

Washington Law Review

Volume 19 | Number 3

7-1-1944

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Recommended Citation

Frank C. Latcham, Comment, *Mortgages of Personal Property to Be Subsequently Acquired*, 19 Wash. L. Rev. & St. B.J. 160 (1944).

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WASHINGTON LAW REVIEW

and

STATE BAR JOURNAL

*Published Quarterly, in January, April, July and November of Each Year
by the Washington Law Review Association, at the Law School
of the University of Washington. Founded by John T.
Condon, First Dean of the Law School.*

SUBSCRIPTION PRICE: \$1.20 PER ANNUM.

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COMMENT

MORTGAGES OF PERSONAL PROPERTY TO BE SUBSEQUENTLY ACQUIRED

Since a man cannot transfer what is not his, a sale of property to be subsequently acquired by the vendor is ordinarily given effect only as a contract to sell such goods after they have been acquired. Such a bargain, under the law of sales, is not self-operating to pass the property in future goods to the purchaser on their mere acquisition by the seller, but requires a subsequent act of performance by the seller assented to by the buyer to carry out the obligation, usually termed a subsequent act of appropriation.¹

¹ VOLD, SALES (1931) §§ 42-44, p. 103; REM. REV. STAT. § 5836-5. Note an exception to this general rule in the "potential existence doctrine" now eliminated by the Sales Act, REM. REV. STAT. § 5836-1 *et seq.*, cf. WILLISTON, SALES (2d ed., 1924) § 136.

The most important exception to this rule is the doctrine of equitable mortgages first discussed in the important English case of *Holroyd v. Marshall* decided by the House of Lords in 1861.² The doctrine, briefly stated, lays down the rule that, although a mortgage of property to be subsequently acquired by the mortgagor is void at law, it is given effect in equity as an implied contract to pledge such property as security when the mortgagor acquires it, so that an equitable mortgage attaches to such property when so acquired in accordance with the doctrine of equitable mortgages. The rule is usually said to rest upon the broader equitable basis of specific performance so that when the property is later acquired by the debtor the creditor's equitable lien at once attaches.³

Problems resulting from mortgages on after acquired property usually arise between the mortgagee and the creditors or purchasers of the mortgagor claiming their rights in the property after title has been acquired by the mortgagor. In a recent Washington case, *Reconstruction Finance Corp. v. Hambright*,⁴ however, a somewhat different problem arose. In that case the buyer under a conditional sales contract of personal property purchased a truck which came within the scope of an after acquired property clause of a mortgage on the buyer's business. A judgment creditor of the mortgagor then asserted a prior right over the mortgagee to the mortgagor's interest in the property before the mortgagor had acquired the legal title under the contract. Two problems thus present themselves: *first*, what is the effect of the chattel mortgage on after acquired property; and, *second*, what is the interests of the conditional sales vendee; is it a present vested interest or is it merely a right to acquire property in the future? It is the purpose here to present a review of the Washington law on these questions as it pertains, for the most part, to chattel mortgages, but with a few speculations as to real property mortgages.

The facts of the *Hambright* case are these: A and wife, operators of a laundry business, received a loan from the Reconstruction Finance Corporation and gave a mortgage back which listed all the machinery and equipment used in the business, including one Ford panel truck, and also certain other items described as follows: ". . . all other personal property of a like nature hereafter acquired for use in connection with the mortgagor's business." A few months after the execution of the mortgage the R.F.C. gave a written release of the Ford truck from the lien of the mortgage so that the mortgagors could trade it in on a new Chevrolet truck purchased on a conditional sales contract. The parties to the mortgage entered into an agreement whereby the mortgagors were to execute a chattel mortgage covering the Chevrolet truck as soon as they acquired title thereto.

While the Chevrolet truck was still being paid for under the conditional sales contract, a general creditor of A and wife obtained a

² 10 H. L. Cas. 191, 11 Eng. Reprint, 999. In JONES ON CHATTEL MORTGAGES AND CONDITIONAL SALES (Bowers ed.) § 173, it is said that Judge Story had announced the same doctrine in the leading American case of *Winslow v. Mitchell*, 2 Story 630, fifteen years prior to the decision of *Holroyd v. Mitchell*.

³ WALSH, MORTGAGES (1934) § 10, p. 56; Cf., also, the reasoning in *Straus v. Wilsonian Investment Co.*, 177 Wash. 167, 31 P. (2d) 516 (1934).

⁴ 16 Wn. (2d) 81, 133 P. (2d) 278 (1943).

judgment against them for a debt arising after the execution of the chattel mortgage to the R.F.C. The creditor, having no knowledge of the unrecorded agreement to mortgage the truck with the R.F.C., attached the truck. The R.F.C. immediately contested the attachment and, by stipulation of the parties, the rights to the truck were adjudicated in an action instituted by the R.F.C. to foreclose the chattel mortgage. A trial court found that the truck was subject to the chattel mortgage and that the lien of the R.F.C. was superior to any lien that the creditor might have.

On appeal, the creditor argued that the chattel mortgage could not cover after acquired property when the property is not described in the mortgage. The Chevrolet truck, he said, is not such a part of an establishment, like repairs to machinery, as to bring it within the after acquired property clause of the R.F.C. mortgage.⁵ Furthermore, since the agreement to place the Chevrolet truck within the mortgage when title should be acquired was not recorded, the defendant did not have even constructive notice of a mortgage on the truck so that any mortgage right the R.F.C. might claim would be void as to the defendant under the chattel mortgage statutes.⁶

The Supreme Court affirmed the trial court's decision and held that the Chevrolet truck was covered by the after acquired property clause in the mortgage. The truck, said the court, was expressly designed for that type of business; was openly used for deliveries, and, furthermore, the inclusion of the Ford truck in the chattel mortgage showed that a delivery truck was used in the business. Thus the case was brought squarely within the court's former decisions holding that replacements and additions to machinery and property generally used in the business come within the scope of an after acquired property clause which purports to cover future property acquired in connection with the mortgagor's business.⁷

The court also pointed out that the interest of a conditional sales vendee could be the subject of a chattel mortgage, and the subject of an attachment. The mortgagee's equitable interest through the after acquired property clause was held to be superior to any lien the attaching creditor might have, however, because, a judgment creditor was held merely to stand in the shoes of a judgment debtor and therefore: "an outstanding equity or prior unrecorded claim or interest in property takes precedence over the lien of a judgment creditor purchasing under its own levy and sale."⁸

The agreement to release the Ford truck and replace the Chevrolet truck under the mortgage when title was acquired by the mortgagor

⁵ The previous cases in the field with the exception of the *Straus* case, *supra*, n. 3, and *Hancock Mut. Life Ins. Co. v. Lewis Realty & Inv. Corp.*, 173 Wash. 444, 23 P. (2d) 572 (1933), dealt with additions and replacements to machinery in industrial plants and additional trackage to railway lines. Cf. *Bank of Calif. v. Clear Lake Lumber Co.*, 146 Wash. 543, 264 P. (2d) 705 (1928); *Marshall-Paine Veneer Co. v. Vancouver Plywood Co.*, 177 Wash. 503, 32 P. (2d) 530 (1934); *Hinchman v. Point Defiance Ry. Co.*, 14 Wash. 349, 44 Pac. 867 (1896).

⁶ REM. REV. STAT. § 3780 *et seq.*

⁷ Cf. cases under n. 5.

⁸ This is the general rule in Washington as to judgment creditors. *Anderson Buick Co. v. Cook*, 7 Wn. (2d) 632, 110 P. (2d) 657 (1943); *Ransom v. Wickstrom*, 84 Wash. 419, 146 Pac. 1041, L. R. A. 1916A 588 (1915).

was held to be unimportant in this case because the after acquired property clause in the mortgage already gave the mortgagee an interest in the truck.

In order that the principal case could be affirmed, it was necessary that affirmative answers be given to the two questions hereinbefore mentioned. That is, the court had to find first, that one may execute a present chattel mortgage that will cover after acquired property and that this property was covered by the mortgage, and, second, that a conditional sales vendee has an interest which may be the subject of a present mortgage. The court could rely on several previous Washington cases to give support to decisions on both of the questions.

Although not the first case in the field, *Straus v. Wilsonian Investment Co.* presents the most far-reaching application of the after acquired property clause.⁹ This case was an action to foreclose a mortgage on the Wilsonian Apartment Hotel and its equipment and was contested by one who had obtained, not as a bona fide purchaser, bills of sale to equipment put in the hotel by successors of the mortgagor. The mortgage listed all the furniture and equipment of the hotel and all replacements thereto under a clause which read in part: ". . . lien of this indenture . . . upon the furniture and fixtures herein provided to be installed by the mortgagors and any and all additional furniture and furnishings which may be installed in said building by said mortgagors . . . or their assigns . . . shall at all times during the lifetime of this indebtedness be superior and paramount to any lien . . . of anyone having any interest in said furniture and furnishings." The mortgage further provided that all agreements therein should be binding upon the heirs, executors, administrators and assigns of the mortgagors. The court held that the property claimed by the intervening purchaser was part of the property liened by the mortgage although the property was purchased for the hotel after the mortgage was executed and by assignees of the mortgagors.

Following the generally recognized rule on mortgages of after acquired property, the court said, ". . . although a mortgage on after acquired property is void at law because it has nothing to operate upon, still equity treats such conveyance as in the nature of an executory contract, to take effect and attach to the subject-matter as soon as it comes into existence . . ."

It is interesting to note that the court found the case to be an exception to the usual holding that ". . . the covenant of the mortgagor to cause after acquired property to feed the mortgage is ordinarily construed to apply only to property subsequently acquired by the mortgagor and not to include property acquired by a successor."¹⁰ The rule when this point is stated in *Trust Co. of America v. City of Rhinelander*:¹¹ "As the mortgagor cannot expressly contract to mortgage the after acquired property of others, such property can never come within the mortgage by the force of such a contract alone, unaided by the rule of accession, estoppel, or some other equitable consideration." The Washington court seemed to find two reasons for

⁹ *Supra*, n. 3.

¹⁰ Cf. "After-Acquired Property Under Conflicting Corporate Mortgage Indentures," 13 MINN. L. REV. 81 (1929).

¹¹ 182 Fed. 64 (C. C., W. D. Wisc., 1910).

including the after acquired property of the subsequent purchasers within the mortgage.

The basis for the first reason was the agreement within the mortgage to repair and replace the hotel property.¹² Of this agreement, the court said: "The obligations cannot be said to be solely *in rem*, or personal to the mortgagors, but are more in the nature of warranties respecting the use and occupancy of the premises. To state it differently, the security of the debt is the entire establishment maintained as required by the mortgage. The lien is upon the entire hotel property . . ."

The second, and, perhaps, most important reason for the inclusion of the after acquired property within the scope of the mortgage was because the court found that such additions were accessions to the hotel property. The court stated: "Personal property of this nature so added to the establishment becomes an accession or an integral part, of the hotel property, which under the clear terms of the mortgage, is what was intended to be the security for the payment of the indebtedness."

The authors of the article in the *Minnesota Law Review*, above referred to,¹³ note the tendency of a few courts to hold that subsequent purchasers may feed the mortgage by basing their decisions on the theory that the after acquired property becomes an accession to the whole industrial plant or railroad. This, of course, is the manner in which the Washington court has applied the doctrine of accession to hotel property. But the authors maintain, however, that this broad theory of accession is against the weight of authority. Accession, the authors say, should be confined to physical annexation to specific, mortgaged chattels.¹⁴

Be that as it may, the broad theory of accession seems to be the principal reason for the court's holding that the property which the subsequent purchasers bought from the mortgagor was covered by the mortgage.¹⁵ The first reason that the court gives, that is, that the obligation in the mortgage to maintain the hotel premises is not personal to the mortgagors but applies to the subsequent purchasers, who took subject to the mortgage, seems to be a very broad statement and, it is submitted, is not a well reasoned basis for the decision.

Two other Washington cases dealing with replacements and additions to lumber plants clearly lay down the rule that after acquired

¹² The court said that there was a definite agreement in the mortgage that "from time to time furnishing and equipment would be repaired and replaced, to the end that the premises will be maintained at all times during the period of the indebtedness as a properly equipped apartment hotel."

¹³ *Supra*, n. 10.

¹⁴ The authors cite *Hinchman v. Point Defiance Ry. Co.*, 14 Wash. 349, 44 Pac. 867 (1896), wherein the after acquired property consisted in part, at least, of additional tracks to the rail line, as a proper example for the accession theory.

¹⁵ As authority for its accession rationale, the court cites *Bank of Calif. v. Clear Lake Lbr. Co.*, 146 Wash. 543, 264 P. (2d) 705 (1928). Speaking of repairs and replacements to a lumber mill, the court said in that case: "The after-acquired property did not, in any sense, become or remain new, different, or additional property, but rather became an integral part of the plant. Establishments such as this are continually requiring repairs, and to hold that the materials used in maintaining the plant as a going, efficient concern are free from the mortgage would soon cause the loss of the security of the mortgage."

property in the nature of repairs and supplies to machinery and equipment are subject to a mortgage clause including such future acquired property within its scope.¹⁶ Although a delivery truck used in a laundry business is not in the nature of a replacement to machinery, it was certainly contemplated by the mortgage for it is "personal property acquired in connection with the mortgagor's business." And since a delivery truck was commonly used as a part of the business, the mortgage would seem fairly to cover any replacement of the truck.

The second problem before the court in the *Hambright* case—the right of a conditional sales vendee to mortgage his interest in the property under the contract—has been considered and upheld by two previous Washington cases.¹⁷ A mere superficial survey of the problem might lead one to believe that a mortgage given by a conditional sales vendee is itself a mortgage upon property to be acquired in the future. However, the court did not so find in *Tope v. Brittain*.¹⁸ Here the conditional sales vendee mortgaged his interest in an automobile. After the mortgagor had acquired title to the car a judgment creditor of the mortgagor levied upon and sold the auto buying it in himself. The mortgagee brought an action to foreclose his mortgage and the creditor sought to enjoin that action. The court affirmed the dismissal of the bill in equity by the trial court. A mortgagor must possess some interest in the mortgaged property said the court, but ". . . the interest of a purchaser under a conditional sales contract in the subject matter of the contract, though a limited or special interest, is sufficient to support a chattel mortgage."

It is entirely possible that before the passage of the Uniform Sales Act, the court might have found that a mortgage by a conditional sales vendee was merely a mortgage on property to be acquired in the future.¹⁹ Following a minority view, it had been held in *Holt Mfg. Co. v. Jassaurd* that since title was reserved in the seller of a conditional sale the loss must fall on the seller.²⁰ The court refused to follow the general rule which gives the conditional vendee an equitable interest in the subject matter of the contract and places the risk of loss on the buyer. The court's refusal to find even an equitable interest in the conditional buyer seems to make the case irreconcilable with the *Tope* case wherein a conditional vendee was allowed to mortgage his interest in the property. The *Tope* case, however, although it does not mention *Holt Mfg. Co. v. Jassaurd*, seems to be merely an extension of the court's policy of limiting the decision in the *Holt* case. In *Kuhn v. Ambrose*,²¹ a case decided in 1933, the court upheld the right of a conditional vendee to make a valid and effective assignment of his interest under the contract. The decision states in part: "The vendor relies on *Holt v. Jassaurd*, in which we held that no title whatever passes under a conditional sale contract of personal property. We have, however, since receded somewhat from that position, and have later held that the vendee does have some interest in the chattel, and that

¹⁶ *Bank of Calif. v. Clear Lake Lbr. Co., Marshall-Paine Veneer Co. v. Vancouver Plywood Co.*, both *supra* n. 5.

¹⁷ *Tope v. Brittain*, 172 Wash. 556, 21 P. (2d) 241; *Snow v. Mitchell*, 2 Wn. (2d) 424, 97 P. (2d) 1097 (1940).

¹⁸ *Supra*, n. 17.

¹⁹ *Supra*, n. 1.

²⁰ 132 Wash. 667, 233 Pac. 35 (1925).

²¹ 171 Wash. 528, 18 P. (2d) 485 (1933).

such interest is subject to attachment.²² If the vendee's interest may be the subject of attachment, then it may also be subject to voluntary transfer, unless prohibited by the agreement of sale." Thus in the *Tope* case the court is merely following an already established policy of limiting the *Holt* decision.²³

Although the Washington cases have all dealt with after acquired property clauses in chattel mortgages, it is interesting to consider, while investigating the mortgageable interest of a conditional buyer of personal property, the possibility of whether a conditional vendee of a contract for the sale of land has an interest in the property sufficient to sustain a mortgage. The Washington court's treatment of the conditional buyer of realty under a forfeitable contract is closely analogous to the court treatment of the conditional buyer of personal property. In the year the *Holt* case came down, the court also decided the famous case of *Ashford v. Reese*²⁴ which refused the purchaser under a forfeitable contract for the sale of land any title, either legal or equitable, to the land until the full consideration is paid and, therefore, placed the risk of loss upon the vendor. But the court has qualified and limited the rule in the *Ashford* case in many subsequent decisions. In *State ex rel. Oatey Orchard Co. v. Superior Court*, the court held that creditors of the conditional vendee could levy on his interest in the property in the manner provided for the levy of a writ on real property.²⁵ The latest pronouncement of the court on the *Ashford* problem is *Lawson v. Helmich*, wherein the court found that the vendee had sufficient interest in the property to sue in trespass.²⁶

From the above discussion, it seems not unreasonable to say that the vendee under a forfeitable contract for the sale of land has a mortgageable interest in the land itself. If such a purchaser of realty has a property interest that may be attached in a manner similar to any real property, or that may be the basis for a suit in ejectment, it would

²² The court cites *Hess v. Starwich*, 149 Wash. 679, 277 Pac. 75 (1928).

²³ It is interesting to speculate whether the *Holt* case has any validity at all today, even in placing the risk of loss on the buyer. Both the *Kuhn* case and the *Hess* case, each of which were decided after the Sales Act, seem to assert the essential validity of the *Holt* decision. Each case speaks only of limiting the rule that no equitable interest passed to the conditional buyer. Neither case mentions section 22 of the Sales Act, however, which generally places the risk of loss of a completed sale upon the buyer and specifically says in subsection (a): "Where the delivery of the goods has been made to the buyer, or to a bailee for the buyer, in pursuance of the contract and the property in the goods has been retained by the seller merely to secure performance by the buyer of his obligations under the contract, the goods are at the buyer's risk from the time of such delivery." Professor Ayer, in his comment on the Sales Act, 2 WASH. L. REV. 65 (1925), at p. 162, discusses the problem and says that the *Holt* case should now be overruled. Note also *Gillingham v. Phelps*, 11 Wn. (2d) 492, 119 P. (2d) 914 (1941), which although not a case involving a conditional sales contract, nevertheless recognized the effect of section 22 as placing the risk of loss "on the person having the property in the goods at the time they are destroyed."

²⁴ 132 Wash. 649, 233 Pac. 29 (1925).

²⁵ 154 Wash. 10, 280 Pac. 350 (1929). REM. REV. STAT. § 228 (3) provides for attachment and constructive notice of a contingent interest in realty.

²⁶ 120 W. D. 160, 146 P. (2d) 537 (1944). Cf. also for comments on cases discussing the interest of the vendee under a forfeitable contract, 3 WASH. L. REV. 80 (1926), 4 WASH. L. REV. 85 (1927). Note also that in his concurring opinion in the *Oatey Orchard Co.* case, Judge French said that *Ashford v. Reese* should be specifically overruled. This has been the view of a continuous minority of the court.

seem that his mortgage should be more than a mere contract to mortgage in the future or an hypothecation which the mortgagor is estopped to deny when he acquires full title. The general rule is stated to be that: "Every kind of an interest in real estate may be mortgaged if it be subject to sale and assignment. It does not matter if it is a right in remainder or reversion, a contingent interest, or a possibility coupled with an interest, if it be an interest in the land itself."²⁷ Since the doctrine of *Ashford v. Reese* seems to be confined to purchasers under forfeitable contracts, there seems little doubt that purchaser under a non-forfeitable contract has a mortgageable interest in the land itself.²⁸

A review of the decision in Washington, shows that a chattel mortgage on after acquired property has been held to have a superior lien to three types of intervening parties: (1) to one who is not a bona fide purchaser of goods acquired by the mortgagor (or his successor) to replace or add to necessary machinery, furniture, or equipment of the mortgagor's business; (2) to prior general creditors of the mortgagor; and (3) to a judgment creditor of a conditional sales vendee before legal title has passed to the vendee. There is at least one additional question, therefore, which is still left to investigate, namely, which party shall prevail when the mortgagor, after acquiring title, sells to a bona fide purchaser for value, or, a bona fide encumbrancer for value?

If the mortgage on after acquired property has not been recorded, the authorities agree, and, indeed, the Washington court would have to so hold in view of the filing statute, that the mortgage is only good as between the parties. But if the mortgage has been recorded, it is submitted that no party, not even a bona fide purchaser of the after acquired property, should have an interest prior to that of the mortgagee. If the mortgage takes effect immediately as the property comes into being, why should not the mortgage on after acquired property be constructive notice to subsequent buyers?

The Washington court noted this problem in *Hancock Mut. Life. Ins. Co. v. Lewis Realty & Inv. Corp.*,²⁹ but failed to pass upon the question because it was not argued in the briefs. In that case the owner of an apartment house gave a mortgage on the building and all the furnishings then in the building or to be later acquired. The owner was then in the process of purchasing furniture from a company, the final delivery of which was made sometime after the above mentioned mortgage. The court determined that under its contract the owner acquired title to the furniture upon each delivery. After the final delivery, the furniture company took a chattel mortgage on the furniture for the remaining payments due upon it. The first mortgage was properly filed and recorded before the furniture company mortgage. Apparently the furniture company had no notice of the first mortgage and there-

²⁷ JONES, MORTGAGE OF REAL PROPERTY (8th ed., 1928) § 190. On the mortgagor being estopped to deny the mortgagee's interest in the property when the mortgagor acquires full title, or, as it is called, the doctrine of estoppel by deed, see *Weber v. Laidler*, 26 Wash. 144, 66 Pac. 400 (1901); WALSH, MORTGAGES § 31.

²⁸ *Dean v. Woodruff*, 200 Wash. 166, 93 P. (2d) 357 (1938): "The rule is that in a contract to purchase real estate if there is a forfeiture clause in the contract the loss must fall on the vendors unless the loss was the result of the vendee's negligence, and if there is no forfeiture the loss must fall on the vendee."

²⁹ 173 Wash. 444, 23 P. (2d) 572 (1933).

fore took its mortgage as a bona fide encumbrancer for value.

Although the court did not pass upon the point but merely assumed that the after acquired property clause of the first mortgage was valid, there is at least strong dictum to the effect that a duly recorded chattel mortgage covering after acquired property will take precedence over subsequent bona fide encumbrancers or purchasers.

The basis for much of the modern law on this problem comes from an early case before the New York Court of Appeals wherein it was decided that a mortgage given by a tenant to a third party on the lease and on chattels which might thereafter be placed on the leased premises was a good equitable mortgage against a subsequent purchaser for value without notice, since it had been duly filed under the New York statute, giving the purchaser constructive notice.³⁰ One authority in the field of mortgages says: ". . . a mortgage to cover later-acquired property duly filed under the statute operates on the property as of the date when it is acquired, like a mortgage made at that date, and should be held to come within the scope of the statute governing chattel mortgages."³¹

Walsh, in his work on chattel mortgages, reviews the applicable cases and concludes that although there have been some irregularities in the decisions, the authorities seem generally to be in accord with the statement that the filing of a mortgage on after acquired property is constructive notice to subsequent encumbrancers and purchasers in good faith.³²

Despite the theoretical logic, however, of the view that such properly filed mortgages are constructive notice to everyone, there is a practical difficulty present. A purchaser would not be likely to investigate a mortgage which has been filed some years before the mortgagor acquired the property in which the purchaser is interested.

It is possible, therefore, that the Washington court, as a matter of policy, might refuse to give these mortgages validity against the claims of bona fide purchasers. But it is submitted that there is nothing in the Washington statutes or past decisions to show that the court will not follow the general rule on this phase of the problem, especially since the court has been liberal in protecting the mortgagee and has some strong dictum in its decision on which to rely.³³

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³⁰ *Kribbs v. Alford*, 120 N. Y. 519, 24 N. E. 811 (1890).

³¹ WALSH, MORTGAGES, p. 60; cf. also JONES, CHATTEL MORTGAGES AND CONDITIONAL SALES, §. 277a.

³² WALSH, MORTGAGES, pp. 56-64. But see 13 MINN. L. REV. at p. 84, where it is said that such mortgages will be good against creditors but not against subsequent bona fide purchasers; however only meager authority is given for this statement.

³³ Cf. *Hancock Mut. Life Ins. Co. v. Lewis Realty & Inv. Corp.*, 173 Wash. 444, 23 P. (2d) 572 (1933). Note also, the *Clear Lake Lbr.* case where, although the court did not mention the constructive notice problem, a mortgage on after acquired property was held good as against general creditors of the company. This is strong inferential support to holding that the mortgage is constructive notice to bona fide purchasers from the mortgagor in view of REM. REV. STAT. § 3780: "A mortgage or personal property is void as against all creditors of the mortgagor, both existing and subsequent, whether or not they have or claim a lien upon such property, and against all subsequent purchasers, pledgees, and mortgagees and encumbrancers for value and in good faith, unless it is accompanied by the affidavit of the mortgagor that it is made in good faith . . . and unless it is acknowledged and filed within ten days from the time of the execution thereof . . ."