

To Our Clients and Friends

Memorandum

March 9, 2021

The First Department Makes It Much Harder for Borrowers to Enjoin UCC Foreclosure Sales

The Appellate Division, First Department recently issued an important decision concerning the availability of injunctive relief to halt foreclosure sales under the Uniform Commercial Code (“UCC”). In *Shelbourne BRF LLC v. SR 677 Bway LLC*, Case No. 2020-03604 (1st Dep’t Mar. 4, 2021), the First Department considered a New York County Supreme Court decision that enjoined a UCC foreclosure sale of interests in LLCs that owned a commercial office building for approximately 86 days from when it was originally scheduled, and required the plaintiff borrowers to post a bond of \$100,000,¹ holding that the Supreme Court erred in granting the injunction because the plaintiffs could not demonstrate irreparable injury. The First Department’s decision is a reminder of the high barriers that borrowers face in obtaining injunctive relief to stop a UCC foreclosure sale from occurring where there had been a default on the underlying obligation.

The Supreme Court Preliminarily Enjoins a UCC Foreclosure Sale

In its August 2020 decision granting a preliminary injunction, the Supreme Court held that the borrowers demonstrated a likelihood of success on the merits of their claim that the proposed UCC sale was commercially unreasonable and that plaintiffs would be irreparably injured by the loss of their LLC interests. The Supreme Court relied heavily on its views that COVID-19 created “severe turmoil in the real estate market” and it was “highly uncertain” that a UCC foreclosure sale would generate fair market value. *Shelbourne BRF*, Index. No. 652971/2020, NYSCEF Doc. No. 38 at 1. The Supreme Court stated that the borrowers “will suffer irreparable harm if the sale proceeds and they lose their interests.” *Id.* The Supreme Court, however, did not provide any further explanation as to why the UCC foreclosure sale would result in irreparable injury, or offer any rationale for its departure from the long line of New York cases holding that loss of equity interests in an entity does not constitute irreparable injury, because such loss can be compensated by monetary damages. Following expiration of the preliminary injunction, a UCC foreclosure sale was conducted on October 30, 2020, and the mezzanine lender was the winning bidder.²

¹ We previously issued a client alert dated August 6, 2020 regarding the Supreme Court’s decision granting a preliminary injunction entitled [New York Supreme Court Issues Preliminary Injunction Halting Another UCC Foreclosure](#).

² We previously wrote about the Supreme Court’s denial of borrower’s attempt to enjoin the October 30, 2020 UCC foreclosure sale in a client alert dated October 29, 2020, entitled [New York Supreme Court Allows Previously Enjoined UCC Foreclosure Sale to Proceed](#).

The First Department Finds Injunctive Relief Was Not Warranted

Although the UCC foreclosure sale had been conducted following expiration of the preliminary injunction, the First Department determined that the mezzanine lender's appeal from the Supreme Court's grant of a preliminary injunction was not moot because a \$100,000 undertaking had been posted to secure the injunction. With respect to the merits, the First Department held that the "plaintiffs failed to demonstrate the requisite irreparable harm." *Shelbourne BRF*, Case No. 2020-03604, NYSCEF Doc. No. 22, slip op. at 2. The Court stated that "[n]otwithstanding the existence of the COVID-19 pandemic, the feared loss of an investment can be compensated in money damages." *Id.* The First Department relied on its prior decision in *Broadway 500 West Monroe Mezz II v. Transwestern Mezzanine Realty Partners II, LLC*, 80 A.D.3d 483 (1st Dep't 2011), where the court explained that the loss of LLC interests through a UCC foreclosure sale was a commercial interest that "can be compensated by damages" because "the harm they fear[] is the loss of []their investment, as opposed to loss of [their] home or a unique piece of property in which they have an unquantifiable interest." *Broadway 500 West*, 80 A.D.3d at 484.

It is worth noting that, on appeal, the borrowers in *Shelbourne* argued that a particular provision of the mezzanine loan agreement precluded an award of monetary damages if the UCC sale was determined to be commercially unreasonable, and authorized the plaintiffs to obtain injunctive relief to halt the purportedly unlawful conduct. In so arguing, the plaintiff borrowers relied on the New York County Supreme Court's decision in *D2 Mark LLC v. Orei VI Investments LLC*, Index No. 652259/2020,³ holding that an almost identical provision in the governing loan agreement justified a finding of irreparable injury and the issuance of injunctive relief precluding a UCC foreclosure sale from occurring. While the First Department's decision did not explicitly address the provision of the mezzanine loan agreement upon which plaintiffs relied or the *D2 Mark* decision, the First Department stated that it "considered the parties' remaining contentions and [found] them unavailing." *Shelbourne BRF*, Case No. 2020-03604, NYSCEF Doc. No. 22 at slip op. at 2.

Conclusion

The Supreme Court's August 2020 decision in *Shelbourne* was one of several decisions from the New York Supreme Court during the COVID-19 pandemic that departed significantly from prior precedent regarding UCC foreclosures and instead preliminarily enjoined UCC foreclosures, typically for up to a 60-day period. The First Department's reversal of such an injunction is a reminder that the barriers borrowers face seeking to enjoin a mezzanine loan foreclosure will not be lessened by the COVID-19 pandemic. The First Department's decision means that the potential negative effects of COVID-19 on the real estate market and its impact on the value of collateral should not serve as a basis for a finding of irreparable injury. The First Department's decision is a welcome development for mezzanine lenders, as they can proceed with more certainty that a borrower will not be able to show the irreparable injury necessary to enjoin a UCC foreclosure sale.

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³ We previously wrote about the Supreme Court's decision in *D2 Mark LLC* in a client alert published on June 24, 2020 entitled [First New York UCC Foreclosure Halted By A Preliminary Injunction—The Mark Hotel](#).

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its contents. If you have any questions about the contents of this memorandum, please call your regular Fried Frank contact or an attorney listed below:

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