Opinion No. 62-125

October 8, 1962

BY: OPINION OF EARL E. HARTLEY, Attorney General Norman S Thayer, Assistant Attorney General

TO: Mr. R. F. Apodaca, Superintendent of Insurance, State Corporation Commission, Santa Fe, New Mexico

QUESTION

QUESTION

1. Can a foreign insurance company declare as an admitted asset its loan secured by a first mortgage on a leasehold and valuable improvements?

CONCLUSION

1. No.

OPINION

ANALYSIS

We are informed that a Texas insurance company contemplates making a loan of its funds to an investment company to enable the investment company to build a building that will be leased as a retail grocery store. The building will be located on land that is under long term lease to the investment company. The insurance company will take as security for the loan a first mortgage on the leasehold estate and on the improvements. The lease provides, and the mortgage will provide, that, in the event of default by the lessee, any mortgages or holder of a security interest may cure the default and continue the lease in full force and effect. By the terms of the lease, all improvements placed on the leased premises remain in the property of the lessee and may be removed upon expiration of the term of the lease.

By the terms of Section 58-5-19.1, N.M.S.A., 1953 Compilation, domestic insurers are permitted to declare as admitted assets the investments, securities, properties, and loans acquired or held in accordance with Section 58-4-7, N.M.S.A., 1953 Compilation. Foreign insurers may declare as admitted assets those investments permitted by the laws of their domiciles, if of a quality substantially as high as the investments permitted to domestic insurers.

We make no attempt to determine whether the contemplated loan is permitted an insurance by the laws of the State of Texas. We assume that to be true. The only

question is whether the contemplated loan is an investment of a quality substantially as high as investments permitted to domestic insurers.

The investments permitted to domestic insurers are listed in Section 58 - 4 - 7, N.M.S.A., 1953 Compilation, which we set out in full:

"Investments. -- It shall be lawful for any domestic insurance company licensed to transact an insurance business in the state of New Mexico to invest any of the funds accumulated in its business, including its capital, in:

(a) Real estate only when acquired for the purpose and in the manner following:

(1) The building in which it has its principal office and the land on which it stands; provided, however, that the investments under this paragraph (1) shall not at any time exceed the aggregate of 25% of the admitted assets of such company.

(2) Such as shall be requisite for branch office or other business facilities necessary for its convenient accommodation in the transaction of its business; provided, however, that investments under this paragraph (2) shall not at any time exceed the aggregate of 5% of the admitted assets of such company.

(3) Such as shall have been acquired for the accommodation of its business; provided, however, that investments under this paragraph (3) shall not at any time exceed the aggregate of 25% of the admitted assets of such company.

(4) Such as shall have been mortgaged to it in good faith by way of security for loans previously contracted or for money due.

(5) Such as shall have been conveyed to it in satisfaction of debts previously contracted in the course of its dealings; provided, however, that investments under this paragraph (5) shall not be held by the company in excess of five (5) years from the date of acquisition.

(6) Such as it shall have purchased at sales on judgments, decrees, or mortgages obtained or made for such debts; provided, however, that investments under this paragraph (6) shall not be held by the company for more than five (5) years from the date of its acquisition.

(7) Such real estate, or any interest therein, as may be held or acquired by purchase, lease or otherwise, as an investment for the production of income and any such real estate or interest therein, may thereafter be held, improved, developed, maintained, managed, leased, sold or conveyed. Such company may elect to hold under the provisions of this Item (7) real estate duly acquired or held by it under other provisions of law; Provided, however, that investments under this paragraph (7) made by any domestic insurance company shall not at any time exceed the aggregate 10% of the admitted assets of such company.

(b) In bonds and obligations of the government of the United States or Canada.

(c) In the bonds or obligations of state, county, or other political subdivisions of the United States, or in obligations which are instrumentalities of the United States.

(d) In the bonds or debentures or secured obligations of any solvent corporation which has not defaulted in the payment of the interest or principal of any of its obligations for ten (10) years previous; provided, however, that investments under this paragraph (d) made on bonds or debentures or secured obligations of wholly owned subsidiaries may be made if such subsidiary is not in default in the payment of interest or principal of any of its obligations and is a fully operating corporation at the time the investment is made.

(e) In first mortgage or first lien loans on improved real estate, such loans not to exceed sixty-five per cent (65%) of the appraised market value of such property, and the improvements on which are continuously insured against the Hazards of fire and extended coverage for not less than seventy-five per cent (75%) of the appraised value of such improvements.

(f) In deposits in solvent state and national banks and trust companies.

(g) In loans secured by deposits of collateral of any of the above classes of investments, provided that the current market value of the said collateral is not less than twenty (20) per cent in excess of the amount of the loan.

(h) In loans on its own policies, in each case for amounts not to exceed the outstanding net terminal reserve carried as a liability in its valuation.

(1) In such loans secured by real property or leasehold, as the federal housing administrator insures or makes a commitment to insure.

(j) In notes or bonds secured by mortgage insured, and debentures issued, by the federal housing administrator, and obligations of national mortgage associations.

(k) In preferred and common stocks of solvent corporations and also in securities of any open-end or closed-end management type investment company or investment trust registered under the Federal Investment Company Act of 1940, as from time to time amended, but not to exceed ten (10) per cent of the admitted assets shall be so invested by any life insurance company. Any such investment shall be made only from an approved list of such stocks and securities prepared by the superintendent of insurance and any investment made under this subparagraph (k) shall be subject, as to each insurance company, to the approval of the superintendent of insurance.

(1) Deposits or equities recoverable from underwriting association, syndicates and reinsurance funds, or from any suspended banking institutions, to the extent deemed by the superintendent available for the payment of losses and claims and at values to be determined by him.

(m) Other assets, not inconsistent with the foregoing provisions, deemed by the superintendent available for the payment of losses and claims, at values to be determined by him.

Clearly, subsection (a) deals with investments in real estate needed for the operation of business or held for the production of income, and does not deal with the making of loans for the production of income. Loans are dealt with under other subsections.

True, under subsection (a) (7) an insurer may itself take a lease on real estate, and manage, develop, maintain, and improve the leasehold. But here the insurer wants to take a mortgage on a lease. The lease itself must be in default before the insurer can step in and operate it. But our ruling is on the basis that subsection (a) does not authorize loans of money for the production of income. Subsection (a) (4) supports this view by authorizing the taking of a mortgage on real estate as security for a loan **previously contracted,** thereby impliedly excluding the taking of a mortgage for a contemporaneous loan.

Subsections (b), (c), (d), (j), and (k) are not applicable, since they deal with securities such as stocks, bonds, and debentures. Subsections (f) and (1) deal with deposits. Subsection (g) does not become operative unless it is shown that the investment deposited as collateral is itself a permissible investment. Subsection (m) adds no different category of investment, and subsection (h) deals with loans on the insurer's own policies.

Subsection (1) permits loans secured by real property or leasehold, but only if insured by the federal housing administrator, thereby impliedly excluding loans on leaseholds not so insured.

This leaves subsection (e), mortgages and first lien loans on improved real estate.

The New Mexico cases hold that a leasehold estate is governed by the laws relating to personal property. See **Ellison v. Ellison,** 48 N.M. 80, 146 P. 2d. 173, **State ex rel. Truitt v. District Court,** 44 N.M. 16, 96 P. 2d. 710; and **American Mortgage Co. v. White,** 34 N.M. 602, 287 Pac. 702. Moreover, the leasehold is not "improved" real estate, if it is real estate at all. The improvements in question are removable, and cannot be deemed attached to the real estate. If they were so attached, they would become the property of the owner of the fee, the lessor, and the mortgage in question does not include the fee. That the improvements in question do not in any sense become attached to the leasehold estate is established by the case of **Jones-Noland Drilling Co. v. Bixby,** 34 N.M. 413, 282 Pac. 382. Hence, the mortgage in question is not a mortgage or first lien loan on improved real estate.

There is more here than simply a question of the quality of the investment. In many instances a mortgage on a lease might be an investment of as high a quality as the lease itself. But here we have a difference in kind, not merely degree. This is a type of investment not permitted to domestic insurers, insofar as the admitted asset laws are

concerned. Approval of this investment would amount to a discrimination against domestic insurers.

It is our conclusion that a loan secured by a mortgage on a leasehold estate (other than those insured by the federal housing administrator) cannot be declared an admitted asset of an insurance company.