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Another factor supporting this view is that there is a possibility that the public policy idea behind the common law right of abandonment and the later Wreck Act is not as compelling today as formerly. For example, ships today are substantially different than they were prior to 1900. They are, for the most part, larger and are made of metal rather than wood, and therefore upon being wrecked pose a greater threat of becoming a serious obstruction in a channel. Also today, there are more ships in operation, and therefore any obstruction in a passage is more harmful in that it may adversely affect the rights of a larger number of people. In view of this, it could be argued that stricter liability should be imposed on wrongdoing shipowners so that they will be more cautious and prudent in their use of navigable waterways. If this enlightened approach were adopted, owners would still be protected from personal liability for removal costs of ships sunk without fault, and thereby continued encouragement would be given to the maritime industry.

EDGAR H. MACKINLAY

SUBORDINATION OF MORTGAGES FOR FUTURE ADVANCES TO FEDERAL TAX LIENS

In *United States v. Pioneer Am. Ins. Co.*¹ the United States Supreme Court for the first time clearly established that the choate rule extends to a mortgagee's contractual lien and also to future advances² or contingent liabilities.³ The question of the applicability of the choate doctrine in the situation where a mortgage competes with a federal tax lien was left unsettled by the 1958 per curiam decision of the Supreme Court in *United States v. R. F. Ball Constr. Co.*⁴ The ambiguity of the *Ball* decision caused much speculation in the interim.

In *Pioneer American*, the taxpayers in 1958 duly executed a deed of trust of certain real estate to secure a note held by the Pioneer American Insurance Company. The deed of trust included a covenant stipulating that, in case the mortgagor defaulted on the note, the mortgagor would pay reasonable attorney's fees expended by the

a vessel owner can absolve himself from the burden of seeing that his vessel does not become, by abandonment, a menace to navigation." In re Eastern Transp. Co., 102 F. Supp. 913, 917 (D. Md. 1952).

¹374 U.S. 84 (1936).

²Glenn, *Mortgages* § 392-406.3 (1943); 59 C.J.S. *Mortgages* § 175-177 (1949).

³59 C.J.S. *Mortgages* § 230 (1949).

⁴355 U.S. 587 (1958) (per curiam).

mortgagee in any suit resulting therefrom. In October of 1960 the taxpayers defaulted. The mortgagee filed a foreclosure suit on March 24, 1961, and asked for the principal and interest and a reasonable attorney's fee. The United States was named a party defendant, since on November 29, 1960, and January 20, 1961, it had filed two tax liens against the taxpayer. It filed three additional tax liens on April 14, July 17, and October 3, 1961.

On November 15, 1961, an Arkansas Chancery Court fixed the amount of the attorney's fee at \$1,200, and awarded a priority over the United States tax liens to the mortgagee for the principal and interest and the attorney's fee. The United States appealed to the Supreme Court of Arkansas,⁵ conceding the mortgagee's priority as to the principal and interest, but denying priority as to the lien for attorney's fees on the ground that it was inchoate at the time of the filing of all the tax liens. The Arkansas Supreme Court affirmed the lower court's decision that the attorney's fee was senior to the tax liens, on the ground that it was an inherent part of, and thus related back to the antecedent mortgage contract.

The United States Supreme Court granted certiorari⁶ because of a conflict between the Arkansas decision and two prior decisions in the lower federal courts.⁷ The Arkansas decision was reversed when the Court held that a mortgage securing contingent liability, like a mortgage securing future advances, is in interest to which the choate test can appropriately be applied. And, since the amount of the attorney's lien was uncertain until entry of the decree of November 15, 1961, which was subsequent to the attachment of all the tax liens, the attorney's lien was inchoate and subordinate to all the tax liens.

In order to appreciate the far-reaching effect of the Supreme Court's extension of the choate lien doctrine to the field of mortgages securing future advances,⁸ it is necessary to examine the development and subsequent extension of the choate rule.

A lien equal to the amount of the tax due arises in favor of the Government upon all property and rights to property belonging to a

⁵United States v. Pioneer Am. Ins. Co., 235 Ark. 267, 357 S.W.2d 653 (1962).

⁶United States v. Pioneer Am. Ins. Co., 371 U.S. 909 (1962).

⁷United States v. Bond, 279 F.2d 837 (4th Cir. 1960); In re New Haven Clock & Watch Co., 253 F.2d 577 (2d Cir. 1959) (holding the relation back doctrine inapplicable, and thus an attorney's lien must be perfected and certain).

⁸Since the rationale applicable to mortgages securing future advances is also applicable to mortgages securing contingent liabilities, the ensuing discussion will be confined to mortgages securing future advances. 374 U.S. at 91; United States v. Bond, supra note 7, at 846.

delinquent taxpayer.⁹ Ordinarily, the tax lien becomes effective as of the date the assessment is made¹⁰ by the District Director of Internal Revenue.¹¹ Since the lien is secret,¹² Congress, in order to prevent inequitable results, has given a special preference to mortgagees, pledgees, purchasers, and judgment creditors by providing that the tax lien does not become effective against these interests until notice of the assessment has been filed in the appropriate place.¹³

The choate lien test was first applied by the Supreme Court in insolvency cases,¹⁴ where Congress expressly granted a priority to the debts owed the United States, whether the debts were secured by liens or not.¹⁵ The initial extension of the choate doctrine to statu-

⁹Int. Rev. Code of 1954, § 6321 (formerly Int. Rev. Code of 1939, § 3670). Originally, the federal tax lien statutes were adopted to prevent the frustration of tax collection processes by transfer of the taxpayer's assets before enforcement proceedings could be instituted. See note, 63 Yale L.J. 905 (1954).

¹⁰Int. Rev. Code of 1954, § 6322 (formerly Int. Rev. Code of 1939, § 3671).

¹¹Int. Rev. Code of 1954, § 6203; Treas. Reg. § 301.6201-1 (1954).

¹²Int. Rev. Code of 1954, § 6103, 7213.

¹³"[T]he lien imposed by section 6321 shall not be valid as against any mortgagee, pledgee, purchaser, or judgment creditor until notice thereof has been filed by the Secretary or his delegate. . . ." Int. Rev. Code of 1954, § 6323(a) (formerly Int. Rev. Code of 1939, § 3672(a)).

The original section, which is now § 6323(a) of the Int. Rev. Code of 1954, did not include a purchaser.

In *United States v. Snyder*, 149 U.S. 210 (1893), it was held that a tax lien arising under the section which is now § 6321 was binding even against a bona fide purchaser for value without knowledge or notice of the existence of such a lien. Twenty years later, Congress amended the section which is now § 6323(a) to include a purchaser. Int. Rev. Code of 1954, § 6323(a).

The reason given for the amendment was: "[T]he lien is so comprehensive that it covers all the property and rights to property of the delinquent situated anywhere in the United States, and any person taking title to real estate is subjected to the impossible task of ascertaining whether any person, who has at any time owned the real estate in question, has been delinquent in the payment of the taxes referred to while the owner of the real estate in question. The business carried on under the internal-revenue law may be at a great distance from the property affected by this secret lien, but this will not relieve the property from the lien." H.R. Rep. No. 1018, 62nd Cong., 2d Sess. 2 (1912).

¹⁴The first reference to the choate lien test is found in *County of Spokane v. United States*, 279 U.S. 80 (1929). The choate test was applied by the Supreme Court in *New York v. Maclay*, 288 U.S. 290, 294 (1933) where, in the case of an insolvent corporation, a claim for state franchise taxes due but not liquidated was held inchoate, "serving merely as a 'caveat' of a more perfect lien to come." Accord, *United States v. City of New Britain*, 347 U.S. 81 (1954); *United States v. Gilbert Associates, Inc.*, 345 U.S. 361 (1953); *United States v. Security Trust & Sav. Bank*, 340 U.S. 47 (1950); *United States v. Waddill, Holland & Flinn, Inc.*, 323 U.S. 353 (1945); *United States v. Texas*, 314 U.S. 480 (1941).

¹⁵"Whenever any person indebted to the United States is insolvent, or whenever the estate of any deceased debtor, in the hands of the executors or administra-

tory liens came in 1950 in *United States v. Security Trust and Sav. Bank*.¹⁶ The Supreme Court held that an attachment lien was inchoate until judgment, even though the California statute said it was perfected as of the time a copy of the writ was recorded. The tax lien, attaching prior to judgment under section 6321 of the 1958 Internal Revenue Code, was entitled to a priority. The Court justified this unique application of the choate test by alluding to the intent of Congress in enacting section 6321.¹⁷ Since the California statute allows a period of three years to proceed to judgment after the writ of attachment is recorded, the Court reasoned that there are many contingencies, any one of which might prevent the termination of the suit, and thus the lien was inchoate, as it was "merely a *lis pendens* notice that a right to perfect a lien exists."¹⁸

The *Security Trust* case is also pertinent in the tax lien field for its enunciation of the rule that the time when a lien becomes specific and perfected is always a matter of federal law.¹⁹ However, if a state court holds that a lien is inchoate, such a determination is nearly always conclusive upon review by the federal courts.²⁰

In *United States v. City of New Britain*,²¹ the Supreme Court clarified the standards of the choate rule. The three prerequisites of choateness are satisfied when the identity of the lienor, the property subject to the lien, and the amount of the lien are established.²² The Court,

tors, is insufficient to pay all the debts due from the deceased, the debts due to the United States shall be first satisfied; and the priority established shall extend as well to cases in which a debtor, not having sufficient property to pay all his debts makes a voluntary assignment thereof, or in which the estate and effects of an absconding, concealed, or absent debtor are attached by process of law, as to cases in which an act of bankruptcy is committed." 31 U.S.C. § 191 (1954).

¹⁶340 U.S. 47 (1950).

¹⁷"If the purpose of the federal tax lien statute to insure prompt and certain collection of taxes due the United States from tax delinquents is to be fulfilled, a similar rule [choateness] must prevail here." *Id.* at 51.

¹⁸*Id.* at 50.

¹⁹*Id.* at 49; *Accord*, *United States v. Vorreiter*, 355 U.S. 15 (1957) (per curiam); *United States v. Arci*, 348 U.S. 211 (1955); *United States v. City of New Britain*, 347 U.S. 81 (1954). This question is to be distinguished from the question of whether the taxpayer has property or rights to property to which a federal tax lien could attach, the determination of which is a matter of state law. *United States v. Durham Lumber Co.*, 363 U.S. 522 (1960); *Aquilino v. United States*, 363 U.S. 509 (1960).

²⁰*Illinois v. Campbell*, 329 U.S. 362, 371 (1946); *In Puissegur v. Yarbrough*, 29 Cal. 2d 409, 412, 175 P.2d 830, 831 (1946), the determination of the California Supreme Court that the attaching creditor, under the California statute creating an attachment lien, derives only a potential right or a contingent lien, was regarded as conclusive.

²¹347 U.S. 81 (1954).

²²*Id.* at 84.

having determined that certain municipal liens were choate prior to emergence of the tax liens, applied the principle: "first in time is the first in right."²³

It is worthy of note that although the *New Britain* case held the lien choate, it imposed a strict double standard which required the lien to be both prior in time and choate;²⁴ and it is the only Supreme Court case to date which has subordinated a section 6321 tax lien to a statutory lien.²⁵ The strictness of the *New Britain* doctrine is illustrated by *United States v. White Bear Brewing Co.*,²⁶ which held that a statutory mechanic's lien, upon which suit for enforcement had been instituted, was inchoate as against a tax claim assessed prior to the date judgment was rendered thereon.²⁷

The first occasion to extend the doctrine of a nonstatutory contractual lien came in 1958 in *United States v. R. F. Ball Constr. Co.*²⁸ A subcontractor, in return for a surety's performance bond covering the completion of a housing project in Texas, assigned his rights to payments due from the principal contractor. Later, the subcontractor secured a second performance bond from the surety to cover a Kentucky project. Then in sequence: the Texas project was completed; the United States filed a tax lien against the subcontractor before the subcontractor was paid; the subcontractor defaulted on the Ken-

²³Id. at 85. The doctrine is comprehensively summarized by Chief Justice Marshall in *Rankin v. Scott*, 25 U.S. 12 (Wheat.) 104, 105 (1827): "The principle is believed to be universal, that a prior lien gives a prior claim, which is entitled to prior satisfaction, out of the subject it binds, unless the lien be intrinsically defective, or be displaced by some act of the party holding it, which shall postpone him in a court of law or equity to a subsequent claimant."

²⁴"We think that Congress had this cardinal rule in mind when it enacted § 3670 [now § 6321], a schedule of priority not being set forth therein. Thus, the priority of each statutory lien contested here must depend on the time it attached to the property in question and became choate." Id. at 86; Accord, *United States v. Bond*, supra note 7, at 844.

²⁵*United States v. Colotta*, 350 U.S. 808 (1955) (mechanic's lien was definite; however, the 'lis pendens' notice required by statute had not been filed); *United States v. Scovil*, 348 U.S. 218 (1955) (landlord's distress lien); *United States v. Liverpool & London-Globe Ins. Co.*, 348 U.S. 215 (1955) (garnishment lien); *United States v. Acri*, 348 U.S. 211 (1955) (attachment lien was contingent upon the outcome of suit for damages).

²⁶350 U.S. 1010 (1956) (per curiam).

²⁷In his vigorous dissenting opinion, Mr. Justice Douglas stated that the majority opinion implied that a lien is never choate until reduced to judgment, and that if this be the holding, it overruled *United States v. New Britain*. But, in his dissent, he impliedly accepted the validity of the choate test in statutory lien cases, while merely disagreeing with the majority as to the interpretation of the term choate. See *United States v. Bond*, supra note 7, at 845.

²⁸355 U.S. 587 (1958) (per curiam).

tucky project; and the surety paid an amount equal to its obligation on the Kentucky project.

The contractor filed an interpleader action to determine whether the tax lien, or the assignment to the surety, was entitled to a priority in the retained fund. The lower courts gave the surety the status of a mortgagee, as was appropriate under state law, and held that the surety's claim was protected under present section 6323(a).²⁹ The Supreme Court reversed, holding that "the instrument being inchoate was unperfected, the provisions of section [6323(a)] . . . do not apply."³⁰ As previously mentioned, the ambiguity of this cursory opinion resulted in considerable speculation,³¹ but this has been resolved by *Pioneer American*, wherein the Supreme Court said in reference to the *Ball* decision:

"While disagreeing on the choateness of the particular assignment involved there, the Court was unanimous in applying the choateness test to those seeking the protection of § 6323(a)."³²

Moreover, the Court concluded that the mortgage in *Ball* was one which secured future advances, the sums due the subcontractor having been assigned to the surety as security for any subsequent advances the surety might make under the surety contract. The Court summarized *Ball* and its application to *Pioneer American* as follows:

"*Ball* therefore rejects as inchoate an assignee's or mortgagee's lien to secure future indebtedness of the taxpayer-debtor . . . Likewise, when a mortgagee has a lien for an attorney's fee which is uncertain in amount and yet to be incurred and

²⁹It was then § 3672(a). *R. F. Ball Constr. Co. v. Jacobs*, 140 F. Supp. 60 (W.D. Tex. 1956), aff'd sub nom. *United States v. R. F. Ball Constr. Co.*, 239 F.2d 384 (5th Cir. 1956).

³⁰Op. Cit. at 587.

³¹Mr. Justice Whittaker, with whom Justice Douglas, Burton and Harlan joined in dissent, considered the assignment to be a valid mortgage, and so concluded that the surety was entitled to the protection of § 6323(a). Looking at the assignment as a mortgage, they doubted that the Court would have held it inchoate due to the fact that the recordation requirement under the state fraudulent conveyances act was not met for two reasons: first, the unique application of the choate doctrine to § 6323(a) would merit a more elaborate opinion; second, the majority supported its decision by citing the *Security Trust and New Britain* cases, two cases which had no applicability to § 6323(a). *United States v. R. F. Ball Constr. Co.*, 355 U.S. 587, 588-594 (1958).

But see *United States v. Bond*, supra note 7, at 845, where the majority of the court held that the *Ball* case had applied the choate doctrine to § 6323 (a), and the court suggests that the difference between the majority and the dissent was as to the interpretation of the term choate.

³²374 U.S. at 90.

paid, such a lien is inchoate and is subordinate to the intervening federal tax lien filed before the mortgagee's lien for attorney's fee matures."³³

The rationale of the Supreme Court in *Pioneer American* represents a logical development of authority for the extension of the choate rule to section 6323(a). It appears, however, that the Supreme Court has misconstrued the intention of Congress by holding that the principal and interest of a mortgage is choate, while another integral part of the mortgage, the right to attorney's fees, is at the same time inchoate. This misconstruction of the intent of Congress appears to be the direct result of the Supreme Court's apparent confusion as to what the word "mortgagee," as used in section 6323(a), actually denotes.

The Supreme Court in *Pioneer American* stated that the purpose of section 6323(a) was to afford a greater degree of protection to certain interests by requiring the tax lien to be filed, not merely assessed. Moreover, as the Court said, section 6323(a) deals with the priority of the federal lien only, and does not specify the time at which non-federal liens arise or become choate. It is difficult to agree, however, that Congress, by granting a preferential status to certain liens in section 6323(a), intended "that they should at least have attained the degree of perfection required of other liens and be choate for the purposes of the federal rule."³⁴ It appears that, inherent in this statement, there lies confusion as to the meaning of the term "mortgagee" as used in the statute.

State courts have traditionally recognized the relation-back doctrine as appropriately applicable in the field of mortgages which secure future advances.³⁵ The Supreme Court in *Security Trust* rejected the applicability of the relation-back doctrine to statutory liens competing with the section 6321 tax lien.³⁶ And, in *Pioneer American*, the Supreme Court rejected the relation-back doctrine as applied to a mortgage securing future advances or contingent liability, when in competition with a section 6323(a) tax lien.³⁷

It is submitted, however, that when Congress granted a preference

³³Id. at 91.

³⁴Id. at 89.

³⁵See notes 42-44 *infra*.

³⁶"Nor can the doctrine of relation back—which by process of judicial reasoning merges the attachment lien in the judgment and relates the judgment lien back to the date of attachment—operate to destroy the realities of the situation." 310 U.S. at 50.

³⁷374 U.S. at 92 n.11.

to any mortgagee, pledgee, purchaser, or judgment creditor, it used these terms in the "usual and conventional sense," as was said in *Hoare v. United States*.³⁸ Two leading Supreme Court cases indicate that in section 6323(a) Congress intended only the conventional usage of the term "judgment creditor."³⁹

Thus, it would seem that Congress also intended under section 6323(a) to apply the conventional interpretation of the word "mortgagee." The essential characteristic of a mortgage is that it is a security transaction. In such a transaction the mortgagee does not receive absolute title but takes the property subject to the mortgagor's equity of redemption.⁴⁰

The paramount question here is whether the purpose of Congress in enacting section 6323(a) will be frustrated by granting recognition to the conventional and historic rights of a mortgagee. Although Congress intended by section 6323 to facilitate the collection of federal taxes, it appears doubtful that Congress intended to subvert a well balanced security structure by such an enactment.

State courts have consistently recognized and validated mortgages for future advances, as was noted in the dissenting opinion in *United States v. Bond*:

"There is nothing novel in recognition of the fact that the protection of the mortgage lien extends to such disbursements and expenses [future advances], made pursuant to such provisions, as fully as to the principal of the mortgage debt itself. It is a usual and conventional right of a mortgagee."⁴¹

Although there is conflict in the state courts, the prevailing view is that a mortgagee who is contractually obligated to make future advances is accorded a senior status as to advances made subsequent to the attaching of a junior lien, even though he has actual notice of the junior lien; Mere voluntary advances, however, are not awarded

³⁸294 F.2d 823, 825 (9th Cir. 1961).

³⁹The Supreme Court made the following statement: "A cardinal principle of Congress in its tax scheme is uniformity, as far as may be.... In this instance, we think Congress used the words 'judgment creditor' in § 3672 [now § 6323] in the usual, conventional sense of a judgment of a court of record, since all states have such courts." *United States v. Gilbert Associates*, 345 U.S. 361, 364 (1953).

The Supreme Court supported this proposition by saying: "The history of this tax lien statute [§ 6323] indicates that only a judgment creditor in the conventional sense is protected." *United States v. Security Trust and Savings Bank*, 340 U. S. at 52.

⁴⁰*United States v. Gargil*, 218 F.2d 556 (1st Cir. 1955) (distinguishing between a valid mortgage and a sham which is in fact an attempted assignment for the benefit of creditors).

⁴¹*United States v. Bond*, 279 F.2d at 851.

priority in competition with prior attaching liens.⁴² The justification for this view is crystallized by the Supreme Court of Nevada:

"[W]e are of opinion that it would be manifestly unsound to hold that plaintiff's actual notice or knowledge of the defendant's subsequent mortgage had the effect of taking from him the security for advances and services he was compelled by his contract to make and perform."⁴³

Only Maryland has adopted by statute⁴⁴ a rule similar to that enunciated by the Supreme Court in *Pioneer American*, and that statute has been severely criticized.⁴⁵

The conventional interpretation of a mortgage securing future advances considers future advances to be an integral part of and inseparably connected with the rest of the mortgage contract. In sum, the future advances are said to relate back to the date at which the mortgage became effective. Consequently, the Supreme Court departed from the congressional intent in using the word "mortgagee" in section 6323, by denying the doctrine of relation-back for a mortgage securing future advances.

Strong policy considerations deny that a valid mortgage securing future advances can be divided into two separate parts, one part being held choate and perfected and the other part being held inchoate and unperfected. A mortgage is an indivisible security device, either

⁴²E.g., *Ashdown Hardware Co. v. Hughes*, 223 Ark. 541, 267 S.W.2d 294 (1954); *Simpson v. Simpson*, 123 So. 2d 289 (Fla. Dist. Ct. App. 1960); *Axel Newman Heating & Plumbing Co. v. Sauers*, 234 Minn. 140, 47 N.W.2d 769 (1951); *North v. McClintock*, 208 Miss. 289, 44 So. 2d 412 (1950); *Chartz v. Cardelli*, 52 Nev. 1, 179 Pac. 761 (1929); *Peaslee v. Evans*, 82 N.H. 313, 133 Atl. 448 (1926); *New York & Suburban Fed. Sav. & Loan Ass'n v. Fi-Pen Realty Co.*, 133 N.Y.2d 33 (Sup. Ct. 1954).

⁴³*Chartz v. Cardelli*, 52 Nev. 1, 279 Pac. 761, 763 (1929).

⁴⁴"No mortgage... shall be a lien or charge on... property for any other... sum... than the principal sum... that shall appear on the face of such mortgage and be specified and recited therein, and particularly mentioned and expressed to be secured thereby at the time of executing the same...; [and] no mortgage to secure future loans or advances shall be valid unless the amount... of the same and the times when they are to be made shall be specifically stated in said mortgage..." Md. Ann. Code art. 66 § 2 (1957).

⁴⁵In *re Shapiro*, 34 F. Supp. 737 (D. Md. 1940) (the court, while expressing its regret, held a mortgage for future advances void as contrary to Maryland law).

"Indeed, the Maryland statute... appears to be almost unique in the English-speaking world. It has never had a State-wide application in Maryland. In other jurisdictions the controversy is not as to the validity of mortgages for future advances, but chiefly whether they should be preferred to the claims of subsequent lienors, especially in cases where the lender was not obligated to made [sic] such advances. However, the call for legislative change... has not been heeded... ." *Leister v. Carroll County Nat'l Bank*, 199 Md. 241, 86 A.2d 393, 396 (1952).