New York County Supreme Court Upholds Accommodation Pledges

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In recent years, the claim that an accommodation pledge attached to a mortgage loan effectively "clogs" a borrower's right of redemption has been the basis of numerous civil actions in New York courts. With the case of *Atlas Brookview Mezzanine LLC v. DB Brookview LLC*, decided by the New York Supreme Court of Trial Courts, New York County in November 2021, the New York state courts finally tackled this claim head on.

Atlas concerned a mortgage loan which was defaulted on by the borrower. Notably, the loan was a dual collateral loan, which meant it was secured by both a mortgage on real property and a pledge of the ownership interests in the mortgagor entity that owned the property. In order to structure this type of agreement, the owner of the mortgage borrower enters into a guaranty secured by a pledge of 100% of the equity interests in the mortgage borrower referred to as an "accommodation pledge." In this case, following the default, the lender chose to foreclose on the accommodation pledge, and a UCC foreclosure sale was scheduled. A UCC foreclosure sale can be accomplished in a matter of months as opposed to a real property foreclosure that can take multiple years. Subsequently, the borrower filed an action in court, attempting to halt the UCC sale. The borrower argued that the accommodation pledge violated their equitable right of redemption in part because it minimized the window of time they had to redeem the property.

The right of redemption, as an equitable doctrine, allows a borrower to pay the full amount owed to the lender in order to "redeem" the property. Under New York state law, this right exists until the finalized sale of a property through mortgage foreclosure.

In *Atlas*, the court opted to dismiss the borrower's action, reasoning that they were a commercially sophisticated party, represented by counsel, who voluntarily agreed to this loan structure that required an accommodation pledge. Allowing the borrower to later void the pledge would be inconsistent with the original agreement. Although an appeal was initially filed in the *Atlas* matter, it was withdrawn in July 2022. To date, the New York courts have not revisited this issue, but some parties continue to try to distinguish their situations from the facts in *Atlas*.

What does *Atlas* mean for borrowers and lenders going forward? For lenders who structure loan agreements with accommodation pledges, this ruling allows them to breathe a sigh of relief – provided the parties are located in New York County and assuming that the borrowers on the opposite side of their agreements are considered "sophisticated." Given that the sophistication of the borrowers was specifically mentioned by the court, it is reasonable to assume that New York will continue to adhere to the ethos that sophisticated parties represented by counsel will be held to the written agreements they enter into willingly.

For our prior thoughts on pledges clogging a borrower's right to redemption, click here.

If you have questions about how this alert or other changes that might impact your business, please do not hesitate to contact Steven Coury (courys@whiteandwilliams.com, 212.631.4412) or Victoria Britton (brittonv@whiteandwilliams.com, 856.317.3673) or any member of the Real Estate and Finance Group*.

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