Washington Law Review

Volume 35
Number 2 *Washington Case Law—1959*

7-1-1960

Security Transactions

Yancey Reser

law but does indicate the extent to which the *Ellis* rules will be applied. It is to be hoped that any future Washington decisions in this area will contain an analysis in terms of these rules.

JOHN F. COLGROVE

SECURITY TRANSACTIONS

Security Transactions — Purchase-money Mortgages, Mechanic's Lien — Priorities. On occasion, a real estate contract vendee will have a mechanic or materialman perform work or furnish materials prior to the vendee's receiving record title in the property. The vendee may also grant a purchase-money mortgage on the same property. The purpose of this Casenote is to consider the priorities between the purchase-money mortgage and the mechanic's or material-man's lien in Washington. The matter has again been raised in the recent decision of *Nelson v. Bailey*.[1]

The mechanic's lien attaches, at the time the work is performed, to the interest in the land of the person who caused the work to be done.[2] If the person for whom work is performed has less than the fee, the lien will not ordinarily attach to the fee. For example, in the case of a mechanic or materialman who performs services for a lessee who is authorized by the terms of the lease to build, the lien attaches only to the lessee's interest and does not attach to the lessor's fee.[3] The Washington court in the lease case rejected an argument that the lessee was the agent of the lessor.[4] In the case of *Newell v. Vervaeke*[5]

used, and trusts to the judgment of the seller the selection of the article which shall be suitable for the intended purpose, there is an implied warranty that the article furnished shall be reasonably fit for the intended purpose. . . . But the converse of the proposition is equally the rule, namely, that when the article ordered is to be manufactured according to certain prescribed specifications, or is an article well known and defined in current trade, the contract is complied with when an article is furnished which is manufactured in accordance with the designated specifications, or is an article of the standard kind known to the trade, even though the seller may know the purposes for which it is intended to be used and it afterwards proves to be unfit or unsitable for the intended purpose." *Id.* at 605-06.

[1] 154 Wash. Dec. 153, 333 P.2d 757 (1959).

[2] RCW 60.04.030.

[3] Stetson-Post Mill Co. v. Brown, 21 Wash. 619, 59 Pac. 507 (1899); Colby & Dickinson, Inc. v. Baker, 145 Wash. 584, 261 Pac. 161 (1927).

[4] See note 3, *supra;* however, in Seattle Lighting Fixture Co. v. Broadway Cent. Market, 156 Wash. 189, 286 Pac. 43 (1930), the court held that a mechanic's lien did attach to the fee of the lessor in a lease which by its terms *required* the lessee to build.

[5] 189 Wash. 144, 63 P.2d 488 (1937). See also, Baker v. Sinclaire, 22 Wash. 462, 61 Pac. 170 (1900). A recorded conditional sale contract with forfeiture clause will prevent the lien from attaching to the fee, Mentzer v. Peters, 64 Wash. 540, 33 Pac. 1078 (1893); Iliff v. Forssell, 7 Wash. 225, 34 Pac. 928 (1893), even if the conditional sale contract requires that work be performed, Northwest Bridge Co. v. Tacoma Shipbuilding Co., 36 Wash. 333, 78 Pac. 996 (1904).

the Washington court held that as a general rule the work done under orders of a contract vendee will not support a lien on property as against the interest of the contract vendor. Upon termination of the vendee's rights the claim of lien fails.

A purchase-money mortgage arises out of a transaction whereby the seller conveys title to the buyer and receives back as a part of the same transaction a mortgage to secure the balance of the purchase price.[6] The general rule is that a purchase-money mortgage will receive priority over any lien, even though it is a mechanic's lien prior in time to the mortgage, which attached to the vendee's interest before the vendee received title.[7] The priority given to the purchase-money mortgagee, who is typically the vendor, seems fair, because the property is brought into the vendee's hands through the financing of the purchase-money mortgagee. In Washington a purchase-money mortgage will receive priority over an earlier judgment lien[8] attaching by the judgment debtor statute on after-acquired real property of the debtor.[9] Thus, for some purposes the Washington court has recognized the priority of purchase-money mortgages over prior-in-time liens attaching through the vendee mortgagor. It is also the general rule that a purchase-money mortgage has priority if it is in favor of a third person who advanced money paid to the vendor, provided the money was loaned for that purpose only.[10] The most satisfactory explanation of the purchase-money mortgagee's receiving priority over the prior-in-time mechanic's lien which attached to the vendee's interest before the vendee received title, is that when the vendee obtains title he takes only the mortgagor's estate. Thus, the mortgagor's estate is the only equity which can be subject to liens previously created by the vendee. The third person who advances purchase-money is said to stand in the shoes of the vendor.[11] Another explanation is "instantaneous seisin," the theory of which is that title rests in the grantee such a short time that the lien does not have time to attach.[12] This bit of fantasy is not helpful in developing an understanding of the problem. It does not work well in a lien theory state because under the lien theory title remains in the mortgagor.

[6] OSBORNE, MORTGAGES § 213 (1951).
[7] OSBORNE, MORTGAGES § 213 (1951). See also, Annot., 72 A.L.R. 1516 (1931).
[8] Bisbee v. Carey, 17 Wash. 224, 49 Pac. 220 (1897).
[9] RCW 4.56.190.
[10] New Jersey Bldg. & Loan & Ins. Co. v. Bachelor, 54 N.J. Eq. 600, 35 Atl. 745 (1896). See also, OSBORNE, MORTGAGES § 213 (1951); WALSH, MORTGAGES § 38 (1934).
[11] See note 10, *supra*.
[12] Keefe v. Cropper, 196 Iowa 1179, 194 N.W. 305 (1923). See also, OSBORNE, MORTGAGES § 213 (1951).

The Washington court has interpreted our mechanics' and materialmen's lien statute as creating a special problem, taking these liens outside of the general purchase-money mortgage-lien priority rule. The rationale of the court is that our mechanis' lien priority statute[13] gives the mechanic or materialman priority over any mortgage of which he does not have actual or constructive notice at the time his lien attaches. In the case of *Colby & Dickinson, Inc., v. McCullock*,[14] a materialman provided materials to a contract vendee prior to the vendee's receiving title. "Knowing" that work was in progress the mortgagee subsequently accepted a purchase-money and construction mortgage, which was recorded. As a part of the same transaction the title to the property was transferred to the vendee. The materialman prevailed over the purchase-money as well as the construction-loan part of the mortgage.

In the cases of *Mutual Sav. & Loan Ass'n v. Johnson*[15] and *Capital Savings & Loan Ass'n v. Vaughn Hardware Co.* [16] the facts were the same as in the *Colby & Dickinson* case except that the purchase-money mortgage and construction-loan mortgages were separate mortgages. By agreement between the mortgagees, the purchase-money mortgage was subordinate to the construction-loan mortgage. The purchase-money mortgagee was not a party to the appeal in either case. The materialmen's liens were held prior to both mortgage liens in each case. In *Stoneway Lumber Co. v. Lovenberg*[17] the facts were the same as in the *Mutual Sav.* and the *Capital Sav.* cases except that the mortgagee did *not* "know" that work was in progress when the mortgage was accepted. In fact, the materials were delivered only a few hours prior to the mortgage being recorded. The purchase-money mortgagee did appeal in this case. The materialman prevailed.[18]

However, there are circumstances in which a materialman who furnishes materials to a contract vendee prior to the vendee receiving title can lose to a subsequent purchase-money mortgagee. In *Hewitt*

[13] RCW 60.04.050.

[14] 145 Wash. 561, 261 Pac. 86 (1927).

[15] 153 Wash. 41, 279 Pac. 108 (1929).

[16] 163 Wash. 396, 1 P.2d 310 (1930).

[17] 156 Wash. 146, 286 Pac. 105 (1930).

[18] In Dunn v. Wolf, 154 Wash. 445, 282 Pac. 842 (1929), a purchase-money mortgage was granted when the vendee received title which was to be subordinate to a second mortgage to be granted at a later date. The purchase-money mortgage was recorded. The purchase-money mortgage prevailed over a subsequent mechanic's lien holder whose lien was prior to and superior to the second mortgage because it was the intent of the purchase-money mortgagee to be subordinate only to the second mortgage and not to mechanics' liens.

Lea Lumber Co. v. Sandell[19] the materialman "knew" that the person with whom he was dealing did not have title and "knew" the real owner-vendor. The vendor purchase-money mortgagee "knew" that work was in progress when he accepted the mortgage, but he prevailed. The reason or this result was that the materialman did not give to the owner or reputed owner the required notice of lien claim required by what is now RCW 60.04.020.[20] This notice by the materialman was not required in the cases previously discussed because the materialman was dealing with the contract vendee as owner.

The Washington court in the recent case of *Nelson v. Bailey*[21] again considered the purchase-money mortgage and mechanics' and materialmen's lien priority problem in a rather unusual factual pattern. In the *Nelson* case a contract vendee of real property, prior to receiving title, granted to a third party a purchase-money and construction mortgage which was recorded. Subsequently the vendee ordered materials from a materialman which were delivered to the property prior to the vendee's receiving title. The materialman dealt with the vendee as the owner of the property. The vendor then conveyed title to the vendee. The court determined that the mortgagee was entitled to priority because the materialman had constructive notice, through the pre-recording of the mortgage, of the encumbrance on the vendee's interest.[22] The mechanics' and materialmen's liens have priority by statute over any lien, mortgage or other encumbrance attaching subsequent to the time of the commencement of furnishing materials, and over those attaching prior to such time if not filed or recorded, if the lien claimant had no actual notice thereof.[23] In *Nelson* the court said that *notice* under "our mechanics' lien statute,"[24] either actual or constructive, is the important factor in determining priorities and that title is not a significant consideration. The court did not consider the fact that after the vendee receives title his interest is different, being greater than the interest to which the liens originally attached. If

---

[19] 66 Wash. 515, 119 Pac. 848 (1912).

[20] RCW 60.04.020 applies only to material men and not to mechanics.

[21] 154 Wash. Dec. 153, 333 P.2d 757 (1959).

[22] In recognizing the validity of the pre-recording of a real property mortgage, the court apparently considered the real property recording statute, RCW 65.08.070, and the after-acquired title statute, RCW 64.04.070. In the *Nelson* opinion, RCW 64.04.060, which states that the use of the word "heirs" is not necessary to convey a fee simple title, was cited, undoubtedly due to a printing error.

[23] RCW 60.04.050.

[24] 154 Wash. Dec. 153, 159, 338 P.2d 757, 761 (1959).

notice is to control priority, we must know what notice is and to whom it must be given.

The court distinguished the *Mutual Sav., Capital Sav.,* and *Stoneway Lumber Co.* cases from the *Nelson* case on two grounds. The first distinction was that the mortgages were recorded after the work commenced while in *Nelson* the mortgage was recorded prior to the work commencing. This distinction would only affect constructive notice to the materialman or mechanic, in the absence of actual notice, and certainly would not determine whether or not the mortgagee had notice that the work was in progress. The second distinguishing factor, the court said, was that in each of the cases the mortgagee "knew" that the work was in progress when the mortgage was taken. This distinction is questionable, since under the *Stoneway Lumber Co.* decision the purchase-money mortgagee who did not "know" that the work had commenced was subordinated to a materialman who delivered materials a few hours prior to the recording of the mortgage. The second distinction can be justified only if we treat the commencement of work by the mechanic or materialman as constructive notice to the mortgagee of the prior lien on the vendee's interest. The use of the words "knew" and "know" in the decisions is ambiguous and does not help in determining what constitutes notice.

The court held in all the above decisions that notice controls the priorities between a mortgagee and a mechanic's lien holder who performed work for a contract vendee. This seems to reject the traditional purchase-money mortgage priority theory.[25] Apparently the commencement of work by the materialman or mechanic will be constructive notice to the mortgagee whether or not he "knows" work has commenced. The only way that a purchase-money mortgagee is going to prevail over a mechanic's lien acquired by performing work for a contract vendee, short of actual notice, is to pre-record the mortgage prior to the deed to the vendee and prior to the commencement of work by the mechanic. In this respect Washington law is unique. The mortgagee has the additional possibility of prevailing over the materialman as indicated above in the *Hewitt Lea Lumber Co.* case. With notice being the sole criteria of determining priority it seems possible that any mortgagee, not just a purchase-money mortgagee, who follows the above procedure would prevail over a mechanic's or materialman's

[25] Cases from other jurisdictions which follow the general purchase-money mortgage priority doctrine were cited in the *Nelson* case, but the court apparently did not follow the reasoning of these cases.

lien holder. Draftsmen of purchase-money mortgages in Washington should be extremely thorough in determining whether or not there are in fact prior mechanics' or matterialmen's liens against the interest of the "reputed" owner-mortgagor.

YANCEY RESER

STATUTORY CONSTRUCTION

Statutory Construction—Retroactivity of Legislation—Workman's Compensation Act—Host-Guest statute. In *Hammack v. Monroe St. Lumber Co.*[1] the Washington court held that the 1957 legislative act[2] amending Washington's Workman's Compensation Act[3] and abolishing the immunity proviso contained therein would not be construed retroactively.

Appellant (plaintiff in trial court) was injured in a traffic accident due to the negligent operation of a truck driven by respondent's employee. The appellant sued for both personal injuries and property damage. As both parties were in the course of extrahazardous employment as defined by the act, the trial court dismissed the action. The dismissal was based on the immunity proviso which was then in effect: "[N]o action may be brought against any employer or any workman under this act as a third person if at the time of the accident such employer or such workman was in the course of any extrahazardous employment under this act."[4]

Upon appeal,[5] the supreme court reversed in part, holding that the immunity extended only to actions for personal injury and not to an action for property damage. The case was remanded for further findings to determine what had been the final disposition of the appellant's claim for compensation under the act.[6]

The case was pending in superior court on remand on the effective date of the repealing statute.[7] Appellant then claimed that the respondent was no longer entitled to the defense provided by the statutory immunity, but the trial court held that the immunity proviso was

---

[1] 154 Wash. Dec. 217, 339 P.2d 684 (1959).
[2] Wash. Sess. Laws 1957, c. 70 § 23.
[3] RCW title 51.
[4] Wash. Sess. Laws 1929, c. 132 § 1.
[5] Hammack v. Monroe St. Lumber Co., 49 Wn.2d 581, 303 P.2d 1095 (1956).
[6] The court's theory was that a rejection of the claim on the ground that the workman was not in the course of his employment would be res judicata in a subsequent action against the employer. Young v. Department of Labor & Indus., 200 Wash. 138, 93 P.2d 337 (1949); Prince v. Saginaw Logging Co., 197 Wash. 4, 84 P.2d 397 (1938).
[7] Technically, the 1957 act was an amendment which simply dropped the immunity provision and not a direct repealing act.