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COMMENTS

FUTURE ADVANCES ON MORTGAGES IN WASHINGTON

When *Elmendorf-Anthony Co. v. Dunn*¹ was decided in August, 1941, it completed the law of future advances on mortgages in this jurisdiction. The case dealt with the problem of optional advances by the mortgagee, and the effect of intervening encumbrances upon such advances. Perhaps it will be well to show the fact situation in order to see the problem more clearly.

The defendants, Dunn and wife, executed and delivered a promissory note for \$2,200, and accompanying the note was a real estate mortgage upon a certain lot in the city of Spokane. The note contained an acceleration clause to be exercised at the option of the mortgagee. The mortgage provided that upon certain events happening, among them an abandonment for a period of fifteen days, the mortgagee might, at its option, enter upon the premises to complete the construction of the building or buildings there, and any amount spent by the mortgagee in connection with the completion of this construction was to be added to the principal amount of the note and secured by the mortgage.² This mortgage was duly recorded. Later, the defendants Dunn executed and delivered to the defendant Long Lake Lumber Co. a note secured by another mortgage on the same premises, which mortgage was duly recorded. The note given here was for a pre-existing debt.

The Dunns failed to complete the construction of the building according to the terms agreed upon, and so informed the plaintiff, which procured a title report on the property. This report revealed the existence of the defendant Lumber Company's mortgage on the premises. Nevertheless, the plaintiff went ahead to complete the construction, expending a substantial sum to effect the completion of the building.

In a subsequent action to foreclose the plaintiff's mortgage, the plaintiff was adjudged to have a prior lien for the amount advanced under the promissory note, he was also entitled to have a lien for the amount expended for completion of the construction after the premises were abandoned by the Dunns. The defendant Lumber Co. was entitled to a judgment against the Dunns for the amount of their note covered by its mortgage, and such judgment lien was to have priority over the lien of the plaintiff for the amount expended under the rider clause of the plaintiff's mortgage. Judgment was entered accordingly, and the plaintiff's appeal immediately centered the attention of the court on this problem of optional advances.

The court considered from the outset the respondent Lumber Company's statement of the rule that when a mortgagee, not being bound to make such advances, exercises his option with actual knowledge of an intervening encumbrance, such advances are made subject to the intervening encumbrance. The treatment this contention received at the hands of the court is in keeping with almost universal authority,³

¹ 10 Wn. (2d) 29, 116 P. (2d) 253 (1941).

² *Ibid.*, at p. 31.

³ 1 JONES ON MORTGAGES (8th ed. 1928) § 453, 41 C. J. § 468.

and in support of the court's position it cited a statement from 5 A. L. R. 398.⁴ In fact, the only possible controversy could not arise in the instant case because the fact situation did not present it. The reference is to the problem of notice in this type of case. Courts are not of uniform opinion as to the kind of notice of subsequent encumbrance required. Some courts say that constructive notice such as is given by a recording statute is sufficient to establish precedence of the lien of the subsequent encumbrance over advances made at the option of the prior mortgagee. Other courts hold that actual notice is necessary before the subsequent encumbrancer can claim such priority.⁵ In the present case the court mentioned this difference of opinion, but pointed out that there was no controversy, when actual notice was admitted, as it was here citing Thompson on *Real Property*.⁶

The court in the *Elmendorf* case points out that this is the first time that the problem of optional future advances has arisen in this jurisdiction, but it had been referred to in two previous cases.⁷ Both cases gave the rule adopted in the instant case as the correct one, but as they were not in point in those cases, they could not be said to have settled the law on the problem in Washington; hence the court in the *Elmendorf* case felt free to treat it as a new one.

As a preface to holding for the majority view, the court said:

"If there were any substantial diversity of opinion in the decisions of our sister states, we would be inclined to view the rights of the first mortgagee relative to advances made pursuant to an optional clause in a construction contract, even after notice of a junior encumbrance, as superior to such junior encumbrance."⁸

They do not enlarge upon this statement, but rather they simply mention the dearth of authority supporting that inclination. It would be interesting to know why they would be in favor of supporting the optional clause against such overwhelming authority to the contrary. But rather than set a contrary precedent for this jurisdiction, the court chose to abide by the majority rule, and cites with approval Pomeroy's statement of the rule.⁹

⁴ "By the weight of authority, a mortgage for future advances becomes effective lien from the time of its execution, or, as to subsequent purchasers and encumbrancers, from the time of its recordation, rather than from the time when each advance is made, where the making of the advances is *obligatory* upon and not merely optional with the mortgagee." 5 A. L. R. 398 (italics by the court).

⁵ 4 POMEROY, EQUITY JURISPRUDENCE (5th ed. 1941) § 1199, 41 C. J. § 468.

⁶ 9 THOMPSON, REAL PROPERTY (Perm ed. 1940) 326: "If such mortgagee is not under any obligation to make advances, and after notice of a subsequent mortgage does make further advances to the extent of such advances, the subsequent mortgagee had the right of precedence; but if such mortgagee is under obligation to make the advances, he is entitled to the security, whatever may be the encumbrances subsequently made upon the property, and whether he has notice of them or not."

⁷ *Inland Trading Co. v. Edgcombe*, 57 Wash. 257, 106 Pac. 768 (1910); and *Eltopia Finance Co. v. Colley*, 126 Wash. 554, 219 Pac. 24 (1923).

⁸ 10 Wn. (2d) 29, at p. 38.

⁹ 4 POMEROY, EQUITY JURISPRUDENCE (5th ed. 1941) § 1199: "When a mortgage to secure future advances reasonably states the purposes for which it is given, its record is a constructive notice to subsequent purchasers and encumbrancers; they are thereby put upon an inquiry to ascertain

The last attempt of the appellants to escape the result of the court's language, was to urge that the subsequent encumbrance in the instant case was given to secure a pre-existing obligation, hence the respondent was not an encumbrancer for value, and could not, therefore, claim priority over the appellant's voluntary advances. The court's answer to this contention is what most courts would say; cases and text writers make no distinction between a junior mortgage made for a present obligation or one made to secure a pre-existing debt.¹⁰ A confirming statement of the rule is found in 1 Jones, *Mortgages* (8th ed.) § 453.¹¹

In deciding the *Elmendorf* case the Washington Court settled the question of optional future advances on mortgages insofar as advances made with actual notice of subsequent encumbrances are concerned. What would have happened if there had been only a constructive notice was left to be decided when an actual case involving the question arose. To venture in a little prophesy, the writer thinks the Washington Court will probably say that one making future advances on a mortgage at his option is assured his prior claim until such time as he had actual notice of a subsequent encumbrance. This feeling is predicated upon the court's hesitancy to renounce the majority rule, as illustrated by the statement in the instant case, that *were it not for such overwhelming authority to the contrary*, they would be inclined to hold that the appellant's rights are superior to those of a junior encumbrancer even as to advances made after knowledge of the junior mortgage.¹² The Washington Court is not alone in this view.¹³ Mr. Pomeroy in his treatise on Equity Jurisprudence says, that this view is based upon the theory that the executory agreement of the mortgagee creates a full and perfect lien in equity, and good against all persons charged with notice, and that recordation furnished such notice affecting all subsequent encumbrances.¹⁴ But when it is at the will of the mortgagee, and at his will only that future advances will be made, how can it be said that recording the mortgage will give constructive notice of that will? It seems to the writer that this would place the possible junior encumbrancer in too unfavorable a position.

what advances or liabilities *have been made or incurred*. The record of a subsequent mortgage or conveyance, or the docketing of a subsequent judgment is not a constructive notice of its existence to such prior mortgagee. The prior mortgage, therefore, duly recorded, has a preference over subsequent recorded mortgages or conveyances, or subsequent docketed judgments, not only for advances previously made, but also for advances made after their recording or docketing *without notice thereof*." (italics by the court.)

¹⁰ The court cites *Reidy v. Collins*, 134 Cal. App. 713, 26 P. (2d) 712 (1933), in which was said: "Where a mortgagee makes advances which it is optional with him to make his lien for such as are made after actual notice of a junior encumbrance will be postponed to that of the latter. And judgment liens are within the same rule." A judgment lien can be a lien for a pre-existing debt, and, as such, would be analagous to the junior incumbrance in the *Elmendorf* Case.

¹¹ ". . . the mortgagee not being bound by his contract to make the indorsements or future advances, the equity of a junior encumbrancer for an existing debt, or of an attaching creditor acquires a lien upon the property as it then is . . ."

¹² *Supra*, note 8.

¹³ 4 POMEROY, EQUITY JURISPRUDENCE (5th ed. 1941) § 1199.

¹⁴ *Ibid.*

It in effect warns him that if the first mortgagee sees fit to advance money after the junior lien attached, that such junior liens must take a secondary position, in spite of the fact that his lien attached prior to the later advance by the first mortgagee. As to the rights of the junior encumbrancer, that would mean that the protection derived from an option clause would not be available. The mortgagee could still make optional advances at will, but such advances as were actually made would be treated as if they were obligatory, and the junior encumbrancer's lien would be subjected to them.¹⁵ Such a situation would without doubt make the task of the court much simpler, but would only be just if we abolish option clauses in this type of mortgage. If we are to retain the law of future advances as it is, i. e., recognizing mortgages with option clauses, then we cannot say that recording of such mortgages will operate as constructive notice sufficient to establish the priority of future advances under the option clause even over junior encumbrances antedating the advance. This would result in holding that the mortgage for optional future advances becomes an effective lien from the time of its execution, like a mortgage for a present advance, and contrary to the general rule. So to hold would be not only contrary to the general rule, but also, in the writer's opinion, unreasonably burdensome upon the junior encumbrancer. These criticisms, well known as they are, must have prompted the court to follow the majority rule. If this be true, what is the basis of their preference, which they refuse to follow?

We may say, however, that so far as the opinion in the *Elmendorf* case went, it was an accurate statement of the prevailing rule as regards future advances at the option of the mortgagee.

So far as the *Elmendorf* case is concerned, it merely touched on the ultimate phase of a much broader rule, which is that "Future advances on mortgages are recognized as being secured by the mortgage lien." Of course, there are many qualifications to this statement, and to see how the rule has been employed in Washington will necessitate a consideration of earlier cases.

*Home Savings and Loan Assn. v. Burton*¹⁶ is the landmark case on this doctrine in Washington. The case involved the question of priority between a recorded mortgage for future advances and mechanics' liens. But perhaps it would be better to show how the problem arose. The defendant Burton planned to build a hotel, and for the purpose of obtaining part of the money, solicited subscriptions about the city. Receiving a substantial sum, he made arrangements to purchase a building site, and employed an architect to draw up the plans and specifications for the building. This done, he applied to the plaintiff for a loan of \$16,000 to be used in the construction of the building. The plaintiff agreed to make the loan provided the defendant Burton executed a mortgage as security, upon the building site and upon which the hotel was to be erected. It was agreed between the parties that it was to be a mortgage for \$16,000, but that it was to be treated in part as a mortgage for future advances. This mortgage was executed and duly recorded. The plaintiff advanced \$2,000 to the mortgagor upon execution of the mortgage, and the balance was to be used in

¹⁵ 1 JONES, MORTGAGES (8th ed. 1928) § 454.

¹⁶ 20 Wash. 688, 56 Pac. 940 (1899).

construction of the building. Periodic advances were arranged for as the building progressed. After the recording of the mortgage, Burton contracted with a construction company to erect the building, and immediately thereafter the work began. Before completion of the work, Burton absconded, and the construction company stopped work because of Burton's breach of the building contract. Then these contractors, together with sub-contractors, materialmen, and laborers filed mechanics' liens for the amounts due them.

After the filing of the lien claims, the Loan Company brought this action to foreclose its mortgage, and made all lien claimants parties defendant with Burton. The Loan Company claimed that the amount due it was the amount stated in the mortgage, and stated further that the mortgage would be declared paramount to the liens claimed by the defendants. The trial court rendered a decree establishing priority of the mechanics' liens, and declared that the Loan Company's claim was paramount only to the extent of monies actually advanced at the time of the execution of the mortgage, that is to say, for \$2,000.

Upon appeal, the Loan Company naturally urged that the decree of the trial court was in error in granting it a priority for only so much as was actually advanced at the execution of the mortgage, and Section 1666 of the General Statutes was cited in support of this contention. This statute provided that:

"The liens provided for . . . are preferred to any lien, mortgage, or other encumbrance which may have attached subsequent to the time when the building, improvement, or structure was commenced, work done, or materials were commenced to be furnished; also to any lien, mortgage, or other encumbrance, of which the lien holder had no notice, and was unrecorded at the time the building, improvement, or structure was commenced, work done, or the materials were commenced to be furnished."¹⁷

This statute, the court said, was clear and unequivocal, and did not need a construction to determine its meaning. Furthermore, when the statute provided that the liens are preferred over any mortgage, lien or encumbrance of which the lien claimant had no notice or was unrecorded, it also provided, in effect, that such liens will not be preferred over mortgages or liens which were recorded, or of which the subsequent lien claimant had notice. This statute protects mechanics' liens only to the extent that they are representative of work or material furnished without actual notice of a preceding encumbrance. The court's holding on this point was supported by Mr. Jones in his work on Liens.¹⁸ Not depending solely upon the authority of a text writer, the court had the earlier Washington case of *Huttig Bros. Mfg. Co. v. Denny Hotel Co.*,¹⁹ in which was said:

"Under the provisions of our statutes a materialman can only claim a lien from the time he commenced to furnish materials for the building, and if such time is subsequent to the creation of the mortgage lien, of which he had notice, his claim for materials is subject thereto."

¹⁷ This statute is now REM. REV. STAT. § 1132.

¹⁸ 2 JONES, LIENS (2d ed. 1894) § 1460, p. 441.

¹⁹ 6 Wash. 122, 32 Pac. 1073 (1893).

The respondents acknowledged the rule as stated in regard to mechanics' liens, but they nevertheless maintained that the Loan Company's priority applies only to the money advanced prior to the commencement of the work upon the building. They held to the proposition that a mortgage given to secure future advances became a charge upon the land, not at the time of its execution, but at the time when the advances were actually made, and that until such time as the advances are made, neither the land described by the mortgage, nor the parties to it, nor third persons are bound by it. Further, it was maintained that the record of this type of mortgage is not constructive notice to subsequent encumbrancers. They cited a number of cases from other jurisdictions in support of their position.²⁰

This contention threw open to the court the whole problem of future advances, giving it an opportunity to declare what the law is in this jurisdiction. The cases cited by the respondents, said the court, were against the great weight of authority, and were based on the erroneous view as to the real nature of equitable liens, and the effect of the recording acts. Mr. Pomeroy discussed these cases, and stated his disapproval of their holding in the following language:

"The fundamental error of this view, in my opinion, consists in its mistaken conception of the nature of an equitable lien, in regarding the lien as arising at and from *the act of making the advance*, instead of from the previous executory agreement by which the land was bound as security for the future advances."²¹

The rule urged by the respondents is acceptable insofar as it applies to future advances at the option of the mortgagee, but where the mortgage stipulates that it was executed as security for a specific amount, most courts interpret it to be obligatory upon the mortgagee to advance such funds. Being obligatory, the mortgage is given priority over mechanics' liens and other junior encumbrances.²² And, adopting this view in the instant case, the court said, "There being no doubt then, that mortgages to secure future advances are valid liens, we think that, under our statute, they are just as effectual against subsequent encumbrances as are mortgages to secure a present indebtedness."²³ In support of this language the court cited a California case, *Tapia v. Demartini*, which said,

"It is firmly settled by a long line of decisions that a mortgage made in good faith to cover future advancements, is valid, not only as between the immediate parties to the instrument, but as against subsequent purchasers or encumbrancers, if properly recorded."²⁴

Other cases to the same effect, from various jurisdictions, were cited in support of this rule.²⁵ Judgment was, therefore, reversed, permitting

²⁰ 20 Wash. 688, at p. 697.

²¹ 3 POMEROY, EQUITY JURISPRUDENCE (2d ed. 1892) § 1199, and note.

²² 4 POMEROY, EQUITY JURISPRUDENCE (5th ed. 1941) § 1199b.

²³ 20 Wash. 688, at p. 699.

²⁴ 77 Cal. 383, 19 Pac. 641 (1888).

²⁵ *Kiene v. Hodge*, 90 Iowa 212, 57 N. W. 717 (1894); *Hill v. Aldrich*, 48 Minn. 73, 50 N. W. 1020 (1892); *Wisconsin Planing Mill Co. v. Schuda*, 72 Wis. 277, 39 N. W. 558 (1888).

the Home Savings and Loan Assn. to have a prior claim not only for the money advanced at the time of the execution of the mortgage, but also for all sums advanced under the mortgage. The mortgage reciting a specific amount, was held to give ample notice to all persons of the amount of the claim, and the mortgagee is entitled to a priority up to that amount.

This case, as was said before, was the landmark case in Washington on the doctrine of future advances. While it was not the first case to touch upon the problem,²⁶ it did define the rule as it was to be applied in Washington henceforth.

Shortly after the *Home Savings and Loan* decision, a similar problem arose in *Stetson-Post Mill Co. v. Brown*.²⁷ In that case the court merely stated that it followed the solution furnished in *Home Savings and Loan Assn. v. Burton*, and let it go at that.

The next case in Washington, in which any extensive consideration of the problem was necessary was in *Andersonian Investment Co. v. Jones*.²⁸ Here a mortgage was given for \$25,000 to secure advances for the construction of a building. The mortgagee advanced only about \$13,000 on the mortgage, and then later sought to bring within the mortgage a loan to the contractor on his personal credit, to the extent of \$10,000. The mortgagor was not a party to this latter agreement. The court ruled that, as the mortgagor was not a party to the agreement, it was not within the contemplation of the mortgage contract to cover his advance, and that the mortgagee had a lien only for the sum actually advanced on the mortgage. This would permit subsequent encumbrancers to come in with their lien claims directly behind the mortgagee's prior claim for the amount actually advanced.

In *Schoemer v. Zeran*²⁹ we have the holder of an overdue mortgage agreeing to take another mortgage in its place covering the total due him, plus \$1,000 which he further agreed to advance. This future advance was to pay for labor and materials used in construction of a building, and the mortgage so stipulated. Thus the second mortgage was one for a pre-existing debt plus a future advance. The mortgagee made several advances subsequently, but only a part of these advances went to pay for materials and labor as required by the terms of the mortgage, and by far the greater part of these later advances were absolutely without the scope of the future advances clause in such mortgage. In a later action to foreclose a mechanics lien subsequently accruing, it was held that although the mortgage was not intitled to priority for the full face value of the mortgage, having failed to make the future advances according to the mortgage terms, yet he was entitled to show the amount of his first mortgage, the advances actually made prior to the second, and such portion of the last advancement that was properly applied, and was entitled to priority for such amount. Thus he was entitled to preference for the entire pre-existing debt, and only such portion of the \$1,000 as he actually applied properly. This is in keeping with the general view as adhered to in Washington.

²⁶ *Supra*, note 18.

²⁷ 21 Wash. 619, 59 Pac. 507 (1899).

²⁸ 104 Wash. 142, 176 Pac. 17 (1918).

²⁹ 126 Wash. 219, 217 Pac. 1009 (1923).

These few cases represent substantially all of the law on future advances on mortgages in Washington. True, there are not many cases, but the few that are on the record display a consistent handling of the problem in line with what seems to be the majority holding on all phases of the problem. The only question which is as yet unsettled in this jurisdiction is the one the court refused to answer in the *Elmendorf* case. The question is, "What effect will the recording of a junior encumbrance have upon the rights of the mortgagee who advances funds at his option subsequent to the recording of the junior encumbrance, but without actual knowledge of the subsequent encumbrance?" This question was passed over in the *Elmendorf* case because, knowledge being admitted, the court did not have to answer it. But when the occasion does arise, it is the writer's guess that the Washington court will follow the majority, as it has in all the other phases of the problem of future advances, and declare that unless the mortgagee making the voluntary advances has actual notice of the subsequent lien, he will be protected as to those voluntary advances.

JOHN B. KRILICH.

RECOVERY OF DAMAGES FOR PRIVATE NUISANCE

With a reversal of position amounting almost to defiance of precedent, the majority opinion in *Powell v. Superior Portland Cement, Inc.*¹ denies damages for injury caused to respondent's premises by dust from appellant's plant at Concrete, Washington. The plant, in operation since 1908, is the main industry of the town, at least half of its residents being economically dependent upon the plant. Respondent, who had resided in Concrete since 1907, in 1934 purchased a home within three blocks of the cement plant, and lived therein until August 1938, when he left Concrete. The home, partially furnished, has been rented since 1938.

The respondent brought suit in which he asked for an injunction against the plant and damages for injury to the property and for personal discomfort caused by the dust blown from the appellant's kilns. Injunctive relief was properly² denied by trial court, which, however, awarded five hundred dollars for damages sustained. On appeal, the Supreme Court unanimously upheld that part of the decision denying the injunction, but it denied³ recovery for damages, as indicated above, and reversed the trial court's decision to that extent.

Essentially, the problem, as viewed by the majority, is whether or not an individual buying property in an industrial community can col-

¹ 115 Wash. Dec. 12, 129 P. (2d) 536 (1942).

² *Bartel v. Ridgefield Lumber Co.*, 131 Wash. 183, 229 Pac. 306, 37 A. L. R. 683 (1924); *Mattson v. Defiance Lumber Co.*, 154 Wash. 503, 282 Pac. 848 (1929); see note, 5 WASH. L. REV. 76.

³ There is one dissenting opinion and three judges concurred in two concurring opinions.