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Receiver of Rents and Profits in New York

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language in describing the lien and thus providing ample protection against fraud would be a great step forward.

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RECEIVER OF RENTS AND PROFITS IN NEW YORK.

The recent decision by the Court of Appeals in the *Holmes* v. *Gravenhorst* case [1] has brought a solution to the problem as to whether, upon the appointment of a receiver in an action brought to foreclose a mortgage containing the covenant: "That the holder of said mortgage, in any action to foreclose it, shall be entitled (without notice and without regard to the adequacy of any security for the debt) to the appointment of a receiver of the rents and profits of said premises," a mortgagor-owner may be required to pay rent to the receiver or be evicted from the premises prior to a sale under a judgment of foreclosure and sale.

Tracing the recent New York decisions [2] our attention is brought to the conflicting interests of the mortgagor,[3] lessee, and mortgagee, exhibiting the forceful influences exerted by them to control the powers of the receiver of rents and profits pending foreclosure.[4] The issue arises most often between the mortgagee and lessee, concerning the handling of leases in existence during the period of receivership. "Confronted by a debtor who has defaulted and a security which is probably inadequate, the mortgagee is concerned with the making of the receiver's right to the rents and profits of the mortgaged premises productive of an amount sufficient to offset the contemplated deficiency.[5] However, leases made by the mortgagor prior to the foreclosure action may not provide for an adequate

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[1] 238 App. Div. 313, 263 N. Y. Supp. 738 (2d Dept. 1933).

[2] See (1933) 33 COL. L. REV. 168. The discussion herein will be confined to New York as the only jurisdiction in which the more complex aspects of this problem have been litigated to any appreciable degree.

[3] Unless otherwise indicated, the terms "landlord" and "mortgagor" will be used to dominate the owner of the equity of redemption at the time of foreclosure, although in cases of assignments subsequent to the execution of the mortgage these parties may have different interests and may be different persons.

[4] Under §254 subd. 10 of N. Y. REAL PROP. LAW, where the mortgagee may have a receiver appointed on default. Heretofore, the rights to the exercise of judicial discretion were unhampered, although it has, at times, been held to be "a contract right." Butler v. Frazer, 57 N. Y. Supp. 900 (Sup. Ct. 1896). In the absence of express provision in the mortgage, a receiver will be appointed upon application by the mortgagee, after the institution of foreclosure proceedings, only where the mortgagor is insolvent and the security inadequate. See Finch v. Ray, 208 App. Div. 251, 255, 203 N. Y. Supp. 560, 562 (3rd Dept. 1924). However, *cf.* Cohen v. Bartlett, 182 App. Div. 245, 169 N. Y. Supp. 604 (1st Dept. 1918) insolvency was not required.

[5] See (1933) 33 COL. L. REV. 1212.

return,[6] or payment of rent by the tenant may threaten to make the space occupied unproductive until the foreclosure sale, since the tenant's inferior interest subsists to that date." [7] Naturally, in cases where the lease made after institution of foreclosure proceedings called for greatly decreased rental where previously it had been very high,[8] or where a short time prior to the action of foreclosure the landlord had collected rents for three months in advance,[9] both cases indicating fraud, there may be rescission of the lease or return of moneys advanced. The policy of the lower courts has always been one which protected the mortgagee, in which case the receiver could practically ignore leases in existence [10] and demand a reasonable rental set by the court,[11] "and irrespective of prepayment by the tenant to the landlord." [12] The decisions were a hardship to the tenant since they foresaw merely the foreclosure's success.[13] With *Metropolitan Life Insurance Co.* v. *Childs Co.*[14] we began the series of decisions culminating in the *Holmes* case.[15] In the *Metropolitan* case [16] the Metropolitan Life Insurance Company was an owner in

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[6] See Note (1933) 46 HARV. L. REV. 491, 493.

[7] Metropolitan Life Insurance Company v. Childs Co., 230 N. Y. 285, 130 N. E. 295 (1921); Knickerbocker Oil Corp. v. Richfield Oil Corp., 234 App. Div. 199, 254 N. Y. Supp. 506 (2d Dept. 1931).

[8] Sager v. Rebdor Realty Corp., 230 App. Div. 106, 243 N. Y. Supp. 314 (1st Dept. 1930). *Cf. infra* note 10.

[9] Peltz v. Broder, unreported N. Y. L. J., June 17, 1933, at 3645 (Sup. Ct. 1933).

[10] Olive v. Levy, 201 App. Div. 262, 194 N. Y. Supp. 80 (2d Dept. 1922); Monro-King & Gremmels Realty Corp. v. 9th Ave.-31st St. Corp., 233 App. Div. 401, 253 N. Y. Supp. 303 (1st Dept. 1931); New Way Bldg. Co. v. Taft Bldg. Co., 129 Misc. 170, 220 N. Y. Supp. 665 (Sup. Ct. 1927).

[11] A rental fixed by the receiver himself has no binding force. Curren v. Gillam, 106 Misc. 652, 176 N. Y. Supp. 573 (Mun. Ct. 1919); Gibbons v. Wasserman, 137 Misc. 377, 244 N. Y. Supp. 26 (App. T. 1st Dept. 1930).

[12] Monro-King & Gremmels Realty Corp. v. 9th Ave.-31st St. Corp., *supra* note 10; Schoenberg v. Makstein Realty Co., 130 Misc. 695, 224 N. Y. Supp. 636 (Sup. Ct. 1927); see Olive v. Levy, *supra* note 10, at 263, 194 N. Y. Supp. at 88. But *cf.* Lawrence v. Conlon, 26 Misc. 44, 56 N. Y. Supp. 345 (Sup. Ct. 1899).

[13] Where the action was discontinued as against the tenant, or judgment rendered for the defendant, the *status quo* could not be restored if the tenant had been forced to move and to make a new lease elsewhere. *Cf.* Metropolitan Life Insurance Co. v. Childs Co., *supra* note 7. If the receiver in such a case had collected an occupational rental greater than the lease rental, the doctrine of voluntary payment would be an obstacle to the tenant's recovery of the excess paid either from the landlord who received the fund or from the receiver who compelled the payment. *Cf.* Note (1933) 33 COL. L. REV. 1030, 1035. Obviously the receiver's conduct did not constitute duress. No authority has been found giving the tenant a claim against the fund in such a situation.

[14] *Supra* note 7. The court held that the mortgagors or their assignees were entitled to recover rent from the lessee from the date it ceased to pay rent to the date of the sale, and that thereafter the purchaser might recover. Equity holds that the judgment of foreclosure is not a complete representation that the mortgage will be foreclosed. Too, at foreclosure sale one takes the property free and clear of subordinate interests.

[15] *Supra* note 1.

[16] *Supra* note 7.

fee with an outstanding lease. As the new owner, it tried to collect back rent after having dropped this defendant as a party to its prior foreclosure action. Childs Company set up estopped. The Court held that the commencement of foreclosure proceedings was a mere representation, and that: if and when judgment is entered, and if and when the sale is complete, then only is the lessee released.[17]

In conjunction with the aforementioned case is the *Monro King & Gremmels Realty Corp.* v. *9th Ave.-31st Street Corporation*,[18] wherein it was held that the receiver's demand for occupational rent constituted "constructive eviction" giving the tenant the option to move out or pay an increased rental.[19]

The Court of Appeals went a step further in the *Prudence* case[20] in which it held that the mortgagor could contract any way he desired, being a legal owner (unless there was fraud),[21] and the receiver must abide by the leases in existence at the time he is appointed, the tenants being protected from paying higher rental than that stipulated in the lease.[22] "Although the courts have since sanctioned the collection of an occupational rental less than that required by the lease,[23] this imposes no hardship on the tenant, and does not

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[17] Mere appointment of a receiver did not give the tenant the privilege of avoiding the lease.

[18] *Supra* note 10.

[19] Unless the tenant was made a party to the action the receiver could not collect a rental other than that provided for in the lease. See Metropolitan Life Insurance Co. v. Childs Co., *supra* note 7, at 289, 130 N. E. at 297.

[20] Prudence Co. v. 160 W. 73rd St. Corp., 260 N. Y. 205, 183 N. E. 365 (1932). In this case the rights of the holders under the "co-operative ownership plan" were derived from the mortgagor. Those rights could not be destroyed by means of a mortgage foreclosure receivership.

[21] Mortgage contained the usual receivership clause for collection of rents and profits by the receiver. But rent was not being paid in the usual rental. The receiver applied to the courts to make the tenants pay a fair and reasonable rental to be applied to the mortgage against foreclosure.

[22] "A mortgage is only a lien on the mortgaged real property. Title remains in the mortgagor and those claiming under or through the mortgagor until the lien is foreclosed. Foreclosure of the lien does not take place upon the commencement of a foreclosure action, but upon the sale under a judgment of foreclosure. Though, during the pendency of the action, a court of equity has power to issue interlocutory orders for the protection of an asserted lien, and cannot deprive any party of a title or right, which though subordinate to the lien of the mortgage, survive and are valid until the lien is foreclosed by a sale under a judgment of foreclosure." Per Lehman, *J.*, in Prudence Co. v. 160 W. 73rd St. Corp., *supra* note 20, at 211, 183 N. E. at 366. The consideration of this case is similar to that in Metropolitan Life Insurance Co. v. Childs Co., *supra* note 7, Knickerbocker Oil Co. v. Richfield Oil Co., *supra* note 7, and Loring M. Hewen Co. v. Malter, 145 Misc. 635, 636, 260 N. Y. Supp. 624, 626 (Sup. Ct. 1932).

[23] Cohen v. 908 Kelly St. Realty Co., N. Y. L. J., Oct. 20, 1932, at 1626; see Markantonis v. Madlan Realty Corp., 262 N. Y. 354, 360, 186 N. E. 862, 864 (1933): "Even under our decision in the Prudence Company case * * * we held only that a receiver could not require a person in occupation of the premises to pay him any sum either for rent or for use and occupation, beyond such sums as were in their nature rents and profits of the premises to which the owner would have been entitled."

conflict with the reasoning in the *Prudence* case." [24]

This brings us to the *Holmes* v. *Gravenhorst* case.[25] Here the action was instituted to foreclose a mortgage on the private dwelling owned and occupied by Mariana Gravenhorst. A receiver was appointed and given the usual authority to demand, collect, and receive from the person or persons in possession all rents due and unpaid or thereafter to become due, and those in possession were directed to attorn to the receiver as tenants. The receiver duly qualified and notice of his appointment and qualification was served upon the occupants of the premises. The receiver then applied to Special Term for an order fixing the fair and reasonable value of the rent, for the premises occupied by M. Gravenhorst. On appeal from the order denying this motion, the determination sought was whether in the absence of agreement by the mortgagor to relinquish possession on default, a court might vest in a receiver appointed in an action to foreclose a mortgage on real property, a right to collect rents which never accrued to the legal owner, who himself enjoyed possession as an incident to his ownership.

The court at Special Term, in holding that it was without power to fix the fair and reasonable value of the use and occupation of the premises as against the owner-mortgagor in possession, expressly relied on the authority of the *Prudence* decision.[26] Mr. Justice Steinbrink's statement was: "There is no contention here that rents and profits now issue from the premises or that there exists any lease or agreement in connection therewith. Nor does it appear that the owner of the equity has agreed to relinquish possession to the mortgagee on default. The receiver having failed to furnish proof of any of these facts, the court is free to assume that the defendant, as an incident to his ownership, rightfully retains possession of the mortgaged premises." In reversing the order of the Special Term, the Appellate Division took the position that there was nothing in the *Prudence* decision inconsistent with the doctrine that with the receivership goes the right to take full possession of the premises from the owner. Without restating the basic principles it is sufficient to quote Judge Lehman: "In no event is the owner deprived of any rights or the mortgagee accorded rights beyond the stipulations of the mortgage. A mortgage is only a lien on the mortgaged real property. Title remains in the mortgagor and those claiming under or through the mortgagor until the lien is foreclosed. Foreclosure of the lien does not take place upon the commencement of the foreclosure action, but upon the sale under a judgment of foreclosure. Though during the pendency of the action a court

[24] *Supra* note 20.

[25] *Supra* note 1. The mortgage contained the following clause: "that the holder of said mortgage, in any action to foreclose it, shall be entitled (without notice and without regard to the adequacy of any security for the debt) to the appointment of a receiver of the rents and profits of said premises."

[26] *Supra* note 20.

of equity has the power to issue interlocutory orders for the protection of an asserted lien, such orders must be auxiliary to the right to foreclose the lien." Under the *Prudence* decision it was made clear that if the mortgage had provided for relinquishment of possession on default or for the payment of rent then the power to fix occupational rent pending the foreclosure action would have been created. In the absence of such provision the power could not exist. It seems to me that the language of the mortgage was quite clear.[27] One must merely bear in mind that a receiver's possession for the purpose of preserving the mortgage security does not include within it the right to collect rents when none in fact accrue. His right is to collect whatever rents the mortgaged premises yield. That right comes from the language of the mortgage only. To grant the receiver greater rights would be to "accord the mortgagee rights beyond the stipulations of the mortgage" in direct violation of the *Prudence* decision.

There is no statutory authority for holding that a mortgagor in possession may be evicted from the mortgaged premises prior to a sale under a judgment of foreclosure and sale. The right of possession given to a receiver is incidental to the purpose for which the receiver is appointed, namely, the collection of the rents and profits. Actual possession being in one having the right of possession inherent in his ownership, no right of possession exists which may be conferred upon a receiver. To prevent the mortgagee from becoming possessory owner, equity will not compel the owner to pay occupational rent unless it is specifically contracted so to do. Thus, the decision in this case, in conformity with former decisions, reaches a definite conclusion and lays down the rule of law for similar situations in the future.

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THE MINNESOTA MORTGAGE CASE.

The present day has brought to this country conditions that never confronted the founders of our country and, it might be safely stated, never came within the purview of their great vision. It is a period in which the very foundations of the nation are being shaken. We all know that we are in the midst of a great economic depression which has brought with it great social questions. How have the states attempted to meet the situation?

One of the methods employed by the legislatures of the various states[1] is the enactment of statutes granting temporary relief to

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[27] See *supra* note 25.

[1] Arizona, Arkansas, Illinois, Iowa, Michigan, Minnesota, Montana, Nebraska, New Hampshire, New York, North Carolina, Ohio, Oklahoma, Pennsylvania, South Dakota, Texas, Vermont, West Virginia, Wisconsin.