

Recent Cases Shed Light on Lien Law Issues

By Thomas A. Glatthaar

In my experience as a title lawyer for more than twenty years, I have found that there are certain eternal truths. One is that, in New York, Lien Law issues strike fear in the hearts of many. That is because the risks are so great in this area of practice. Shortcomings in documentation or in procedure oftentimes result in the mortgage loan being completely subordinated to mechanic's liens regardless of when filed, regardless of whether the lienors can show that they were injured (or, frankly, whether their actions were affected in any way) by these flaws. Because of the technical nature of Lien Law compliance, and because of the "winner-take-all" nature of these disputes, lien priority issues are perhaps the most litigated area of any lending practice.

Four recently decided cases help shed some light on certain technical New York Lien Law issues. Almost by definition, they all arise under circumstances where the project went bad and the loan at issue went south. Each of the cases underscore traps for the unwary that can result in a loss of priority. In at least some instances, I would expect that the decisions discussed will not be the last word on these subjects.

Altshuler Shaham Provident Funds, Ltd. v. GML Tower LLC involved a mortgage loan on property in the Syracuse area.¹ Pursuant to a loan agreement dated March 29, 2007, the plaintiff agreed to lend \$10 million to defendant GML Tower LLC ("GML"). The loan agreement expressly stated that the proceeds of the \$10 million loan were to be used as follows: \$5.5 million was to be used to pay off and take the existing mortgage on the property by assignment,² and the remaining \$4.5 million was specifically earmarked to be used to pay for improvements to be made by the borrower on the property. It is unclear, however, whether there

was an express promise by the borrower in the loan agreement to make improvements. At the loan closing on May 2, 2007, plaintiff advanced \$5.5 million for the purpose of paying off and taking by assignment the existing mortgage. The assignment of mortgage was recorded on May 3, 2007, as was a modification and extension agreement related to the existing mortgage.³ This modification and extension agreement did not speak to the planned construction of improvements.⁴

Construction commenced on the project no later than July 2007, and plaintiff advanced the remaining funds in several advances over time.⁵ On March 4, 2008, the parties entered into a modification of the loan agreement, and on March 6, 2008, the last of the \$4.5 million loan proceeds were advanced. The following day, a Mortgage Increase, Modification and Spreader Agreement between the parties was recorded. This document did not address planned improvements, nor is there any indication that this document treated the loan in any way other than as a single, \$10 million loan.⁶

Neither the original loan agreement nor the March 4, 2008 modification thereof was ever filed with the county clerk.⁷ Mechanic's liens were filed against the property starting in September 2008. When plaintiff commenced the action to foreclose in December 2008, the lienholders answered and raised various affirmative defenses, including an assertion that the filed liens had priority over the lien of the mortgage because plaintiff had failed to file a building loan contract or the March 4, 2008 modification thereof in violation of New York Lien Law Section 22.⁸ The plaintiff disputed the assertion that the March 29, 2007 loan agreement was a building loan contract,⁹ or that the mortgage itself was a building loan mortgage,¹⁰ pointing out, among other

things, that the \$4.5 million was not even secured at the time it was advanced. In addition, plaintiff argued that even assuming that the loan at issue was in violation of Section 22, the \$5.5 million then-existing mortgage that was taken by assignment at closing had unquestioned priority over the later-filed mechanic's liens because the priority of that mortgage was established when its proceeds were advanced and the mortgage itself recorded.¹¹

The court rejected both of these arguments.¹² It found that a building loan contract is an agreement to provide a loan to a borrower for the purpose of erecting an improvement on the premises where the loan is advanced in installments as construction progresses,¹³ and that the loan agreement in this case is a building loan contract. The obligation to comply with the Section 22 filing requirements can exist even if the loan is not secured by a contemporaneous mortgage.¹⁴

Further, the court rejected the plaintiff's arguments with respect to the priority of the \$5.5 million portion of the loan that was originally purchase money and which was taken by assignment by plaintiff.¹⁵ The court pointedly followed the **holding** of the *Atlantic Bank of New York v. Forrest House Holding Co.*,¹⁶ **holding** that a failure by a lender to meet the requirements of New York Lien Law Section 22 will result in the lender's "entire mortgage, including [the] part securing loan proceeds advanced for the purchase of the property..."¹⁷ suffering Section 22's subordination penalty.¹⁸

In so concluding, the court rejected the holding in *Federal Deposit Insurance Corporation, as receiver for Yankee Bank for Finance & Savings, FSB v. Task Associates, Inc.*,¹⁹ (coincidentally, also arising out of Syracuse).²⁰ *Yankee Bank* arose in the context of a material modification to a build-

ing loan contract²¹ for which no modification was in fact filed.²² The court followed a long line of cases in holding that the failure to file a material modification triggered the subordination penalty under Lien Law Section 22.²³ However, the court in *Yankee Bank* distinguished between the building loan funds actually expended towards the purchase of the building (which the court found were not subject to the statutory subordination penalty and which, together with interest thereon, had a first priority claim on the foreclosure sale proceeds) from the balance of the building loan funds (which was subordinated to the claims of mechanic's lienors).²⁴

Comment: Of note is the fact that the court in *Altshuler* seems to put substantial emphasis on its finding that the mortgage recorded March 7, 2008 (labeled "Mortgage Increase, Modification and Spreader Agreement") did in fact consolidate multiple mortgages into a single lien, and seemed to imply this element (a single, consolidated lien) was necessary to its conclusion that the entire mortgage loan (including the \$5.5 million portion which was, originally, purchase money) was subject to the Section 22 subordination penalty. To avoid this penalty affecting the entire loan, the existing mortgage debt needs to be kept outside the building loan agreement (say, covered by a separate loan agreement) and should also be kept as a separate mortgage lien.

One should be cautious about taking any existing mortgage by assignment through the use of building loan funds, the more careful approach being to keep these mortgages being acquired by assignment separate, and keep the funds needed to acquire these mortgages outside of the building loan and the building loan contract. By doing so, one could retain the priority of these mortgages as against any mechanic's lien subsequently filed.

An interesting unpublished decision in *International Exterior Fabrications, LLC v. J. Petrocelli Contracting, Inc.* involves, at its heart, the filing requirement in New York Lien Law Section 22.²⁵ The owner of the property acquired title in 2006. In conjunction with the acquisition, the owner executed and delivered an acquisition loan note and mortgage, a building loan note and mortgage, and a project loan note and mortgage. A building loan agreement and a project loan agreement were also executed, and the building loan agreement was filed with the County Clerk prior to the recording of the mortgages. Work on the project commenced shortly after that closing with J. Petrocelli Contracting, Inc., as general contractor. In September Fidelity National Family 2007, the owner, seeking additional funds, refinanced its mortgages with Citicorp. The new lender took the existing mortgages by assignment, advanced additional funds, and consolidated the loans and mortgages into two distinct liens. First, a building loan, comprised of the old and new building loans only and secured by a consolidated, amended and restated building loan mortgage, and second, a project loan, comprised of additional project loan funds and the existing acquisition loan and project loan that were assigned at closing and secured by a consolidated, amended and restated project loan mortgage. Again, owner and lender entered into an amended and restated building loan agreement and an amended and restated project loan agreement. The amended and restated building loan agreement was filed more than ten days after it was executed²⁶ but before the recording of the consolidated, amended and restated building loan mortgage.²⁷

The project ran into difficulties, and several mechanic's liens were filed, including one by plaintiff.²⁸ Plaintiff commenced an action to foreclose on its mechanic's lien. Plaintiff named the new lender and asserted priority over the lien of the building loan mortgage by virtue of a failure to file amended and restated

building loan agreement in compliance with the requirements of Section 22. The court disagreed:

There is no question that the Citigroup Building Loan Mortgage was "made pursuant to" the Citigroup Building Loan Agreement—this mortgage was newly created to secure the additional funding governed by that loan agreement—and it was created on the same day that loan agreement was executed. Thus, Lien Law section 22 only required the Citigroup Building Loan Agreement to be filed before the Citigroup Building Loan Mortgage was recorded, which was done here. The ten-day filing requirement would only have applied if there were *subsequent* modifications to the Citigroup Building Loan Agreement, and in this case there were none.²⁹

Comment: Although there is ample case law on the question of whether a modification to a building loan contract is "material," this case appears to be one of first impression on a question that could arise any time in what is a fairly common fact pattern: when an existing building loan agreement (and the building loan mortgage securing advances) is assigned to a new lender who adds new money and amends and restates both the building loan agreement and the mortgage, is the resulting building loan a new building loan (requiring the filing of a building loan agreement prior to or simultaneously with the recording of the building loan mortgage) or is it a modification of an existing building loan (requiring filing of a modification of the original agreement within ten days of execution thereof)? The court does not seem to hesitate in concluding that the resulting building loan agreement is not a modification under Section 22, to the detriment of lien claimants.

Another unpublished ruling presents (among a series of others) the interesting question of whether, under the facts set forth in the case, a project loan agreement should be subject to the filing requirements for building loan contracts in Lien Law Section 22.

Lehman Brothers Holdings, Inc. v. 25 Broad, LLC involves a mortgage foreclosure action covering three mortgages (a term loan mortgage, building loan mortgage and project loan mortgage) encumbering property in New York County.³⁰ The mortgages were made on March 9, 2007. The first mortgage was the term loan in the amount of \$231,677,693.00, as a refinance of existing mortgage indebtedness, with existing mortgages being assigned to the new lender and a consolidated mortgage executed and recorded. The second mortgage was a building loan mortgage in the amount of about \$19.6 million. Again, the existing mortgage loan was assigned to the new lender as part of a refinance of existing mortgage indebtedness, and an amended and restated mortgage was executed and recorded.³¹ The third mortgage, also assigned to the new lender as part of a refinance of existing mortgage indebtedness, and also for which an amended and restated mortgage was executed and recorded, was a project loan mortgage. Over time, various contractors who performed work or furnished materials or services on the property in connection with the project were purportedly not paid and filed liens against the property. The borrower defaulted on its mortgage obligations, and the lender commenced an action to foreclose on all three mortgages. Some of the mechanic's lienors asserted priority over all three of the mortgages, the assertion being that each of the mortgages was, for varying reasons, subject to the filing requirements of Lien Law Section 22, which, these mechanic's lienors assert, were not met. With regard to the senior mortgage, three arguments are presented to support this view:

1. the senior mortgage "is a building loan contract" because it was executed contemporaneously with a completion guaranty, and a default under the guaranty is a default on the senior mortgage.

2. a promise to make improvements³² is implied from the fact that a default under the building loan contract that was filed was also a default under the senior mortgage.

3. the senior mortgage is actually a consolidated mortgage, and one of the earlier mortgages is a 1996 building loan mortgage.³³

The court dismissed these arguments in swift fashion.³⁴ The court pointed out that a building loan contract is an agreement to provide a loan for the purpose of erecting a building;³⁵ the senior mortgage, however, was advanced in one lump sum and was not made for the purpose of making improvements on real property; in fact, the loan agreement called for the proceeds of the senior loan to be used to refinance the existing debt (and for no other purpose). All of the monies secured by the senior mortgage (including the 1996 building loan mortgage) were advanced long ago, and there was no express promise in the senior mortgage to make an improvement. On the question of the completion guaranty, the court held that the existence of a cross-default between the completion guaranty and the senior mortgage was not enough to transform the senior mortgage.³⁶

With regard to the building loan mortgage, the lienholder argues that it should achieve priority over the recorded building loan mortgage on two bases:³⁷

1. certain letter agreements were entered into between the borrower and the lender after closing that the lienholder asserts are "material modifications," and applicable law required that

such modifications be filed in accordance with Lien Law Section 22.³⁸

2. the 2007 building loan mortgage amends and restates a 2005 building loan mortgage, and "it is impossible to determine if the original 2005 Building Mortgage was filed as required under Lien Law Section 22."³⁹

The court found that the lienholder failed to establish the letter agreements that the parties signed were material.⁴⁰ The court also held that whether or not a building loan contract was ever filed in connection with the 2005 building loan mortgage is "irrelevant." What is relevant, according to the court, is that the plaintiff filed a building loan agreement with the County Clerk in conjunction with the 2007 building loan mortgage, and that this building loan agreement "was filed prior to the filing of the mechanic's liens."⁴¹

This is noteworthy in two respects. First, interestingly (to me at least), in establishing the priority of the building loan mortgage, the court strongly implies that it agrees with the holding in the *International Exterior Fabrications* case (infra) that where one takes an existing building loan mortgage and building loan agreement by assignment and files an amended and restated building loan agreement in connection therewith, that amended and restated agreement is *not* a building loan modification, but is a *new* building loan contract.⁴² Second, the fact that a building loan agreement is filed prior to the filing of the mechanic's liens is not a statutory requirement to establishing priority.⁴³

The court then turned to the project loan mortgage and project loan agreement.⁴⁴ Lienholder asserted once again that the project loan documents were actually building loan documents. They pointed to a provision in the project loan agreement (among others, the court says) that linked that loan to the construction of the "Project Improvements."⁴⁵

The lender argued that this loan was earmarked for development-related costs and not for cost of improvement, and that there was no express promise to make improvements as required by Section 2(13) of the New York Lien Law. Nevertheless, the court held for the lienholder, pointing out that "even if not labeled a building loan contract, the Project Mortgage can still be denominated as a building loan contract (sic) if it meets the Lien Law requirements of a building loan."⁴⁶ The court points out that the Project Loan Agreement has a section regarding "Conditions for Final Construction Advance," and finds that "there can be no dispute that the Project Loan Agreement provides for loan payments in consideration of making improvements to the property," and that the lender provided no evidence of how the project loan proceeds were to be used (if, in fact, they were not being used to pay for cost of improvement). Because the Project Loan Agreement was not filed, the project loan mortgage suffers the subordination penalty in Lien Law Section 22.⁴⁷

Comment: I am not quite sure what to make of this decision, and would caution, at this point, against overreaction or reading too much into it. The court seemed to put great emphasis, in deciding that the senior loan was not a building loan, on the fact that the loan agreement specified that the "[b]orrower shall use the proceeds of the Senior Loan to refinance the existing financing encumbering the Property (and for no other purpose)."⁴⁸ If the court is charging a lender with stating clearly in a loan agreement the uses for which a loan made in this context is intended, then that is a new and unusual requirement, but such a requirement could be accommodated. The project loan agreement is not available for review, so it is uncertain how the parties detailed the anticipated use of these loan proceeds or how closely the advance of funds under the project loan was tied in to progress of the construction job.⁴⁹ It is certain, however, that there is not enough information

in the decision to determine whether "there can be no dispute" that the project loan agreement should have been filed as a building loan agreement under Section 22.⁵⁰

One more noteworthy point that this case brings up is the importance of carefully considering, in this context, which mortgages the lender should foreclose. There may have been good reason for the lender here to initially seek to foreclose all three mortgages. Once the lienholders raised defenses, the lender shifted tactics, seeking to split off the priority of the senior and building loan mortgages (where, as the court holds, the lienholders had no valid basis for attack) from the project loan mortgage (where, at least in the eyes of this court, they did have grounds to challenge priority). Of the \$277.97 million total loan package, almost all of it was in the senior and building loans, and the project loan had not been fully advanced. Hindsight being 20-20, if the lender was concerned about the priority of the project loan,⁵¹ it could likely have foreclosed on the two other mortgages and, because of the amounts involved, would likely have ended up completing the foreclosure without incident (and would have been able to bid in at a high enough level to protect almost all of its loan package).

In what appears to be a case of first impression in New York, the Supreme Court, Monroe County addressed the question of whether a mortgage loan, advanced in whole or in part into an escrow account to fund certain required repair work, is a building loan mortgage in *Lehman Brothers Holdings, Inc. v. Genwood Strathallan LLC*.⁵² This court answered in the affirmative.⁵³

The transaction involved the refinance of an existing mortgage on property in Rochester, N.Y.⁵⁴ At the time of closing (January 30, 2007), the lender made a first mortgage loan in the amount of \$12.75 million (evidenced by a consolidated, amended

and restated note of even date) and a second in the amount of \$1.75 million. The bulk of the loan proceeds were used to take an existing mortgage by assignment. In addition, at least some portions of the first mortgage loan were advanced by lender at closing into two interest-bearing escrow accounts, which were to be disbursed pursuant to a First Repair Escrow Agreement ("First Repair Escrow Agreement") that was entered into at closing. The First Repair Escrow Agreement requires the borrower to perform certain repairs and deferred maintenance at the property, and provides that "...the escrows shall be used for the...work." It also affirmatively states that the escrow deposits secure the borrower's obligation to complete the work. The consolidated mortgage documents with respect to this loan were recorded promptly after closing.⁵⁵

Further, the parties also entered into a Second Repair Escrow Agreement ("Second Repair Escrow Agreement") at the closing, and opened another interest-bearing escrow account for the same.⁵⁶ This Second Repair Escrow Agreement covered different required work than the first agreement but otherwise contained the same material terms. This Escrow Agreement was funded by an advance made by the lender several months after closing, which advance was secured by a second mortgage on the property. Funding for this loan took place subsequent to closing, and the second mortgage was recorded in August 2007.⁵⁷

Defendant M&T Remodeling Services, Inc. ("M&T") performed work at the property.⁵⁸ M&T was not paid and filed a lien in the amount of \$299,500.00 in April 2009. When the borrower defaulted on the mortgage loans, lender commenced a mortgage foreclosure action, naming and serving numerous defendants, including M&T. M&T answered the complaint, asserting its lien and requesting a determination of priority. The lienholder argued that, even though the notes, loan agreement and the first

and second mortgages contained no promise on the part of the borrower to make improvements on the property, the loan agreement when read in tandem with the First Repair Escrow Agreement and the Second Repair Escrow Agreement is a building loan contract as defined in New York Lien Law Section 2(13). In doing so, the court underscores the following points:

1. the work set forth in the First and Second Repair Escrow Agreements was "required" by the Lender, and the existence of the escrow accounts was to secure the borrower's "obligation" to perform under the First and Second Repair Escrow Agreements.⁵⁹

2. there was a timeline for the completion of the work. This, in the court's view, seems to reinforce the point that the work was not discretionary, though it is difficult to ascertain how important an element this is.⁶⁰

Further, the court dismisses the argument that the loans are not building loans because the funds were advanced in a lump sum rather than installments.⁶¹ The money, the court points out, was not made available to the borrower in one lump sum; the borrower was required to fund the escrows, and those escrowed funds could not be used for the purposes specified in the First and Second Repair Escrow Agreements. The court quoted approvingly a commentator who criticized the escrow mechanism as an effort to avoid Lien Law requirements that may not work, and pointed out that such an arrangement still required periodic disbursements from the escrow account. In view of the foregoing, the court imposed the "harsh...statutorily imposed penalty" in Lien Law Section 22, subordinating the entire first and second mortgages to the filed liens.⁶²

Comment: Many people have expressed Lien Law concerns over the years regarding loan structures involving the funding of an escrow account at closing, the proceeds of which are controlled by the lender and are intended to be used to pay for improvement of real property. There are many variations on this structure, and this case leaves a number of questions unanswered. For example, the court seems to go out of its way to point out that the work at issue needs to be completed within a time frame. Is that a necessary element to finding that the loan agreement and the First and Second Repair Escrow Agreements, when read together, constitute a building loan contract?

One little-noticed but important conclusion that the court reached was that the loan wasn't fully funded at closing but was instead advanced in installments.⁶³ The court found that the funding of the First and Second Repair Escrow Agreements with loan proceeds was a disbursement "in a sense"; it was apparently not a disbursement for lien law purposes because the money "was not available to the Borrower in a lump sum."⁶⁴ Assuming that this rationale withstands scrutiny, its import lies in the fact that, even assuming that one could structure a transaction that circumvents the Lien Law Section 22 issue (that is, the loan would not be a building loan), the loan proceeds would, in this court's view, still not be "advanced," and any advance from the escrow account might be subject to matters arising after the date of the initial closing and prior to the escrow advance.⁶⁵

On a separate point, again, one should be cautious about taking any existing mortgage by assignment through the use of building loan funds. The more careful approach would be to keep these mortgages being acquired by assignment as a separate mortgage loan, and keep the funds needed to acquire these mortgages outside of the building loan and the building loan contract. By doing so, one could retain the priority

of these mortgages as against any mechanic's lien subsequently filed.

To conclude, there is one thing you can certainly say about the New York Lien Law: there are certain well-worn principles that guide the construction lending practice, but there seems to be a limitless number of fact patterns to test those principles. The courts seem to be forever answering questions that reinforce, expand or contract these seemingly simple and unquestionably fundamental questions: What is a building loan contract? When do you need to file one? And what happens if you don't? Stay tuned, because if there is one thing you can be sure of, it is that more will follow.

Endnotes

1. 28 Misc. 3d 475, 900 N.Y.S.2d 846 (Sup. Ct. Onondaga Cnty. 2010), *aff'd*, 83 A.D.3d 1563, 921 N.Y.S.2d 601 (4th Dep't 2011), *appeal denied*, 86 A.D.3d 934, 926 N.Y.S.2d 838 (4th Dep't 2011), *appeal denied*, 18 N.Y.3d 892, 963 N.E.2d 778 (2012).
2. Remember, the money used to acquire by assignment a pre-existing mortgage on the real property is a "cost of improvement" as defined in N.Y. LIEN LAW § 2(5) (McKinney 2012).
3. The modification and extension agreement, among other things, reduced the principal balance of the existing mortgage from \$7 million as appeared on the public records, to the \$5.5 million reduced principal amount.
4. *Altshuler*, 28 Misc. 3d at 477, 900 N.Y.S.2d at 848.
5. *Id.*
6. *Id.* at 478, 900 N.Y.S.2d at 849.
7. *Id.* at 477, 900 N.Y.S.2d at 848.
8. N.Y. LIEN LAW § 22.
9. *See id.* § 2(13).
10. *See id.* § 2(14).
11. *Altshuler*, 28 Misc. 3d at 480, 900 N.Y.S.2d at 850.
12. *Id.*
13. *Id.* at 479, 900 N.Y.S.2d at 850 (citing *Alden State Bank v. Sunrise Builders, Inc.*, 48 A.D.3d 1162, 1164, 853 N.Y.S.2d 230, 232 (4th Dep't 2008); *Finest Inv. v. Security Trust Co.*, 96 A.D. 2d 227, 229, 468 N.Y.S.2d 256, 258 (4th Dep't 1983)).
14. *Id.* at 480, 900 N.Y.S.2d at 850.
15. *Id.* at 481, 900 N.Y.S.2d at 851.

16. 234 A.D.2d 491, 492, 651 N.Y.S.2d 607, 608 (2d Dep't 1996); *see also* Thomas A. Glatthaar, *Uncertainty in the Lien Law Raises Lenders' Concerns*, N.Y. L.J., June 8, 1998, at 1.
17. *Altshuler*, 28 Misc. 3d at 481, 900 N.Y.S.2d at 851.
18. *See Atlantic Bank*, 234 A.D.2d at 492, 651 N.Y.S.2d at 608 (concluding that § 22 subordination provision is a "statutorily imposed penalty").
19. 731 F. Supp. 64 (N.D.N.Y. 1990).
20. *Altshuler*, 28 Misc. 3d at 481, 900 N.Y.S.2d at 851.
21. *See Yankee Bank*, 731 F. Supp. at 70. The "material modification" at issue was a waiver by the lender of a requirement that a surety bond be provided for lender's benefit prior to any advance of funds beyond the funds advanced at the closing where the property was acquired.
22. *See Yankee Bank*, 731 F. Supp. at 70.
23. *See, e.g., HNC Realty Co. v. Bay View Towers Apartments, Inc.*, 64 A.D.2d 473 (2d Dep't 1978). *See also* Thomas A. Glatthaar, *Pitfalls of Modifying Building Loan Contracts*, N.Y. REAL PROP. L.J., Spring 2009, at 64 (discussing the unique problems involved in modifying building loan contracts and mortgages).
24. *Yankee Bank*, 731 F. Supp. 64, 71-72 (N.D.N.Y. 1990).
25. No. 101679/10, 2011 NY Slip Op. 31545(U), 3 (Sup. Ct. N.Y. Cnty. April 11, 2011).
26. *See* N.Y. LIEN LAW § 22 (requiring modifications of building loan contracts to be filed within ten days of their execution).
27. *See id.* (requiring a building loan contract "with or without the sale of land" to be filed in the office of the county clerk in which the property is located prior to or simultaneously with the recording of the building loan mortgage).
28. *See Int'l Exterior*, 2011 NY Slip Op. 31545(U), 5.
29. *Id.* at 7.
30. *See Lehman Brothers Holdings, Inc. v. 25 Broad LLC.*, No. 100886/2009, 2011 NY Slip Op. 31931(U), 4 (Sup. Ct. N.Y. Cnty. June 16, 2011).
31. *Id.* at 6-7 (noting that an amended and restated Building Loan Agreement was filed prior to the recording of the amended and restated mortgage).
32. N.Y. LIEN LAW § 2(13) (defining a "building loan contract" as an agreement that exists when one party expressly promises to make an improvement on real property and the other, in consideration for that promise, promises to make a loan advances secured by a mortgage).
33. *Lehman Brothers*, 2011 NY Slip Op. 31931(U), 13.
34. *Id.* at 15-16.
35. *Id.* at 16; *see also* *Alden State Bank v. Sunrise Builders, Inc.*, 48 A.D.3d 1162, 853 N.Y.S.2d 230 (4th Dep't 2008).
36. *Lehman Brothers*, 2011 NY Slip Op. 31931(U), 19.
37. *Id.* at 20-21.
38. *Id.* *See also* Glatthaar, *supra* note 23 (discussing modifying building loan contracts, including "material modifications").
39. *Lehman Brothers*, 2011 NY Slip Op. 31931(U), 21 (citing one of many instances in this case where the court and/or the parties appear to a building loan contract (which is required to be filed under Lien Law § 22) and a building loan mortgage, which is not).
40. *Id.* at 22.
41. *Id.* *See also id.* at 22 n.5 (noting that, as a technical matter, whether the building loan contract is filed before the filing of a mechanic's lien is not relevant to the question of priority).
42. *Int'l Exterior Fabrications, LLC v. J. Petrocelli Contracting, Inc.*, No. 101679/10, 2011 NY Slip Op. 31545(U), 7 (Sup. Ct. N.Y. Cnty. April 11, 2011) (indicating that if the 2007 building loan agreement was a modification and the 2005 agreement had never been filed, this defect would result in a loss of priority regardless of whether the 2007 modification was done in accordance with statute); *see also* *Packard v. Sugarman*, 31 Misc. 623 (Sup. Ct. Onondaga Cnty. 1900); *P.T. McDermott v. Lawyers Mortgage Co.*, 232 N.Y. 336 (1922).
43. A detailed discussion of this subject is beyond the scope of this article. Suffice to say, to achieve priority in a building loan context to the extent of funds advanced prior to the filing of a mechanic's lien, a mortgagee must file a building loan contract, including a Lien Law affidavit that is materially correct, prior to or simultaneously with the recording of the building loan mortgage.
44. *Lehman Brothers*, 2011 NY Slip Op. 31931(U), 22.
45. *Id.* at 23 (defining "Project Improvements" in the project loan agreement as "the renovation and construction work show on the plans and specifications").
46. *See id.* at 23-24 (citing *Lincoln First Bank, N.A. v. Spaulding Bakeries Inc.*, 117 Misc. 2d 892 (Sup. Ct. Broome Cnty. 1983). Interestingly, the *Lehman* court seems to use the phrase "building loan contract" for the phrase "building loan mortgage" interchangeably throughout the decision, which is cause for some concern.
47. *Id.* at 24.
48. *See id.* at 16.
49. There is an obvious link between these two points, but it seems to me that once the project loan funds are earmarked for their anticipated uses, disbursement has to be tied to incurring those expenses and not to the overall progress of the construction project.
50. *Lehman Brothers*, 2011 NY Slip Op. 31931(U), 24.
51. *See* Thomas A. Glatthaar, *Soft Cost Mortgages May Run Afoul of State Lien Law*, N.Y. L.J., Nov. 14, 1994, at S3, for a discussion on project loan mortgages, their uses and potential issues, including priority issues.
52. *See* *Lehman Brothers Holdings, Inc. v. Genwood Strathallan LLC*, No. 2010/10157 (Sup. Ct. Monroe Cnty. Oct. 29, 2011).
53. *See id.* at 14-15.
54. *Id.* at 3.
55. *Id.*
56. *Id.*
57. *Id.*
58. *Genwood Strathallan*, No. 2010/10157, 3.
59. It is unclear whether the failure to complete the "required" work, or to do so within the time frames set forth in the First and Second Repair Escrow Agreements, would constitute a default under the mortgage, or simply preclude the borrower from gaining access to the escrowed funds.
60. *See Genwood Strathallan*, No. 2010/10157, 13.
61. *Id.*
62. *Id.* at 8 (citing *Atlantic Bank of New York v. Forrest House Holding Co.*, 234 A.D. 2d 491 (2d Dep't 1996)). It is interesting, to me at least, to note that, had the existing mortgage not been consolidated with the new first in this case, it is likely that the existing mortgage would not have been subordinated to the mechanic's lien so long as the First and Second Repair Escrow Agreements made no reference to this existing mortgage and the funds needed to acquire it.
63. *See id.* at 13-14.
64. *Id.* at 13.
65. *See id.* at 14.

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