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Prior Lien on Rents and Profits Upheld as a Method of Financing Repairs— *In re Dep't of Bldgs.**

Official findings of the New York Legislature in 1962 revealed the existence in certain cities of housing conditions which, unless immediately corrected, might cause irreparable damage to buildings or endanger the life, health and safety of their occupants or the general public.[1] To facilitate the correction of these conditions and to increase the supply of adequate, safe dwelling units, the legislature enacted the 1962 Receivership Law,[2] which creates a procedure enabling a city to enforce its housing codes by compelling needed repairs and improvements.

Under the 1962 law, whenever the department of real estate certifies the existence in a multiple dwelling of a nuisance[3] consti-

* 14 N.Y.2d 291, 200 N.E.2d 432 (1964).

1. N.Y. SESS. LAWS, ch. 492, § 1 (McKinney 1962).

2. N.Y. MULT. DWELL. LAW § 309.

3. "The term 'nuisance' shall be held to embrace public nuisance as known at common law or in equity jurisprudence. Whatever is dangerous to human life or detrimental to health, and whatever dwelling is overcrowded with occupants or is not provided with adequate ingress and egress or is not sufficiently supported, ventilated, sewered, drained, cleaned, or lighted in reference to its intended or actual use, and whatever renders the air or human food or drink unwholesome, are also severally, in contemplation of this law, nuisances." N.Y. MULT. DWELL. LAW § 309(1)(a).

tuting a serious fire hazard or threat to life or safety, the department may issue a written order to the owner directing the elimination of the nuisance within a specified time.[4] Should the department feel that a receiver must be appointed to carry out its order, every mortgagee and lienor of record must be sent a copy of the order within five days of service upon the owner, along with notice that, in the event the nuisance is not properly removed, the department may apply to the supreme court for an order to show cause why a receiver should not be appointed.[5] Upon application by the department, the supreme court may appoint a receiver who will be given a prior lien on the rents and profits of the property to secure payment for the expenses incurred in removing the nuisance.[6] Alternatively, if any owner, mortgagee, lienor, or other person having an interest in the property applies for permission to repair the premises, the court may authorize that person to remove the nuisance within a specified time and give the person a lien equivalent to the lien that would have been granted to the receiver.[7]

The constitutionality of the 1962 Receivership Law was recently challenged in *In re Dep't of Bldgs.*,[8] where a receiver was appointed and a prior lien created on rents and profits despite the existence of a mortgage entered into prior to the enactment of the law. The New York Court of Appeals affirmed the lower court order and held the statute constitutional.[9]

Housing code enforcement constitutes an interference with vested property and contract rights. Due process therefore requires that those affected be given adequate notice of any order involving their interests and a fair hearing in which to contest the legality or propriety of the order.[10] The 1937 amendment to New York's Multiple Dwelling Law[11] was held unconstitutional by the court of appeals in *Central Savings Bank v. City of New York;*[12] unlike that provision, however, the 1962 Receivership Law fully protects the procedural rights of the persons affected. Given no chance to contest the determination of the existence of a nuisance under the 1937 law, the owner and mortgagee now are afforded full opportunity

4. N.Y. MULT. DWELL. LAW § 309(1)(e).

5. N.Y. MULT. DWELL. LAW § 309(5)(a).

6. N.Y. MULT. DWELL. LAW §§ 309(5)(c)(3), 309(5)(e). A mortgagee may foreclose prior to payment of the receiver's lien but he is not entitled to possession, rents or profits until the receiver's claim is satisfied.

7. N.Y. MULT. DWELL. LAW §§ 309(5)(g), 309(5)(c)(3).

8. *In re* Dep't of Bldgs., 20 App. Div. 2d 851, 248 N.Y.S.2d 199 (1964).

9. 14 N.Y.2d 291, 200 N.E.2d 432, 251 N.Y.S.2d 441 (1964).

10. *E.g.*, Southern Ry. v. Virginia, 290 U.S. 190 (1933); Thain v. City of Palo Alto, 207 Cal. App. 2d 173, 24 Cal. Rptr. 515 (1962); Chicago, M., & St. P. Ry. v. Board of Comm'rs, 76 Mont. 305, 247 Pac. 162 (1926); See New York v. Gebhardt, 151 F.2d 802 (2d Cir. 1945).

11. Laws of N.Y., 1937, ch. 353, § 2.

12. 279 N.Y. 266, 18 N.E.2d 151 (1938), *cert. denied*, 306 U.S. 661 (1939).

at a fair hearing before the supreme court to introduce any facts challenging the department's certification that the property in question constitutes a public nuisance.[13] Whereas a mortgagee or lienor had no opportunity to intervene on his own behalf under the earlier law, now it is possible for him to protect his interest by making the repairs himself, receiving the lien to secure payment of his expenses.[14] In addition, where the owner and mortgagee were conclusively bound by the amount of the lien filed against the property under the 1937 law,[15] they now have the opportunity to contest the reasonableness of the expenses reflected in the lien.[16]

Since the 1962 Receivership Law provides for the creation of liens on rents and profits which will have priority over existing mortgages, the owner and mortgagee in *In re Dep't of Bldgs.* relied upon *Central Savings*, arguing that the 1962 law was unconstitutional as an impairment of contract rights. Although the contracts clause[17] prohibits state impairment of contract rights, all contracts are subject to the reasonable exercise of the states' police power.[18] As a general rule, a statute will be upheld so long as it bears a substantial relationship to public health, safety, or morals and is reasonably adapted to meeting the exigencies that occasioned its enactment.[19] Thus, statutes enacted to meet conditions constituting a public emergency have regularly been upheld as proper exercises of the police power.[20] In 1962 the New York legislature made it abundantly clear that, in its opinion, the shortage of adequate, safe housing in certain New York cities constituted a public emergency.[21] Conditions in New York City provide dramatic support for the legislature's conclusion. Between 1950 and 1960 the city's population increased by 2,802,876 persons but only 324,651 additional housing units were constructed.[22] In 1960, of the city's 2,758,116 housing

13. N.Y. MULT. DWELL. LAW § 309(5)(c)(3).

14. N.Y. MULT. DWELL. LAW §§ 309(5)(c)(3), 309(5)(g); see text accompanying note 6 *supra*.

15. Laws of N.Y., 1937, ch. 353, § 3(6)(g).

16. N.Y. MULT. DWELL. LAW § 309(4)(d).

17. U.S. CONST. art. I, § 10.

18. See, *e.g.*, Home Bldg. & Loan Ass'n v. Blaisdell, 290 U.S. 398 (1934); Marcus Brown Co. v. Feldman, 256 U.S. 170 (1921); Taylor v. Brown, 137 F.2d 654 (Emerg. Ct. App.) *cert. denied*, 320 U.S. 787 (1943); Loring v. Commissioner of Pub. Works, 264 Mass. 460, 163 N.E. 82 (1928).

19. See Home Bldg. & Loan Ass'n v. Blaisdell, *supra* note 18.

20. See, *e.g.*, Honeyman v. Jacobs, 306 U.S. 539 (1939); Home Bldg. & Loan Ass'n v. Blaisdell, *supra* note 18; Marcus Brown Co. v. Feldman, 256 U.S. 170 (1921); Loab Estates Inc. v. Druhe, 300 N.Y. 176, 90 N.E.2d 25 (1949); People *ex rel.* Durham Realty Corp. v. La Fetra, 230, N.Y. 429, 130 N.E. 601 (1921) (landlords not permitted to evict tenants during a housing shortage even after expiration of leases).

21. N.Y. SESS. LAWS, ch. 492, § 1 (McKinney 1962).

22. UNITED STATES DEP'T OF COMMERCE, CENSUS OF POPULATION AND HOUSING—CENSUS TRACT 104, 1960, p. 752. "A house, an apartment or other group of rooms, or

units, 84,246 were in dilapidated condition and 343,311 were in deteriorating condition; 30,303 units were without heating, 19,468 were without hot water, 198,395 units shared bathrooms or had none at all, and 172,259 lacked other plumbing facilities.[23] In view of these circumstances, the court justifiably concluded that the 1962 Receivership Law, providing a technique which could be used both to facilitate the immediate repair of substandard dwellings and to preserve the physical standards of sound neighborhoods, is a permissible exercise of the state's police power. *Central Savings* was properly distinguished on the ground that the conditions which confronted the legislature in 1962 were far more serious than those which existed in 1937.[24]

The court was also correct in distinguishing the *Central Savings* case on the additional ground that the impairment of contracts under the 1937 law was more severe than under the 1962 law, and consequently the state's exercise of the police power was less reasonable in 1937.[25] By creating a lien with a limited rather than an absolute priority, the legislature avoided one of the features that had led the *Central Savings* court to hold the 1937 paramount lien provision an unconstitutional impairment of contracts.[26] Under the 1937 legislation the receiver was given the right to foreclose his paramount lien, possibly wiping out the mortgagee's interest completely.[27] Under the new legislation the lien attaches not to the fee itself but only to the rents and profits.[28] The mortgagee's interest can thus be postponed but not eliminated.

The 1962 Receivership Law represents a significant development in the urban renewal field. The complex task of renewing major

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a single room is regarded as a *housing unit* when it is occupied or intended for occupancy as separate living quarters, that is, when the occupants do not live and eat with any other persons in the structure and there is either (1) direct access from the outside or through a common hall or (2) kitchen or cooking equipment for the exclusive use of the occupants of the unit." *Id.* at 5.

23. "Deteriorated housing needs more repair than would be provided in the course of regular maintenance. It has one or more defects of an intermediate nature that must be corrected if the unit is to continue to provide safe and adequate shelter. Dilapidated housing does not provide safe and adequate shelter. It has one or more critical defects, or has a combination of intermediate defects in sufficient number to require extensive repair or rebuilding, or is of inadequate original construction. Critical defects result from continued neglect or lack of repair or indicate serious damage to the structure. . . ." *Id.* at 6.

24. 14 N.Y.2d 291, 251 N.Y.S.2d 449 (1964).

25. *Ibid.*

26. 279 N.Y. 226, 18 N.E.2d 151 (1938).

27. "Every such assessment . . . shall be a lien or charge upon the property or premises . . . which lien shall have priority over all other liens and encumbrances, including mortgages whether or not recorded previously to the levying of such assessment. . . ." Laws of New York, 1937, ch. 353, § 3(6)(g).

28. N.Y. MULT. DWELL. LAW § 309(5)(e).

cities cannot be accomplished by clearance and redevelopment alone. Although clearance and redevelopment is effective in eliminating small pockets of slums, it is extremely expensive and does nothing to prevent the growth of new slum areas.[29] As a result, the success of the urban renewal effort depends upon effective conservation and rehabilitation programs aimed at preserving and restoring existing neighborhoods.[30] Essential to the success of a conservation and rehabilitation program is firm and vigorous enforcement of housing codes. These codes, however, have not been stringently enforced because of ineffective administration and a lack of adequate sanctions.[31] In some cities, fines or even jail sentences result when repair orders are violated,[32] but owners frequently treat the fines as a cost of doing business, preferring the risk of a fine to the expense of making repairs.[33] Code provisions requiring vacation of substandard dwellings until repairs are made[34] have proved ineffective because many owners would rather vacate than make the required repairs. The result is boarded-up dwellings which accentuate the decline of the neighborhood and decrease the supply of adequate low-rent housing.[35] Some municipal ordinances permit the city to make needed repairs and to place a subordinate lien on the property for the cost.[36] This approach also has been ineffective since the city often does not recover the cost of repair because the property is already mortgaged in excess of its value.[37]

In light of past failures to enforce housing codes adequately,

29. It has been estimated that the total cost to redevelop the residential slums and blighted areas in the United States would be 85.5 billion dollars. DEWHURST, AMERICAN NEEDS AND RESOURCES 511-12 (1955). See generally JOHNSON, MORRIS, & BUTTS, RENEWING AMERICA'S CITIES 76-103 (1962); Siegel, *Slum Prevention—A Public Purpose*, 35 CHICAGO B. RECORD 151 (1954); Note, 72 HARV. L. REV. 504 (1959).

30. See NEW YORK CITY PLANNING COMMISSION, URBAN RENEWAL (1958); PRESIDENT'S ADVISORY COMM. ON GOVERNMENT HOUSING POLICIES AND PROGRAMS, REPORT TO THE PRESIDENT OF THE UNITED STATES (1953); Guandolo, *Housing Codes in Urban Renewal*, 25 GEO. WASH. L. REV. 1 (1956); Osgood & Zwerner, *Rehabilitation & Conservation*, 25 LAW & CONTEMP. PROB. 705 (1960). See generally Comment, *Conservation and Rehabilitation of Housing—An Idea Approaches Adolescence*, 63 MICH. L. REV. 892 (1965).

31. See Note, 78 HARV. L. REV. 801 (1965); Note, 72 HARV. L. REV. 504 (1959).

32. See, *e.g.*, Sarasota, Fla., Ordinance No. 827, § 11 (1954); NEW HAVEN, CONN., HOUSING CODE ¶ 102 (1962); WASHINGTON, D.C., HOUSING REGULATIONS § 2104 (1962); PHILADELPHIA, PA., GENERAL ORDINANCES § 7-104 (1956), as amended, March 31, 1964; CHICAGO, ILL., MUNICIPAL CODE § 39-4 (1963). See Note, 78 HARV. L. REV. 801, 820 (1965).

33. See N.Y. Times, Nov. 28, 1955, p. 33, cols. 3-4.

34. See, *e.g.*, CHICAGO ILL., MUNICIPAL CODE § 39-12 (1963); Houston, Tex., Ordinance No. 9354, §§ 7-9 (1953); see 69 HARV. L. REV. 1115, 1123 (1956).

35. See 69 HARV. L. REV. 1115 (1956).

36. See People *ex rel.* Gutknecht v. Chicago, 3 Ill. 2d 539, 121 N.E.2d 791 (1954). See, *e.g.*, LA. REV. STAT. §§ 40:561-72 (1950); N.C. GEN. STAT. § 160-184 (1964); S.C. CODE ANN. § 36-502 (1962); TENN. CODE ANN. § 13-1203 (1955).

37. See Note, 72 HARV. L. REV. 504 (1959).

New York's 1962 law represents an important step forward. The law, however, does have shortcomings.[38] Generally, the appointment of a receiver is a time-consuming process because of the numerous procedural safeguards built into the statute.[39] Furthermore, utilization of a city agency as receiver may put severe strains on public financial resources, thus reducing the number of dwellings repaired and curtailing vigorous prosecution of the program. In addition, political expediency may demand that only buildings in the poorest state of repair be included in the receivership program, so as to provide immediately noticeable improvements. Inherent in such a situation, moreover, is the possibility that the repairs may be so costly that rental income during the useful life of the building will not be sufficient to pay for the renovations; the receivership may then amount to little more than a disguised subsidy. An increase in the rental rates to eliminate the subsidy, however, would tend to displace low-income tenants, thus defeating in large part the goals of the urban renewal program.[40]

Since most of the above shortcomings can be avoided if the receivership program is well administered, the advantages of the 1962 Receivership Law seem to outweigh its possible deficiencies. Furthermore, as the Housing Act of 1964 has made federal funds available to aid municipalities in financing code enforcement,[41] it is to be expected that more thorough inspections will uncover more code violation than heretofore. Strict code enforcement, employing the sanctions of the 1962 Receivership Law, is likely to produce wider voluntary compliance, thereby creating an atmosphere of improvement rather than of decline.[42] It is to be hoped that this will restore the confidence of private investors and attract new capital to declining areas.[43] Since prior liens can serve as an effective additional tool in a comprehensive conservation and rehabilitation program, it is hoped that similar laws will be enacted in other jurisdictions where emergency conditions warrant use of the police power.

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38. See generally Note, 78 HARV. L. REV. 801, 828-30 (1965).

39. See text accompanying notes 13-16 *supra*.

40. Notwithstanding these potential shortcomings, the Deputy Commissioner of New York City's Department of Buildings speaks of the Receivership Law in enthusiastic terms: "Receivership is an essential and primary code enforcement weapon. . . . Unlike other available remedies, receivership provides a means of assuring, as an end product, total or substantial code enforcement. . . . [It] is the only legal weapon that generates activity by all parties who have an interest in the property. . . . For the first time we possess a tool which can assure the repair of dilapidated structures." Gribetz, *New York City's Receivership Law*, 21 J. HOUSING 297-300 (1964).

41. Housing Act of 1964, § 301(b), 78 Stat. 785, 42 U.S.C.A. §§ 1460(c), 1453(a)(2)(A) (1964).

42. Gribetz, *supra* note 40, at 300.

43. NEW YORK CITY PLANNING COMMISSION, URBAN RENEWAL (1958).