Mortgages

MORTGAGES

THE PROBLEM OF SUBROGATION—FULL STANDING AS A CREDITOR OR INDEMNITY

THE extent of the right to which one becomes subrogated, that being his intention, upon discharge of an obligation for another is a matter which has caused Texas courts some difficulty. The question in each case is whether the payor is subrogated to the full rights of the creditor, which often include interest and attorney's fees if suit is necessary, or whether he is merely entitled to indemnity. Often this decision is very important to the parties for the additional reason that it will determine which statute of limitations will run against the claim for subrogation. Full standing as a creditor carries with it four years[1] in which to enforce such rights; whereas, if the claimant is held entitled to indemnity alone, the statutory period is two years.[2]

The question was considered in *Buchanan v. Buchanan*[3] where plaintiff asserted a claim against the estate of a debtor whose debt in the principal sum had been evidenced by the usual promisory note but secured by a chattel mortgage upon plaintiff's automobile. To protect her property in the automobile plaintiff had paid to the creditor the face amount of the note. The court held that plaintiff did not by such payment become legal owner of the note so as to create between herself and the estate of deceased a contractual relationship for payment of interest and attorney's fees, but held that plaintiff's claim was, rather, an equitable one, arising out of an implied promise of deceased to indemnify plaintiff against loss to her property in the amount she was required to expend in such protection.

The court relied for precedent upon the case of *Faires v. Cock-*

[1] TEX. REV. CIV. STAT. ANN. (Vernon's, 1925) art. 5527.
[2] *Id.*, art. 5526.
[3] 205 S. W. (2d) 409 (Tex. Civ. App. 1947).

erell,[4] which established the general rule that subrogation gives indemnity and no more,[5] or in the words of the court: "Where one is subrogated to the securities held by the creditor he is not entitled to recover the rate of interest expressed in the judgment or note which is the evidence of the debt. The amount of the payment made with legal interest is the measure of recovery."[6]

It is important to note that the *Faires* case concerned joint obligors on a contract, one of whom had paid, in performance of the joint obligation, and sought contribution from the other. Under such a fact situation, an obviously fair and reasonable result was reached in allowing recovery only on implied promise.

The doctrine of the *Faires* case did not go unchallenged, however, for the Supreme Court in the case of *Fox v. Kroeger*[7] specifically criticized the *Faires* case because of failure to distinguish between rights of surties and indorsers and joint makers.[8] The court in the *Fox* case announced the rule to be:

> ". . . that where the surety pays the debt of the principal, he has his election to either pursue his legal remedies and bring an action on assumpsit, or the obligation implied by law in his favor for reimbursement by the principal; or he can prosecute an action on the very debt itself, and in either event he stands in the shoes of the original creditor as to any securities and rights of priority."[9]

As a result of the criticism of the *Faires* case by the Supreme Court in the *Fox* case, the Commission of Appeals in 1933 in the case of *Hanchett v. Ward*[10] spoke of the *Faires* case as overruled, and allowed agents of an insurance company, who had remitted premiums from their own pockets minus commissions, to be subro-

---

[4] 88 Tex. 428, 31 S. W. 190 (1895).

[5] Phipps v. Fuqua, 32 S. W. (2d) 660 (Tex. Civ. App. 1930) *writ of error refused.* See also, 39 TEX. JUR. 801.

[6] 88 Tex. 428, 437; 31 S. W. 190, 194 (1895).

[7] 119 Tex. 511, 35 S. W. (2d) 679 (1931).

[8] Gaines v. Gaines, 119 S. W. (2d) 427, 430 (Tex. Civ. App. 1938).

[9] 119 Tex. 511, 517, 35 S. W. (2d) 679, 681 (1931).

[10] 65 S. W. (2d) 268 (Tex. Comm. App. 1933).

gated to contract rights of the company upon policies issued to a policyholder.

Nor was this to be the final word on rights to pass by subrogation, for both lines of authority were followed and applied in the case of *Patterson v. Fuller*.[11] It was there held that two or four sureties on a note, who gave a new note in payment of the old note acquired against non-paying sureties a right of action, one, upon implied promise for reimbursement, or two, upon the old note itself, citing both the *Faires* and *Fox* cases, the former upon the proposition that execution of the second note gave the sureties so paying a right of action upon implied promise and relying upon the *Fox* case to sustain a possible suit upon note one.

It is the opinion of the writer that one seeking subrogation in Texas courts will receive substantial justice in the event his claim is valid, but the question as to how bountiful will be his recovery will depend upon whether that claim is classed as one entitling him to indemnity or to full standing as a creditor. It is further submitted that consideration of the problem in the light of the distinction between payment and purchase will substantially aid in determining which classification is to apply.

Subrogation—Extinguishment of Lien on Payment by Agent

The case of *Somerville v. Smith*[12] established an agency principle that affects the rights of one who pays the debt of another and seeks subrogation to the rights of the creditor. If the third party who pays is an agent of the debtor, he will be limited to recovery from that debtor to the amount expended rather than subrogated to rights of the creditor. This holding, while in accord with *Buchanan v. Buchanan*,[13] *supra*, reaches this result by application of a different principle.

In the *Somerville* case, Smith had purchased a refrigerator unit

[11] 110 S. W. (2d) 1230, 1232 (Tex. Civ. App. 1937).
[12] 200 S. W. (2d) 242 (Tex. Civ. App. 1947).
[13] 205 S. W. (2d) 409 (Tex. Civ. App. 1947).

from Ed Fredrich Sales Corporation, vendor, executing a promissory note and a chattel mortgage. Later defendant Smith got behind in his payments and traded the unit to one Sheeler for another unit, Sheeler agreeing to assume the balance unpaid against the first unit. Payment had not yet been made when plaintiff, at the request of Smith, purchased the old note and took a transfer of it from the payee along with an assignment of the chattel mortgage. Neither Smith nor Sheeler paid; so, plaintiff instituted suit against those two and McGuire, the latter having purchased the unit from Sheeler. Against McGuire, only foreclosure was sought.

McGuire plead that plaintiff acted as agent for Smith—in effect, that the plaintiff loaned Smith the money with which to pay the balance on the note, and the jury found the agency to exist. As a result, the trial court denied foreclosure against McGuire but allowed recovery against both Smith and Sheeler in the amount of the unpaid balance plus interest and attorney's fees as stipulated in the original note made by Smith.

The court sustained the judgment, holding the legal effect of the transaction, "... to be that Smith was indebted to plaintiff for repayment of the moneys so advanced for him. Plaintiff's cause of action was then not on the note, but for the amount paid out."[14]

The *Somerville* case has several loose ends but these are not the fault of the appellate court. Defendants Smith and Sheeler did not complain of the trial court's action in rendering judgment against them in an amount greater than indemnity. This discrepancy was pointed out by the appellate court. The opinion did not, however, discuss Sheeler's liability, his promise, in the nature of a third party creditor beneficiary contract, having been, in fact, to assume the unpaid balance on the refrigerator unit, presumably as claimed by the creditors against Smith rather than a promise to pay Somerville, the plaintiff.

For authority the court cited Corpus Juris Secundum, to the effect "that where the agent of the maker of a note takes up the

[14] 200 S. W. (2d) 242, 244 (Tex. Civ. App. 1947).

obligation with funds furnished by the maker, it will generally operate as a payment of the note"[15]

HOMESTEAD EXEMPTION V. PARTITION—OWELTY PAYMENTS

In *Travelers Insurance Company v. Nauert*[16] the court handled the problem of priority between a claim for homestead exemption and that of a lien claim which arose out of owelty payments in an equitable partition, and rendered an opinion upholding the lien claim that can be said to extend the doctrine of *Sayers v. Pyland.*[17]

Sayers v. Pyland held that where an undivided interest in land is dedicated by occupancy as a homestead, such homestead is held subject to the right of partition by other co-tenants. The husband and wife have the power, in effecting an agreed partition thereof, to subject the land awarded them to an incumbrance to the end that the land be equitably partitioned.

In the *Nauert* case, defendant's father devised land, one-half to his wife and one-fourteenth to each of seven children. The wife, by will, divided the land into four parts and devised them to four of the seven children on the condition that they pay certain sums to the other three children. One child, defendant here, with his wife, had been occupying land as a homestead. He was given a partition deed, reserving a lien in accordance with his mother's will, on execution of notes to secure and evidence his debt in favor of other children.

After some difficulty,[18] the court held that he and his wife could encumber the land with a deed of trust securing the notes.

---

[15] 10 C. J. S. 986 (1938).

[16] 200 S. W. (2d) 661 (Tex. Civ. App. 1942).

[17] 139 Tex. 57, 161 S. W. (2d) 769 (1942).

[18] The opinion, appearing in the 200 S. W. (2d) 661, was published in 1947, though it bears the date, Dec. 4, 1941, Rehearing Denied, April 30, 1942. On April 29, 1942, the Supreme Court delivered the opinion in the case of Sayers v. Pyland. The court believing its decision conflicted with that case, set aside the order overruling motion for rehearing on its own motion, and on reconsideration this result was reached. The delay in printing resulted from a belief by the court that the doctrine of the *Sayers* case was not extended. However, several years later upon request of appellant's attorney, this opinion was certified to West Publishing Company.

As a result of this hard found conclusion, the insurance company was adjudged the owner of the land in a trespass to try title suit, its claim being founded upon sale and foreclosure under the said deed of trust.

It is believed that this opinion does extend the doctrine of the *Sayers* case in that here the homestead had previously attached to an interest owned absolutely by the mortgagor and it was to take an additional undivided interest under devise that the mortgagor pledged both his newly acquired interest and his previous absolute interest to which homestead rights had attached.

Estoppel of Successors to Grantor to Assert Superior Title to Purchaser from Grantee on Default of Land Contract

In *Wickwire-Mitchell Royalty Trust v. Taylor*[19] the court found successors to an original vendor who had encouraged his vendee to sell mineral rights "like you had it paid for; like it was yours," estopped from asserting superior title upon reconveyance by the vendee and a subsequent transfer to said successors.

In this case one McDaniel had conveyed to Barnett, reserving a vendor's lien. While in possession, Barnett, encouraged by McDaniel to do so, conveyed mineral rights to Reed, from whom appellants derived title. Prior to the conveyance by Reed to appellants, Barnett reconveyed to McDaniel; however, this conveyance remained unrecorded until after the conveyance from Reed to appellants. Appellees, plaintiffs in an action of trespass to try title, were successors in a chain of transfer from McDaniel; however, in their deed, the title to certain mineral rights was excepted from the general warranty.

Between the parties to the suit appellants stood in the better position as far as notice[20] was concerned, their deed being of record at the time appellees took, and appellees having notice by exception in their deed.

---

[19] 200 S. W. (2d) 441 (Tex. Civ. App. 1947).

[20] 14 Tex. Jur. 970 (1931).

The court first found that as a result of his acts the grantor, McDaniel, was estopped to assert superior title to that of Reed, purchaser of the minerals, or his transferees, the appellants here. Then the court adopted into Texas law the doctrine stated in *Corpus Juris Secudum* that "An estoppel of a grantor to assert title to property extends to his grantee."[21]

Thus was the court able to reverse and hold for appellants, they having relied upon the action of the original grantor of all parties. The court, however, recognized the general rule to be that where a vendee defaults in the payment of the purchase money, the vendor may, when it is not inequitable, rescind.

The opinion did not raise the question of constructive notice to the mineral purchasers by recordation of the land cotract between McDaniel and Barnett. The words, "Like you had it paid for; like it was yours" leave a little to be desired as an estoppel situation, as it seems to this writer that there is inherent in such statements, when made in the presence of a prospective purchaser, notice that he who is being urged to sell does not own. It is submitted that apparent authority would have been a better basis for this decision.

Subrogation—Rights Acquired Under Assignment Of a Deed of Trust

The strength of a power of sale in a deed of trust was illustrated somewhat forcefully in the case of *Sohio Petroleum Co. v. Gunter*[22] where title to a subsequently conveyed undivided interest in oil, gas, and other minerals was cut off upon failure of the grantor of said deed of trust to perform conditions therein. This result was reached even though the note evidencing the debt was cancelled in an assignment of said deed of trust.

W. L. Gunter owned land on which he executed and delivered to the trustee of the Federal Land Bank of Houston a deed of trust

[21] 31 C. J. S. 401.

[22] 205 S. W. (2d) 110 (Tex. Civ. App. 1947).

to secure payment of a note, and to renew and extend the balance due on the amortization plan of a certain note previously executed against the property.

Thereafter, he executed and delivered to two purchasers a deed of an undivided interest in gas, oil, and other minerals. Subsequently, the bank transferred and assigned to one Miss Tompkins the unpaid balance of said indebtedness and the deed of trust lien securing payment. The note evidencing the debt was cancelled. In the transfer and assignment there was included a provision for subrogation to all rights of the bank.

Prior to these assignments, W. L. Gunter executed and delivered to Miss Tompkins a new deed of trust to secure the payment of the indebtedness, it being renewed and extended, and conditioned upon new and different provisions in regard to interest and payment.

Later, the trustee, reciting default and sale under the original deed of trust, deeded to Miss Tompkins, vendor to plaintiffs, Loyd Gunter and others. The latter then brought this suit in trespass to try title to oust claimants to the minerals under assignment from the purchasers of W. L. Gunter. They were successful.

The court held that the original lien had not been permitted to lapse and that the rights of Miss Tompkins had been preserved by assignment of the debt and lien as well as by the provision for subrogation in the renewal and extension agreement. Takers under the mineral deed were held precluded by superior rights that passed under the deed of trust, duly recorded, and, in brief, by the fact that their position had not been changed by these transactions, there being no need to advise them personally of foreclosure, they being held to constructive notice of the foreclosure proceedings.

The court relied for authority, primarily on Corpus Juris, wherein the general rule is stated to be,

> "... that the original mortgage will not be discharged in the absence of a clear intention to that effect," and that, 'Where a note secured by a mortgage is taken up, at or before its maturity, and a new note substi-

tuted for it, the mortgage continues as security for the debt in its new form . . .' "[23]

This case has then reaffirmed Texas to the position that changes in the form, condition of payment, date of maturity, or interest rate, or cancellation of the original and substitution of a renewal note, will not impair the security under a deed of trust, providing there is no intent to do so.

The case of *Willis v. Sanger*[24] had previously committed Texas to the same approximate position and the opinion there is relied upon by the court in the *Sohio* case.

A further implication of the *Sohio* case in regard to the priority of claims is found in the court's conclusion that had foreclosure been under the second deed of trust, the result would have been the same. It is submitted by the writer that the court was here paying due regard to the subrogation provisions in the assignment transaction and regarding the execution of the new deed of trust as a mere paper transaction with no extinguishment of the lien rights.

Drawing of an analogy for comparison purposes between an absolute interest purchased and a mortgage interest in land will result in the *Sohio* case appearing to give a result contra, but in reality distinguishable from the case of *Herbert v. Denman*[25] in which case it was held that the purchaser at a trustee's sale on foreclosure of a deed of trust taken on renewal of senior vendor's lien note took title subject to a junior vendor's lien note, this, though renewals were intended to remain first liens.

It is believed that inclusion of the original power of sale is the point of divergence. In the *Sohio* case, the purchaser took subject to the duly recorded deed of trust instrument, which instrument encompassed power of sale without court action; whereas, in the *Denman* case, while the junior lien holder took subject to the

[23] 41 C. J., *Mortgages*, 806, 807, 808 (1926).

[24] 15 Tex. Civ. App. 655, 664, 40 S. W. 229, 233 (Tex. Civ. App. 1897) *writ of error refused.*

[25] 44 S. W. (2d) (Tex. Civ. App. 1931) *writ of error refused.*

senior holder and his assigns, he was not subject to an out of court sale.

This distinction is best illustrated by the two following quotations: "The rule is announced by all the authorities that a junior encumbrancer who is not made a party to a suit to foreclose a prior mortgage or lien is not affected by the judgment is such suit."[26]

". . . The foreclosure involved . . . is limited to a foreclosure by suit. It does not apply to a foreclosure by sale made under, and in compliance with, a valid contract of sale."[27]

STATUTES

The Texas Legislature in regular session, the 50th, provided for registration, and certification of title to house trailers,[28] provided for cancellation of recorded liens on automobiles after six years,[29] and provided for a speedy, revamped registration of title to used automobiles, penalizing delay and failure to record.[30]

—J. B. H.

[26] McDonald v. Miller, 90 Tex. 309, 39 S. W. 89, 94 (1897).

[27] Winchester v. Boggs, 112 S. W. (2d) 207, 209 (Tex. Civ. App. 1937).

[28] Tex. Laws 1947, c. 105, § 2a., p. 168.

[29] Tex. Laws 1947, c. 426, § 47a., p. 1008.

[30] Tex. Laws, 1947, c. 364, pp. 732, 733, 734.