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Deed of Trust Mortgage: Foreclosure Problems Student Symposium - Texas Land Titles: Part II Student Symposium.

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DEED OF TRUST MORTGAGE: FORECLOSURE PROBLEMS

A deed of trust is a mortgage agreement which enables the trustee to conduct a nonjudicial foreclosure in order to enforce the mortgage.[585] Since Texas follows the lien theory of mortgages, the mortgagor retains title to the real estate pledged as security.[586] The mortgagee holds neither title nor a possessory right to the mortgaged property[587] but does retain a "security interest" which affords a right to the proceeds realized from a foreclosure sale.[588]

The question of who has title to real estate subject to a deed of trust does not generally arise until after foreclosure. Much of the litigation involving deeds of trust, therefore, focuses on the question of whether a foreclosure sale was valid, clearly transferring title from the mortgagor to the purchaser.[589]

The law of notice regarding trustee's sales must be strictly followed in order to accomplish a valid foreclosure.[590] In *Crow v. Heath*[591] the court distinguished two types of notice—notice of trustee's sale as op-

585. Johnson v. Snell, 504 S.W.2d 397, 399 (Tex. 1973); McLane v. Paschal, 47 Tex. 365, 369 (1877); Phillips v. Campbell, 480 S.W.2d 250, 253 (Tex. Civ. App.—Houston [14th Dist.] 1972, writ ref'd n.r.e.); Lucky Homes, Inc. v. Tarrant Sav. Ass'n, 379 S.W.2d 386, 388 (Tex. Civ. App.—Fort Worth 1964), *rev'd on other grounds*, 390 S.W.2d 473 (Tex. 1965); Graham & Locke Inv., Inc. v. Madison, 295 S.W.2d 234, 242 (Tex. Civ. App.—Dallas 1956, writ ref'd n.r.e.).

586. *See* Warnecke v. Broad, 138 Tex. 631, 634, 161 S.W.2d 453, 454 (1942); Texas Loan Agency v. Gray, 34 S.W. 650, 651 (Tex. Civ. App. 1896, writ ref'd).

Under the title theory of mortgages, the mortgagee would have a right to possession prior to default. Lightcap v. Bradley, 58 N.E. 221, 223 (Ill. 1900).

587. *See* Warnecke v. Broad, 138 Tex. 631, 634, 161 S.W.2d 453, 454 (1942); Lucky Homes, Inc. v. Tarrant Sav. Ass'n, 379 S.W.2d 386, 388 (Tex. Civ. App.—Fort Worth 1964), *rev'd on other grounds*, 390 S.W.2d 473 (Tex. 1965).

Under the lien theory of mortgages, title can be taken from the mortgagor only by a foreclosure. Foster v. Millinger, 8 S.W.2d 514, 515 (Tex. Civ. App.—San Antonio 1928), *aff'd*, 17 S.W.2d 768 (Tex. Comm'n App. 1929, jdgmt adopted). The basis for this reasoning is that the parties always intended a debtor-creditor relationship, rather than that of a vendor-vendee. This intent is looked on as *ab initio* as long as there is an underlying debt. Duffy, *The Character of Morgages of Real Estate in Texas*, 12 S. TEX. L.J. 129, 131 (1970).

588. Duffy, *The Character of Mortgages of Real Estate in Texas*, 12 S. TEX. L.J. 129, 135 (1970).

589. *E.g.*, Crow v. Heath, 516 S.W2d. 225 (Tex. Civ. App.—Corpus Christi 1974, no writ); Calverley v. Gunstream, 497 S.W.2d 110 (Tex. Civ. App.—Dallas 1973, writ ref'd n.r.e.); French v. May, 484 S.W.2d 420 (Tex. Civ. App.—Corpus Christi 1974, writ ref'd n.r.e.).

590. *See also* Chamberlain v. Trammell, 131 S.W. 227, 229 (Tex. Civ. App. 1910, writ dism'd); Roedenbeck Farms v. Brousard, 124 S.W.2d 929, 935 (Tex. Civ. App.—Beaumont), *writ ref'd per curiam*, 133 Tex. 126, 127 S.W.2d 168 (1938), *appeal dism'd per curiam*, 308 U.S. 514 (1939).

591. 516 S.W.2d 225 (Tex. Civ. App.—Corpus Christi 1974, no writ).

posed to notice of intention to accelerate an obligation to pay a debt evidenced by a note.[592] A valid notice of the sale must follow either the statutory requirements[593] or the notice provisons of the deed of trust itself.[594] Under the statutory requirements personal notice to the mortgagor is not required;[595] however, if the deed of trust provisions require personal notice, they must be followed.[596] Additionally, any time the mortgagee has chosen to exercise the option of an acceleration clause, the courts have required that the mortgagor be given "actual notice" of the demand for payment and of the mortgagee's desire to accelerate the entire balance of the debt.[597] The courts in Texas have looked with disfavor on the exercise of an acceleration clause because of the inequities which may result.[598] It is for this reason that there must be "actual notice" to the mortgagor which is "clear, positive, and unequivocal" when the mortgagee exercises the option to accelerate payment of the debt.[599] Thus, the rationale for notice requirements is to protect the mortgagor for two reasons: first, to encourage as many bidders as possible at the foreclosure sale in order to obtain an adequate price and avoid a later deficiency action,[600] and second, to pro-

592. *Id.* at 228; *accord*, Lockwood v. Lisby, 476 S.W.2d 871, 873 (Tex. Civ. App.—Fort Worth 1972, writ ref'd n.r.e.).

593. TEX. REV. CIV. STAT. ANN. art. 3810 (1966). *But see* Goode v. Davis, 135 S.W.2d 285, 292 (Tex. Civ. App.—Fort Worth 1939, writ dism'd jdgmt cor.) (article 3810 is for the benefit of the mortgagor and may be waived by him).

594. Roedenbeck Farms v. Brousard, 124 S.W.2d 929, 935 (Tex. Civ. App.—Beaumont), *writ ref'd per curiam*, 133 Tex. 126, 127 S.W.2d 168 (1938), *appeal dism'd per curiam*, 308 U.S. 514 (1939).

595. TEX. REV. CIV. STAT. ANN. art. 3810 (1966). The statute requires merely public notice of the trustee's sale. Fischer v. Simon, 95 Tex. 234, 241, 66 S.W. 447, 449 (1902); Koehler v. Pioneer Am. Ins. Co., 425 S.W.2d 889, 892 (Tex. Civ. App.—Fort Worth 1968, no writ); *see* Comment, *Nonjudicial Foreclosure Under a Deed of Trust: Some Problems of Notice*, 49 TEXAS L. REV. 1085, 1087-1091 (1971).

596. TEX. REV. CIV. STAT. ANN. art. 3810 (1966); *see* Smith v. Allbright, 279 S.W. 852, 854 (Tex. Civ. App.—Austin 1925), *rev'd on other grounds*, 5 S.W.2d 970 (Tex. Comm'n App. 1928, jdgmt adopted).

597. Covington v. Burke, 413 S.W.2d 158, 160 (Tex. Civ. App.—Eastland 1967, writ ref'd n.r.e.); Jernigan v. O'Brien, 303 S.W.2d 515, 516 (Tex. Civ. App.—Austin 1957, no writ).

An "acceleration clause" generally empowers the mortgagee in the event of a default by the mortgagor to advance the date of maturity of the mortgage debt or to declare it be due. McCormick v. Dagget, 257 S.W. 358, 361 (Ark. 1924); *see* Covington v. Burke, 413 S.W.2d 158 (Tex. Civ. App.—Eastland 1967, writ ref'd n.r.e.).

598. Motor & Indus. Fin. Corp. v. Hughes, 157 Tex. 276, 289, 302 S.W.2d 386, 394 (1957); Crumley v. Ramsey, 93 S.W.2d 191, 192-93 (Tex. Civ. App.—Waco 1936, writ ref'd). *See generally* 39 TEX. JUR. 2d *Mortgages and Trust Deeds* §§ 77-81 (1962).

599. Motor & Indus. Fin. Corp. v. Hughes, 157 Tex. 276, 289, 302 S.W.2d 386, 394 (1957); Crumley v. Ramsey, 93 S.W.2d 191, 192-93 (Tex. Civ. App.—Waco 1936, writ ref'd).

600. Goode v. Davis, 135 S.W.2d 285, 292 (Tex. Civ. App.—Fort Worth, 1939, writ

vide the mortgagor with a last chance to avoid the necessity of a sale.[601]

The only notice which the mortgagor received in *Crow* was a copy of the letter sent to his vendee who had assumed the mortgage. This letter indicated merely the mortgagee's desire to foreclose on the property pledged as security, without any indication of the mortgagee's desire to accelerate payment of the note involved. The notice by letter did not afford the mortgagor the opportunity to remedy the default of his vendee or provide that failure to remedy the breach would accelerate the note involved.[602] Thus the court found the sale did not meet the requisite standards of notice for a valid trustee's sale.

The lack of "actual notice" would, in itself, have been adequate grounds for setting aside the foreclosure sale,[603] but the judgment was also based on the inadequacy of the purchase price paid at the trustee's sale.[604] In Texas the mere inadequacy of price at a foreclosure sale is not sufficient justification for the cancellation of a trustee's deed.[605] There must be "proof of inadequacy of price coupled with a circumstance tending to establish a wrongdoing" in order for a trustee's sale to be set aside.[606] The "wrongdoing" in *Crow* was the lack of proper notice.[607]

The finding of inadequate consideration is also important in determining the mortgagor's remedy. The supreme court has held that when a trustee's sale is invalid but title has passed to a third person or the property has been appropriated by the mortgagee, the mortgagor is "entitled to have the reasonable market value of the property credited on the note . . . ."[608]

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dism'd jdgmt cor.); see Phipps v. Fuqua, 32 S.W.2d 660, 662 (Tex. Civ. App.—Amarillo 1930, writ ref'd); Reisenberg v. Hankins, 258 S.W. 904, 909 (Tex. Civ. App.—Amarillo 1924, writ dism'd).

601. *See* Reisenberg v. Hankins, 258 S.W. 904, 909 (Tex. Civ. App.—Amarillo 1924, writ dism'd).

602. Crow v. Heath, 516 S.W.2d 225, 229 (Tex. Civ. App.—Corpus Christi 1974, no writ).

603. Covington v. Burke, 413 S.W.2d 158, 160 (Tex. Civ. App.—Eastland 1967, writ ref'd n.r.e.).

604. Crow v. Heath, 516 S.W.2d 225, 228 (Tex. Civ. App.—Corpus Christi 1974, no writ).

605. Tarrant Sav. Ass'n v. Lucky Homes, Inc., 390 S.W.2d 473, 475 (Tex. 1964).

606. Crow v. Heath, 516 S.W.2d 225, 228 (Tex. Civ. App.—Corpus Christi 1974, no writ); *accord*, Biddle v. National Old Line Ins. Co., 513 S.W.2d 135, 138 (Tex. Civ. App.—Dallas 1974, writ ref'd n.r.e.); Jacobson v. National W. Life Ins. Co., 403 S.W.2d 528, 531 (Tex. Civ. App.—Houston 1966, no writ).

607. Crow v. Heath, 516 S.W.2d 225, 228 (Tex. Civ. App.—Corpus Christi 1974, no writ).

608. Tarrant Sav. Ass'n v. Lucky Homes, Inc., 390 S.W.2d 473, 475 (Tex. 1965). Applying this rule to *Crow* no deficiency existed on the $15,000 note since the trial

The general rule regarding the trustee's conduct is that he must strictly follow the instructions in the deed of trust provisions.[609] This rule is imposed because the deed of trust is the sole source of the trustee's power and because of the harshness resulting to the mortgagor from a foreclosure sale.[610] In those situations in which the deed of trust provisions are clearly violated by the trustee's conduct, the mortgagor may have the foreclosure sale declared a nullity.[611] For example, a trustee may appoint an attorney in fact to conduct the foreclosure,[612] but an unauthorized third person may not conduct the sale.[613] Any foreclosure conducted prior to a mortgagor's default would clearly violate the deed of trust provisions.[614]

The case of *French v. May*[615] illustrates an exception to the requirement that the trustee follow the instructions in the deed of trust. The deed of trust in *French* required that the trustee conduct any necessary foreclosure at a "public auction to the highest bidder for cash."[616]

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court found the reasonable market value of the property sold to be $28,675.00. Crow v. Heath, 516 S.W.2d 225, 229 (Tex. Civ. App.—Corpus Christi 1974, no writ). In *Crow* the mortgagee appropriated the property to his own use.

If the sale was invalid, but the property is retained by the mortgagor the mortgagee may by alternative pleading request a judicial foreclosure. John Hancock Mut. Life Ins. Co. v. Howard, 85 S.W.2d 986, 988 (Tex. Civ. App.—Waco 1935, writ ref'd). *See generally* 38 TEX. JUR. 2d *Mortgages and Trust Deeds* § 158 (1962).

609. Slaughter v. Qualls, 139 Tex. 340, 346, 162 S.W.2d 671, 675 (1942); Michael v. Crawford, 108 Tex. 352, 354, 193 S.W. 1070 (1917).

The provisions in a deed of trust may also be applicable against mortgagors, Criswell v. Southwestern Fidelity Life Ins. Co., 373 S.W.2d 893, 895 (Tex. Civ. App.—Houston 1963, no writ) (tenant at will provision applicable against mortgagor when invoked by purchaser at foreclosure through a forcible detainer action). The deed of trust may also provide the mortgagee with the power to appoint a substitute trustee. When the deed of trust requires that the appointment be filed in the county clerk's office, the substitute trustee has no power until his appointment has been filed. Therefore, any sale before the filing will be nullified. Faine v. Wilson, 192 S.W.2d 456, 459-60 (Tex. Civ. App.—Galveston 1946, no writ).

610. Smith v. Allbright, 279 S.W. 852, 854 (Tex. Civ. App.—Austin 1925), *aff'd*, 288 S.W. 178 (Tex. Comm'n App. 1926, jdgmt adopted). The legal presumption of regularity which prevails over judicial foreclosures does not prevail over trustee's sales. *Id.* at 854.

611. Slaughter v. Qualls, 139 Tex. 340, 346, 162 S.W.2d 671, 675 (1942). When a bona fide purchaser acquires land which has been sold through a void foreclosure, the mortgagor may not regain title from the bona fide purchaser. The reason for this rule is that the mortgagor, through the deed of trust, created the apparent power in the trustee to convey the land. It would be inequitable to permit a former mortgagor to regain land from those who have purchased in good faith on the basis of the "apparent" power. *Id.* at 346, 162 S.W.2d at 675.

612. Natalia v. Witthaus, 134 Tex. 513, 525, 135 S.W.2d 969, 976 (1940).

613. Slaughter v. Qualls, 139 Tex. 340, 346, 162 S.W.2d 671, 675 (1942).

614. *Id.* at 346, 162 S.W.2d at 675.

615. 484 S.W.2d 420 (Tex. Civ. App.—Corpus Christi 1972, writ ref'd n.r.e.).

616. *Id.* at 425.

Since the trustee actually sold the land on credit, the mortgagor alleged that the sale was void.[617]

The civil appeals court upheld the validity of the foreclosure, relying on the authority of *Chase v. First National Bank*.[618] In *Chase* the facts were similar, and the supreme court upheld the sale on the rationale that there was "no injury [to] the mortgagor, or those claiming under him."[619] This was also true in *French* because the purchase on credit relieved the debtor of any deficiency claim. Other relevant considerations were the absence of fraud and any unreasonable action by the trustee.[620]

The *French* and *Chase* cases exemplify an exception to the general rule that the trustee should strictly follow the deed of trust provisions, and their holdings should therefore be applied only to fact situations of an essentially identical nature. Their basic rationale, benefit to the mortgagor as grounds for upholding the foreclosure, should not be taken as a talismanic rule upholding foreclosures even when the trustee's instructions are not followed. A broad application of this rationale would cause many determinations of the validity of foreclosures to turn merely on subjective fact questions.

An essential procedure for a mortgagor whose land has been sold under a foreclosure and who desires to recover title is to bring a suit before the applicable statute of limitations has run. Different periods of limitation apply in different types of suits to overturn foreclosure: when a foreclosure is void, the 10-year statute of limitations governing actions for recovery of land applies;[621] when a foreclosure is merely voidable, however, suit must be brought within 4 years from the time the cause of action accrued.[622]

The test of whether the trustee's deed is void or voidable depends on the effect on title at the time it was executed and delivered. If the deed is a mere nullity, it is void, but if title is passed by the deed, subject to being set aside because of an improper sale, it is voidable.[623]

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617. *Id.* at 425.

618. 20 S.W. 1027 (Tex. Civ. App. 1892, no writ).

619. Id. at 1029. *See also* First Fed. Sav. & Loan Ass'n v. Sharp, 359 S.W.2d 902, 903 (Tex. 1962) (bidder allowed time to obtain cash while sale is being conducted).

620. French v. May, 484 S.W.2d 420, 425 (Tex. Civ. App.—Corpus Christi 1972, writ ref'd n.r.e.).

621. TEX. REV. CIV. STAT. ANN. art. 5523a (1958); *see* Slaughter v. Qualls, 139 Tex. 340, 345, 162 S.W.2d 671, 674 (1942).

622. TEX. REV. CIV. STAT. ANN. art. 5529 (1958); Slaughter v. Qualls, 139 Tex. 340, 345, 162 S.W.2d 671, 674 (1942).

623. Slaughter v. Qualls, 13 Tex. 340, 345, 162 S.W.2d 671, 674 (1942); *accord,*

Calverley v. Gunstream[624] was a suit to recover title to land which had been foreclosed and, alternatively, for damages for wrongful foreclosure. Defendant Gunstream had conveyed land by warranty deed in August, 1954 to plaintiffs, Mr. and Mrs. Calverley. As consideration for the purchase the Calverleys executed a note to Gunstream secured by a deed of trust. In June, 1958 the trustee foreclosed the land and executed a deed to Gunstream. The trustee's deed contained a recital that the mortgagor had defaulted on the note secured by the deed of trust. The plaintiffs did not file suit to overturn the foreclosure until March, 1972, thus encountering the dual problem of overcoming the statute of limitations as well as the recitals in the trustee's deed.[625]

The court of civil appeals affirmed the lower court's holding that article 5523a barred any relief prayed for based on the invalidity of the trustee's sale.[626] The purpose of the limitation statute is to safeguard the titles of vendees claiming under a trustee's deed against attacks based on facts which could have been ascertained in a timely suit after the recording of the trustee's deed.[627] Both grounds of attack asserted by the plaintiffs—lack of default and want of personal notice of the foreclosure—were not apparent from "matters of record," meaning the recitals in the trustee's deed. Therefore, since the plaintiff's claim was based on evidence extrinsic to the recorded document, the statute of limitations prevented recovery of the land.[628]

Addressing a question of first impression in Texas, the court in *Calverley* held that article 5523a does not apply to a suit for damages for wrongful foreclosure.[629] The court explained that in an action for damages the validity of the trustee's deed and its effectiveness to pass title are not questioned; thus, there is no question of title, and article 5523a is inapplicable.[630]

The plaintiffs in *Calverley* were granted a remand for a determination of whether the foreclosure was wrongful on the ground that no

Slaughter v. Qualls, 139 Tex. 340, 346, 162 S.W.2d 671, 675 (1942) (void foreclosure; no default by mortgagor); Cline v. Cline, 323 S.W.2d 276, 284 (Tex. Civ. App.—Houston 1959, writ ref'd n.r.e.) (voidable foreclosure; inadequate price at trustee's sale coupled with failure to give adequate notice of sale to mortgagor); Wilie v. Hays, 207 S.W. 427 (Tex. Civ. App.—Austin 1918, no writ) (void foreclosure; failure to give notice of trustee's sale).

624. 497 S.W.2d 110 (Tex. Civ. App.—Dallas 1973, no writ).
625. *Id.* at 112-13.
626. *Id.* at 114-15.
627. *Id.* at 114.
628. *Id.* at 114-15.
629. *Id.* at 116.
630. *Id.* at 116.

default had occurred.[631] This was allowed despite the recitals in the trustee's deed that there had been a default on the note secured by the deed of trust. This illustrates the possibility that deed recitals may be rebutted by parol evidence in a trial where the validity of a foreclosure is in doubt. It is standard in Texas for a deed of trust to contain instructions regarding its recitals.[632] A trustee's deed will generally recite the mortgagor's default, the request of the mortgagee to conduct the sale, and instructions for posting of the written notices of sale.[633] The recitals in the trustee's deed usually constitute prima facie evidence that all prerequisites for a valid foreclosure have been followed.[634] It is now established that the recitals in the trustee's deed may be rebutted in suits which are not barred by the statute of limitations.[635] Thus, if the plaintiffs in *Calverley* had timely filed their suit to recover title, parol testimony to rebut the recitals in the trustee's deed would have been admissible.

The inherent validity of a foreclosure pursuant to a deed of trust is governed essentially by the trustee's actions. If the trustee's sale is conducted in accordance with the deed of trust provisions and the statute regarding notice for a foreclosure, the foreclosure may be successfully defended. In those suits which are filed prior to the running of the statute of limitations or which do not affect the title to land, the recitals in a trustee's deed may be rebutted.

COLLATERAL PROCEEDINGS

Collateral proceedings which may prevent a valid nonjudicial foreclosure are those in which mortgaged property comes in to the custody of a court. Property may not be effectively foreclosed if it has previously been subject to any of four other judicial proceedings: bankruptcy in federal courts,[636] pendency of receivership in the state

631. *Id.* at 116.

632. *See* R. STAYTON, TEXAS FORMS § 3684 (1960). These instructions must be strictly followed. *See* Smith v. Allbright, 279 S.W. 852, 854 (Tex. Civ. App.—Austin 1925), *rev'd on other grounds*, 5 S.W.2d 970 (Tex. Comm'n App. 1928, jdgmt adopted).

633. *See* R. STAYTON, TEXAS FORMS § 3745 (1960).

634. *See id* § 3684. For case law sanctioning this interpretation of the recitals in the trustee's deed see Adams v. Zellner, 107 Tex. 653, 654, 183 S.W. 1143, 1144 (1916); Cline v. Cline, 323 S.W.2d 276, 283 (Tex. Civ. App.—Houston 1959, writ ref'd n.r.e.); Faine v. Wilson, 192 S.W.2d 456, 458 (Tex. Civ. App.—Galveston 1946, no writ).

635. Slaughter v. Qualls, 139 Tex. 340, 348, 162 S.W.2d 671, 676 (1942).

636. On the filing of a petition in bankruptcy, the property of a bankrupt mortgagor will come into the custody of the bankruptcy court. *Ex parte* Baldwin, 291 U.S. 610, 615 (1934). This rule applies even if the property is not located within the jurisdic-

court,[637] injunctions against the trustee from exercising his power of sale,[638] or custody and control of state courts sitting in probate matters.[639]

The case of *Hutchison v. Bristol Court Properties, Ltd.*[640] illustrates the mortgagor's burden of proof to obtain a temporary injunction against the exercise of the trustee's sale. In *Hutchis*on a note holder refused to advise the debtor of the amount past due. The court found that such conduct, in itself, was sufficient to invoke its equity powers to prevent acceleration and the trustee's sale.[641] To obtain a temporary injunction the relator must prove only a "probable right to a permanent injunction and probable injury if the temporary injunction is not granted."[642] Therefore, the burden of proof required for a temporary injunction against the exercise of a trustee's sale is less onerous than that required for a permanent injunction. This is significant because a mortgagor may take advantage of the time allowed by a temporary injunction to remedy a minor breach, preventing the harshness of a nonjudicial foreclosure.

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tional boundaries of the federal district court where the bankruptcy proceeding originated. Isaacs v. Hobbs Tie & Timber Co., 282 U.S. 734, 737-38 (1930).

Most sales pursuant to a deed of trust are invalid if completed after the bankruptcy proceeding. *Compare* Cohen v. Nixon & Wright, 236 F. 407 (S.D. Ga. 1916); *In re* Hasie, 206 F. 789 (N.D. Tex. 1913) *with In re* Smith, 3 F. Supp. 40 (S.D. Tex. 1924), *aff'd*, 8 F.2d 1021 (5th Cir. 1925); Bray v. Aikin, 60 Tex. 688 (1884); Saunders v. Given, 79 S.W.2d 310 (Tex. Civ. App.—El Paso), *cert. denied*, 293 U.S. 599 (1934); Nations v. First Real Estate & Inv. Co., 13 S.W.2d 949 (Tex. Civ. App.—El Paso 1929, no writ).

637. A trustee's sale of property placed in charge of a receiver is void. Hacker v. Hacker, 4 S.W.2d 218, 221 (Tex. Civ. App.—Galveston 1928, no writ); *accord*, Cline v. Cline, 323 S.W.2d 276, 282 (Tex. Civ. App.—Houston 1959, writ ref'd n.r.e.); Scott v. Crawford, 41 S.W. 697, 699 (Tex. Civ. App. 1897, writ ref'd). The rationale is not that the appointment of a receiver destroys prior liens; rather, their enforcement should be through the court. Ellis v. Vernon Ice, Light & Water Co., 86 Tex. 109, 115-16, 23 S.W. 858, 862 (1893).

638. No title can be transferred at a trustee's sale which is conducted in violation of an injunction. Lindley v. Easley, 59 S.W.2d 927, 929 (Tex. Civ. App.—Eastland 1932, no writ). *See generally* 39 TEX. JUR. 2d *Mortgages and Trust Deeds* § 142 (1962); Blood, *Injunction Bonds: Equal Protection for the Indigent*, 11 S. TEX. L.J. 16, 22-24 (1969); Pittman, *Foreclosure Problems—A Review*, 30 TEX. B.J. 949, 988 (1967).

639. Pearce v. Stokes, 155 Tex. 564, 291 S.W.2d 309 (1956); Delley v. Unknown Stockholders, 509 S.W.2d 709 (Tex. Civ. App.—Tyler 1974, writ ref'd n.r.e.); American Sav. & Loan Ass'n v. Jones, 482 S.W.2d 62 (Tex. Civ. App.—Houston [14th Dist.] 1972, writ ref'd n.r.e.). *See generally* 39 TEX. JUR. 2d *Mortgages and Trust Deeds* § 140 (1962); Pittman, *Foreclosure Problems—A Review*, 30 TEX. B.J. 949, 988-95 (1967); Note, 11 SW. L.J. 247 (1957).

640. 508 S.W.2d 486 (Tex. Civ. App.—Fort Worth 1974, no writ).

641. *Id.* at 488; *accord*, Hiller v. Prosper Tex., Inc., 437 S.W.2d 412, 414, 415 (Tex. Civ. App.—Houston [1st Dist.] 1969, no writ).

642. Hutchison v. Bristol Court Properties, Ltd., 508 S.W.2d 486, 487 (Tex. Civ. App.—Fort Worth 1974, no writ).

In *Riverdrive Mall, Inc. v. Larwin Mortgage Investors*[643] the trial court had denied the mortagor's request for a temporary injunction restraining the trustee's sale. Since the notice of sale had been posted, and it was apparent that, unless enjoined, a foreclosure would occur, the mortgagor sought a temporary injunction from the court of civil appeals on the grounds that if the trustee had conducted the sale prior to the final adjudication of the appeal, a civil appeals court ruling reversing the trial court would have then been meaningless.[644] The court granted the injunction in order to preserve the subject matter of the appeal.[645]

The power conferred by a deed of trust is a power coupled with an interest, and therefore continues after the death of the mortgagor.[646] The mortgagee should be careful, however, not to request a trustee's sale when, due to the death of the mortgagor, the jurisdiction of the probate court has been invoked over the mortgaged property.

One of the most significant cases regarding foreclosure after the death of the mortgagor is *Pearce v. Stokes*[647] in which the administrator sought to cancel a trustee's sale 5 months after it had occurred and 2½ years after the death of the mortgagor. Recognizing the benefits of forcing mortgagees to collect their debts through procedures sanctioned by the Probate Code rather than through a trustee's sale interfering with the administration of the estate,[648] the supreme court held that a mortgagee may not successfully request a trustee's sale within 4 years after the death of the mortgagor unless the administration has been completed: any trustee's "sale made after the death of the mortgagor and within four years thereof will be cancelled if an administration is opened and . . . seeks cancellation . . . ."[649]

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643. 515 S.W.2d 2 (Tex. Civ. App.—San Antonio 1974, no writ).

644. *Id.* at 4.

645. *Id.* at 4. As a condition for granting the injunction, the court required the mortgagor to post a bond of $40,000. *Id.* at 4. The court granted the injunction under the authority of TEX. REV. CIV. STAT. ANN. art. 1823 (1964).

646. Weiner v. Zweib, 105 Tex. 262, 267, 141 S.W. 771, 773 (1912); Slay v. Gose, 233 S.W. 348, 350 (Tex. Civ. App.—Fort Worth 1921, no writ).

647. 155 Tex. 564, 291 S.W.2d 309 (1956).

648. *See id.* at 568, 291 S.W.2d at 312. The court cited TEX. PROB. CODE ANN. §§ 77, 80, 306 (1956).

649. Pearce v. Stokes, 155 Tex. 564, 569, 291 S.W.2d 309, 312 (1956); *accord*, Delley v. Unknown Stockholders, 509 S.W.2d 709, 718 (Tex. Civ. App.—Tyler 1974, writ ref'd n.r.e.); American Sav. & Loan Ass'n v. Jones, 482 S.W.2d 62, 63 (Tex. Civ. App.—Houston [1st Dist.] 1972, writ ref'd n.r.e.).

The application to open the administration of an estate must be filed within 4 years after the death of the mortgagor. TEX. PROB. CODE ANN. § 74 (Supp. 1974).

FEDERAL AND STATE TAX LIENS

Before a mortgagee requests the trustee to exercise his power of sale, he should check to see if any federal or state tax liens exist against the mortgagor's property.[650] The Federal Tax Lien Act of 1966[651] requires that notice of a trustee's sale be given to the federal government if a federal tax lien has been filed and recorded for more than 30 days before the trustee's sale.[652] If the requisite notice of the trustee's sale is not given, the sale will not extinguish the federal tax lien or any cloud which it may cause on title.[653] State tax liens include, in addition to a general tax lien,[654] numerous tax statutes which expressly provide for a superior lien on all property of a delinquent taxpayer.[655]

MATERIALMEN'S LIENS

A common lien which competes with deeds of trust is the materialmen's lien.[656] In Texas there are actually two materialmen's liens, one constitutional[657] and the other statutory.[658] The case of *First National Bank v. Whirlpool Corp.*[659] exemplifies the basic issues of validity for a statutory materialmen's lien, as well as the priority of this lien which

650. The Federal Tax Lien Act of 1966 amends and repeals several provisions of the Internal Revenue Code of 1954, *see* Pub. L. No. 89-719, 80 Stat. 1125. For the general state tax lien, *see* TEX. TAX-GEN. ANN. art. 1.07 (1969). Such liens must be filed and recorded. INT. REV. CODE OF 1954, § 6323(a), (f) (federal); TEX. TAX-GEN. ANN. arts. 1.07A, 1.07B (1969).

651. *See* Pub. L. No. 89-719; 80 Stat. 1125.

652. INT. REV. CODE OF 1954, § 7425(b).

653. *Id.*

654. TEX. TAX-GEN. ANN. art. 1.07 (1969).

655. *E.g.*, TEX. TAX-GEN. ANN. arts. 8.09 (Cigar and Tobacco Products tax); 12.13 (Franchise tax); 14.20 (Inheritance tax); 18.03 (Cement Production tax); 21.04(2) (Admissions tax 1969). When necessary, each particular chapter of the tax statutes should be checked to determine if there is a specific tax lien on the property. *See* Miller v. Calvert, 418 S.W.2d 869 (Tex. Civ. App.—Austin 1967, no writ). The court held that the specific lien provisions in chapters 2-23 were not repealed by the enactment of the general lien provision found in article 1.07. *Id.* at 872.

656. Essentially, the materialmen's lien was created to give construction companies and related industries a lien for securing payment of materials and services provided. *See* Hayek v. Western Steel Co., 478 S.W.2d 786, 795 (Tex. 1972); University Sav. & Loan Ass'n v. Security Lumber Co., 423 S.W.2d 287, 296 (Tex. 1967).

657. TEX. CONST. art. XVI, § 37. It is well settled that the lien created by the constitution is self-executing and exists independently of any statute. Hayek v. Western Steel Co., 478 S.W.2d 786, 790 (Tex. 1972); Strang v. Pray, 89 Tex. 525, 528, 35 S.W. 1054, 1056 (1896). *See generally* Youngblood, *Mechanics' and Materialmen's Liens in Texas*, 26 SW. L.J. 665, 687-89 (1972); Comment, *The Constitutional Mechanic's Lien in Texas*, 11 S. TEX. L.J. 101 (1969).

658. TEX. REV. CIV. STAT. ANN. art. 5452 (Supp. 1974).

659. 502 S.W.2d 185 (Tex. Civ. App.—Waco 1973), *aff'd in part, rev'd in part*, 517 S.W.2d 262 (Tex. 1974).

may arise by operations of law. Whirlpool Corporation had furnished refrigerators, electric ranges, dishwashers and disposals to the defendant, Beckwood, Inc. When it became apparent that Beckwood was not going to pay the remaining balance on the appliances furnished, Whirlpool perfected its statutory materialman's lien. Beckwood had also executed a deed of trust to its co-defendant, First National Bank, to secure payment of a note for $1,850,000. The record clearly indicated that the deed of trust was filed and recorded prior to the filing of the materialman's lien. Whirlpool brought suit in order to foreclose on its materialman's lien.[660]

The threshold issue was whether the furnished appliances were covered by the statutory materialman's lien. The statutory materialmen's lien is available where the materials provided have been incorporated into a structure with the intention that they will not be removed[661] and therefore become a part of the realty. If the materials retain the characteristics of chattels after installment, security for payment of the indebtedness is derived from Chapter 9 of the Texas Business and Commerce Code.[662]

Assuming the materials provided come within the nature of property covered by the materialmen's lien statute,[663] the claimant also has to perfect his lien by fulfilling certain notice requirements.[664] An affidavit claiming the lien should be filed in the county clerk's office within 120 days after the indebtedness accrues. Also, two copies of the affidavit need to be mailed to the owner.[665] "Accrual of indebtedness" is defined as occurring on the 10th day of the month following the original contractor's completion or abandonment of his work.[666]

The supreme court found that plug-in refrigerators and ranges retained the characteristics of chattels after installation and, therefore, were not within the purview of the materialmen's lien statute.[667] "Merely plugging in an electrical cord is simply not the 'incorporation' or 'consumption' envisioned in the [Hardeman] Act. Such items have not lost their identity as chattels."[668]

660. *Id.* at 187-91.
661. First Nat'l Bank v. Whirlpool Corp., 517 S.W.2d 262, 266 (Tex. 1974); *see* McConnel v. Frost, 45 S.W.2d 777, 780 (Tex. Civ. App.—Waco 1931, writ ref'd).
662. TEX. BUS. & COMM. CODE ANN. §§ 9.101-9.507 (1968).
663. TEX. REV. CIV. STAT. ANN. art. 5452 (Supp. 1974).
664. TEX. REV. CIV. STAT. ANN. art. 5453 (Supp. 1974).
665. *Id.* § 1.
666. TEX. REV. CIV. STAT. ANN. art. 5467, § 19 (Supp. 1974).
667. First Nat'l Bank v. Whirlpool Corp., 517 S.W.2d 262, 266 (Tex. 1974).
668. *Id.* at 266. The holding of the court was in agreement with the majority of

Priority of Materialmen's Liens

When a materialmen's lien is prior in time to other liens, it has the superior status.[669] There has been considerable litigation, however, regarding the priority of a materialmen's lien when not prior in time to the attachment of other liens.[670] The situations involving materialmen's liens and other prior liens may be divided into two categories: those involving removable improvements and those involving non-removable improvements.

When the materials furnished by the lienholder may be removed without "material injury" to the land or other improvements, the materialmen's lien has priority.[671] This prevents the enhancement of real estate mortgagees' security at the expense of those who have later furnished labor and materials for improvements.[672]

In *Whirlpool* the materialman's lien was given preference over a deed of trust lien which was clearly filed and recorded prior to the

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other jurisdictions which have made the same distinction between appliances which are merely plugged-in and those which are so annexed to a structure as to be subject to a materialman's lien. *See* Elliott v. Tallmadge, 297 P.2d 310 (Ore. 1956). *See generally* Annot., 57 A.L.R.2d 1103 (1958).

The court also decided that Whirlpool did not have a constitutional lien on the refrigerators and ranges. Relying on the precedent of Reeves v. York Eng'r & Supply Co., 249 F. 513 (5th Cir. 1918), *cert. denied*, 248 U.S. 584 (1919), and Huttig Sash & Door Co. v. Stitt, 218 F. 1 (5th Cir. 1914), the court held that the constitutional lien on manufactured chattels is "available to [a] manufacturer only upon articles made especially for a purchaser pursuant to a special order and in accordance with the purchaser's plans." First Nat'l Bank v. Whirlpool Corp., 517 S.W.2d 262, 268 (Tex. 1974).

669. *See* University Sav. & Loan Ass'n v. Security Lumber Co., 423 S.W.2d 287, 293 (Tex. 1967); Hammann v. H.J. McMullen & Co., 122 Tex. 476, 482, 62 S.W.2d 59, 61 (1933); Mutual Bldg. & Loan Ass'n v. McGee, 43 S.W. 1030, 1031 (Tex. Civ. App. 1898, no writ).

670. *See generally* Helm, *Establishment and Priority of Liens for the Development and Improvement of Real Estate*, 20 BAYLOR L. REV. 387 (1968); Woodward, *The Hardeman Act—Some Unanswered Questions*, 6 ST. MARY'S L.J. 1 (1974); Youngblood, *Mechanics' and Materialmen's Liens in Texas*, 26 SW. L.J. 665, 689-98 (1972); Comment, *Procedures for Claiming and Priority of Mechanics' and Materialmen's Liens in Texas*, 21 BAYLOR L. REV. 21 (1969); Comment, *Priority of Mechanics' and Materialmen's Liens in Texas*, 40 TEXAS L. REV. 872 (1962).

671. TEX. REV. CIV. STAT. ANN. art. 5459 § 1 (Supp. 1974). Improvements have been held severable and subject to the preference in: Freed v. Bozman, 304 S.W.2d 235, 240-41 (Tex. Civ. App.—Texarkana 1957, writ ref'd n.r.e.) (a ticket booth, a speaker stand, and a screen at a drive-in theatre); Wallace Gin Co. v. Burton-Lingo Co., 104 S.W.2d 891, 892 (Tex. Civ. App.—Austin 1937, no writ) (a frame building); Mogul Prod. & Ref. Co. v. Southern Engine & Pump Co., 244 S.W. 212, 213 (Tex. Civ. App.—Beaumont 1922, no writ) (pumps from an oil refinery); R.B. Spencer & Co. v. Brown, 198 S.W. 1179, 1180 (Tex. Civ. App.—El Paso 1917, writ ref'd) (a rock house).

672. Woodward, *The Hardeman Act—Some Unanswered Questions*, 6 ST. MARY'S L.J. 1, 26 (1974).

filing of the materialman's lien.[673] This holding resulted directly from the finding that the disposals and dishwashers could have been removed without material injury to the building in which they were embodied.[674]

In situations where the materials cannot be removed without causing material injury to the land or other improvements, resulting litigation often involves competing claims for the funds received from a single foreclosure on the entire property.[675] Since the claim of the lienholder in such a case is inferior to any other lien prior in time,[676] the time of inception of the materialmen's lien is critically important.[677]

In *Irving Lumber Co. v. Alltex Mortgage Co.*,[678] the improvement consisted of the "shell" stage in building a house. It was obvious that the shell could not have been removed and sold separately without damaging the realty or other improvements. Irving Lumber Company had orally contracted with Merit Homes to build the shells while Merit was still negotiating to purchase the lots. Alltex Mortgage Company acquired a deed of trust lien from Merit for both the purchase money and the construction loans as well as subrogation rights to the vendor's lien. Irving Lumber's oral agreement became effective prior to the execution of the deed of trust by Merit, but Irving did not begin construction until afterwards. After Merit defaulted on the payment of its note to Alltex, the deed of trust was foreclosed. The land was purchased by Alltex at the trustee's sale for $27,000 and subsequently sold to other purchasers.[679]

The supreme court ruled in favor of Irving, employing the doctrine that the inception of a materialmen's lien relates back to the formation

673. First Nat'l Bank v. Whirlpool Corp., 517 S.W.2d 262, 269 (Tex. 1974).

674. *Id.* at 269.

675. *See* Yeager Elec. & Plumbing Co. v. Gaines Bldg., Inc., 492 S.W.2d 921, 922 (Tex. Civ. App.—Corpus Christi 1973, no writ).

676. Improvements have been held non-severable in: Cameron County Lumber Co. v. Al & Lloyd Parker, Inc., 122 Tex. 487, 490, 62 S.W.2d 63, 64 (1933) (a house): Irving Lumber Co. v. Alltex Mortgage Co., 446 S.W.2d 64, 69 (Tex. Civ. App.—Dallas 1969), *aff'd*, 468 S.W.2d 341 (Tex. 1971) (a shell home); McCallen v. Mogul Prod. & Ref. Co., 257 S.W. 918, 923 (Tex. Civ. App.—Galveston 1923, writ dism'd) (window frames).

677. For the determination of "inception" see TEX. REV. CIV. STAT. ANN. art. 5459, § 2 (Supp. 1974). Before a lien may be claimed, it must be perfected through the procedure specified in TEX. REV. CIV. STAT. ANN. art. 5453 (Supp. 1974). Home Sav. Ass'n v. Southern Union Gas Co., 486 S.W.2d 386, 392 (Tex. Civ. App.—El Paso 1972, writ ref'd n.r.e.).

678. 14 Tex. Sup. Ct. J. 212 (Feb 6, 1971) (opinion subsequently withdrawn).

679. *Id.* at 212-13.

of the contract between the original contractor and the landowner.[680] The court decided in favor of Irving, viewing the inception of its materialman's lien as having occurred upon the formation of the oral contract with Merit. Since this happened prior to the execution of the deed of trust with Alltex, the materialman's lien was declared superior.[681]

Prior to *Irving Lumber* materialmen's liens could incept only in one of three methods: recording of contracts;[682] the combination of an unrecorded contract and visible material on the premises;[683] or the mere delivery of materials.[684] The novelty of the *Irving Lumber* case was that a lien would have its inception upon the mere formation of an oral contract.[685]

Mortgagees viewed this decision as most unreasonable, feeling that it would make it impossible for lenders to assure themselves of first lien position prior to any oral contract which mortgagor-developers could make with companies in the construction industry.[686] As a result of this decision the legislature amended article 5459 to provide that the "inception" of materialmen's liens shall occur upon the happening of the earliest of three events: (1) the construction of improvements or delivery of materials which are actually visible from the inspection of the land; (2) the filing of any written contracts; or (3) the recording by affidavit of any oral contracts.[687]

From the viewpoint of mortgagees and title examiners the statute is an improvement over the previous case law. There is now a definite procedure for discovering a materialmen's lien on a potential borrower's land. Also, the holders of materialmen's liens have the further advantage of the codification of the relation back theory.[688]

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680. Oriental Hotel Co. v. Griffiths, 88 Tex. 575, 583-84, 33 S.W. 652, 662 (1895).

681. Irving Lumber Co. v. Alltex Mortgage Co., 14 Tex. Sup. Ct. J. 212, 213 (Feb. 6, 1971).

682. Recording is authorized by TEX. REV. CIV. STAT. ANN. art. 5453 (Supp. 1974) as well as TEX. REV. CIV. STAT. ANN. art. 6626 (1969).

683. Oriental Hotel Co. v. Griffiths, 88 Tex. 574, 581-82, 33 S.W. 652, 661 (1895).

684. University Sav. & Loan Ass'n v. Security Lumber Co., 423 S.W.2d 287, 296 (Tex. 1967).

685. Irving Lumber Co. v. Alltex Mortgage Co., 14 Tex. Sup. Ct. J. 212, 213 (Feb. 6, 1971).

686. *See* Youngblood, *Mechanics' and Materialmen's Liens in Texas,* 26 SW. L.J. 665, 693 (1972).

687. TEX. REV. CIV. STAT. ANN. art. 5459, § 2 (Supp. 1974), *amending* Tex. Laws 1971, ch. 231, § 2, at 1082-83.

688. *See* Youngblood, *Mechanics' and Materialmen's Liens in Texas,* 26 SW. L.J. 665, 693-94 (1972); Note, 9 HOUS. L. REV. 174, 177 (1971); Note, 50 TEXAS L. REV. 398, 401 (1971).

The Second Irving Lumber Case

Prior to the amendment of article 5459, the supreme court granted a rehearing in *Irving Lumber Co. v. Alltex Morgage Co.*[689] and altered its prior decision. There were essentially two holdings in the court's opinion requiring reevaluation in light of the new statute. First, the court believed that the "priority of a secured interest [could] not be determined on the date of the 'inception' of an agreement between [a] contractor and a *prospective owner* [of land].[690] Therefore, by virtue of the fact that Merit did not own the land when it orally contracted with Irving for lumber, the court believed that the relation back theory would not apply in determining the inception of Irving's lien.

Although the court cited cases in which liens had been "subsequently perfected" even though at the time the contract was formulated the purchaser had not owned the land, these cases were distinguished as not applicable in determining the "inception" of an agreement for priority purposes.[691]

It would seem more equitable in this type of situation for the acquisition of title by the landowner to relate back and exist at the time of the contract for the purchase of materials from the lien claimant.[692] This is especially reasonable in light of the fact that "Alltex had seen the plans . . . for [the work to be done by Irving] prior to the making of its loan; otherwise, it would not have known whether a loan . . . was justified."[693]

Additionally, in light of the amendment to article 5459 the prohibition against inception of a materialmen's lien with a prospective landowner seems unnecessary. That provision was enacted to eliminate the possibility of secret oral contracts being used to determine the inception of a materialmen's lien[694] and does not require a contract with

689. 468 S.W.2d 341 (Tex. 1971).

690. *Id.* at 34 (court's emphasis).

691. *Id.* at 343, *citing* Enlow v. Brown, 357 S.W.2d 608 (Tex. Civ. App.—Dallas 1962, no writ); Breckenridge City Club v. Hardin, 253 S.W.2d 873 (Tex. Civ. App.—Fort Worth 1923, no writ). *See also* Sprowls v. Youngblood, 23 S.W.2d 879, 882 (Tex. Civ. App.—Fort Worth 1930), *rev'd on other grounds sub nom.*, Harveson v. Youngblood, 38 S.W.2d 781 (Tex. Comm'n App. 1931, holding approved); Schultze v. Alamo Ice & Brewing Co., 21 S.W. 160, 162 (Tex. Civ. App. 1893, no writ). *See generally* Annot., 52 A.L.R. 693 (1928).

692. *See* Breckenridge City Club v. Hardin, 253 S.W. 873, 875 (Tex. Civ. App.—Fort Worth 1923, no writ).

693. Irving Lumber Co. v. Alltex Mortgage Co., 468 S.W.2d 341, 344 (Tex. 1971) (McGee, J., dissenting).

694. *See* Tex. Laws 1971, ch. 231, § 2, at 1082-83, *as amended*, TEX. REV. CIV. STAT. ANN. art. 5459, § 2 (Supp. 1974).

an "owner." Since mortgageee lenders are thus protected, the only effect of preventing "inception" with prospective landowners is to create an unnecessary obstacle to holders of materialmen's liens.

The court in *Irving* also refused to assign a priority to the deed of trust lien given for the construction loan different from that given the vendor's lien for the purchase money on the basis that both came into being "by the same instrument and transaction at the moment when the debtor-purchaser first acquire[d] his title to the land."[695] This effectively elevated the deed of trust lien to the same level of priority given to the vendor's lien.[696]

A vendor's lien is generally recognized as being superior to a materialmen's lien since the vendor's lien is viewed as being "on the land" at the time a materialmen's lienholder makes his contract.[697] For example, the lien of a materialman who contracts with a prospective owner of land is not superior to a vendor's lien which arises when title is transferred.[698] The novelty of the *Irving* case was that it allowed a deed of trust executed to secure a loan for construction expenses and to purchase land to have the same "on the land" status as a vendor's lien.[699] This effectively cut off the holder of the materialmen's lien from receiving any part of the proceeds from the foreclosure which was conducted. In light of the amendment to article 5459, a materialmen's lienholder should be recognized as second in priority in situations similar to that in *Irving*. Otherwise, the inception of a materialmen's lien under the new statute may be effectively altered when a lender loans money for purchasing land and construction expenses and takes a single deed of trust to secure the aggregate debt.

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695. Irving Lumber Co. v. Alltex Mortgage Co., 468 S.W.2d 341, 342 (Tex. 1971).

696. *See* Note, 9 HOUS. L. REV. 174, 180 (1971). For an explanation of the remedies available for a debt secured by a vendor's lien see Norvell, *The Vendor's Lien and Reservation of the Paramount Legal Title—The Rights of Vendors, Vendees, and Subvendees*, 44 TEXAS L. REV. 22 (1965).

697. *See* Youngblood, *Mechanics' and Materialmen's Liens in Texas*, 26 SW. L.J. 665, 697 (1972).

698. Harveson v. Youngblood, 38 S.W.2d 781, 783 (Tex. Comm'n App. 1931, holding approved).

699. *See* Irving Lumber Co. v. Alltex Mortgage Co., 468 S.W.2d 341, 342 (Tex. 1971).