



THE CANADIAN BAR ASSOCIATION  
L'ASSOCIATION DU BARREAU CANADIEN

The Voice of  
the Legal Profession  
La voix de la  
profession juridique

February 14, 2005

The Honourable Senator Jerahmiel S. Grafstein, Q.C.  
Chair  
Standing Committee on Banking, Trade and Commerce  
The Senate  
Ottawa ON K1A 0A4

Dear Senator Grafstein:

**Re: Bill S-19: Criminal Interest Rate**

I refer to my appearance on February 3, 2005, before the Standing Committee on Banking, Trade and Commerce on behalf of the Canadian Bar Association Business Law and Real Property Law Sections (CBA Sections).

As per the request of the Committee, I enclose an article on New York State usury rules.<sup>1</sup> The article makes it clear that the law is not simple. There is indeed a 16% state law for usury and also a federal 25% cap for criminal usury. However, there are other laws affecting compounding, first mortgages, prepayment, and the like. The article notes that many loans are exempted, with the result:

- virtually all business loans over \$2.5 million are exempted from these statutes
- loans from certain federally regulated lenders are exempted

There are also other exemptions and cases that reinforce the CBA Sections' point that there is no "simple" fix to the situation and this is not achieved by merely adjusting the rate.

Yours truly,

*(Original signed by Trevor M. Rajah on behalf of Jennifer E. Babe)*

Jennifer E. Babe  
Vice Chair, Business Law Section

cc: The Honourable Senator Madeleine Plamondon

Encl.

---

<sup>1</sup> Joshua Stein, "Confusory Unraveled: New York Lenders Face Usury Risks when in Atypical or Small Transactions", 2001 New York State Bar Association Journal, (July/August).

[Estate-Law.com](#) | [Mortgage Lending](#) | [How to Contact Joshua Stein](#)

Search

## Confusury Unraveled: New York Lenders Face Usury Risks When in Atypical or Small Transactions

By [Joshua Stein](#)

*New York State Bar Association Journal*, July/August 2001

[Click Here for Consent Information and Caveats Regarding the Reprinting of This Article](#)

Copyright © 2001 Joshua Stein

[Joshua Stein](#) is a real estate and finance partner in the New York office of [Latham & Watkins](#) (e-mail [joshua.stein@lw.com](mailto:joshua.stein@lw.com)). A member of the [American College of Real Estate Lawyers](#), he serves as chair of the [Practising Law Institute](#) annual seminar on commercial real estate financing. This article, an updated and revised version of a review of usury law that appeared in the fall 1993 newsletter of the [NYSBA](#) Real Property Law Section, is to be a chapter in the author's forthcoming book, [New York Commercial Mortgage Transactions](#) (Aspen Law & Business). The author is a graduate of the [University of California at Berkely](#) and received his J.D. degree from [Columbia University](#).

New York's usury law consists of a scrambled collection of statutes, most of which appear in the New York General Obligations Law.<sup>[1]</sup> Combined with federal preemption in certain areas described below, these statutes exempt most substantial commercial lending transactions from any usury restrictions.<sup>[2]</sup>

"Usury" remains a potential trap only for the unwary loan shark (who probably does not care, because the judicial system is not highly relevant to his activities anyway) and participants in a few other atypical or small lending transactions.<sup>[3]</sup>

In the occasional weird case where usury restrictions do apply, a violation can invalidate the entire loan and constitute a felony.<sup>[4]</sup> A practitioner must be alert to this risk whenever considering any loan transaction that is small or involves a borrower other than a corporation or limited liability company.<sup>[5]</sup>

As in any other area, the practitioner should always refer to the most current version of the applicable statutes and other law before rendering any advice on New York usury law.

The following discussion of New York usury law does not cover any loan

restrictions beyond usury and compound interest, such as prepayment, attorneys' fees, discount points, prepaid interest, and late charges. Adjustable-rate residential mortgages are subject to their own interacting federal and state limitations and disclosure requirements, which are beyond the scope of this article. [6] Exemptions for broker-dealer loans are also not addressed. [7] For ordinary mortgage loan transactions, the most common escape hatches from usury include those discussed below.

The flowchart accompanying this article is designed to summarize New York's usury maze. The flowchart analysis begins on page \_\_\_, with the oval marked "START." It continues down the page. Lines indicate the sequence of issues to consider. Diamond boxes indicate decision points, each with a question that can be answered "YES" or "NO." Depending on the answer, the analysis continues down one path or the other. [NOTE: ADD FLOWCHART.]

The paths of analysis sometimes lead to more diamond boxes, each another decision point. Eventually, all roads lead to rectangles, representing conclusions. Some of these rectangles represent incomplete conclusions. In those cases, the rectangle has a second path leading out of it, and the analysis continues down that path because one must ask more questions.

Most boxes on the flowchart contain small reference number(s). Each such number refers to a footnote in the following discussion, directing the reader to the text and footnotes where a discussion of the particular issue begins. That discussion contains citations, details, qualifications, and more information to consider. The flowchart should be considered only in the context of this article as a whole.

Do not take this flowchart too literally. It merely summarizes information in a way that many people find practical and interesting. An attorney considering a particular set of facts may find that by using some other order or approach instead, the attorney will achieve the best possible result and the most appropriate analytical basis for it.

### **Maximum Rate**

In the rare factual circumstance where New York's usury ceiling actually applies and federal law does not preempt it, a lender usually cannot charge interest higher than 16% per annum. [8] The Banking Law contains similar provisions. [9] "Interest" includes certain other charges payable to the lender on account of the loan. The usury ceiling rises by 150 basis points to 17.5% per annum for loans secured by cooperative apartments. [10]

Floating-rate loans and loans that contemplate future advances create a few special complications of their own, which are beyond the scope of this article. [11]

The courts have established some rules for calculating just how much interest a lender is actually collecting on a loan (such as the effect of prepayment of interest). These rules can be crucial in close cases but are outside the scope of the present discussion.

## **Compound Interest**

Independent of the usury restrictions, New York limits a lender's ability to collect compound interest. Even if a loan is not usurious, the lender may be barred from charging interest on the borrower's unpaid interest. In general, New York prohibits compound interest on any loan of \$250,000 or less, except in the following cases:

- *Certain Business Loans.* Business loans of \$100,000 or more secured under the Uniform Commercial Code with a rate at or below prime plus 8% percent per annum; [12]
- *Certain UCC Loans.* Demand loans of \$5,000 or more secured by certain Uniform Commercial Code documents [13]; and
- *Other.* Statutory exceptions enacted for particular industries. [14]

New York prohibits compound interest on any loan, regardless of amount, secured by a "one or two family owner-occupied residence," including a cooperative apartment. [15]

If a lender illegally charges compound interest and the net effective interest rate after compounding is at or below the usury ceiling, he or she must refund the "compounded" part of the interest but not the other interest already paid. In that case, the lender faces no other forfeiture risk. If the effective interest rate, after compounding, exceeds the usury ceiling, then the severe penalties for regular "usury" will apply. [16]

Until 1989, New York courts had, for almost two centuries, invalidated compound interest in a number of cases, as if interest payable on unpaid dollars of "interest" was something completely different from interest payable on unpaid dollars of "principal." Although in recent years courts have sometimes apparently struggled to find exceptions to the general New York rules against compound interest, New York has retained its rule against compound interest. The Legislature solved the problem in 1989 primarily at the urging of Martin E. Gold, formerly director of corporate law in the New York City Law Department and now with Sidley Austin Brown & Wood in Manhattan. [17]

If a mortgage loan that provides for "compound" interest does not run afoul of New York's rules in this area, the lender must still confront another old friend, the mortgage recording tax. If the loan documents provide, or the parties ever agree, that unpaid interest shall be added to principal (for example, as part of a workout), then the loan thereby incurs additional mortgage recording tax on the resulting new "principal indebtedness." Moreover, the Department of Taxation and Finance takes the view that as soon as interest starts to accrue on previously accrued interest, the previously accrued interest becomes principal and hence itself subject to mortgage recording tax. [18]

## **Penalties for Usury**

If a loan is usurious, it becomes wholly void. [19] The lender forfeits all

principal and interest<sup>[20]</sup> (the loan becomes a gift) and the borrower can also recover the usurious portion of the interest previously paid. [21] If the lender is “a savings bank, a savings and loan association or a federal savings and loan association” or within certain other categories of institutional lender, the statute provides a different penalty: the lender forfeits all interest (not just the usurious part of the interest), but not principal, and may also be required to repay the borrower twice the interest actually paid. [22]

### **Criminal Usury**

New York has a separate criminal usury ceiling of 25% per annum on nonexempt loans. Any lender that knowingly collects criminally usurious interest commits a felony. [23] The criminal usury ceiling applies to some loans that are not subject to civil usury restrictions at all: loans of \$250,000 or more; and certain secured loans of \$5000 or more that are payable on demand.

In these cases, however, New York law does not appear to give the victim of usury any express civil remedy against the lender. [24] A few cases say that banking institutions are exempt from criminal liability for usury. [25] The only penalty available against them would thus appear to be forfeiture.

### **Federal Preemption for Residential First-Mortgage Loans**

Federal law preempts all state interest-rate restrictions, presumably both “usury” and “compound interest” restrictions, for residential first-mortgage loans (including first-lien co-op loans) made to any borrower by any federally insured institution, federally regulated lender, federal government agency, lender approved by the Federal Home Loan Mortgage Corporation (Freddie Mac), any other lender that regularly makes residential mortgage loans totaling more than \$1,000,000 a year, or a number of other lenders regulated by or connected with the federal government.

Although Congress allowed the states to override the federal usury preemption for residential first-mortgage loans, New York did not. To the contrary, New York affirmed the federal override. [26] As a result, virtually all residential first mortgages [27] are exempt from New York usury restrictions. [28] Federal law also supersedes state usury restrictions for certain other categories of loans, but these miscellaneous exemptions generally will have no practical effect given the other exemptions and preemptions available and today’s rate environment. [29]

### **Junior Mortgages; Other Institutional Lender Exemptions**

A New York state-chartered bank or trust company or licensed mortgage banker may make junior mortgage loans to individual borrowers at whatever interest rate is “agreed to by the [lender] and the borrower.” [30] By implication these loans are exempt from the usury ceiling in the New York General Obligations Law. [31]

Similar exemptions-by-implication would probably apply to certain “personal loans” made by a state bank or trust company, foreign bank, or other licensed

lenders. [32] Other state banking-related statutes may permit specific regulated lenders to charge interest above the usury ceiling.

### **Loans of \$2,500,000 or More**

\* Any loan of \$2,500,000 or more (including obligatory future advances), is exempt from all usury restrictions, including criminal usury. [33] This simple provision of New York law basically solves the usury problem for all substantial commercial loans and is a major part of the reason that multistate loan transactions are often governed by New York law.

If, however, the loan is secured by a “one or two family owner-occupied residence,” including a cooperative apartment, [34] the lender still cannot collect compound interest. [35] For most residential first mortgages, however, as previously described, federal law would preempt even the restriction on compound interest.

### **Limited Liability Company and Corporate Borrowers**

\* A limited liability company (LLC) or corporate borrower cannot “interpose the defense of usury in any action,” [36] nor can a guarantor of a corporation’s debt. [37] The same logic would suggest that a guarantor of a limited liability company’s obligations should also not be able to raise a usury defense. The courts do not seem, however, in any reported case to date to have addressed the implications for a guarantor.

Some very old cases suggest that a corporation also cannot affirmatively commence an action to invalidate a usurious obligation. [38] No recent New York case has considered this question. The courts’ general attitude in this area would indicate, however, that a corporation (presumably also an LLC) probably could not assert usury even as an affirmative claim. A New York corporate or LLC borrower can still assert the invalidity of compound interest on loans of \$250,000 or less. [39] The usury exemption for loans made to a corporate or LLC borrower does not apply to entities formed to own a one- or two-family dwelling. [40] Finally, a corporate loan remains potentially subject to criminal usury restrictions, as described elsewhere in this article, although these restrictions are enforceable solely by the state.

A commentator on New York usury law recently described the remaining usury restrictions on corporate loans as being much like “the appendix in humans and wings on flightless birds,” and as an economic matter “not only useless, but unsound as well.” [41]

### **Loans of \$250,000 or More**

\* Any loan of \$250,000 or more not “secured primarily by an interest in real property improved by a one or two family residence” is treated the same as any loan of \$2,500,000 or more, except that criminal usury restrictions still apply.

[42]

Various additional statutory exemptions sometimes also come into play. [43]

### **Usury Savings Clauses**

Lenders will often include in their documents "usury savings clauses," language saying that if the loan turns out to be usurious, then any payments by the borrower above the allowable rate shall be retroactively recharacterized as repayments of principal. In the few cases that have considered the validity and effectiveness of such clauses, the results were not encouraging for lenders.

The decision in *Federal Home Loan Mortgage Corporation v. 333 Neptune Avenue Limited Partnership* offers an interesting, though typically unilluminating, example. [44] There, a bankruptcy court applying New York law initially found that the loan, although usurious, was saved by the "usury savings" clause. The District Court for the Eastern District of New York rejected that reasoning, concluding instead that the "'usury-avoidance' provision does not save the otherwise usurious loan. Since the loan is usurious, it is void." [45] The court followed by analogy an old and well-established line of New York cases holding that a lender cannot cure an otherwise usurious loan by simply returning to the borrower (or alternatively, allowing credit for) interest payments above the usury cap. [46]

On appeal of the *333 Neptune Avenue* case, the Second Circuit explicitly refused to adjudicate the issue, saying that the "usury savings" provision raises "knotty and undecided questions of New York state law that are best avoided by federal courts." [47] The appellate court vacated and remanded the decision of the District Court. No published opinion was available at the time of this research.

A few years earlier, the Appellate Division in a memorandum decision ignored a "usury savings" provision. Although the loan documents in that case said that if the interest rate were found to be usurious it would drop to the legal rate, the court decided this was not enough to make the loan nonusurious. [48]

The court cited its own 1965 decision, *Durst v. Abrash*, where it had concluded that even if the parties agree to arbitrate any disputes over the interest rate, the courts can still examine whether a loan is usurious and impose appropriate remedies. [49] Over a dissent that implied the usury statutes may be second- or third-class citizens in the statute books, [50] the *Durst* majority concluded that usury statutes are to be taken seriously and the parties should not be able to sidestep them. [51] By citing the *Durst* case in its 1994 case on usury savings clauses, the court suggested that it regards usury savings clauses as the functional equivalent of using arbitration to avoid usury issues.

The question of the enforceability of usury savings clauses has not been resolved by the New York Court of Appeals. The reported cases to date suggest serious skepticism regarding such clauses, though they would appear to do no harm.

In contrast, it is the author's sense that practitioners in this area do place some weight on usury savings clauses. Practitioners may assume that usury

savings clauses work based perhaps on the general theories that (a) the courts don't like usury law very much; and (b) words in a document usually mean what they say. The preceding discussion demonstrates, however, that neither assumption is necessarily correct in the area of usury savings clauses. Practitioners should place little or no reliance on usury savings clauses. In particular, if counsel is asked to opine that a loan is not usurious, counsel should reach that conclusion based on something other than a usury savings clause.

### Usury Summary and Conclusion

Considered as a whole, the usury exemptions and preemptions summarized above virtually assure that any significant commercial loan, and almost every residential mortgage loan, will be exempt from New York usury restrictions. Aside from the exemptions and preemptions discussed above, particular factual situations may suggest other usury defenses and definitional exclusions found in the cases but not discussed here.

\* Common escape hatches from usury include: (1) interest after default or after maturity; (2) deferred purchase price [52]; (3) waiver; (4) burdens of proof; (5) standing (the usury defense is available only to the original borrower); (6) application of another state's law; (7) estoppel (including the borrower's delivery of an estoppel certificate [53]); and (8) other equitable defenses.

Does title insurance solve any possible usury problem? No. The American Land Title Association 1992 standard loan policy of title insurance expressly excludes any coverage for usury. [54] And the New York title insurance industry's rate manual does not allow title insurance companies to insure against usury risks, such as by issuing a usury endorsement.

Given how easy it is to steer clear of usury problems in New York commercial transactions, however, the lack of title insurance protection against New York usury rarely causes much concern in this area of practice.

---

JOSHUA STEIN is a real estate and finance partner in the New York office of Latham & Watkins (e-mail A member of the American College of Real Estate Lawyers, he serves as chair of the Practising Law Institute annual seminar on commercial real estate financing. This article, an updated and revised version of a review of usury law that appeared in the fall 1993 newsletter of the NYSBA Real Property Law Section, is to be a chapter in the author's forthcoming book, *New York Commercial Mortgage Transactions* (Aspen Law & Business). The author is a graduate of the University of California at Berkely and received his J.D. degree from Columbia University.

---

### Endnotes



[1] For a more on New York usury law, see Bruce J. Bergman, Bergman on New York Mortgage Foreclosures, Volume 1 at 6-4 (Matthew Bender, updated annually).

[2] Although this work generally disregards residential transactions, they must be taken into account to provide a reasonable summary of New York usury law.

[3] This article is based in substantial part on the author's previous article on New York usury law. See Joshua Stein, *Confusury Unraveled: A Road Map of New York's Usury Law*, N.Y. STATE BAR ASS'N REAL PROP. L. SECTION NEWSL., Fall 1993, at 17. That article was extensively updated and expanded for this republication.

[4] See N.Y. PENAL LAW §§ 190.40, 190.42 (McKinney 1999).

[5] Thus New York, which prides itself on being more practical and business-like than California, ends up with a usury law functionally the same as California's, which one article described as follows:

[U]sury law [in California] does not seriously inconvenience most lenders and offers very little protection to most borrowers. The law in this area has a loud bark but rarely bites. However, its rare bite can be painful indeed. This may be good politics, but it makes for complex law.

E. Rabin & R. Brownlie, "Usury Law in California: A Guide Through the Maze," 20 U.C. Davis L. Rev. 397, 440 (Spring 1987).

[6] See 12 U.S.C. § 3803(c) (1998); 12 C.F.R. § 226.19 (1999); N.Y. BANKING LAW §§ 6-f, 6-g (McKinney 1999).

[7] See N.Y. GEN. OBLIG. LAW ("GOL") § 5-525 (McKinney 1999).

[8] See GOL § 5-501(1) (maximum usury rate 6% unless otherwise provided in N.Y. BANKING LAW § 14-a); N.Y. BANKING LAW § 14-a(1) (McKinney 1999) (16% maximum usury rate for purposes of GOL § 5-501). GOL § 5-501(3)(b) sets special rules for most residential loans where the annual interest rate exceeds 6%. In these cases, the borrower has the statutory right to prepay at any time. The lender cannot collect a prepayment fee unless the prepayment occurs in the first year and the documents expressly provide for such a fee. See GOL § 5-501(3)(b). This statute expressly provides for federal preemption.

[9] See N.Y. BANKING LAW § 14-a(1) (McKinney 1999); see also, e.g., N.Y. BANKING LAW §§ 108(1) (state bank or trust company), 173(1) (private bankers), 202(1) (foreign banks), 510-a (investment companies) (McKinney 1999); 3 N.Y. COMP. CODES R. & REGS. tit. 3, § 4.1 (McKinney 1999).

[10] N.Y. BANKING LAW §§ 103(5), 235(8-a), 380(2-a) (McKinney 1999).

[11] GOL § 5-501(4), (4-a); N.Y. BANKING LAW § 14-a(1)-(2); N.Y. COMP. CODES R. & REGS. tit. 3, §§ 4.1-4.2 (regulations adopted by Banking Board) (McKinney 1999).

[12] GOL § 5-526. The prime rate means "the average prime rate on short term business loans which is published by the board of governors of the federal reserve system for the most recent week which was publicly available from the board of governors of the federal reserve system on the previous business day." GOL § 5-526(4).

[13] GOL § 5-523.

[14] See, e.g., N.Y. INS. LAW § 3203(a)(8)(G) (McKinney 1999); Martin E. Gold, New York Approves Law Legalizing Compound Interest, 62 N.Y. STATE BAR J. 26, 27-28 (October 1990) (citing other industry-specific statutory exceptions).

[15] See GOL § 5-527(2). The statute defines "residence" to "include" a cooperative apartment, but says nothing about condominiums. A court would probably say "residence" also includes a condominium apartment.

[16] *Giventer v. Arnow*, 37 N.Y.2d 305 (1975).

[17] The history of compound interest in New York and the 1989 legislation are described in two articles by Mr. Gold: *Compound Interest: Legalization Wins Approval*, N.Y.L.J., June 15, 1989, page 1; and *New York Approves Law Legalizing Compound Interest*, N.Y. STATE BAR J., October 1990, page 26.

[18] See Op. N.Y. State Dep't of Taxation & Fin., *Ticor Title Guarantee Company*, N.Y. St. Tax Rptr. (CCH) 401-177 at 46,171 (June 25, 1993) (mortgage recording tax imposed on capitalized interest "as if the interest had been actually paid to the mortgagee and the mortgagee then loaned the same amount back to the mortgagor"). Goldberg asks whether the parties might avoid this result by recharacterizing the "compound interest" as simple interest calculated using a different formula. "If interest has become due, and the lender then agrees to defer payment of that interest in return for the borrower's agreement to pay interest on the deferred interest, or if the borrower exercises an option to capitalize interest, then it would seem that the deferred interest has become principal. However, if the initial loan agreement provided that interest would be compounded, then it would seem, although this is not the present state of the law, that the compounding is merely the means of calculating the cost of borrowing the original principal." David M. Goldberg, *Transfer and Mortgage Recording Taxes in New York Title Closings* § 6-13(a) (Lexis Law Publishing, republished annually). In *Cosmopolitan Broadcasting Corp. v. State Tax Comm'n*, 435 N.Y.S.2d 804 (App. Div. 1981), the court required payment of mortgage recording tax on the total amount of principal indebtedness when the documents failed to distinguish between principal and interest. If unpaid interest is added to principal, the logical extension of this case would require payment of mortgage recording tax on the additional principal indebtedness.

[19] GOL § 5-511(1) (unless lender is savings bank, savings and loan association, or federal savings and loan association). See also *Eikenberry v. Adirondack Spring Water Co.*, 65 N.Y.2d 125, 126 (1985).

[20]

[21] GOL § 5-511, 5-513 (McKinney 1999). But see GOL § 5-519 (granting partial relief if lender repays excess interest).

[22] GOL §§ 5-511(1), 5-513; see also, e.g., N.Y. BANKING LAW §§ 108(6), 202(7), 235-b, 380-e, 510-(a)(1) (McKinney 1999).

[23] N.Y. PENAL LAW §§ 190.40, 190.42 (McKinney 1999).

[24] See *American Express Co. v. Brown*, 392 F. Supp. 235, 238 (S.D.N.Y. 1975) (discussing the inability of the victim "to personally enforce the criminal usury law of the state") (dictum).

[25] See *Flushing Nat'l Bank v. Pinetop Bldg. Corp.*, 387 N.Y.S.2d 8 (2d Dep't. 1976), citing *Franklin Nat'l Bank v. DeGiacomo*, 248 N.Y.S.2d 586 (App. Div. 1964); *Reisman v. Hartman & Sons*, 273 N.Y.S.2d 295 (1966). See also *Tides Edge Corp. v. Central Fed. Sav., F.S.B.*, 542 N.Y.S.2d 763 (App. Div. 1989).

[26] N.Y. BANKING LAW § 14-a(7) (McKinney 1999).

[27] The term "first mortgage" would probably not include a wraparound mortgage. See *Mitchell v. Trustees of U.S. Mut. Real Estate Inv. Trust*, 375 N.W.2d 424, 430 (Mich. Ct. App. 1985). This type of mortgage arises where the parties want to preserve an existing mortgage, probably with a below-market interest rate. The borrower signs a new mortgage, part of which is "new money" and part of which just replicates the principal indebtedness secured by the old underlying mortgage. The borrower makes payments only to the holder of the "wraparound," who is supposed to pay the "underlying" mortgage. Typically the holder of the wraparound mortgage benefits from the difference between a low interest rate on the underlying mortgage and a higher rate on the entire wraparound mortgage. These transactions are less common today than they once were, for several reasons. First, interest rates are relatively low. Second, most existing mortgages categorically prohibit any further mortgages. Third, wraparound mortgages create substantial risks for all parties except the holder of the wraparound — risks that were not adequately identified, analyzed, and dealt with during the last wave of wraparound financing. Finally, those risks created unique problems for cooperative apartment corporations, which were often left as potential bagholders in the early Nineties when a sponsor took back a wraparound mortgage, assigned it to "Wrap, Inc." (literally, in at least one case), then defaulted on maintenance payments for the unsold apartments, yet continued to collect payments on the wraparound mortgage. The "wraparound mortgage" structure is not highly favored today, but is still occasionally seen.

[28] Common exceptions include mortgages involving unusual lenders and careless lenders taking a mortgage on a "residential manufactured home" that fail to comply with certain consumer protection requirements. See 12 U.S.C. § 1735f-7a(c), (d), (e)(4); *Quiller v. Barclays American/Credit Inc.*, 764 F.2d 1400 (11th Cir. 1985) (construing the transaction as nevertheless complying with federal regulations because language allowing borrower a right to cure implied borrower would receive notice of default), *aff'g en banc* 727 F.2d 1067, 1072 (11th Cir. 1984) (denying protection of federal preemption because a contract term allowed lender to commence foreclosure without notice upon default); 12 C.F.R. §

590.1-4 (1999) (implementing regulations for consumer protection).

[29] See, e.g., 12 U.S.C. § 1735f-7a (1998) (loans insured under Titles I and II of National Housing Act); 38 U.S.C. § 3728 (1998) (Veterans Administration guaranteed loans); 12 U.S.C. § 85 (1998) (national banks not subject to states' discriminatory rate caps or caps below discount rate plus 1%); 12 U.S.C. § 1831d (1998) (preempting state usury ceilings below discount rate plus 1%); Depository Institutions Deregulation and Monetary Control Act of 1980, § 511(a), Pub. L. No. 96-221, 94 Stat. 132 (1980) (certain business and agricultural loans made between 1980 and 1983); GOL § 5-501(5) (loans insured by "federal housing commissioner" or pursuant to "Servicemen's Readjustment Act of 1944") (McKinney 1999). The foregoing does not purport to list all banking-related statutes that could preempt New York usury laws.

[30] See N.Y. BANKING LAW §§ 103(4-a) (state bank or trust company), § 591-a(1) (licensed mortgage bankers, limiting security to residential real property on mortgage that is not a first lien) (McKinney 1999).

[31] See *Novelty Textile Mills, Inc. v. Hopkins*, 547 N.Y.S.2d 516, 517 (Sup. Ct. 1989).

[32] See N.Y. BANKING LAW §§ 108(4)(b), (5)(b), 202(4)(b), 352(a) (McKinney 1999). These "exemptions-by-implication" might not avoid criminal usury problems.

[33] See GOL § 5-501(6)(b) (McKinney 1999).

[34] The statute does not expressly refer to condominium apartments. One would expect a court to treat condominium apartments the same as cooperative apartments, as they would seem to be functionally equivalent at least for purposes of usury and consumer protection.

[35] See GOL § 5-527(2) (McKinney 1999).

[36] GOL § 5-521(1) (McKinney 1999); N.Y. Ltd. Liab. Co. Law § 1104 (McKinney 1999).

[37] See *First Nat'l Bank of Amenia v. Mountain Food Enter., Inc.*, 553 N.Y.S.2d 233, 234 (App. Div. 1990). The documents in this case were vague about whether the corporation or the individual guarantor was the true borrower. The court decided that the availability of the usury defense hinged on "whether the loan was made to repay personal obligations or to further a profit-oriented enterprise." *Id.* at 235. If the latter, then neither borrower nor guarantor could raise a usury defense.

[38] See, e.g., *Atlantic Trust Co. v. Proceeds of the Vigilancia*, 68 F. 781, 782 (S.D.N.Y. 1895) (stating that the usury statute is, in effect, repealed as to corporations, citing *Merchants Exch. Nat'l Bank v. Commercial Warehouse Co.*, 49 N.Y. 635 (1872); *Rosa v. Butterfield*, 33 N.Y. 665 (1865); *Curtis v. Leavitt*, 15 N.Y. 9 (1857)).

[39] Although loans to a borrower of this type remain subject to

"criminal usury" limits, that statute is a criminal one enforceable only by the State.

[40] See GOL § 5-521(2) (McKinney 1999).

[41] Paul Golden, Evolution of Corporate Usury Laws Has Left Vestigial Statutes That Hinder Business Transactions, N.Y. STATE BAR J., May 2001, page 20. Mr. Golden is right on all counts.

[42] See GOL § 5-501(6)(a) (McKinney 1999).

[43] These include the following: Any loan of \$5,000 or more, payable on demand, secured by a pledge of documents of title or negotiable instruments under Article 3, 7, or 8 of the Uniform Commercial Code, is exempt from all restrictions on interest rates and interest compounding, except criminal usury. See GOL § 5-523 (McKinney 1999). The Banking Law contains similar provisions. See, e.g., N.Y. BANKING LAW § 510-a(2) (McKinney 1999) (loans by investment companies) (McKinney 1999). In general, no usury restrictions apply, not even criminal usury, when a corporation borrows \$100,000 or more (not including future discretionary advances) for business purposes, at a rate of up to prime plus eight percent per annum, granting a UCC security interest as security. See GOL § 5-526 (McKinney 1999).

[44] the usury savings clause at issue stated in relevant part:

Under no circumstances shall Mortgagor be charged under the note or this Mortgage, more than the highest rate of interest which lawfully may be charged by the holder of this Note and paid by the Mortgagor on the indebtedness secured hereby . . . Should any amount be paid to Mortgagee in excess of such legal rate, such excess shall be deemed to have been paid in reduction of the principal balance of the Note.

201 F.3d 431, 1999 WL 1295933, 3 (2d Cir. 1999) (as quoted in an unpublished Second Circuit opinion).

[45] Federal Home Mortgage Corp. v. 333 Neptune Avenue L.P., 1999 WL 390837 (E.D.N.Y. 1999).

[46] See Babcock v. Berlin, 475 N.Y.S.2d 212 (Sup. Ct. Suffolk County 1984); Bowery Sav. Bank v. Nirenstein, 269 N.Y. 259 (1935). See also Yakutsk v. Alfino, 349 N.Y.S.2d 718 (1st Dep't 1973) (giving credit for excess interest will not cure a usurious loan).

[47] 201 F.3d 431, 1999 WL 1295933, 3 (2d Cir., 1999).

[48] See Simsbury Fund, Inc. v. New St. Louis Assocs., 611 N.Y.S.2d 557 (1st Dep't. 1994).

[49] Durst v. Abrash, 253 N.Y.S.2d 351, 355, *aff'd*, 17 N.Y.S.2d 445 (1965) ("[if] usurious agreements could be made enforceable by the simple device of employing arbitration clauses the courts would be surrendering their control over public policy in a way in which the Court of Appeals . . . made very clear could not happen.").

[50] This is a characterization with which the author would agree, at

least in the world of commercial mortgage loans.

[51] Id. at 356 ("The welter of legislation in this area makes clear that the concern is one of grave public interest and not merely a regulation with respect to which the immediate parties may contract freely").

[52] See, e.g., *Mandelino v. Fribourg*, 23 N.Y.2d 145, 295 N.Y.S.2d 654 (1968); *Christopher v. Gurrieri*, 655 N.Y.S.2d 654, 655 (App. Div. 1997) (mem.) (where promissory note arose from purchase of business, it "was neither a loan nor a forbearance . . . but was in the nature of a purchase money mortgage which is not subject to the usury laws"). Compare, *C&M Air Systems, Inc. v. Custom Land Dev. Group II*, 692 N.Y.S.2d 146 (App. Div. 1999) (upholding an interest rate defined in the documents as "the highest rate of interest permitted," without deciding whether the transaction was an exempt purchase money loan). The usury exemption for deferred purchase price may also be available to a third-party lender that finances an acquisition. *Dallas vs. Dallas*, 582 N.Y.S.2d 835, 836 (3rd Dep't. 1992) ("[a] mortgage given to secure money, borrowed for the purpose of purchasing real property, is generally held to be a purchase-money mortgage, notwithstanding that the mortgage was given to a person other than the seller," citing *Barone v. Frie*, 472 N.Y.S.2d 119, 121 (App. Div. 1984)). But see Bruce J. Bergman, *Usury and the Purchase Money Mortgage — An Appellate Division Faux Pas (?)(!)*, 21 N.Y. STATE BAR ASS'N REAL PROP. L. SECTION NEWSL. 4 (January 1993) (describing *Dallas* case as "manifestly incorrect"). There is no reason to think that New York's usury exemption for purchase-money mortgages applies only to first mortgages, although the author is not aware of any authority on point.

[53] In *Hammelburger v. Foursome Inn Corp.*, 54 N.Y.2d 580, 584, 446 N.Y.S.2d 917, 919 (1981), the Court of Appeals concluded that, based on delivery of an estoppel certificate in connection with an assignment of the loan, the mortgagor "will be estopped from asserting the defense of criminal usury" unless the assignee knew about the problem or knew that the estoppel certificate was obtained under duress. If criminal usury arises whenever the rate exceeds 25% per annum, how could an assignee claim ignorance of the criminal usury problem? Answer: the rate in the documents might have been 24%, but if the original lender had extracted a 10% loan fee, not mentioned in the documents, this would probably bring the effective interest rate above 25%, depending on the term of the loan. Such a loan might be criminally usurious, but the assignee might not know it. If an estoppel certificate can immunize an otherwise usurious loan, can the original holder use this principle protectively, such as by requiring the borrower to deliver an estoppel certificate either at the closing or shortly thereafter to induce the holder to agree to some modification of the loan? Can the original holder rely on such an estoppel certificate?

[54] See "Exclusion from Coverage" No. 5 in the ALTA 1992 Loan Policy of Title Insurance.

---

[Top of Document](#)

Copyright © 2001 [Joshua Stein](#)