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A MANHATTAN APARTMENT FOR THE PRICE OF A CAR?

Co-ops, once thought to be immune, now more vulnerable to foreclosure

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By Sarah Ryley

Amongst a handful of onlookers huddled around an auctioneer in the rotunda of the New York State Supreme Courthouse last month, a real estate investor placed the winning bid on an alcove studio for what seemed like the deal of the century.

100 West 81st Street

The price: $28,000.

Yes, that's right, $28,000 for an apartment in a pristine Upper West Side co-op building across from the Museum of Natural History.

By comparison, a similar studio in the 100 West 81st Street building sold for $460,000 in 2005, the most recent comparable sale.

The shockingly low sale price -- more on par with a car than a Manhattan home -- was just $600 more than the amount owed on the apartment. In foreclosure auctions, banks generally set the starting bid, or "upset price," at the outstanding amount on the mortgage. The owner keeps any additional cash raised beyond that.

Keith Sheppard, the studio's owner, purchased the unit in 1982. He only had $27,400 left on his 30-year mortgage with Citibank when he fell behind on his bills, after being diagnosed with cancer, and the bank foreclosed, confirmed his attorney, Ron Hollander.

The auction not only illustrates how deeply Manhattan apartments can be discounted when sold at public auction, it also exposes the vulnerability of Manhattan's most prevalent housing type, co-ops, which generally aren't included in foreclosure statistics.

Of the 103 housing units in Manhattan scheduled for auction during the first three quarters of last year, 87 were co-ops, according to PropertyShark.

Unlike other types of residential property, co-ops don't go through the court when they fall into foreclosure because the unit owners are actually shareholders in the building, rather than property titleholders. Instead, the auctions usually take place on the courthouse steps or in the rotunda.

Also, the road to auction is significantly shorter for co-ops: Owners can sometimes receive as little as 30 days' notice that their shares are scheduled for auction, after just one missed payment, the state Banking Department confirmed. The foreclosure process generally lasts one or two years for other homeowners.

A lender can move that speedily regardless of how much equity the co-op owner has amassed -- contrary to the commonly held belief that co-ops' notoriously high down payments protect them from foreclosures.

While these co-op foreclosure auctions can offer big bargains for investors, Hollander and others say the system is flawed, both for those who fall into foreclosure and for those who bid on property.

"All co-op apartment foreclosures should have judicial oversight as part of the process," said Hollander, who filed a lawsuit to overturn the sale, the only way a judge would review the case. (Senator Klein said mandatory court-monitored settlement agreements for co-ops will be considered this legislative session.)

"If this were a regular condominium, a judge would say, 'Are you kidding me?'" Hollander said, adding, "We wouldn't be here."

There were a few irregularities with the auction that could help Sheppard's efforts to get the sale overturned. For one, the auctioneer didn't read the terms of sale aloud, which is required. And other investors didn't get a chance to bid because someone erroneously re-bid $28,000. Rather than overlooking the mistake, the auctioneer closed the sale, potentially denying Sheppard more money (other investors told *The Real Deal* they were prepared to bid). Meanwhile, at press time, Adam, the investor who bid on the West 81st Street co-op and requested that his last name be withheld, said he wouldn't fight the lawsuit to overturn the sale because he learned the owner has cancer.

87 OF THE 103
auctions scheduled in 2009 for Manhattan were for co-ops.
(PropertyShark)

Still, he claimed judges commonly engage in "judicial activism," overturning sales for more than 80 percent of the co-ops he's bid on. He suggested they side with homeowners because they are sympathetic toward the emotional plight of those going through the gut-wrenching foreclosure process, while they generally villainize banks.

"In my experience, judges don't really care what the cause [of foreclosure] is, or the merits of the case. They see that somebody is going to lose their home," he said.

Last month, Adam teamed up with another investor to place the winning bid on two combined co-ops on the Upper West Side for $1.51 million, slightly more than the amount left on the mortgage. The auction took place even though an attorney representing one of the owners showed up at the auction to stop the sale, claiming a buyer had offered $3.75 million for the apartments that morning. The auction on the properties was the result of a spiteful divorce, the wife's attorney explained, which again highlights how vulnerable co-op mortgages are to sudden life changes.

Attorney Lior Aldad of Aldad & Associates, a law firm that specializes in co-ops and condos, said he's been dealing with an increasing number of co-op foreclosures for seven-figure apartments.

And, he said, banks have been strategic about which properties they foreclose on.

"If they see the apartment is worth much more than the value of the note, they will handle those cases as a priority," as opposed to apartments that are underwater, Aldad said. "Banks will press to start a foreclosure action and expedite the legal proceedings in cases that they know once they complete a foreclosure judgment, they can recoup the value of the foreclosure note.

"Banks are very savvy and they know how to analyze the value of apartments compared to the value of the outstanding note," he added.

Adam still needs to pass the co-op board before either sale is finalized -- a process that is by no means a guarantee.

But there may be more opportunities for investors coming down the pike.

The quarterly rate of foreclosure filings increased 108 percent in Manhattan during the first three quarters of last year compared to 2008, the highest increase of the five boroughs, according to the Furman Center.

Overall, however, Furman found that the number of Manhattan foreclosure filings is still relatively small -- only 521 during the first three quarters of 2009. That figure excludes co-ops, which don't have public filings like lis pendens leading up to the auction, making it difficult to determine exactly how many co-ops are en route to foreclosure.

But several factors indicate Manhattan's foreclosure rate could continue increasing.

The borough's average sales price declined 24 percent from peak to trough, according to appraiser Jonathan Miller. That slide has wiped out a lot of existing equity on newly purchased homes, leading to more underwater mortgages. With no equity left to protect, some homeowners may simply stop making payments -- which will ultimately lead to more foreclosures.

Rents also fell, which has caused certain investors to fall short on their monthly carrying costs. And unemployment in high-paying sectors like the financial industry has hit Manhattan's wealthy homeowners particularly hard.

Sam Heskel, executive vice president of the appraisal firm HMS Associates, said he's counted 581 bank-owned, pre-foreclosure and auction listings for sale in Manhattan, excluding co-ops.

Some of those listings are for new, luxury condos at towers like Tribeca's 200 Chambers Street. Eleven apartments in that building, all purchased during the height of the market, had lis pendens issued during the third quarter of 2009, according to PropertyShark, and two were listed for sale. Not all lis pendens make it to foreclosure because the owners are able to sell them, sometimes at reduced prices, or work out agreements with their lenders, experts said.

Susie Park, a broker for Pari Passu who represented a distressed seller at 200 Chamber Street, said many of the investors who bought there aren't able to cover their monthly expenses by renting the apartments.

"I wouldn't be surprised if in the next quarter or so we saw more investor foreclosures," she said.

Other new condos that had lis pendens filed on multiple units during the third quarter included the Atelier on West 42nd Street; the Cipriani Club Residences at 55 Wall Street; 1600 Broadway on the Square; and 555 West 23rd Street.

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COMMENTS

Anonymous

Here it comes. Big time foreclosures in established Manhattan nabes. This will cause a wave of panic. Prices to tumble quickly and remain there for years. Maybe a drop of 10-20% more until it is in line with rent to buy ratio.

Comment #1 Posted By: Anonymous 01/03/10

Anonymous

This reminds me of my friend's advise 3 years ago when he used to tell me to buy now or be priced out for ever. Good thing I did not listen.

Comment #2 Posted By: Anonymous 01/05/10

Anonymous

#1 your prediction is based on one indiviual with a terrible terminal illness and one especially nasty divorce and the rest of the article is unsubstantiated blather on the part of the author. To make sweeping predictions based on two extreme examples and "talk" is just plain silly. For TRD to apss this off as responsible journalism is shockingly negligent.

Comment #3 Posted By: Anonymous 01/06/10

Anonymous

No one knows what is going to happen. I remember linving in California before the boom and then moving back to NYC and getting priced out. Something is going to have to give and it is going to be the prices.

Comment #4 Posted By: Anonymous 01/06/10

Anonymous

#3 Those cases were just examples, but the story said 87 co-ops were auctioned in nine months (and these two were in December). How do you know that that those 87 owners also didn't get sick, divorced, or lose their jobs?

Comment #5 Posted By: Anonymous 01/08/10

Anonymous

Similar inside dealing occurred in the late 1980's. So many auctions, and then the deals were overturned. A few individuals did well , but so many sales got overturned.

Comment #6 Posted By: Anonymous 01/10/10

Anonymous

Thank you for the update and the information TRD.

Comment #7 Posted By: Anonymous 01/13/10

Anonymous