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RIGHTS OF VENDEES UNDER EXECUTORY CONTRACTS OF SALE

IT has been held by the Supreme Court of the State of Washington in a number of cases, that an executory contract to sell either real or personal property, generally designated as a conditional sales or installment contract, does not create in the vendee or buyer any legal or equitable interest in the property In so far as the rule applies to real property, there was a disposition on the part of many members of the bar to adversely criticise those decisions and to become fearful of their effect upon the status of the vendee's rights, after the court decided the case of *Ashford v. Reese*,[1] in which the rule was given as the basis for holding that the vendee is entitled to rescind the contract, upon destruction of the subject-matter while the contract is unperformed, in other words, that loss caused by destruction of the property without fault of the vendee falls upon the vendor.

The vendee having no interest in the *res*, it was feared that a conveyance or encumbrance of the property by the vendor would be held superior under all circumstances to the rights of the vendee, leaving the vendee with only a right of action for damages against his vendor, and, if not superior where the grant or encumbrance is taken with notice, that placing the contract of record or possession of the property would not constitute constructive notice of the vendee's rights.

This paper is written in support of the rule and to demonstrate that there is no reasonable basis for fear as to the effect of its application upon the vendee's rights, not in support of the use of the rule as a premise for holding that loss resulting from destruction of the property must be borne by the vendor.

The first principle of argument requires that terms be defined.

[1] 132 Wash. 649, 233 Pac. 29 (1925).

The word "interest" is an indefinite term which is given various meanings. It is frequently used in referring to pure contractual rights pertaining to property, that is, where the contract creates no ownership or title in the property It is also used, and in a more accurate sense, as expressing the idea of ownership or title. The expression, "equitable interest," is also used in different senses. It is necessary to arrive at the meaning given to the latter expression by our court when it formulated the rule under discussion, in order to intelligently discuss the subject for consideration.

Ownership or title is created only by a present transfer or conveyance. When, according to legal formalities, it creates a "legal" interest. When a contract for ownership or title has been performed by the vendee and he has become entitled to a present transfer or conveyance,[2] or when there has been an attempted transfer or conveyance which has failed by reason of failure to observe the legal formalities,[3] a court of equity deems that to have been done which should have been performed, and gives effect to it as a present transfer or conveyance, which vests the vendee with what is termed an "equitable" interest. It is clear from our decisions that the terms used in the rule were intended to express this meaning of legal and equitable interest.[4]

The court used the terms in accordance with correct legal terminology The court cannot be said to have conveyed the idea that contractual rights pertaining to property have no effect of limiting the acquisition of adverse rights. It would be contrary to fundamental legal principles for a court to hold that such contracts have no effect upon the right of the owner of the property, or his successor in interest, to deal with or dispose of that property as he sees fit. If there were nothing more than the statement of the rule itself by which to gauge the court's meaning, it could not be assumed that the court intended thereby to hold that such contracts are a nullity in so far as is concerned the right of the vendee to receive title, when he has performed his contract, from the other party to the contract or one who acquires his interest with notice of it.

The rule itself, when its terms are given a proper meaning, is sound. It is elementary that the court, when interpreting a contract, should give effect to the intention of the parties to it as

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[2] *Ahern v. Ahern*, 31 Wash. 337, 71 Pac. 1023 (1903).
[3] *Pease v. Baxter* 12 Wash. 573, 41 Pac. 899 (1895).
[4] *Younkman v. Hillman*, 53 Wash. 663, 102 Pac. 773 (1909).

disclosed by the language they employed, that intention is always the controlling factor.[5] There is a marked difference between a promise to sell and a present transfer or conveyance of an interest in property.[6] In the one case, a transfer or conveyance is merely contemplated, in the other it is completed. To hold that an interest in the *res* passes in the former case, would be making a contract for the parties instead of interpreting the one made by them. The Washington rule but gives effect to the expressed intention of the parties. The words "will sell" or "agrees to sell," especially when there is also a provision that the title shall remain in the vendor until performance by the vendee, clearly express the intention of the parties, and the purpose of the rule is to give effect to that intention.

It may be that under the common law an executory contract to sell real property was treated in equity "as if already specifically executed," and the "purchaser" held to be the "equitable owner of the lands, and the vendor of the purchase money," as indicated by quotations found in Judge Tolman's dissenting opinion in *Ashford v. Reese, supra.* If so, our court is to be congratulated on its departure from that rule, founded on a fiction, and on its adoption of a rule giving effect to the expressed intention of the parties.

The rule has been logically applied, according to the meaning of its terms and its purpose, in holding that the wife is not a necessary party to a declaration of forfeiture, a relinquishment or an assignment of the rights of the marital community arising out of such contracts, prior to performance by the vendee, for the reason that the husband is the statutory agent of the community with authority to dispose of choses in action and all kinds of personal property;[7] in holding that such contracts are valid when signed by the parties to be charged, though not executed with the formalities required for the execution of deeds;[8] and in holding that the heirs of the wife have no interest in the realty itself but do have an interest in the contract, the chose in action, in proportion to the share of the payments made with community funds.[9]

Any rule which gives effect to the intention of the parties to a

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[5] *Yakima Sash & Box Co. v. Kopp*, 140 Wash. 422, 249 Pac. 786 (1926).

[6] Ayer, *"Uniform Sales Act,"* 2 WASH. L. REV. 67.

[7] *Tieton Hotel Co. v. Manheim*, 75 Wash. 641, 135 Pac. 658 (1913) *Converse v. LaBarge*, 92 Wash. 282, 158 Pac. 958 (1916) *Pain v. Morrison*, 125 Wash. 267, 216 Pac. 29 (1923).

[8] *First National Bank of Kennewick v. Conway*, 87 Wash. 506, 151 Pac. 1129 (1915).

[9] *In re Kuhn's Estate*, 132 Wash. 678, 233 Pac. 293 (1925).

contract is intrinsically sound and can work no hardship on the parties. However, a formula which serves to give effect to the intention of the parties when applied to facts out of which it grew, may be so applied that it has a directly opposite result. Courts do not always look to the reason of a rule before applying it and, consequently, rules sometimes receive condemnation which should be directed to a particular application of it. That is what has happened to the one under consideration.

In the dissenting opinions to *Ashford v. Reese, supra,* and *Holt Manufacturing Company v. Jaussaud,*[10] the general rule that no legal or equitable interest in real or personal property passes to the vendee while such a contract remains executory is adversely criticised. But the dissents on that ground should be regarded as protests against misapplications of the rule rather than well considered disapprovals of the rule itself.

In the *Holt Manufacturing Company* case, involving personalty, it is also held that the risk of loss while the contract remains executory falls on the seller. Not only is it held in those cases that the vendors or sellers are entitled to no further payments under the contracts, but that payments made by the vendee or buyer may be recovered by him. Whether or not the vendor would be entitled to the reasonable value of the use of the property as an offset was not considered.

While our court's holding in the two last mentioned cases, that the vendor or seller bears the loss resulting from destruction of the property prior to performance, has the approval of an eminent jurist,[11] it would seem that a different position might well have been taken.

There are at least two kinds of executory contracts to sell property, one in which there is a delivery of the property to the vendee and another in which there has been no delivery of the property at the time of loss or destruction. By the latter, the vendor is under obligation to deliver the property Where the property is lost or destroyed while in the possession of the vendor, he fails to perform his contractual obligation to deliver. But where it is lost or destroyed after being delivered to the vendee, the vendor has performed that important obligation under the contract and there is no failure on his part to perform—of course, he is able and

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[10] 132 Wash. 667, 233 Pac. 35 (1925).

[11] Mr. Justice Harlan F Stone's "*Equitable Conversion by Contract,*" 13 COL. L. REV. 369.

willing to execute the instruments required of him by the contract, upon the performance of the vendee's promise to make the payments specified in the contract. Performance or non-performance by the vendor ought to be the factor of controlling importance in such cases, in whom the title lies is a matter of total indifference. In neither the *Ashford* nor the *Holt Manufacturing Company* case did the vendor fail in the performance of his obligations. Furthermore, where there has been a delivery, the intention of the parties that the loss shall fall on the vendee is clear. The intention is just the opposite where there has been no delivery, in the absence of express language to the contrary Hence, decisions in those cases in accordance with Judge Bridges' and Judge Parker's dissenting opinions, would have had a sounder foundation upon which to rest.

The Uniform Sales Act of 1925,[12] so far as personalty is concerned, makes the loss fall upon the one who should bear it, the buyer. However, the question of upon whom the loss resulting from destruction should fall is beside the question.

Judge Tolman, in dissenting, made argumentative assertions which gave rise to the doubts following those decisions. In his effort to give reasons for an apparently strong feeling that an injustice was being done the vendor and seller in those cases, he expressed fears concerning the consequences of the rule that a vendee or buyer under such a contract has no legal or equitable interest in the *res,* which should not have been expected to become realities, and which, in part at least, have been proven groundless by subsequent decisions.

He states, as a part of his argument against the rule itself.

> "The recording of his contract will avail him nothing because, having no interest in the real estate, the contract evidences no interest and is not entitled to be recorded, and consequently cannot be constructive notice to anybody"

But the contrary has long been the law, and is a settled rule of property in Washington.

In *Bernard v. Benson,*[13] it is squarely held that the recording of such a contract imparts constructive notice. It is true the court gave as one reason for its decision that the contract came within

[12] Rem. Comp. Stat. §5836-22; P. C. §6227-22.
[13] 58 Wash. 191, 108 Pac. 439 (1910).

the meaning of the words, "deeds, grants and transfers of real property," contained in the recording statute, but gave as the principal reason for the decision that it was the settled custom to consider the recording of such contracts as notice and that the custom had become a rule of property, as any other holding "would be productive of great mischief." The decision has stood as the law for a long time, and it is outside of the realm of possibility that the court would now overrule that decision and destroy rights acquired on the faith of it. That construction of the recording statute is now as much a part of it as if such contracts were expressly mentioned therein.[13a]

Judge Tolman, no doubt, did not have in mind *Bernard v. Benson* when that statement was made, and having in mind *Schaefer v. Gregory*,[14] which is cited in support of the majority opinion in *Ashford v. Reese* and in which the opinion was written by the same judge, there is some excuse for his conclusion. In the *Schaefer* case, it was held that a vendee of such a contract who was made a party to eminent domain proceedings affecting the realty but did not appear therein, was unaffected by the proceedings, notwithstanding the eminent domain statute provided for making parties to the proceedings and determining their damages "all tenants, encumbrancers, and others interested for the taking or injuriously affecting such land." The reason given by the court for so holding was that "the vendee has no interest in the land, that he has no right *in rem*, but one *in personam* against the vendor in the event of breach upon the vendor's part."

The court, in deciding the *Schaefer* case, entirely overlooked the reason for the rule. The opinion was apparently written without thought of the fact that the intention of the parties as disclosed by the language used is of primary importance and that the rule is merely a formula which gives effect to the intention as expressed in executory contracts to sell. Had the court looked to the four corners of the statute for the intention of the legislature, instead of gauging it by a formula, a different result would probably have been reached.

It is unbelievable that *Bernard v. Benson* will be affected by the

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[13a] Since this article was written the legislature has set all doubts on this point at rest. See Rem. Comp. Stat. §10596-3; P C. §1914-3, providing that executory contracts for the sale of real property, when acknowledged, may be recorded, and that such recording imparts constructive notice of the vendee's rights under the contract.

[14] 112 Wash. 408, 192 Pac. 968 (1920)

Schaefer decision. The latter can be considered only as a construction of the eminent domain statute, just as the former is limited in its effects to the general recording statute. However, the *Schaefer* case should be overruled or the eminent domain statute amended to remedy the situation created by that case.

Specific statutory provision is made for giving record notice of executory contracts relating to personalty [15]

Recording or filing, therefore, gives constructive notice of executory contracts of both realty and personalty It cannot be said that statutory notice is without effect, upon the theory that since the vendee or buyer has no equitable or legal interest in the *res* a purchaser or encumbrancer may treat the contract as a nullity so far as he is concerned. The only purpose of providing for notice by recording or filing is to make his rights in the property subject to the contractual rights of the vendee or buyer. Contractual rights pertaining to property, as distinguished from equitable or legal interests in the property itself, are by that legislation and always have been recognized as subjects of legal protection.

Possession by the vendee or buyer also constitutes notice. It is a familiar rule that possession is notice to all the world of the rights of the possessor. That rule has never been limited to the protection of ownership or title. Any contractual rights which the party in possession may have pertaining to the property, regardless of whether or not such rights have ripened into title or ownership of the whole or any part of the property, are protected by such notice, and the successors in interest of the title holder or owner take subject to the contractual rights of the possessor.[16]

A judgment creditor or a purchaser on execution at his own sale stands in the position of the debtor, and lack of notice adds nothing to his rights.[17] The judgment or a levy of execution does not constitute a lien as against the vendee or buyer.[18] (The judgment creditor is not without a remedy He may sell the vendor's or seller's interest in the property under execution and notify the

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[15] Rem. Comp. Stat. §§ 3790-3791, P. C. §§ 9767-9768.

[16] *Noyes v. Hall*, 97 U. S. 34, 24 L. ed. 909, cited with approval in *Dennis v. Northern Pacific Ry Co.*, 20 Wash. 330, 55 Pac. 210 (1898) *Field v. Copping, Agnew & Scales*, 65 Wash. 359, 118 Pac. 329 (1911), an oral lease case—such a lease creates no interest in the *res*. 24 Cyc. 958; 39 Cyc. 1646-1651.

[17] *White v. McSorley*, 47 Wash. 21, 91 Pac 243 (1907) *Ransom v. Wickstrom & Co.*, 84 Wash. 423, 146 Pac. 1041 (1915).

[18] *McDonald v. Curtis*, 119 Wash. 384, 205 Pac. 1041 (1922), 23 Cyc. 1382; 39 Cyc. 1657-1659.

vendee that he has acquired the same,[19] or he may cause garnishment to issue, and thus realize on his judgment. Unless he does so, when the contract is paid out, the interest of the vendor or seller terminates and the lien ceases to have anything on which to operate.)

In *Cunningham v. Long*,[20] a successor in interest of a vendor of personalty was held in no better position than his vendor, and as the vendor had given an extension of time for payments no forfeiture could be had without giving the vendee an opportunity to pay

Possession is not the equivalent of ownership of or title to property, but one in possession under such a contract, like any other bailee, may maintain an action for conversion of or injury to the property *Oros v. Allen*,[21] approving *Stotts v. Puget Sound, Etc. Co.*,[22] in which it is said

> "This court, as previously noted in this opinion, has held that a vendee under a conditional sale has no title, but it does not follow that the law will not define and protect such rights as he may have."

The full value of the property may be recovered where wrongfully converted notwithstanding only part of the payments have been made.[23]

The decision in *Ashford v. Reese, supra,* has not altered the law in such respect. In *Katewa v. Snyder*,[24] it is said

> "The respondent defends the judgment on the ground that the appellants have only a conditional contract for the purchase of the land occupied by them, and therefore have no right to complain of any action of the respondent, citing our case of *Ashford v. Reese*, 132 Wash. 649, 233 Pac. 29, where we held that an executory contract for the sale of real estate creates no title, legal or equitable, in the vendee. But we did not hold that such a contract was a nullity Unquestionably, as between the parties to this action, it is sufficient upon which appellants can base their right to possession of the land which they are purchasing, and sufficient to authorize them to forbid any person to interfere with that possession."

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[19] 39 Cyc. 1657, note 75.
[20] 134 Wash. 437, 235 Pac. 964 (1925).
[21] 133 Wash. 268, 233 Pac. 314 (1925).
[22] 94 Wash. 339, 162 Pac. 519 (1917).
[23] *Messenger v. Murphy*, 33 Wash. 359, 74 Pac. 475 (1903).
[24] 143 Wash. 172, 254 Pac. 857 (1927).

The vendee is entitled to declare a homestead in the subject matter of an executory contract.[25]

Where land or any estate or interest in land is the subject matter of the contract, specific performance will be invariably decreed.[26] The same relief will be granted as against the vendor's grantee who takes with actual or constructive notice.[27] In *Pratt v. Rhodes*,[28] it is said in discussing *Ashford v. Reese*

> "It was not there meant that an executory contract for the sale of land vests no right in the vendee which the court will enforce at the suit of the vendee. It is not held that such a contract is a nullity The contract, on the contrary, has all of the validity that any other executory contract has which is duly and regularly executed by parties competent to contract. Nor will the courts in every instance relegate the vendee to an action in damages where the contract is breached by the vendor. If equity, justice and good conscience require that the contract be specifically enforced, the courts will enforce it specifically The cited case, and the cases referred to therein, do not announce a contrary doctrine. To hold that an executory contract for the sale of land does not by its mere execution vest in the vendee any title or interest in the land contracted to be conveyed, is not to hold that the vendor may deprive the vendee of the benefit of the contract by his mere whim or caprice."

Judge Tolman also questioned whether the vendee has anything which could be insured. The answer is that there are many kinds of loss other than legal or equitable interests in property Risks which may be insured against are matters of contract. Where there is an intention to insure against a risk arising out of a contractual relation and independent of title, the contract of insurance, of course, will be given effect by the courts. There is nothing against public policy in such an insurance contract. The court, in *Washington Fire Relief Association v. Albro*,[29] had occasion to set the question at rest, saying·

> "So, also, we think, he had an insurable interest in the barn, notwithstanding it may have been legally the separate property of his wife. As is shown by the cases

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[25] *Desmond v. Shotwell*, 142 Wash. 187, 252 Pac. 692 (1927).
[26] Cyc. 552-553.
[27] 36 Cyc. 761-764.
[28] 142 Wash. 411, 253 Pac. 640 (1927).
[29] 137 Wash. 31, 241 Pac. 356 (1925).

> collected in 20 C. J 20, under par. 3, the term 'interest,' as used in the phrase 'insurable interest,' is not limited to property or ownership in the subject matter of the insurance, that where the interest of the insured in, or his relation to, the property is such that he will be benefited by its continued existence, or will suffer a direct pecuniary loss by its destruction, his contract of insurance will be upheld, although he has no legal or equitable title."

In all the foregoing citations, it is assumed or recognized that contractual rights pertaining to property, notwithstanding no present transfer or conveyance takes place, are given effect by the courts as against the other party to the contract and all persons claiming through him except innocent purchasers or encumbrancers. Almost numberless decisions, in which such rights have been protected, might be collected. Failure to distinguish between contractual rights pertaining to, and an interest in property, is responsible for the confusion and doubts.

Criticism of the rule that no interest, legal or equitable, passes by an executory contract, has been for the most part based on precedent, which lays down a contrary rule as to realty contracts only The same language means exactly the same thing, whether it be used in a contract relating to realty or personalty No logical reason can be assigned for holding that identical language when relating to real estate shall be given an effect directly opposite to that given when personal property is the subject matter of the contract.

It is believed by many that it is not to the best interests of the marital community for the husband to have the right to assign or transfer contracts pertaining to realty without the consent of the wife. But that is a matter for legislation, and that right may be abrogated by an enactment simply requiring both members of the marital community to join in such assignments and transfers.

It has been proposed that legislation be enacted providing in effect that executory contracts to sell property be deemed to transfer or convey an interest therein. Legislation of that kind would be far from satisfactory It would amount to an interfer ence, or attempted interference, with the right to contract. It would give an effect to the language of the contract directly opposite to its intended and evident meaning. If it should be construed as declaratory of the common law, it might work disaster to a great many titles. Such proposals have nothing to commend them. Undesirable consequences flowing from the applica-

tion of the rule—in most instances, from an incorrect application of it—can be remedied by more appropriate and less harmful legislation.

While confusion of terms has resulted in incorrect applications of the rule that no equitable or legal interest in the property passes to the vendee under an executory contract to sell, in the *Schaefer, Ashford* and *Holt Manufacturing Company* cases, and unfortunate language was used in the dissenting opinions, there is no reasonable probability of the court holding that the vendee's contractual rights in the property will not be fully protected by the courts.

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