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Legality of Agreements To Pay Interest on Interest in New York

COMMENT

LEGALITY OF AGREEMENTS TO PAY INTEREST ON INTEREST IN NEW YORK

"That court best serves the law which recognizes that the rules of law which grew up in a remote generation may, in the fullness of experience be found to serve another generation badly, and which discards the old rule when it finds that another rule of law represents what should be according to the established and settled judgment of society. . . ."[1]

Nevertheless it should be noted in connection with the aforementioned guide for a judicial prerogative that, while the aims expressed therein may be laudable, the results are not always their heirs. The adherence of the courts to the principle of *stare decisis* is often too compelling to permit the complete abandonment of a particular judicial precedent and thus the courts are inclined to resort to fine distinctions and qualifications which at the time ameliorate, but, when viewed in retrospect, often make for an incongruous maze. Thus while the old rule remains, the exceptions to it increase and the ensuing inconsistencies multiply.[2] To such a situation, one might well append the late Chief Justice Holmes' classic remark, "The life of the law has not been logic. . . ."[3]

No better manifestation of this judicial pattern can be found than in the case of the law of New York which considers invalid agreements to pay interest on interest.[4] The attempts of the New York courts to exercise the judicial prerogative previously alluded to, especially with reference to interest coupons, has produced anomalies and inconsistencies which form the *raison d'etre* of this comment.

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1. Wheeler, J. in Dwy v. Connecticut Co., 89 Conn. 74, 99, 92 Atl. 883 (1915); quoted with approval in CARDOZO, NATURE OF THE JUDICIAL PROCESS (1921) 151, as expressing the ". . . tone and temper in which problems should be met."

2. While recognizing the need for judicial sensitivity to sociological and economic changes, the late Justice Cardozo issues with his usual clarity and eloquence a caveat: "The rule that functions well produces a title deed to recognition. Only in determining how it functions we must not view it too narrowly. We must not sacrifice the general to the particular. We must not throw to the winds the advantages of consistency and uniformity to do justice in the instance." CARDOZO, NATURE OF THE JUDICIAL PROCESS (1921) 103.

3. HOLMES, THE COMMON LAW (1881) 1.

4. The confusion apparent in the New York law on this subject has had its repercussions in the federal courts which have been called on to apply the New York Law. The resultant conflict bears eloquent testimony to the uncertainty in the New York Law. Compare Shoe & Foundry Co. v. Interborough Rapid Transit Co., 26 F. Supp. 954 (S. D. N. Y. 1935) with Transbel Investment Co. v. Roth, 36 F. Supp. 396 (S. D. N. Y. 1940). For a review of some of these divergent Federal cases which have considered the policy of New York with reference to the right of a creditor to collect interest on interest, see McNiece, *The Interest on Interest Rule in New York* (1946) 20 ST. JOHN'S L. REV. 71.

Rationale of the New York Law

The New York rule which invalidates agreements to pay interest on interest exists because interest on interest ". . . may serve as a temptation to negligence on the part of the creditor and a snare to the debtor, and prove in the end oppressive, and even ruinous."[5] It is upon such an apparently over-paternalistic and unrealistic rationale that the New York view is based. While this New York rule is followed in some jurisdictions,[6] there is considerable and substantial authority in other jurisdictions sustaining the validity of such agreements.[7]

It might be well to point out in this connection that the expressions "compound interest" and "interest on interest" are used interchangeably by the New York courts in their discussions of the subject.[8] Such identity is natural for the difference is merely one of quantity rather than of quality.[9] Interest on interest is the interest paid on the interest due upon the original sum. Compound interest[10] is the interest paid when the unpaid interest due is added

5. Young v. Hill, 67 N. Y. 162 (1876). It is an interesting circumstance that none of the cases recognizing this general rule were directly concerned with its application. The cases uniformly cited for the proposition that agreements to pay interest on interest are invalid, involved agreements made *after* the interest had accrued. For example, *see* Young v. Hill, *supra*; Van Benschooten v. Lawson, 6 Johns Ch. 313 N. Y. (1822). As will be shown hereafter such agreements, covering past due interest have from the earliest times been treated as an exception not covered by the general rule.

6. *See* for example Bowman v. Neeley, 137 Ill. 443, 27 N. E. 758 (1891); Gay v. Berkey, 137 Mich. 658, 100 N. W. 920 (1904); Cox v. Smith, 1 Nev. 161 (1865).

7. Greer v. Greer, 56 Ariz. 394, 108 P. (2d) 389 (1940); Honey v. Edmison, 3 Dak. 449, 22 N. W. 594 (1884); Morgan v. Mortgage Disc. Co., 100 Fla. 124, 129 So. 589 (1930); Bradley v. Merrill, 91 Me. 340, 40 Atl. 132 (1898); Hale v. Hale, 1 Coldw. 333 (Tenn. 1860); Shealy v. Cappelmann, 145 S. C. 408, 143 S. E. 178 (1928).

8. The court points this out in *In Re* Wisconsin Cent. Ry., 63 F. Supp. 151, 154 (D. Minn. 1945). However, *cf.* Young v. Hill, 67 N. Y. 162 (1876), in which the court, appearing to note a distinction, said at 174: "An agreement to pay simple interest upon the several installments of interest as they become due and a computation based upon such an agreement, . . . might not be unreasonable or inequitable." A recent federal case, relying for the most part on the aforementioned quotation from Young v. Hill, *supra,* differentiated between interest on interest and compound interest, and held that an allowance of interest on unpaid accrued interest was not contrary to New York public policy. *In Re* Realty Associates Securities Corporation, 66 F. Supp. 416 (E. D. N. Y. 1946). This decision accentuates further the sharp conflict already evident in the federal cases which have attempted to interpret the New York law on this subject. See note 4 *supra.*

9. As Judge Clancy so aptly observed in Transbel Inv. Co. v. Roth, 36 F. Supp. 396, 398 (S. D. N. Y. 1940).

10. Under the broad plenary power given to the Banking Board ". . . to prescribe from time to time: (1) the rates of interest which may be paid on deposits with any banking organization" (N. Y. BANKING LAW § 14 (h)), commercial banks, trust companies, private bankers and industrial banks have been authorized by General Regulation No. 3 of the New York State Banking Board to compound interest on deposits. It should be noted however that the agreements to pay interest by these institutions normally contain

to the principal and the resulting sum is the basis for the next computation.[11] Neither compound interest nor interest on interest can rightfully be considered usurious.[12] By definition usury is ". . . the taking of more interest for the use of money than the law allows."[13] In either the case of compound interest or interest on interest, the debtor may pay his debt when due and thus avoid the contract which obliges him to pay the additional interest so that there is in such cases no absolute contract for the payment of more than legal interest.[14]

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a provision whereby the banking organization may, upon notice change the interest rate. In this way these banking organizations protect themselves from the possible adverse effects of commitments to compound interest on deposits. It may also be apposite to note that the so-called "compound interest" paid by mutual savings banks on depositors' accounts is not really interest at all but rather is more in the nature of dividends paid to the depositors who are considered to be actually the beneficial owners of the corporate estate. *See* Huntington v. Savings Bank, 96 U. S. 388, 394 (1877); NEW YORK BANKING LAW §§ 244, 245. Thus it has been succinctly noted that "Whether the profits of a savings bank, when distributed be called 'interest' or 'dividends' is purely a question of definition. As a matter of fact, the money distributed among the depositors is the profit on their investment of their own money, and is in all material respects similar to the dividends paid to the shareholders of an ordinary corporation." 1 MORAWETZ, PRIVATE CORPORATIONS § 391 n. 2.

11. The important difference in the two forms of calculation is that in "interest on interest" the accrued interest is not combined with the principal but each installment of interest itself becomes a new principal which bears simple interest, and no interest is allowed on the interest on the interest. A simple mathematical calculation may serve to illustrate this latter point more concretely: let us assume a $1000 note payable with annual interest at 6%. At the end of 5 years, the amount due if "compound interest" were computed would be $1338.23 while if "interest on interest" were computed, it would be $1336. The following chart illustrates the progressive difference which, as is evident, becomes slightly larger as time elapses.

TOTAL AMOUNT DUE (nearest hundredth)

	COMPOUND INTEREST	INTEREST ON INTEREST
1st Yr.	$1060.00	$1060.00
2nd Yr.	1123.60	1123.60
3rd Yr.	1191.02	1190.80
4th Yr.	1262.48	1261.60
5th Yr.	1338.23	1336.00

12. At early common law usury was originally synonymous with interest. Usury denoted the money received for the use of other money and as such was universally condemned by philosophers and theologians as against the laws of God and morality and by economists on the now discredited theory that money was barren and unproductive and could not beget money. The demands of a mercantile economy however, gradually compelled the acceptance of the concept of interest as we know it today. 2 BL. COMM. 454. For an excellent historical and analytical treatment of the theological objections to the taking of interest for money lent *see* 15 CATHOLIC ENCYCLOPEDIA 237 (Usury).

13. 3 PARSONS, LAW OF CONTRACTS (9th ed. 1904) 107. For the N. Y. statutory definition of Usury see N. Y. GEN. BUSINESS LAW §§ 370, 371.

14. The essence of a usurious contract lies in the absolute reservation of interest beyond

Anomalies and Inconsistencies in the New York Law

The New York rule invalidating agreements to pay interest on interest is easy to state: ". . . a promise to pay interest upon interest is void if made at a time before simple interest has accrued."[15] However the search for concrete applications of the rule becomes involved in the quagmire of exception and qualification which a judiciary faced with the necessity of applying an outmoded and unreasonable rule has engrafted upon it. Thus from the earliest times[16] an agreement to pay interest on interest, on interest already due, as distinguished from interest to become due, was valid if supported by a sufficient consideration. In this type of transaction the promise by the debtor to pay interest on the defaulted interest is entirely dependent upon and supported by the promise on the part of the creditor to forbear and extend the time for payment.[17] It would appear that the policy which condemns agreements made before the interest is due does not fully apply to these situations where the agreement is made after the interest has fallen due. While it may be true that, in a sense, the continuation of the debt (now increased by the addition of the already due interest) serves as a temptation to the creditor to continue the debtor-creditor relationship, it cannot be said that the new arrangement constitutes a snare to the debtor for its occurrence must fully awaken him to the extent of his obligation. The possibility of interminable interest accumulations which gave rise to the general rule finds no place in this arrangement since the debt is limited to an ascertainable amount until the debtor is again awakened by a new agreement.

That the law on even this elemental exception, which permits interest on already accrued interest, is beclouded by inconsistencies can be readily ascertained by an examination of a few New York cases. Thus at a very early date in the case of *Van Benschooten v. Lawson*[18] the court made the distinction

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the legal rate, and if there is no certain agreement to pay excessive interest it is not usurious. *In re* Becktoldt's Estate, 159 Misc. 725, 289 N. Y. Supp. 838 (Surr. Ct. 1936); Hartley v. Eagle Ins. Co., 222 N. Y. 178, 118 N. E. 178 (1918); Home Insurance Co. v. Dunham, 33 Hun 415 (N. Y. 1884); Sumner v. The People, 29 N. Y. 337 (1864).

15. Newburger-Morris Co. v. Talcott, 219 N. Y. 505, 511, 115 N. E. 846 (1916). *Contra:* Hale v. Hale, 1 Coldw. 233 (Tenn. 1860), in which the court, after reviewing the conflicting decisions on the question said: "If it be assumed that it was stipulated in the original contract that the interest should be compounded, if not punctually paid, we hold that there is nothing illegal or immoral, or contrary to policy in such an agreement. The interest is both legally and equitably due at the expiration of the period limited for its payment, ..."

16. For a complete review of the current of early English decisions with especial reference to the early exceptions and limitations by which the general rule was attended *see* Conn. v. Jackson, 1 Johns Ch. 13 (N. Y. 1814).

17. Thus in Young v. Hill, 67 N. Y. 162 (1876), the court in discussing the necessity for the promise to forbear as the consideration for an expressed or implied promise to pay compound interest stated at 105: "It is the agreement to forbear for a time in the future that gives vitality to the promise."

18. 6 Johns Ch. 313 (N. Y. 1822).

between a retrospective agreement and one prospective in holding that an agreement to allow interest retroactively for the year preceding on the interest which was due for that year could not be permitted since the retrospective effect of such an agreement ". . . leads to oppression."[19] Inferentially the court indicated that an agreement prospective in its operation, as that the interest due and payable shall carry interest *thereafter,* would be valid.

This dichotomy is achieved without any reference to the necessity of a sufficient consideration and is based solely on the public policy which is thought to be involved.[20] In fact much of the confusion in the application of the rule that agreements to pay interest on interest then due are valid results from a failure on the part of the courts to apprehend correctly the part which consideration plays. This becomes clear when we consider what the courts have said in this regard. In the case of *Mowry v. Bishop*[21] the court stated: "I conclude therefore that the moral obligation of the debtor to make the usual remuneration for the loss of interest which the creditor sustains by the non-fulfillment of his contract in such a case, is a sufficient consideration to support a subsequent agreement in writing to pay the interest on such arrears of interest. . . ." Similarly, in the case of *Guernsey v. Rexford,*[22] although an agreement to pay compound interest so far as it stipulated to pay interest from the date of the agreement on the amount of interest then due and unpaid was declared valid, the reported facts disclose no sufficient consideration therefor. Although the requirement that agreements to pay interest on interest already due must be supported by a sufficient consideration is no doubt the law,[23] these cases are illustrative of the precarious footing on which such a clear-cut exception to the general rule stands.

The case of *Quakenbush v. Leonard*[24] presents another exception which

19. *Id.* at 315.

20. While this case (*Van Benschooten v. Lawson*) has been criticized it never has been expressly abandoned. Thus in Stewart v. Petree, 55 N. Y. 621, 623 (1874), in sustaining a note given for interest upon the arrears of interest, the court said: "Chancellor Kent seems to have doubted the correctness of the last proposition [validity of agreement to pay interest on arrears of interest] and to have decided adversely to it in *Van Benschooten v. Lawson* . . . , but the doctrine is too well settled by authority to be questioned in this state; and a note given on settlement of an account, or a statement of interest past due on an obligation, in any form, for compound interest is not usurious." However, in the case of Young v. Hill, 67 N. Y. 162 (1876), the decision in the *Van Benschooten* case was reaffirmed and the court stated that *Stewart v. Petree* was decided only on the question of usury (which was held not to exist) and in no way impaired the authority of the *Van Benschooten* case. See note 23 *infra.*

21. 5 Paige 98, 103 (N. Y. 1835).

22. 63 N. Y. 631 (1875).

23. Newburger-Morris Co. v. Talcott, 219 N. Y. 505, 114 N. E. 846 (1916). Thus, although *Young v. Hill* affirmed *Van Benschooten v. Lawson* as noted in note 20 *supra,* it was only to ". . . the extent that an agreement not made upon some new and sufficient consideration for the payment of interest upon interest for a time already past, will not be sustained or enforced in equity."

24. 9 Paige 334 (N. Y. 1841).

raises provocative possibilities. The court decided that the principle of not giving effect to a stipulation for compounding future interest did not apply to a contract where the person who advanced the money to purchase land for the mutual benefit of himself and others provided for a refund with compound interest out of the proceeds of the property. The court differentiated this case on the ground that the creditor had no right to demand payment of either principal or interest until the land was sold and that the rationale underlying the general rule (i.e. the prevention of an accumulation of compound interest in favor of a negligent creditor) did not apply. While at first blush such judicial construction might seem plausible, a moment's consideration will reveal its possible deleterious consequences. There is no doubt that the judicial function in its highest form often calls for a search of the reasons underlying rules of law so that such rules will not be applied indiscriminately. However, certainty in the law and its stability require caution before there is a refusal to apply a settled rule of law (especially a rule of law pertaining to property) to the facts of a particular case. There is no objection to qualifying the application of the rule—in fact the proper use of the judicial process requires it—where the very nature of the transaction clearly shows that the reasons, which gave rise to the rule, do not apply.[25] However, only confusion and instability can result where the rule as then established is abandoned on the slightest pretext. If it is merely speculative whether or not, in the circumstances of the particular case, the agreement to pay interest on future interest will render the creditor forgetful or negligent to the detriment of the unwary debtor, it would be better to apply the rule until the highest court in the exercise of its peculiar prerogative has seen fit to discard it entirely.[26]

Interest Coupons

While coupons representing accrued interest could appropriately be considered under the preceding subdivision, their importance and the body of law which has developed concerning them make advisable their separate study. Interest coupons are severable instruments attached to the usual corporate

25. See notes 15 and 16 *supra*, and accompanying text.

26. It is of interest to note that in the recent case of *In Re* Wisconsin Cent. Ry., 63 F. Supp. 151 (D. Minn. 1945), the creditors proceeded on the ground that the rule invalidating agreements to pay interest on interest was not applicable to the facts in the instant case because the debtor-railroad company was able to conduct its affairs without the aid or benefit of the rule. Since the agreement was made in New York and was to be performed there, the court applied the New York law and properly rejected this contention stating (at 155): "However, if this argument is sound, such an exception could be applied to other corporations, large or small or even to individuals. The difference between application and non-application of the rule would rest on a tenuous foundation, in fact, the problem would really resolve itself into a determination of the Debtor's ability as a business man, rather than the determination of the ultimate facts of the case." One may speculate that in this case the creditor, in advancing the contention, sought some support from the generally recognized rule that usury is not a defense to a corporation (e.g. N. Y. GENERAL BUSINESS LAW § 374). However, the rule invalidating agreements to pay interest on interest does not involve any question of usury.

bond and represent the interest then due and payable. Each coupon is, in and of itself, an independent instrument containing an independent and distinct promise to pay the sum due and is fully negotiable.[27] Interest coupons, therefor, have a dual nature: in substance they are interest; in form they are when severed from the bond, negotiable instruments.[28] The difficulty encountered by the New York Courts in harmonizing the legal consequences of the rule under discussion as applied to such a hybrid creation is easily understandable.

From the beginning the incongruity of applying the general rule rendering void agreements to pay interest on interest to corporate and municipal financing arrangements has been apparent.[29] Thus the court in *Connecticut Mutual Life Insurance Co. v. Cleveland etc. R.R. Company*,[30] denying the applicability to corporate organizations of the principle that agreements to pay interest on interest are void, allowed interest on the unpaid interest coupons which were attached to certain railroad bonds. However, such forthright abandonment of a settled principle of law found little favor and, although never expressly overruled, the case has been allowed to fade into oblivion.[31] Exception, rather than complete rejection, has been the way the courts have handled the problem. Thus the court in one of the landmark cases on this phase of the law said:

27. OGDEN, LAW OF NEGOTIABLE INSTRUMENTS (2d ed. 1922) 262.

28. While not strictly within the confines of our present discussion, there are many incidental problems concerning interest coupons that commend themselves to study. Thus, for example, the question has arisen, which party, as between a person who issued the coupons and holder of such coupons who has failed to present them for payment after they became due, shall bear the loss resulting from the failure of a bank in which the funds have been deposited for the payment of the coupons? The holder of a check must present it for payment within a reasonable time after its issue or else the drawer will be discharged from liability to the extent of the loss caused by the delay in the event of the drawee bank's insolvency. Sanders v. Lifsey, 41 Ga. App. 395, 153 S. E. 104 (1930); Sinclair Ref. Co. v. Keith, 97 Okla. 55, 221 Pac. 1003 (1923). On the other hand, the rule as to promissory notes in a similar case would be different, and the loss resulting from the failure of the bank at which the instrument was payable would not fall upon the holder of the instrument. Chapman v. Wagner, 1 Neb. 492, 96 N. W. 412 (1901). The courts have by analogy applied the rules governing negotiable promissory notes, rather than those governing checks, to cases involving interest coupons and have thus held that the loss resulting from the failure of the bank at which the interest coupons were made payable, and in which the issuer of the coupons has deposited money for their payment, does not fall upon the holder of the coupons who has failed to present them for payment after they became due. John K. & Catharine S. Mullen Benev. Corp. v. School Dist., 99 Mont. 388, 43 P. (2d) 902 (1935); Williamsport Gas Co. v. Pinkerton, 95 Pa. 62 (1880); Lusk State Bank v. Lusk, 48 Wyo. 547, 52 P. (2d) 413 (1935).

29. See note 26 *supra*.

30. 41 Barb. 9 (N. Y. 1863).

31. It has only been cited some six times, the last time having been in the case of Beattys v. Town of Solon, 64 Hun 127 (N. Y. 1892), in which it was heavily relied upon to support an award of interest on interest. However, on appeal this case was subsequently modified in a memorandum opinion to exclude this award of compound interest. Beattys v. Town of Solon, 136 N. Y. 662, 32 N. E. 1062 (1893).

"Interest, as a rule, follows the principal without becoming principal, and cannot be compounded by force merely of the contract; but that general rule has been modified somewhat by an exception growing out of the character and purposes of interest coupons. They may become separate and independent instruments. When they do, the exception is for the first time needed and for the first time applies."[32] So that while the general rule invalidating agreements to pay interest on interest was considered applicable to interest coupons, it was only when they were in the hands of the holder of the bonds.[33] While a strong objection might be urged against the equity of denying a bondholder the same rights as a mere assignee of the coupon, the logic might be conceded if the rupture were complete. But such is not the case. Thus while an interest coupon in the hands of an assignee is a separate and independent instrument so as to permit the accrual of interest thereon, the assignee of the coupon is entitled to maintain an action in foreclosure to compel a sale of the mortgaged premises, so far as might be necessary to pay the interest represented by unpaid coupons.[34] This ambulatory feature of the interest coupons defies any attempt to draw a line demarcating the respects a coupon is to be deemed an incident of the bond and the respects in which it is to be deemed a separate instrument.[35] In *Clakey v. Evansville*[36] a majority of the court held that where by an endorsement upon a coupon bond a corporation guaranteed ". . . to the holder of the within bond the punctual payment of principal and interest . . . as then shall become due and payable," the guaranty did not enure to the benefit of a holder of a detached coupon, since the coupon was then a separate and independent instrument. The strong dissent in this case,

32. Williamsburg Savings Bank v. Town of Solon, 136 N. Y. 465, 481, 32 N. E. 1058 (1893), in which the court held that interest could not be collected on past due interest coupons since the coupons were in the hands of the original owners. Inferentially, therefore, the court indicated that had they been detached and owned by an assignee interest would have been allowed. Inasmuch as there was no covenant to pay interest on interest in the trust indenture securing the bonds, or on the face of either the bonds or the coupons, it appears that not only does New York allow agreements to pay interest on interest coupons which have been detached and are in the hands of an assignee but it goes to the extent of implying such an agreement where there is no provision therefor. *In Re* American Fuel and Power Co. *et al.*, 151 F. (2d) 470, 478 (C. C. A. 6th 1945). For a cogent discussion of interest as damages for the non-payment of interest see 1 SEDGWICK, DAMAGES (9th ed. 1920) § 345 *et seq.* *See also* for a tersely written defense of the right to interest as damages for the non-payment of interest due by contract, (1922) 8 VA. L. REV. 388.

33. Bailey v. Buchanan, 115 N. Y. 297, 22 N. E. 155 (1889).

34. Long Island Loan & Trust Co. v. Long Island City, 85 App. Div. 36, 82 N. Y. Supp. 644 (2d Dept. 1903), *aff'd*, 178 N. Y. 588, 70 N. E. 1002 (1904).

35. It would appear that although the coupons have not been detached, the statute of limitations runs upon them separately at the date of the maturity of the coupons. 6 WILLISTON, CONTRACTS (rev. ed. 1938) § 2024. For a rather concise treatment of this problem see (1929) 38 YALE L. J. 823.

36. 16 App. Div. 304, 44 N. Y. Supp. 631 (1st Dept. 1897).

concurred in by at least one text-book writer,[37] accentuates further the unsatisfactory state of the law with regard to this question. There is no doubt that, while a detached coupon becomes a separate and independent instrument, a nexus to the original bond remains. How strong a nexus? When does it control? The unsettled state of the law makes any answers to these problems at best highly speculative. Thus we might ask: if the coupon is separated from the bond and negotiated and then finally re-negotiated back to the original bond owner, would such coupon draw interest? While it might well appear that the coupon's subsequent negotiations had reinforced its independent character as a separate and distinct instrument and thus entitled its owner, whoever he might be, to interest thereon, such does not appear to be the case. In *Klein v. East River Electric Light Co.*[38] it was held that where the plaintiff, who was the holder of interest coupons of certain bonds, did not show whether or not he was the owner of the bonds to which the coupons were originally attached, nor the time when they were detached, nor whether he became owner before or after detachment, he could not recover interest, since so long as the coupons are held by the owner of the bond interest follows principal and cannot be compounded. A literal reading of this decision would also indicate that a condition precedent to even a stranger obtaining the right to interest on an interest coupon would be the detachment of the coupon from the bond prior to his ownership of it. While this latter conclusion might appear to be tenuous and strained, in the light of the previous decisions, it would be foolhardy emphatically to reject it.

The history of a recent New York case may shed some light on the present attitude of the New York courts towards this outmoded doctrine. In *In Re Schuster's Will,*[39] the decedent's will had given a life estate to his widow. In a prior decision construing this will the Surrogate's Court had held that a power of sale contained in the will was imperative and had resulted in a conversion of the realty into personalty as of the date of his death. It had, therefore, been held that the real property should have been sold by the executrices one year after the date of the issuance of letters testamentary and thus they were surcharged four per cent interest on the value of the realty from the date of the testator's death to the date of the widow's death.[40] The question in this case was whether the Surrogate should allow interest on such surcharge. The Surrogate denied the request for interest on the express ground that ". . . it is well settled in this state that in the absence of an express contract or statutory authority, compound interest is not allowed."[41] Upon appeal, the Appellate Division modified the decree of the Surrogate without

37. 2 MACHEN, MODERN LAW OF CORPORATIONS (1908) § 1776, in which the author commenting on this decision said: "It is submitted, however, that this conclusion is very narrow and defeats the real intention of the parties, and that the opinion of the dissenting judge contains the preferable reasoning."

38. 33 Misc. 596, 67 N. Y. Supp. 922 (App. Term 1901).

39. 167 Misc. 194, 3 N. Y. S. (2d) 702 (Surr. Ct. 1938).

40. *In Re* Schuster's Will, 150 Misc. 444, 269 N. Y. Supp. 546 (Surr. Ct. 1934).

41. 167 Misc. at 195, 3 N. Y. S. (2d) at 704.

even considering the general rule invalidating compound interest which was alluded to and relied on in the Surrogate's court. The Appellate Division appeared to place its decision on the broad generalization that ". . . more and more courts are coming to the view, that in actions on implied contract to recover for services or property, interest is a concomitant, very nearly automatic. . . . Interest is now held to be an incident to just compensation. . . ."[42] This decision was affirmed in a memorandum opinion by the New York Court of Appeals.[43]

Conclusion

It is hoped that the last cited decision is indicative of a realization on the part of the New York courts that the rule invalidating agreements to pay interest on interest is archaic and not compatible with the needs of an industrialized and commercialized society in which creditors and debtors either are, or should be, wide-awake to their obligations. Possibly the New York Court of Appeals may in the future, making use of its judicial prerogative, discard the old rule, which has been found to have served "another generation badly." Such action could not justifiably be condemned as judicial legislation when we consider the unplausible and weak foundation upon which the existing rule is based. In that event—the Court might well reaffirm, and quote with approval, the language employed by another Court when called on to determine as a case of first impression this precise question: ". . . we think the rule allowing interest, is upon the whole, better grounded in the principles and analogies of the law and more consonant with the modern ideas in regard to interest as exhibited both in jurisprudence and legislation."[44]

42. 257 App. Div. 55, 57, 12 N. Y. S. (2d) 20, 22 (2d Dept. 1939).
43. 284 N. Y. 569, 29 N. E. (2d) 392 (1940).
44. Wheaton v. Pike, 9 R. I. 132 (1868).