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CONTRACTS - THIRD PARTY BENEFICIARY - RIGHT OF PROMISOR TO SET OFF CLAIM AGAINT PROMISEE IN A SUIT BY BENEFICIARY

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CONTRACTS — THIRD PARTY BENEFICIARY — RIGHT OF PROMISOR TO SET OFF CLAIM AGAINT PROMISEE IN A SUIT BY BENEFICIARY — *A* and *B* mortgaged real estate to the plaintiff to secure their notes aggregating $9,000. Six months later *A* and *B* exchanged this property to the defendant for certain real estate owned by her. By the deed the defendant assumed the mortgage indebtedness owed to the plaintiff. As a further consideration for the exchange,

A and *B* executed a note for $13,050 to the defendant. The plaintiff instituted this action against *A* and *B*, seeking to recover the balance, and by amended petition joined the defendant. The defendant claimed the right of set-off on the uncollected judgment against *A* and *B*, now insolvent, on the ground that the plaintiff's right was derivative through *A* and *B*, and so subject to the same defenses. *Held*, that the beneficiary's right of recovery against the promisee is subject only to defenses arising from the contract, and therefore is not subject to set-off. *Commonwealth Life Ins. Co. v. Eline*, 274 Ky. 539, 119 S. W. (2d) 637 (1938).

It is generally held that a mortgagee can enforce the personal obligation of the assuming grantee.[1] The courts describe the basis of this action either as equitable subrogation on suretyship principles,[2] or as a third party beneficiary contract enforceable by the beneficiary.[3] While in most cases it makes little difference which view is adopted so far as the result is concerned, this is not always so. If a court resolves the problem on suretyship principles, any defense or set-off available to the assuming grantee as against his vendor is available to him as against the mortgagee.[4] However, on principles of beneficiary contracts, it is said that the assuming grantee is limited to those legal or equitable defenses that arise from the contract.[5] Thus defenses of lack of capacity, want of mutual assent, want of consideration, fraud, mistake, or failure of consideration are available to the assuming grantee; [6] but the right of set-off cannot be asserted, as it is not a defense to the action, but an independent cause of action.[7] Since the principal case was decided on the contract beneficiary theory, the court's refusal to allow the set-off is justified by the authorities.[8] But it should be noted that the application of this principle to the situation where the grantee

[1] 2 WILLISTON, CONTRACTS, rev. ed., § 383 (1936). *Contra*: Creesy v. Willis, 159 Mass. 249, 34 N. E. 265 (1893). Some courts, following the first New York case, on these facts allow recovery only in equity. WILLISTON, ibid., § 384. But most courts allow an action at law. 2 JONES, MORTGAGES, 8th ed., § 957 (1928). The contracting parties cannot mutually rescind. Bohnert v. Radke, 189 Wis. 203, 207 N. W. 284 (1926).

[2] Episcopal City Mission v. Brown, 158 U. S. 222, 15 S. Ct. 833 (1895) (leading case); Waddell v. Roanoke Mutual Bldg. & Loan Assn., 165 Va. 229, 181 S. E. 288, 100 A. L. R. 906 at 911 (1935); 21 A. L. R. 439 (1922); 47 A. L. R. 339 (1927).

[3] 2 JONES, MORTGAGES, 8th ed., § 949 (1928); Dunning v. Leavitt, 85 N. Y. 30 (1881); Alabama-Florida Co. v. Mays, 111 Fla. 100, 783, 149 So. 61, 661 (1933) (right of mortgagee is cumulative, not substitutional).

[4] See references, note 2, supra. 2 WILLISTON, CONTRACTS, rev. ed., § 394 (1936); Kyner v. Clark, (C. C. A. 8th, 1928) 29 F. (2d) 545; WALSH, MORTGAGES, § 51 (1934).

[5] Fulmer v. Goldfarb, 171 Tenn. 218, 101 S. W. (2d) 1108 (1937), noted in 36 MICH. L. REV. 847 (1938); Franklin Fire Ins. Co. v. Howard, 230 Ala. 666, 162 So. 683 (1935) (reformation).

[6] 2 WILLISTON, CONTRACTS, rev. ed., § 394 (1936).

[7] Yarger v. Chicago, M. & St. P. Ry., 78 Iowa 650, 43 N. W. 469 (1889).

[8] See references, notes 3 and 5, supra.

assumed the mortgage indebtedness has been criticized.[9] It is submitted that the court, had it been anxious to find for the defendant, could have held that this was a defense based on a supervening circumstance arising in connection with the contract, namely, failure of consideration, or failure to substantially perform an implied condition.[10] Although the facts are explicit in this regard apparently this was a partly bilateral contract in which the promises, although they were not the full agreed exchange for each other, were dependent so that a material failure of performance should operate to excuse the defendant.[11] On this ground it is arguable that the inability to pay the mortgage debt of $13,000, as against the promise to pay $9,000, is sufficiently material to amount to a failure of consideration.

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[9] Warm, "Some Aspects of the Rights and Liabilities of Mortgagee, Mortgagor, and Grantee," 10 TEMP. L. Q. 116, at 130 (1936).

[10] See 3 WILLISTON, CONTRACTS, rev. ed., § 813 (1936).

[11] Ibid., § 858.