

CHAPTER 9

Security and Mortgages

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§9.1. Second mortgages: Statute limiting interest. In *Levin v. Smith*,¹ the Supreme Judicial Court considered the meaning of the words "assessed value" in G.L., c. 140, §§90A-90D, providing that no person shall charge mortgage interest at a greater rate than 1.5 percent per month for a mortgage loan, other than a first mortgage loan, of more than \$1500 secured wholly or partially by a mortgage on real estate having an "assessed value" of not more than \$10,000.² The Court held that the words "assessed value" in this statute relate only to such public assessment record as is available at the time of the execution and delivery of the mortgage; therefore, if at the time of the execution and delivery of the second mortgage and note on January 15, 1960, the latest available assessment record showed an assessed value of \$8600 for the mortgaged premises, the statute would apply, even though on April 23, 1960, the assessed valuation for the mortgaged premises was fixed at \$10,100 as of January 1, 1960.

The Court held that legality must be known at the time of the loan and cannot be ambulatory until an uncertain date when the local tax rate is fixed. Otherwise, the Court pointed out, fluctuations in assessed valuations above and below \$10,000 would cause shifts in the legality and illegality of the loans.

§9.2. Assignment for the benefit of creditors. In the case of *Wasserman v. Tonelli*,¹ it was held that an assignee for the benefit of creditors under an ordinary assignment cannot recover property which has been fraudulently conveyed by the debtor corporation.² The Su-

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§9.1. 1 343 Mass. 169, 178 N.E.2d 33 (1961).

² Acts of 1962, c. 286, increased this limit to \$25,000 and applies the restrictions to dwelling houses for six or fewer separate households. The previous law applied to dwelling houses for three or fewer separate households.

§9.2. 1 343 Mass. 253, 178 N.E.2d 477 (1961).

² An assignment for the benefit of creditors covers only those items clearly covered either by the general language or in specific schedules; if specific schedules are included, these schedules limit the effect of general language. *Bock v. Perkins*, 139 U.S. 628, 633-638, 11 Sup. Ct. 677, 679-680, 35 L. Ed. 314, 317-318 (1891); *United States v. Howland*, 17 U.S. (4 Wheat.) 108, 4 L. Ed. 526 (1819); *United States v. Langton*, 26 Fed. Cas. 862 (No. 15,560) (C.C.D. Mass. 1829); *Driscoll v. Fiske*, 21 Pick. 503 (Mass. 1839). The Court in the *Wasserman* case concluded that the terms

preme Judicial Court held that a general assignee for the benefit of creditors has no greater right than the debtor and does not have the rights of a creditor even though his trust is for the benefit of creditors. A fraudulent conveyance is not void but voidable.³ A fraudulent conveyance can be set aside by creditors. However, only creditors and not the assignee for the benefit of creditors can set aside a fraudulent conveyance.

In *Friedman v. First National Bank of Boston*,⁴ the Court held that the defendant bank had an equitable right to set off a claim on its unmatured note against a claim by the assignee for the benefit of creditors. Although the right of equitable set-off against an unmatured note does not exist in the case of mere insolvency,⁵ the *Friedman* decision held that it does exist in the case of an assignment for the benefit of creditors. In reaching this conclusion, the Court pointed out that bankruptcy⁶ or statutory insolvency⁷ will give a right of equitable set-off in this situation. The Court reasoned that, as in bankruptcy, a debtor whose assets have been transferred to an assignee for the benefit of creditors no longer has the power to pay its obligations. On the basis of this analogy, the Court held that in an assignment for benefit of creditors the same rule should apply as in the case of bankruptcy and that the bank was entitled to the right of equitable set-off.

Certain funds of the assignor were held by the bank subject to claims of creditors under a trustee process writ. The assignee for the benefit of creditors argued that these funds should be turned over to the assignee even though they were the subject of a trustee process attachment. The Court rejected this claim, holding that the assignee for the benefit of creditors had no greater right than the debtor to require the bank to pay over amounts in the debtor's account which were held under a trustee process writ. Actual bankruptcy within four months would be necessary in order to upset the trustee process attachment.

In *Lima v. Avery*,⁸ it was held that the intention of the parties is the essential element in determining whether an instrument had the effect of a mortgage.⁹ The Court upheld as a valid mortgage an instrument which secured performance of an agreement entered into between two parties other than the mortgagor. The plaintiff was an assignee for the benefit of creditors of the mortgagor and brought a bill

of the assignment were not broad enough to include fraudulently conveyed property. The Court then proceeded to hold that in any event an assignment for the benefit of creditors cannot include property transferred by the assignor in fraud of his creditors.

³ *Service Mortgage Corp. v. Welton*, 293 Mass. 410, 200 N.E. 278 (1936).

⁴ 1962 Mass. Adv. Sh. 1087, 183 N.E.2d 722, also noted in §6.3 *supra*.

⁵ *Harding v. Broadway National Bank*, 294 Mass. 13, 200 N.E. 386 (1936); *Jump v. Leon*, 192 Mass. 511, 78 N.E. 532 (1906); *Wiley v. Bunker Hill National Bank*, 183 Mass. 495, 67 N.E. 655 (1903); *Spaulding v. Backus*, 122 Mass. 553 (1877).

⁶ Bankruptcy Act §68, subpar. a, 11 U.S.C. §108, subpar. a (1958); *Studley v. Boylston National Bank*, 229 U.S. 523, 33 Sup. Ct. 806, 57 L. Ed. 1313 (1913); *Harding v. Broadway National Bank*, 294 Mass. 13, 200 N.E. 386 (1936).

⁷ *Demmon v. Boylston Bank*, 5 Cush. 194 (Mass. 1849).

⁸ 343 Mass. 179, 177 N.E.2d 787 (1961).

⁹ *Jacobson v. Jacobson*, 334 Mass. 658, 661, 138 N.E.2d 206, 208 (1956).

in equity seeking to have the mortgage declared a nullity. The Court rejected this claim holding that the mortgage and agreement in question were valid and in full force and effect.

§9.3. Subcontractors' bonds. In *Morse Brothers Electrical Co. v. Martin Shore Realty Co.*,¹ the Supreme Judicial Court held that a subcontractor on a construction contract could not recover against the owner of a building on the basis of the owner's failure to provide an adequate surety bond. The instructions to general bidders on the contract stated:

The successful bidder shall furnish a guarantee bond in the full amount of the contract . . . which shall cover the faithful performance of the contract, and *the payment of all obligations thereunder*. [Emphasis supplied.]

The general conditions which were part of the specifications provided that the owner would:

. . . require the contractor to furnish bond of the amount of the contract price, covering faithful performance of the contract, and the payment of all obligations arising thereunder *in such a form as the owner may prescribe* and with such securities as he may approve. [Emphasis supplied.]

The bid form in referring to subcontracts stated: "The contract, terms and general conditions . . . shall govern the requirements of this division."

The plaintiff's subcontract with the prime contractor was made "in accordance with the provisions of the invitation for bids." The invitation for bids incorporated by reference all of the provisions of the instructions to bidders, and the general conditions and specifications.

The prime contractor furnished a bond that was satisfactory to the owner. This bond required the prime contractor to perform the contract and further stipulated that the contractor "shall cause . . . all lien claims for labor and materials furnished in the prosecution of the work thereunder to be discharged."

The plaintiff, as a subcontractor, knew that the invitation for bids provided for a bond, but did not know the terms and conditions of the bond although it relied upon the existence of a bond in making its bid and entering into the subcontract. The plaintiff did not speak to the owner before making its subcontract, and the owner made no representations to the subcontractor with respect to the bond. The subcontractor was not paid for its work. The subcontractor never filed nor perfected a mechanic's and materialmen's lien, and when it learned of the terms of the bond it was too late to do so.

The subcontractor brought suit against the owner claiming that the owner had not lived up to its contractual agreements in that the owner had not required a bond covering payment of all claims but only required a bond covering payment of claims upon which valid liens were

§9.3. 1 1962 Mass. Adv. Sh. 487, 181 N.E.2d 549.

perfected. The Court rejected this contention holding that the contract provisions with respect to a bond were intended to benefit the owner and were not intended to benefit the subcontractor.² The Court also relied upon the fact that there was no evidence that the plaintiff had relied upon the specific terms of the general contractor's guaranty bond and had not relied upon any representations by the owner.³

§9.4. **Priority between sureties and lenders.** In the case of *Aetna Casualty and Surety Co. v. Harvard Trust Co.*,¹ the Supreme Judicial Court considered the question of priority as between a surety and a lender. The case involved proceedings by a construction contractor's surety against a bank and a contractor to determine priority with respect to funds earned under the contract. The bank claimed the contract proceeds under an assignment executed by the contractor for securing loans. The surety claimed the proceeds from the contract as a prior assignee under the subrogation provisions in the surety bond.

The Court held that a prior assignee takes in preference to the later assignee even though the debtor has not been given notice of the prior assignment. However, the prior assignee takes the risk that the debtor may make payment to later assignees if no notice has been given to the debtor.² If the debtor pays the later assignees before he has notice of the prior assignment, then the debtor will be protected in paying the subsequent assignees.³

² A bond given in connection with a construction contract which is valid as the basis of a common law obligation may operate to benefit all parties who, in reliance upon it, have furnished material or labor if the bond contains certain peculiar terms. *Johnson-Foster Co. v. D'Amore Construction Co.*, 314 Mass. 416, 50 N.E.2d 89 (1943). The bond in the *Johnson-Foster Co.* case expressly stated, not only that it created an obligation to the owner for whom the work was being done, but that it was also made for the use and benefit of all persons who furnish any material or perform any labor for the contract. The bond also specifically provided that such persons were made obligees and might sue on the bond.

³ In order for a subcontractor to bring suit on a performance or payment bond, the provisions of the bond or other contractual arrangements must show an intention to benefit subcontractors and suppliers and to give them a direct right upon the bond or contract, and there must have been reliance on the bond by the subcontractors and suppliers. See *Waite Hardware Co. v. Ardini & Pfau, Inc.*, 339 Mass. 634, 637-638, 162 N.E.2d 13, 15-16 (1959); *Robinson Clay Products Co. v. Beacon Construction Co. of Mass.*, 339 Mass. 406, 408-410, 159 N.E.2d 530, 531-532 (1959). See also *Frigidaire Sales Corp. v. Maguire Homes, Inc.*, 186 F. Supp. 767, 768-769 (D. Mass. 1959), *aff'd sub nom. American Surety Co. of New York v. United States*, 282 F.2d 427, 428 (1st Cir. 1960); *Gordon v. Robinson Homes, Inc.*, 342 Mass. 529, 174 N.E.2d 381 (1961); *Philip Carey Manufacturing Co. v. Peerless Casualty Co.*, 330 Mass. 319, 322, 113 N.E.2d 226, 228 (1953); 2 Williston, Contracts §372, pp. 916-917 (3d ed. 1959).

§9.4. ¹ 1962 Mass. Adv. Sh. 569, 181 N.E.2d 673, also noted in §6.6 *supra*.

² See *Salem Trust Co. v. Manufacturers' Finance Co.*, 264 U.S. 182, 199, 44 Sup. Ct. 266, 270-271, 68 L. Ed. 628, 635 (1924); *Goodyear Tire & Rubber Co. v. Bagg*, 292 Mass. 125, 128, 197 N.E. 481, 482 (1935).

³ See *Goodyear Tire & Rubber Co. v. Bagg*, 292 Mass. 125, 128, 197 N.E. 481, 482 (1935); *Rabinowitz v. People's National Bank*, 235 Mass. 102, 103-104, 126 N.E. 289, 290 (1920); 1 Restatement of Contracts §173(b); 3 Williston, Contracts §435, pp. 221, 225 (3d ed. 1960).

The defendant bank had taken payment from the construction contractor's general bank account without knowledge of the contractor's default or the surety's claims. This money was taken in payment of advances on contracts. The Court held that the defendant bank could retain this money against the prior rights of the surety. While the bank had knowledge that the bond existed, the Court held that the bank was not bound to make inquiry as to whether there had been a default each time it advanced funds on the security of assignments.⁴

§9.5. Mortgage bond indentures. In *New York Central Railroad Co. v. New England Merchants National Bank of Boston*,¹ the Supreme Judicial Court considered G.L., c. 160, §47, which requires that a railroad mortgage bond indenture secure previous unsecured obligations on equal terms with the mortgage bonds.

The New York Central Railroad Company had outstanding certain unsecured debenture bonds. The railroad proceeded to float an issue of mortgage bonds. In accordance with the requirements of the statute, these bonds equally secured the previously unsecured debentures. However, the indenture provided that upon payment of the mortgage bonds the mortgage was to be discharged unless this statute was held by the courts to require continued preservation of the mortgage lien for the benefit of unsecured obligations.

All of the mortgage bonds were eventually paid, but certain of the debenture bonds had not been paid. In this litigation the railroad sought a decree that the mortgage was no longer effective because all of the mortgage bonds had been paid. The debenture bondholders claimed that the mortgage was still outstanding for purposes of securing their debenture bonds.

The railroad urged that since the mortgage bonds had been paid in full there was no longer any need for the mortgage indenture. It was argued that the sole purpose of the statute was to prevent any preference of mortgage bondholders over previously outstanding unsecured indebtedness, and that, once the mortgage bondholders were paid off, there was no longer any possibility of preference over the previously unsecured indebtedness. The Court rejected this argument stating that persons who purchase debentures during the period when the mortgage bonds are outstanding are, as a result of the statute, entitled to rely upon continuation of the mortgage lien as security until their debentures are paid.

§9.6. Attorney's lien. The application of G.L., c. 221, §50, which establishes an attorney's lien, was considered in *Elbaum v. Sullivan*.¹ It was there held that an attorney's fee is to be determined on the basis of the entire case, although he was discharged and replaced before the final settlement of the case. The services in the present case being

⁴ *American Fidelity Co. v. National City Bank of Evansville*, 266 F.2d 910, 917 (D.C. Cir. 1959).

§9.5. 1 1962 Mass. Adv. Sh. 1219, 183 N.E.2d 852.

§9.6. 1 1962 Mass. Adv. Sh. 1167, 183 N.E.2d 712.

substantial, the Court upheld a judgment for a \$3500 lien, even though the case had only resulted in a \$2500 offer of settlement up to the time of the attorney's discharge.

§9.7. Legislation. A variety of new statutes dealing with the subject matter of this chapter have been enacted by the legislature during the period covered by the 1962 SURVEY year, as noted for the various acts of 1962 following:

Chapter 44: Time of payment for certain savings bank loans.

Chapter 46: State bank and credit union home improvement loans insured under National Housing Act.

Chapter 50: Permits a savings bank to invest 15 percent (instead of 10 percent) of its deposits in excess of 70 percent in federal insured or guaranteed mortgages and to amortize 60 percent mortgage loans over twenty-five years instead of twenty years.

Chapter 52: Assignments for the benefit of creditors.

Chapter 124: Making and acquisition of F.H.A. and V.A. insured loans by cooperative banks.

Chapter 125: Increasing the maximum amount for an individual mortgage loan by a cooperative bank to \$30,000 provided that the aggregate amount of loans, as to each of which the unpaid balance of principal outstanding is more than \$25,000, shall not at any time exceed 20 percent of the total deposits of the bank, and provided that loans over \$25,000 and not exceeding \$30,000 shall not exceed 75 percent of the value of the mortgaged property as certified by the security committee.

Chapter 127: Credit union records.

Chapter 286: The second mortgage loan regulation act is expanded to include a mortgage on real estate having a fixed value of not over \$25,000 and having thereon a dwelling house with accommodation for six or less separate households.

Chapter 332: Permits revision by banks or other lending institutions of mortgage payments so as to give relief to mortgagors whose tax assessments have been increased through a general reassessment.

Chapter 469: Veterans' liens on real estate may be subordinated to mortgages obtained for necessary repairs.

Chapter 523: Criminal penalty for charging higher interest than is allowed by law regulating second mortgages.

Chapter 551: In the case of first mortgages on dwelling houses of three or less separate households occupied or to be occupied in whole or in part by the mortgagor the premium for prepayment upon a bona fide sale shall not exceed three months' interest or the balance of the first year's interest, whichever is greater, and no premium is chargeable after three years from the date of the note. These conditions do not apply to loans which are being refinanced or to F.H.A. and G.I. loans and do not prevent any note being a negotiable instrument under the Uniform Commercial Code.