Cornell Law Review

Volume 16
Issue 1 *December 1930*

Article 4

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Recommended Citation

Leonard B. Zeisler, *Mortgage Registry Tax in New York*, 16 Cornell L. Rev. 74 (1930)
Available at: http://scholarship.law.cornell.edu/clr/vol16/iss1/4

THE MORTGAGE REGISTRY TAX IN NEW YORK

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Under Article II of the Tax Law a tax is imposed on each mortgage on real property situated within the state recorded on or after July 1, 1906 of 50 cents for each $100 of principal debt secured thereby and it is further provided (Section 255) that

> "If subsequent to the recording of a mortgage on which all taxes, if any, accrued under this article have been paid a supplemental instrument or mortgage is recorded for the purpose of correcting or perfecting any recorded mortgage, or pursuant to some provision or covenant therein, or an additional mortgage is recorded imposing the lien thereof upon property not originally covered by or not described in such recorded primary mortgage for the purpose of securing the principal indebtedness which is or under any contingency may be secured by such recorded primary mortgage, such additional instrument or mortgage shall not be subject to taxation under this article, unless it creates or secures a new or further indebtedness or obligation other than the principal indebtedness or obligation secured by, or which under any contingency may be secured by, the recorded primary mortgage."

Two of the questions arising under these statutes will be discussed here.

I. Under what circumstances must a tax be paid upon the recording of a mortgage which does not create a new debt?

II. Under what circumstances will a mortgage be regarded as creating a new debt?

At first it was thought that no mortgage could be a supplemental mortgage if the primary mortgage had been discharged of record.[1]

Later it was decided in two cases that where a subsequent mortgage is executed "pursuant to some provision or covenant" of a primary mortgage, it is supplemental thereto even though the primary mortgage is discharged of record.[2] In the first of these cases it was held

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[1]People *ex rel.* Astor Trust Co. v. State Tax Commission, 174 App. Div. 320, 160 N. Y. Supp. 859 (3rd Dept. 1916), relying upon a dictum of Kellogg, J., in Hygienic Ice Co. v. Franey, 142 App. Div. 143, 127 N. Y. Supp. 30 (3rd Dept. 1911). In People *ex rel.* U. S. Title Guaranty Co. v. State Commission, 230 N. Y. 102, 129 N. E. 222 (1929), some of the court's language indicated that it held the same opinion.

[2]People *ex rel.* Home Mortgage Investment Co. v. State Board of Tax Commissioners, 182 App. Div. 699, 169 N. Y. Supp. 978 (2nd Dept. 1928); People *ex rel.* New York Title & Mortgage Co. v. State Tax Commission, 220 App. Div. 396, 221 N. Y. Supp. 646 (3rd Dept. 1927), *aff'd,* in 245 N. Y. 603, 157 N.E. 875 (1927).

that a supplemental mortgage was exempted from tax by Section 255 even if the provision of the primary mortgage pursuant to which it was executed did not require its execution but merely gave one of the parties an option to require it. This case was cited with approval in *People ex rel. U.S. Title Guaranty Co. v. State Tax Commission,*[3] which held that a mortgage, executed pursuant to a provision of the primary mortgage that upon the request of the mortgagor, the mortgagee might, at its option, satisfy the primary mortgage and make a larger loan, to be secured by a new mortgage in lieu of the one discharged, was not exempted from tax by Section 255. The court said that such a provision imposed no obligation on anyone and therefore was not a covenant at all but merely an assertion that the parties had capacity to make another contract if they chose.

In *People ex rel. New York Title & Mortgage Co. v. State Tax Commission*[4] the primary mortgage provided that "upon completion of the buildings about to be erected upon the premises covered and affected by this mortgage, this mortgage shall be divided into two separate mortgages, each to cover a portion of the premises herein described, in such sums as may be agreed upon by the mortgagor and mortgagee, but not to exceed the aggregate sum hereby secured."

The Appellate Division held that this was a covenant within the meaning of Section 255, saying:

> "Here the only uncertainty in the provision for the new mortgages was that the separate mortgages were to be divided 'in such sums as may be agreed upon by the mortgagor and mortgagee.' Very likely this provision could not have been enforced by specific performance or otherwise, if one party had refused to be bound by it . . . The situation did not arise. The parties recognized the obligation and performed; and no significance need now be attached to this indefinite term."[5]

The court went on to hold that the tax was imposed erroneously, and this decision was affirmed without opinion by the Court of Appeals.

In *People ex rel. Williamsburgh Savings Bank v. State Tax Commission,*[6] decided by the Court of Appeals on the same day as the previous case, the supplemental mortgage was executed pursuant to the

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[3]Supra note 1.

[4]Supra note 2.

[5]*Ibid.* 400, 221 N. Y. Supp. at 649. In St. Regis Paper Co. v. Hubbs & Hastings Paper Co., 235 N. Y. 30, 138 N. E. 495 (1923) cited by the Court it was held that a similar agreement was merely an agreement to make a future agreement and not enforceable.

[6]245 N. Y. 414, 157 N. E. 513 (1927).

following provision of the primary mortgage: "It is expressly understood and agreed that the party of the second part [the mortgagee], its successors or assigns, if it so elects, *may replace* this mortgage by twelve permanent mortgages, each to cover a portion of the hereinbefore described premises, and which twelve mortgages shall be given as security for a sum aggregating the amount of the principal sum secured hereby." The Appellate Division construed the provision as binding upon the mortgagor and held that the supplemental mortgage was executed pursuant to a covenant of the primary mortgage. The Court of Appeals came to the opposite conclusion.

Since the Court of Appeals wrote no opinion in the former case and since its opinion in the second case gives no reason for its conclusion, it is impossible to tell on what ground the court based the distinction which it seems to have made. It may have believed that both provisions were too vague to be enforced, and yet affirmed the *New York Title & Mortgage Co.* case on another ground. But the only other ground on which the mortgage in that case could possibly be exempted from tax is that is was recorded "for the purpose of correcting or perfecting any recorded mortgage." And it is difficult to see how a mortgage which has been discharged of record can be corrected or perfected. Whatever the court's reasons may have been, these decisions cannot fail to bring confusion into the law on this subject.

If we disregard that *New York Title & Mortgage Co.* case there is very little authority on the question when a supplemental mortgage may be regarded as being recorded "for the purpose of correcting or perfecting any recorded mortgage." But on general principles it seems clear that so long as the primary mortgage is not discharged, any instrument making changes in any of its provisions is embraced in this language.

In *Metropolitan Trust Co. v. State Board of Tax Commissioners,*[7] the court held that an instrument in the form of a supplemental mortgage, which makes no change in the provisions of the primary mortgage except to subordinate it to additional mortgages should be construed as a mere subordination agreement, not subject to tax, though not executed for the purpose of correcting or perfecting the original mortgage or pursuant to any provision thereof. The decision is no doubt correct though the reason given therefor is wrong. The instrument in question was in the form of a mortgage, and it changed one of the provisions of the mortgage. Section 255 applies to any *instrument* supplemental to a mortgage and it is difficult to see what else the instrument in question was, whether it be regarded as a

[7]172 App. Div. 653, 158 N. Y. Supp. 796 (1st Dept. 1916).

mortgage or a contract. Nor is there any reason why it should not be regarded as correcting or perfecting the primary mortgage.

That this clause will be very liberally construed would seem to follow from the case of *People ex rel. Banner Land Co. v. State Tax Commission*.[8] There it was held that where, at the time of recording certain mortgages, a mortgagor paid the recording tax measured by the full amount to be advanced, but transferred the premises after receiving less than one-third of that amount, and where thereafter the purchaser, in order to procure from the mortgagee the balance secured by and agreed to be advanced under the mortgages, was compelled to execute new mortgages upon the same premises as collateral security for the payment of the original bonds and mortgages, a recording tax upon the new mortgages was improperly imposed. The court said that:

> "[T]he mortgagee under its agreement with the first mortgagor had the right to refuse to make further advances because of the transfer by that mortgagor to the present mortgagor, and by virtue of this right it insisted that the latter should execute the second mortgages as collateral before making the full advances under the first mortgages. For practical purposes the second mortgages were therefore executed for the purpose of 'perfecting' the original mortgages. By the execution of the latter mortgages the first ones were so strengthened or perfected that the mortgagee was willing to proceed under them and make advances which it had originally agreed to make."[9]

Another situation which requires some examination is the following. Supposing that a mortgagee wishes to make the mortgagor an additional loan, and to have the entire amount secured by a first mortgage on the same piece of land. He may do this in several ways. (1) He may enter into an agreement with the mortgagor that the additional amount he lends him shall be secured by the mortgage which he already holds or (2) he may have the mortgagor execute to him a new bond and mortgage for the amount of the old debt plus the new loan, cancel the old bond and discharge the old mortgage of record, or (3) he may have the mortgagor execute to him a new bond and mortgage for the amount of the new loan and enter into an agreement with him consolidating the old and new bonds and mortgages, and substituting a single bond for the two thus consolidated. If the mortgagee adopts the first alternative a tax will be assessed only on the amount of the additional loan. If he adopts either of the other two, a tax will be assessed on the amount of the entire debt, old and new, unless the original mortgage made provision for such an additional loan.

[8] 244 N. Y. 159, 155 N. E. 84 (1926).

[9] *Ibid.* 165, 155 N. E. at 86.

If he adopts the first alternative he will bring himself within the provisions of Tax Law Section 250.[10] The second alternative was the one adopted by the parties in *People ex rel. U. S. Title Guaranty Co. v. State Tax Commission.*[11] Though the substance of what the parties did there was the same as if the first method had been adopted, the instrument to be recorded was in form a mortgage and was not exempted from the tax by Section 255. Therefore the court could reach no other conclusion than that a tax must be assessed on the entire amount of the debt.

The third alternative was that adopted in *People ex rel. Jewelers Building Corp. v. State Tax Commission.*[12] There it was held that a mortgage recording tax was properly assessed on $1,000,000 upon the recording of an agreement consolidating a prior bond and mortgage for $750,000 with a bond and mortgage for $250,000 executed and delivered at the time of the consolidation agreement and covering the identical property, where the consolidation agreement was accompanied by a bond of $1,000,000 and provided for the elimination of the prior bonds of $750,000 and $250,000 respectively. The court said that the consolidation agreement was a mortgage because it imposed upon the real property described in the instruments a mortgage lien to secure the payment of the bond for $1,000,000; and since it was not within any of the exceptions provided for in Section 255, the tax should be assessed on the full amount of the new bond, but that no tax could be imposed on the $250,000 mortgage because the bond for that amount created no debt and the mortgage never had any vigor.

It is difficult to see how this decision can be sustained on any ground. The substance of what the parties did was to increase the amount of the indebtedness secured by the first mortgage. If the consolidation agreement was in the ordinary form, and there is nothing in the case to show that it was not, it did not create any lien nor purport to do so. All it purported to do was to combine two existing liens into one. The mortgages for $750,000 and $250,000 were

[10]Section 250 provides so far as material here that "the term 'mortgage' as used in this article includes every mortgage or deed of trust which imposes a lien on or affects the title to real property, notwithstanding that such property may form a part of the security for the debt or debts secured thereby... A contract or agreement by which the indebtedness secured by any mortgage is increased or added to, shall be deemed a mortgage of real property for the purpose of this article, and shall be taxable as such upon the amount of such increase or addition."

[11]*Supra* note 1.

[12]214 App. Div. 99, 210 N. Y. Supp. 263 (3rd Dept. 1925), *aff'd,* 241 N. Y. 524, 150 N. E. 539 (1925).

not discharged of record nor did the cancellation of the bonds for those amounts and the substitution of the bond for $1,000,000 have that effect. It is elementary that no change in the form of the instrument evidencing an indebtedness discharges the mortgage unless a contrary intention appears.[13] This rule was recognized by the courts

[13]Noel v. Murray, 13 N. Y. 167 (1856) holding that the acceptance of the note of a third person by the creditor from his debtor does not operate as a satisfaction of the precedent debt unless it be shown that such at the time was the agreement of the parties and the onus of proving it is upon the debtor. Followed in Dibble v. Richardson, 171 N. Y. 131, 138, 63 N. E. 829, 831 (1902).

Hill v. Beebe, 13 N. Y. 556, (1856) holding that where a first mortgage was given to secure a debt evidenced by the note of the mortgagor and after default the note was surrendered and a new note was given for its amount and some additional indebtedness and a second mortgage on the same property executed to secure that amount the first mortgage was not extinguished.

Feldman v. Beier, 78 N. Y. 293 (1879) following Hill v. Beebe.

Flower v. Lance, 59 N. Y. 603, 608 (1875): "The taking by a creditor of a new obligation for a pre-existing debt, does not discharge the latter unless it is so agreed; and the intent that a new security shall extinguish the original indebtedness must be proved, or else it will be regarded as still subsisting, and the new obligation will be deemed to have been taken as security only."

Jagger Iron Co. v. Walker, 76 N. Y. 521, 525 (1879): "The giving up of one promise to pay, and taking another from the same party, is but a continuation of the promise, and the giving of further time to perform it. As the first did not pay the debt, the other does not redeem the promise of the first, nor itself pay the debt." *In re* Utica Nat. Brewing Co., 154 N. Y. 268, 48 N. E. 521 (1897) holding that whether the second note pays the first depends upon the intention of the parties as manifested by the facts and circumstances attending the transaction. Riegel v. Belt, 119 Ohio St. 369, 378, 379, 164 N. E. 347, 350 (1928): "By the overwhelming weight of authority it is established that no change in the form of indebtedness, or in the mode or time of payment, will operate as payment or discharge of a mortgage; that a mortgage secures the debt, and not the note or bond or other evidence of the debt; and that nothing short of actual payment of the debt or an express release, will operate to discharge the mortgage."

Lomas & Nettleton Co. v. Isaes, 101 Conn. 614, 127 Atl. 6 (1924).

Stein v. Kaum, 244 Ill. 32, 91 N. E. 77 (1910).

Christian v. Newberry, 61 Mo. 446 (1875),

Bond v. Liverpool & London & Globe Ins. Co., 106 Ill. 654 (1883) where the original note was replaced by the note of a third party. Cansler v. Sallis, 54 Miss. 446 (1877) where the substituted note and mortgage were made to the grantee of the original mortgagee.

Bachmann v. Hurtt, 26 Wyo. 332, 184 Pac. 709 (1919) where it was held that the rule applied where there was a change of debtor as well as where there was a change of creditor.

United States v. Grover, 227 Fed. 181, 183 (N. D. Col. 1915): "It is well settled that, where a mortgage is renewed before maturity, or the evidence of the debt is changed by the substitution of new notes therefor, or such portion of the state long before the enactment of Chapter 11 of the tax law and had been applied by the courts in at least two cases decided under that law before the decision in the case under consideration, as will be seen below. The fact that the bond for $250,000 was cancelled before any money was advanced on it is therefore entirely immaterial. The court should have held that the $250,000 mortgage was subject to tax and that the consolidation agreement was not.

The first of the decisions above referred to holding that a "new or further indebtedness" is not created within the meaning of Section 255 by a change in the form of the instrument evidencing an indebtedness is *People ex rel. Home Mortgage Investment Co. v. State Board of Tax Commissioners.*[14] In that case thirty-three $1,000 bonds, and a mortgage securing them were given by a borrower to a lender to take up a former bond for $33,000 and a mortgage securing it given by the former to the latter. The terms of payment of the new bonds were the same as those of the old bonds. The court said:

> "The tax is upon the debt . . . The new mortgage did not affect the debt; it was but the substitution of an instrument that afforded the same collateral security. The mere change of 33 bonds for $1,000 each for 1 bond of $33,000 was but a change in the form of the debt and did not extinguish or affect the lien . . . Hence, to exact a second tax is to lay a second

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thereof as may remain unpaid, the lien of the mortgage is not lost or affected, unless the circumstances of the transaction disclose clearly that it was the intention of the parties to create a new security and treat the old as canceled.... And the fact of entering satisfaction of the existing mortgage when taking a new one, if the latter be designed by the parties as a mere continuation of the first, when the two acts are a part of the same transaction, does not operate as an extinguishment of the mortgage, but will be regarded as a renewal thereof, and not as abandoning the lien and letting in intervening equities.... So long as the same debt or some part of it, subsists, the presumption ordinarily is that the new mortgage is intended as a renewal of the old, and a continuance of the same security....Nor does the including in the new mortgage of an additional indebtedness not covered by the first discharge the lien of the old mortgage, so far as the indebtedness thereby secured remains unpaid, unless such be the purpose of the parties....And very clearly the difference in the rate of interest between the two mortgages where, as here, the rate is less in the last mortgage, than in the first, cannot be regarded as material to indicate an intention to create a new obligation and abandon the security of the old.... So far as the difference in the parties to the two instruments is concerned, to which the master refers, manifestly that cannot be regarded as a material circumstance supporting his conclusion, where, as here, the mortgagee in the second mortgage are the successors in interest and privies in estate with the one who held the first."

[14]*Supra* note 2.

impost upon the self-same debt because of a variation in the form of the obligation and the security for the debt."[15]

The next case in which this question was involved is *People v. Boston & Maine Railroad*.[16] There bonds issued under the terms of a trust mortgage were sold and their proceeds used for the purpose of retiring matured bonds secured by the same mortgage. The question arose whether a recording tax measured by the principal sum of the new bonds was payable under Section 259, which provides that if the amount of principal indebtedness secured by a mortgage has not been advanced when the mortgage is recorded the tax shall be measured by the advances which have then actually been made and whenever a further amount is to be advanced a tax on such further amount shall be paid.[17] The court held that the new bonds represented a further amount advanced under the original mortgage. It said:

> "There is no provision in the mortgage or otherwise requiring the original bondholders to accept new bonds in place of those matured. They were entitled to have their bonds paid. The transaction was in no sense an exchange of bonds. The new bonds were placed on the market and the proceeds thereof used to pay and discharge the old bonds. The indebtedness, therefore, was not the same. The transaction consisted of the substitution of one 'principal indebtedness' in place of another . . . ."
>
> "If this trust mortgage contained no refunding provisions and the defendant were required to resort to another mortgage to secure its new bonds there would be no question about its liability for the tax. This court has said: 'The statute does not contemplate that if a man pays one mortgage with money borrowed upon another mortgage, the latter mortgage is exempt from taxation.' (*People ex rel. Astor Trust Co. v. State Tax Commission*, 174 App. Div. 320, 326). A party may not indirectly accomplish that which by direct methods the law does not permit."[18]

In *Matter of New York State Gas & Electric Corporation v. Gilchrist*,[19] it was held that a mortgage tax cannot legally be imposed

[15] *Ibid.* 701, 169 N. Y. Supp. at 980.

[16] 202 App. Div. 54, 195 N. Y. Supp. 402 (3rd Dept. 1922), *aff'd*, 234 N.Y. 629, 138 N. E. 475 (1922).

[17] Although this case and the one following were decided under section 259 of the Tax Law, whose language is not the same as that of section 255 which is under consideration here, the issue upon which the decision in these cases hinged is the same, namely, whether a new debt was created. Therefore these cases are deemed relevant here.

[18] *Ibid.* 55, 195 N. Y. Supp. at 403.

[19] 209 App. Div. 771, 205 N. Y. Supp. 501 (3rd Dept. 1924), *aff'd*, 240 N. Y. 552, 148, N. E. 701 (1925).

upon bonds of a corporation issued to replace bonds theretofore issued under the same mortgage though the new bonds mature at a later date and carry a different interest rate, where the mortgage authorizes the issuance of refunding or replacing bonds and the substituting bonds so issued are not sold but are delivered to the original bondholders in exchange for the original bonds which are surrendered and cancelled. The *Boston & Maine* case was distinguished on the ground that in the latter case the bonds were issued for the purpose, not of sale, but of direct substitution. The court said:

> "The mortgagor, by an agreement made in advance of the issue, was obliged to give new bonds for old, while the mortgagee was obliged to make the exchange. It is true that by the new bonds the mortgagor promised to pay in 1962 what it had previously agreed to pay in 1947 and 1952. It is also true that it promised to pay interest at five and one-half per cent whereas it had previously agreed to pay interest at five and six per cent. Was there an additional 'principal debt or obligation' to measure an additional tax upon the identical mortgage? A debt is not merely a promise to pay money. It involves the relationship of debtor and creditor, of borrower and lender, and ordinarily signifies an exchange of cash for a promise to return it with an increment of interest. There was here the creation of no new relationship; there was no new creditor, no new debtor, no new loan. It must be remembered that it is the principal sum of a loan, not the interest to be paid thereupon, which measures a mortgage tax. Here there was no new principal sum although there was a new interest rate and a new date of payment. 'Whenever a further amount is to be advanced under the original mortgage,' a tax, measured by the advance must be paid. No 'further amount' was advanced under this mortgage. In this respect the case is essentially different from the *Boston & Maine* case. In my judgment the tax which has been paid was not legally imposed."[20]

The distinction between the cases seems to be that in the first case both debtor and creditor apparently intended to extinguish the original indebtedness, whereas in the latter they did not so intend. Two recent cases in which this question arose were *People ex rel. Banner Land Co. v. State Tax Commission*,[21] and *People ex rel. Williamsburgh Savings Bank v. State Tax Commission*.[22] In both cases the supplementary mortgage was executed by the grantee of the original mortgagor. In the former case the court thought that the supplemental mortgage did not create a new debt, because it was executed as

[20]*Ibid.* 774, 205 N. Y. Supp. at 504.
[21]*Supra* note 8.
[22]*Supra* note 6,

collateral to the existing primary obligation. In the latter case it said:

> "The mortgage is clearly taxable. One lien has been satisfied of record and destroyed. Another debtor has created another lien in its place. There is a new transaction with a new tax."[23]

In the *Williamsburgh Savings Bank* case it clearly appeared from the facts as stated by the Appellate Division that the parties did not intend to extinguish the original indebtedness but intended to change merely the form of the security evidencing the indebtedness. In the *Banner Land Co.* case the supplemental mortgage obviously was not evidence of the original debt since the original mortgage remained in force. According to the principles theretofore established the court would have been obliged to hold that a new obligation had been created by the collateral mortgage though one payment would extinguish both old and new obligations.

But it seems to be settled, as the result of the last four decisions of the Court of Appeals, that the criteria, previously established, for determining when an old debt has been extinguished and a new one created will not be applied when the question arises under the Mortgage Registry Tax Law.

What criteria will be applied is not so clear. It might be argued from the *Jewelers Building Corporation* case, the *Banner Land Co.* case and the *Williamsburgh Savings Bank* case that the court had decided that the instrument evidencing the debt must be treated, at least for the purposes of this statute, as the debt itself. But in the *New York Title & Mortgage Co.* case the old evidences of debt were cancelled and new ones substituted. Yet the court decided in favor of the relator. The decision of the Appellate Division was expressly based on the ground that no new debt had been created and was affirmed by the Court of Appeals without opinion. There seems to be no principle on which the cases can be reconciled with each other or with the previous cases.

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[23]*Ibid.* 418, 157 N. E. at 514.