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Is Mortgagor's Liability Extinguished by Extension of Time for Payment without His Consent

Gale Blocki
IS MORTGAGOR'S LIABILITY EXTINGUISHED BY EXTENSION OF TIME FOR PAYMENT WITHOUT HIS CONSENT?

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No mortgagor is pleased to have a deficiency decree against him after he has parted with his land under the belief that his grantee will pay the mortgage. Many courts have found a way to relieve the mortgagor of embarrassment where the grantee had, at the time of the conveyance, before maturity of the debt, expressly assumed and agreed to pay the mortgage and where the mortgagee had subsequently extended the time of payment without the consent or knowledge of the original mortgagor.

If the mortgage note is a negotiable instrument, the personal liability of the mortgagor cannot, consistently with the statutes on negotiable instruments, be extinguished by extension of time for payment. The Illinois Supreme and Appellate Courts, for many years, have permitted this question to turn upon a determination of whether the mortgagor's grantee (i.e. the one to whom he sold the property subject to the mortgage) assumed and agreed to pay the mortgage debt. If he did and thereafter extended the time for payment of the note without the consent of his grantor (the mortgagor), the liability of such grantor was extinguished; if the grantee did not assume and agree to pay the mortgage debt and extended

1 Member of Illinois Bar.
the time for payment thereof without the consent of his grantor, the liability of such grantor, as mortgagor, was not extinguished.

The theory of law assumed by the court in these decisions was that where A, the owner of a piece of property which had been encumbered by him, conveyed the same to B, the relationship as between A and B became that of principal and surety, B being the principal debtor and A the surety; that the principles of suretyship apply, and if X, the owner of the mortgage note, extended the time of payment thereof without the consent of A, then A was discharged from liability upon the note.

An examination of Illinois cases upon this question discloses that there was, in all cases, evidence that the purchaser had assumed and agreed to pay the encumbrance and it was, therefore, held that the mortgagor's liability was extinguished by the extension of the time for payment without his consent.\(^2\)

On the other hand, where a purchaser had not assumed or agreed to pay an encumbrance, no relationship of principal and surety existed, the theory of law above set forth did not apply, and an extension, without the mortgagor's consent, did not release him from liability. An interesting case supporting this last statement is *Sholten v. Barber.*\(^3\) Sholten executed her promissory note to Cooper for five thousand dollars, payable five years after its date, secured by trust deed upon certain real estate. Sholten thereafter conveyed the property to Dexter, who assumed the payment of the encumbrance. There were several subsequent conveyances of the property by quit-claim deeds, containing no assumption of the mortgage debt, ending with a deed of that character from Martin to Millam. The note later became the property of Barber. Upon the maturity of the note, the interest was reduced from 8 per cent to 6 per cent and the time of payment extended for three years by endorsement on the


\(^3\) 217 Ill. 148.
note. Millam, the then owner of the real estate, executed interest notes for the extended period. Thereafter the trust deed was foreclosed and the proceeds of the foreclosure sale endorsed on the principal note, leaving a balance due, for which suit was brought against Sholten, the maker of the note. Judgment was entered in the lower court for the plaintiff and, on appeal, it was argued against the ruling of the court that Millam, by the extension agreement, became the principal debtor to the plaintiff and that the defendant, the maker of the note, became surety for Millam; that the plaintiff extended the time of payment to Millam, as principal debtor, without the knowledge or consent of the defendant and that defendant, being a mere surety, was released from all liability. In sustaining the holding of the lower court, the Supreme Court, after reviewing the authorities relating to a situation where the purchaser of the property has assumed and agreed to pay the encumbrance, says:

The mere purchase of land does not render the purchaser liable for an encumbrance upon it, and an obligation on his part to pay it can only arise from his contract, either express or implied by law from the circumstances. . . . There was no agreement by Millam to pay the amount of the encumbrance when the endorsement was made on the note or at any other time. Whatever legal effect could be given to the endorsement signed by Donovan Real Estate Company or to the interest notes executed by the same company, as agent, there was no agreement on the part of Millam to pay the principal note. Plaintiff could not have maintained an action against Millam for the amount of such note, and as he never assumed or agreed to pay it, the defendant never became, and could not become, his surety.

The court refused to admit in evidence a copy of one of the quit-claim deeds in the chain of conveyances to Millam for want of sufficient evidence upon which to introduce such copy. The question whether the ruling was correct is immaterial. The promise of Dexter [the original grantee] to pay the encumbrance was not a covenant running with the land, and if the deed had been admitted so as to show the legal title given
to Millam, the rights of the parties would not have been affected in any way. There was no evidence tending to prove a defense to the note, and the court was right in directing a verdict for the amount due on the note.

In the year 1928 in the State of Nebraska, in the case of Peter v. Finzer, the Supreme Court of Nebraska held that since the adoption of the Nebraska Negotiable Instruments Act the liability of the maker of a note could only be extinguished by one of the methods prescribed in the Act, and that extending the time for payment of a mortgage note by agreement of the then owner of the property with the holder of the note, whether the owner of the property had assumed and agreed to pay the mortgage note or not, was not included in the Act as one of the methods by which this liability could be extinguished. In that case it was urged upon the court, by the maker of the note, that his liability had been extinguished by an extension of time for payment by the subsequent owner of the property, who had assumed and agreed to pay the note, and the court said:

On the basis of the facts set forth in his answer, the defendant in the court below, as a matter of law, contended that where one buys land encumbered by a mortgage debt and, as a part of the consideration of the purchase, assumes the payment thereof, his promise creates a principal obligation which the mortgagee may enforce against him; that the maker of the note and mortgage thereafter, between the parties, sustains the relation of surety only; that a subsequent agreement by the mortgagee and payee with such subsequent grantee, without the assent of the grantor and mortgagor, extending time of payment of the debt, evidenced by the note and mortgage which has been assumed by such grantee, discharges the maker and mortgagor from all personal liability thereon. This conclusion seems fully supported by the doctrine announced by this court in Merriam v. Miles. 

The controlling question now is, to what extent, if any, has the doctrine thus announced been modified or affected by the

4 116 Neb. 380.
5 54 Neb. 566, decided in 1898.
provisions of the Nebraska Negotiable Instruments Act adopted, effective August 1, 1905?

This court is committed to the doctrine that, so far as applicable, the provisions of our Negotiable Instruments Act determine the mutual rights of the immediate parties to the instrument as between themselves.

Finzer, at its inception, was the sole maker of the instrument in suit.

"The maker of a negotiable instrument by making it engages that he will pay it according to its tenor, and admits the existence of the payee and his then capacity to endorse," [citing Negotiable Instruments Act].

Section 4801, Comp. St. 1922, provides: "The person 'primarily' liable on an instrument is the person who by the terms of the instrument is absolutely required to pay the same. All other parties are 'secondarily' liable."

It would seem incontestable that Finzer, by the terms of the instrument in suit, being absolutely required to pay the same, is "primarily" liable thereon. The language of Section 4801, supra, affirmatively excludes him from the classification of "secondarily" liable.

Article 8 of our Negotiable Instruments Law covers the subject of discharge of negotiable instruments. The first section thereof provides: "A negotiable instrument is discharged: First. By payment in due course by or on behalf of the principal debtor. Second. By payment in due course by the party accommodated where the instrument is made or accepted for accommodation. Third. By the intentional cancellation thereof by the holder. Fourth. By any other act which will discharge a simple contract for the payment of money. Fifth. When the principal debtor becomes the holder of the instrument at or after maturity in his own right."

Applicable to those exclusively who are "secondarily" liable on negotiable instruments, the second section of Article 8 provides: "A person secondarily liable on the instrument is discharged: First. By any act which discharged the instrument. Second. By the intentional cancellation of his signature by the holder. Third. By the discharge of a prior party."
Fourth. By a valid tender of payment made by a prior party. Fifth. By a release of the principal debtor, unless the holder's right of recourse against the party secondarily liable is expressly reserved. Sixth. By any agreement binding upon the holder to extend the time of payment, or to postpone the holder's right to enforce the instrument, unless made with the assent of the person secondarily liable, or unless the right of recourse against such party is expressly reserved."

It may also be said that the statute under consideration makes no provision for the proof of another and different relation than that expressly undertaken and defined by the tenor of the instrument signed. This Act further provides in definite terms that the instrument, and hence one primarily liable, is discharged in one of the five ways set forth in Section 4729, above quoted. There is no mention in this Section of a discharge of a person "primarily" liable by an extension of time. But, among the ways in which a party "secondarily" liable may be discharged as above set forth, in Section 4730, supra, is "any agreement binding upon the holder to extend the time of payment, or to postpone the holder's right to enforce the instrument, unless made with the assent of the person secondarily liable," etc. Whatever interpretation might be required of Section 4729, supra, containing an enumeration of the ways in which the instrument, and consequently the parties primarily liable thereon, might be discharged, if this provision stood alone, the inference arising from the omission of extension of time from such enumeration, and its inclusion among the ways in which parties "secondarily" liable may be discharged as above set forth in Section 4730, supra, necessitates and renders irresistible the conclusion that the Legislature did not intend that persons primarily liable should be discharged in that manner. Or, in other words, parties to a negotiable instrument, primarily liable thereon, may be discharged only in the manner provided by statute.

The conclusion follows that the extension of time set forth in defendant's answer did not constitute a valid defense to the action upon the note in suit, in view of the fact that the defendant was, under the terms of the statute, primarily liable
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thereon. . . . This conclusion is, in principle, in full accord with the great weight of authority in other states. . . .

The identical question arose in the State of Washington in Continental Mutual Savings Bank v. Elliott, where it was likewise held that the maker of the note was not discharged from liability by virtue of the extension of time entered into between a subsequent grantee and the mortgagee, although the grantee had assumed and agreed to pay the mortgage encumbrance.

The same conclusion has been reached by courts of the following states: Arizona, Colorado, Indiana, Kansas, Kentucky, Maryland, Massachusetts, Minnesota, New York, Ohio, Oklahoma, Oregon, Tennessee, Texas, and Utah. Iowa alone stands contrary.

Of course, it is fundamental that the court of no state in which the law is enacted is bound by the construction of the statute by the courts of other states; but courts, with full knowledge of the history of this legislation, and knowing that its chief purpose is as stated above, should, we think, upon all questions of construction, where the rule adopted by other states is not plainly erroneous, be disposed to follow the con-

6 166 Wash. 283.
7 Cowan v. Ramsey, 15 Ariz. 533.
8 Hall v. Farmers' Bank, 74 Colo. 165.
11 First State Bank v. Williams, 164 Ky. 143.
14 Vernon Center State Bank v. Mangelsen, 166 Minn. 472.
18 Cellers v. Meachem, 49 Or. 186.
19 Graham v. Shephard, 136 Tenn. 418.
21 Wolstenholme v. Smith, 34 Utah 300.
22 Fullerton Lumber Company v. Snouffer, 139 Iowa 176.
struction given to the act by the courts of the state in which
the act has heretofore been adopted and construed; and particu-
larly should this be true where the statute involves a question
upon which the authorities, independent of a statute, are so
greatly divided as they are upon the question presented in the
case at bar, for by no other course may uniformity be obtained.

The Illinois Negotiable Instruments Act is substan-
tially the same as those of Nebraska and the states before
named. In the latter jurisdictions, where prior to the
enactment of the Negotiable Instruments Act the courts
held that, in cases where the grantee had assumed and
agreed to pay the mortgage, a subsequent extension of
time to him by the holder of the mortgage released the
maker of the note, the same courts now hold that such
rule of law is, since the enactment of the Negotiable In-
struments Act, no longer applicable. But the point seems
never to have been raised in Illinois. There are un-
doubtedly other states whose Negotiable Instruments
Acts would alter the decisions of the courts if the point
were once raised.

Quite recently the Illinois Appellate Court, First Dis-
trict, in the case of Fleming v. Gannon, held that the Ne-
gotiable Instruments Act specifies how a person primar-
ily liable or secondarily liable may be discharged and
holds that subordinating a lien without the knowledge
and consent of the defendants (who were the makers of
the note) was not among them. The judgment rendered
by the Municipal Court was reversed and the case re-
manded. It is regrettable that the Appellate Court
could not have made a finding of facts and entered judg-
ment, that the cause might have gone to the Supreme
Court. It was not necessary, in the decision, that the
court find whether the defendants were primarily or sec-
ondarily liable but the court, in its opinion, stated that
even conceding that defendants were secondarily liable,
their liability was not discharged under the Negotiable

24 267 Ill. App. 163.
Instruments Act, which Act specifies in detail how persons primarily and secondarily liable might be discharged. It is unfortunate that the court, in its opinion, did not find that defendants were primarily liable under the Act and that the subordinating of the lien, without their consent, was not among the ways specified in the Act for discharging persons primarily liable. The Gannons were the makers of the note and the Illinois Negotiable Instruments Act particularly sets forth that "The person 'primarily' liable on an instrument is the person who, by the terms of the instrument, is absolutely required to pay the same. All other parties are 'secondarily' liable."

Under the Negotiable Instruments Act the maker of a promissory note, secured by a mortgage upon real estate, is primarily liable and his liability can only be discharged in the ways set forth in the Act relating to a person primarily liable. Even though he may thereafter sell the property to one who agrees to assume and pay the mortgage indebtedness, he is, by the tenor of the instrument, the one primarily liable under the Act, and this liability can only be extinguished in the manner provided for in the Act. Under former decisions, if his

25 Cahill's Ill. Rev. St. (1931), Ch. 98, par. 214.
26 In Schrader v. Helebower, 243 Ill. App. 139, the defendant signed as surety and the plaintiff knew this, and had not the defendant waived the provisions of the statute, he would have been discharged by an extension of time under Art. 8, sec. 119, par. 5 of the Negotiable Instruments Act, Cahill's Ill. Rev. St. (1931), Ch. 98, par. 141. The court apparently assumed that a surety is secondarily liable. But a surety is by common law primarily liable and he certainly comes within the definition of persons primarily liable in the statute.

27 Cahill's Ill. Rev. St. (1931), Ch. 98, par. 140. It is worth noting that the Illinois Act omits one provision of the Uniform Negotiable Instruments Law, i.e. "by any other act which will discharge a simple contract for the payment of money." Nevertheless it was held in Gorin v. Wiley, 215 Ill. App. 541, that parties primarily liable on a negotiable instrument were discharged by any act which would discharge a simple contract for the payment of money, and the maker was held to be released by a novation. This view was based on the provision "In any case not provided for in this act, the rules of the law merchant shall govern," Cahill's Ill. Rev. St. (1931), Ch. 98, par. 218. But this provision was certainly not intended to cover a method of discharge impliedly excluded by the Act—"Inclusio unius est exclusio alterius." Cellers v. Meachem, 49 Or. 186; Vanderford v. Farmers' and Mechanics' National Bank, 105 Md. 164.
grantee, who assumed and agreed to pay the mortgage, extended the time for payment, such grantee would have become the principal debtor and the original mortgagor would have become the surety. In none of the cases so holding, however, subsequent to the passage of the Negotiable Instruments Law, has the decision either referred to the law or discussed its provisions. The statute has changed the common law with respect to this subject, and the maker of a note, who is primarily liable, can only be discharged by one of the methods provided for in the Act.