

# YALE LAW JOURNAL

Vol. XXXIX

MARCH, 1930

No. 5

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## CONTRACTS FOR THE BENEFIT OF THIRD PERSONS IN THE FEDERAL COURTS

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The law of contracts for the benefit of third persons has gone through the same development in the federal courts as in the state courts; and the result is now substantially the same, especially because the federal courts are usually applying what purports to be the law of some particular state.

While the law of third party beneficiaries is a part of the general common law of the land, that "common law" must be regarded as a continually developing law. It is not the law of the Anglo-Saxons, nor the Norman law of Edward I, nor even the law of the American colonies in 1776. It is certainly not the English law of *Tweddle v. Atkinson*<sup>1</sup> or *Dunlop Tyre Co. v. Selfridge*.<sup>2</sup> It now contains large elements derived from equity sources, the law merchant, and the Roman law. Above all, it has undergone a continual process of change and development by legislative and judicial action. In this process of change and development, the law of no subject can long remain "common" to fifty jurisdictions, in the sense that the courts of those jurisdictions will continue to decide with uniformity and to lay down uniform general rules of decision. There are some differences among the states as to the law of third party beneficiaries. This law is within the control of the state courts and legislatures, and it will be recognized and applied by the federal courts.

The question whether a third party has a right against the promisor is a question of substantive law and not one of procedure only. Therefore, the federal courts will apply the law of

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<sup>1</sup> 1 Best & S. 393 (1861).

<sup>2</sup> [1915] A. C. 847. As to the law of England, see the article by the present writer in (1930) 46 L. Q. Rev. 12.

the state whose law is regarded as determining the legal operation of the contract. It cannot be said that there is "a federal law" or a law of the federal courts. Cases in the federal courts will be determined in accordance with that system that the court deciding the case thinks is applicable to the contract involved in that case. This means that in the federal courts there may be many laws as to third party beneficiaries, not merely one law or system.

The question whether a third party has a right against the promisor is a question of substantive law and not one of procedure. But the question of substantive "rights" cannot be separated from the question of remedies; and remedies and procedure are also overlapping fields. Pragmatically, the test of existence of a legal right is the availability of some legal remedy, direct or indirect. Unless the judicial and executive officers of government take some notice of a supposed "right" and will act in such a way as to constitute a societal sanction, there is no reason for saying that the claimant has a jural right. If this is "pragmatically" true, it is mere inconsequential verbiage to say that it is "theoretically" not true. Of course, any one can by constructing his own language and his own definitions build up a consistent "theory" of rights; but the problem of the lawyer and the judge is, What are we to do about it? In the case of a third party beneficiary, therefore, the particular court must determine whether or not under the system of law that it administers it should act in such a way as to sanction the third party's claim—should give some direct or indirect remedy. If it does anything that will operate practically as a sanction, it is recognizing and in some degree enforcing a right in the third party. The form taken by this sanction—the form of the "remedy" given—varies. It varies in effectiveness as well as in "directness"; and it varies with the particular jurisdiction. Therefore a court may feel limited in the remedies that it can apply and in the procedure by which the issues are to be determined, even though it can apply some remedy in accordance with a particular procedure; Remedies and procedure are indeed determined by the law of the forum; but in determining its remedies and procedure, the court is also determining its substantive law of rights and duties.

As to the substantive law, it is true that the federal courts, like all other courts, must determine for themselves the rights of the parties before them. In so far as they recognize and enforce rights and duties, they adopt the law involved as the law of the federal court and make it the federal law for the sort of case before the court. But the law that they adopt does not have to be drawn from federal statutes or antecedent federal decisions; nor is it drawn from some "brooding omnipres-

ence in the sky" called a federal common law. It is drawn from exactly the same sources that a state court draws its law, including state statutes and decisions, customs and business practices, the mores of the time and place. In the process, the desire for uniformity has caused the federal court sitting within a particular state to follow the rules that seem to have been definitely established within that state. Therefore, while statements are not infrequent that the federal courts will determine questions of general commercial law for themselves, it is necessary to understand along with this that where commercial law is not "general," the federal court will select its controlling law in accordance with the practice that prevails in cases where laws conflict.<sup>3</sup>

What then have the federal courts in fact done with the claims of third party beneficiaries? In fact they have recognized and enforced them in the same cases in which the state courts enforce them, with about the same amount of variation in explanatory theory and inconsistency in decision. There is no federal system as such, determining the rights of third parties. Each federal district court sits within the limits of some state and determines its own contract law, including that affecting third parties, and it selects the particular jurisdiction whose system of law is to be applied in the case in hand just as a state court would do. If by that law the third party has an enforceable right, the federal court recognizes and enforces it. The remedies and the procedure of enforcement may not be identical with those of the state court, although usually they are nearly so.

#### CASES IN THE SUPREME COURT OF THE UNITED STATES

In *Hendrick v. Lindsay*,<sup>4</sup> *H* wrote to *L* requesting him to execute a certain appeal bond, and promised to give him "whatever security may be desired in the shape of a personal bond." *L* procured *M* to execute the appeal bond with him. *H* executed no bond of indemnity. Later, having had to pay on the appeal bond, *L* and *M* sued *H* on his promise to *L* to give security. The court held that *M* was a proper party plaintiff, since *H*'s promise

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<sup>3</sup> In *Federal Sur. Co. v. Minneapolis S. & M. Co.*, 17 F. (2d) 242 (C. C. A. 8th, 1927), the federal court sitting in Minnesota applied what it erroneously supposed to be the law of Montana, the *lex loci contractus*, deciding against the plaintiff.

In *Duvall-Percival Trust Co. v. Jenkins*, 16 F. (2d) 223 (C. C. A. 8th, 1926), the federal court sitting in Kansas properly applied the law of Missouri, deciding for the plaintiff, although on the exact issue the law of Kansas was *contra*.

In *Federal Surety Co. v. City of Staunton*, 29 F. (2d) 9 (C. C. A. 5th, 1928), the federal court sitting in Alabama applied the law of Illinois.

<sup>4</sup> 93 U. S. 143 (1876).

to *L* was for the benefit of whoever might sign the appeal bond. The court said:

"It is also argued, as Mansfield's name does not appear in the letters of Hendrick, that he could not join in this action. This would be true, if the promise were under seal, requiring an action of debt or covenant; but the right of a party to maintain assumpsit on a promise not under seal, made to another for his benefit, although much controverted, is now the prevailing rule in this country."

This case has never been overruled or disapproved,<sup>5</sup> although it has occasionally been speciously explained as being a case in which the co-plaintiff Mansfield was a promisee and "in privity."

The next case is *National Bank v. Grand Lodge*,<sup>6</sup> in which a bondholder sued the defendant because it had adopted the following resolution:

"Resolved, That this Grand Lodge assume the payment of the \$200,000 bonds, issued by the Masonic Hall Association, provided that stock is issued to the Grand Lodge by said association to the amount of said assumption of payment by this Grand Lodge as the said bonds are paid."

It does not appear that this resolution was even an offer made to the Association; if it was communicated as an offer, it does not appear that it was ever accepted; it certainly does not appear that the Association ever delivered or tendered any stock to the Grand Lodge. It is perfectly clear that if the Grand Lodge ever made any promise whatever, it was conditional upon the concurrent delivery of stock. The court rightly gave judgment for the defendant on this ground; but it also based its decision on the following statement of third party law:

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<sup>5</sup> In *Austin v. Seligman*, 18 Fed. 519, 522 (C. C. S. D. N. Y. 1883), speaking of the supposed English rule that no one but the promisee can enforce a contract, the court said: "It has the merit of simplicity, but is artificial instead of being reasonable. According to good sense and upon principle there is no reason why a person may not maintain an action upon a contract, although not a party to it, when the parties to the contract intend that he may do so. The formal or immediate parties to a contract are not always the persons who have the most substantial interest in its performance. Sometimes a third person is exclusively interested in its fulfillment. If the parties choose to treat him as the primary party in interest, they recognize him as a privity in fact to the consideration and promise. And the result of the better-considered decisions is that a third person may enforce a contract made by others for his benefit, whenever it is manifest from the nature or terms of the agreement that the parties intended to treat him as the person primarily interested. The cases of *Hendrick v. Lindsay* and *Nat. Bank v. Grand Lodge*, and the expressions in the opinions, do not antagonize this proposition, but accord with it."

<sup>6</sup> 98 U. S. 123, 124 (1878).

"We do not propose to enter at large upon a consideration of the inquiry how far privity of contract between a plaintiff and defendant is necessary to the maintenance of an action of assumpsit. The subject has been much debated, and the decisions are not all reconcilable. No doubt the general rule is that such a privity must exist. But there are confessedly many exceptions to it. One of them, and by far the most frequent one, is the case where, under a contract between two persons, assets have come to the promisor's hands or under his control which in equity belong to a third person. In such a case it is held that the third person may sue in his own name. But then the suit is founded rather on the implied undertaking the law raises from the possession of the assets, than on the express promise. Another exception is where the plaintiff is the beneficiary solely interested in the promise, as where one person contracts with another to pay money or deliver some valuable thing to a third.<sup>7</sup> But where a debt already exists from one person to another, a promise by a third person to pay such debt being primarily for the benefit of the original debtor, and to relieve him from liability to pay it (there being no novation), he has a right of action against the promisor for his own indemnity; and if the original creditor can also sue, the promisor would be liable to two separate actions, and therefore the rule is that the original creditor cannot sue."

In this statement the Court recognizes the right of a sole beneficiary as one enforceable in assumpsit at law.<sup>8</sup> Secondly, assumpsit is said to be maintained if "assets" have come into the promisor's hands that "in equity" belong to the plaintiff. And thirdly, the plaintiff cannot maintain assumpsit on a promise by the defendant to discharge the promisee's debt to the plaintiff. In this third case the plaintiff is not a sole beneficiary; but it may nevertheless be a case in which "assets" are in the defendant's hands that "in equity" should go to the plaintiff. This statement of the Court was far from denying beneficiaries a right "at law"; but the case has been cited a good many times as so holding. The facts of the case were not such as to require careful consideration of third party law; and the decision has not in fact determined that law.

*Keller v. Ashford*<sup>9</sup> was a suit in equity by a mortgagee against the mortgagor's grantee who had assumed the debt. Judgment was given for the plaintiff, Gray, J., basing the decision on

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<sup>7</sup> This dictum as to the right of a sole beneficiary seems never to have been denied; it is supported by the decisions on insurance policies issued to one party for the benefit "of whom it may concern." Cf. *Hagan v. Scottish Union Ins. Co.*, 186 U. S. 423, 22 Sup. Ct. 862 (1902); *Merchants & M. T. Co. v. Robinson etc. Co.*, 191 Fed. 769 (C. C. A. 1st, 1911).

<sup>8</sup> A donee beneficiary; to whom the promisee owed a moral duty only, was given judgment in *Maumee Val. Elec. Co. v. Toledo*, 13 F. (2d) 98 (C. C. A. 6th, 1926), and *Gooch v. Buford*, 262 Fed. 894 (C. C. A. 6th, 1920), where a husband contracted for the benefit of his wife.

<sup>9</sup> 133 U. S. 610, 10 Sup. Ct. 494 (1890).

the ground that the mortgagor was in the position of a surety, with the grantee as the principal debtor, and that the mortgagee creditor would be subrogated to the surety's rights against the principal. This theory had been used in some of the early New York cases, though not in England; and it has continued to be used in some of the mortgage cases down to the present time. Gray said that the defendant was under no "direct obligation" to the mortgagee; but the practical result of the case was the same as if he had called the relation of the defendant to the plaintiff a "direct obligation." When the result is thus identical, the fact that it was reached by a "subrogation" theory is of no importance in the particular case. In order to show that it is anything more than one possible intellectual expedient to reach a desired result, actual decisions must be produced in which the practical results have been affected by it.<sup>10</sup>

The subrogation theory may have had a decisive effect in *Willard v. Wood*,<sup>11</sup> where the Court held that an action "at law" could not be maintained in the District of Columbia by a mortgagee against the mortgagor's grantee who assumed the debt. At any rate the creditor was denied a remedy "at law" because such was the law of "the forum." After a good deal of fumbling, the plaintiff's attorney finally brought a bill in equity against the grantee; and the Supreme Court dismissed the bill because of laches.<sup>12</sup>

In *Union Life Ins. Co. v. Hanford*,<sup>13</sup> the Court held that an extension of time given by the mortgagee to a grantee who had assumed the debt wholly discharged the mortgagor for the reason that the assumption contract made the grantee the principal debtor of the mortgagee and the mortgagor only a surety. Mr. Justice Gray thought there would be difficulty in so holding if the mortgagee's right was regarded as a merely equitable one, as decided in *Keller v. Ashford* and *Willard v. Wood*. He avoided that difficulty by saying that the plaintiff's right was determined by the law of Illinois. The Court said:

"The question whether the remedy of the mortgagee against the grantee is at law and in his own right, or in equity and in the right of the mortgagor only, is, as was adjudged in *Willard v. Wood*, 135 U. S. 309, to be determined by the law of the place where the suit is brought. By the law of Illinois, where the

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<sup>10</sup> Mr. Justice Gray brought with him to the Supreme Court the intermediate Massachusetts views that he himself had laid down in *Exchange Bank v. Rice*, 107 Mass. 37 (1871). The earlier and more satisfactory views of Chief Justice Shaw must have appealed to him more strongly when he rendered the opinion in the *Hanford* case, *infra* note 13, and dissented in the *Constable* case, *infra* note 17.

<sup>11</sup> 135 U. S. 309, 10 Sup. Ct. 831 (1890).

<sup>12</sup> *Willard v. Wood*, 164 U. S. 502, 17 Sup. Ct. 176 (1896).

<sup>13</sup> 143 U. S. 187, 12 Sup. Ct. 437 (1892).

present action was brought, as by the law of New York and of some other states the mortgagee may sue at law a grantee who, by the terms of an absolute conveyance from the mortgagor, assumes the payment of the mortgage debt."

This case can be reconciled with *Willard v. Wood* only by supposing that the law of the District of Columbia differs from that of Illinois. The "forum" was a federal court in both cases; but in the *Hanford* case the Court purported to be applying Illinois law because the federal court in which the suit was brought sat in that state.

In *Johns v. Wilson*,<sup>14</sup> a mortgagee brought an action under the Arizona code against the mortgagor's grantee who had assumed the debt. After reviewing cases to the effect that the mortgagee's right was by subrogation only, the Court gave judgment for the plaintiff, inasmuch as by the Arizona code "there is no distinction between suits at law and in equity." From the foregoing cases it appears that the Court has consistently recognized that a mortgagee beneficiary has an enforceable right and that the Supreme Court will give the form of remedy that is given by the local law applicable to the particular case.

In *Hagen v. Scottish Union Ins. Co.*,<sup>15</sup> an owner of a boat took out a marine insurance policy for the benefit "of whom it may concern" and later sold an interest in the boat to another. It was held that the purchaser and the promisee could jointly maintain a libel in admiralty on the policy. The purchaser seems to be a third party beneficiary. He might perhaps be regarded as an assignee of part of the promisee's right; but fire insurance policies are not ordinarily assignable, and the purchaser's right seems rather to rest upon the promisee's intention to have the contract of insurance so drawn as to create rights in the subsequent purchaser.<sup>16</sup>

In several cases the Supreme Court decided against the plaintiff on grounds that go to the merits of his claim and that would be held to invalidate it in nearly all of the state courts.<sup>17</sup>

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<sup>14</sup> 180 U. S. 440, 21 Sup. Ct. 445 (1901).

<sup>15</sup> *Supra* note 7.

<sup>16</sup> "We concur in the view that by virtue of the language contained in the policy, 'on account of whom it may concern,' it is not necessary that the person who takes out such a policy should have at that time any specific individual in mind. If he intended the policy should cover the interest of any person to whom he might sell the entire or any part of the interest insured, that would be enough." *Hagan v. Scottish Ins. Co.*, *supra* note 7, at 425, 22 Sup. Ct. at 865.

*Cf.* *Merchants & M. T. Co. v. Robinson etc. Co.*, *supra* note 7, holding to the same effect.

<sup>17</sup> In *Constable v. National S. S. Co.*, 154 U. S. 51, 14 Sup. Ct. 1062 (1894), the defendant promised a collector of duties to be responsible for

It was not a question of form of remedy, whether at law or in equity by subrogation or otherwise. Indeed in one of these cases three justices dissented and argued that the beneficiary could maintain the suit that he had brought, a libel in admiralty. Mr. Justice Gray was one of these dissenters.

Following the example of the states, Congress has enacted a statute applicable to public contracts requiring the contractor to give a surety bond to the United States for the benefit of laborers and materialmen.<sup>18</sup> This statute has been very liberally construed for the benefit of the third parties to be protected; and they have been held to have rights enforceable in an action "at law," although the statute does not say what the remedy shall be or in what kind of court the beneficiaries may sue.<sup>19</sup>

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losses by fire; but the consignee had already directly contracted with the defendant to carry this risk himself. It was held that the consignee could not hold the defendant on its promise to the collector. The court said:

"No case has gone so far as to hold that, where the person for whose benefit the contract is made, has himself or by his privy in estate entered into a contract inconsistent with this, he may repudiate such prior contract, and claim the benefit of the second simply because it has become for his interest to do so."

Gray, Field, and Jackson, JJ., dissented, finding that there was no conflict between the contracts, and holding that the consignee could maintain a libel in admiralty to enforce the contract made for his benefit with the collector, by analogy with either law or equity.

*German Alliance Ins. Co. v. Home Water Co.*, 226 U. S. 220, 33 Sup. Ct. 32 (1912) held that a citizen has no rights by virtue of a contract between a water company and a city to supply water for putting out fires, because that contract is not made for the benefit of particular citizens. This agrees with the great weight of state authority.

In *Robins Dry Dock & R. Co. v. Flint*, 275 U. S. 303, 48 Sup. Ct. 134 (1927), the decision was in the field of torts; but it was also said that a contract to refit a ship in dry dock made with the owner and without knowledge that the ship was under charter gave no right to the charterer against the contractor.

<sup>18</sup> 7 U. S. COMP. STAT. § 6923 (1916).

<sup>19</sup> *Brogan v. Nat'l Sur. Co.*, 246 U. S. 257, 38 Sup. Ct. 250 (1918); *Illinois Sur. Co. v. John Davis Co.*, 244 U. S. 376, 37 Sup. Ct. 614 (1917); *Illinois Sur. Co. v. Peeler*, 240 U. S. 214, 36 Sup. Ct. 321 (1916); *Texas Cement Co. v. McCord*, 233 U. S. 157, 34 Sup. Ct. 550 (1914); *United States Fid. & G. Co. v. United States*, 231 U. S. 237, 34 Sup. Ct. 88 (1913); *Title Guar. & T. Co. v. Crane*, 219 U. S. 24, 31 Sup. Ct. 140 (1910); *Mankin v. Ludowici-Celadon Co.*, 215 U. S. 533, 30 Sup. Ct. 174 (1910); *Davidson Marble Co. v. Gibson*, 213 U. S. 10, 29 Sup. Ct. 324 (1909); *U. S. Fid. Co. v. Struthers-Wells Co.*, 209 U. S. 306, 28 Sup. Ct. 337 (1908); *United States v. Amer. Sur. Co.*, 200 U. S. 197, 26 Sup. Ct. 168 (1906).

"The objection in the present case is merely technical, as the parties stipulated to waive trial by jury, and the case was heard and decided by the district judge upon facts about which there is no dispute. The question has not been raised heretofore in this court, but it has been assumed in many cases that the action to be brought under the statute upon the contractor's bond; whether the action were instituted by the United



## DECISIONS OF THE CIRCUIT AND DISTRICT COURTS

The earlier cases in the lower federal courts agreed with *Hendrick v. Lindsay*. They were somewhat shaken by the reasoning in *National Bank v. Grand Lodge* as to creditor beneficiaries, and some of them have made use of the subrogation theory set forth in *Keller v. Ashford*; but almost uniformly in a large number of cases they have been able to give to a third party the substantial relief that he would get in the state courts.<sup>20</sup> They have often said that the remedy is "in equity";

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States, or by the creditors in the name of the United States, was an action at law." *Hughes, J., in Illinois Sur. Co. v. Peeler, supra* at 223, 36 Sup. Ct. at 324.

<sup>20</sup> *Federal Surety Co. v. City of Staunton, supra* note 3; *Slavens v. Standard Acc. Ins. Co., 27 F. (2d) 859 (C. C. A. 9th, 1928)* (injured party sued on liability insurance policy); *Dunn v. Clinchfield R. R., 19 F. (2d) 810 (C. C. A. 6th, 1927)* (at law for a tort); *Compagnie Francaise v. Bonnasse, 19 F. (2d) 777 (C. C. A. 2d, 1927)* (in admiralty, following either law or equity); *First Nat. Bank v. Caples, 17 F. (2d) 87 (C. C. A. 5th, 1927)* (at law on a contractor's surety bond); *Duvall-Percival Trust Co. v. Jenkins, 16 F. (2d) 223 (C. C. A. 8th, 1926)* (at law in favor of the mortgagee against a grantee who had assumed the debt, the promisee not being personally bound); *Collins Mfg. Co. v. Wickwire Steel Co., 14 F. (2d) 871 (D. Mass. 1926)* (in equity, against a defendant who received assets and assumed debts); *Evans v. Sperry, 12 F. (2d) 438 (E. D. Ill. 1926)* (mortgagee sued grantee, and failed to prove a promise by the latter); *Smith & Co. v. Wilson, 9 F. (2d) 51 (C. C. A. 8th, 1925)* (at law, against one who assumed debts); *Town of Readsboro v. Hoosac T. & W. R. R., 6 F. (2d) 733 (C. C. A. 2d, 1925)* (action lay on a promise by defendant to keep a bridge in repair, the promisee being bound to plaintiff to do this); *Davis v. Dittmar, 6 F. (2d) 141 (C. C. A. 2d, 1925)* (promise to supply seaworthy barges); *In re Walker Grain Co., 3 F. (2d) 872 (C. C. A. 5th, 1925)* (trustee for creditors can sue on a bond to the United States for their benefit); *Mobile Shipb. Co. v. Federal Bridge & S. Co., 280 Fed. 292 (C. C. A. 7th, 1922)* (at law, defendant having assented thereto; certiorari denied, 260 U. S. 726, 43 Sup. Ct. 88 (1922)); *Phila. Rubber W. Co. v. U. S. Rubber R. Works, 277 Fed. 171 (C. C. A. 2d, 1921)* (bill in equity against the purchaser of a business who had assumed all its obligations).

*In re Roth, 272 Fed. 516 (N. D. Ohio 1920)* (a grantee who assumes mortgage debt is principal debtor); *Princess Amusement Co. v. Wells, 271 Fed. 226 (C. C. A. 6th, 1921)* (in equity); *Commercial Trust Co. v. Laurens Co., 267 Fed. 897 (S. D. Ga. 1920)* (bank taking over obligations and assets of a debtor bank can be sued in equity); *Gooch v. Buford, 262 Fed. 894 (C. C. A. 6th, 1920)* (wife sued at law on contract made by her husband for special hospital attendance); *In re H. L. Herbert & Co., 262 Fed. 682 (C. C. A. 2d, 1919)* *semble*; *Weinhard v. Thompson Est., 242 Fed. 315 (D. Ore. 1917)*; *Smith v. Robins, 236 Fed. 114 (C. C. A. 8th, 1916)*; *Gibson v. Victor Talking Mach. Co., 232 Fed. 225 (D. N. J. 1916)* (at law); *Silver King Coalition M. Co. v. Silver King Consol. M. Co., 204 Fed. 166 (C. C. A. 8th, 1913)* (in equity, to enforce defendant's promise to discharge plaintiff's unliquidated claim for a trespass); *Penn. Steel Co. v. N. Y. City Ry., 189 Fed. 661 (C. C. S. D. N. Y. 1911)* *semble*

and they have in a very few instances denied the plaintiff a remedy "at law,"<sup>21</sup> supposing that the Supreme Court so required. It can now be said to be well established, however, that an action "at law" will be sustained in the federal courts if that remedy would be available by the local law.<sup>22</sup> In addition, the

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(in equity); *Hanlon v. Smith*, 175 Fed. 192 (G. C. N. D. Iowa 1909); *Loose v. Hartford etc. Corp.*, 159 Fed. 318 (C. C. Conn. 1908) (in equity); *Gray v. Grand Trunk W. Ry.*, 156 Fed. 736 (C. C. A. 7th, 1907) (buyer of assets from a receiver who assumes all previous obligations can be sued at law by one having a claim for damages for a tort); *Bethlehem Iron Co. v. Hoadley*, 152 Fed. 735 (C. C. R. I. 1907) *semble* (at law); *Good-year Shoe Mach. Co. v. Dancel*, 119 Fed. 692 (C. C. A. 2d, 1902); same, 144 Fed. 679 (C. C. A. 2d, 1906) (in equity); *Quigley v. Spencer Stone Co.*, 143 Fed. 86 (C. C. A. 7th, 1906) (in equity, said to be no right "at law"); *Newport News v. Potter*, 122 Fed. 321 (C. C. A. 4th, 1903) (applying a Virginia statute); *Central Elec. Co. v. Sprague Elec. Co.*, 120 Fed. 925 (C. C. A. 7th, 1902) *semble* (at law); *Mercantile Trust Co. v. Baltimore & O. R. R.*, 94 Fed. 722 (C. C. S. D. Ohio 1899) (in equity); *Green v. Turner*, 86 Fed. 837 (C. C. A. 7th, 1898) *semble* (in equity); *Stephenson v. Monmouth M. & M. Co.*, 84 Fed. 114 (C. C. A. 6th, 1897) (at law on a contractor's surety bond); *Winters v. Hub. M. Co.*, 57 Fed. 287 (C. C. Idaho 1893) (in equity but not at law); *Orman v. N. Ala. Development Co.*, 53 Fed. 469 (C. C. N. D. Ala. 1892) (law); *Pope v. Porter*, 33 Fed. 7 (C. C. S. D. Iowa 1887) (law); *In re Lloyd*, 22 Fed. 88 (C. C. W. D. Pa. 1884) (creditor beneficiary can prove in bankruptcy); *Timayenis v. Union M. L. Ins. Co.*, 21 Fed. 223 (C. C. S. D. N. Y. 1884) (beneficiary of insurance policy sued at law); *Sonstiby v. Keeley*, 7 Fed. 447, 11 Fed. 578 (C. C. Minn. 1882) (law).

In *Penna. Cement Co. v. Bradley Con. Co.*, 7 F. (2d) 822 (C. C. A. 2d, 1925), the defendant promised a city to pay abutting owners all damages caused to them by certain subway construction. The court, following New York law, said that the plaintiff had a right as a beneficiary of this promise, but held that a condition precedent had not been fulfilled.

<sup>21</sup> *Goodyear Shoe Mach. Co. v. Dancel*, *supra* note 20 (plaintiff won in equity, after remedy at law was denied); *Winters v. Hub. M. Co.*, *supra* note 20 (remedy in equity only); *Jesup v. Illinois Cent. R. R.*, 43 Fed. 483 (C. C. N. D. Ill. 1890) (dictum); *Anderson v. Fitzgerald*, 21 Fed. 294 (C. C. S. D. Iowa 1884) (promise to pay subcontractor's creditors).

In *Quigley v. Spencer Stone Co.*, 143 Fed. 86 (C. C. A. 7th, 1906), X had promised the plaintiff to perform the plaintiff's duty to another to supply stone ballast for a railroad. The defendant promised X to perform this duty. *Held*, that the plaintiff could sue the defendant "in equity" for breach; but the court said there was no remedy "at law."

<sup>22</sup> *Union Mut. Ins. Co. v. Hanford*, *supra* note 13 (Illinois law); *Johns v. Wilson*, *supra* note 14 (Arizona law); *In re Roth*, 272 F. 516 (N. D. Ohio 1920); *Gibson v. Victor Talking M. Co.*, 232 Fed. 225 (D. N. J. 1916) (applying New Jersey law, and sustaining an action at law in favor of a creditor beneficiary; the court gave a very intelligent review of the cases); *Fish v. First Nat. Bank*, 150 Fed. 524 (C. C. A. 9th, 1907) (Alaska law); *Adams v. Shirk*, 105 Fed. 659 (C. C. A. 7th, 1901) *semble*.

In *Mobile Shipb. Co. v. Federal Bridge & S. Co.*, 280 Fed. 292 (C. C. A. 7th, 1922), where the plaintiff was a creditor beneficiary, the court thought its right was equitable only; but since there had been trial at:

federal courts will not refuse a remedy "in equity" even though the local law gives a remedy "at law" also.<sup>23</sup> The third party need not be a "sole" beneficiary and need not have been identified when the contract was made.<sup>24</sup> The contract may create a privilege in the third party as well as a right—a defense as well as a cause of action.<sup>25</sup> Occasionally the court avoids the issue by creating an artificial privity and finding that the plaintiff was a promisee.<sup>26</sup>

In a comparatively small number of cases, the federal court has denied the plaintiff a remedy for reasons that would likewise prevail in the state courts, but not because third parties have no rights because not in privity. Thus, the court may find that the plaintiff is at most a mere incidental beneficiary,

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law with the defendant's assent the court affirmed the judgment. The court said:

"The case was fully tried by the court without a jury. The facts respecting liability are not in serious dispute. The parties have fully and fairly litigated the question of damages. If we were to reverse the judgment, it would not be with directions to dismiss, but to transfer the cause from the law to the equity side of the calendar. The district judge who presided over the law action would sit as chancellor in the equity suit, and upon the same evidence no doubt make the same findings. Unless required by the rules and the established precedents, we are unwilling thus to pay tribute to form."

<sup>23</sup> Pittsburgh etc.' R. R. v. Keokuk & H. Bridge Co., 68 Fed. 19 (C. C. A. 7th, 1895).

<sup>24</sup> Central Trust Co. v. Berwind-W. Coal Co., 95 Fed. 391 (C. C. S. D. N. Y. 1899) held that a mortgagee could sue a coal lessee who had promised to pay royalties for coal mined to the mortgagee for interest on the mortgage debt. The court said, "It is not required that the benefit of the plaintiff should be the sole object of the agreement."

In Barker v. Pullman's P. Car Co., 124 Fed. 555 (C. C. S. D. N. Y. 1903), a debtor transferred its assets to the defendant and the latter assumed all its debts. The creditor was held to have an enforceable right against the defendant. "The question is not free from doubt, but this court is of the opinion that it was not necessary to name the creditors of the Wagner Co., or specify their respective claims, their nature or amount, or that the benefit of such creditors should have been the sole object of this clause of the agreement."

<sup>25</sup> Central Trust Co. v. Cincinnati, J. & M. Ry., 58 Fed. 500 (C. C. N. D. Ohio 1892) held that if a creditor accepts the bonds of a newly organized company in satisfaction of the debt of an old company, the latter as beneficiary of the contract is thereby discharged even though it says and does nothing in the matter. Taft, J., rendering the opinion, cited Hendrick v. Lindsay, *supra* note 4, as authority.

<sup>26</sup> American Can Co. v. Garnett, 279 Fed. 722 (C. C. A. 9th, 1922). The defendant promised a patentee to make and supply the article to the patentee's agents on certain terms. The court held that the agents became parties to this contract and could sue for its breach. Certiorari was denied, 260 U. S. 722, 43 Sup. Ct. 12 (1922).

Adams v. Shirk, *supra* note 22 (plaintiff's assent to the undertaking by the defendant as assignee of a lease held to make him a promisee and hence in privity).

the parties not having intended him to benefit by the contract.<sup>27</sup> The suit may be on a contractor's surety bond, and the court may follow the rule in some minority state refusing the plaintiff a remedy.<sup>28</sup> There may have been an agreement between the plaintiff and the promisor that contradicts the inference that the plaintiff was a beneficiary of the new contract.<sup>29</sup> Or the third party's right may have been subject to a condition precedent that has not been fulfilled.<sup>30</sup>

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<sup>27</sup> In re Gubelman, 13 F. (2d) 730 (C. C. A. 2d, 1926) (a banking agency contract, of which the plaintiff was a mere incidental beneficiary; there are some statements in the opinion that the federal decisions do not sustain); American Exch. Bank v. Northern Pac. R. R., 76 Fed. 130 (C. C. N. D. Wash. 1896); Jackson Iron Co. v. Negaunee Con. Co., 65 Fed. 298 (C. C. A. 6th, 1895). (defendant's promise was in the alternative giving him option to pay another than the plaintiff).

In Sayward v. Dexter, Horton & Co., 72 Fed. 758 (C. C. A. 9th, 1896), a creditor made a contract with another person whereby that other person was to market the debtor's goods and was to make payments to the creditor, the latter promising not to sue his debtor so long as the payments were made as agreed. The creditor later sued the debtor, and the latter set up the contract not to sue. The court held that the contract was a marketing agreement made for the benefit of the contracting parties alone and that it gave the debtor no defense. The decision should not be followed.

<sup>28</sup> Federal Sur. Co. v. Minneapolis S. & M. Co., 17 F. (2d) 242 (C. C. A. 8th, 1927) (applied what the court erroneously believed to be Montana law and denied the third party a right under a contractor's surety bond); United States F. & G. Co. v. Vermont Marble Co., 16 F. (2d) 83 (C. C. A. 7th, 1926) (same, following Minnesota cases as to contractor's bonds); Sturtevant Co. v. Fidelity & D. Co., 275 Fed. 114 (S. D. N. Y. 1921) (followed a recent New York decision denying a materialman a remedy "at law," but suggested a remedy "in equity"; affirmed in 285 Fed. 367 (C. C. A. 2d, 1922)); National Sur. Co. v. Brown-Graves Co., 7 F. (2d) 91 (C. C. A. 6th, 1925) (laborers and materialmen too remote where the surety bond was given to lenders of capital to protect them against liens on the building in which the capital was used).

In Minneapolis S. & M. Co. v. Federal Sur. Co., 34 F. (2d) 270 (C. C. A. 8th, 1929), a second hearing of the first case cited in this note, the court adhered to its first decision, even though a Montana decision had meantime shown the error as to Montana law. This time, however, the decision was put on the ground that by the terms of the bond the plaintiff was not made a beneficiary.

<sup>29</sup> Constable v. National S. S. Co., *supra* note 17.

<sup>30</sup> In Penna. Steel Co. v. New York City Ry., 198 Fed. 721 (C. C. A. 2d, 1912), a lessee from a mortgagor assumed and promised to pay the debt secured; it was held that this was a promise to pay a deficiency only and that foreclosure was a condition precedent—a doubtful interpretation. But the court said:

"In England and in some of the States the rule is adhered to that the only persons who can sue upon a contract are the parties; that a third person for whose benefit a contract is made cannot maintain an action upon it. The reason for the rule is said to be that there is no privity between the contracting party making the promise and the third person

## IS THE THIRD PARTY'S RIGHT LEGAL OR EQUITABLE?

It should be evident from what is written above that there is no "federal" system apart from the state systems and that the third party has no "federal" right with a uniform character of its own distinct and apart from his right in the state courts. But in the federal courts there are still procedural distinctions between "law" and "equity" and there still lingers a trace of the notion that a right "in equity" differs from a right "at law" in some "substantive" way, quite independent of remedy and procedure. This has caused a good deal of argument over whether the right of a beneficiary was "in equity" or "at law."

This is a dispute over words and forms of remedy. In actual results, in what the court in fact does for the beneficiary and against the promisor, there is no very substantial difference between the cases saying that the right is "in equity" and those giving a remedy "at law." The beneficiary gets the money and the promisor has to pay it. There is some difference in the form of pleadings. In the equity suit the parties have no right to a trial by jury, although the court may make use of a jury if it desires. The beneficiary's right is no less "direct" in the one case than in the other, for the third party is suing the promisor "directly" in either case and the judgment or decree is for a "direct" payment. By the "subrogation" theory it might be supposed that the third party can win only in case he has a valid claim against the promisee and the latter has a valid claim against the promisor, that there may be defenses available to the promisor "in equity" that would not be available to him if the third party's remedy is held to be "at law." The actual decisions do not show this to be the case.<sup>31</sup> The subrogation theory, when resorted to by the plaintiff, always gets him his decree for payment, except in those cases where his action at law would likewise be defeated. Defenses that are good "in equity" are available "at law" also; and it is believed that defenses that would fail "at law" will equally fail "in equity."

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and that the consideration does not move directly from the latter. The rule has the merit of simplicity but is calculated to permit injustice. It is founded, too, upon wholly artificial distinctions. There is no real and substantial reason why, if the parties to a contract recognize the interest of a third person in it and desire and intend to give him a right of action upon it, they should not be able to do so. And the prevailing doctrine in this country is contrary to the English rule. It is generally held, subject to qualifications, that a third person may sue upon a promise made to another for his benefit. *Ibid.* 749.

<sup>31</sup> *Duvall-Percival Trust Co. v. Jenkins*, *supra* note 3, was a case that could not rest on a theory of subrogation. The defendant was a mortgagor's grantee who assumed the debt, but the mortgagor (promisee) was not himself bound to pay it. The mortgagee was given judgment; the federal court sitting in Kansas applied the law of Missouri.

Of course there are equitable remedies, such as injunction and specific performance, that were not available at common law and that must still be petitioned for in the federal courts in accordance with "equity" pleading; but this does not mean that the right being enforced was not a "legal" right.

The Supreme Court has rightly determined that the difference is only one of form of remedy. Thus, in an action "at law," by a mortgagee against a grantee who had assumed the debt, Mr. Justice Gray said: "The form of his remedy, whether it must be in covenant or in assumpsit, at law or in equity, is governed by the *lex fori*, the law of the District of Columbia, where the action was brought"; and the Court gave judgment for the defendant.<sup>32</sup> This has at times been understood to mean that the federal courts constitute a single "forum," and that in those courts the only remedy available to a third party beneficiary is "in equity."<sup>33</sup> That Justice Gray did not mean this is shown by the opinion of the Court, written by himself, in a later case.<sup>34</sup> Instead, the decision meant only that if the law of the District of Columbia recognized no right enforceable by a remedy at law, that law would be applied in a suit brought in the District of Columbia.

Statutory reformation of procedure, the abolition of common law forms of action, and the joinder of common law and equity, are slowly having their effect upon the legal profession and are breaking down the conception of law and equity as necessarily separate and independent systems. It is now settled that if, by the state law that the federal court selects as that by which the rights of the parties are determined, the third party can recover a judgment for damages against the promisor without the use of equity forms and terminology, he can recover in the federal court in the same manner. That is, as the courts may put it, if the plaintiff could recover in an action at law in the state court, he can do the same in the federal court and is not compelled to bring a bill in equity.

The state law cannot empower a federal court to give a remedy that the federal law does not empower it to give; but the federal law fully empowers the federal courts to give all the remedies that courts of common law and courts of equity have been accustomed to give. Therefore, when a state recognizes that a third party has a right against a promisor, enforceable by a judgment for money damages, the federal court has power to

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<sup>32</sup> Willard v. Wood, *supra* note 11.

In a later case between the same parties, the mortgagee's bill in equity was dismissed on the ground of laches. Willard v. Wood, *supra* note 12.

<sup>33</sup> See Goodyear Shoe M. Co. v. Dancel, 119 Fed. 692 (C. C. A. 2d, 1902).

<sup>34</sup> Union Ins. Co. v. Hanford, *supra* note 13.

give a like remedy derived from the federal law that created the court.<sup>35</sup>

#### THE BENEFICIARY'S RIGHT IN ADMIRALTY

A federal judge, sitting in his customary chair, or on his usual bench, changes his juristic coat with chameleon-like rapidity. Now he is a judge at common law; next he is a chancellor in equity; again he wears the gold lace of the Lord High Admiral; soon he puts on the dusty shoes of the merchant judge who administered the law merchant in the court of Pipowder (*pied poudre*); he administers the law of taxation and finance, perhaps without observing that he is sitting before the checkered table with the Barons of the Exchequer; through it all he continually applies rules laid down for him by constitutions and by legislatures, seldom being told whether in so doing he is a law judge, a chancellor, or an admiral. He must be puzzled occasionally to know in what capacity he sits on his single bench and whence comes the law that he applies. In whichever capacity he sits, he cannot escape from the petitions of the third party beneficiary. And so we have cases "in admiralty" as well as "in equity" and "at law"; and we find our court with Joseph's coat sustaining a libel "in admiralty"<sup>36</sup> in behalf of the beneficiary as well as a bill "in equity" or *assumpsit* "at law." The right that the admiral is enforcing is the same right that he enforces as a judge or a chancellor; the remedies that he gives will produce substantially the same results, but his procedure will have a rolling gait and his language will carry a salty flavor.

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<sup>35</sup> Thus where the state law gives a mechanic's lien enforceable by both legal and equitable remedies, the fact that there is a remedy at law does not prevent the federal court from giving its usual equitable remedy. *Sheffield Furnace Co. v. Witherow*, 149 U. S. 574, 13 Sup. Ct. 936 (1893).

<sup>36</sup> *Compagnie Francaise v. Bonnasse*, 19 F. (2d) 777 (C. C. A. 2d, 1927); *Munich Ins. Co. v. Dodwell*, 128 Fed. 410 (C. C. A. 9th, 1904); see also *Hagan v. Scottish Union Ins. Co.*, *supra* note 7; *Constable v. National S. S. Co.*, *supra* note 17.