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Rights and Estates of Vendor and Vendee under an Executory Contract for the Sale of Real Property

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RIGHTS AND ESTATES OF VENDOR AND VENDEE UNDER AN EXECUTORY CONTRACT FOR THE SALE OF REAL PROPERTY

THE question of the rights and estates of vendor and vendee under an executory contract for the purchase of real property is governed by the doctrine of equitable conversion. This doctrine has come down to us from the chancery courts of England and is based upon the maxim:

> "Equity will regard as done that which ought to be done."

Probably the best exposition of this subject that is to be found in any text book is in Pomeroy's *Equity Jurisprudence,* 4 Ed., where he has the following to say concerning the effect of an executory contract in equity:[1]

> "The full significance of the principle that equity regards and treats as done what ought to be done throughout the whole scope of its effects upon equity jurisprudence is disclosed in the clearest light by the manner in which equity deals with executory contracts for the sale of land or chattels, which presents such a striking and complete contrast with the legal method above described. While the legal relations between the two contracting parties are wholly personal,—things in action,—equity views all these relations from a very different standpoint. In some respects, and for some purposes, the contract is executory in equity as well as at law; but so far as the interest or estate in the land of the two parties is concerned, it is regarded as executed, and as operating to transfer the estate from the vendor and to vest it in the vendee. By the term of the contract the land ought to be conveyed to the vendee, and the purchase price ought to be transferred to the vendor; equity therefore regards these as done: the vendee as having acquired the property in the land, and the vendor as having acquired the property in the price."

The statement of the text is universally recognized as the law by the courts of all English speaking races, and a citation of authorities

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1 Pomeroy's Equity Jurisprudence, 4 ed., Vol. 1, page 685, sec. 368.

to sustain that principle is useless as they can be found by the hundreds with scarcely a dissenting voice raised anywhere. [2]

The general rule seems to be well established that when an executory contract for the purchase and sale of real property has been executed with a binding obligation on the part of the vendor to sell upon the receipt of the purchase price, and upon the vendee to purchase and pay the purchase price, the conversion is immediately effected and that it is not affected in any manner by provisions in the nature of conditions which may entitle either party subsequently to forfeit or rescind the contract. Pomeroy has the following to say concerning this feature: [3]

> "Enforceability of the contract at the time of death of one of the parties refers to the validity of the contract and not to events in the nature of conditions which may not have been performed because such performance was not due at the time of the death of testator. It is sufficient if these conditions are performed by his representatives. Provisions of the nature of conditions in contracts of sale do not alter the rule that the contract of sale is an equitable conversion of the realty into personalty."

Here again the text appears to be well sustained, both in reasoning and by weight of authority. [4]

The great English chancellors for hundreds of years have regarded the doctrine of equitable conversion as a fixed rule of equity and have held that a court of equity would always treat the vendee under an executory contract for the purchase of real property as being the equitable owner of the land itself. The English judges

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2 Lysaght v. Edwards, 2 Ch. Div. 499. Seton v. Slade, 7 Ves. Jr. 265. Laws v. Bennett, 1 Cox Ch. 167. Williams v. Haddock, 145 N. Y. 144, 39 N. E. 825. Clapp v. Towner, N. D. 93 N. W. 862. Wollgast v. Henning, Ia. 112 N. W. 86. Rhodes v. Meredith, Ill. 102 N. E. 1063. Ostrander v. Davis, 191 Fed. 159. In re Ashbach's Estate, 169 N. Y. S. 1058. Hyde v. Heller, 10 Wash. 586. Davie v. Davie, 47 Wash. 231. Griggs Land Co. v. Smith, 46 Wash. 185.

3 Pomeroy's Equity Jurisprudence, 4 Ed., Sec. 2268.

4 Williams v. Haddock, 145 N. Y. 144, 39 N. E. 825. In re Bernhard-Wollgast v. Henning, 134 Ia. 606, 112 N. W. 86, 12 L. R. A. (N. S.) 1029. In re Ashbach's Estate, 169 N. Y. S. 1058. In re Boshart's Estate, 177 N. Y. S. 574. Flomerfelt v. Siglim, Ala. 47 S. 106. In re Miller's Estate, Ia., 119 N. W. 977. Ingraham v. Chandler, Ia., 161 N. W. 434. Insurance Company of N. A. v. Erickson, 50 Fla., 419, 39 S. 495. Brighton Beach Racing Association v. Home Insurance Co., 99 N. Y. S. 219. Baker v. State Insurance Company, 31 Ore. 41. Loventhal v. Home Insurance Co., 112 Ala. 108, 57 A. S. R. 17. Wimbish v. Montgomery, 69 Ala. 575. Hyde v. Heller, 10 Wash. 586 .

have set forth the position in equity of the vendor and vendee under an executory contract with greater accuracy and clearness than have the American judges and have stated their reasons for their decisions showing them to be based upon well considered principles. Lord Eldon's admirable discussion in *Seton v. Slade,* Sir George Jessel's remarkable analysis in *Lysaght v. Edwards,* and the judgment of Judge Kenyon in *Laws v. Bennett,* are all masterpieces of analysis and research. This doctrine, as applied to the testimentary disposition of property, has a wider reaching effect in England than it has in this country, for under their laws the descent and distribution of real and personal property upon the death of a testator were controlled by widely different principles, and generally passed to a different person, as the real property went to the heirs at law and the personal property to the next of kin, while in this country under our laws of descent and distribution, the estate, whether real or personal, generally passes to the same person. However, many cases still arise even in this country where it is necessary to determine whether or not there has been an equitable conversion for the purpose of construing a will.

The question that has probably occasioned the greatest disturbance and led to the greatest conflict in the authorities is whether or not an option to purchase works an equitable conversion, and if so, at what time the conversion will be held to have taken place. The leading case from England on this question is the case of *Laws v. Bennett.*[5] This case was decided by Lord Kenyon in 1785. A lease had been made for a long term with an option to the lessee to purchase. The lessor died before the expiration of the term and his will disclosed that he had devised all his real estate to his cousin several years before the execution of the lease, and his personal property in equal parts to his cousin and his sister, Mary. After the death of the testator, the lessee exercised the option and paid the money to the executor. Both the devisee and the legatee claimed the purchase money. In that case Lord Kenyon held:

> "When the party who has the power of making the election has elected, the whole is to be referred back to the original agreement and the only difference is that the real estate has been converted into personal estate at a future period."

The chancellor thus declared the purchase price to be a part of the personal estate of the testator. This case has been uniformly,

[5] Laws v. Bennett, 1 Cox Ch. 167.

although reluctantly, followed in England, and it has received great criticism even there, [6] while in this country the rule laid down by that case has been almost uniformly rejected and our courts have held that the conversion takes place as of the date of the exercise of the option, and not as of the date of the option agreement. Thus it will be seen that our courts have carried out the idea that there must be a binding obligation to purchase and a binding obligation to sell before the conversion will be deemed to have taken place. [7]

Since the purchaser immediately upon the signing of the contract becomes the equitable owner of the land, by the great weight of authority he assumes the risk of loss. Equity from the moment the contract is binding gives the vendee the entire benefit of any rise in value of the land, of subsequent improvements, and of any other advantage that may accrue to the estate. If the vendee has the right to the increase in value why should he not assume any liability for the decrease in value? Especially is this true if the vendee be let into possession, as in that case he is the person who should primarily see that there is no loss to the property. The vendee has an insurable interest and can insure to protect himself. In fact, it is generally held that the vendee is the sole owner of the property within the meaning of that clause in an insurance policy.[8]

The courts of the State of Washington have strayed widely from the path beaten for them by the decisions of centuries, and have held that an executory contract such as we have been discussing conveys to the purchaser no element of title, legal or equitable. It is interesting to trace their decisions upon this subject and note wherein they have drifted from this path.

The first case I can find that hits this matter squarely is the case

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[6] Townley v. Bedwell, 14 Ves. 591. Collingwood v. Rowe, 3 Jur. (N. S.) 785.

[7] Rockport Lime Co. v. Leary,20 N. Y. 469, 87 N. E. 43. Gilbert v. Port, 28 Ohio St. 276. Caldwell v. Frazier, 65 Kan. 24, 68 Pac. 1076. Ex parte Hardy, 30 Beaver, 206. Richardson v. Hardwick, 106 U. S. 252, 27 L. E. 145. In re Evans, Minor, 177 N. W. 126. Smith v. Lowenstein, 50 Ohio St. 346, 34 N. E. 159. Sheehy v. Scott, 128 Ia., 551, 104 N. W. 1139. Ingraham v. Chandler, Ia., 161 N. W., 434, L. R. A. 1917 "D" 713.

[8] Insurance Company of North America v. Erickson, 50 Fla. 419, 39 S. 495. Brighton Beach Racing Association v. Home Insurance Co., 99 N. Y. S. 219. Clinton v. Hope Insurance Co., 45 N. Y. 465. Goldman v. Rosenberg, 116 N. Y. 85, 22 N. E. 260. Neponsit Realty Co. v. Judge, 176 N. Y. S. 133. Cammarota v. Merkeewitz, 198 N. Y. S. 825. Sewell v. Underhill, 197 N. Y. 168, 90 N. E. 430, 27 L R. A. (N. S.) 233. Phoenix Insurance Co. v. Kerr, 129 Fed. 723. Baker v. State Insurance Co., 31 Ore. 41. Loventhal v. Home Insurance Co., 112 Ala. 108, 57 A. S. R. 17. Wimbish v. Montgomery, 69 Ala. 575.

that came up from Yakima County: *Tieton Hotel v. Manheim.*[9] In that case the court cites as authorities for its holdings five Washington cases, *Reddish v. Smith;* [10] *Pease v. Baxter;* [11] *Churchill v. Ackerman;* [12] *Johnson v. Sekor,* [13] and *Younkman v. Hillman.*[14] I will examine these cases in their order.

The first: *Reddish v. Smith* only concerns itself with the question of whether or not the vendor under an executory contract for the purchase of real property providing that the vendor may upon default declare a forfeiture and re-enter the premises, may retain the purchase money upon the declaration of forfeiture. The court held that the forfeiture could be declared and there was no discussion of the interest conveyed.

The second: *Pease v. Baxter* affirmed the holding in *Reddish v. Smith,* and in that case there was no discussion of the estate conveyed by the contract.

In the third: *Churchill v. Ackerman,* for the first time the court intimates what its holdings will be on this question of title and estate. In that case the plaintiff had entered into a contract for the purchase of real property and did not take immediate possession. A party under a former forfeited contract had remained in possession and harvested the crops after the new purchaser had contracted to purchase. Plaintiff brought an action to recover for the conversion of the crop which had all been severed before plaintiff took possession. The court held that even though plaintiff had been the holder of the legal title he could not have recovered, and then goes on to say:

> "Much less would he be enabled to do so where he holds simply an executory contract, such as is held by the plaintiff in this case, which might, or might not, ripen into a title. And that such a contract as this is executory and conveyed no element of title, but could be forfeited upon violations of its conditions, see *Reddish v. Smith,* 10 Wash. 178 (38 Pac. 1003, 45 Am. St. Rep. 781); *Pease v. Baxter,* 12 Wash. 567 (41 Pac. 899)."

It will thus be seen that their first expression on this question was dictum and was not necessary for the decision of the case and had not been considered in the cases cited to sustain the proposition,

9 75 Wash 641, 135 Pac. 658.
10 10 Wash. 178, 38 Pac. 1003, 45 Am. St. Rep. 781.
11 12 Wash. 567, 41 Pac. 899.
12 22 Wash. 227, 60 Pac. 406.
13 53 Wash. 205, 101 Pac. 829.
14 53 Wash. 661, 102 Pac. 773.

the matter not having been discussed in either the 10th Washington or the 12th Washington cases.

In the fourth: *Johnson v. Sekor,* the question presents itself as to whether or not a judgment became a lien upon the interest of the vendee under a contract for the purchase of real property. The purchaser had not taken possession of the premises, in fact there were no buildings on the premises, which were vacant lots in the City of Tacoma, and the contract provided for a forfeiture in case of default. The court there held that a judgment would not become a lien upon the interest of the vendee under an executory contract for the purchase of real property such as the one in question, but cited no authority for their holding; however, in that case, the contract had been forfeited prior to the levy of any execution by the judgment creditors and therefore the holding that there was no interest of the vendee in the property which could be reached, was probably correct.

In the fifth: *Younkman v. Hillman,* the question arose whether or not the party described as a purchaser in a contract could apply to a party who had contracted to purchase. The court held that the purchaser meant a party who had paid for and received the legal title and not a vendee under an executory contract. The court there says:

> "The whole tenor and effect of the contract is clearly in contemplation of a future and not a present sale. Such contracts have invariably been held to be contracts for title or agreements to convey, not ripening into even an equitable title until the vendee has placed himself in such a position by performance that he can compel a conveyance. *Chappell v. McKnight,* 108 Ill. 570; *Numgesser v. Hart,* 122 Iowa 647, 98 N. W. 505; *Stewart v. Fowler,* 37 Kan. 677, 15 Pac. 918."

The statement of the court is not, as there represented to be, the weight of authority and is contrary to the well decided cases. In fact, an examination of the cases cited in the *Younkman v. Hillman* case do not themselves constitute authority for the point on which they are cited. In the *Numgesser v. Hart* case the only question was who was liable for taxes accruing after the date of the contract, the vendor having retained possession until all payments were made under the contract. The court there says:

> "In fixing the liability for taxes the test of ownership under a contract of sale of real estate is possession."

The question of the estate conveyed by the contract was not discussed. In *Stewart v. Fowler,* a real estate broker sued for a com-

mission. The only question to be decided was whether or not he made a sale by finding a party willing to buy on contract. In this case there was no discussion as to the interest or estate which is conveyed under a contract. The case *Chappell v. McKnight* does seem in a measure to sustain the point in question, the court there saying:

> "A mere contract or covenant to convey at a future time, on the purchaser performing certain acts, does not create an equitable title."

The language, however, was not necessary for a decision of the case, as the court held there was no valid contract. The only authority cited in the case of *Chappell v. McKnight* to sustain the language therein used is Bispham's *Equity,* Sec. 365. An examination of that text shows that Section 365 does not deal with the subject of equitable conversion. On the contrary, that author has the following to say on the subject of equitable conversion, Sec. 313:

> "Where the conversion is claimed to have taken place by virtue of a contract, it is necessary, as a general rule, that the contract be binding. The rule is not changed by anything happening after the death of the purchaser by which the binding character of the contract could be affected, *nor by the circumstance that the purchase is entirely at the option of the vendee.*"

By the last sentence it is seen that the author accepts the doctrine of equitable conversion to its extreme limit, as laid down in *Laws v. Bennett.*

Again on page 664 of *Younkman v. Hillman,* the cases of *Reddish v. Smith, Pease v. Baxter* and *Johnson v. Ackerman* are cited as holding that executory contracts convey no title. Manifestly they are not authority for such a holding, as that question was not discussed in any of the three cases unless by the word "title" the court meant the legal title and was not considering an equitable estate.

Now arriving at the *Manheim* case. The facts in that case are these: Priscilla Lee, the owner of certain lots in Yakima, entered into a contract for the sale thereof to William Manheim for $7,500.00. Five hundred dollars was paid in cash and the contract provided for the balance to be paid prior to May 9, 1906, when a deed would be given. It was the usual contract providing for forfeiture in case of default. William Manheim was a married man at the time he entered into the contract and his wife died on February 11, 1906. After her death Manheim defaulted and notice for forfeiture was served upon him. He acknowledged the forfeiture and

in writing agreed to surrender the premises and the writing was filed for record. The children of William Manheim and the wife who died in February, 1906, asserted an interest in the property and this case was brought to quiet title. In that case the court again repeated the quotation from *Churchill v. Ackerman*:

> "Such a contract as this is executory and conveyed no element of title, but could be forfeited upon violations of its conditions."

The court then discusses all the other Washington cases hereinbefore discussed and at that time, in a case where the decision was necessary for a determination of the case, the court evidently adopted the rule that an executory contract in this state was personalty and would not pass to the heirs of a deceased person; that the wife acquired no interest under an executory contract which was not subject to the control, management and disposition of the husband, and that until the full purchase price had been paid the purchaser had no interest in the realty under a contract which provided that the vendor might forfeit the same upon default. However, the court in the *Manheim* case does not discuss a case which had been decided some years before that.

In the case of *Baker v. Sinclaire,*[15] the contract under consideration had the forfeiture provision but the court in discussing the relation of the vendor and vendee uses the following language:

> "The contract above mentioned created the relation of debtor and creditor between Watson and Sinclaire. Their relation to the real property was in the nature of that of mortgagor and mortgagee. They stood in the same relation to it as they would have stood had Sinclaire conveyed the property outright to Watson, and taken a mortgage back as security for the purchase price. 'There can be no sensible distinction between the case of a legal title conveyed to secure the payment of a debt and a legal title retained to secure payment.' *Jones, Liens,* 1108. See further, *Shelton v. Jones,* 4 Wash. 692 (30 Pac. 1061); *St. Paul & Tacoma Lumber Co. v. Bolton, supra.* This being the relation of the parties, the provisions of the statute subordinate the lien of the respondents to the interests of the Sinclaires in the property."

Just a month before the decision in the *Manheim* case our Supreme Court had decided the case of *Taylor v. Interstate Investment Company.*[16] In this case a bond for a deed had been given for land, the

15 22 Wash. 462, 61 Pac. 170.
16 75 Wash. 490, 135 Pac. 240.

purchase price of which was $150,000.00. Fifty thousand dollars had been paid in cash and the remainder was represented by two promissory notes, one payable in five years and the other in ten. There was no provision for a forfeiture and the vendee went into possession, and the court in that case cites *Baker v. Sinclaire* with approval, quotes the section from Pomeroy, providing that the vendee should be looked upon and treated as the owner of the land, and says:

> "Under the foregoing authorities it is plain that the vendee acquired the full equitable title as against the vendors and that the bond created an equitable mortgage securing the unpaid balance of the purchase price."

How the court overlooked citing this case in the *Manheim* case is hard to explain, the only distinguishing feature between the two cases being the inclusion in the *Manheim* case of the provision for forfeiture upon default and the lack of that provision in the *Taylor* case. The cases of *Hyde v. Heller,*[17] *Davie v. Davie,*[18] and *Griggs Land Co. v. Smith,*[19] are also cases which might have been cited in the Manheim case as tending to show an adoption by the courts of the State of Washington of a doctrine contrary to that therein announced.

The next case I find is *Converse v. LaBarge.*[20] In that case Kelly, the owner in fee simple, executed a contract for the sale of property to A. B. Converse, husband of the appellant. Kelly forfeited that contract after default without notice the wife of Converse and she brought suit, claiming a community interest in the property. The court in discussing her claim says:

> "But we cannot think this contention tenable. Its fallacy lies in the assumption that the community had such title to the property in virtue of the contracts as could not be forfeited without the consent of the community, or after notice to the community. Such, however, is not the rule. Contracts of this sort confer title in the contract purchaser only when fully performed on his part, or performance in so far as it is capable of being performed on his part. Until that time, such contracts are merely initiatory of title. By performance, they ripen into title, either legal or equitable, but fail of either by nonperformance. Since, therefore, the husband alone may enter into them on behalf of the com-

17 10 Wash. 586, 39 Pac. 249.
18 47 Wash. 231, 91 Pac. 950.
19 46 Wash. 185, 89 Pac. 477.
20 92 Wash. 282, 158 Pac. 958.

> munity so he may also forfeit them on its behalf before performance is completed, either by consent, or by failing to comply with the conditions on his part to be performed. Such in effect was our holding in the case of *Tieton Hotel Co. v. Manheim,* 75 Wash. 641, 135 Pac. 658. This case in its facts is parallel in many respects to the one at bar."

The statement made that since the husband may enter into the contract on behalf of the community so he may also forfeit them on its behalf will not bear a logical examination, for though the husband may also take the legal title to real property on behalf of the community, he cannot in like manner dispose of it without the consent of the wife.

The next case I find is *Schaefer v. Gregory Co.,*[21] which is the case that holds that the vendee is not a person interested in the property within the meaning of the statute providing for condemnation and that the vendor is the only necessary party to an action to condemn. The holding of this case seems wrong to me in many respects. First, whether or not the vendee holds title, either legal or equitable, it can hardly be said that he has no interest in the property that should make him a party to condemnation. If the holding in the case of *Schaefer v. Gregory Co.* is correct this risk of loss by condemnation must fall upon the vendor, for if the property has depreciated at the time of the condemnation and he receives less than the price for which he has contracted to sell it, the loss will surely fall upon him, as the vendee can recover from him for failure to convey. In the last cited case the court cites cases from other jurisdictions holding that the vendee under such a contract becomes the equitable owner and decline to accept that rule. The court says:

> "We come to the conclusion, therefore, that, under the well settled law of this state, the vendee in a forfeitable, executory contract of sale has no legal of equitable interest in the property, the subject-matter of the contract."

Thus showing that it is now the accepted and settled doctrine of this state.

The last case that touches upon this question is the case of *Casey v. Edwards,*[22] where the court makes the following statement:

> "It is true that in an executory contract for the purchase of real estate, the purchaser has, during the existence of the contract, no legal or equitable title to the property. *Schaefer v. Gregory Co.,* 112 Wash. 408, 192 Pac. 968. But

[21] 112 Wash. 408, 192 Pac. 968.
[22] 123 Wash. 661, 212 Pac. 1082.

> this does not determine that the purchaser under such a contract has no property interest in the contract itself which is subject to execution. Such purchaser has an interest. Although it may not be an interest in the land itself, it is personal property and is liable for judgment against such purchaser."

In conclusion it must be stated that our courts have adopted a rule concerning the rights of the parties to a contract for real property that if not followed by them alone is at least the rule only in a small minority of states. That an examination of the cases that lead up to a final holding to this effect show that the court did not accept this rule knowingly and intentionally, but that one step led to another until they were irretrievably confirmed to the doctrine and it had become a rule of property and it was too late to turn back. Having taken one step in the wrong direction it was much easier to take the next than to retrace their steps and admit their error and reconsider the entire question. I doubt if the court would ever have taken the position it has been forced into if the ultimate holding had ever been presented to it as one proposition. It leads in its final analysis to a holding that a husband, the community holding an interest in vacant, unimproved lots under a bond for deed without the forfeiture clause, may not convey the community interest in those lots without the wife joining in the conveyance; but that, where the husband has contracted to purchase a house, the residence of himself and family, under a contract with the forfeiture clause, and has only a few small payments to make, he can arbitrarily and without the consent of his wife, sell the contract or surrender the same and the wife has no chance to complete the payments and save the home. I have tried to find some reason why the element of defeasibility should make this difference, but I have been unable to do so. I doubt very much if under the present holdings of our courts a homestead exemption can be claimed and enforced out of property occupied as a homestead by a vendee under an executory contract, although when that proposition is finally presented to the court they may decline to follow their former holdings and to carry their doctrine out to its logical conclusion.

Since this article was written the Supreme Court of the State of Washington has decided the case of *Ashford v. Reese,*[23] which case holds that the vendor under an executory contract in this state assumes the risk of loss and that the vendee may rescind his contract and recover from the vendor the amount paid thereon in case of

[23] 32 Wash. Dec. 526, 233 Pac. 29.

the destruction of any part of the property. Three of the judges dissented from this opinion, and as their position is well set out in the dissenting opinion there is no need to discuss that case further than to state that the dissenting opinion seems to be the correct holding irrespective of the question of title or estate in the vendee, and that the decision as it stands in the reports of the State of Washington merely adds one more block to the wall of *stare decisis* which will prevent a re-examination and reconsideration of this question upon its merits.

SEATTLE *P. John Lichty.*