, the identity and employer of the person who performed each action, and all other information necessary to evidence compliance with the statute."

Changes to Federal Law and Federal Guidelines (Section 422.7)

Section 422.7 now includes subparagraphs (d) and (e), which cover Fannie Mae and Freddie Mac investor and insurer guidelines. Under these new provisions, where Fannie Mae or Freddie Mac require a mortgage to be serviced based on their investor or insurer guidelines as they exist on December 20, 2016, a servicer's compliance with the property preservation requirements included in such guidelines will be deemed to be compliant with RPAPL Section 1308. If the property preservation requirements of those guidelines change after December 20, 2016, compliance with such future requirements shall be deemed to be in compliance with RPAPL Section 1308 "... only if future property preservation requirements impose the same or greater property preservation requirements as compared to the requirements included in the guidelines in effect on December 20, 2016."

Changes to Disclosure of Information Maintained in the Statewide Vacant and Abandoned Property Registry (Section 422.8)

Under Section 422.8, “the superintendent may, in his or her sole discretion, release any information in the statewide vacant and abandoned property registry if the superintendent determines that such disclosure is in the best interest of the public.” A language that required all such released information to be kept confidential by the receiving party has been removed.

Additional Information

If you have any questions regarding the Final Regulation or the “zombie properties” legislation, please feel free to contact Joseph D. Simon at 516-357-3710 or via email at jsimon@cullenanddykman.com, Kevin Patterson at 516-296-9196 or via email at kpatterson@cullenanddykman.com, Elizabeth Murphy at 516-296-9154 or via email at emurphy@cullenanddykman.com, or Adam Barazani at 516-357-3767 or via email at abarazani@cullenanddykman.com.

Practices

- Regulatory and Compliance
- Banking and Financial Services

Industries

- Financial Institutions

Attorneys

- Kevin Patterson
- Joseph D. Simon