

# Condominium Liens and the Priority of a Consolidated First Mortgage—Revisited

By Joel David Sharrow

In *Bankers Trust Company v. Bd. of Mngrs of Park 900 Condominium*,<sup>1</sup> the Court of Appeals held that a first mortgage of record has priority<sup>2</sup> over a condominium board's subsequently filed statutory lien for unpaid common charges<sup>3</sup> and that such subordinate lien is cut off by foreclosure of the first mortgage of record.<sup>4</sup> But there appears to be some uncertainty whether foreclosure of a first mortgage of record, which has been consolidated with a junior mortgage recorded (collectively, the "Foreclosing Mortgage") and the consolidation occurring before a condo board's lien is filed, fully wipes out the statutory lien or if the Foreclosing Mortgage must be split into its component parts with only the initial first mortgage of record retaining its priority over the condo board's lien.<sup>5</sup> Yet, detailed familiarity with all of the facts, motions and appellate briefs in *Bankers Trust Co.* (where the bank held two (2) separate consolidated and cross-collateralized first mortgages of equal priority upon two condominium units) as well as the legislative history of RPL § 339-z suggests—indeed, may compel—the conclusion that there should be no such uncertainty. A Foreclosing Mortgage retains the first mortgage priority of all of the previously recorded and consolidated mortgage liens over the condominium's later filed lien.

## The Basis of the Confusion

The apparent confusion arose out of the nature of consolidated liens, predicated upon the interplay of two well-settled concepts. First, a mortgagee's rights generally are fixed at the time its mortgage(s) are recorded, and cannot be enlarged or

impaired by subsequent acts of the mortgagor.<sup>6</sup> Second, and as a result of that first rule, is the elementary tenet that consolidation benefits only the parties to it:

A consolidation of outstanding loans is a device intended for the convenience of only the contracting parties. A consolidation agreement cannot impair liens in favor of parties that are not the contracting parties, which retain their independent force and effect ([citing, *Dime Sav. Bk. v. Levy*]; *Dominion Fin. Corp. v. 275 Washington St. Corp.*, 64 Misc. 2d 1044 [Sup., Westch. Co., 1970]).<sup>7</sup>

In *Dominion Fin. Corp.*, cited by *Fed. Dep. Ins. Co.*, the court correctly held that where a lease had been recorded during the interstitial gap of the recording of an earlier second mortgage with a subsequently recorded and consolidated third mortgage, such consolidation could not "prime" the interests of the priority of the lease because the tenant was not a party to the consolidation agreement. Thus, the lease retained its priority over the later recorded third mortgage portion of the consolidated liens.

Therefore, the Court in *Societe Generale*, while citing the Appellate Division's affirmance of summary judgment to the bank under RPL § 339-z in *Bankers Trust*,<sup>8</sup> nevertheless found the nature and effect of consolidation agreements to be controlling. It held that although the lender recorded a consolidation of a reduced pre-existing first mortgage with a new second mortgage earlier than the recording of the condo

board's statutory lien, there still were two mortgages, only one of which could be a first mortgage under RPL § 339-z.<sup>9</sup>

It may be, and this writer submits, that such "split priority" injected into RPL § 339-z by *Societe Generale* (later expressly rejected by both *Dime Sv. Bk.* and *Greenpoint Bank*),<sup>10</sup> stemmed from the fact that in *Bankers Trust* the Appellate Division—and, thereafter, the Court of Appeals—held that the lender's two equal in lien cross-collateralized and consolidated first mortgages were, for purposes of RPL § 339-z, only one first mortgage of record. Consequently, it may be that the court in *Societe Generale* was unaware of the number of mortgages held by the bank in *Bankers Trust*, that they were consolidated mortgages, and then spread and cross-collateralized.

## The Bankers Trust Case

In *Bankers Trust* a series of purchase money and other mortgages on two condominium units had been assigned to the bank by a prior mortgage. The bank then advanced additional funds to the unit owner and the repayment of such new monies was secured by new mortgages on each of the units. The previously assigned and the bank's subsequent new mortgages on each unit were consolidated; and, as consolidated, each was cross-spread. As a result, the bank wound up holding two equal first mortgages of record on both units.<sup>11</sup> The Board filed its statutory lien after the bank recorded its mortgages, their consolidation and cross-collateralization.

During the pendency of the Board's appeal to the Appellate Divi-

sion from the award of summary judgment to the bank, the Board cross-moved in the IAS Court for an Order, among other things, splitting the consolidated mortgages into their earlier and later new mortgages. If successful, the Board's much later lien for unpaid common charges would have had priority over the lien of the bank's new mortgages. The IAS Court denied that motion<sup>12</sup> and the Appellate Division affirmed summary judgment for the bank.<sup>13</sup>

Thereafter, the Board did a one hundred and eighty degree turn-around. In its brief to the Court of Appeals, the Board went out of its way to explicitly acknowledge that the bank held two consolidated *first* mortgages of record.<sup>14</sup>

The Court of Appeals did not address the fact that the bank held two consolidated mortgages or the general rule regarding the nature and effect of consolidation of liens. Instead, just as the Appellate Division had previously concluded, the Court of Appeals viewed the bank's Foreclosing Mortgages as but a single first mortgage of record.<sup>15</sup>

The implicit holding in each of the decisions in *Bankers Trust* was that when the new mortgages granted to the bank had been recorded and consolidated with the previously assigned pre-existing mortgages on the two units and cross-collateralized, all of which took place before the Board filed its lien for unpaid common charges, any subordinate status of the bank's new mortgages to the previously assigned earlier mortgages was irrelevant.<sup>16</sup>

### **The Legislative History of RPL § 339-z**

The Appellate Division's decision to affirm summary judgment for the bank rested not only upon the express language of RPL § 339-z, but also upon the statute's legislative history.<sup>17</sup> The bank showed that on

and after the 1964 enactment of the Condominium Act, RPL Art. 9-B,<sup>18</sup> RPL § 339-z, its then amendments, and a 1991 unadopted proposed amendment, that the Legislature consistently intended that a lender's earlier recorded first mortgage of record retains its priority over a residential condominium's board's subsequently filed "priming" statutory lien for unpaid common charges.

The proof is in the pudding: First, the initial amendment of RPL § 339-z occurred in 1974, and provided that the declaration of an exclusively non-residential condominium could provide that a board's lien for unpaid common charges would be superior to even a first mortgage of record.<sup>19</sup> Second, in 1988, RPL § 339-z was amended to exclude from the priority of a board's lien subordinate mortgages granted to the Urban Development Corporation, and the State Assembly's Legislative Memorandum in support of such amendment stated: "*The statutory protection of first mortgages against the risk of subordination to liens for subsequently occurring unpaid common charges should likewise be extended to subordinate mortgages held by UDC, and Section 339-z should be modified accordingly (emphasis added).*"<sup>20</sup> Third, by contrast in 1991, a bill was introduced in the state Senate which provided that even in an exclusively residential condominium, there should be certain instances where a board's later lien would prime even a pre-existing first mortgage of record, either to the extent of six (6) months of unpaid common charges or six (6) months of unpaid charges which became due immediately before commencement of an action to foreclose the first mortgage.<sup>21</sup> That proposed amendment, to alter the established priority scenario, was not enacted.

Similarly not enacted was the post-*Bankers Trust* 1993 Assembly Bill A.438, Senate Bill S.2887, which, similar to the 1991 unenacted proposal, proposed awarding priority to a

condo lien over a pre-existing first mortgage but limiting the priming effect of a board's later filed lien "to the extent of . . . unpaid common charges . . . which would have become due during the six months immediately preceding the date on which the first delinquent installment of the mortgage was due."<sup>22</sup> If adopted, that unenacted 1993 amendment, just like the unadopted 1991 proposal, would have restricted the amount of any legislatively created subordination of a first mortgage of record.

More recently, RPL § 339-z was again amended, with the primary purpose to aid New York City. The 1997 amendment was enacted to give priority to subordinate mortgages of record held by a city municipality having a population of one million or more persons or by the New York City Housing Development Corporation over a condo board's statutory lien.<sup>23</sup> The Memorandum of Legislative Representative of the City of New York, as well as the identical State Senate's Supporting Memorandum, urged enactment of that amendment, as follows:

This legislation will authorize the City and HDC to utilize subordinate mortgage loans as a means to finance the development of condominium units throughout the City of New York. These amendments will remove the existing technical prohibition stifling the City's and HDC's efforts to increase homeownership opportunities in many of New York City's distressed neighborhoods.

Both the City and HDC often utilize their loan powers to advance housing development within the City of New York by leveraging private sector financing. In most cases, the private sector lender's participation in a project is conditioned upon

receiving a sole first mortgage position. Thus, the City or HDC loan may be secured by a second mortgage. Because a condominium unit constitutes real property pursuant to the Section 339-g of the Real Property Law, the City and HDC should be able to accept a subordinate mortgage with respect to a condominium unit, as they currently accept a subordinate mortgage with respect to any other real property.

The State Legislature has previously determined that the first mortgage limitation in the New York Condominium Act does not apply to other development instrumentalities of the State. After enactment of the New York Condominium Act in 1964, Section 339-z and 339-ff were amended twice. Initially these sections were changed to specifically allow the New York State Job Development Authority to accept subordinate mortgages with respect to condominium units and, most recently, to provide the Empire State Development Corporation with similar authority. The City and HDC should be granted a similar exemption.

*The statutory protection of first mortgages of record against the risk of subordination to liens of unpaid common charges should likewise be extended to subordinate mortgages held by the City and HDC. This protection is added in Section 339-z. (Emphasis added).*<sup>24</sup>

Thus, it is beyond cavil that at all times the legislature always knew what it was doing when it enacted, amended—and, rejected certain amendments to—RPL § 339-z. The legislature has never waived in its clearly stated intention that a first

mortgage of record have and retain its priority over a subsequently filed condo board's lien for unpaid common charges which—but for few statutorily stated exceptions—primes and subordinates all other prior liens. Notably, none of these exceptions make a distinction between the initial portions versus the later portions of a consolidated first mortgage of record where all portions are recorded and consolidated before a condominium board gets around to filing its unpaid common charges lien—despite the then-extant, and twice expressly rejected, decision in *Societe Generale*.<sup>25</sup>

## Conclusion

The notion of “hybrid priority” has been around since 1989 and of “split priority” since 1993.<sup>26</sup> Nevertheless, the legislature has not even attempted to overrule the judicial rejections of those concepts by statutory amendment to RPL § 339-z.

Furthermore, based upon the legislative history of the Condominium Act, amendments to RPL § 339-z, as well as the non-enacted proposed amendments thereto, and the legislature's knowledge of the well-settled law regarding consolidated liens,<sup>27</sup> it is submitted that the legislature never intended to allow a pre-existing consolidated first mortgage of record to be broken into its initial and junior liens upon foreclosure when there is a subordinate condominium board's lien encumbering the subject realty.

In addition, each of the Courts in *Bankers Trust* had before them the documentary evidence that the bank held consolidated mortgages.<sup>28</sup> Yet, both the Appellate Division and the Court of Appeals considered the Foreclosing Mortgages to be a single first mortgage of record.

As a result, it is submitted that there should be no reason for any concern arising out of the holding in *Societe Generale*. It is this writer's

opinion that the decision in *Societe Generale* was an isolated aberration; and, as held in both *Greenpoint Bank and Dime Svc. Bk.*, is not to be followed.

## Endnotes

1. 81 N.Y.2d 1033 (1993), *aff'g* 181 A.D.2d 274 (1992), *aff'g* \_\_\_\_ Misc. 2d \_\_\_\_, N.Y.L.J., June 26, 1991, p. 23, col. 1 (Sup. Ct., N.Y. Co.; Gammerman, J.).
2. See Real Property Law § 339-z.
3. See RPL § 339-z and § 339-aa.
4. *Bankers Trust Co.*, 81 N.Y.2d 1033.
5. Compare *Societe Generale v. Charles & Co. Acquisition*, 157 Misc. 2d 643 (Sup. Ct., N.Y. Co. 1993), which “split” a consolidated first mortgage—and thereby extended the basic concept that consolidation of a third or more junior liens with a first lien can not “prime” an intervening pre-existing second lien [e.g., *Skaneateles Svc. Bk. v. Herold*, 50 A.D.2d 85 (4th Dep't 1975), *aff'd* on Op. of App. Div., 40 N.Y.2d 999 (1976)—holding that a condo board's lien for unpaid common charges, filed after the consolidation of earlier recorded mortgage liens, nevertheless “primed” the consolidated first mortgage to the extent that all additional monies advanced by the lender and secured by new liens for such extra funds are subordinate to the condominium's subsequently filed statutory lien, in effect creating a “split priority” of the lender's consolidated first mortgage, not dissimilar to the since-rejected “hybrid priority” of a lender's non-consolidated first mortgage of record lien as enunciated by a court in *East River Savings Bank v. Saldivia*, \_\_\_\_ Misc. 2d \_\_\_\_, N.Y.L.J., Oct. 11, 1989, p. 21, col. 4 (Sup. Ct., N.Y. Co.) and its progeny; see also the affirmed Appellate Division decision in *Bankers Trust*, 181 A.D.2d 274 at 276 (1st Dep't 1992), referring to such unwarranted “hybridization” of priority effected by *Saldivia*, *supra*] with *Greenpoint Bank v. El-Basary*, 184 Misc. 2d 888 (Sup. Ct., N.Y. Co. 2000), rejecting *Societe Generale*, *supra*, and *Dime Svc. Bk. of New York*, F.S.B. v. *Levy*, 161 Misc. 2d 480 (Sup. Ct., Rockland Co. 1994), similarly rejecting *Societe Generale*, *supra*. A more comprehensive discourse of this dichotomy in IAS Court holdings is set out in “Consolidated Mortgage Priority Over Condo Lien,” by Bruce J. Bergman, NYSBA N.Y. Real Property Law Journal, Summer 2003, Vol. 31, No. 2, pp. 77–78.
6. *Fed'l Dep. Ins. Co. v. Five Star Mgm't, Inc.*, 258 A.D.2d 15 (1st Dep't 1999). See also *UMB Bank and Trust Co. v. S.H.M. West Parking Corp.*, 181 A.D.2d 577 (1st Dep't

- 1992) (where three of the four mortgages were consolidated and recorded prior to the recording of a tenancy agreement; those three mortgages, as consolidated, were held to be superior in lien to and, upon foreclosure, wipe out the leasehold rights emanating from the recorded tenancy agreement); and *Citibank, N.A. v. Chicago Title Ins. Co.*, 214 A.D.2d 212 (1st Dep't 1995), *app. dsm.*, 87 N.Y.2d 896 (1995) (each mortgage comprising a consolidated mortgage retains its own original priority).
7. *Fed. Dep. Ins. Co.*, 258 A.D.2d at 22.
  8. 181 A.D.2d 274 (1st Dep't 1992).
  9. 157 Misc. 2d at 646–648.
  10. See note 5, *supra*.
  11. See Record on Appeal in *Bankers Trust* (the "Record") pp. 50–130; 35–38.
  12. The IAS Court orally denied the Board's motion "from the Bench." As a result, the IAS Court's decision was not reported. The short-form Order, simply denying the Board's cross-motion, was entered in the N.Y. Co. Clerk's Office on Apr. 6, 1992.
  13. At the outset of the case, and shortly after the Board had commenced foreclosure of its statutory lien, the bank and the Board stipulated that the bank's consolidated mortgages had complete priority over the Board's unpaid common charges lien. Record, pp. 216–17; and pp. 11–12. See also 181 A.D.2d at 275. Nevertheless, the IAS Court, the Appellate Division, and the Court of Appeals, did not rely upon that stipulation; instead, their respective decisions rested upon the language of RPL § 339-z and/or its legislative history. See, Record, at pp. 12–14 (the IAS Court also expressly agreed with other similar IAS Court holdings construing RPL § 339-z, *id.*, at pp. 13–14); 181 A.D.2d at 276–77 and 278–80 (the Appellate Division also referred to the condominium's By-laws, 181 A.D.2d at 280); and, 81 N.Y.2d, at 1035–36.
  14. See Board's Main Brief on its appeal to the Court of Appeals, at pp. 7–8 thereof.
  15. 181 A.D.2d at 576; 81 N.Y.2d at 1034 and 1035.
  16. See also *Economic Necessity of Lien Priority Of First Mortgages*, by Joel David Sharrow, N.Y.L.J., Apr. 13, 1994, p. 5, col. 2. Compare with *Washington Fed'l Svc. & L. Assoc. v. Scheider*, 95 Misc. 2d 924 (Sup. Ct., Rockland Co. 1978), the first reported decision under RPL § 339-z, where the court correctly held that a lender's second mortgage recorded before a condo board filed its lien nevertheless was statutorily relegated to a position subordinate to the later filed condo lien; and *Foxwood Run Condominium v. Goller Place Corp.*, 166 Misc. 2d 216 at 217 (Sup. Ct., Richmond Co. 1995), where the court acknowledged that while then recent amendments to RPL § 339-z were enacted to induce lenders to extend mortgages to condominiums [op. cit. om.], the amendment[s] had no intention of furthering this goal by derogating the well-established legal concept of 'prior in time, prior in right' [cit. om.]. The logical conclusion is that [RPL § 339-z] applies to the common situation of a first mortgage recorded prior to a recorded common charge lien, but the less common situation as the one at bar, in which a first mortgage is recorded subsequent to a recorded common charge lien, is governed by priority of recording.
  17. At oral argument, the author handed up to the Appellate Division the relevant legislative history of RPL § 339-z and a copy of the condominium's filed By-laws, neither of which had been presented to the IAS Court. The Appellate Division appropriately took judicial notice of and relied upon both. 181 A.D.2d at 278–80, 280. A court may judicially notice legislative history of a statute, *Riley v. County of Broome*, 95 N.Y.2d 455, at 463 (2000), quoting McKinney's Cons. L. of N.Y., 1 Statutes § 92[a] (Courts are to "ascertain and give effect to the intention of the Legislature") and *id.*, § 124 ("legislative history of an enactment may also be relevant 'and is not to be ignored, even if words [of a statute] be clear'") as well as of public documents. See *Sunhill Water Corp. v. Water Resources Comm'n*, 32 A.D.2d 1006 (3d Dep't 1969) (noticing public records); *Siwiek v. Mahoney*, 39 N.Y.2d 159 (1976) (taking judicial notice of information culled from public records); *Rex Paving Corp. v. White*, 139 A.D.2d 176 (3d Dep't 1988) (judicially noticing on appeal public records, including official Executive Memorandum and the Governor's letter). Similarly, the bank submitted the legislative history to the Court of Appeals via an Appendix—albeit raised during oral argument, in its decision the Court of Appeals did not address the legislative history.
  18. See Session Laws of 1964, Ch. 82.
  19. See Session Laws of 1974, Ch. 1056, § 8.
  20. See Memorandum, 1988 Session Laws, at pp. 2128, 2130.
  21. See Senate Bill S.5183, as amended by S.5183-A and S.5183-B.
  22. Assembly Bill A.438.
  23. See Session Laws of 1997, Ch. 349.
  24. See The Legislature, Memoranda, Session Laws of 1997, at pp. 2335–6, 2336–7.
  25. See note 5, *supra*.
  26. *Saldivia*, \_\_\_ Misc. 2d \_\_\_, N.Y.L.J., Oct. 11, 1989, p. 21, col. 4; *Societe Generale*, 157 Misc. 2d 643.
  27. See notes 5, 12 and 16–23, *supra* (Further, it has long been well-settled that the legislature, upon amending a statute, is presumed to know how the courts have construed and enforced the unamended statute); *Orinoco Realty Co., Inc. v. Bandler*, 233 N.Y. 24 at 30 (1922) ("When the Legislature amends or considers afresh a statute it will be assumed to have knowledge of judicial decisions interpreting the statute as then existing, and, if it deals with it in a manner which does not rebut or overthrow the judicial interpretation, it will be regarded as having legislated in the light of and as having accepted such interpretation."); followed by, *Foy v. 1120 Ave. of Americas Assoc.*, 223 A.D.2d 232 at 237 (1st Dep't 1996). See also *Conesco Industries, Ltd. v. St. Paul Fire and Marine Ins. Co.*, 184 A.D.2d 956 at 958–59 (3d Dep't 1992) ("In the absence of a contrary intent, the language of an amendment should be construed in the light of previous judicial decisions construing the original act and the Legislature is presumed to have known of existing judicial decisions in enacting amendatory legislation. [cit. om.]").
  28. See the Record, pp. 50–130; 35–38.

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