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CONTRACTS - WILLS - THIRD PARTY BENEFICIARY CONTRACT AS TESTAMENTARY DISPOSITION

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CONTRACTS — WILLS — THIRD PARTY BENEFICIARY CONTRACT AS TESTAMENTARY DISPOSITION — The defendant executed a bond and mortgage to one Catherine McCarthy Jackman. Subsequently the parties entered into an extension agreement wherein it was provided that in the event of the death of the mortgagee prior to the maturity of the mortgage, the interest and principal were to be paid one-half to a brother of the mortgagee and one-half to the heirs of a deceased sister. After the death of the mortgagee prior to the maturity of the mortgage, the plaintiffs (the brother and heirs of the deceased sister) claimed a right to the payment of interest as third party beneficiaries. *Held*, the plaintiffs were not entitled to the payments because the provision in the extension agreement was testamentary in nature and not executed as a will. *McCarthy v. Pieret*, 281 N. Y. 407, 24 N. E. (2d) 102 (1939).

The court's refusal to uphold the extension agreement as a third-party beneficiary contract may have rested in part upon the proposition that a third-party beneficiary who has given no consideration and who is not in privity has no direct enforceable right.[1] In spite of the fact that it was a New York court that decided the great case of *Lawrence v. Fox*,[2] the right of a donee beneficiary to enforce a contract in his favor is still uncertain in New York.[3] However, the great weight of American authority recognizes a direct enforceable right in a donee beneficiary,[4] and recent New York decisions make it doubtful that the court intended to deny a right of action to a donee beneficiary.[5] The decision is rested primarily upon the proposition that the extension agreement was an attempt to make a testamentary gift without complying with the statute of wills. The

[1] See the dissenting opinion in the lower court. McCarthy v. Jackman, 255 App. Div. 1025, 8 N. Y. S. (2d) 554 (1938). See 6 UNIV. CHI. L. REV. 473 (1939).

[2] 20 N. Y. 268 (1859).

[3] New York courts have frequently required that the promisee owe some duty to a donee beneficiary. However, a moral duty arising from affinity of blood seems to be enough. See Vrooman v. Tilden, 69 N. Y. 280 (1877). Priester v. Hohloch, 70 App. Div. 256, 75 N. Y. S. 405 (1902), and Buchanan v. Tilden, 158 N. Y. 109, 52 N. E. 724 (1899). Compare these cases with Lawrence v. Fox, 20 N. Y. 268 (1859), and Seaver v. Ransom, 224 N. Y. 233, 120 N. E. 639 (1918).

[4] 2 WILLISTON, CONTRACTS, rev. ed., § 356 at p. 1042 (1936). See 1 CONTRACTS RESTATEMENT, § 135 (1932).

[5] Seaver v. Ransom, 224 N. Y. 233, 120 N. E. 639 (1918). See 2 WILLISTON, CONTRACTS, rev. ed., § 368 (1936).

court laid down the familiar rule that where a gift does not take effect as an executed and complete transfer to the donee, either legally or equitably, during the donor's life, it is a testamentary disposition good only when made by a properly executed will.[6] The court then drew the inference that the mortgagee never intended to divest herself of control over the mortgage so as to be unable to accept the principal and satisfy the mortgage at any time during her life. As the court puts it, "Suppose there had been default in the payment of taxes and interest and foreclosure was necessary. Could the mortgagee have foreclosed or would it have been necessary to join these collateral relatives? To put the question is to answer it."[7] The court then concluded that since the mortgagee intended to retain control over the mortgage, there was no immediate transfer to the donee and therefore the agreement was an attempt to make a gift to take effect after death. This portion of the opinion reflects a confusion between contract rights and property rights—rights which should be distinguished because of the fundamental differences in their nature. The court's frequent use of the term "gift" indicates that the court was thinking in terms of property law rather than contract law. A gift implies a transfer of property.[8] All courts agree that a gift (in the sense used above) cannot be made to take effect after the death of the donor unless made by will,[9] but does the transaction in the principal case fall within this rule? Clearly the agreement in the principal case was not an attempt to transfer property—it was an attempt to create a right to enforce a promise upon the happening of a contingency. The fact that the parties attempting to enforce the promise gave no consideration for their right to do so should not make them the recipients of a gift in the sense used above and should be irrelevant in determining whether or not the transaction was testamentary in nature. Is there then any other element in the extension agreement to render it testamentary in nature? The mere fact that death of one of the parties to a contract is a condition precedent to its enforcement does not make the agreement testamentary.[10] The possibility of revocation would seem to be merely another condition, the happening of which would prevent the beneficiary's rights from ripening into a cause of action. Why such a condition should render a contract testamentary is not clear, but courts have frequently so held,[11] and this was the ground taken in the principal case. To quote from the opinion, "Contracts made for the benefit of third parties are well recognized today, but they are executed contracts, where the promisee is unable to revoke or control the

[6] 28 C. J. 624 (1922).

[7] Principal case, 24 N. E. (2d) 102 at 103 (1939).

[8] See 1 BOUVIER, LAW DICTIONARY 1352 (1914), defining a gift as a voluntary transfer of property.

[9] 28 C. J. 624 (1922); Taylor v. Harmisan, 179 Ill. 137, 53 N. E. 584 (1899); Ga Nun v. Palmer, 159 App. Div. 86, 144 N. Y. S. 457 (1913); McGrath v. Reynolds, 116 Mass. 566 (1875).

[10] Sheldon v. Blackman, 188 Wis. 4, 205 N. W. 486 (1925) (promissory note payable upon death of the maker); Estate of Beyschlag, 201 Wis. 613, 231 N. W. 165 (1930); In re Fuhrmann's Estate, 209 Wis. 218, 244 N. W. 628 (1932). But see Sliney v. Cormier, 49 R. I. 74, 139 A. 665 (1928).

[11] ATKINSON, WILLS, § 64 (1937); Sliney v. Cormier, 49 R. I. 74, 139 A. 665 (1928) (intent that contract should operate as a will); Juneau v. Dethgens, 200 Wis. 360, 228 N. W. 496 (1930). Also see 23 MINN. L. REV. 112 (1938).

promisor in the fulfillment of the promise. . . . I do not say that the passing of property at death may not be provided for by contract or by deed, but the donor in such cases divests himself of all interest and vests it in the beneficiary." [12] Again, the court seems to be using the term vested in the sense of property rights rather than contract rights. Conceding that the mortgagee intended to retain the right to revoke the extension agreement, it does not follow that no immediate interest passed to the beneficiaries. It would seem that the agreement became an executed contract the moment the mortgagor and mortgagee assented thereto, and since the beneficiaries were to be recipients of a gratuity, their assent could be presumed.[13] It should follow that the beneficiaries took an immediate right subject to being defeated by the happening of certain contingencies.[14] The mere fact that a party takes an interest which is totally defeasible does not mean that he takes no interest at all.[15] This is the view taken of insurance policies [16] and tentative or savings bank trusts [17] and seems entirely in keeping with sound principles of contract law. Though the court probably felt itself bound by New York precedents in the present case,[18] it is submitted that the agreement could have been upheld as a third party beneficiary contract.[19] Such transactions do not circumvent the purpose of the statute of wills because the possibility of fraud

[12] Principal case, 24 N. E. (2d) at 103. See Whittier, "Contract Beneficiaries," 32 YALE L. J. 790 (1923), where it is suggested that a donee beneficiary acquires his rights as an immediately executed gift consisting of new contract rights in his favor.

[13] Rogers v. Gosnell, 58 Mo. 589 (1875); Rodgers v. Reinking, 205 Iowa 1311, 217 N. W. 441 (1928); 1 CONTRACTS RESTATEMENT, § 137 (1932). But see ibid., § 142, comment (a), indicating that the right to revoke must be in express terms.

[14] Copeland v. Beard, 217 Ala. 216, 115 So. 389 (1928); Henderson v. McDonald, 84 Ind. 149 (1882); Waterman v. Morgan, 114 Ind. 237, 16 N. E. 590 (1888). *Contra*: Townsend v. Rackham, 143 N. Y. 516, 38 N. E. 731 (1894). Cf. Knowles v. Erwin, 43 Hun 150 (1887), affd. 124 N. Y. 633, 26 N. E. 759 (1891).

[15] See Matter of Totten, 179 N. Y. 112, 71 N. E. 748 (1904) (holding that in the absence of evidence that an irrevocable trust was intended or that no trust at all was intended, the inference arises that the depositor intended to create a trust but also intended to reserve a power of revocation). Cf. Sullivan v. Sullivan, 161 N. Y. 554, 56 N. E. 116 (1900). See 1 SCOTT, TRUSTS, § 58 (1939).

[16] 12 COL. L. REV. 551 (1912). See 19 A. L. R. 654 (1922); 52 A. L. R. 386 (1928); 59 A. L. R. 172 (1929). A very close analogy exists between an endowment insurance policy where the insured retains a right to change the beneficiary and take out the cash value and the situation presented in the principal case.

[17] Matter of Totten, 179 N. Y. 112, 71 N. E. 738 (1904).

[18] Townsend v. Rackham, 143 N. Y. 516, 38 N. E. 731 (1894); Priester v. Hohloch, 70 App. Div. 256, 75 N. Y. S. 405 (1902); Seager v. Tholens, 182 App. Div. 317, 170 N. Y. S. 482 (1918).

The facts of the Townsend case were similar to the principal case, except that in the earlier case the mortgagee had revoked the agreement. After the death of the mortgagee, the beneficiaries claimed that the revocation was void since they had not been parties thereto. The court, however, based its decision on the principle that the agreement was testamentary rather than that the mortgagee retained a right of revocation. The latter would have been the sounder ground.

[19] See Rodgers v. Reinking, 205 Iowa 1311, 217 N. W. 441 (1928).

is very slight, and it seems doubtful that it was ever intended that the statute of wills should apply to the kind of interest involved in third party contracts.

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