Equitable Conversion of Surplus Mortgage Foreclosure Proceeds

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enacting CPLR 214-a.\textsuperscript{263} Moreover, as Dean McLaughlin has suggested, it would be somewhat ironic if the discovery rule was applied liberally in negligence actions yet strictly applied in those actions which were the source of the rule—medical malpractice actions.\textsuperscript{264} Despite these obstacles, it is submitted that the Reis court’s extension “of the Flanagan rule make[s] eminently good sense;”\textsuperscript{275} it seems manifestly unjust to bar a plaintiff from asserting a cause of action before he even knows of its existence.

\textit{Equitable conversion of surplus mortgage foreclosure proceeds.}

It is a settled principle of New York law that there cannot be a tenancy by the entirety in personal property.\textsuperscript{296} When there is a voluntary sale of real property held as a tenancy by the entirety, the proceeds are considered personalty and the tenancy by the entirety is terminated, creating either a joint tenancy or a tenancy in com-


\textsuperscript{265} CPLR 214, commentary at 55 (McKinney Supp. 1977).

\textsuperscript{266} Originally, the New York rule prohibiting tenancies by the entirety in personal property was established by case law. See, e.g., Hawthorne v. Hawthorne, 13 N.Y.2d 82, 192 N.E.2d 20, 242 N.Y.S.2d 50 (1963); \textit{In re Estate of Blumenthal}, 236 N.Y. 448, 141 N.E. 911 (1923); \textit{In re Albrecht}, 136 N.Y. 91, 32 N.E. 632 (1892). The principle since has received statutory codification. EPTL § 6-2.1(a)(4); N.Y. GEN. OBLIG. LAW § 3-311(1) (McKinney 1969).

Only a husband and wife can hold property as tenants by the entirety. \textit{See} Vlcek v. Vlcek, 42 App. Div. 2d 308, 310, 346 N.Y.S.2d 893, 896 (3d Dep't 1973) (there can be no tenancy by the entirety in real property held by parties never married); Ackerman v. Ackerman, 78 Misc. 2d 1, 2, 342 N.Y.S.2d 720, 722 (Sup. Ct. Westchester County 1973), aff'd mem., 45 App. Div. 2d 856, 358 N.Y.S.2d 535 (2d Dep't 1974) (tenancy by the entirety may exist only between a husband and wife validly married at time of transfer of property). EPTL § 6-2.2 is the operative statute in determining the type of tenancy created by a disposition. The only instance in which a tenancy by the entirety may exist appears in subdivision (b) which provides: “A disposition of real property to a husband and wife creates in them a tenancy by the entirety, unless expressly declared to be a joint tenancy or a tenancy in common.” EPTL § 6-2.2(b).

As tenants by the entirety, no one spouse may unilaterally partition the real property, nor dispose of any interest in such property which will adversely affect the other spouse’s right of survivorship. Hiles v. Fisher, 144 N.Y. 306, 312, 39 N.E. 337, 338 (1895). Tenancy by the entirety is based on the common law concept of the unity of husband and wife. \textit{Id.}; Ackerman v. Ackerman, 78 Misc. 2d 1, 1, 342 N.Y.S.2d 720, 722 (Sup. Ct. Westchester County 1973); 9A P. ROHAN, NEW YORK CIVIL PRACTICE § 6-2.2[6][a] (1970). The right of survivorship can be destroyed only by the dissolution of the marriage or the voluntary act of both husband and wife. \textit{In re Estate of Dickie}, 55 Misc. 2d 976, 978, 286 N.Y.S.2d 893, 896 (Sur. Ct. Erie County 1968). For a general discussion of tenancies by the entirety, with emphasis on the spouse’s right to alienate his or her own interest, see Klorfein, \textit{Tenancies by the Entirety in New York}, 9 N.Y.L.F. 460 (1963).
In contrast, where the conversion of real property is deemed involuntary, as in a condemnation proceeding, courts of equity have determined that the resulting funds retain the characteristics of realty and the tenancy by the entirety continues. The distinction between voluntary and involuntary conversions is not always clear, however, and classifying the proceeds is often a difficult task. As a result, substantial controversy has developed as to whether the surplus proceeds of a mortgage foreclosure sale of property owned by tenants in the entirety are to be treated as realty or personalty.

Recently, in Mojeski v. Siegmann, the Supreme Court, Suffolk County, held that surplus monies from a mortgage foreclosure sale are personalty, and, as such, cannot be held as a tenancy by the entirety.

Mojeski was an action to confirm a referee's report in a surplus money proceeding following a mortgage foreclosure and sale of the realty. The referee determined that the surplus funds were personal property and therefore severable, enabling the husband's creditors to be immediately compensated from the husband's share of the funds. The wife contested this determination, asserting that the

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237 See, e.g., In re Estate of Blumenthal, 236 N.Y. 448, 141 N.E. 911 (1923) (without more, a bond and mortgage obtained on the sale of a tenancy by the entirety is held in common); Secrist v. Secrist, 284 App. Div. 331, 132 N.Y.S.2d 412 (4th Dep't 1954), aff'd, 308 N.Y. 750, 125 N.E.2d 107 (1955) (cash proceeds of sale held as a tenancy in common with each spouse entitled to one-half). The dissolution of a marriage by divorce also converts a tenancy by the entirety into a tenancy in common. See, e.g., Steiz v. Shreck, 128 N.Y. 263, 28 N.E. 510 (1891); Martos v. Martos, 206 Misc. 860, 134 N.Y.S.2d 832 (N.Y.C. Mun. Ct. 1954). It should be noted that if the parties expressly so stipulate, the estate will be converted into a joint tenancy, rather than a tenancy in common. EPTL § 6-2.2(a).

238 See, e.g., City of New York v. Gorman, 252 App. Div. 103, 297 N.Y.S. 415 (2d Dep't 1942); In re Idlewild Airport, 85 N.Y.S.2d 617 (Sup. Ct. Queens County 1948).

239 Several courts have adopted the principle of "equitable conversion" to find a tenancy by the entirety in mortgage foreclosure surplus funds, while other decisions have characterized the ownership of the surplus funds as tenancies in common. See notes 275-76 and accompanying text infra.


271 Id. at 694, 386 N.Y.S.2d at 612.

272 Id. at 691-92, 386 N.Y.S.2d at 610.

273 The effect of the referee's decision was to treat the foreclosure sale as a voluntary disposition. Absent a contrary expression, husband and wife are deemed to hold the proceeds of a voluntary sale as tenants in common. See note 267 and accompanying text supra. It has occasionally been argued that because one spouse contributed all or a greater portion of the purchase price, that spouse's interest in the proceeds should be proportionately greater. The courts have generally rejected this argument, however, instead presuming that a gift was intended on the part of the spouse furnishing the consideration. Thus, each spouse is deemed entitled to an equal share of the proceeds. See Secrist v. Secrist, 284 App. Div. 331, 132 N.Y.S.2d 412 (4th Dep't 1954), aff'd, 308 N.Y. 750, 125 N.E.2d 107 (1955); Martos v. Martos, 206 Misc. 860, 134 N.Y.S.2d 832 (N.Y.C. Mun. Ct. 1954).
funds were held by her and her husband as tenants in the entirety. Should the court find an estate by the entirety, no payments could be made from the foreclosure proceeds until the wife's death established her husband's right to dispose of the funds without her consent.274

Noting that the issue presented has not received uniform treatment in New York, the Mojeski court first reviewed the conflicting authorities. Whereas one line of cases holds that surplus funds from a foreclosure sale are constructively real property and therefore accorded tenancy by the entirety status,275 the other line of authority holds that a mortgage foreclosure of realty is to be treated the same as a voluntary conversion of real property.276 Under the latter approach, the resulting proceeds are personal property held as a tenancy in common.277 Basing its decision primarily on a recent Court of Appeals case, Hawthorne v. Hawthorne,278 the Mojeski court aligned itself with the cases holding that surplus proceeds are personalty.279

In Hawthorne, it was necessary for the Court to determine whether the proceeds of a fire insurance policy covering real property held as a tenancy by the entirety should be "impressed in equity with the inseverable quality of the ownership of the realty against whose loss they are payable."280 Declaring that the right to the proceeds stemmed from a "voluntary contractual act,"281 the

274 87 Misc. 2d at 691, 386 N.Y.S.2d at 610. The wife did not object to paying their joint creditors from the surplus fund. Id.

275 The line of decisions construing the surplus funds to be real property held as a tenancy by the entirety began with the case of Germania Sav. Bank v. Jung, 18 N.Y.S. 709 (Sup. Ct. N.Y. County 1892). The Mojeski court disapprovingly noted, however, that the authority cited in Germania for this proposition was only dictum. 87 Misc. 2d at 692, 386 N.Y.S.2d at 610. The Germania approach has been followed in several cases, including First Fed. Sav. & Loan Ass'n v. Lewis, 14 App. Div. 2d 150, 218 N.Y.S.2d 857 (2d Dep't 1961); Security Trust Co. v. Miller, 72 Misc. 2d 269, 338 N.Y.S.2d 1015 (Wayne County Ct. 1972); Stretz v. Zolkoski, 118 Misc. 806, 195 N.Y.S. 46 (Sup. Ct. Kings County 1922).


277 See note 273 supra.


279 87 Misc. 2d at 693-94, 386 N.Y.S.2d at 611-12.

280 13 N.Y.2d at 83, 192 N.E.2d at 20, 242 N.Y.S.2d at 52.

281 Id. at 85, 192 N.E.2d at 22, 242 N.Y.S.2d at 52. The Court's rationale in Hawthorne provides some guidelines for distinguishing voluntary and involuntary conversions. The Court said:

[M]ere involuntary loss . . . does not suffice to support the analogy suggested. . . . In the condemnation cases the forced conversion from realty to personal-
Hawthorne Court concluded that the property had not been invol-

ually converted, and thus the funds could not be deemed

ally. Noting that an estate by the entirety could not exist with

respect to personalty, and stressing the belief that to hold other-

wise would result in "a decision that ties up money" and impedes

the enjoyment thereof, the Court held that the proceeds should be

divided. Furthermore, in dictum, the Hawthorne Court cited with

approval the earlier decision of Franklin Square National Bank v.

Schiller, wherein it was expressly held that surplus mortgage fore-
closure funds are personalty subject to a tenancy in common. Em-

bracing the rationale of Hawthorne, the Mojeski court ruled that the

mortgage foreclosure proceeds in the instant case were indeed per-

sonalty subject to severance.

The decision reached by the Mojeski court is a sound one. A

finding that a tenancy by the entirety exists might well dictate that

the proceeds be placed with the court, a result which would prevent

either spouse from reaching the funds until the death of the other.

Additionally, just as the Hawthorne Court found that the proceeds

did not spring from the loss of the realty, but rather from the con-

tract for insurance, and as such were not the result of an involuntary

conversion, it can also be argued that the loss in a mortgage foreclo-
sure is the natural consequence of a voluntary mortgage agreement.

Finally, the cases which have treated surplus funds as real property

held by the entirety trace their inception to an era when the right

of a wife to control, use, and possess her own property had only

recently been recognized. At that time it would have been a drastic

aly as fully involuntary. The involuntary loss was also the legal source of the new

res. Here, while the loss was the occasion of the issuance of the now disputed draft,

neither the draft nor the right thereto springs from the involuntary loss. It is not a

substituted res as in the condemnation cases. It is not involuntary conversion.

Id. at 85, 192 N.E.2d at 21-22, 242 N.Y.S.2d at 52 (emphasis in original).

Id. at 86, 192 N.E.2d at 22, 242 N.Y.S.2d at 53. 323 Id. at 85-86, 192 N.E.2d at 22, 242 N.Y.S.2d at 53.

Id. at 86, 192 N.E.2d at 22, 242 N.Y.S.2d at 53. See note 288 infra.

Id. at 86, 192 N.E.2d at 22, 242 N.Y.S.2d at 53. Id. at 86, 192 N.E.2d at 22, 242 N.Y.S.2d at 53, citing Franklin Square Nat'l Bank v.


87 Misc. 2d at 693-94, 386 N.Y.S.2d at 611-12.

323 Id. at 86, 192 N.E.2d at 22, 242 N.Y.S.2d at 53.

324 In those mortgage foreclosure actions wherein the courts treated the surplus proceeds

as real property held by the entirety, the monies generally were paid into the court or the

county treasurer's office until the death of one of the spouses. See, e.g., South Shore Fed.

Sav. & Loan Ass'n v. Gundel, 42 Misc. 2d 510, 248 N.Y.S.2d 427 (Sup. Ct. Nassau County

1963); Leis v. Shaughnessy, 26 Misc. 2d 536, 209 N.Y.S.2d 648 (Sup. Ct. Nassau County

1960); Empire State Fed. Sav. & Loan Ass'n v. Wukowitz, 197 N.Y.S.2d 87 (Sup. Ct. West-

chester County 1959).
step for a court to have granted a wife one-half of a fund which constituted the remains of property in which her only prior interest was thought to be a right of survivorship.289

It is submitted that the importance of having free access to the surplus proceeds coupled with the possible injustice to creditors mandates concurrence with the rule of Franklin Square as recently reaffirmed in Mojeski. Meanwhile, the lack of controlling authority may lead to further contradictory results in this already confused area of the law. Hopefully, therefore, the Court of Appeals will conclusively resolve the issue at the earliest opportunity.

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289 The early restrictions placed on a wife's right to control, use, or possess property held as tenants by the entirety are amply illustrated by Germania Sav. Bank v. Jung, 18 N.Y.S. 709, 710 (Sup. Ct. N.Y. County 1892), wherein the court ordered that the surplus proceeds held as a tenancy by the entirety be placed in trust with the income and profits paid to the husband during the couple's lives. Id. at 711. It was 3 years later that the Court of Appeals recognized a wife's right to share equally in the control, use, and possession of a tenancy by the entirety. See Hiles v. Fisher, 144 N.Y. 306, 315 (1895).