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Real Property

Jesse B. Heath Jr.

Barton R. Bentley

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# REAL PROPERTY

_by_  
_Jesse B. Heath, Jr.* and Barton R. Bentley**_

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This article discusses more than 100 of the real property cases reported during the survey period. Although many of these cases provide little more than a review of basic real property law, significant and exciting new developments did occur in such areas as title insurance, slander of title, contracts, brokerage, mortgages, usury, and mechanics' and materialmen's liens. The basic format established in the Survey articles for the previous three years has been followed. Topics such as homestead and community property, oil and gas, and ad valorem taxation, which constitute major portions of other articles in this Survey issue, are omitted from this article. Further, due to the wealth of significant discussion topics, and in keeping with the previously established format, no discussion of cases concerning condemnation or eminent domain is included.

1. The Board of Editors of the Journal has designated cases reported in South Western Reporter and Federal Second advance sheets received by Oct. 12, 1976, as the end of the survey period. A few noteworthy cases reported subsequent to that date are, however, discussed in this Article.


3. See, e.g., homestead and community property, McKnight, Family Law—Husband and Wife; mineral rights, Roach, Oil and Gas; ad valorem taxes, Burke, Taxation.
I. TITLE PROBLEMS

A. Ownership and Boundary Disputes

1. Title by Limitations.4

As in previous years, proof of title by adverse possession received substantial attention in litigation during the survey period.5 In Calfee v. Duke6 the plaintiffs and defendant Calfee were descendants of J. H. Duke, who had recovered title by limitations to the tract in question in 1935. Calfee acquired a deed and went into possession of the property in July 1946; however, part of the claimed tract was not covered by the description in the deed. The other Duke heirs brought this action, claiming that as to the tract not described in the 1946 deed to Calfee, limitations could not run against them since Calfee became a cotenant with the other Duke heirs upon the death of Calfee’s father.7 The trial court held for Calfee, but the court of civil appeals reversed and held that Calfee and the other Duke heirs were co-tenants, and therefore that limitations could not run against the other Duke heirs.8 The Texas Supreme Court reversed the court of civil appeals, holding that Calfee’s claim of right, coupled with actual and visible possession and use, satisfied the ten year statute9 and could not be defeated merely because of a defect in his record title or because he was unaware of other claimants to the land. The court did not reach the issue of the existence of a co-tenancy. Rather, the court held that Calfee had acquired title to the tract by limitations prior to the death of his father, and, therefore, before any co-tenancy could have arisen.

In Chapman v. Moser10 the Fifth Circuit held that the plaintiffs and their grandparents had peaceably and adversely possessed the disputed lands continuously for at least 25 years under a “claim of right,” and, thereby, had established title by limitations under article 5519.11 The court defined “claim of right” as used in article 5519 as “a bold and open, a downright and persistent claim asserted not furtively by stealth and artifice, but openly, notoriously, unequivocally, adversely and continuously.”12 The Fifth Circuit also held that the district court properly apportioned between the two adjoining land owners one tract of accreted land.13

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5. In addition to the cases discussed in the text see McMahon v. Texas Bank & Trust Co., 535 S.W.2d 384 (Tex. Civ. App.—Eastland 1976, no writ).


7. Generally, possession by a tenant in common will be presumed to be in right of the common title. It must clearly appear that the co-tenant has repudiated the title of the others and holds adversely to them. The acts necessary to establish an adverse claim must be more certain and unequivocal than in ordinary cases. Moreover, notice of the adverse claim must be brought home to the other co-tenants. See Poenisch v. Quarnstrom, 361 S.W.2d 367 (Tex. 1962); Phillipson v. Flynn, 83 Tex. 580, 19 S.W. 136 (1892).


10. 532 F.2d 426 (5th Cir. 1976).


A purchaser who takes possession under a contract of sale, as in Fant v. Howell, holds equitable title to the property. He therefore has the right to support or defend an action in trespass to try title involving third persons who were not parties to the contract of sale. Any loss occurring by reason of adverse possession or outstanding title by limitations must thus be borne by the purchaser as holder of equitable title.

2. Boundary Line Agreements; Boundary by Acquiescence.

When there is uncertainty as to the true dividing line between two adjoining tracts, the boundary line may be established by an oral agreement between the respective owners. The court in Doria v. Suchowolski held that without evidence of a dispute concerning the true boundary, there can be no valid boundary line agreement. The plaintiff argued alternatively that the boundary in question had been established by acquiescence. Boundary by acquiescence, according to the court, is also dependent upon the existence of doubt or uncertainty. Thus, the mere erection of a fence which was located off the true boundary line was not in itself sufficient to establish a boundary by acquiescence.

Another case involving a disputed boundary was United States v. Denby, where the Government claimed that a certain parcel of land was located within the boundaries of the Sabine National Forest. Under Texas law the true location of a disputed boundary line may be proved by retracing, as nearly as possible, the footsteps of the original surveyor. Here the Government offered the testimony of two registered surveyors who retraced the original surveyor's steps. The court found this evidence conclusive in establishing the boundary line alleged by the Government.


The land surface in the Texas Gulf Coast Area has been slowly subsiding during the last several decades, primarily caused by the removal of under-
ground water for industrial and municipal purposes.\(^{23}\) The question of ownership of riparian land which has subsided beneath the water level was before the Texas Supreme Court in *Coastal Industrial Water Authority v. York*.\(^{24}\) The land in question had become submerged below the water level of the Houston Ship Channel, the bed of which is owned by the City of Houston. The water level on the York land, however, did not fluctuate with the ebb and flow of the tides.\(^{25}\) The court held that mere submersion of land does not necessarily destroy the title of the landowner.\(^{26}\) Since there had been no erosion of the soil, title to the submerged land remained in York.\(^{27}\)

A well established rule of law declares that an owner of land owns "all ordinary springs and waters arising thereon."\(^{28}\) This rule stems from the general proposition that the surface owner also owns water beneath the surface. These principals, however, are not applicable to water flowing in subterranean streams or to the overflow of rivers.\(^{29}\) In *Bartley v. Sone*\(^{30}\) the court held that in the absence of evidence to the contrary it is to be presumed that a landowner owns all water flowing from springs upon his land.

### B. Easements

1. **Easements by Operation of Law.**

   As an interest in land, an easement is subject to the Statute of Frauds and the Statute of Conveyances; thus, an express easement must be conveyed in writing.\(^{31}\) Easements may however be created in several ways by operation of law without the necessity of a writing. An easement by prescription exists where the claimant shows that the use of the alleged servient estate was open, notorious, hostile, adverse, uninterrupted, and exclusive for a period of more than ten years.\(^{32}\) An implied easement may be shown if the dominant and servient estates were at some time under a common ownership, the use was apparent at the time of the grant to the dominant estate, the use of easement was continuous, and the easement is reasonably necessary to the use and enjoyment of the dominant estate.\(^{33}\) Additionally, in some circumstances an

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\(^{24}\) 532 S.W.2d 949 (Tex. 1976), noted in 30 Sw. L.J. 943 (1976); see Wallenstein & St. Claire (1976), supra note 2, at 31.

\(^{25}\) This fact was crucial to the court's holding. See 532 S.W.2d at 951-52 n.1.


\(^{27}\) The general rule is that a riparian owner acquires or loses title to land gradually added or taken from his shoreline. Giles v. Bashore, 154 Tex. 366, 378 S.W.2d 830 (1955). A different rule is applied in cases of sudden, rapid changes. See 5A G. THOMPSON, REAL PROPERTY § 2561 (Grimes ed. 1937). In York there was no "transportation of the land beyond the owner's boundary" so as to destroy the owner's title. 532 S.W.2d at 954. See 5A G. THOMPSON, supra, § 2562.


\(^{29}\) Texas Co. v. Burkett, 117 Tex. 16, 296 S.W. 273 (1927).

\(^{30}\) 527 S.W.2d 754 (Tex. Civ. App.—San Antonio 1974, writ ref'd n.r.e.).

\(^{31}\) Anderson v. Tall Timbers Corp., 378 S.W.2d 16 (Tex. 1964).


easement may be created by estoppel where in a conveyance of land there is a representation communicated by the vendor to the vendee which the vendee believes and relies upon. Finally, an implied dedication to the public may be established by showing that the road in question was expressly or impliedly thrown open to the public, that the public accepted the dedication by general and customary use, and that the public will lose valuable rights if the road is closed. Two cases decided during this survey period provide a virtual guidebook to these theories.

In *Davis v. Carriker*, although the court held that the plaintiff failed to establish an easement under theories of prescription, express easement, implied easement or way of necessity, or implied public dedication, its analysis in arriving at its holding embodies a review of each theory and its characteristics. The theory of easement by implication was discussed in *Exxon Corp. v. Schutzmaier*, where the court concluded that strict adherence to the four requirements discussed above is essential to the creation of an implied easement. In *Schutzmaier* the lack of a common grantor prevented the application of this doctrine. The court also considered the creation of an easement by estoppel. Recognizing that the "exact nature and extent of the doctrine of estoppel in pais have not been clearly defined," the court held that where the desired easement was the only means of ingress and egress to the plaintiffs' tract, the plaintiffs' predecessor in title had received permission to use the road from the defendant and this access had been used for 22 years, and the plaintiffs had made improvements and had expended money on their property without objection by the defendant, an easement by estoppel was created. Finally, the court held that a party who obtains an easement by operation of law is not entitled to use all means of access to the property. Use must be limited to those means which are reasonably necessary and which cause the least burden to the servient estate.

2. **Construction of Express Easements.**

The construction of language in express easements gave rise to some...
interesting decisions during the survey period. In *Mapco, Inc. v. Ratliff* an express pipeline easement required the pipeline owner to maintain the pipe at a sufficient depth to permit cultivation. The court held that where the pipe was not at such a depth, the pipeline owner could not recover on the basis of trespass for damage to the pipeline caused by a plowing contractor.

In *Lower Colorado River Authority v. Ashby* the easement provided for a right-of-way along a strip of land 100 feet wide for an "electric transmission and/or distribution line, consisting of variable number of wires, and all necessary or desirable appurtenances (including towers, H-Frames or poles made of wood, metal or other materials, telephone and telegraph wire, props and guys)." The court held that this language was sufficiently broad to give the River Authority the right to substitute steel towers for wooden H-Frames and to add additional wires.

The question of damages recoverable within the language of certain easement deeds was considered in *Melder v. Phillips Pipe Line Co.* The express pipeline easements in question provided that the grantee was obligated "to pay any damages which may arise to crops, timber, fences or buildings" because of the use of the easement by the grantee. Citing the rule that words in a contract are to be given their ordinary and accepted meanings, the court held that natural grasses, ground cover and shrubs were not "crops," trees which afforded shade and ornamentation were not "timber," and that a rock wall was not a "fence" within the meaning of those terms as used in the easement deeds.

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43. 528 S.W.2d 622 (Tex. Civ. App.—El Paso 1975, writ ref'd n.r.e.).
44. 530 S.W.2d 628 (Tex. Civ. App.—Austin 1975, writ ref’d n.r.e.).
45. *Id.* at 632.
46. The result in this case must be contrasted with those cases involving easements which merely permit the construction of some facility or laying of a line. In such cases, after the facility or line has been located, what was general and indefinite becomes fixed and certain and thereafter cannot be changed by the grantee. See, e.g., *Houston Pipeline Co. v. Dwyer*, 374 S.W.2d 662, 666 (Tex. 1964). The opinion of the court in *Ashby* clearly indicates a finding that the easement originally granted was sufficient in scope to encompass the new metal towers and the additional wires. Unfortunately, however, the court states that a servitude originally granted may be somehow enlarged, citing *Knox v. Pioneer Natural Gas Co.*, 321 S.W.2d 596 (Tex. Civ. App.—El Paso 1959, writ ref'd n.r.e.). The *Knox* case holds only that where an easement grants rights in excess of those actually used, such greater rights exist notwithstanding the exercise of a lesser privilege. *Ashby* should not be regarded as authority for the rather novel proposition that an easement may be enlarged merely to satisfy the grantee. Additionally, another case involving the Lower Colorado River Authority makes it clear that no interest in property or other rights pass by implication as incidental to the grant of an express easement, except that the grantee of an easement will be permitted to do what is reasonably necessary for the fair enjoyment of the easement itself. *Wall v. Lower Colorado River Authority*, 536 S.W.2d 688 (Tex. Civ. App.—Austin, 1976, writ ref’d n.r.e.). Compare the corresponding rule with respect to implied easements stated in the text accompanying note 40 supra. See also *Gheen v. Diamond Shamrock Corp.*, 529 S.W.2d 289 (Tex. Civ. App.—Waco 1975, no writ), where the court upheld an express easement providing for ingress and egress. The court also held that a payment to extend an easement which was mailed one day too late was nevertheless sufficient to keep the easement in force and effect.
47. 539 S.W.2d 208 (Tex. Civ. App.—Austin 1976, writ ref'd n.r.e.).
48. *Id.* at 210.
49. *Id.* The court cited *Fox v. Thoreson*, 398 S.W.2d 88 (Tex. 1966), and *Lilac Variety, Inc. v. Dallas Texas Co.*, 383 S.W.2d 193 (Tex. Civ. App.—Dallas 1964, writ ref’d n.r.e.).
50. 539 S.W.2d at 210-11.
C. **Effect of Conveyances**

1. **Construction of Deeds.**

   A conditional limitation exists when the duration of an estate is limited by the happening of an event which, when it occurs, terminates the estate without the necessity of reentry by the grantor.\(^{51}\) On the other hand, a condition subsequent gives the grantor the right to terminate the estate by reentry.\(^{52}\) In *Field v. Shaw*,\(^{53}\) the court held that the following language in a deed created a condition subsequent and not a conditional limitation:

   
   "the land . . . is expressly restricted in use to that of the operation of a Cotton Gin and that no other business shall ever be operated thereon and in the event this restriction is violated, the land herein conveyed shall revert to the grantor herein."\(^{54}\)

   The court noted that the usual language for creating a limitation are the terms "so long as," "until" and "during." Terms such as "if," "but if," "on condition that," and "provided however" constitute the classic language for the creation of a condition subsequent.\(^{55}\) Moreover, language in a deed is generally construed against the grantor,\(^{56}\) and in cases of doubt, a construction giving rise to a condition subsequent will be favored as less burdensome upon the grantee than a conditional limitation.\(^{57}\) Since affirmative assertion of reentry was found to be necessary for a condition subsequent to exist, the court examined the actions of the grantor and found that the right of reentry was now barred by the three year statute of limitations involving suits to recover title and possession of real property.\(^{58}\)

2. **Execution and Delivery of Deeds.**

   It is a rather common practice in this state for a certificate of a corporate resolution to be presented to the title company in order to verify the corporate agent’s authority to execute closing papers on behalf of a corporation. One case decided during the survey period hints at some of the potential ramifications which could flow from an abuse of this practice. In *Nobles v. Marcus*\(^{59}\)

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\(^{51}\) The estate is known as a fee simple determinable. That is, a fee simple created to continue until the happening of a stated event. The grantor retains an interest known as a possibility of reverter. See generally W. Burby, *supra* note 34, § 91.

\(^{52}\) The grantee’s interest is referred to as a fee simple subject to a condition subsequent. The grantor has a right of reentry which must be exercised within a reasonable time. Zambrano v. Olivas, 490 S.W.2d 218 (Tex. Civ. App.—El Paso 1973, writ ref’d n.r.e.). Limitations may bar an action to enforce a right of reentry. City of Dallas v. Etheridge, 152 Tex. 9, 253 S.W.2d 640 (1952).

\(^{53}\) 533 S.W.2d 3 (Tex. Civ. App.—Amarillo 1976, no writ).

\(^{54}\) *Id.* at 4.

\(^{55}\) *Id.* at 5-6; see Lawyers Trust Co. v. City of Houston, 359 S.W.2d 887 (Tex. 1962).


\(^{57}\) Lawyers Trust Co. v. City of Houston, 359 S.W.2d 887 (Tex. 1962).

\(^{58}\) *Tex. Rev. Civ. Stat. Ann.* art. 5507 (Vernon 1958). For other cases involving the construction of language in deeds see Boyd v. Welch, 539 S.W.2d 93 (Tex. Civ. App.—Eastland 1976, writ ref’d n.r.e.) (when deed is ambiguous, extrinsic evidence is admissible to show intent); Wylie v. Reed, 538 S.W.2d 186 (Tex. Civ. App.—Waco 1976, writ granted) (mineral reservation does not reserve coal and lignite which must be removed by open pit or strip-mining); DuBois v. Jacobs, 533 S.W.2d 149 (Tex. Civ. App.—Austin 1976, no writ) (mineral reservation not ambiguous); Pearson-Sibert Oil Co. v. Burney, 331 S.W.2d 422 (Tex. Civ. App.—Eastland 1976, no writ) (when deed required grantors to maintain cattle guards at most commonly used entrances to property, grantee could not recover costs of rounding up stock which came through open gate not commonly used as an entrance).

\(^{59}\) 533 S.W.2d 923 (Tex. 1976).
the plaintiffs, judgment creditors of the corporation, brought suit to set aside a deed from the corporation to a third party which had been executed and delivered prior to the date of the plaintiffs' judgment. The plaintiffs argued that the deed was void as a matter of law because the individual executing the deed as vice-president on behalf of the corporation had not been elected to that position by the board of directors. Further, the corporate resolution delivered at the closing was executed by an employee of the corporation who was not an assistant secretary of the corporation as recited in the certificate. The court held that the signing of the deed did not amount to a forgery, but rather constituted at most a fraud upon the corporation, of which the plaintiffs had no standing to complain. Another case concerning the execution of a deed by a corporate agent is Sheldon v. Farinacci.

In Neel v. Fuller suit was brought to cancel a mineral deed given by the trustee of the owners while the property was in a receivership. The court of civil appeals held that the sale by the property owner during a receivership did not interfere with the receivership, but was subject to it. The Texas Supreme Court reversed, however, holding that the deed was void because the interest conveyed was in custodia legis.

There were several cases during the survey period involving the question of what constitutes delivery of a deed. For example, in Hart v. Rogers the court held that in order to accomplish delivery it is not necessary that the deed be manually transmitted to the grantee, nor even placed out of the grantor's physical possession. The key factor is that the grantor relinquishes dominion and control over the deed. Further, the court held that evidence of general reputation of ownership may not be used as proof of ownership. On the issue of the grantor's intent to deliver a deed, the court in Bennett v. Mings sustained the jury's finding that the ninety-one-year-old grantor did not intend the deed to her nephew to become operative as the conveyance of her property.

60. The court also distinguished an action for fraudulent conveyance from an action for fraud. The plaintiffs did not plead a fraudulent conveyance, and since they had no standing to complain of any fraud committed against the corporation, relief was denied. Id. at 926-27.

61. 535 S.W.2d 938 (Tex. Civ. App.—San Antonio 1976, no writ). In this case the deed had been executed by an individual on behalf of a corporation, and the acknowledgment was complete and correct except that the name of the individual was left blank. The court construed the acknowledgment in light of the instrument itself and held that the acknowledgment was not defective. See Williams v. Cruse, 130 S.W.2d 908 (Tex. Civ. App.—Beaumont 1939, writ ref'd).


63. In addition to the cases discussed in the text see Bell v. Smith, 532 S.W.2d 680 (Tex. Civ. App.—Fort Worth 1976, no writ), in which the court held that when the evidence shows that the grantee has possession of a duly executed deed, a presumption arises that the deed was delivered and, in the absence of evidence to the contrary, a deed is presumed to have been delivered at the time of its execution and not on the date of the acknowledgment. For other issues in this case see 69-76 infra and accompanying text. See also Jones v. Young, 539 S.W.2d 901 (Tex. Civ. App.—Texarkana 1976, writ ref'd n.r.e.); DeGrassi v. DeGrassi, 533 S.W.2d 81 (Tex. Civ. App.—Texarkana 1976, writ ref'd n.r.e.).

64. 527 S.W.2d 230 (Tex. Civ. App.—Eastland 1975, writ ref'd n.r.e.).

65. 535 S.W.2d 408 (Tex. Civ. App.—Texarkana 1976, writ ref'd n.r.e.).
In *Fuqua v. Fuqua* the heirs of the grantor brought suit to set aside a deed which had been executed by the grantor and placed in escrow six days before his death. Subsequently, the purchaser under the contract complied with the terms of the escrow and obtained delivery of the deed from the escrow agent. The court refused to set aside the deed, holding that the grantor’s death did not invalidate the deed, and upon performance of the conditions of the escrow agreement, the grantee became entitled to delivery of the deed. The grantee’s title, the court said, related back to the date of the original deposit of the instrument in escrow.

**D. Fraud; Duress; Undue Influence and Equitable Remedies**

*Bell v. Smith* presents an interesting illustration of the doctrine of resulting trusts as well as the rules associated with the rights of parties in possession. Lonnie Smith was the son of Gene Smith and the former Lucille Smith, now Lucille Bell, the plaintiff. After Gene and Lucille were divorced, Gene married Christine Smith, the defendant. When Christine and Gene purchased their home, Gene had the title placed in the name of Lonnie Smith, his son by the prior marriage. This home was purchased with community funds. In October 1973 Lonnie died intestate, with his father and mother (plaintiff Lucille Bell) as his only heirs. Shortly thereafter, Gene and Christine Smith were divorced. In the divorce proceeding Gene was ordered to execute a quitclaim deed in favor of Christine conveying his interest in the home.

Lucille Bell then filed suit, claiming a one-half interest in the property through intestate succession from her son, Lonnie. The court, however, rejected this claim, and held that Christine Smith was the owner of the entire fee simple, reasoning that under the doctrine of resulting trusts Lonnie merely held title to the property in trust for the benefit of the community.

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66. 528 S.W.2d 896 (Tex. Civ. App.—Houston [14th Dist.] 1975, writ ref’d n.r.e.).
68. In addition to the cases discussed in the text, there were several decisions concerning the topics covered in this section of the Article. Nobles v. Marcus, 533 S.W.2d 923 (Tex. 1976), distinguishes an action for fraudulent conveyance from an action for fraud. *See notes 59, 60 supra and accompanying text. With regard to undue influence, the court in Stieler v. Stieler, 537 S.W.2d 954 (Tex. Civ. App.—Austin 1976, writ ref’d n.r.e.), held that the mere opportunity to exercise undue influence will not support a jury finding of undue influence. In DeGrassi v. DeGrassi, 533 S.W.2d 81 (Tex. Civ. App.—Amarillo 1976, writ ref’d n.r.e.), a jury finding of no undue influence was upheld. The court found that the burden of proof had been properly placed on the wife of the grantor-husband where the wife also joined in the deed. Moreover, the court stated that a presumption of unfairness is not present in a husband-wife relationship where the wife has independent legal advice from an attorney. *See also Bradshaw v. Naumann, 528 S.W.2d 869 (Tex. Civ. App.—Austin 1975, no writ).*
70. *Id.* at 685.
71. A resulting trust may arise when a party purchases land but takes title in the name of another. A trust results in favor of the party whose money was used to make the purchase. When community funds are used, a trust results in favor of the community. First State Bank v. Thurman, 12 S.W.2d 146 (Tex. Comm’n App. 1929, jdgmt adopted). Resulting trusts may also arise in other circumstances. *See generally* G. Bogert, *Trusts* §§ 71-76 (1963); 89 C.J.S. *Trusts* §§ 98-138 (1955); 57 Tex. Jur. 2d *Trusts* §§ 40-53 (1964). *See also Comment, Parol Evidence to Prove Resulting Trusts, 7 St. Mary’s L.J. 165 (1975).
estate. Thus, prior to the divorce Christine and Gene Smith each owned an undivided one-half interest in the home, and Lucille Bell acquired no interest through intestate succession. The court held that Christine acquired the other one-half interest in the property by quitclaim deed from Gene in the divorce proceedings.

Another issue in the case concerned the fact that after Gene had executed the quitclaim deed to Christine, he then gave a warranty deed for the same property to Lucille Bell. The warranty deed was recorded prior to the recording of the quitclaim deed, but at a time when Christine Smith was occupying the property. Lucille contended that her deed, being recorded before the quitclaim deed, cut off all rights of Christine Smith. The court stated that it is not necessary that a deed be recorded in order to be effective as a conveyance of title, and reasoned that the notice of title given by possession is equivalent to the constructive notice afforded by the registration statutes. Therefore, since Lucille Bell’s deed was obtained while Christine Smith was in possession of the property, Lucille was charged with notice of all the rights and title of the possessor to such property.

In contrast to the above, all unrecorded conveyances are void as to creditors and subsequent purchasers for value without notice. In a somewhat confusing opinion the Amarillo court of civil appeals in North East Independent School District v. Aldridge held that a judgment creditor’s lien was superior to the interest of a holder of equitable title to a tract of land which was inadvertently omitted from a prior unrecorded deed.

E. Title Insurance

One of the most interesting cases decided during the survey period is Stone v. Lawyers Title Insurance Corp. The purchaser of a tract of land sued the title insurer, the title insurance agency, its president, and the real estate agent,
but not the grantor, to recover damages arising from certain gas pipeline easements which, although listed as exceptions in the title report prepared for the title insurance agency, were not listed as exceptions in the owner's policy of title insurance issued by Lawyers Title. Subsequent to the purchase of the tract, the purchaser secured a commitment from the Federal Housing Administration to insure a loan upon the completion of a 147 space mobile home park. Upon discovery of the pipelines, certain FHA regulations regarding the location of residential structures relative to pipelines forced a redesign of the park. The new plan contained only 129 spaces, which reduced the amount of financing available under the FHA commitment.

The court noted that title insurance is a contract of indemnity, and as such, the insured party is entitled to recover only a portion of the whole liability of the insurance company based on the ratio which the adverse claim bears to the whole estate. For example, if the amount of the policy equals the value of title insured, the loss recoverable is simply the value of the outstanding interest. Accordingly, the court held that under the provisions of the owner's policy of title insurance, testimony concerning reduction of the value of the original FHA commitment, loss of income from the redesigned mobile home park and the cost of the redesign work was properly excluded by the trial court as immaterial. Moreover, expert testimony concerning the diminished value of the tract based upon projected rental income, management fees and expenses was found to be too speculative. A $2,879.00 judgment against the title insurer, based on the value of the outstanding interest, was therefore affirmed.

The purchaser also claimed that the failure by the agency and its president to inform the purchaser of the contents of the title report was both negligent and fraudulent. The court held that a title insurance company is not a title abstractor and owes no duty with regard to the examination of title. Thus, any recovery for negligence was precluded by the nature of the parties' relationship. With regard to the claim of fraud, the court held that the purchaser's pleadings failed to state a cause of action. There were no allegations showing a duty to disclose the contents of the report or showing that the agency's president made false representations concerning the easements with the intent that the purchaser rely upon them to his detriment.

81. The tract was conveyed by general warranty deed with no exceptions or reservations with respect to the easements.
82. See Southern Title Guar. Co. v. Prendergast, 494 S.W.2d 154 (Tex. 1973). The court also denied a recovery of attorneys' fees stating that it was incumbent on the claimant to allege and prove the reasonable value of the legal services rendered in enforcing the terms of the title policy against the insurer. 537 S.W.2d at 63-64.
83. 537 S.W.2d at 65. In this connection the court noted that the purchaser, under the contract of sale, could have elected to order an abstract of title for examination by his own counsel, or he could have, as he did, elected to rely upon title insurance. While this statement is hardly surprising, the court added that "the title opinion which was written by the Agency's attorney to the Agency was personal to the Agency and was prepared for its exclusive use and benefit. It did not inure to the benefit of [the purchaser], a complete stranger to that transaction." Id. at 73. While not mentioned by the court, many, if not most, title reports contain a printed disclaimer to the effect that the report is intended for in-house use only, and any outside reliance shall be without liability on the part of the title company. This aspect of the case should be of interest to those lawyers who are accustomed to contracts of sale which require that the seller provide a title report to the purchaser for his review and approval prior to the closing.
84. Id. at 65.
Therefore, the court affirmed the judgment of the trial court that the purchaser take nothing from the title insurance agency or its president. Curiously, the court in *Stone* indicated by way of dicta that there was nothing in the record which would have legally excused the purchaser's refusal to close the transaction. This statement is presumably subject to provisions in a contract of sale which require the seller to furnish a title report prior to the closing and which specify the encumbrances, exceptions and reservations which will be acceptable to the purchaser.85

In *Clements v. Stewart Title Guaranty Co.*86 the plaintiff purchased two tracts of land which were separated from a public road by a third tract. The sellers of one of the tracts represented that an easement existed across the third tract, and the deed purported to convey such an easement. After the closing, the plaintiffs discovered that no such easement existed.

The owner's title insurance policy provided in part that it guaranteed a "good and indefeasible title to the estate or interest in the land described or referred to in this policy."87 The land was described therein as follows:

FIRST TRACT: 1.395 acres of land, more or less, out of the JOSEPH D. RICE Survey NO. 10, in Hays County, Texas, and being the same property conveyed by deed dated July 1, 1971 from J.A. Caballero and wife, Rose B. Caballero, to Manning C. Clements and wife, Winn M. Clements, said deed having been filed for record in the office of the County Clerk of Hays County, Texas, on July 23, 1971, under Clerk's file No. 72736.88

The policy further specified the exceptions from coverage and did not mention the purported easement which was described in the Caballero deed.

The trial court entered judgment for $2,000.00 against the sellers, but provided that the plaintiffs take nothing from the title insurance company. On appeal the title insurer argued that the easement was not described as part of the insured estate and that the insurer had no contractual liability with respect to title to the easement. The court of civil appeals reversed, holding that since the description in the title policy referred to the Caballero deed which purported to convey the easement, and since the policy contained no exception with respect to the easement, the title insurance policy therefore insured against any loss suffered because of the failure of the easement purportedly conveyed by the sellers. The court noted that as a contract of indemnity, an owner's policy of title insurance provided coverage against all losses of title, and, except for certain designated risks, included loss from any cause not expressly excepted.89

At the annual meeting of the State Board of Insurance in November 1976, several new procedural and rate rule changes concerning title insurance were adopted. Most of the changes were of a technical nature and are discussed in

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85. With respect to the real estate agent, the court remanded the case for a jury determination on the issues as to whether he recklessly represented to the purchaser that no pipeline easements existed and whether such representation, if made, was made with the intent that the purchaser rely thereon. *Id.* at 74-75.
86. 537 S.W.2d 126 (Tex. Civ. App.—Austin 1976, writ ref'd n.r.e.).
87. *Id.* at 127-28.
88. *Id.* at 128.
89. *Id.* See *San Jacinto Title Guar. Co. v. Lemmon*, 417 S.W.2d 429 (Tex. Civ. App.—Eastland 1967, writ ref'd n.r.e.).
the footnotes (for the full text of all changes, consult the Basic Manual of Rules, Rates and Forms for the Writing of Title Insurance in the State of Texas). Most notably, the Board announced an overall rate increase of ten percent for the 1976 Schedule of Base Premium Rates. The Board also considered, but did not adopt, a change which would have prohibited the deletion of the standard printed exception as to area and boundaries from all future policies of title insurance issued in the State of Texas.

F. Miscellaneous Title Cases

1. Covenants Running with the Land.

Several interesting questions were presented in Clear Lake Apartments, Inc. v. Clear Lake Utilities Co., a case which concerned covenants running with the land in the context of exclusive contract rights to furnish water and sewer services. A contract between the utility company (Utilities) and the predecessor in title of Clear Lake Apartments (Apartments) granted Utilities "the exclusive right to furnish water and sewer service" to a certain tract of land and the apartment project thereon. When Apartments purchased the project, however, it informed Utilities that the contract was being terminated. Utilities then brought suit for declaratory judgment, contending that its contract rights constituted a covenant running with the land and thereby bound Apartments to perform pursuant to the contract. The court rejected this contention, finding the necessary privity of estate to be lacking. Utilities also argued that the contract should be enforced in equity because it was on record at the time of the conveyance to Apartments. The purchaser, it was argued, therefore had at least constructive notice of the provisions of the contract. The court held that while a purchaser is on notice of all recorded instruments within his chain of title, he is only bound by those instruments

90. The Basic Manual contains all procedural and rate rules, as well as the official forms promulgated by the State Board of Insurance and the Texas Title Insurance Act, Tex. Ins. Code Ann. arts. 9.05-.36 (Vernon Supp. 1976-77). Highlights of the more pertinent changes include additional endorsement instructions for the "Down Date Endorsement" and a premium of $50 for each such endorsement issued as provided in Procedural Rule P-9d. Rate Rule R-8 was amended to extend the periods of renewed credits from six months to one year, to extend the total period of renewal credits from two years to four years and to allow an additional renewal credit to cover phase development programs. The "Direct Access Agreement" form was eliminated from the Basic Manual. Rate Rule 12-11, concerning mortgagee policy endorsements, was amended. Procedural Rule P-16 was amended to change the procedure for the issuance of a mortgagee title policy binder on interim construction loans (interim binder). Now, an interim binder shall be issued only when it is contemplated in good faith that the issuing company will be asked to issue its mortgagee policy, issued simultaneously with an owner's policy or at the basic rate, on a permanent loan covering the identical property. The foreclosure information letter and foreclosure binder, formerly provided for in Rate Rule R-15 and Procedural Rule P-17, was eliminated, and Rate Rule R-14, which allows a rate credit of $15 when property which has been directly acquired through foreclosure involving an insured mortgagee policy is being sold and an owner’s policy or a mortgagee’s policy on a lien retained in the deed of conveyance is being issued in connection with the transaction, was amended to delete reference to former Rate Rule R-15. Finally, the board added language to the endorsement instruction for endorsement of a mortgagee policy at the time of periodic construction advances. The Basic Manual is available from Hart Graphics, P.O. Box 968, Austin, Texas 78767. For a recent general discussion of title insurance see Curtis, Title Assurance in Sales of California Residential Realty: A Critique of Title Insurance and Title Covenants With Suggested Reforms, 7 PAC. L.J. 1 (1976).

91. See Procedural Rule P-2 which permits the deletion of the areas and boundaries exception upon an acceptable survey and the payment of a higher premium.


93. Id. at 51.
which affect his title. In so holding, the court indicated that an equitable interest cannot be created merely by the recordation of an instrument which itself provides for no such interest.⁹⁴

Another issue in the case concerned the effect of a second contract between Utilities and the Clear Lake Water Authority providing that Utilities had the exclusive right to provide water and sewer service within a certain tract of land. Clear Lake Water Authority had entered into a waste disposal agreement with the City of Pasadena. On appeal, it was held that the trial court had lacked jurisdiction to decide this issue because certain indispensable parties were absent from the case. The disposition of this case by the Texas Supreme Court should be watched with interest.

2. Slander of Title.

A significant case of great interest and even greater importance is Walker v. Ruggles⁹⁵ which involved a suit to remove cloud on title coupled with an action for slander of title. The Ruggles had refused to sign an earnest money contract for the sale of their home presented to them by the Walkers, brokers under a listing agreement with the Ruggles, because the contract did not contain a description of a certain encroachment by the Ruggles' property onto an adjacent tract. The Walkers filed the unexecuted earnest money contract in the Harris County deed records, and later sent a letter to all real estate agents and title companies active in the area, including the agency then listing the Ruggles' home, inferring that the Walkers had a "standing judgment" against the Ruggles and their home.

The court held that in order for a party to recover in Texas on an action for slander of title, he must allege and prove that false, disparaging words were uttered against him and published with malice, that he sustained special damages, and that he possessed an interest in the property disparaged.⁹⁶ Deliberate and false claims by the Walkers of a standing judgment, made without reasonable cause, were sufficient evidence of malice to sustain an award of actual damages.⁹⁷ Moreover, the court found the mailing of the letters to be as follows:

a blatant attempt . . . to interfere with [Ruggles'] economic relations, as well as with [Ruggles'] existing contractual relations. The letter could not have served to protect any legitimate interest of [the Walkers] in a commission, because they had none. The purpose was to prevent [the Ruggles] from selling their house and to force them to pay an unearned commission. We hold that there was sufficient evidence of ill will, spite, and reckless disregard for the rights of others to support an award of punitive damages against [the Walkers].⁹⁸

The issue of the necessity of proving loss of a specific sale as a result of the disparaging utterance was considered by the court. Several Texas cases have

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⁹⁴ Id. Writ of error was granted on this point. 20 Tex. Sup. Ct. J. 3, 4 (Oct. 9, 1976).
⁹⁶ Id. at 473.
⁹⁷ Id. at 473-74.
⁹⁸ Id. at 474.
held that a plaintiff must plead and prove a lost sale to satisfy the special
damages element in slander of title cases. The court in Walker v. Ruggles,
however, rejected these earlier decisions, finding that the trend in the law is
not to rigidly circumscribe special damages in actions such as slander of
title. Inviting further clarification from the Texas Supreme Court, the court
of civil appeals stated that it did not believe the supreme court would adhere
to the rule requiring a plaintiff to prove loss of a specific pending sale in order
to recover in a slander of title action.

Finally, the court set forth the items of damage recoverable as actual
damages in a disparagement action. Financial loss such as loss of sales or
leases, including any decrease in the salable value of property along with
reasonable expenses incurred in maintaining the property during the time its
vendibility is impaired, constitutes the basic measure of damages. Signifi-
cantly, the court also held that the reasonable expenses of litigation necessary
to remove the cloud from the title to the property are recoverable.

The decision of the court is sound in its recognition of the difficulty of
proving the loss of an actual sale. Moreover, the potential for recovery of
attorneys’ fees and other litigation expenses which this decision makes
available should provide an incentive for the execution of releases with
respect to recorded instruments possessing no validity, but which, absent a
release, constitute a cloud on title.

3. Mistaken Improver.

Traditionally, one who in good faith entered upon land and built on it had no
affirmative remedy if his title later proved defective. He could not sue
either at law or in equity to recover the value of his improvements from the
true owner. Recently, however, the trend has been to permit relief not only
where elements of estoppel are present, but also where the true owner has
no knowledge of the activity. Additionally, many states have adopted so
called “betterments statutes” which allow recovery to mistaken impro-
vers. Many of these statutes, including those in Texas, require the
mistaken improver to claim the property under color of title.

99. Shell Oil Co. v. Howth, 159 S.W.2d 483 (Tex. 1942); Humble Oil & Ref. Co. v. Luckel,
171 S.W.2d 902 (Tex. Civ. App.—Galveston 1943, writ ref’d w.o.m.); Houston Chronicle
100. 540 S.W.2d at 474.
101. Id. For authority, the court relied on the Restatement (Second) of Torts §§ 633, 624
(1965).
102. 540 S.W.2d at 476.
103. Id.
106. See, e.g., Toalson v. Madison, 307 S.W.2d 52 (Mo. App. 1957).
107. See, e.g., Beacon Homes, Inc. v. Holt, 266 N.C. 467, 146 S.E.2d 434 (1966); D. Dobbs,
Remedies § 5.8, at 368-69 (1973).
108. See D. Dobbs, supra note 107, § 5.8, at 369.
App.—San Antonio 1960, writ ref’d n.r.e.).
not limited to persons suing in trespass to try title under the statutes as recovery may also be had under principles of equity.\footnote{112}{See, e.g., Gause v. Gause, 430 S.W.2d 409 (Tex. Civ. App.—Austin 1968, no writ).}

In Whelan v. Killingsworth\footnote{113}{537 S.W.2d 785 (Tex. Civ. App.—Texarkana 1976, no writ).} the court recognized that the general rule in Texas permits one who improves real estate under an erroneous but good faith belief that he owns the land to recover the cost of the improvements to the extent that such improvements have enhanced the value of the land. The court held, however, that when the entry and improvements are made during the pendency of litigation involving the validity of the improver's claim of title, such improvements are made at the peril of the improver, and no recovery will be allowed. The court also held that improvements made after a favorable trial court judgment but before the time for appeal has expired will be considered as made during the pendency of litigation and therefore not made in good faith.

II. PURCHASES AND OTHER TRANSACTIONS

A. Contract Validity and Interpretation

A number of cases which involve the enforceability and construction of contracts of sale are discussed in this article under the topic of Seller's and Purchaser's Remedies.\footnote{114}{See discussion beginning with text accompanying note 123 infra.} The few remaining cases dealing with this topic are discussed in this section.

In Harris v. Potts\footnote{115}{528 S.W.2d 321 (Tex. Civ. App.—Beaumont 1975, aff'd, 20 Tex. Sup. Ct. J. 95 (Dec. 8, 1976).} the court was asked to enforce an oral agreement to sell an undivided interest in real property. The Texas Statute of Frauds,\footnote{116}{TEX. Bus. & COMM. CODE ANN. § 26.01 (Vernon 1968).} of course, requires that a contract to sell real property be in writing in order to be enforceable. The statute is not without exceptions, however. If certain conditions have been met, the courts have been willing to enforce an oral contract. These conditions, as stated in Hooks v. Bridgewater,\footnote{117}{111 Tex. 122, 229 S.W. 1114 (1921).} are: (1) the consideration must have been paid; (2) the seller must have surrendered possession to the purchaser; and (3) the purchaser must have made valuable and permanent improvements upon the land. The purchaser in Harris testified that he had paid the consideration, helped make some minor improvements on the land, and had signed and helped repay a promissory note which financed other improvements. The court of civil appeals held that even if the purchaser had satisfied two of these conditions, he had failed to show he had taken possession of the land. Apparently, the purchaser and seller were developing the property to be sold for residential lots and the purchaser argued that under the circumstances he had done all he could to take possession. The court, on the authority of Bridgewater, disagreed and found the contract within the Statute of Frauds. The Texas Supreme Court has granted writ of error.
If a contract of sale simply makes reference to a recorded deed for a description of the property "for full description and all purposes" and provides that the seller will convey the property by general warranty deed "free and clear of all encumbrances except those named herein," must the purchaser accept title burdened with any encumbrances listed or referred to in that deed? The court of civil appeals thought not in *Fajkus v. Bland,* 118 The court seems to have been primarily concerned with the sufficiency of the notice given to the purchaser finding that a mere reference for "all purposes" to a recorded deed was not sufficient to alert him to encumbrances listed in the deed. On the other hand, a statement in the contract that the conveyance would be subject to all encumbrances listed in the recorded deed probably would have been sufficient notice.119 The court concluded as follows: "The simple rule, which we are laying down in a contract of sale case, is that a seller must set forth any mineral or other interest which is outstanding, or at least let the description show specifically that the conveyance will be subject to an exception or reservation."120 A purchaser would be wise not to rely too heavily on the court's decision, especially if the contract incorporates a recorded instrument by reference, or, as is often the case, the contract states that the conveyance will be subject to all easements, reservations, and other encumbrances of record.

In *Wirtz v. Orr*121 the court of civil appeals reversed and remanded a judgment that the parties were entitled to certain adjustments on the exchange of properties. Two of the special issues submitted asked whether the jury found from the evidence that certain obligations arose "under the contract between the parties." These issues were held to have asked the jury to construe the meaning of the contract, which was a question of law for the court.

B. **Seller's and Purchaser's Remedies Under Contracts of Sale**

The various remedies available to a party to a contract of sale of real property upon the default of the other party include the following: (1) avoidance or annulment of the contract through rescission by mutual agreement; (2) the right to treat the default as an offer of rescission; (3) quiet title, ejectment and similar actions to terminate the contract and any obligation for future performance; (4) specific performance or an action for damages; and

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118. 535 S.W.2d 398 (Tex. Civ. App.—Beaumont 1976, writ ref'd n.r.e.).
119. The court stated: "Where, as here, reference is made to deeds or other instruments only generally, we decline to require the purchaser to be charged with notice of the reservations contained in those instruments, unless the earnest money contract itself speaks of them." *Id.* at 400.
120. *Id.* The court refused to extend to a contract of sale the rule that references made in deeds to other instruments put the grantee on notice of title exceptions disclosed in those instruments, as set forth in *Harris v. Windsor,* 156 Tex. 324, 294 S.W.2d 798 (1956), and *Remuda Oil Co. v. Wilson,* 264 S.W.2d 192 (Tex. Civ. App.—Galveston 1954, writ ref’d n.r.e.). The court’s holding is one of fairness, but the reason for not extending the deed cases is wrong—the court said that to extend the *Harris* rule to a contract would require a title search prior to execution. Of course, so would a provision, which the court apparently would approve, that the conveyance would be subject to encumbrances listed in the recorded instruments. The court further stated that the purchaser could not have determined the extent of the minerals reserved by an examination of the recorded deeds, one of which deeds merely stated that the conveyance was subject to all recorded encumbrances.
121. 533 S.W.2d 468 (Tex. Civ. App.—Eastland 1976, writ ref’d n.r.e.).
(5) forfeiture and liquidated damages. The availability of a number of these remedies has been the subject of several decisions pertinent to this Survey.

1. Rescission and Specific Performance.

A suit brought by the sellers for rescission of a contract ended in an award of specific performance for the purchasers in Grundmeyer v. McFadin. The sellers apparently were advised by their attorney that the contract provided for payment of the purchase price within sixty to ninety days. When they later learned this statement was incorrect, the sellers sought to have the contract rescinded on the basis that they were misled into entering into the contract. The court of civil appeals, however, held that since the jury had found that the market value of the property was the same as the contract price, the sellers had failed to show they had sustained any injury or damage.

The sellers argued that the purchasers were not entitled to specific performance because the purchasers were guilty of tortious interference with a pre-existing contract and did not, therefore, have "clean hands." The court rejected this argument and granted specific performance on the basis that the pre-existing contract was unenforceable, and the sellers could not show any damages from the interference, and because the sellers were not parties to the prior contract.


123. 537 S.W.2d 764 (Tex. Civ. App.—Tyler 1976, writ ref'd n.r.e.).

124. The court relied upon the following pronouncement in Bryant v. Vaughn, 33 S.W.2d 729, 730 (Tex. Comm'n App. 1930, opinion adopted):

The rule in this state is settled that the equitable remedy of cancellation is not available because of fraudulent representation made to induce the execution of a contract unless it be shown in connection therewith that some injury or damage has resulted to the party claiming to be aggrieved. The rule announced in the above case [Russell v. Industrial Transp. Co., 113 Tex. 441, 251 S.W. 1034 (1923)] bars defendants in error's right to rescission of the trade in view of the jury's finding that the value of the property received by them was equal to that with which they parted possession.

125. This issue had been litigated and resulted in a judgment in the sellers' favor in Walzem Dev. Co. v. Gerfers, 487 S.W.2d 219 (Tex. Civ. App.—San Antonio 1972, writ ref'd n.r.e.).

126. The sale price in the prior contract was for $1,700 an acre, while the second contract was for $2,500 an acre.

127. A cause of action for wrongful interference with a contract requires, among other elements, actual damage to the complaining party. Tippett v. Hart, 497 S.W.2d 606 (Tex. Civ. App.—Amarillo), writ ref'd n.r.e. per curiam, 501 S.W.2d 874 (Tex. 1973). Inducing a party to breach a contract to the damage of another party to the contract is an actionable wrong. Brown Hardware Co. v. Indiana Stoveworks, 96 Tex. 453, 73 S.W. 800 (1903); Raymond v. Yarrington, 96 Tex. 443, 73 S.W. 800 (1903). A party who accuses another party of having "unclean hands" must show he has been injured by that party's conduct. Omohundro v. Matthews, 161 Tex. 367, 341 S.W.2d 401 (1960).

The sellers in Grundmeyer also challenged the purchaser's right to specific performance on the ground that, because the contract incorrectly named a party to the contract as guardian for another party, the purchases were seeking to bind the judicial process. The court held that even if this allegation were true, it was not a defense to specific performance because the purchasers "do not require any aid from the illegal act to maintain their action." 537 S.W.2d at 771, citing Morrison v. City of Fort Worth, 138 Tex. 10, 153 S.W.2d 908 (1941), and other Texas cases. The court coupled this rule with the rule that where a contract is void or illegal in part, a cause of action may be maintained under the valid part, citing Hazzard v. Morrison, 104 Tex. 589, 143 S.W. 142 (1912).

The sellers further attacked the conduct of the attorney who represented them in the contract negotiations, because of his representations concerning the contract and his relationship with the purchasers. The court found there to be some evidence to indicate the attorney was an agent for the purchasers, but refused to find any conflict of interest. 537 S.W.2d at 769, 772.
N.R.C., Inc. v. Huckabee\[128\] represents an unsuccessful effort on the part of a purchaser of a Lake Travis subdivision lot to rescind his contract for deed on the basis of fraud and a violation of the Interstate Land Sales Full Disclosure Act.\[129\] The jury had found that representations made by the salesman as to the suitability for a particular type of housing were false. The court of civil appeals, however, viewed these representations as promises of future action which lacked the requisite present intention not to perform.\[130\] The allegation of a violation of the Interstate Land Sales Full Disclosure Act was premised upon a statement in the property report that no "special foundation work" would be required to build a house on the lot. The court held that special foundation work referred to "some unusual soil condition not apparent to the viewer . . . rather than merely to a hillside lot."\[131\] A judgment for rescission entered by the trial court was therefore reversed and rendered.

In McDaniel v. Pettigrew\[132\] the purchasers sought cancellation and rescission of a contract to purchase residential lots, as well as cancellation of the notes, deeds of trust, and lien agreement executed in connection with the contract. Cancellation was sought under the Home Solicitation Act.\[133\] One of the purchasers further alleged misrepresentation and failure to perform the contract on the part of the seller. The trial court entered a summary judgment denying the purchasers any relief. The court of civil appeals held that, since the transaction was for the sale of realty and conducted by a licensed real estate broker it was expressly excluded from coverage under the Act.\[134\] It was further held that summary judgment was properly rendered on the issue of misrepresentation because the evidence failed to establish a genuine issue of fact as to the essential element of lack of intent on the part of the sellers to perform any promise that might have been made by them at the time of the transaction.

\[128\] 539 S.W.2d 375 (Tex. Civ. App.—Austin 1976, no writ).
\[130\] Stanfield v. O'Boyle, 462 S.W.2d 270 (Tex. 1971); Chicago, T. & M.C. Ry. v. Titterington, 84 Tex. 218, 19 S.W. 472 (1892). Is a false representation that a lot is suitable for a modular residence a promise of future action? This is the representation the jury found to be false, but the court refers to the representation as being "that appellants could, and would, build a granada model house on the desired location." 539 S.W.2d at 377. See McDaniel v. Pettigrew, 536 S.W.2d 611 (Tex. Civ. App.—Dallas 1976, writ ref'd n.r.e.), discussed in notes 132-36 infra and accompanying text, for another unsuccessful allegation of the seller's misrepresentation.
\[131\] 539 S.W.2d at 378. The court's opinion does not indicate what sort of foundation work would have been required on the lot.
\[132\] 536 S.W.2d 611 (Tex. Civ. App.—Dallas 1976, writ ref'd n.r.e.).
\[133\] TEX. REV. CIV. STAT. ANN. arts. 5069-13 to .06 (Vernon Supp. 1976-77).
\[134\] Id. art. 5069-13.01(B) excludes from the definition of "home solicitation transaction" any sale of realty where "the purchaser is represented by a licensed attorney or in which the transaction is being negotiated by a licensed real estate broker or in which the transaction is being negotiated by the person who owns the property not at the residence of the consumer." The court noted that in order to bring the transaction within the exclusion the attorney must be representing the purchaser, and the broker need not be representing the purchaser. 536 S.W.2d at 615. The purchasers argued that the contracts were not for the sale of realty, within the meaning of the statutory exception, but were agreements for services, i.e., the construction of a house on the lots. The court disagreed with this argument, however, but in any event the court concluded that this was not a "solicitation" by the seller within the meaning of the act, because the purchaser had sought out the broker who negotiated the transaction. Id. at 615-16.
execution of the instruments in question.\textsuperscript{135} In response to the purchaser's argument that the seller breached the contract by failing to build the house in a good and workmanlike manner, the appellate court noted that while the appellants did not seek damages or correctly plead breach of warranty or failure of performance of the contract at the trial court level, the appellants did present summary judgment proof which would create an issue of fact if pleaded. The court held that in such a situation summary judgment would be improper.\textsuperscript{136}

The essential terms of a contract of sale must be ascertainable with reasonable certainty in order to entitle a party to specific performance.\textsuperscript{137} One of these essential terms is a sufficient description of the property. Due to the absence of readily available information, lawyers, or their clients, often must improvise in describing real property for purposes of a contract of sale. In several cases decided during the survey period these efforts failed. One such case is \textit{U.S. Enterprises, Inc. v. Dauley},\textsuperscript{138} a suit which was filed to enforce specific performance of a contract to sell 600 acres of land. Only thirty acres of the 600 acres in question were at issue before the Texas Supreme Court.\textsuperscript{139} This thirty acres was in a survey neither mentioned in the contract nor on the map attached to the contract.\textsuperscript{140} By a five to four decision the court held that the failure to name the survey in which the thirty-acre tract was located was fatal,\textsuperscript{141} but that even if the survey had been named, the thirty-acre triangular

\textsuperscript{135} See also \textit{N. R. C., Inc. v. Huckabee}, 539 S.W.2d 375 (Tex. Civ. App.—Austin 1976, no writ), discussed in notes 128-31 supra and accompanying text. The alleged misrepresentation in \textit{McDaniel} was said to have been the seller's promise not to enforce the renewal note and security instruments.

\textsuperscript{136} The appellate court stated the rule that while a contract remains wholly executory, a partial breach of a material part of the contract is enough to allow rescission, even though rescission ordinarily will be denied when there is an adequate remedy at law, citing \textit{Hausler v. Harsing-Gill Co.}, 15 S.W.2d 548 (Tex. Comm'n App. 1929, jdgmt adopted); the "purchaser" has the option of requesting rescission or holding the builder to the contract and requesting damages, citing \textit{Greenwall Theatrical Circuit Co. v. Markowitz}, 97 Tex. 479, 481, 79 S.W. 1069, 1071 (1904), and \textit{Cantu v. Bage}, 467 S.W.2d 680, 682 (Tex. Civ. App.—Beaumont 1971, no writ). In \textit{McDaniel}, however, the court said that the house had been completed, with a few minor exceptions, at the time the purchaser refused to accept the house, and, therefore, the contract was not wholly executory. The builder had performed to the extent that rescission would have been inequitable. 536 S.W.2d at 617. See generally McNamara, \textit{The Implied Warranty in New-House Construction: Has the Doctrine of Caveat Emptor Been Abolished?}, 1 REAL EST. L.J. 43 (1972).

\textsuperscript{137} Bryant v. Clark, 358 S.W.2d 614, 616 (Tex. 1962). Specific performance is an equitable remedy which is generally available to enforce a contract of sale, unless to do so would be substantially inequitable or unconscionable. Kress v. Soules, 261 S.W.2d 703 (Tex. 1953); \textit{Bennett v. Copeland}, 235 S.W.2d 605, 609 (Tex. 1951). The right to the remedy of specific performance depends upon certain conditions: "(a) The contract must be reasonably certain, unambiguous and based upon valuable consideration; (b) it must be fair in all its parts, free from misinterpretation, misapprehension, fraud, mistake, imposition or surprise; (c) the situation of the parties must be such that specific performance will not be harsh or oppressive; and (d) the one seeking the remedy must come into court with clean hands." Nash v. Conatser, 410 S.W.2d 512, 519 (Tex. Civ. App.—Dallas 1966, no writ). See generally 8A G. THOMPSON, supra note 122, §§ 4479-4481; 59 TEX. JUR. 2d Vendor and Purchaser §§ 510-516 (1964).

\textsuperscript{138} U.S. Enterprises, Inc. sued to specifically enforce the total contract, but while the suit was pending, the owner sold approximately thirty acres to Dauley. Dauley, after being interpleaded in the suit, moved for summary judgment on the basis that the contract failed to describe sufficiently his thirty-acre tract.

\textsuperscript{139} Three other surveys were listed as encompassing all of the 600 acres. A map which is a part of the contract can supplement an inadequate property description, provided the map contains sufficient information. 535 S.W.2d at 623; \textit{Pritchard v. Burnside}, 140 Tex. 212, 167 S.W.2d 159 (1942). See generally \textit{Hudon v. Fin. Co.}, 136 Tex. 149, 146 S.W.2d 977 (1941).

\textsuperscript{140} Although the court cited several examples where descriptions had been upheld without reference to a survey, it stated that "our cases have stressed the importance of identifying land as
tract, although bounded on all three sides by identifiable streets and highways, still would not have been sufficiently described. The disturbing aspect of the court's opinion is that there is a suggestion, at least under the facts before the court, that the enforceability of the contract with respect to a portion of the property may be challenged even though the description of the whole of the tract covered by the contract is sufficient.

Another purchaser's effort to specifically enforce a contract fell short for lack of a sufficient legal description in Guenther v. Amer-Tex Construction Co. The contract did not show the length of the boundary lines, the size of the tract, nor the name of the owner of the tract. Further, it failed to refer to a recorded deed or other instrument from which the land might be identified, and did not otherwise sufficiently identify the property. The careful lawyer should, therefore, collect all available information before attempting to describe the property. Helpful documentation would include the following: the deed conveying the property to the seller (but only if all of the same property is to be conveyed); a deed of trust covering the property; a statement that the seller owns the property; the survey or surveys in which the property is located; reference to a recorded map or plat; street address, city, county and state; any boundary line references (streets, highways, easements, waterways, other surveys or property owners, and the like); and survey plats, maps or sketches. If the sufficiency of the legal description remains in doubt and litigation ensues, the party seeking to enforce the contract should consider having the contract reformed to cure the deficiency, if reformation is available for this purpose.

being within a certain league, labor, or survey," 535 S.W.2d at 629. The opinion contains a text-book discussion of the requisites for a legally sufficient description of property, beginning with the requirement that the contract "furnish within itself, or by reference to some other existing writing, the means or data by which the particular land to be conveyed may be identified with reasonable certainty," as set forth in Wilson v. Fisher, 144 Tex. 33, 188 S.W.2d 150 (1945). The court said that there was no question that the parties intended the thirty-acre tract to be included in the contract, but that "the knowledge and intent of the parties will not give validity to the contract..." 535 S.W.2d at 628, citing Morrow v. Shotwell, 477 S.W.2d 538 (Tex. 1972); Rowson v. Rowson, 154 Tex. 216, 218, 275 S.W.2d 468, 470 (1955).


143. 534 S.W.2d 396 (Tex. Civ. App.—Austin 1976, no writ).

144. In American Sav. & Loan Ass'n v. Musick, 531 S.W.2d 581 (Tex. 1975), discussed in Wallenstein & St. Claire (1976), supra note 2, at 50, the deed referred to 618.7 acres more or less out of a particular survey "more particularly described by metes and bounds" in a certain pre-existing deed of trust. The deed of trust covered the 618.7-acre tract and two smaller tracts. The purchaser's mortgagee argued that the deed, and thus its deed of trust, covered all three tracts. The court disagreed, and held that although the deed referred to the prior deed of trust for a more particular description, it was only for the purpose of giving a more particular metes and bounds description of the 618.7-acre tract, and that the deed did not purport to convey all of the tracts described in that deed of trust. Id. at 585.

145. The court noted in U.S. Enterprises, Inc. that the plaintiff had not moved to reform the contract to correct a mutual mistake as to the name of the surveys or other descriptive deficiencies. 535 S.W.2d at 630. In National Resort Communities, Inc. v. Cain, 526 S.W.2d 510, 513 (Tex. 1975), the Texas Supreme Court said that the two requirements for reformation are: (1) proof of the true agreement of the parties (a mistake about some aspect of the agreement may justify rescission, but not reformation), and (2) proof that the provision that was erroneously included in or omitted from the agreement was a mutual mistake; that is, reformation is to make the agreement say what the parties wished it to say. See also Morrow v. Shotwell, 477 S.W.2d 538 (Tex. 1972).
Schwope v. Kiesling involved an appeal from a summary judgment entered against the purchaser who was seeking specific performance of a contract for sale of a large parcel of land. The court reversed and remanded, holding that the purchaser was entitled to specific performance because he had timely accepted the seller's offer by signing the contract of sale on the date on which the offer was to expire. The fact that the seller may have owned only one-half of the minerals was not held to be material to the enforceability of the contract. The court further held that the purchaser's deletion of two contingencies, which had been inserted for his benefit, at the time he signed the contract was not a rejection of the seller's offer.

2. Recovery of Escrow Deposit.

During the recent real estate boom it has not been at all uncommon for a purchaser to enter into a contract to acquire property and then to attempt to sell his contract to another. There is nothing intrinsically wrong with a person selling property before he obtains legal title. The seller's inability later to acquire title to property he had contracted to sell, however, was fatal to his effort to recover his purchaser's escrow deposit in Bradley v. Apel.

Although the contract stated that closing would occur ninety days after the date of the contract, the court of civil appeals held that the seller was unable to show that there was a date certain set for the closing, at which the purchaser had breached the contract. Concerning the forfeiture of the purchaser's escrow deposit, the court stated "that in the absence of language plainly dispensing therewith the vendor must, as a rule, give notice of forfeiture or a notice of intention to forfeit within a specified time unless in the meantime the default is made good." The purchaser successfully stalled Apel beyond the

147. The contract made no mention of the seller's mineral ownership. The seller alleged that the contract could not be enforced, because he owned only one-half of the minerals and could not convey all of the minerals. The result reached by the court in response to the seller's argument is correct, but the reasoning of the court is faulty. The court stated that, since it was not established that the purchaser expected to receive all of the minerals, it was not shown that the seller was unable to perform. The inability of the seller to convey all of the minerals would not have excused the seller, even if the purchaser had been unwilling to accept less than all minerals. The seller, by making no exception in the contract for outstanding minerals, agreed to convey all of the minerals. Reville v. Poe, 249 S.W.2d 241, 245 (Tex. Civ. App.—Austin 1952, writ dism'd judgm cor.); Sibley v. Pickens, 273 S.W. 897, 898 (Tex. Civ. App.—Amarillo 1925, no writ); 58 TEX. JUR. 2d Vendor and Purchaser § 141 (1964). The seller in this situation, or in any situation where the extent of mineral ownership is unknown or uncertain, should have provided in the contract that he would convey only the minerals he owned, or that the conveyance was subject to outstanding mineral interests, and that if the title report or abstract reflected that he owned a lesser mineral estate, the purchaser could either terminate the contract or accept title subject to the additional encumbrances.
148. The court cited United Concrete Pipe Corp. v. Spin-Line Co., 430 S.W.2d 360 (Tex. 1968), in which the Texas Supreme Court held that an alteration of an instrument which could only benefit the minerals owned, or that the conveyance was subject to outstanding mineral interests, and that if the title report or abstract reflected that he owned a lesser mineral estate, the purchaser could either terminate the contract or accept title subject to the additional encumbrances.
150. A contract of sale is not invalid because the seller does not have title on the date the contract is signed. However, the seller's inability to convey title would subject him to a suit for damages; and in Irwin v. Whirley, 538 S.W.2d 150 (Tex. Civ. App.—Waco 1976, no writ), the purchaser of a lot under a contract for deed recovered the price of the lot, the value of the improvements, and punitive damages from a seller who had no title and knew he could not obtain title.
151. 531 S.W.2d 678 (Tex. Civ. App.—Fort Worth 1975, writ ref'd n.r.e.).
152. Id. at 681. The court said that it did not construe the contract to provide for forfeiture of
ninety day closing date, and Apel never gave Bradley notice setting a closing date. On June 13, about two weeks after the ninety day period had expired, Apel's right to acquire the property from the owner was forfeited because he failed to close on the specified closing date. Time not being of the essence, for the closing of the sale to Bradley, and Apel not having given Bradley notice of a closing date, the court held that Bradley was not in default under the contract on the date Apel lost his right to acquire title under his contract with the owner. Thereafter, the court stated that Apel had no title or means of procuring title to convey to Bradley and, thus, he was not ready, willing, and able to perform his part of the contract. The trial court's judgment awarding the escrow deposit to Apel was therefore reversed and judgment rendered for Bradley.

The seller fared better in Dunham & Ross Co. v. Stevens, where the seller was held to be entitled to the escrow deposit after the purchaser refused to close. The title objections raised by the purchaser as the basis for refusing to close were, in the court's view, without merit. Moreover, the purchaser's repudiation of the contract was held to have excused the seller from fulfilling his obligations under the contract. In Innes v. Webb it was held that between two "apparently inconsistent

153. The owner had given Apel notice of the date for closing the contract, which Apel was unwilling or unable to meet. In fact Apel released his rights under that contract and forfeited his earnest money.

154. Ordinarily time is not of the essence in a contract of sale of real property, unless the contract so provides, Tabor v. Ragle, 526 S.W.2d 670, 675 (Tex. Civ. App.—Ft. Worth 1975, writ ref'd n.r.e.), or unless the terms of the contract show a clear intent that time is of the essence. Smith v. Warth, 483 S.W.2d 834, 836 (Tex. Civ. App.—Waco 1972, no writ). See 8A G. THOMPSON, supra note 122, § 4460. If time is of the essence, then the performance of the contract within the specified time is essential to the right to require performance by the other party. McKnight v. Renfro, 371 S.W.2d 740, 745 (Tex. Civ. App.—Dallas 1963, writ ref'd n.r.e.). The opposite rule applies to option contracts, in which time is of the essence unless the parties otherwise agree. See White v. Miller, 518 S.W.2d 383, 386 (Tex. Civ. App.—Tyler 1974, writ dism'd), which also demonstrates that it may not always be easy to distinguish between the contract and an option. Because the purchaser's obligation to close the contract was conditioned upon his obtaining financing, the court found the contract to be an option. See also Tabor v. Ragle, supra, where the court, after discussing the tests for determining if a contract is an option, held that there was a contract.

155. The court, on the authority of Brown v. Lee, 192 F. 817 (5th Cir. 1911), said that Apel could not, under these circumstances, either enforce specific performance or recover the escrow deposit. The party seeking specific performance of a contract of sale must show that he is ready, willing, and able to perform his part of the contract. See Hendershot v. Amarillo Nat'l Bank, 476 S.W.2d 919 (Tex. Civ. App.—Amarillo 1972, no writ); Beck v. South, 423 S.W.2d 188 (Tex. Civ. App.—Fort Worth 1967, writ ref'd n.r.e.) (purchaser failed to prove he had purchase money on date for closing).

156. 538 S.W.2d 212 (Tex. Civ. App.—Waco 1976, no writ).

157. The title objections were (1) the seller's ownership of only one-half the minerals (the contract only required the seller to convey the minerals he owned), (2) certain easements (which the court found to be within the permitted exception for utility easements), and (3) a mortgage lien which was broader than as described in the contract (of which the court said the purchaser was on constructive or actual notice, because the deed of trust was recorded).

158. The court cited as authority, among others, Universal Life & Accident Co. v. Sander, 179 Tex. 344, 102 S.W.2d 405 (1937); Miller v. Puritan Fashions Corp., 516 S.W.2d 234 (Tex. Civ. App.—Waco 1974, writ ref'd n.r.e.).

159. 538 S.W.2d 237 (Tex. Civ. App.—Corpus Christi 1976, writ ref'd n.r.e.). The court of civil appeals relied upon the authority of Universal C.I.T. Credit Corp. v. Daniel, 150 Tex. 513, 243 S.W.2d 154 (1951), for the rule that a typed provision controls over a printed provision in deciding which of two conflicting provisions will be applied; and, furthermore, that this rule of construction is to be applied instead of the rule that a contract will be construed against the person who prepared it (the realtor). 538 S.W.2d at 239.
provisions in a contract of sale, the typed provision (which required the broker to deliver the purchaser’s escrow deposit to the seller for initial deposit for materials and administrative cost) controlled over a printed provision (which entitled the purchaser to the return of his deposit if the seller failed to perform). Accordingly, the trial court’s judgment that the purchaser recover his escrow deposit from the broker was reversed. Actually, the two contract provisions were not inconsistent, but the court reached a correct result on the facts stated in the opinion. The purchaser’s cause of action would have been more successful had it been directed against the seller.

3. Risk of Loss and Damages.

The execution of a contract to purchase real estate passes the risk of loss to the purchaser unless the contract stipulates to the contrary. This rule was applied in Fant v. Howell to place the risk of loss on the purchaser due to the ripening of adverse possession after the date the contract was signed and the purchaser took possession. The court, therefore, affirmed the trial court’s judgment that the purchaser was not entitled to a general warranty deed covering that portion of the property which had been lost to the adverse possessor. The Texas Supreme Court has granted writ of error.

In Littleton v. Woods the purchaser of a house filed suit for breach of warranty to construct the house in a good and workmanlike manner and for relief under the Texas Consumer Protection Act. The jury found that the

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160. It is not clear from the opinion why suit was brought against the realtor instead of the seller, although the following statement in the opinion may be a hint: “[The next day Innes [the realtor] endorsed the check over to Huller [the seller]. Subsequently, Huller left town and no further action was taken on the contract.]” 538 S.W.2d at 239. Clearly, the realtor was within his authority to deliver the escrow deposit to the seller.

161. The two contract provisions would be inconsistent only if the seller had the right to use the escrow deposit for the stated purposes, whether or not the seller later defaulted under the contract. A more logical interpretation is that the escrow deposit, if used as an initial deposit for materials and administrative costs, had to be returned to the purchaser if the seller defaulted. Thus, the two provisions were not inconsistent. The opinion does not state whether or not the seller used the escrow deposit for the authorized purpose.

162. Whittenburg v. Miller, 139 Tex. 586, 164 S.W.2d 497 (1942); Northern Tex. Realty & Constr. Co. v. Lary, 136 S.W. 843 (Tex. Civ. App. 1911, writ ref’d). This statement of the rule assumes that any loss suffered by damage to the property is not the fault of the seller. Between the seller’s insurer and the purchaser’s insurer, the purchaser’s insurer must shoulder the loss. Paramount Fire Ins. Co. v. Aetna Cas. & Sur. Co., 353 S.W.2d 841 (Tex. 1962). Could the purchaser recover on the seller’s insurance policy if the purchaser has no insurance? The court in Paramount Fire Ins. Co. left this question unanswered, by stating: “[W]e leave open the question of whether, where the vendee has no insurance, there can be a recovery on the vendor’s policy subject to a constructive trust for the vendee, who is often ignorant of his legal liability in such a situation.” Id. at 845. If, in a situation unlike Paramount Fire Ins. Co. the seller has no right of specific performance, or the contract of sale for some other reason is found to be an option, who bears risk of loss? A contract of sale was held to be an option in Tabor v. Ragle, 526 S.W.2d 670, 675 (Tex. Civ. App.—Fort Worth 1975, writ ref’d n.r.e.). See also White v. Miller, 518 S.W.2d 383 (Tex. Civ. App.—Tyler 1974, no writ); Gala Homes, Inc. v. Fritz, 393 S.W.2d 409 (Tex. Civ. App.—Waco 1965, writ ref’d n.r.e.); 8A G. THOMPSON, supra note 122, § 4443, at 258. The careful drafter will consider both risk of loss and right to insurance proceeds in his contract.

163. 537 S.W.2d 350 (Tex. Civ. App.—Austin 1976, writ granted), also discussed in note 14 supra and accompanying text.

164. Writ was granted to consider two points: (1) whether performance of the contract was excused by a foreseeable impossibility; (2) whether an undertaking to bring about a condition is an implied condition precedent. 20 Tex. Sup. Ct. J. 5 (Oct. 9, 1976).

165. 538 S.W.2d 800 (Tex. Civ. App.—Texarkana 1976, no writ).

builder had breached the warranty, but the court of civil appeals held that the measure of damages applied by the jury was improper. The court further found, following Cape Conroe, Ltd. v. Specht, that since the sale took place in 1972, the Texas Consumer Protection Act was not applicable. The act was amended effective September 1, 1975 to include "real property purchased or leased for use" within the definition of "goods" under section 12.45(1) of the Act. Finally, in Irwin v. Whirley the purchaser of a lot under a contract for deed recovered the price paid for the lot, the value of the improvements, and punitive damages from a seller who had no title when he signed the contract and who then knew he would be unable to deliver title to the purchaser.

C. Brokerage

1. Real Estate Brokerage Commissions.

Every year disputes involving the payment of real estate commissions produce a great deal of litigation, and this survey period was no exception. On the whole, brokers were not very successful at selling the courts on their claims. In Del Andersen & Associates v. Jones the broker sued to recover a commission under an exclusive agency listing agreement. The broker alleged that it had procured a ready, willing, and able purchaser who signed a contract with the owner to purchase a motel, but the owner refused to pay the brokerage commission. The defendant contended that no commission was owed because (1) the broker failed to advise the purchaser to have an abstract of title examined by an attorney or to obtain title insurance, as required under section 28 of article 6573a, (2) the description of the property in the listing agreement was legally insufficient, and (3) the contract signed by the purchaser and owner was not an enforceable contract.

The court of civil appeals referred to West Realty & Investment Co. v. Hite and Cooper v. Wildman for the general rule that a broker earns his commission when he procures a ready, willing, and able purchaser on the terms specified in the listing agreement, even though the contract is not closed 167. The court refers to Humber v. Morton, 426 S.W.2d 554 (Tex. 1968), for a discussion of the warranty implied in the sale of a new house.

169. Wallenstein & St. Claire (1976), supra note 2, at 44.
172. TEX. REV. CIV. STAT. ANN. art. 6573a, § 20 (Vernon Supp. 1976-77) provides in part as follows:

At the time of the execution of any contract of sale of any real estate in this state, the Real Estate Salesman, Real Estate Broker, Real Estate Agent or Realtor shall advise the purchaser or purchasers, in writing, that such purchaser or purchasers should have the abstract covering the real estate which is the subject of the contract examined by an attorney of the purchaser’s own selection, or that such purchaser or purchasers should be furnished with or obtain a policy of title insurance; and provided further, that failure to so advise as hereinabove set out shall preclude the payment of or recovery of any commission agreed to be paid on such sale.

Article 6573a was amended in 1975, and substantially the same provision is now contained in TEX. REV. CIV. STAT. ANN. art. 6573a, § 20 (Vernon Supp. 1976-77).

174. 528 S.W.2d 80 (Tex. Civ. App.—Corpus Christi 1975, no writ).
because of some fault or inability of the seller. In response to the owner’s third defense the court of civil appeals held that the plaintiff, upon procuring a ready, willing, and able purchaser, was entitled to a commission under the listing agreement whether or not there was an enforceable contract to purchase the property.\footnote{175} Defendant’s second defense was also rejected by the court which found that the notation in the listing agreement that the defendant was the owner, coupled with evidence that the defendant owned no other property in Comanche County, was a sufficient description of the property.\footnote{176} Finally, the court of civil appeals held that the broker was not required to comply with article 6573a, section 28, in order to earn his commission under the listing agreement. All he was required to do was procure a ready, willing, and able purchaser for the property.

On appeal, however, the Texas Supreme Court refused to give article 6573a such a narrow interpretation, reversed the court of civil appeals, and affirmed the trial court’s summary judgment in favor of the seller.\footnote{177} Article 6573a, section 28, the court held, was intended to apply in all situations, whether or not there was a separate listing agreement and whether or not the seller or the purchaser was paying the commission.\footnote{178} The Texas Supreme Court stated that the only exception to the broker’s obligation to comply with this requirement of article 6573a occurs when the broker is wrongfully deprived of the opportunity to comply.\footnote{179}

\textit{V.W. Realty Sales Agency v. Long Meadow Country Club, Inc.} \footnote{180} represents another effort by a broker to recover a commission for negotiating a sale that was never completed. The contract for the sale of a country club which was signed by the broker provided for the seller to pay the broker a commission of six percent of the sale price. It also provided that if the purchaser failed to complete the sale, the seller had the right to retain the purchaser’s $10,000.00 deposit as liquidated damages and to pay the broker...

\footnote{175} McNeny v. Radford, 70 S.W.2d 824 (Tex. Civ. App.—Eastland 1934), rev’d, 129 Tex. 568, 104 S.W.2d 472 (1939); Schmidt v. Willmann, 235 S.W. 629 (Tex. Civ. App.—San Antonio 1921, no writ), and other cases, were cited by the court in support of the holding. See generally 9 \textsc{Tex. Jur. 2d} Brokers \S 50 (1969).

\footnote{176} \textit{See} Pickett v. Bishop, 148 Tex. 207, 208, 223 S.W.2d 222, 223 (1949). The property in \textit{Del Andersen} was described as the Deluxe Motel, 1302 E. Central, Comanche, Comanche County, Texas. The court also found the street address coupled with the “owner” designated to be sufficient, citing Parks v. Underwood, 280 S.W.2d 320 (Tex. Civ. App.—Dallas 1955, writ ref’d n.r.e.). \textit{See generally Annot., supra} note 142. The broker, however, had the same difficulty convincing the court of civil appeals that summary judgment should have been rendered in its favor. The court found that a fact issue existed as to whether the purchaser was ready, willing, and able. The broker argued that the owner, by her execution of the contract of sale, was estopped to deny that the purchaser was ready, willing, and able; but the court held that this rule was inapplicable in this case, because the contract of sale which the broker alleged to be the basis of this estoppel was unenforceable because of an insufficient legal description of the property. The description used in the contract is not set forth in the court’s opinion.

\footnote{177} Jones v. Del Andersen & Associates, 539 S.W.2d 148 (Tex. 1976).

\footnote{178} Nor did it matter that the purchaser had in fact consulted with his attorney concerning the seller’s title. \textit{Id.} at 351.

\footnote{179} \textit{Id.} In \textit{Knight v. Hicks}, 505 S.W.2d 638, 644 (Tex. Civ. App.—Amarillo 1974, writ ref’d n.r.e.), cited by the court, the court stated that the requirement of written notice under article 6573a, \S 28 applies “where the broker charged with the obligation to give such notice has an opportunity to participate in or be present at the execution of the contract of sale;” but he will not be denied recovery of his commission “if he is precluded from doing so by the act of the seller in dealing directly with the buyer.”

\footnote{180} 537 S.W.2d 533 (Tex. Civ. App.—Corpus Christi 1976, writ ref’d n.r.e.).
$5,000.00 of that deposit, or enforce specific performance. The purchaser, John Jamail, defaulted and subsequently instituted proceedings under Chapter XI of the Federal Bankruptcy Act. The defendant dismissed a suit for specific performance against Jamail, and elected to retain the escrow deposit. The broker, however, refused to accept $5,000.00 in full payment of its commission, and filed this suit to recover the $90,000.00 commission which he would have been entitled to had the sale been completed. The court limited the broker's recovery to $5,000.00, stating that

if the contract provides that upon the failure of the purchaser to comply, the owner has the option of retaining the earnest money as liquidated damages, and is required to divide it with the agent, then if the owner exercises that option, the agent is limited to his share of the earnest money and he may not recover a commission based on a percentage of the purchase price.

The court acknowledged the general principles discussed in Del Andersen & Associates v. Jones that the broker earns his commission when he procures a ready, willing, and able purchaser, at least if the completion of the sale is prevented by the seller's default. Thus, the result in V.W. Realty would undoubtedly have been different had the consummation of the sale been prevented by the seller's default. Furthermore, if the broker in V.W. Realty had not signed the contract of sale and had an enforceable listing agreement on the property, it probably would not have been limited by the provision in the contract of sale but could have recovered its commission under the listing agreement. Provisions such as the one at issue in V.W. Realty are common, especially in short-form printed contracts. The broker or his attorney should carefully review the commission provision before executing a contract of sale in order to avoid an unexpected result or inconsistency with the listing agreement.

Hard trading by the purchaser of real property sometimes leaves the seller with a smaller down payment than he had hoped for and than will be necessary if the deal is to be completed. When this occurs the parties, in order to make the deal, may ask the real estate broker to defer a portion (and often a large portion) of his commission for several years after the closing. The seller also may insist that the broker share in his risk that the deferred portion of the sales price may not be paid. This is especially true where the purchaser makes a small down payment and is not personally liable on the promissory note, and particularly so if the broker also is a participant in the purchase of the property. Storey v. Dick Matz Agency should serve as a warning to brokers who expect to earn interest on the deferred portion of the commission. The contract in Storey stated that the commission would be equal to six percent of the sale price and that the broker would receive the commission in increments of six percent of each payment made by the purchaser to the seller. The court held that the broker was entitled to receive only six percent of the sale price,

182. 537 S.W.2d at 536.
183. See notes 171-76 supra.
184. 537 S.W.2d 507 (Tex. Civ. App.—Austin 1976, writ ref'd n.r.e.).
without interest, even though a part of his commission would be paid out of interest installments made on the sale price by the purchaser.\textsuperscript{185}

The right of a licensed real estate salesman to sue for and recover a real estate commission was the key issue in Justice v. Willard.\textsuperscript{186} The bank, as purchaser of a large ranch, agreed to pay plaintiff a commission of $37,800.00, less certain deductions including fees payable to the attorneys representing the salesman and the bank. The bank paid the commission to the salesman but only after deducting an attorney’s fee of $18,700.00, which prompted the salesman to file this suit. The salesman sought to avoid the restrictive commission requirements of section 26 of the Real Estate License Act\textsuperscript{187} by arguing that the suit was one to recover an unreasonable attorney’s fee wrongfully paid. The court disagreed and held that the suit was for the recovery of the real estate commission, brought by a licensed real estate salesman against someone other than the broker under whom he was licensed, which the salesman could not maintain under the provisions of section 26 of the Real Estate License Act. Summary judgment entered in favor of the defendant, therefore, was affirmed. The plaintiff-salesman, the court said, was required either to be a licensed real estate broker at the time the commission was earned, or to have the suit brought by the broker under whom he was licensed.

In Elrod v. Becker\textsuperscript{188} the plaintiff, who did not have a real estate broker’s license, failed to qualify for the exemptions from the licensing requirement provided in the Real Estate License Act\textsuperscript{189} under section 6(3) for a person acting for the owner under a duly executed power of attorney, or section 6(4) for an owner or his employees if the owner is not engaged in whole or in part in the business of selling real estate. The plaintiff, therefore, was denied the recovery of a commission. The plaintiff’s action was unsuccessful because he did not have a written power of attorney, as required by section 6(3). Furthermore, since the owners of the property, by buying, developing, and

\textsuperscript{185} If the payment of the balance of the commission is to be made only if and when the seller receives payments on the deferred portion of the sale price, and only out of these payments (as may very well have been the agreement in Storey), then the broker’s receipt of payment is conditioned upon the seller’s receipt of payment. This would not be the case if the broker’s commission is merely made payable at future intervals, with no requirement that the seller receive payments from the purchaser. In either event, however, the broker should have the deferred portion of his commission represented by a promissory note, providing for the payment of interest, attorney’s fees, and containing other standard note provisions. The promissory note should also provide that the note is not payment of the commission, but only evidences the indebtedness, and, if this is the case, that the payment of the note is conditioned upon the purchaser’s performance of his obligation, in an effort to avoid the note’s being treated for tax purposes as the payment of the full commission in the year the note is delivered. See Jay A. Williams, 28 T.C. 1000 (1957); Robert J. Dial, 24 T.C. 117 (1955). See generally Brandes, Is the Receipt of a Promissory Note the Same as Cash for Federal Income Tax Purposes?, 3 TAXATION FOR LAWYERS 8 (1974). If the payment to the broker is conditioned upon receipt of payment from the purchaser, the broker may want some assurance that the seller will use reasonable efforts to collect payments from the purchaser and will not change the manner of these payments. See Groot, Equitable Enforcement of Deferred Brokerage Commissions, 51 TEXAS L. REV. 76 (1972), which focuses upon deferred commissions on leasing of real property, but is also of general interest.

\textsuperscript{186} 538 S.W.2d 651 (Tex. Civ. App.—Amarillo 1976, no writ).

\textsuperscript{187} TEX. REV. CIV. STAT. ANN. art. 6573a, § 26 (Vernon 1969) provides in part that "[N]o Real Estate Salesman shall be employed by or accept compensation from any person other than the Broker under whom he is at the time licensed . . . ."

\textsuperscript{188} 537 S.W.2d 84 (Tex. Civ. App.—Beaumont 1976, writ ref’d n.r.e.).

\textsuperscript{189} TEX. REV. CIV. STAT. ANN. art. 6573a, §§ 6(3), 6(4) (Vernon 1969).
subdividing the property, were in the business of selling real estate, he was not entitled to the exemption under section 6(4), even though the owner personally may never have sold a lot.

The availability of the exemption under section 6(1) of the Real Estate License Act was an issue in Lehman Brothers Inc. v. Sugarland Industries, Inc.\textsuperscript{190} Section 6(1) exempts from the licensing requirement of the act certain activities in the sale or exchange of real property, if those activities are conducted by a person who does not engage in the activities of a real estate broker "as an occupation, business or profession on a full or part-time basis." The prefatory issues involved in the case were whether Lehman Brothers was employed to find a buyer for Sugarland's stock or realty, and whether Lehman Brothers acted as a finder in the sale of realty, and if so, whether it was exempt from the licensing requirements of the Real Estate License Act. The court of civil appeals held that these issues were disputed fact issues and reversed the trial court's summary judgment entered in favor of the plaintiff. Lehman Brothers had located a purchaser for most of Sugarland's stock, but after suit was filed by the minority shareholders of Sugarland to block the sale, the agreement between Sugarland and the purchaser was restructured to provide instead for the sale of Sugarland's realty, which was its principal asset. Sugarland had been instructed by the court hearing the shareholders' suit to offer the property for sale on competitive bids. Sugarland subsequently sold its realty to a different purchaser.\textsuperscript{191} It was observed that Texas courts have recognized a distinction between finders and brokers,\textsuperscript{192} but declined to decide whether section 4(1)(j) of the Real Estate License Act precludes an unlicensed person from recovering a finder's fee on the sale of realty.\textsuperscript{193} The court stated that whether Lehman Brothers was employed to find a buyer for stock or realty depended upon the nature of the contract and not the form which the principal's transaction ultimately takes.\textsuperscript{194}

\textit{Walters v. Thomas}\textsuperscript{195} concerned the amount of commission a broker is entitled to receive after a contract of sale is rescinded by agreement of the seller and purchaser. The broker was to be paid a real estate commission of

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  \item \textsuperscript{190} 537 S.W.2d 121 (Tex. Civ. App.—Houston [14th Dist.] 1976, writ ref’d n.r.e.).
  \item \textsuperscript{191} The court's opinion does not state how the ultimate purchaser was found; thus, it is unclear on what theory Lehman Bros. was seeking to recover the finder's fee. It could have been on the basis that it had procured a purchaser in accordance with its finder's agreement, although that purchaser did not ultimately buy the property. It could also have been on the basis that the seller was made during the time covered by its finder's agreement, or it might have been that it claimed to have found the ultimate purchaser.
  \item \textsuperscript{192} The court cited Rogers v. Ellsworth, 501 S.W.2d 756, 757 (Tex. Civ. App.—Houston [14th Dist.] 1973), writ ref’d n.r.e.). The struggle faced by brokers in an effort to recover a commission on a sale involving both securities (thus requiring a license to sell securities) and realty (thus requiring a license to sell realty) is illustrated in Taylor Communications, Inc. v. Harte-Hanks Newspapers, Inc., 447 S.W.2d 401 (Tex. 1969), and in Hall v. Hard, 160 Tex. 565, 335 S.W.2d 584 (1960), and in many other Texas decisions.
  \item \textsuperscript{193} TEX. REV. CIV. STAT. ANN. art. 6573a, § 4(1)(j) (Vernon 1969) defines a real estate broker as one who "procures or assists in procuring of prospects, calculated to result in the sale, exchange, leasing or rental of real estate." Sugarland argued that the definition encompasses a finder, and requires licensing in order for a finder to recover a real estate commission.
  \item \textsuperscript{194} The court cited Thywissen v. FTI Corp., 518 S.W.2d 947, 950 (Tex. Civ. App.—Houston [1st Dist.] 1975, writ ref’d n.r.e.), which is discussed in Wallenstein & St. Claire (1976), supra note 2, at 41-42.
  \item \textsuperscript{195} 535 S.W.2d 903 (Tex. Civ. App.—Fort Worth 1976, no writ).
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PROPERTY

$5,000.00 "at time sale is consummated." After the rescission the broker retained $5,000.00 of the purchaser's escrow deposit which he held. After reimbursing the purchaser, the seller sued the broker. The court, upon the authority of West Realty & Investment Co. v. Hite, held that where a contract of sale is not closed due to the fault of the seller, the broker is entitled to his commission, even though the contract contemplated that the commission was to be paid at the time the sale was consummated. Finally, in Porter v. Striegler the broker who had accepted a reduced commission from the purchaser was precluded from thereafter recovering any additional commission from the seller under his listing agreement with the seller. The court reiterated the well-established rule that a broker cannot recover a real estate commission from both the seller and the purchaser unless, with full knowledge, they have consented to such an arrangement.

2. Liability of Brokers Arising from Sales.

Two cases dealing with the liability of brokers for acts arising out of the sale of realty reached decisions during this survey period. In Walker v. Ruggles actual and punitive damages were awarded against the real estate brokers and in favor of the owner of residential property because of false claims made by the brokers that they had a standing judgment for a real estate commission against the owner. Stone v. Lawyers Title Insurance Corp. involved a suit brought by the purchaser of property against the real estate agent for damages alleged to have arisen out of the agent's misrepresentations regarding the location of a pipeline easement. The court found that there was at least some evidence of the agent's liability, and therefore reversed an instructed verdict in favor of the agent and remanded the action for a new trial.

196. 283 S.W. 481 (Tex. Comm'n App. 1926, jdgmt adopted); see note 173 supra and accompanying text.
197. The stipulation in the "listing" agreement that a commission would be paid "at time sale is consummated" may have required that the sale actually be consummated as a condition precedent to the earning of the commission. A provision for the payment of a commission "at closing" was held not to make the commission contingent upon consummation of the contract in McPherson v. Osborn, 475 S.W.2d 804, 807 (Tex. Civ. App.—Amarillo 1971, no writ). There is a growing minority view that would require consummation of the sale, according to Tristan's Landing, Inc. v. Wait, 327 N.E.2d 727 (Mass. 1975). See also Henry v. Schweitzer, 435 S.W.2d 915, 945 (Tex. Civ. App.—San Antonio 1968, writ ref'd n.r.e.); Golden v. Halliday, 339 S.W.2d 715, 717-18 (Tex. Civ. App.—Dallas 1960, writ dism'd).
199. See Armstrong v. O'Brien, 83 Tex. 635, 19 S.W. 268 (1892). See also Phillips v. Campbell, 480 S.W.2d 250, 253 (Tex. Civ. App.—Houston [14th Dist.] 1972, writ ref'd n.r.e.). A correlative rule is that the broker cannot recover a commission if, without disclosing the fact, he participates in the purchase of the property. Anderson v. Griffith, 501 S.W.2d 695 (Tex. Civ. App.—Fort Worth 1973, writ ref'd n.r.e.).
200. 540 S.W.2d 470 (Tex. Civ. App.—Houston [14th Dist.] 1976, no writ). For further discussion of this case see text accompanying notes 95-103 supra.
201. Although a real estate broker who has earned a commission may have a lien against earnest money held by him, or against funds withheld at the closing for the purpose of paying his commission, the broker has no lien against the property itself, unless (1) the contract so provides, or (2) he obtains a lien through a judgment entered against the owner of the property. Minchen v. Kimmel, 210 S.W.2d 644, 645 (Tex. Civ. App.—Galveston 1948, no writ). See generally 9 Tex. Jur. 2d Brokers § 87 (1969).
D. Miscellaneous

1. Execution Sale.

In *Collum v. DeLoughter* a sale of real property under a writ of execution on a judgment was set aside because of the inadequacy of the bid price coupled with the following irregularities in the sale which contributed to the inadequacy of price: (1) mistake in the description of the property in the published notice of sale, which would have adversely affected an ordinary person's ability to locate the property, and (2) failure of the officers to give the owner an opportunity to designate property which he desired to be levied upon first, as required by rule 637. Furthermore, the court held that the sale could also be set aside because of the inadequacy of the sale price, when, as here, the judgment debtor had made a prompt offer to make the purchaser whole by returning his investment in the property and paying all costs.

2. Promissory Estoppel.

*Southwest Water Services, Inc. v. Cope* concerned the employment of the doctrine of promissory estoppel to enjoin the developer of lake subdivision lots from raising the rate charged for water services to lot owners. Representations had been made during the sale of the lots that the rate to be charged lot owners during the time they owned their lots would be the same as that charged to residents living inside the city limits of a neighboring city. The court held that these representations had been substantially carried forward in contracts for the water services. It was thus held that this was a proper case for applying the doctrine of promissory estoppel:

Language in what has been written upon the doctrine of promissory estoppel might mislead and cause one to believe that its use must be purely defensive. Here we have stated that the plaintiffs are benefitted and are entitled to prevail thereby under the fact finding of the trial court. It is now settled that there may be appropriate use of the doctrine by a plaintiff as a ground of entitlement to relief.

III. Real Estate Financing

A. Mortgages

A commitment to make a loan secured by a mortgage on real property was held to be subject to the Statute of Frauds in *Edward Scharf Associates*,

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203. 535 S.W.2d 390 (Tex. Civ. App.—Texarkana 1976, writ ref'd n.r.e.).
204. Gross inadequacy of the bid price on an execution sale, as in a sale under a deed of trust, does not justify setting the sale aside, unless there were other irregularities in the sale, or as some cases have held, unless the debtor makes a prompt offer to reimburse the purchaser.
205. TEX. R. CIV. P. 637.
206. 535 S.W.2d at 393, citing Prudential Corp. v. Bazaman, 512 S.W.2d 85 (Tex. Civ. App.—Corpus Christi 1974, no writ); Moore v. Miller, 155 S.W. 573 (Tex. Civ. App.—San Antonio 1913, writ ref'd); and other cases. There is no correlative rule applicable to a foreclosure under a deed of trust.
207. 531 S.W.2d 873 (Tex. Civ. App.—Fort Worth 1975, writ ref'd n.r.e.).
208. Id. at 877, citing "Moore" Burger, Inc. v. Phillips Petroleum Co., 492 S.W.2d 934 (Tex. 1972); Wheeler v. White, 398 S.W.2d 93 (Tex. 1965).
209. TEX. BUS. & COMM. CODE ANN. § 26.01 (Vernon 1968).
Thus, unless the commitment is in writing it is neither enforceable nor the basis for a suit for damages for breach. In *First Savings & Loan Association v. Avila* the extent to which a mortgagee must inquire into the rights of a prior owner and present occupant of property being mortgaged was considered. The court of appeals, in reversing the trial court, held that the mortgagee was entitled to rely upon a recorded deed from the prior owner to the mortgagor in the absence of any evidence that the mortgagee actually knew that the deed to the mortgagor was only intended as a mortgage or security agreement.

2. *Mortgagee’s Duty to Insure; Right to Insurance Proceeds.*

The typical deed of trust requires the mortgagor to maintain casualty insurance on all improvements on the property, with loss payable to the mortgagee in an amount as required by the mortgagee (not to exceed the mortgage balance or insurable value), and gives the mortgagee the right to obtain the insurance if the mortgagor fails to do so. Such a provision was before the court in *Colonial Savings Association v. Taylor.* The mortgagee had agreed to obtain fire insurance coverage on property covered by a deed of trust under which it was the beneficiary. Apparently by mistake, the mortgagee obtained coverage on only one of two houses on the property, and, of course, the uninsured house burned. The owner of the property filed suit to recover the loss, on the ground that the mortgagee’s negligence in failing to insure all of the improvements had caused his loss. The insured admitted that the insurance policy, which indicated that only one house was covered, had been delivered to him, but stated that he did not examine it carefully and assumed that the mortgagee had obtained adequate insurance on his behalf. The court of civil appeals held that while the mortgagee had no obligation under the deed of trust to secure the insurance, after it undertook the duty the mortgagee was liable for its failure to exercise reasonable care to keep all

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212. The court extended to mortgages the same rule that has been applied to grantees under a deed, with regard to the notice imparted to the purchaser by the possession of the property by a prior owner. If the recorded deed is an absolute conveyance of title, absent any knowledge to the contrary, the purchaser is entitled to rely upon the recorded deed to his seller and is not required to inquire of the prior-owner-in-possession as to what rights he holds. *See Eyler v. Eyler,* 60 Tex. 315 (1883); *Graves v. Guaranty Bond State Bank,* 161 S.W.2d 118 (Tex. Civ. App.—Texarkana 1942, no writ); *Dallas Trust & Sav. Bank v. Pickett,* 59 S.W.2d 1090 (Tex. Civ. App.—Waco 1933, writ dism’d).

213. The court, however, recognized the exception to this rule made in *Anderson v. Barnwell,* 52 S.W.2d 96 (Tex. Civ. App.—Texarkana 1932), aff’d, 126 Tex. 182, 86 S.W.2d 41 (1935), where a purchaser was required to make inquiry beyond the recorded deed, because the prior owner had continued in possession for six years after the conveyance, and other evidence indicated ownership rights in the prior owner.

If a deed is intended as a mortgage, the mortgagor-grantor has an equity of redemption after the debt is paid, at least in the absence of intervening rights of innocent third parties. *See Humble Oil & Ref. Co. v. Atwood,* 150 Tex. 617, 244 S.W.2d 637 (1951); *Bradshaw v. McDonald,* 147 Tex. 455, 216 S.W.2d 972 (1949). *See generally 39* *Tex. Jur. 2d Mortgages and Trust Deeds §§ 26-33 (1976).*

improvements insured against fire loss. The Texas Supreme Court, however, reversed the appellate court, instructed the trial court to make a finding as to whether Taylor relied upon Colonial Savings' undertaking to obtain the insurance, and held that "Colonial cannot be liable for Taylor's loss unless Taylor forbore from obtaining his own insurance in reliance upon Colonial's undertaking to obtain it for him." Neither the Texas Supreme Court nor the appellate court discussed whether this award, which in effect was a substitute for insurance proceeds, would constitute insurance proceeds payable to the mortgagee under the loss payable clause of the deed of trust. Presumably, under such a clause, which is common in deeds of trust, the mortgagee could require the owner to apply this award to the restoration of the improvements and the mortgagee's security.

Who is entitled to insurance proceeds paid after the mortgagor has used its own funds to repair the damage to the improvements on which the insurance is payable? The answer is the mortgagee, at least under the deed of trust provision before the court in Zidell v. John Hancock Mutual Life Ins. Co.
The deed of trust required the mortgagor to keep the improvements in good repair, to replace any improvements which were lost or destroyed, and to

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215. The following authorities were cited by the court of civil appeals for the principle that one who gratuitously undertakes to render a service to another, which is necessary for the other person's protection, is subject to liability for his failure to exercise reasonable care in the performance of the task: Fox v. Dallas Hotel Co., 111 Tex. 461, 240 S.W. 517 (1922); Reeves County Gas Co. v. Church, 464 S.W.2d 489 (Tex. Civ. App.—El Paso 1971, no writ); 2 Restatement (Second) of Torts § 323 (1965). See also 59 C.J.S. Mortgages § 328b, at 449-50 (1949). The result reached by the court of civil appeals in Taylor is logical, but it would seem more appropriate to base it upon negligence under a principal-agent relationship rather than under a mortgagee-mortgagor relationship, since the procurement of insurance by the mortgagee under the deed of trust would have arisen upon the failure of the mortgagor to obtain the insurance. See, e.g., Barile v. Wright, 256 N.Y. 1, 175 N.E. 351 (1931), where the mortgagee was found to be acting as the owner's agent in failing to obtain valid insurance after undertaking to do so (when owner notified it she was financially unable at that time to obtain the insurance).

The Texas Supreme Court in Colonial Savings agreed that Colonial Savings' duty to Taylor did not arise under the deed of trust, but on the basis that Taylor did not assume the deed of trust and, therefore, was not a party to the deed of trust. Mr. Taylor had acquired the property subject to the deed of trust lien, and simply followed the practice of the former owner in having the lender obtain the insurance and then submitting the bill to the owner for payment. First Nat'l Bank v. Dowdell, 275 Ala. 622, 157 So. 2d 221 (1963), is a case much like Taylor, in which the mortgagee agreed from the inception to procure the insurance required under the mortgage (recovery to mortgagee based upon fraud by mortgagee's failing to procure the insurance). But see Hampton v. Gulf Fed. Sav. & Loan Ass'n, 287 Ala. 172, 249 So. 2d 829 (1971), noted in 59 C.J.S. Mortgages § 328d (1949). In Barile v. Wright, 256 N.Y. 1, 175 N.E. 351 (1931), where the mortgagee was held not to be liable for failing to renew fire insurance coverage, although payments for the premiums had been paid into escrow by the mortgagor.

216. 544 S.W.2d at 119. The court stated that the presumption that an insured knows the contents of an insurance policy can be overcome by proof to the contrary, such as proof he put it away without examining it, citing Fireman's Fund Indem. Co. v. Boyle Gen. Tire Co., 392 S.W.2d 352 (Tex. 1965) (a suit brought by an insured for reformation of a fidelity bond). It was then the mortgagee's burden, the court held, to prove Taylor was negligent in failing to examine the policy, which it had failed to do.

217. See generally 59 C.J.S. Mortgages § 328d (1949). In Barile v. Wright, 256 N.Y. 1, 175 N.E. 351, 352 (1931), the court said that the mortgagee was required to credit the note balance or deliver the appropriate amount for insurance proceeds to the mortgagee to restore the property. The court of civil appeal further held that if the insurance policy had covered the other house (which it did not), the policy would have limited the owner's recovery to the relative value of the garage apartment, and, therefore, he could not recover an amount from the mortgagee that was greater than he could have recovered under the policy had the improvements been insured.

218. See, for example, the clause recited in Zidell v. John Hancock Mut. Life Ins. Co., 539 S.W.2d 162, 163 n.1 (Tex. Civ. App.—Dallas 1976, no writ), which is the next case discussed in this Survey.

The deed of trust further provided that all insurance policies were for the mortgagee’s benefit, and that all insurance proceeds were assigned to the mortgagee, who then had the option of applying those proceeds to the indebtedness or to the restoration of the property. The mortgagor had made the repairs caused by the loss out of his own funds, but by the time the insurance company made payment on the loss the mortgagee had foreclosed against the property on account of subsequent failures to make installments on the secured indebtedness. The mortgagor, for obvious reasons, chose to apply those proceeds to the deficiency remaining on the debt after the foreclosure sale. The mortgagor claimed that he was entitled to the insurance proceeds because he had used his own funds to repair the damage, and because the mortgagee had failed to exercise formally its option to apply the insurance proceeds to the indebtedness. The court of civil appeals, however, affirmed the trial court’s holding and held that the assignment of the insurance proceeds to the mortgagee under the deed of trust was absolute, and that the mortgagee was entitled to use those proceeds in any manner authorized under the deed of trust. The court, in so holding, refused to follow Huey v. Ewell. Faced with such a deed of trust provision, a mortgagor, before investing his own funds in repairs, should seek to obtain approval of the use of the insurance proceeds for this purpose, and notify the insurer of the decision in order to avoid the result in Zidell.

3. Other Indebtedness and Other Security.

In Airline Commercial Bank v. Commercial Credit Corp. the mortgagee was allowed to retain an amount of the proceeds of the foreclosure sale sufficient to pay reasonable attorney’s fees and the contractually stipulated five percent trustee’s fee, but the court refused to allow the mortgagee to deduct the amount owed on an indebtedness other than the one described in the deed of trust. The deed of trust contained a “dragnet” or “other indebtedness” clause providing that the lien also applied to existing and

220. The mortgagee was not, the court said, required to make its election immediately or lose its election to the mortgagor. Id. at 164. The court also noted that the plaintiff had made no argument that the lender was estopped or otherwise precluded from making its choice. Id. at 164. The court found there to be no inequity in allowing the mortgagee to apply the insurance proceeds to the indebtedness after the mortgagor had used his own funds to make the repairs, for the reduction of the amount of the indebtedness (and in this case the amount of the deficiency) benefited the mortgagor.

221. 55 S.W. 606 (Tex. Civ. App.—Dallas 1900, no writ) (holding that the mortgagees were not entitled to the insurance money).

222. 531 S.W.2d 171 (Tex. Civ. App.—Houston [14th Dist.] 1975, writ ref’d n.r.e.).

223. If the deed of trust so provides, Texas law allows retention of attorney’s fees out of the proceeds of a trustee’s sale if it is shown that ‘the amount was reasonable and that the services of the attorney were necessary to enable the trustee to properly execute the power, and that he actually rendered services to the company in the matter.’ 531 S.W.2d 171, citing American Nat’l Ins. Co. v. Schenck, 85 S.W.2d 833, 839 (Tex. Civ. App.—Amarillo 1935, no writ), but rejecting the inference in Schenck that the recovery of attorney’s fees is limited to judicial foreclosures. Attorney’s fees are not recoverable under a deed of trust unless there is a specific provision in the instrument. Jolly v. Fidelity Union Trust Co., 15 S.W.2d 68 (Tex. Civ. App.—Fort Worth 1929, writ ref’d).

224. The United States, one of the parties to the suit, unsuccessfully argued that the trustee’s fee could not be recovered because there was no evidence that the fee was actually incurred. 531 S.W.2d at 176.
future indebtedness not described in the deed of trust. The court, however, held that the other indebtedness, consisting of a renewal note signed by a partnership (only guaranteed by the same debtors) and originally executed before the deed of trust, was not "reasonably within the contemplation of the parties to the mortgage at the time it was made." 

Does a deed of trust provision which, upon the occurrence of default, assigns "all rents, profits and income from the property covered by this deed of trust" extend to accounts receivable of a business operated on the property? The Bankruptcy Court held that it did in *In Re: Space Center Memorial Hospital Foundation, Bankrupt.* A clause such as the one involved in this case is very common to deeds of trust and, undoubtedly, many would expect it to cover tenant rentals, revenues from oil and gas leases and operations, and similar income produced by the property, but not income generated by a commercial business located on the property. Surely the court's opinion would not extend to income from a business operated on the property by a tenant, other than the mortgagor, whose lease is subject to such a deed of trust. The court further held that the mortgagee was required to file a financing statement under the Uniform Commercial Code in order to establish its priority as to profits and income, and since it did not, its lien

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225. *Id.* at 175, citing and quoting from *Moss v. Hipp*, 387 S.W.2d 656 (Tex. 1965). See also *Vaughn v. Crown Plumbing & Sewer Serv., Inc.*, 523 S.W.2d 72, 76 (Tex. Civ. App.—Houston [1st Dist.] 1975, writ ref'd n.r.e.); *Finger Furniture Co. v. Chase Manhattan Bank*, 413 S.W.2d 131 (Tex. Civ. App.—San Antonio 1967, writ ref'd n.r.e.). The danger of a dragnet clause to an unsuspecting purchaser of property subject to a deed of trust is well illustrated in *Estes v. Republic Nat'l Bank*, 462 S.W.2d 273 (Tex. 1970), and its impact on a materialman is demonstrated in *Justice Mortgage Investors v. C.B. Thompson Constr. Co.*, 533 S.W.2d 939 (Tex. Civ. App.—Amarillo 1976, writ ref'd n.r.e.), discussed in notes 325-40 infra and accompanying text. The mortgagor's attorney should attempt to have such a clause deleted, and the mortgagee's attorney should list any existing indebtedness which is not already described and which his client expects to be covered by the deed of trust, as well as the identity of persons other than the mortgagors whose debts are to be covered. Actually, in *Airline Commerce Bank* the court could have found that the dragnet clause did not extend to the other indebtedness of a different person.

226. *Technology Inc. v. Space Center Memorial Hosp. Foundation, Bk. No. 74-HP-808* (S.D. Tex., Nov. 16, 1976), is a severed portion of the adversary proceeding filed in this bankruptcy proceeding. The court said: "The Court has concluded that the contract assignment of rents, profits and income is broad enough to cover accounts receivable regardless of the source of the money." Although this opinion was issued after the end of this survey period, it is included in this Survey because of its significance and because of the obscurity often enjoyed by bankruptcy court decisions. By way of fair disclosure, the authors' firm represents the plaintiff in the adversary proceeding, although the deed of trust involved in the proceeding is held by the Federal Housing Administration.

227. See, e.g., *Detroit Trust Co. v. Detroit City Serv. Co.*, 262 Mich. 14, 23, 247 N.W. 76, 85 (1933), where the court said: "Under the common law, the word 'profits,' when used in connection with rents, meant the usufruct of the land." The Michigan Supreme Court then interpreted its statute which authorized the assignment of rents and profits under a mortgage as follows: "We do not believe that the word 'profits' as used in Act No. 228, supra, means business profits arising out of the operation of mortgaged premises not rented to others but occupied and used by the mortgagor," and, thus, the court reversed the lower court's holding that the mortgagee was entitled to profits made by the receiver through operation of the mortgaged premises and business (mortgage allowed mortgagee's trustee to collect "rents, income, issues and profits" of the mortgaged property after default). See also 31 Mich. L. Rev. 1124, 1129 (1935).

228. A tenant's lease is subject to an existing mortgage, unless the mortgage otherwise provides or the mortgagee later subordinates to the lease. See 1 M. FRIEDMAN, LEASES § 8.1 (1974); 36 Tex. Jur. 2d Landlord & Tenant § 262 (1962); discussion in note 419 infra.

229. *Tex. Bus. & Com. Code* Ann. art 9.104(10) (Vernon Supp. 1976-77), exempts from the coverage of that article "the creation or transfer of an interest in or lien on real estate, including a lease or rents thereunder." Thus, an assignment of leases and rents is enforceable without filing under the Uniform Commercial Code. *In re Bristol Assocs. v. Girard Trust Bank*, 505 F.2d 1056
with respect to the accounts receivable was not perfected until it took possession as mortgagee in possession under the deed of trust. The court held that the mortgagee is entitled to accounts receivable which accrue, are made, and are generated after the mortgagee takes possession.

4. Due on Sale Clause.

A "due on sale" clause generally gives the noteholder an option either to accelerate the maturity of the note if the property covered by the deed of trust is sold, or to deal with the new purchaser without releasing the original maker of the note. In Ashley v. Leitch the maker of the note unsuccessfully

(3d Cir. 1974). The court, however, in Space Center Memorial Hospital Foundation, held that "profits and income" is not exempt from the Uniform Commercial Code filing requirements, citing United States v. PS Hotel Corp., 404 F. Supp. 1188, 1192 (E.D. Mo.), aff'd, 527 F.2d 500 (8th Cir. 1975).

The mortgagee took possession prior to the filing of the bankruptcy proceeding, and, with the consent of the court, foreclosed against the property afterwards. The court cited as authority for the right of a mortgagee-in-possession to rents, profits, and income: Groves v. Fresno Guarantee Sav. and Loan Ass'n, 373 F.2d 440 (9th Cir. 1967); Central States Life Ins. Co. v. Carlson, 98 F.2d 102 (10th Cir. 1938); Simon v. State Mut. Life Assurance Co., 126 S.W.2d 682 (Tex. Civ. App.—Dallas 1939, writ ref'd). See generally G. OSBORNE. MORTGAGES § 150 (1970); 59 C.J.S. Mortgages §§ 316-321 (1949).

The court states in the opinion that the mortgagee "became entitled only to rents, profits and income which accrued thereafter, i.e., monies for services, charges, etc. which were from that date forward made by the hospital," citing F. Groos & Co. v. Chittim, 100 S.W. 1006 (Tex. Civ. App.—San Antonio 1907, no writ), and 59 C.J.S. Mortgages § 317 (1949). In F. Groos & Co., supra, the court discussed the relative rights between the mortgagor and mortgagee to receive rents from leases on the property under a deed of trust which specifically assigned rents from leases to the mortgagee. The court said that the one who has the right of possession "at the time the rents fall due" is entitled to the rents, and then continues by saying: "And a general rule is that an apportionment of rents is never made under the common law in reference to the length of time of occupation; but whoever owns the reversion at the time the rent falls due is entitled to the entire sum due at that time." 100 S.W. at 1010. The following comment appears in 59 C.J.S. Mortgages § 317, at 426 (1949): "Ordinarily when the mortgagee takes possession or otherwise asserts his right to the rents he is not entitled to claim rents accrued prior thereto but unpaid, but it has been held that rents due but unpaid at the time of default may be included in an assignment of rents." The deed of trust being interpreted in Space Center Memorial Hospital Foundation is FHA Form No. 4181-B, which simply provides:

That all rents, profits and income from the property covered by this Deed of Trust are hereby assigned to the holder of the Note for the purpose of discharging the debt hereby secured. Permission is hereby given to Grantor, so long as no default exists hereunder, to collect such rents, profits and income for use in accordance with the provisions of the Regulatory Agreement.

Whether the deed of trust entitles the mortgagee to rents, profits, and income collected after it takes possession, or only those which accrue or are attributable to operations after possession will depend upon an interpretation of the particular deed of trust provision. It probably does not matter, practically speaking, if the deed of trust also commits the mortgagor to use all rents to pay the mortgage; in such a case it would seem that the mortgagee who collects rentals attributable to pre-possession periods could apply those rentals to the indebtedness. Most comprehensive assignments of rental agreements (usually an agreement separate and in addition to the deed of trust) provide how rents or income collected from the property, whether accruing before or after possession, by the mortgagee will be applied.

A provision prohibiting sale without the mortgagee's consent may be an invalid restraint on alienation; but a provision that the mortgagee may accelerate the mortgage in the event the property is sold without its consent probably is valid. Malouff v. Midland Fed. Sav. & Loan Ass'n, 509 P.2d 1240, 1244 (Colo. 1973); Gunther v. White, 489 S.W.2d 529 (Tenn. 1973); Mutual Fed. Sav. & Loan Ass'n v. Wisconsin Wire Works, 58 Wis. 2d 99, 205 N.W.2d 762 (1973); Conopore A. B. Clark Inv. Co. v. Green, 375 S.W.2d 425 (Tex. 1964), and Sanders v. Hicks, 317 So. 2d 61 (Miss. 1975), with Mutual Fed. Sav. & Loan Ass'n v. American Medical Serv., Inc., 66 Wis. 2d 210, 223 N.W.2d 921 (1974) (invocation of due on sale clause is governed by equitable principles, primarily whether sale impairs mortgagee's security—here it did not). Contra, Tucker v. Pulaski Fed. Sav. & Loan Ass'n, 252 Ark. 849, 481 S.W.2d 725 (1972). See also Tucker v. Lassen Sav. & Loan Ass'n, 12 Cal. 3d 629, 526 P.2d 1169, 116 Cal. Rptr. 633 (1974) (foreclosure denied on basis of sale under contract for deed did not impair the first lien). See generally Goldberg, What to Do About Mortgages in the Sale of Real Property, 17 PRAC. LAW., Nov. 1971,
challenged the noteholder’s right to accelerate after a sale of the property. The court rejected the maker’s argument that the clause applied only in the event of a sale to a purchaser who assumed the payment of the note.

5. Presumptions in Trustee’s Deed.

Deeds of trust generally provide that in the event of a foreclosure sale, the recitals contained in the trustee’s deed are conclusive evidence that those recitals are true and that all prerequisites to a valid sale have been performed.234 The weight such a provision carries in a motion for summary judgment is demonstrated in Pachter v. Woodman.235 The owner of the property, who acquired it subject to the mortgage, contended that the foreclosure sale was void because the notices of sale had not been posted for three weeks, as required by statute,236 and because the mortgagee’s attorney had promised to notify him if the foreclosure sale was going forward. The court of civil appeals held that the affidavit of the mortgagor’s attorney which stated that he did not see any foreclosure notice posted at the time he posted another notice, and failed to state that the mortgagee’s attorney had not notified him of the sale, was insufficient to overcome the presumption of regularity that attached to the trustee’s deed. The court also held that the plaintiff failed to prove fraud237 on the part of the mortgagee’s attorney or to show there was a genuine issue of fact with respect to the allegation of fraud. The court then observed that the plaintiff was seeking to set aside the trustee’s sale to bona fide purchasers without offering to place the purchasers in status quo, as he is required to do.238 Writ of error has been granted by the Texas Supreme Court.


233. 533 S.W.2d 831 (Tex. Civ. App.-Eastland 1975, writ ref’d n.r.e.). The provision in the promissory note stated: "[I]n the event of sale or transfer of the herein described property, the payee reserves the right to approve the purchaser, or of declaring this note due and payable in full." 234. This provision is valid, although it will not be inferred in the absence of such a provision. See Koehler v. Pioneer Am. Ins. Co., 425 S.W.2d 889, 892 (Tex. Civ. App.—Fort Worth 1968, no writ).


236. TEX. REV. CIV. STAT. ANN. art. 3810 (Vernon 1966).

237. The elements of fraud that would have to be proved, the court stated, were the following: [T]hat Woodman’s [mortgagee’s attorney] alleged promise not to proceed with the foreclosure sale was false in that Woodman failed to notify him; that the promise was made for the purpose of keeping appellant from attending the sale; that appellant relied thereon and had no actual knowledge of the sale; that had Woodman notified him that he intended to proceed with the foreclosure sale, he would have been in a position to have protected his interest in the land by payment of the amount due upon Woodman’s vendor’s lien note and that he was damaged thereby.

534 S.W.2d at 945.

[Editor’s Note: Since this Article was written the Texas Supreme Court has recently reversed this decision and held that the affidavit of the mortgagee’s attorney presented questions of fact as to whether notice of the foreclosure sale was posted at the specified locations and whether the mortgagee’s attorney notified the mortgagee’s attorney of the sale. 20 Tex. Sup. Ct. J. 186 (Feb. 19, 1977).]

238. The court cited two Texas cases as authority for this holding: Price v. Reeves, 91 S.W.2d 862 (Tex. Civ. App.—Fort Worth 1936, writ dism’d); Chase v. First Nat’l Bank, 20 S.W. 1027 (Tex. Civ. App. 1892, no writ). See also Jasper State Bank v. Braswell, 130 Tex. 549, 554, 111 S.W.2d 1079, 1084 (1938), where the court said:

The Texas decisions extend equitable rights to third persons, as well as to mortgagees, who purchase at void foreclosure proceedings, by treating the
6. **Wrongful Foreclosure Under Deed of Trust.**

In *First Southern Properties, Inc. v. Vallone*\(^{239}\) the receiver appointed by a domestic relations court filed suit to set aside a conveyance under a trustee’s deed, alleging, among other irregularities, that the sale was void because the property was *in custodia legis* at the time of the foreclosure sale. The Texas Supreme Court held that the purchaser at the foreclosure sale, First Southern Properties, Inc., could only obtain the title the trustee had authority to convey.\(^{240}\) Since the trustee had no authority to sell the property while it was held by the receiver *in custodia legis* without the court’s authorization, the sale was invalid.\(^{241}\) The failure of the receiver to file a notice of lis pendens did not, in the court’s opinion, estop the receiver in this action, for there is nothing for a receiver to file under Article 6640.\(^{242}\) The court, however, invited the legislature to consider legislation requiring receivers to file a notice of the receivership proceedings in the deed records or lis pendens records. The purchaser at the foreclosure sale was held by the court to be entitled to recover its purchase money.

In *Owens v. Grimes*\(^{243}\) the mortgagors filed suit to set aside a non-judicial foreclosure sale and, in the alternative, sought damages for wrongful foreclosure. The basis for the mortgagee’s foreclosure was the mortgagors’ breach of covenants in the deed of trust not to remove improvements and not to allow a lien of any kind to be placed against the property.\(^{244}\) The trial court, however, found that the mortgagee had consented both to the removal of the improvements (which were replaced with new improvements) and to the creation of mortgage as still in effect and subrogating the purchaser to the rights of the mortgagee to the extent of the purchase money paid at the foreclosure sale. See also Loomis Land & Cattle Co. v. Diversified Mortgage Investors, 533 S.W.2d 420, 424 (Tex. Civ. App.—Tyler 1976, writ ref’d n.r.e.), *discussed in notes* 256-62 infra and accompanying text. See generally 39 *Tex. Jur. 2d Mortgages and Trust Deeds* § 196, at 257 (1976). [Editor’s Note: Since this Article was written the Texas Supreme Court has recently reversed this decision and held that the affidavit of the mortgagee’s attorney presented questions of fact as to whether notice of the foreclosure sale was posted at the specified locations and whether the mortgagee’s attorney notified the mortgagee of the sale. 20 Tex. Sup. Ct. J. 186 (Feb. 19, 1977).] 239. 533 S.W.2d 339 (Tex. 1976).

240. *Id.* at 341, *citing* Slaughter v. Qualls, 139 Tex. 340, 162 S.W.2d 671 (1942), and other Texas authority.


244. These are two common deed of trust covenants, except that the covenant against other liens generally is limited to a lien equal to or superior than the deed of trust lien, such as a statutory lien for nonpayment of property taxes. A covenant against permitting any lien against the property, even an inferior lien, may, however, be useful, especially on income property, where the first lienholder is concerned that further indebtedness against the property may impair the mortgagor’s ability to pay the first lien indebtedness.
the second lien. The court found that the foreclosure sale was conducted for the purpose of defrauding the mortgagors of their money and property and awarded the mortgagors $29,600.00 in damages for the wrongful foreclosure.\textsuperscript{245} The court further held that since the mortgagors had abandoned their action to set aside the foreclosure sale, the trustee’s deed vested title in the purchaser at the sale and the mortgagors could not later attack the trustee’s deed.\textsuperscript{246}

B. Usury

Article 1302-2.09\textsuperscript{247} provides an exception to the maximum lawful rate of interest of ten percent,\textsuperscript{248} and allows corporations to agree to pay interest not to exceed one and one-half percent per month on any bond, note, debt, contract, or other obligation exceeding $5,000. The article also prohibits “the claim or defense of usury by such corporation, its successors, guarantors, assigns or anyone on its behalf . . . .”

It has become a rather common practice for individual borrowers during periods when loans to many borrowers are available only at rates of interest in excess of ten percent a year to obtain loans through a corporate nominee. The corporate nominee may have no assets beyond those which are security for the loan and, thus, the lender requires the principal stockholders or other persons with more extensive assets to guarantee the loan. While the decision in \textit{Collins v. United States}\textsuperscript{249} makes the use of a corporate nominee unattractive from a tax standpoint by recognizing nominee corporations as taxable entities and thereby precluding guarantors from deducting loan charges paid through the nominee corporation, the practical necessity of using the corporate vehicle nevertheless remains.

Most lawyers began the survey period thinking that the rules were fairly well established under article 1302-2.09, but on March 10, 1976, this confidence was shattered by the Texas Supreme Court’s first opinion in \textit{Universal Metals & Machinery, Inc. v. Bohart}.\textsuperscript{250} In \textit{Bohart} the court first held that the guarantors, who signed the instrument as “primary obligor(s),” and who “jointly and severally unconditionally” guaranteed the prompt payment of the promissory note, were co-makers, and because the note executed by the

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\item \textsuperscript{245} As authority for the award of damages, the court cited: \textit{League City State Bank v. Mares}, 427 S.W.2d 336 (Tex. Civ. App.—Houston [14th Dist.] 1968, writ ref’d n.r.e.); \textit{John Hancock Mut. Life Ins. Co. v. Howard}, 85 S.W.2d 986 (Tex. Civ. App.—Waco 1935, writ ref’d), and other cases.
\item \textsuperscript{246} 539 S.W.2d at 390, citing \textit{Peterson v. Kansas City Life Ins. Co.}, 339 Mo. 700, 705, 98 S.W.2d 770, 775 (1936). The court went even further, on the authority of \textit{Estelle v. Hart}, 55 S.W.2d 510 (Tex. Comm’n App. 1932, jdgmt adopted), to state that only the mortgagor or his privities can challenge the regularity of a foreclosure sale, insofar as the divesting of the mortgagor’s title and investing of title in the purchaser are concerned. This could mean that a guarantor who is not given notice of the sale under TEX. REV. CIV. STAT. ANN. art. 3810 (Vernon Supp. 1976-77), or a materialmen’s lien claimant, if they are not in privity with the mortgagor, could challenge an invalid foreclosure sale only to the extent that, as to the guarantor, the invalid sale discharged him, and, as to the materialman, that the purchaser took subject to his lien.
\item \textsuperscript{247} \textit{Id.} art. 1302-2.09 (Vernon Supp. 1977-78).
\item \textsuperscript{248} Id. art. 5069-1.04 (Vernon 1971).
\item \textsuperscript{249} 514 F.2d 1282 (5th Cir. 1975).
\item \textsuperscript{250} 19 Tex. Sup. Ct. J. 212 (March 10, 1976). Upon rehearing the court reversed itself. The second \textit{Bohart} opinion is in 539 S.W.2d 874 (Tex. 1976).
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corporation provided for interest at a rate in excess of ten percent a year.251 were entitled to the defense of usury. The factual setting in Bohart, however, was unique. Unknown to the plaintiff, the signature of the president of the corporation on the $225,000 note had been forged. Unable to recover against the maker of the note, the plaintiff elected to sue only the guarantors, who, as primary obligors, could not escape liability because of the forgery.252

The Texas Supreme Court was deluged with amicus curiae briefs from lenders’ counsel across the state, who had more than a passing interest in the outcome.253 On motion for rehearing the supreme court withdrew its first opinion, and held that the term “guarantors” as used in article 1302-2.09 includes payment guarantors such as the Boharts, and, accordingly, that the Boharts were prohibited by that statute from using the claim or defense of usury.254 The court’s second opinion was followed in Hartnett v. Adams & Holmes Mortgage Co.,255 a case involving a mortgage, and the second Bohart opinion was anticipated in several decisions reached before the first Bohart opinion was rendered.

Loomis Land & Cattle Co. v. Diversified Mortgage Investors256 represents another unsuccessful attempt by a corporate borrower to prove that a loan made in its name with a rate of interest in excess of ten percent was actually made to an individual and, therefore, usurious.257 The evidence showed that the corporation was not a sham, had been doing business for almost two years, had a large net worth, and that the money was borrowed to allow the corporation to continue to operate and to expand the operation of the shopping center owned by it. The court concluded as follows:

While the corporate entity may in some instances be disregarded where it is utilized as a cloak for fraud or illegality, such is not the situation here. There is no summary judgment proof suggesting fraud or illegality. The mere fact that Diversified refused to make the loan to Loomis Company unless Richard F. Loomis, Jr., agreed to act as guarantor does not render the loan transaction void or illegal. As we view the record the loan was made to Loomis Company and not to Richard F. Loomis, individually.258

251. The court, in its first opinion, divided guarantors into two groups—they either were “payment” guarantors or “collection” guarantors. TEX. BUS. & COMM. CODE ANN. § 3.416 (Vernon 1968). If they were payment guarantors (i.e., the holder of the note was not required first to pursue the maker), as are most guarantors in modern loan guarantees, then the court had said they could assert the defense of usury if the rate of interest on the note exceeded the lawful rate that could be charged to the guarantor.

252. 539 S.W.2d at 877-78, citing Ganado Land Co. v. Smith, 290 S.W. 920 (Tex. Civ. App.—Galveston 1927, writ ref’d); El Paso Bank & Trust Co. v. First State Bank, 202 S.W. 522 (Tex. Civ. App.—El Paso 1918, no writ), and other cases in the second Bohart opinion.

253. Although their efforts were rewarded in the court’s second opinion, many of these lawyers had scurried to change their guaranty forms, and the authors understand that some of these changes remain intact even after the court’s second opinion.

254. 539 S.W.2d at 879.

255. 539 S.W.2d 181 (Tex. Civ. App.—Texarkana 1976, no writ). The court’s first opinion, rendered on May 4, 1976, followed the first Bohart opinion and allowed the guarantor’s estate to recover usury penalties, but that opinion was withdrawn after the second opinion was rendered in Bohart.

256. 533 S.W.2d 420 (Tex. Civ. App.—Tyler 1976, writ ref’d n.r.e.). See also American Century Mortgage Investors v. Regional Centers, Ltd., 529 S.W.2d 578 (Tex. Civ. App.—Dallas 1975, writ ref’d n.r.e.); Sween v. Glenn Justice Mortgage Co., 526 S.W.2d 252 (Tex. Civ. App.—Dallas 1975, no writ). Both of these cases are ably discussed in Wallenstein & St. Claire (1976), supra note 2, at 46-47.

257. See also Moss v. Metropolitan Nat’l Bank, 533 S.W.2d 397, 399.
The corporate borrower next argued that the loan was usurious as to the individual guarantor because the interest rate on the loan was in excess of ten percent a year. The court correctly anticipated the second opinion in Bohart,259 and held that article 1302-2.09260 precluded the defense of usury to a guarantor of a loan to a corporation at an interest rate not in excess of one and one-half percent a month. The borrower further challenged the standing of the lender, a Massachusetts Business Trust, to maintain a suit on the loan in a Texas court. The court, however, found that the borrower had standing to sue as a joint stock company under article 6133.261 The court stated further that the exculpatory language in the loan agreement protected the individual shareholders from liability under article 6137.262

In Micrea, Inc. v. Eureka Insurance Co.,263 a suit for a deficiency following a foreclosure under the deed of trust, the individual guarantor of a loan made to a corporation also failed to convince the court that the loan was, in fact, made to him and, therefore, usurious. The court stated that "[n]othing in the evidence proves anything fraudulent by the company’s loan of the money, or that it was in fact a loan to Adler [the guarantor] with the language of the contract(s) actually fictional in statements that the loan was to Micrea [corporate borrower]."264 The court noted that there was no contention that the corporation was the alter ego of the guarantor or that the guarantor

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261. Id. art. 6133 (Vernon 1970).
262. Id. art. 6137 provides as follows:
   In a suit against such company or association, in addition to service on the president, secretary, treasurer or general agent of such companies or association, service of citation may also be had on any and all of the stockholders or members of such companies or associations; and, in the event judgment shall be against such unincorporated company or association, it shall be equally binding upon the individual property of the stockholders or members so served, and executions may issue against the property of the individual stockholders or members, as well as against the joint property; but executions shall not issue against the individual property of the stockholders or members until execution against the joint property has been returned without satisfaction.

263. 534 S.W.2d 348 (Tex. Civ. App.—Fort Worth 1976, writ ref'd n.r.e.).
264. Id. at 354.
otherwise was in privity with the corporation, and concluded as follows: "Rights of redress provided thereby [Texas usury statutes] are therefore to be restricted to those who are original parties to the usurious contract." The mortgagee was again met with the defense of usury and counterclaims for penalty interest when suit was filed against the maker and guarantor of the note in Commerce Savings Association v. GGE Management Co. Gertner, individually and as president of GGE Management Co., executed in 1970 a $600,000 promissory note which provided for interest at twelve percent a year. The lender agreed that Gertner's liability would be limited to such loss as the lender might realize with respect to a stated percentage of the unpaid balance of the note at the time of foreclosure. The loan was obtained for the purpose of providing financing in connection with an apartment project owned by Merrill. Merrill conveyed the project for $349,000 to the lender which then conveyed it to GGE for $400,000, resulting in a $51,000 profit to the lender. The payment of the $600,000 note was secured by a deed of trust covering the project, and was guaranteed by Merrill and another man. In 1972 Gertner and GGE executed an agreement to modify and extend the $600,000 note, which reduced the principal balance to $539,226.28, reduced the interest rate to eight and one-half percent a year, and extended the maturity date. In 1974 the lender filed suit on the note against the guarantors to foreclose the deed of trust lien. The court of civil appeals held as follows: (1) since Gertner's liability on the note was limited to a certain amount of the unpaid principal balance, it was not usurious as to him; (2) the $51,000 profit

265. *Id.* The guarantor and his wife owned all the stock of the corporation, and he was its president. It is not clear what the court had in mind with the reference to the assertion of usury by one in "privity" with the borrower. The court cites 91 C.J.S. *Usury* §§ 71, 132, 151, 153 (1955), which state generally that guarantors and those otherwise in privity with the borrower may assert the defense or raise a claim of usury. However, in Texas it is clear that when an individual guarantees a corporate debt TEX. REV. CIV. STAT. ANN. art. 1302-2.09 (Vernon 1956) is controlling. *Universal Metals & Mach., Inc. v. Bohart*, 539 S.W.2d 874 (Tex. 1976).

266. 534 S.W.2d at 354. The loan was not usurious as to the corporation. *See* TEX. REV. CIV. STAT. ANN. art. 1302-2.09 (Vernon 1956). This statement by the court is broader than necessary since art. 1302-2.09 ultimately controls the result.


268. *Id.* at 77. The court's reasoning on this point is not clear, but the opinion seems to indicate that the court was agreeing with the lender's argument that, although Gertner was a co-maker of the note, since his liability on the note was limited, he was only a guarantor. The court may have avoided making this distinction, because under the first *Bohart* opinion it would not have mattered that Gertner was a guarantor. On the other hand, is the court saying that since Gertner was only required to pay principal under the letter agreement, he was not liable for any interest, usurious or otherwise? However, the principal balance could have included accrued interest. *See* Bothwell v. Farmers' & Merchants' State Bank & Trust Co., 120 Tex. 1, 3, 30 S.W.2d 289, 291 (1930). The court's opinion does not state the percentage of the loan balance for which Gertner was liable, but it may have been that his percentage, if applied separately to the interest, would have reduced the rate of interest below 10% a year. Would this point really...
realized by the lender on the resale of the property to GGE was interest, but when this additional interest was spread over the effective term of the loan it was not usurious; (3) the restoration of the $51,000 to GGE under the agreement modifying and extending the loan did not remove any taint of usury; (4) brokerage fees paid to third parties for the purchase of brokered certificates of deposit did not constitute additional loan charges; (5) the guarantors were not released because the modification agreement was executed without their consent; and (6) the mortgagee was entitled to forclose

matter? Gertner was responsible, as a maker, for the payment of all principal and all interest on the note in order to avoid a default, and his limited liability arose only after default. Tex. Rev. Civ. Stat. Ann. art. 5069-1.04 (Vernon 1967) subjects to penalty any contract "which may in any way, directly or indirectly" provide for an excessive rate of interest, and art. 5069-1.06 speaks of "any person who contracts for, charges or receives" excessive interest. See, e.g., Moore v. Sabine Nat'l Bank, 527 S.W.2d 209 (Tex. Civ. App.-Austin 1975, writ ref'd n.r.e.); Wallenstein & St. Claire (1976), supra note 2, at 48. The court cites Crow v. Home Sav. Ass'n, 522 S.W.2d 457 (Tex. 1975), as authority for this holding, but it is difficult to see the application of Crow to this case, unless it is for the purpose of comparing Gertner's lack of involvement with that of Home Savings Association.

269. 539 S.W.2d at 79. The court stated that it was for the jury to determine whether the $51,000 was a bona fide real estate profit or an additional charge for the loan of money. The jury found that this sum was interest and that the transaction was a disguise to evade the usury statute.

270. Id. at 81, where the court held:

Since the loan was prematurely terminated by the borrowers' default and since the loan documents do not, on their face, evidence a usurious contract it is our opinion that in making this determination, we should consider the loan charges actually charged or received by Commerce during the period of time the loan remained in effect.

The court in its first opinion had disallowed spreading, but on this third motion for rehearing decided that the savings provision in the deed of trust should be applied to the $51,000 of interest and that this interest should be apportioned over the period beginning on the date it was paid and ending on the date it was "restored" under the modification agreement. Id. at 82. The court treated the $51,000 as a discount and, following Nevels v. Harris, 129 Tex. 190, 102 S.W.2d 1046 (1937), deducted it from the face amount of the note.

The court acknowledged that Tex. Rev. Civ. Stat. Ann. art. 1302-2.09 (Vernon 1967) may require that each month be considered as a separate time interval for the purpose of determining if interest in excess of one-and-one-half percent a month was charged, but refused to apply such a standard under these circumstances, where the lawful rate was not exceeded by the aggregate interest charges over the effective period of the loan. The court in reaching its decision may have been influenced by the fact that Tex. Rev. Civ. Stat. Ann. art. 5069-1.07 (Vernon Supp. 1976-77) was amended, effective Sept. 1, 1976, to allow spreading, but the court acknowledged that since that amendment was prospective it did not apply to this loan. For a discussion of spreading see Comment, Usury in Texas: Spreading Interest over the Entire Period of the Loan, 12 Hous. L. Rev. 159 (1974); Comment, Usury Implications of Front-End Interest and Interest in Advance, 29 Sw. L.J. 748 (1975).

271. 539 S.W.2d at 79. The jury found that Gertner and GGE did not intend to release any claim for usury by the execution of the modification agreement. The court cited Commerce Trust Co. v. Ramp, 135 Tex. 84, 87, 138 S.W.2d 531, 534 (1940), in which the commission of appeals said:

That a removal of the taint of usury cannot be accomplished by merely a renewal, or successive renewals, of an original usurious contract, is settled beyond all controversy. . . . In our opinion in all cases where it has been held by our courts that an executory contract has been purged of usury, as distinguished from release of liability for usurious interest which has been paid, it will be found that there was a new contractual arrangement which in legal effect amounted to a novation, or the substitution of a new contract, based on a sufficient consideration, in lieu of the original usurious one.

272. 539 S.W.2d at 79-80, citing Nevels v. Harris, 129 Tex. 190, 102 S.W.2d 1046 (1937), and distinguishing Terry v. Teachworth, 431 S.W.2d 918, 924 (Tex. Civ. App.—Houston [14th Dist.] 1968, writ ref'd n.r.e.). The jury at the trial in GGE Management Co. had found the fee to be interest on the loan. A similar result was reached in Moss v. Metropolitan Nat'l Bank, 533 S.W.2d 397, 399 (Tex. Civ. App.—Houston [1st Dist.] 1976, no writ).
its liens. The Texas Supreme Court affirmed on all points, but modified the lower court's opinion reducing the rate of interest on the debt from ten percent a year to eight and one-half percent a year.

The usury case with probably the greatest impact is Ferguson v. Tanner Development Co. Ferguson purchased a tract of land in 1973 subject to a first lien note with a principal balance of $151,900.00. He paid $6,000.00 down on the sale price, prepaid one year's interest of $21,506.93 at the closing, and executed a non-recourse wrap-around-note for $226,338.77. The wrap note was payable at nine and one-half percent per annum interest in quarterly installments for four years, after which no interest was to be paid until all of the interest which had been prepaid at closing had been exhausted. Principal installments began in October 1977 with the entire note balance being payable in November 1978. Thus, the interest which was prepaid at closing was not credited to interest payments on the note until 1977. Apparently the purchaser had persuaded the seller to accept the prepaid interest in 1973 in lieu of a more substantial down payment on the sale price of the land, in order that the purchaser's investors could receive the tax benefits from the interest deductions.

After the purchaser defaulted on the note and foreclosure proceedings were started, the purchaser filed this suit to enjoin the foreclosure and to collect usurious interest. The trial court found for the seller, but the court of civil appeals reversed and held as follows: (1) the prepaid interest was a portion of principal which was not advanced until 1977 and which was to be deducted from the principal of the note in order to arrive at the amount of money on which the seller was due interest; (2) the savings clause in the note and deed of trust permitted the spreading of the prepaid interest, but for the purposes of avoiding usury interest would not be enforced for the purpose of allocating to principal any of the usury interest charged on the note; (3)
the $5,087.75 of interest charged was usurious, entitling the purchaser to recover penalty interest of $202,865.74 plus reasonable attorney's fees.\(^{280}\) (4) the fact that the purchaser requested and voluntarily paid the usurious interest was immaterial;\(^ {281}\) (5) the failure to pay interest on a usurious and thus unenforceable contract is not a default, and consequently the seller could not declare a default on the note;\(^ {282}\) and (6) consistent with Wall v. East Texas Credit Union\(^ {283}\) the purchaser could also recover the amount of usurious interest paid to the seller without any reduction for the amount of interest which might lawfully have been collected.

The result reached in Ferguson, even if correct, seems manifestly unfair, considering that the purchaser had requested the seller to accept the prepaid interest in order that the purchaser's investors could enjoy the greater year-end tax deduction. The prepaid interest did not cause the interest to be paid over the term of the note to exceed the lawful rate. The court, however, was concerned about allowing a lender to collect prepaid interest so far in advance. The note might not have been held to be usurious if it had provided that the prepaid interest would be credited to interest due in the first year of the note.\(^ {284}\) Furthermore, had the prepayment of the $21,506.93 of interest

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\(^{280}\) Tex. 400, 30 S.W.2d 282 (1930), in which the holder of the note after default could accelerate even unaccrued interest. The note at issue in Nevels v. Harris, on the other hand, expressly provided that on acceleration any unearned interest would be cancelled. The court said that the doctrine of "spreading" was rejected by the court of civil appeals in Commerce Trust Co. v. Ramp, 135 Tex. 84, 138 S.W.2d 531 (1940), which complicated its holding. For an excellent analysis of the "spreading" concept in usury law see Comment, Usury Implications of Front-End Interest and Interest in Advance, 29 Sw. L.J. 748 (1975).

\(^{281}\) Tex. Rev. Civ. Stat. Ann. art. 5069-1.06 (Vernon 1971) provides that any person who "contracts for or receives" usurious interest must forfeit to the obligor twice the amount of interest contracted for and reasonable attorney's fees. The seller argued, unsuccessfully, that the court should base any calculation of penalty interest upon the sum of $74,488.74, the difference between the interest payable on the wrap note and the first lien note. The court acknowledged that this argument may have been appropriate under the former usury statute, which made a person liable only for usurious interest he "received," but was not under the present Tex. Rev. Civ. Stat. Ann. art. 5069-1.06 (Vernon 1971), which authorizes a penalty of the amount of twice the interest "contracted for, demanded or received." 541 S.W.2d at 494.

\(^{282}\) A "wrap note" includes the principal balance of the notes secured by prior liens, as well as the deferred portion of the price on the new sale. A good discussion of the wrap note can be found in Galowitz, How to Use Wraparound Financing, 5 Real Est. L.J. 107 (1976) (see id. at 124-25 with respect to usury aspects of wrap notes).

\(^{283}\) The note required the usurious prepayment of interest, so that it was not voluntary in a strict contractual sense. See note 285 infra and accompanying text.

\(^{284}\) 541 S.W.2d at 493. The court cited Wall v. East Texas Credit Union, 533 S.W.2d 918 (Tex. 1976), for the holding that interest on a usurious contract is unenforceable, and added: "It follows logically that the failure to pay interest as stipulated in a usurious contract does not authorize the lender to accelerate future payments of either principal or interest." 541 S.W.2d at 493. Thus, Tanner Development Co. could not offset the principal balance of the note against the penalty interest, because the principal was not due. This holding in Ferguson and Wall suggests a return to the pre-1967 usury statute, which made a usurious contract void as to interest. Compare Riverside Mall, Inc. v. Larwin Mortgage Investors, 315 S.W.2d 5, 9 (Tex. Civ. App.—San Antonio 1974, writ ref'd n.r.e.), where the court held: "The 1967 Usury Statute does not provide that a usurious contract is void as did the previous statutes."

\(^{285}\) 533 S.W.2d 918 (Tex. 1976).

\(^{284}\) The court in Ferguson observed that in Bothwell v. Farmers & Merchants State Bank, 120 Tex. 1, 3, 30 S.W.2d 289, 291 (1930), it was held that the "rule sanctioning the reservation of interest in advance at the highest conventional rate for a year or less is too firmly established to be departed form"; and that in Southwestern Inv. Co. v. Hockley County Seed & Delinting, Inc., 511 S.W.2d 724 (Tex. Civ. App.—Amarillo 1974, writ ref'd n.r.e.), the Texas Supreme Court, in refusing writ of error, said a like procedure did not involve the spreading of front-end charges over the life of a loan.
been voluntary (i.e. a voluntary prepayment under the prepayment privilege in the note) instead of being required under the note, the court may have viewed the payment differently.\textsuperscript{285} The court also volunteered this advice: "Had the interest rate in the transaction before this court been adjusted downward, the requirement of one year's interest in advance would not have rendered the contract usurious."\textsuperscript{286} Spreading during the full stated term of the loan is now permitted by statute on loans or agreements on loan made after September 1, 1975 which are secured by a lien on real property.\textsuperscript{287}

The Texas Supreme Court affirmed the court of civil appeals in \textit{Gonzales County Savings \\& Loan Association v. Freeman},\textsuperscript{288} but granted writ to note its disagreement with some of the statements contained in the appellate court's opinion. The borrower asserted that a two percent "loan fee" charged on a loan, bearing interest at the rate of ten percent a year, was additional interest. The lender argued that the loan fee was compensation for allowing the borrower the opportunity to make another loan in the future, which the appellate court said would be a commitment fee and, thus, interest. The Texas Supreme Court disagreed, stating that if the evidence shows that the loan fee is a legitimate commitment fee, intended only as compensation for having the future loan available and for no other purpose, then such a fee is not interest.\textsuperscript{289} The court emphasized that its opinion was limited to bona fide commitment fees, and that labels provided by the lender would not control. "For example, whether or not a charge labeled a 'commitment fee' is merely a cloak to conceal usury depends upon whether or not the fee is unreasonable in light of the risk to be borne by the lender."\textsuperscript{290}

The lender also sought to have the loan fee treated as a "premium," which savings and loan associations are authorized by statute\textsuperscript{291} to charge. The court answered this argument by observing that in the statute the legislature attempted to exclude these reasonable expenses, premiums and penalties from the definition of interest, but had failed to fix a maximum rate for these charges. Regardless of this "extremely complex problem... concerning the Legislature's power to 'define interest and fix maximum rates of interest,'"\textsuperscript{292} the courts were left with some flexibility. For example, in the case of "reasonable expenses" the courts have the power to determine the following: "the reasonableness of the expenses in light of the amount of actual work done;" "penalties need bear some reasonable relationship to the amount of

\textsuperscript{286} 541 S.W.2d at 483.
\textsuperscript{287} TEX. REV. CIV. STAT. ANN. art. 5069-1.07 (Vernon 1975). It has been suggested that this statute violates TEX. CONST. art. XVI, § 11, in that effective ceilings on interest rates are eliminated. See Comment, supra note 279, at 764-65. However, previous authors of this \textit{Survey} article have stated that, if properly construed, art. 5069-1.07 should not be vulnerable to this claim. Wallenstein \\& St. Claire (1976), \textit{supra} note 2, at 45 n.151.
\textsuperscript{288} 534 S.W.2d 903 (Tex. 1976).
\textsuperscript{289} Id. at 906. This holding was correctly predicted in Wallenstein \\& St. Claire (1976), \textit{supra} note 2, at 48.
\textsuperscript{290} 534 S.W.2d at 906.
\textsuperscript{291} TEX. REV. CIV. STAT. ANN. art. 852a, § 5.07 (Vernon 1964), excepts from the definition of interest "all reasonable expenses incurred in connection with the making, closing, disbursing, extending, readjusting or renewing of real estate loans..." In addition, associations may charge premiums for making such loans as well as penalties for prepayments or late payments.
\textsuperscript{292} 534 S.W.2d at 908.
loss or inconvenience suffered by the lender due to prepayment or late payment;" \(^ \text{293} \) and premiums "will be deemed to constitute interest when seeking to determine the existence or nonexistence of usury." \(^ \text{294} \)

IV. REAL ESTATE DEVELOPMENT: MECHANIC'S AND MATERIALMEN’S LIENS; BUILDING AND CONSTRUCTION CONTRACTS

The survey period has been an active one in the area of construction litigation. There were many cases construing the Hardeman Act, \(^ \text{295} \) and other cases involving general problems in building and construction contracts. Despite the increased judicial "fleshing-out" of the Texas mechanic's and materialmen's lien laws, however, there is still a great deal of uncertainty which perhaps points out more than ever the need for simplification of these statutes. \(^ \text{296} \)

A. Perfecting the Lien

1. Sufficiency of Affidavit.

It has been said that the mechanic's and materialmen's lien statutes of Texas will be liberally construed in favor of protecting laborers and materialmen. \(^ \text{297} \) Substantial compliance with the statutory requirements is generally sufficient to give rise to a valid lien. \(^ \text{298} \) The decisions of two Texas courts of civil appeals during the survey period illustrate the varying application of this rule of substantial compliance.

In *Conn, Sherrod and Co., Inc. v. Tri-Electric Supply Co.* \(^ \text{299} \) it was held that where the purported lien affidavit bore only an acknowledgment, the instrument was not an affidavit within the meaning of article 5453, \(^ \text{300} \) which requires subcontractors claiming a lien to file an affidavit not later than 90 days after

\(^ {293} \) Id.

\(^ {294} \) Id. The court said that with regard to "premiums" the statute "does not purport to define interest and cannot be regarded as an attempt by the Legislature to fix maximum rates of interest," citing Community Fin. & Thrift Corp. v. Texas, 161 Tex. 619, 343 S.W.2d 232 (1961). With regard to "points" charged for a loan by a savings and loan association compare Wagner v. Austin Sav. & Loan Ass'n, 525 S.W.2d 724 (Tex. Civ. App.—Austin 1975, no writ).

\(^ {295} \) Sanford A. Weiner has posed the following questions in light of the Freeman decision:

- In light of the Court's emphasis on the option aspect of a legitimate commitment fee, must the commitment limit the lender's remedy for failure to 'take down' the loan to a forfeiture of the commitment fee?
- Must the commitment clearly specify that the borrower merely has an option, and not an obligation, to 'take down' the loan?
- What if the borrower is required to close the permanent loan as a result of a Tri-Party Agreement or similar agreement?
- What if there is a pre-closed loan and a Buy-Sell Agreement between the interim and permanent lenders?

Presentation at Houston Junior Bar Real Estate Seminar, Nov. 19, 1976; see note 266 *supra.*


\(^ {297} \) Hayek v. Western Steel Co., 478 S.W.2d 786 (Tex. 1972).

\(^ {298} \) Texcalco, Inc. v. McMillan, 524 S.W.2d 405 (Tex. Civ. App.—Eastland 1975, no writ).

\(^ {299} \) 533 S.W.2d 31 (Tex. Civ. App.—Tyler 1976, writ ref'd n.r.e.).

\(^ {300} \) An acknowledgment is not an affidavit. See Perkins v. Crettendon, 462 S.W.2d 294 (Tex. Civ. App.—Dallas 1976, writ ref'd n.r.e.). An acknowledgment is not an affidavit. See Perkins v. Crettendon, 462 S.W.2d 565 (Tex. 1970); Crockett v. Sampson, 439 S.W.2d 355 (Tex. Civ. App.—Austin 1969, no writ). An acknowledgement generally states that an instrument is executed for the purposes expressed therein. It does not state that the person swears to the truth of the matters set out in the instrument. An affidavit must contain jurat, which is the attestation to the truth of the matters contained in the writing.
the indebtedness accrues. Since Tri-Electric filed an “Affidavit of Correction” outside the 90 day period, the Tyler court of civil appeals held that Tri-Electric had not substantially complied with article 5453 and therefore had no valid lien. On the other hand, the court in Marathon Metallic Building Co. v. Texas National Bank found that a materialman had substantially complied with the lien laws even though the affidavit claiming the lien erroneously named the wrong party as “owner or reputed owner” of the property. Marathon’s lien affidavit named “O’Grady Containers, Inc.” as the owner or reputed owner, while the property in question was actually owned by two individuals, each of whom was an officer and stockholder of the Corporation. The property had formerly been owned by O’Grady Containers, Inc., and the county tax assessor’s rolls still showed the corporate owner. Additionally, the general contractor’s purchase order named the corporation as the customer, and Marathon’s supplies were held by the corporation at its plant. The Waco court of civil appeals held that in light of these circumstances Marathon had substantially complied with the requirements of the lien laws.

Article 5455(c) requires that a lien affidavit contain a “general statement of the kind of work done or materials furnished . . . , or both.” Where the lien affidavit made a claim for “materials furnished,” and the two contracts attached called for both labor and materials, the court in Mathews Construction Co. v. Jasper Housing Construction Co. held that there had been substantial compliance since the statute only requires a general statement.

2. The Statutory Retainage Fund.

Article 5469 provides for a preference lien on the ten percent retainage fund which the owner must, if properly notified, hold for thirty days after completion of the work. The court in Donahue v. Rattikin Title Company stated, in dicta, that even where a lien could not be obtained against the homestead because of the lack of a written contract, had written notice

303. Tex. Rev. Civ. Stat. Ann. art. 5455(b) (Vernon Supp. 1976-77) provides, among other things, that the affidavit claiming a lien must contain in substance the “name of the owner or reputed owner, if known.”
304. Id. art. 5455(c).
305. 528 S.W.2d 323 (Tex. Civ. App.—Beaumont 1975, writ ref’d n.r.e.). For discussion of other aspects of this case see notes 355-58 and 363-65 infra and accompanying text.
306. See Youngblood, supra note 296, at 482. Prior to 1961 it was necessary for a detailed summarization to be made in the affidavit. See Woodward, supra note 296, at 482.
308. The owner must retain 10% of the contract price for work done under each original contract. This rule reflects the legislative reversal of the decision in Hayek v. Western Steel Co., 478 S.W.2d 786 (Tex. 1972), which held that the owner must retain 10% of the total improvement cost rather than merely 10% of a particular contract for specific work. Section 2 of art. 5452 was amended by the legislature in 1972, changing the definition of “work” to that “which is performed pursuant to an original contract.” The 1972 amendments also added a definition of “contract price” which is limited to costs incurred “pursuant to an original contract.” See Wallenstein (1974), supra note 2, at 51. See generally Youngblood, supra note 296, at 682-87, 707.
309. 534 S.W.2d 156 (Tex. Civ. App.—Fort Worth 1976, no writ).
310. See Tex. Const. art. XVI, § 30. A valid mechanic’s lien against the homestead requires a contract in writing, signed by both husband and wife, and recorded with the county clerk before
been served upon the owner as required, personal judgment could have been obtained to the extent of ten percent of the contract price which should have been, but was not, retained by the owner. No cases were cited by the court in support of this dictum. It is clear that the failure to retain the ten percent as required by law may expose the owner to a personal judgment as provided in article 5463, section 2, but it is not clear that this rule should have any application in the case of a homestead where the provisions of article 5460 and article XVI, section 50, of the Texas Constitution are not satisfied. The court also held that the title company breached its agency contract with the owner by paying subcontractors in violation of the terms of an escrow agreement. The owner had placed money in escrow with the title company under an agreement which authorized Rattikin to apply the funds in payment of "perfected valid mechanic's or materialmen's liens." The court found this provision unambiguous, and held that as the title company had paid subcontractors whose liens were not perfected and valid, the title company was liable to the owner for such amounts.

Sixty-Seven Properties v. Cutsinger Electrical Contractors illustrates the relationship between the concept of recovery in quantum meruit and the ten percent retainage provision of the mechanic's and materialmen's lien statutes. The court permitted a subcontractor which had been wrongfully terminated to recover in quantum meruit and to foreclose a lien on the property to the extent of the ten percent retainage fund. While there is some authority that when recovery is in quantum meruit there can be no lien on the land, the courts have rather consistently allowed a lien to the extent of the work done where work is wrongfully halted by the owner or where there has

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312. The owner gave the original contractor a promissory note for $60,000 which the court treated as being payment in full. 534 S.W.2d at 157. See W & W Floor Covering Co. v. Project Acceptance Co., 412 S.W.2d 379 (Tex. Civ. App.—Austin 1967, no writ).
316. This is not to say, however, that unpaid contractors may not recover personal judgments from homestead owners. But where, as in Donahue v. Rattikin Title, the general contractor is fully paid, it seems anomalous to permit his unpaid subcontractors to trap funds and recover under arts. 5469 and 5463, absent compliance with the requirements of article 5460 and the Texas Constitution. See note 310 supra.
318. Quantum meruit is one of the two major "value counts," the other being quantum valebant. Quantum meruit is for the recovery of the value of services, while quantum valebant pertains to goods. See D. Dobbs, Remedies § 4.2, at 237-38 (1973).
320. In order to secure recovery under the lien statutes for less than full performance, there must either be substantial compliance with the contract or the owner must wrongfully prevent the contractor's compliance. If the materialman or laborer does not substantially perform, recovery is limited to the value of the improvement to the owner, and there is no lien or recovery of attorneys' fees available. Davidson v. Clearman, 391 S.W.2d 48 (Tex. 1965). If further performance is prevented by the owner, the builder may recover in quantum meruit. Austin Stone Indus., Inc. v. Capital Powder Co., 290 S.W.2d 689 (Tex. Civ. App.—Austin 1956, writ ref'd n.r.e.).
been substantial compliance with the contract.\footnote{322} In \textit{Sixty-Seven Properties} the subcontractor was held to have perfected a valid lien against the land to the extent of the ten percent fund which should have been retained under article 5469, even though the lien affidavit was not filed within thirty days after the work was completed. The court noted that while the claimant must both send notice \textit{and} file an affidavit within thirty days after completion of the work in order to perfect a lien against the retainage fund under article 5469, the filing of an affidavit within thirty days is not required in order to secure a lien against the property.\footnote{323} In such a case the contractor need only comply with the notice provisions of article 5453.\footnote{324}

\section*{B. Priorities}

\subsection*{1. Inception of the Lien.}

One of the more noteworthy decisions during the survey period is that of the Amarillo court of civil appeals in \textit{Justice Mortgage Investors v. C.B. Thompson Construction Co.}.\footnote{325} As security for the original construction loan note, Justice took a deed of trust covering the realty together with a financing statement covering all personal property then or thereafter on or attached to the land and/or improvements thereon. The deed of trust contained a "drag-net clause" providing that it secured payment of renewals of and increases in the amount of the original note.\footnote{326} In February 1973 Thompson moved a tool shed on the property and began some preliminary staking. Later, in November 1973 after Justice had advanced approximately one million dollars on the loan, a new note was executed by the owner as a renewal of, substitution for, and an increase in the original note. When the owner failed to make the designated payments, Justice exercised its rights under the optional

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\item See, \textit{e.g.}, Grayson County State Bank v. Osborne, 531 S.W.2d 846 (Tex. Civ. App.—Dallas 1975, writ ref’d n.r.e.); Robinson v. Leach, 237 S.W.2d 366 (Tex. Civ. App.—Fort Worth 1951, writ ref’d n.r.e.). While it appears well settled that a lien may be had to secure the payment of the value of services rendered up to the time of the breach of the construction contract by the owner, should such a recovery be limited by the contract price? Moreover, in situations where the contractor would have sustained a substantial loss on the contract had he been allowed to complete the work, should he nevertheless be permitted a quantum meruit recovery and hence a lien when he is saved this loss because of the owner’s breach? There are two competing theories at work here. On one hand, the law attempts to provide the builder with the benefit of his bargain; on the other hand, there is a strong policy in favor of avoiding the unjust enrichment of the owner. The general rule seems to permit the contractor to recover in excess of the contract price where he bases his recovery on the theory of rescission and restitution. See \textit{Boomer v. Muir}, 24 P.2d 570 (Cal. App. 1933). In Texas it is clear that a builder may not recover both under the contract and on a quantum meruit basis. \textit{See Osage Oil & Ref. Co. v. Lee Farm Oil Co.,} 230 S.W. 518 (Tex. Civ. App.—Amarillo 1921, writ ref’d). \textit{See also Sherrill v. Bruce Advertising, Inc.,} 538 S.W.2d 865 (Tex. Civ. App.—Houston [14th Dist.] 1976, no writ); \textit{Freeman v. Carroll,} 499 S.W.2d 668 (Tex. Civ. App.—Tyler 1973, writ ref’d n.r.e.). \textit{But see Black Lake Pipeline Co. v. Union Constr. Co.,} 538 S.W.2d 80 (Tex. 1976), \textit{discussed in note 375 infra.} However, it is not clear whether in cases of rescission and restitution the quantum meruit recovery may exceed the contract price. \textit{Compare Texas Associates, Inc. v. Bland Constr. Co.,} 222 S.W.2d 413 (Tex. Civ. App.—Austin 1949, writ ref’d n.r.e.), \textit{with Schulz v. Tessman,} 48 S.W.207 (Tex. Civ. App.—Amarillo 1898), \textit{rev’d on other grounds,} 92 Tex. 488, 49 S.W. 1031 (1899). \textit{See also Texas Delta Upsilon Foundation v. Fehr,} 307 S.W.2d 124, 131 (Tex. Civ. App.—Austin 1957, writ ref’d n.r.e.).


\item \textit{325. 533 S.W.2d 939 (Tex. Civ. App.—Amarillo 1976, writ ref’d n.r.e.).}

\item \textit{326. For a discussion of drag-net or future advance clauses see Wallenstein & St. Claire (1976), supra note 2, at 53 n.214.}
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acceleration clause in the note and declared the entire loan due. Thompson filed suit claiming that its recorded mechanic's lien was superior to Justice's deed of trust lien and security interest, and asked for and obtained a temporary restraining order and a temporary injunction preventing the trustee's sale. The trial court issued a temporary restraining order and, after hearing, granted the temporary injunction.

In the court of civil appeals the central controversy concerned the relative priorities of the liens. A deed of trust mortgagee claiming under a deed of trust given solely to secure payment of a non-purchase money debt will have priority only if the deed of trust was recorded prior to the inception of the mechanic's and materialmen's lien.\textsuperscript{327} Section 2 of article 5459\textsuperscript{328} establishes the inception of a mechanic's and materialmen's lien at the occurrence of the earliest of (1) actual commencement of construction or delivery of material to be used in construction to the land if either is actually visible from inspection of the land, or (2) the proper recording of the written agreement, if any, to perform or furnish materials, or (3) the proper recording of a sufficient affidavit by the lien claimant of an oral agreement for construction. The court in Justice Mortgage Investors held that Thompson's lien had its inception when Thompson actually commenced construction or delivered materials to be used in construction, and not when Thompson placed a tool shed and did preliminary staking of the property.\textsuperscript{329} Thus, Justice's deed of trust lien, including advances made pursuant to the renewal of the original construction loan note, was found to be prior in time and superior to Thompson's mechanic's and materialmen's lien.\textsuperscript{330}

\textsuperscript{327} It has been held that a vendor's lien on the land or the lien of a mortgagee claiming under a purchase money deed of trust will by necessity have its inception prior to that of a mechanic's lien. See Irving Lumber Co. v. Alltex Mortgage Co., 468 S.W.2d 341 (Tex. 1971); National W. Life Ins. Co. v. Acreman, 415 S.W.2d 265 (Tex. App.—Beaumont 1967), aff'd in part and modified in part, 425 S.W.2d 815 (Tex. 1968); Shamburger Lumber Co. v. Holbert, 34 S.W.2d 614 (Tex. Civ. App.—Amarillo 1931, no writ). A mechanic's lien claimant who contracts with a prospective owner cannot obtain priority over a vendor's lien which encumbers the property when title is transferred. Harveson v. Youngblood, 38 S.W.2d 781 (Tex. Comm'n App. 1931, holding adopted), except as provided in TEX. REV. CIV. STAT. ANN. art. 5459, § 1 (Vernon Supp. 1976-77).

\textsuperscript{328} TEX. REV. CIV. STAT. ANN. art. 5459, § 2 (Vernon Supp. 1976-77). For the very interesting history of the circumstances leading up to the enactment of this provision see Youngblood, supra note 296, at 665. See also Note, Deed of Trust Mortgage Foreclosure Problems, 7 ST. MARY'S L.J. 135, 146-50 (1975).

\textsuperscript{329} This result is based on the theory that mere preparation for construction, such as staking the property, is insufficient to constitute the commencement of construction. See Kloster-Madsen, Inc. v. Tafi's, Inc., 226 N.W.2d 603 (Minn. 1975); M.E. Craft Excavating & Grading Co. v. Barac Constr. Co., 279 Minn. 278, 156 N.W.2d 748 (1968); Mortgage Associates, Inc. v. Monona Shores, Inc., 47 Wis. 2d 171, 177 N.W.2d 340 (1970). The wording of art. 5459, § 2 supports this result. What is not clear, however, is whether the lien of a second original contractor will relate back to and have its inception at the commencement of visible construction by the first original contractor. See Woodward, The Hardeman Act—Some Unanswered Questions, 6 ST. MARY'S L.J. 1 (1974).  

\textsuperscript{330} Generally, whether a prior deed of trust lien secures additional indebtedness depends on whether the additional advances were reasonably within the contemplation of the parties at the time the deed of trust was executed. See Wood v. Parker Square State Bank, 400 S.W.2d 898 (Tex. 1966); Moss v. Hipp, 387 S.W.2d 656 (Tex. 1965); Coke Lumber & Mfg. Co. v. First Nat'l Bank, 529 S.W.2d 612 (Tex. Civ. App.—Dallas 1975, writ ref'd). See generally Wallenstein & St. Claire (1976), supra note 2, at 53 n.214. Dragnet clauses such as the one involved in this case often create problems for subsequent purchasers. See, e.g., Estes v. Republic Nat'l Bank, 462 S.W.2d 273 (Tex. 1970). See also Airline Commerce Bank v. Commercial Credit Corp., 531 S.W.2d 171 (Tex. Civ. App.—Houston [14th Dist.] 1976, writ ref'd n.r.e.), discussed in notes 222-25 supra and accompanying text.
2. "Whirlpool Doctrine."\textsuperscript{331}

A mechanic’s and materialmen’s lien is given preference over all prior recorded liens unless the prior lien will be “affected” by the enforcement of the mechanic’s lien.\textsuperscript{332} A prior lien will be affected if the removal of improvements will cause material injury to the land, to pre-existing improvements, or to the improvements to be removed.\textsuperscript{333} The court in \textit{Justice Mortgage Investors} reaffirmed this rule holding that Justice’s deed of trust lien was superior except with respect to items of improvement furnished by Thompson which could be removed without material injury to the land, to the building, and to the items themselves.\textsuperscript{334}

Although implied by the language of the opinion, the court did not specifically state whether the preference lien for mechanics and materialmen is limited to severable improvements furnished by the claimant himself, or whether the claimant is entitled to remove any and all severable improvements sufficient to satisfy his lien, including those on which the claimant never worked and those which he did not furnish. The early decisions on this issue held the preference lien applicable to all severable improvements.\textsuperscript{335} More recent authority, however, supports the view implied in the \textit{Thompson} case that priority is allowed only with respect to improvements furnished by the lien claimant.\textsuperscript{336}

Justice argued that with respect to the severable improvement its prior recorded security interest was superior to Thompson’s mechanic’s lien, even though the deed of trust lien had no such priority. The court rejected this contention, citing \textit{Whirlpool},\textsuperscript{337} which held that mechanic’s and materialmen’s liens have a preference with respect to improvements which are sufficiently affixed to the real estate so as to become part thereof.\textsuperscript{338} Finally, the court held that although Thompson had shown a probable right of recovery with respect to severable improvements, it was not shown that an interim legal injury would probably result unless the trustee’s sale was

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\item \textsuperscript{331} First Nat’l Bank v. Whirlpool Corp., 517 S.W.2d 262 (Tex. 1974).
\item \textsuperscript{332} TEX. REV. CIV. STAT. ANN. art. 5459, § 1 (Vernon Supp. 1976-77).
\item \textsuperscript{333} First Nat’l Bank v. Whirlpool Corp., 517 S.W.2d 262 (Tex. 1974); Hammann v. McMullen & Co., 122 Tex. 476, 62 S.W.2d 59 (1933); see Wallenstein (1975), \textit{supra} note 2, at 48-49.
\item \textsuperscript{334} 533 S.W.2d at 944.
\item \textsuperscript{335} Wallace Gin Co. v. Burton-Lingo Co., 104 S.W.2d 891 (Tex. Civ. App.—Austin 1937, no writ); R.B. Spencer & Co. v. Brown, 198 S.W. 1179 (Tex. Civ. App.—El Paso 1917, writ ref’d). This view is grounded on the theory that a mechanic’s and materialman’s lien is a charge on the entire parcel of real property, so that when improvements are affixed to the realty and lose their identity as personalty, such improvements are thus subject to the lien, regardless of who actually placed them on the land.
\item \textsuperscript{337} 533 S.W.2d at 944-45.
\item \textsuperscript{338} Cf. Gulf Coast State Bank v. Nelms, 525 S.W.2d 866 (Tex. 1975). This rule creates an obvious grey area between those items which are placed on the land, but are not sufficiently attached and thus remain personalty subject to ch. 9 of the Texas Business and Commerce Code, those which are sufficiently affixed so as to be subject to a mechanic’s and materialmen’s lien, and those which are so affixed that they are not severable without material damage and are thus subject to a prior deed of trust lien.
\end{itemize}
enjoined. Presumably, there could be no injury since foreclosure under the deed of trust could not affect the mechanic's lien to the extent it had priority. Therefore, the court of civil appeals held that the trial court had abused its discretion in granting the temporary injunction.

3. Trust Fund Statute

In *American Amicable Life Insurance Co. v. Jay's Air Conditioning and Heating, Inc.* the court held that a materialman was not a trustee of funds for the benefit of the beneficiary under the deed of trust covering the property. On the contrary, the court found that the trust fund statute gives a materialman a preferred status with respect to funds borrowed by the general contractor. The court also held that for the purpose of determining whether there has been payment in full a subcontractor who has several existing unpaid accounts owed to him by a particular general contractor is permitted to follow a "first-in, first-out" rule with random payments received from that general contractor applied to the oldest existing debt. The court did not discuss the applicability of this rule where the subcontractor knows the source of the payments and/or is instructed as to how the payments should be applied.

C. Performance and Payment Bonds

*Parliament Insurance Co. v. L. B. Foster Co.* involved a supplier bringing suit against a surety on a performance and payment bond executed by a subcontractor in favor of the original contractor. The supplier had furnished materials to the subcontractor who was unable to pay for them. The surety argued that the payment language in the bond was solely for the purpose of indemnifying the general contractor for any payments for which it might become liable on account of the subcontractor, and as such, the bond was not for the benefit of the supplier. In holding that the bond was intended to and did enure to the benefit of suppliers and subcontractors, the court noted that ordinarily a performance bond is for the benefit of the principal (here the general contractor), whereas a payment bond generally benefits the beneficiary.

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339. 533 S.W.2d at 946. A temporary injunction is not proper unless the applicant shows a probable injury. Armendariz v. Mora, 526 S.W.2d 542 (Tex. 1975); Chisholm v. Adams, 71 Tex. 678, 10 S.W. 336 (1888).

340. It is well settled that the foreclosure of a junior lien does not affect a senior lien. 39 Tex. Jur. 2d Mortgages and Trust Deeds § 174 (1976).


342. 535 S.W.2d 23 (Tex. Civ. App.—Waco 1976, writ ref'd n.r.e.).


344. 535 S.W.2d at 26.

345. See related discussion in note 352 infra.


347. 533 S.W.2d 43 (Tex. Civ. App.—Corpus Christi 1976, writ ref'd n.r.e.).

348. The original contractor required the subcontractor to secure a performance and payment bond. See A.B.C. Truck Rental & Leasing Co. v. Pletz, 540 S.W.2d 532 (Tex. Civ. App.—San Antonio 1976, writ ref'd n.r.e.), for another case involving a subcontractor's performance bond.
laborers and materialmen. While the result in this case seems correct, in further support of its decision the court unnecessarily stated that all doubts and ambiguities in a bond must be resolved against a surety. This statement is a departure from the general rule that a surety’s obligation will be strictly construed within the terms of the contract, and should be questioned since among the cases relied on as authority the court cited *First State Bank v. Metropolitan Casualty Insurance Co.*, a Texas Supreme Court decision which actually held in accordance with the general rule of strict construction.

The court went further in holding that where a bond is for the benefit of materialmen, it is inconsequential that some materials are supplied prior to the execution of the bond. As long as the materials are used in performance of the work covered by the sub-contract, a payment bond will secure payment of the price of such materials. Generally, as between principal (contractor) and surety, the latter will be discharged from liability because of a violation by the principal of the terms of the bond, including a material alteration of the contract between the contractor and owner. As pointed out in a recent case, however, where there is a payment bond for the benefit of materialmen, the surety is not discharged as to materialmen who furnished supplies after a material alteration of the original contract but who were without actual or constructive notice of such alteration.

Article 5472d, section 6, provides that a claim under a payment bond must be made within fourteen months after the required notice is given. In *Mathews Construction Co. v. Jasper Housing Construction Co.*, the plaintiff filed its original petition within the fourteen month period, but its amended petition was filed beyond the statutory period. In reversing the trial court, the court of civil appeals held that as the amended complaint was not sufficiently invoked its claim against the surety within the statutory period.

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349. 533 S.W.2d at 49.
351. 125 Tex. 113, 79 S.W.2d 835 (1935). The court also cited a civil appeals case, Fidelity & Deposit Co. v. Central State Bank, 12 S.W.2d 611 (Tex. Civ. App.—Waco 1928, no writ), which goes against the weight of authority.
352. Another issue in the case concerned the fact that prior to the subcontract in question, the subcontractor owed outstanding balances for other materials; the materialman apparently applied some of the proceeds of the subcontract to discharge these prior obligations. Generally, a surety is entitled to have the proceeds from the contract covered by the bond applied toward the discharge of the debt for which the surety is bound. See Aetna Cas. & Sur. Co. v. Hawn Lumber Co., 128 Tex. 296, 97 S.W.2d 460 (1936). However, this rule is qualified in cases where the recipient of the payments does not know the source of the funds and does not receive any special instructions regarding the application of the payments. Here there was no evidence that the materialman knew of the source of the payments or received any instructions as to their application.
353. Straus-Frank Co. v. Hughes, 138 Tex. 50, 156 S.W.2d 519 (1941).
356. Notice may be given either in compliance with *id.* art. 5453, or as provided in art. 5472d(4). See Barker & Bratton Steel Works, Inc. v. North River Ins. Co., 541 S.W.2d 294 (Tex. Civ. App.—Dallas 1976, writ ref'd n.r.e.).
357. 578 S.W.2d 323 (Tex. Civ. App.—Beaumont 1975, writ ref'd n.r.e.). For discussion of other aspects of this case see notes 305-06 supra and 363-65 infra and accompanying text.
358. Leonard v. Texaco, Inc., 422 S.W.2d 160 (Tex. 1967), sets forth the rule as to when the statute of limitations should apply to amended pleadings. See also Hallaway v. Thompson, 148 Tex. 471, 226 S.W.2d 816 (1950); John H. Pelt Co. v. American Cas. Co., 513 S.W.2d 128 (Tex. Civ. App.—Dallas 1974, writ ref'd n.r.e.).
First Hutchings-Sealy National Bank v. Aetna Casualty & Surety Co. concerned the priority of a surety under a contractor's payment and performance bond as against the bank which made a loan to the contractor and obtained a security interest in the construction contract. The bank advanced over $35,000.00 before the contractor became unable to perform and defaulted on the contract, and the surety assumed the contract and completed the job. Thereafter, the owner paid the balance of the contract funds to the surety. The defaulting contractor never paid the surety the amount of its loss under the contract, and the contractor also defaulted in the payment of its note to the bank. The bank then brought suit against the contractor, the owner, and the surety. The trial court entered a take nothing judgment against the owner and the surety. On appeal, the bank argued that its perfected security interest in the construction contract gave it priority to funds paid to the surety who completed the work under the contract.

Article 5160, section E, provides that in the event a contractor who has furnished a performance bond fails to perform his contract, no further proceeds of that contract shall be payable to him until the cost of completing the work has been paid by the contractor. That section also provides that any balance remaining on the contract shall be payable to the contractor or his surety in accordance with their respective interests. The court held that as the bank had no greater right to the contract funds than the defaulting contractor, and the contractor was barred from recovering funds under the contract by article 5160, section E, the bank was likewise barred from any recovery.

D. Building and Construction Contracts

Mathews Construction Co. v. Jasper Housing Construction Co. also involved several issues concerning construction contracts. An unpaid sub-

359. 532 S.W.2d 114 (Tex. Civ. App.—Houston [1st Dist.] 1975, writ ref'd n.r.e.).
360. TEX. REV. CIV. STAT. ANN. art. 5160(E) (Vernon 1971).
361. The bank had argued that its security interest in the construction contract gave the bank a prior right to funds earned under that contract by the surety who assumed the contract and performed the remaining contractual obligations. The bank’s theory seems to suggest that the surety, not the bank, stood in the shoes of the defaulting contractor. This argument has a certain amount of force, but it goes against the weight of authority in Texas which holds that the rights of a surety are superior to the rights of a bank as the contractor’s assignee. See, e.g., O’Neil Eng’r Co. v. First Nat'l Bank, 222 S.W. 1091 (Tex. Comm'n App. 1920, holding approved); Deer Park Bank v. Aetna Ins. Co., 493 S.W. 2d 305 (Tex. Civ. App.—Beaumont 1973, no writ). These cases as well as First Hutchings-Sealy cast the position of the surety as having subrogation rights under the owner. 532 S.W.2d at 117. Subrogation means that one person is allowed to stand in the shoes of another and assert his rights. See generally D. Dobbs, supra note 107, § 4.3, at 250-52. What the courts seem to be saying is that a surety who performs for the defaulting contractor is subrogated to the rights of the owner against that contractor. In First Hutchings-Sealy these rights followed out of a construction contract which was prior in time and right to the bank's assignment. Moreover, since the bank stood in the contractor's shoes as its assignee, the surety thus had a position superior to that of the bank. See Hess & Skinner Eng’r Co. v. Turney, 110 Tex. 148, 216 S.W. 621 (1919). In spite of the case law supporting the surety's position, it is submitted that had the original contract been terminated and a new "completion contract" been entered into, the bank's argument would have been insupportable. This latter procedure would be advisable under cases such as First Hutchings-Sealy.
363. 528 S.W.2d 323 (Tex. Civ. App.—Beaumont 1975, writ ref'd n.r.e.). For discussion of other aspects of this case see notes 305-06 and 355-58 supra and accompanying text.
contractor assigned its lien to a bank and executed two promissory notes. The general contractor guaranteed payment of the notes and orally promised to pay the subcontractor the interest on the notes. The court held that the general contractor's oral agreement to pay the interest was not barred by the Statute of Frauds since this was not a promise to pay the debt of another, but rather a direct promise to reimburse the subcontractor for interest charges incurred. Since Jasper Housing had agreed to pay the interest in order to defer paying its obligation to Mathews, this promise was supported by adequate consideration. The court also held that when Mathews performed the ground preparation work for Jasper Housing, Mathews was performing a service so that attorneys' fees would be recoverable under article 2226.

Muller v. Light concerned issues under both an express contract and an oral agreement. The contractor sued the owner for the cost of construction and certain extra items, and to foreclose a lien on the property. The owner brought a counterclaim based on a liquidated damage provision in the construction contract under which the owner was given the right to deduct $100.00 per day for each day the work remained unfinished after the scheduled completion date. In refusing to honor the liquidated damages clause, the court noted that the clause would establish damages of $3,000.00 per month while the undisputed rental value of the home was approximately $400.00 per month. Since actual damages would not have been difficult to estimate when the contract was made, and since the liquidated sum was clearly excessive, the court found that "the provision was intended to serve as an in terrorem device to insure prompt performance by the builder, rather than as a reasonable estimate of actual damages."

The jury, in answering certain special issues, found an oral agreement whereby the builder promised to perform certain extra work in a "good and workmanlike manner." It was also found that the builder had breached this contract by not properly constructing the extra items. The court held that although the work was defective, it was of some value to the owner, and that the builder was therefore entitled to recover the value of the extras less the estimated cost to repair them.

It was held in Syring-Workman, Inc. v. Colbert that a contract providing that the "Approximate Maximum Cost shall be $120,000 for remodeling and renovating a building did not limit the maximum cost of the project to the owner to $120,000.00. The court stated that the word "approximate" indicated that the parties contemplated a "reasonable variance."

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364. TEX. BUS. & COMM. CODE ANN. § 26.01 (Vernon 1968).
366. 538 S.W.2d 487 (Tex. Civ. App.—Austin 1976, writ ref'd n.r.e.).
367. Id. at 488. See also Loggins Constr. Co. v. Stephen F. Austin State Univ., 543 S.W.2d 682 (Tex. Civ. App.—Tyler 1976, no writ).
368. See Rogowicz v. Taylor & Gray, Inc., 498 S.W.2d 352 (Tex. Civ. App.—Waco 1973, writ ref'd n.r.e.). A builder is precluded from any recovery whatsoever only if his work is worthless to the owner. The court did not discuss the availability of a lien in this case. See notes 310-22 supra and accompanying text.
369. 532 S.W.2d 708 (Tex. Civ. App.—Waco 1976, writ ref'd n.r.e.).
370. Id. at 710. Such a provision does not render the contract so indefinite as to be unenforceable. See Norton v. Menard Lumber Co., 523 S.W.2d 791, 793 (Tex. Civ. App.—San Antonio 1975, no writ).
In *Board of Regents of the University of Texas v. S. & G. Construction Co.*<sup>371</sup> the written contract for the construction of married students apartments included as attachments maps, plats, drawings, and site plans, and contained a provision requiring the Board of Regents to furnish the contractor with "instructions and detail drawings necessary to carry out the work included in the contract."<sup>372</sup> The Board failed to provide correct plans, specifications, instructions, and detailed drawings necessary to carry out the work called for in the contract. In fact, the topographical survey provided by the Board contained numerous errors which greatly increased the cost of construction to the builder. After completing the project the builder brought this action for additional compensation, seeking damages incurred as a result of the Board's failure to supply a correct survey. The trial court entered judgment in favor of the builder.

The Board of Regents argued that the builder, having elected to complete the work in spite of the Board's breach of the contract, waived the breach and was estopped from asserting any claim for additional compensation other than under the change-order procedure contained in the contract. The court rejected this theory holding that the builder's election to continue construction simply precluded the builder from subsequently ceasing its performance based on the Board's breach.<sup>373</sup> The court stated that the builder's additional compensation was not limited by the change-order procedure set forth in the contract. The builder was held entitled to recover the additional costs incurred, this being the measure of damages which would place the builder as nearly as possible in the position in which it would have been had the Board not breached the contract.<sup>374</sup>

Another case decided during the survey period, however, denied the builder any recovery for additional expenses incurred in the performance of a construction contract. In *Brown-McKee, Inc. v. Western Beef, Inc.*<sup>375</sup> a builder sought to recover additional expenses incurred because of the unforseen presence of rock under the construction site. The court considered the distinction between extras and work required by the contract, and held that extra work is that which arises outside and independent of the contract. Thus, any work done incidental to the performance of the contract would not be compensable as extra work. The court found that the expense of clearing rock was incurred in order to facilitate the performance of the builder's contractual obligations. Moreover, the builder could not recover on the basis of mistake since the court found that any mistake relating to the presence of underlying rock did not go to the substance of the contract, but related to a mere collateral matter.<sup>376</sup> The court, however, did not indicate the criteria for

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371. 529 S.W.2d 90 (Tex. Civ. App.—Austin 1975, writ ref'd n.r.e.).
372. Id. at 95.
373. Id. at 97.
374. Id. at 98.
375. 538 S.W.2d 840 (Tex. Civ. App.—Amarillo 1976, writ ref'd n.r.e.). During the survey period the Texas Supreme Court made the distinction between "extras" and work called for under an express contract clear in *Black Lake Pipe Co. v. Union Constr. Co.*, 538 S.W.2d 80 (Tex. 1976), where the court held that the existence of an express contract bars recovery in quantum meruit only with respect to work covered by the express contract. Compare the general rule discussed in note 322 *supra*.
376. 538 S.W.2d at 845.
distinguishing mere collateral matters from those which go to the substance of a contract. This metaphysical distinction is not a sound basis for decision. 377 The result reached by the court ultimately rests on its finding that the expense incurred in clearing the rock was necessary in the performance of the builder’s contractual obligations. 378 Thus, such expenses were part and parcel of the risks incurred by the builder under the contract in question, and accordingly must be borne by him.

An interesting case only tangentially related to building contracts nevertheless exemplifies the hidden obstacles which can often impede the development of real property. The court in Brodhead v. City of Forney 379 held that developers could not recover damages from the city because of the city’s breach of an agreement to install water lines and sanitary sewer lines and do street work in a subdivision developed by the plaintiffs. Article 11, sections five and seven of the Texas Constitution 380 provide that no debt shall ever be incurred by a city or county unless, at the same time, provision is made for levying and collecting a sufficient tax to provide payment of interest on the debt and a sinking fund of at least two percent for payment of principle. The court held that the plaintiffs failed to meet the burden of pleading and proving that the constitutional requirements were met or that the debt when made was payable out of available current revenues. 381

V. LANDLORD AND TENANT

A. Construction of Lease Agreements

1. Renewal Options.

Most landlord and tenant cases decided during this survey period involved the interpretation of lease provisions. Three cases dealt with options to renew leases. In Stephenson v. Chrisman 382 the court was asked to decide whether an option to renew a lease at a rental rate to be fixed by future agreement of the parties was enforceable. The parties had been unable to agree on a renewal rental at the end of the primary term. The trial court held the renewal option enforceable, and set the renewal rental at a rate it found to be reasonable. The court of civil appeals reversed because, in its view, reason-

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377. The courts in Pruett v. Munroe, 474 S.W.2d 798, 800 (Tex. Civ. App.—Houston [1st Dist.] 1971, no writ), and City Inv. & Loan Co. v. Wichita Hardware Co., 57 S.W.2d 222, 223 (Tex. Civ. App.—Fort Worth 1931), rev’d in part on other grounds, 127 Tex. 44, 91 S.W.2d 683 (1936), struggled with the meaning of “collateral.”

378. 538 S.W.2d at 844.

379. 538 S.W.2d 873 (Tex. Civ. App.—Waco 1976, writ ref’d n.r.e.).

380. TEX. CONST. art. XI, §§ 5, 7.


383. The lease agreement gave the lessee the option to renew the lease for an additional five-year period “upon such money rents as may be agreed upon by the parties but not more than the sums for which same could be leased to a bona fide lessee.” Presumably, all the terms of the original lease, other than the rental rate, were to be carried forward in the renewal. See 2 M. FRIEDMAN, supra note 228, § 14.1, at 557; 51C C.J.S. Landlord and Tenant § 71 (1968).
able rental value was not necessarily the rate at which the property could be leased to a bona fide lessee, as required by the lease. Before abandoning its effort to decide the enforceability of the option, the court noted that a lease agreement which gave the lessee the "first refusal to renew this lease at a price to be agreed upon or to meet any bona-fide offer" had been held to be unenforceable in Schlusselberg v. Rubin because such a provision was indefinite and uncertain. Nevertheless, the court appears to have felt that Pickrell v. Buckler was some authority for the enforceability of the renewal option. The court of civil appeals in Stephenson, after discussing these two cases, concluded that there is a division of authority among the various states as to the enforceability of renewal option provisions which leave the rental rate to the future agreement of the parties. The court, however, refused to expressly adopt either view and remanded the case for a new trial on the issue of the proper renewal rate. This aspect of the decision is unfortunate; if, after a new trial the court of civil appeals holds the renewal option to be unenforceable, the time and expense of the second trial will have been wasted. The Schlusselberg decision is in line with the majority rule unless the Texas courts are ready to adopt a rule that such a renewal option will be enforced at a reasonable rental rate where the parties are unable to agree upon a rate.

Parties to a lease should avoid this problem either by agreeing in advance upon the rentals for the renewal period, or by providing in the lease a method of arriving at the rental, such as by appraisal, arbitration, application of a definite formula, or reference to comparable properties. In agreeing upon a future rate the lessee should consider adjustments for improvements he will make during the primary term and reductions in value due to condemnation, depreciation, and other factors.

The lessor was the one contending that the renewal option of an office lease had been exercised in Pratt v. Dallas County. The lessee, by giving written notice, had the option to renew the lease on the same terms, except that the

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384. 465 S.W.2d 226 (Tex. Civ. App.—El Paso 1971, writ ref’d n.r.e.). In Schlusselberg the court found the requirement that the renewal rate be agreed upon by the parties to be fatal. It would appear that the court in that case probably would have upheld the option if it had omitted that requirement and had merely given the lessee the right to meet any bona fide offer. There was no evidence that a bona fide offer to lease the property had been made by a third party. A “first refusal to renew” is comparable to a first refusal right, which gives the lessee the right to renew the property only in the event the lessor wants to relet at the end of the lease term. 2 M. FRIEDMAN, supra note 228, § 14.1, at 550.

385. 293 S.W. 667 (Tex. Civ. App.—El Paso 1927, writ ref’d). Pickrell is discussed in 36 TEX. JUR. 2d Landlord and Tenant § 243, at 89 n.2 (1962). The renewal of the lease under the option before the court in Pickrell was to be “at the price the party of the first part is willing to rent to any one else.” The court of civil appeals in Stephenson observed that, while the appeals court in Pickrell held that the renewal option was void for uncertainty, the Texas Supreme Court in refusing error disagreed with that holding. The Pickrell case was distinguished in Schlusselberg on the basis that the rental rate under the renewal option was not to be set by agreement of the parties, but by the choice of the lessor. The lessor could, under an option allowing him to set the renewal rate, simply set the rate higher than the lessee would be willing to pay. One court, however, has held that if the lessor chooses a renewal rate that is unconscionable, the court will set a proper rate. Tai On Luck Corp. v. Cirota, 35 App. Div. 2d 380, 316 N.Y.S.2d 438 (1970).

386. 2 M. FRIEDMAN, supra note 228, § 14.1, at 562.


388. 531 S.W.2d 904 (Tex. Civ. App.—Waco 1975, writ ref’d n.r.e.).

389. The court held that the lessor can waive the requirement for written notice, since it is for the lessor’s sole benefit, citing Pruett Jewelers, Inc. v. J. Weingarten, Inc., 426 S.W.2d 902, 905 (Tex. Civ. App.—Tyler 1968, writ ref’d n.r.e.). See note 390 infra.
rental rate would be increased by five percent. No written notice was given by the lessee; however, it held over after the termination of the original lease. After the lessor gave the lessee notice that the rental rate was increased by five percent, the lessee paid this increased rate for two months before abandoning the premises and refused to pay additional rentals. The lessor took the position that the lessee had, as a matter of law, exercised the renewal option by remaining in possession and paying the increased rentals. The court of civil appeals affirmed the trial court, holding that although, in the absence of an express or implied agreement, a lessee’s holding over and payment of rentals would constitute an election to exercise the renewal option, in this case the lease expressly provided that a holding over would be construed as a tenancy from month-to-month only. The court found that this provision controlled the relationship of the parties after the expiration of the primary lease term, even though the lessee did pay the rental rate provided for under the renewal clause.

As illustrated by *Parham v. Gloss Club Lake, Inc.*, Texas follows the rule that in the absence of a lease provision to the contrary a lessee can exercise an option to renew the lease even though he is then in default under the lease. Although the court in *Parham* found that the lessee had violated the lease by fencing a part of the lake, a breach of that covenant did not excuse the lessor from the obligation to renew the lease. The lease did not provide that the lessor could forfeit the lease because of a violation or nonperformance of a covenant other than the failure to pay rent. Further, the exercise of the option to renew was not conditioned upon performance of or compliance with all or any of the covenants in the lease. A different result should be reached in a case where the lease requires that the lessee be in good standing at the time the renewal option is exercised, unless, of course, the lessor waives the default or

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390. The hold-over clause involved in Pruett Jewelers, Inc. v. J. Weingarten, Inc., 426 S.W.2d 902 (Tex. Civ. App.—Tyler 1968, writ ref’d n.r.e.), provided that the lessee would pay the same rental rate as was paid during the last month of the primary term. One Texas court has held that a lease provision which states that holding over does not constitute a renewal can be waived. In *McCue v. Collins, 208 S.W.2d 652* (Tex. Civ. App.—Eastland 1948, no writ), the court held that acceptance of increased rentals for fifteen months after the expiration of the primary term and evidence of an oral agreement to extend the lease term resulted in a waiver of both the provision requiring written notice to extend, and the provision that any holding over would not, without written agreement, extend the lease. However, *Pruett* demonstrates that it will take something more than the lessee’s payment of rentals at the renewal rate in order to constitute waiver.

The following commentary appears in 2 M. Friedman, *supra* note 228, § 14.3, at 597:

> Other matters may bar an implication of a renewal from a tenant’s continuance in possession. It is not uncommon for a lease to provide that a tenant’s continuance in possession after expiration shall constitute a month-to-month tenancy. This protects both landlord and tenant against perhaps unintentionally binding themselves for another year. When a lease includes both this clause and a right to renew, the renewal usually being on notice, a failure to give notice results in the month-to-month tenancy, absent evidence of intention otherwise.

Haltom City State Bank v. King Music Co., 474 S.W.2d 9 (Tex. Civ. App.—Fort Worth 1971, writ ref’d n.r.e.), Corpier v. Lawson, 366 S.W.2d 361 (Tex. Civ. App.—Waco 1962, no writ), and Nortex Foods, Inc. v. Burnett, 278 S.W.2d 485 (Tex. Civ. App.—Dallas 1955, no writ), are authority for the above quote and for the holding in *Pratt*, although in each of those cases the renewal rate was the same as the rate for the primary term. *But see* Coulter v. Capitol Fin. Co., 266 N.C. 214, 146 S.E.2d 97 (1966), where the opposite result was reached, largely because the renewal rate (which was greater than the primary term rate) was paid and accepted for months. *See generally 36 Tex. Jur. 2d Landlord and Tenant §§ 246 (1962).*

391. 533 S.W.2d 96 (Tex. Civ. App.—Texarkana 1976, writ ref’d n.r.e.).

the court finds the lessee to be in substantial compliance with the lease terms. Thus, in *Tidwell v. Lange* it was held that the lessee could not enforce a lease option to purchase the property because he was in default under the lease.

2. **Indemnity.**

The lessor's right to recover against the lessee under an indemnity clause in a lease agreement was the issue in *Bernard v. L.S.S. Corp.* Mother Blues, Inc. leased the property in 1967 for use as a nightclub. A state tax lien was imposed against the property in 1969 because of the failure of Mother Blues to pay admission tax on its business. The State of Texas filed suit in 1973 to collect the tax and to foreclose the statutory lien. The lessor filed a cross-claim against the lessee for indemnity under the lease, and against the guarantors of the lease. Summary judgment was entered in favor of the State of Texas for the deficient taxes, for foreclosure of the statutory lien, and in favor of the lessor for indemnity and attorneys' fees. Against the contention of the appellees that the lessor's cause of action for indemnity arose when the taxes became delinquent and, thus, was barred by the four-year statute of limitations, the court of civil appeals held that the lessor became entitled to indemnity only upon the foreclosure of the tax lien, so that its claim for indemnity was not barred by limitations. On the other hand, the court of civil appeals found that the guarantors were liable on their guaranty of the lease even though the guaranty, by its own terms, expired before the date the judgment for indemnity was entered in favor of the lessor. The court said that the guarantor's liability arose out of the lessee's failure to pay the admissions tax, which was a breach of a provision in the lease requiring the lessee to comply with all laws applicable to the property. The lessee's liability for payment of the taxes and its breach for failure to pay the taxes arose while the guaranty was in effect, and the guarantors would not be allowed to escape liability simply because the lessor's claim for indemnity did not arise until after the guaranty had expired.

3. **Subrogation.**

The effect upon the insurer of a lease clause which waives the parties' right to subrogation was the issue in *Williams v. Advanced Technology Center*, the court finds the lessee to be in substantial compliance with the lease terms. Thus, in *Tidwell v. Lange* it was held that the lessee could not enforce a lease option to purchase the property because he was in default under the lease.

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394. 531 S.W.2d 384 (Tex. Civ. App.—Waco 1975, no writ).
395. 532 S.W.2d 409 (Tex. Civ. App.—Austin 1976, writ ref’d n.r.e.).
396. TEX. TAX.—GEN. ANN. art. 21.04(2) (Vernon 1969) provided that the state had a lien for delinquent taxes and penalties on all property *used* by the owner or operator of any place of amusement. This statute was amended in 1971 to make the lien applicable only to property belonging to the owner or operator of a place of amusement. The court cited Texas Auto Servs., Inc. v. Kemp, 478 S.W.2d 646 (Tex. Civ. App.—Austin 1972, no writ), and Russell v. Lemons, 205 S.W.2d 629 (Tex. Civ. App.—Amarillo 1947, writ ref’d n.r.e.), for the rule that "a cause of action accrues to the indemnitee only when liability becomes fixed, as upon rendition of judgment." 532 S.W.2d at 410. It is curious, then, why the court followed that statement with the holding that in this case liability became "fixed" upon foreclosure of the tax lien. Presumably, foreclosure had not occurred at the time this decision was rendered, and the lessor would not have to wait for foreclosure in order to establish its right of recovery.
The subrogation clause provided that to the extent of the recovery on the insurance each party waived any claim against the other party for any loss or damage to property which was covered by fire and extended coverage insurance. Another lease provision contained a covenant of the lessee not to use the property for a purpose which would be extra hazardous because of fire. The full amount of a loss claim for an explosion and accompanying fire damage to the property was paid by the lessor's insurer, who on the theory of subrogation sued the lessee to recover for the loss. The lessee did not dispute the insurer's allegation that the lessee's use of the property was extra hazardous. The trial court entered summary judgment for the lessee and the court of appeals affirmed, holding that where the insured settles with or releases another from liability for a loss before the insurer makes payment on the loss, the insured's right to subrogation is abrogated to the extent of the waiver. The lessor had recovered under the insurance policy, and the court held that since the lessor had no claim against the lessee under the waiver of subrogation clause, the insured had no claim against the lessee. The lessee's breach of its covenant not to use the property for an extra hazardous purpose was held to have no effect on the waiver of subrogation.

4. Merger of Agreements.

The lessee in *Austin Shoe Stores v. Elizabeth Co.* sought a partial rebate of rents based upon the provisions of a letter written by the original lessor prior to the execution of the lease. The defendant, a subsequent owner of the property, refused to abide by the agreement contained in the letter, relying upon the parol evidence rule and the merger provision in the lease which stated that the lease contained all the agreements of the parties. The court acknowledged that in the absence of fraud, accident, or mutual mistake, the parol evidence rule is applicable, particularly if the lease contains a merger provision. It was held, however, that parol evidence may be introduced to show mutual mistake and to show the modifications required to correct it, where, as here, mutual mistake has been alleged. The court further held that parol evidence is admissible if it demonstrates the inducements that led to the execution of the lease or the circumstances under which it was executed. Denial of summary judgment for the lessee was affirmed, but the trial court's summary judgment for the lessor was reversed.

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399. 537 S.W. 2d 531 (Tex. Civ. App.—Eastland 1976, writ ref’d n.r.e.).
400. The court relied upon *International Ins. Co. v. Medical-Professional Bldg.*, 405 S.W. 2d 867 (Tex. Civ. App.—Corpus Christi 1966, writ ref’d n.r.e.).
404. The trial court, in effect, excluded affidavits offered by the lessee to show that the letter agreement was omitted by mutual mistake, that the lessee was induced to execute the lease in reliance upon the letter, that the original lessor and subsequent owners prior to the defendant had acknowledged and honored the lessee's right to renewal rebates, and that the defendant acquired the property with actual knowledge of the letter.
5. **Duty to Repair.**

Lease agreements often obligate the lessor to make repairs to the leased property, and give the lessee the right to make the repairs if the lessor fails to do so. The lease agreement in *McCreless Properties, Ltd. v. F. W. Woolworth Co.* provided that the lessor would make all exterior repairs caused by leakage or flowing of water. If the lessor failed to make the repairs within ten days' written notice from the lessee, the lessee could cure the default at the lessor's expense. Standing water on the roof over the lessee's premises, which prior repairs by the lessor failed to correct, caused the roof to collapse and resulted in substantial damage to the lessee's store. The lessor argued that its liability was limited to the cost of repairs since the lessee had the right to make the repairs and failed to do so. The trial court and the court of civil appeals disagreed and held that the lease agreement did not limit the lessor's obligation to make only the repairs demanded by the lessee or limit the lessor's liability to make the repairs.

6. **Condemnation.**

The lessee's right to compensation when the leased premises are condemned was considered in *Evans Prescription Pharmacy, Inc. v. County of Ector.* The lease agreement stated that the lease would terminate if the property was taken by eminent domain. The condemning authority paid the lessee for moving expenses and damages to trade fixtures, but because of the lease provision, refused to pay the lessee any damages for its leasehold interest. The court of civil appeals, following *United States v. Petty Motor Co.* and *Fort Worth Concrete Co. v. Texas,* affirmed the trial court's declaratory judgment and denied the lessee any recovery for the taking of the leasehold. This interpretation of such a lease provision should, however, be limited to cases where the entire premises are condemned, and should not

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405. 533 S.W.2d 863 (Tex. Civ. App.—San Antonio 1976, writ ref’d n.r.e.).
406. The lessor relied upon McCrory Corp. v. Nacol, 428 S.W.2d 414 (Tex. Civ. App.—Beaumont 1968, writ ref’d n.r.e.), and Hamblen v. Mohr, 171 S.W.2d 168 (Tex. Civ. App.—Galveston 1943, writ ref’d w.o.m.), which the court of civil appeals distinguished on the ground that the covenants in the leases before those courts required the lessor to make only the repairs demanded by the lessee. A lessee would be rightfully cautious in making repairs at the lessor's expense. See generally 2 M. Friedman, supra note 228, § 10.501a2.
407. The court noted that the lessee's right to repair at the lessor's expense was not even triggered until the lessor refused to make the repair, which it had not done, after notice from the lessee, which was never given. In fact, the court reasoned, the lessor earlier had attempted to make the repairs to the roof.
408. The court alluded to the rule that the lessor is responsible for maintaining the portion of the leased property it retains possession or control of, even if the lease did not impose this obligation, citing Brown v. Frontier Theatres, Inc., 369 S.W.2d 299 (Tex. 1963). See generally 2 M. Friedman, supra note 228, § 10.103. The lessee's remedies for breach of a covenant to repair are discussed in 51C C.J.S. Landlord & Tenant § 373(1) (1968).
410. The lessee's right to recover for fixtures is separate from his right to recover on the leasehold estate. See generally 2 M. Friedman, supra note 228, §§ 13.4, 13.5. See 29A C.J.S. Eminent Domain § 165 (1965) for discussion of a lessee's claim for damages to his business.
412. 416 S.W.2d 518 (Tex. Civ. App.—Fort Worth 1967, writ ref’d n.r.e.). The court followed the general rule, citing 2 P. Nichols, Eminent Domain § 5.23(a) (3d ed. 1976). See also 51C C.J.S. Landlord & Tenant § 98 (1968).
preclude a lessee from a recovery for a partial taking of the property.\textsuperscript{413} Lease agreements often allow the tenant to participate in condemnation proceeds, especially where there is only a partial taking. Absent any provision in the lease as to the effect of a condemnation, the lessee has a claim against the condemning authority for the value of the unexpired portion of the lease.\textsuperscript{414} It should be noted further that even under a clause such as the one present in \textit{Evans Prescription}, the lessee may be entitled to damages if the lessor consents to the taking and there is no actual condemnation.\textsuperscript{415}

B. Remedies for Breach

1. \textit{Effect of Foreclosure on Lessee’s Breach.}

In \textit{Thomas v. Morrison}\textsuperscript{416} the court considered the proper measure of damages where the lessee breaches the lease, abandons the property, and the property is subsequently foreclosed upon before the end of the lease term under a deed of trust made prior to the inception of the lease. The court held that a lessor has two remedies for the breach of a lease and the abandonment of the leased premises: (1) he may accept the breach, retake possession, and sue for damages, and if he then relets for the balance of the lease term,\textsuperscript{417} his measure of damages will generally be the difference between rentals owed under the lease and the rentals he collects from the reletting; or (2) he may elect not to accept the breach and sue for damages for the anticipatory breach without reletting or being obligated to exercise reasonable diligence to relet, in which event the measure of damages is the difference between the present cash value of the rentals owed under the lease and the reasonable cash market value of the lease for its unexpired term.\textsuperscript{418} The lessor in this case apparently elected the second remedy, but because there was no finding in the trial as to the present cash value of the rentals owed for the balance of the lease term, or as to the reasonable cash market value of the lease for the unexpired term, the court reversed and remanded the case for a new trial. The court further held that since the foreclosure under the pre-existing deed of trust terminated the rights of both the lessor and lessee,\textsuperscript{419} the lessor’s damages would be limited to a period of the lease up to the date of foreclosure.

\textsuperscript{413} \textit{See} 2 M. \textit{Friedman, supra} note 228, § 13.3, at 511.

\textsuperscript{414} 2 \textit{id.} § 13.3. But the lessor should have no liability to the lessee because of the taking. \textit{See generally} 35 \textit{Tex. Jour. 2d Landlord and Tenant} § 73 (1962).

\textsuperscript{415} It could be argued in such a case that the property was taken by voluntary conveyance, and was not taken by condemnation or the exercise of the power of eminent domain, and accordingly, that a lease provision which terminates the lease upon a taking by condemnation or eminent domain is inapplicable. There is some authority for the position that a taking by condemnation or exercise of the power of eminent domain means the taking by court proceeding and under the applicable constitutional and statutory authority, and does not apply to a voluntary conveyance. \textit{See, e.g.}, L-M-S \textit{Inc. v. Blackwell}, 149 \textit{Tex.} 348, 233 \textit{S.W.2d} 286 (1950); \textit{Texas v. Steck Co.}, 236 \textit{S.W.2d} 866 (\textit{Tex. Civ. App.—Austin} 1951, \textit{writ ref’d}); \textit{29A C.J.S. Eminent Domain} § 5 (1965).

\textsuperscript{416} 537 \textit{S.W.2d} 274 (\textit{Tex. Civ. App.—El Paso} 1976, \textit{writ ref’d n.r.e.).}

\textsuperscript{417} The lessee would be under an obligation to use reasonable diligence to relet the property. \textit{See} Evans \textit{v. Winkler}, 388 \textit{S.W.2d} 265, 269 (\textit{Tex. Civ. App.—Corpus Christi} 1965, \textit{writ ref’d n.r.e.).}


\textsuperscript{419} The lessee’s rights would not have been terminated under a deed of trust which came \textit{after} the lease, unless the lessee agreed to subordinate his rights to the deed of trust. \textit{In F. Groos & Co. v. Chittim}, 100 \textit{S.W. 1006}, 1010 (\textit{Tex. Civ. App. 1907}, no \textit{writ}), the court, in holding that a
2. Landlord’s Lien; Conversion by Lessee.

_Dill v. Graham_ 420 involved a suit by a lessor against her lessee for breach of the lease and against Keaton McCrary Cotton Co., Inc., 421 the purchaser of cotton from the lessee, for conversion of the lessor’s share of the cotton. The lessee farmed the lessor’s land under an oral agreement which provided that one-fourth of the cotton crop was to be rented to the lessor. The lessee, before the cotton crop was harvested, contracted to sell all of the crop, and subsequently refused to deliver one-fourth of the crop, or any of the cards held on the ginned cotton, to the lessor. The jury found that the lessor had not agreed that the lessee could contract the cotton for future delivery. The court of civil appeals stated that unless the lease agreement provides otherwise, the lessee owns the entire crop prior to harvest, but the lessor becomes the owner of his share when the crop is harvested. 422 To secure her right, the lessor has a statutory lien under article 5222-423 which the court held is good against a purchaser whether or not the purchaser is aware of the lessor’s right. 424 The lessor can enforce his lien either by foreclosing his lien against the cotton or by suing the purchaser for conversion. 425 The court stated that although the lessee could waive his lien by authorizing the lessee to sell the crop, 426 there was no evidence that the lessor did so in this case. Accordingly, it was held that the purchaser of the cotton from the lessee was liable for the conversion of the lessor’s share of the crop. “If a purchaser buys the crop or a part of it on which the landlord has a lien, without the landlord’s consent or authorization to sell, the purchaser is liable in conversion to the landlord to the extent of the lesser of the value of the crop converted or the amount of rent due.” 427 The purchaser was held to have a duty to determine the lessee’s authority to sell if he wants to protect himself from this liability. 428

Virtually the same facts involved in _Dill_ were present in _Keaton McCrary Cotton Co., Inc. v. Herron_, 429 but the lessor apparently chose to sue only the purchaser, Keaton McCrary Cotton Co., Inc., and the ginner for conversion of her share of the cotton crop. The purchaser, as in _Dill_, contended that the lessee had the right to sell the entire cotton crop, and in the alternative, filed a

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420. 530 S.W.2d 157 (Tex. Civ. App.-Amarillo 1975, writ ref’d n.r.e.).
422. The court cited Milligan v. Foster, 17 S.W.2d 768, 769 (Tex. Comm’n App. 1929, jdgmtn adopted) in support of this statement.
424. 530 S.W.2d at 160, citing Mathews v. Burke, 32 Tex. 419 (1870).
427. 530 S.W.2d at 160. Zapp v. Johnson, 87 Tex. 641, 30 S.W. 861 (1895), and Farmers’ Elevator Co. v. Advance Thresher Co., 189 S.W. 1018 (Tex. Civ. App.—Dallas 1916, writ ref’d), were cited by the court.
428. See Kimbell Milling Co. v. Greene, 162 S.W.2d 991, 997 (Tex. Civ. App.—Fort Worth), aff’d, 141 Tex. 84, 170 S.W.2d 191 (1943).
429. 529 S.W.2d 630 (Tex. Civ. App.—Amarillo 1975, no writ).
cross action against the lessee for damages for breach of the contract to sell the cotton. The court of civil appeals reached the same conclusions as in *Dill*, and found the purchaser to be liable for conversion of the lessor's one-fourth share of the crop. The court, however, reversed the trial court's judgment to the extent it denied the purchaser any recovery of damages against the lessee. No ambiguity was found in the contract to sell the crop, and since the lessee contracted to sell the lessor's share of the crop which he could not deliver, he was liable to the purchaser for the breach of that portion of the contract.

3. Lessor's Liability for Theft.

The liability of a lessor for the burglary of a lessee's apartment was alleged in *Knapp v. Wilson*. The court found that there was no causal connection between the loss of an unmarked apartment key by a former tenant and the burglary of the tenant's apartment. But it was recognized that in a proper case a lessor may be held liable for loss due to theft by third parties if that consequence is reasonably foreseeable by the lessor.

VI. RESTRICTIONS ON LAND USE

A. Private Restrictive Covenants

As in past years, there were several cases involving private restrictions on land use, primarily restrictive covenants in residential areas. In the 1969 case of *MacDonald v. Painter* the Texas Supreme Court held that a deed restriction which limits improvements to those "built and used for residential purposes only" does not as a matter of law prohibit the construction of a duplex. Deed restriction cases, however, generally turn on their particular facts and the language of the restriction itself. Thus, in the case of *Stephenson v. Perlitz* the Texas Supreme Court was again presented with the question of whether the construction of a duplex violated a residential deed restriction. The restriction in question provided that all improvements must be "built and used for residence purposes," but added that "[o]nly one residence shall be erected upon the premises." The court stated that this additional language was sufficient to distinguish the general rule of *MacDonald v. Painter*, and

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430. The purchaser argued that the lessee either waived her landlord's lien or was estopped to assert that the lessee had no authority to sell the entire crop, because the lessor had previously allowed the lessee to sell the crop after the harvest. The court disagreed, and stated that the fact the lessor in a previous year had allowed the lessee to sell the lessor's share of the crop after it was segregated was not evidence of the lessee's authority to contract before segregation for the sale of the lessor's share. *Id.* at 633.

431. 535 S.W.2d 369 (Tex. Civ. App.—El Paso 1976, writ ref'd n.r.e.).


433. 441 S.W.2d 179 (Tex. 1969).

434. 532 S.W.2d 954 (Tex. 1976). See *Wallenstein & St. Claire* (1976), supra note 2, at 64. On remand the court of civil appeals held that previous violations of the one-residence restriction were not such as to constitute a waiver. There were only nine violations in an addition of over 100 lots. 537 S.W.2d 287 (Tex. Civ. App.—Beaumont 1976, writ ref'd n.r.e.).

435. 532 S.W.2d at 955. The court held that the term "one residence" is not ambiguous.

436. 441 S.W.2d 179 (Tex. 1969). See text accompanying note 433 supra. The court stated that
held that the restriction prohibited the erection of a duplex.\textsuperscript{437}

In \textit{Edwards v. Southampton Extension Civic Club}\textsuperscript{438} the tract constituting the Southampton Place Extension Subdivision was conveyed by general warranty deed dated July 1, 1925, subject to certain restrictions which prevented the use of the property for business purposes. Paragraphs one and two of the deed restrictions stated that no part of the property should ever be used for business purposes of any kind. In paragraph seven, however, it was stated that "the foregoing Restrictions" were for twenty-five years, and provided that if a majority of the owners in the subdivision so desired, the restrictions could be extended for a further period of twenty-five years or less. In 1950 the deed restrictions were extended for an additional twenty-five year period. In June 1975, just prior to the expiration of the extended restrictions, a campaign was organized to obtain signatures for another extension. A majority of the homeowners agreed to a further extension, but certain homeowners refused to sign the agreement. Thereafter, the homeowners association and a number of individual homeowners brought suit against those owners who refused to sign, seeking a declaration that the deed restrictions had again been renewed. The district court held in favor of the plaintiffs, but the court of civil appeals reversed. Noting that a deed should be construed so as to ascertain the intention of the parties,\textsuperscript{439} that this intention should be gathered from the entire instrument construed as a whole,\textsuperscript{440} and that restrictions are generally construed strictly in favor of the grantee against the grantor and in favor of the free use of the property,\textsuperscript{441} the court found that paragraphs one and two were expressly made subject to the provisions of paragraph seven, the extension clause, and that the language of paragraph seven clearly contemplated a single extension of twenty-five years or less. Therefore, the court held that the deed restrictions expired in 1975 and could not be extended.\textsuperscript{442}

\textsuperscript{437} In another case decided by the Texas Supreme Court, Zmotony v. Phillips, 529 S.W.2d 760 (Tex. 1975), the restrictive covenant in question prohibited, among other things, the use of mobile homes as residences. The trial court held that the plaintiffs were not entitled to a temporary injunction compelling defendants to remove a mobile home from their property; the court of civil appeals reversed, but the Texas Supreme Court then affirmed the judgment of the trial court. While not reaching the question of waiver, the court noted that another trailer home had been located across the street from one of the plaintiffs for over three years. Additionally, the court noted that the plaintiffs had failed to show that they would suffer any irreparable harm pending trial on the merits or that defendants would incur costs of $1,000 in removing the mobile home. See Wallenstein & St. Claire (1976), supra note 2, at 65, for a discussion of the civil appeals decision. With respect to waiver, another case decided during the survey period, Fowler v. Brown, 535 S.W.2d 46 (Tex. Civ. App.—Waco 1976, no writ), reaffirmed the rule that violations of restrictions outside the area in question cannot be relied upon as a waiver. Also on the issue of waiver see Alcorn v. Brown, 536 S.W.2d 80 (Tex. Civ. App.—Fort Worth 1976, writ ref’d n.r.e.).

\textsuperscript{438} The dissenting judge took the position that the trial court found as a "fact" that the language of paragraphs 1 and 2 of the restrictions indicated that the true intent of the grantor was
Harrison v. Air Park Estates Zoning Committee\textsuperscript{443} concerns the modification of deed restrictions. Harrison purchased a lot under a contract for deed in a subdivision designed for "people who like airplanes."\textsuperscript{444} The development contemplated that those buying lots would build both a hangar and a residence on each lot. The contract for deed contained certain restrictions and provisions which stated in part that a hangar could be built prior to the construction of a home and that the restrictions would be binding until revoked or modified by three-fourths majority of the then owners of the real property. Acting under this modification provision by written agreement of over three-fourths of the property owners, the restriction was modified to provide that a home could be built with a hangar as a later addition, but that no hangar could be built prior to the construction of a home. Harrison argued that the modification was void because it was more restrictive than the original covenant. The court rejected this contention, however, finding that the modification, although more restrictive, was both consistent with the overall plan and development and reasonable.

B. Public Restrictions

There was also litigation during the survey period concerning public restrictions on land use. In Mahler v. City of Seabrook\textsuperscript{445} the city and others brought suit to enjoin the purchaser of a certain tract from violating a city zoning ordinance which restricted the use of the property to single family residences. The defendants, who had been using this property as a sand pit, relied on the doctrine of estoppel, contending that the city had used sand and other fill material from the pit in constructing city improvements and therefore should now be estopped from enforcing the zoning ordinance. The court rejected this argument, holding that an estoppel against a municipality acting in its proprietary capacity will not be allowed to defeat a mandatory provision of a statute. Thus, this act was not such as to estop the city from enforcing its zoning ordinance, a governmental function.

In Coffee City v. Thompson\textsuperscript{446} a property owner in Coffee City brought suit against the town and members of the town council to have the town zoning ordinance declared null and void, and also for a mandatory injunction for the issuance of a building permit which had been denied under the ordinance. Affirming the trial court, the court of civil appeals held that the ordinance was unconstitutionally vague because it merely described "a certain area as commercial and declared that all other property is zoned residential,"\textsuperscript{447} failed to describe what structures may be built, provided no guidelines or criteria for the town secretary to follow in granting or refusing building

\textsuperscript{443} 533 S.W.2d 108 (Tex. Civ. App.—Dallas 1976, no writ).
\textsuperscript{444} Id. at 110.
\textsuperscript{445} 538 S.W.2d 870 (Tex. Civ. App.—Houston [14th Dist.] 1976, no writ).
\textsuperscript{446} 535 S.W.2d 758 (Tex. Civ. App.—Tyler 1976, writ ref’d n.r.e.).
\textsuperscript{447} Id. at 763.
permits, and provided no appeal procedure through a zoning commission as required by article 101f. The town argued that article 974d-18, a validation statute affecting small towns, cured any failure by Coffee City to appoint a zoning commission. The court, however, rejected this contention, holding that validating acts are intended merely to cure technical procedural defects in the proceedings of city and town governments, and, as such, do not serve to excuse compliance with a mandatory duty required by statute.

VII. MISCELLANEOUS

A. Real Estate Partnerships and Ventures

Although real estate syndications have lost much of their former glamour, partnerships and joint ventures continue to be popular vehicles for group ownership of real property. While an in-depth discussion of partnership law is beyond the scope of this Survey Article, several decisions during the survey period are of interest to real estate lawyers.

In Park Cities Corp. v. Byrd the deceased general partner's capital account showed a $1,987,344.00 deficit upon dissolution of the partnership, mainly because of a special allocation to her account of depreciation on the partnership's apartment project for federal income tax purposes. The Texas Supreme Court held that this deficit was an asset of the partnership, and the estate of the general partner was required to contribute funds to bring her capital account up to zero, resulting in a tremendous windfall to Park Cities Corporation, the limited partner. To the extent that special allocations are still available under federal tax law, when drafting partnership agreements containing such allocations consideration should be given to the desired treatment of such artificial deficits upon dissolution of the partnership.

Sherrill v. Bruce Advertising, Inc. involved an advertising agency's suit against a developer with whom the advertiser had a contract for services in connection with the development of certain real property. The agency also sued the trustee of the trust which owned the property seeking to establish a

448. Id. The court reasoned that an ordinance allowing the exercise of arbitrary discretion is invalid. See Spann v. City of Dallas, 111 Tex. 350, 235 S.W. 513, 517 (1921).
450. Id. art. 974d-18 (Vernon Supp. 1976-77) provides in substance that "all . . . acts performed by the governing bodies of . . . cities and towns . . . since their incorporation . . . are hereby in all respects validated . . . ."
451. Finally, in dictum, the court hinted that the ordinance may have been motivated by a desire to advance the pecuniary interests of certain town councilmen and might be invalid on this basis as well. 535 S.W.2d at 767-68.
452. 534 S.W.2d 668 (Tex. 1976).
453. The court interpreted the partnership agreement in light of the Texas Uniform Partnership Act, TEX. REV. CIV. STAT. ANN. art. 6132b (Vernon 1970), and found that section 40(a), which includes among the assets of a partnership "the contributions of the partners necessary for the payment of all liabilities," supported the decision that Mrs. Byrd's negative capital account was an asset of the partnership. Even if correct, this result seems unfair. As a practical matter the only loss to the partnership was on paper. As general partner, with all losses and liabilities allocated to her, Mrs. Byrd bore the lion's share of the risks of the enterprise. Additionally, the language of the Texas Uniform Partnership Act can be read as referring to real money liabilities rather than mere accounting losses such as depreciation. Under this view, it could be argued that unless the partnership agreement provides that such a deficit be restored, it need not be brought up to zero upon dissolution.
455. 538 S.W.2d 865 (Tex. Civ. App.—Houston [14th Dist.] 1976, no writ).
joint venture between the developer and the trust and to hold them jointly and severally liable on the contract. The court stated that in order to constitute a joint venture it must be shown that the parties had joint control of the enterprise, participated in profits, and shared the losses of the enterprise. Since no agreement for the sharing of losses was shown, the court held that as a matter of law no joint venture existed between the trust and the developer.

The court stated that there was evidence showing that the developer was acting as the agent for the trust, which was an undisclosed principal. Citing the Restatement (Second) of Agency, section 210(1), the court held, however, that an undisclosed principal is discharged from liability under a contract if the other party, with actual knowledge of the identity of the undisclosed principal, takes a judgment against the agent who made the contract. Since the advertiser had won a final judgment against the developer, the court held that the trust was not liable as an undisclosed principal.

Section six of the Texas Uniform Partnership Act defines a partnership as "an association of two or more persons to carry on as co-owners a business for profit." In Cherokee Village v. Henderson the court held that the evidence supported the finding of the trial court that a partnership existed with respect to the ownership and management of an apartment complex, notwithstanding the fact that legal title was held by a designated trustee. The case involved an action to recover damages for personal injuries allegedly sustained by a minor when she fell into an open hole filled with scalding hot water on the premises of the Cherokee Village Apartments in Dallas. The suit was brought, however, in Harris County against Cherokee Village, alleged to be a general partnership, the trustee holding legal title to the property, and the corporation responsible for maintenance and management of the apartment complex. The plaintiffs sought to establish venue in Harris County on the basis that one of the alleged general partners resided in Harris County, arguing that the partnership continued to exist notwithstanding the fact that title to the property had been conveyed into trust for the benefit of certain individuals who were partners in the original partnership.
The court of civil appeals indicated that the evidence supported the trial court’s “implied finding” that the trust was merely a mechanism used by the co-owners to carry on the apartment business for profit. Therefore, the court found that the partnership existed at the time the accident occurred, and since one of the partners was a resident of Harris County, venue was proper in Harris County.

B. The Tax Reform Act of 1976

Extensive tax reform was enacted on October 4, 1976, and while real estate lawyers may, at first glance, feel that their practice and clients escape this extensive tax surgery with few scars, the indirect effect on real estate investments may be substantial. Obviously, this is not a survey of tax law or of the Act. Nevertheless, due to the impact of tax law on real estate transactions, mention will be made of certain provisions of the Act which apply to real estate.

The chief aim of the Act was to eliminate or reduce the tax preferences that flow from tax shelter investments. To many this meant mainly real estate tax shelters, although the Act may have a broader effect. Section 201(a) of the Act denies a deduction to individuals, subchapter S corporations, and personal holding companies for interest and taxes paid or accrued during the construction period of improvements held in a trade or business in an activity conducted for profit. These amounts must be capitalized and amortized in the manner provided in the Act. The depreciation recapture rules made applicable to non-residential rental property by the Tax Reform Act of 1969 have been extended to residential rental property, except for certain government financed or assisted residential rental property. Thus, any gain according to their respective beneficial interests. Some two years after the execution of the trust instrument, an instrument purporting to be an amendment to the earlier partnership agreement was executed. This amendment provided for the withdrawal of three of the original partners and also stated that except as amended, the original partnership agreement was to remain in full force and effect. Shortly after this amendment an assumed name certificate was filed for the name “Cherokee Village,” which certificate listed the names of individuals conducting the business in accordance with the amended partnership agreement. Beside each person’s name was the designation “general partner.” It was not until after this lawsuit was filed that the assumed name certificate was withdrawn and a new certificate of assumed name filed showing the trustee as the owner. Up until the year of suit partnership income tax returns were filed in the name of Cherokee Village.

465. 538 S.W.2d at 174.
467. Act § 201(a), adding I.R.C. § 189 [hereinafter referred to in the text as the “Code”].
468. “Carrying costs” incurred or paid before construction begins, such as taxes or interest paid or accrued while waiting for plans to be approved or for property to be rezoned, would not be affected. New § 189 applies only to construction which was started after Dec. 31, 1975, in the case of nonresidential real property, or after Dec. 31, 1977, in the case of residential real property (other than low-income housing), or after Dec. 31, 1981, in the case of low-income housing.
469. For example, if construction of a shopping center began in 1976, only 50% of the construction period interest and taxes paid in 1976 can be deducted. The other 50% must be capitalized and amortized over the three years following the date the property is first placed in service or is ready for sale. See TAX REFORM ACT OF 1976, § 118 (P-H 1976). The period over which the costs must be amortized increases by one year for each year after 1976, and over 10 years for construction commenced in or after 1982.
realized on the sale of residential rental property, regardless of how long that property has been held, will be ordinary income to the extent accelerated depreciation after December 31, 1975, exceeds straight-line depreciation. Present rules requiring that all the depreciation taken, excess or otherwise, will be recaptured as ordinary income if the property is held twelve months or less have been retained.472 For the purposes of eliminating the benefit taxpayers sometimes have won (e.g., through bankruptcy proceedings or temporary restraining orders) by delaying the foreclosure of property until a later year or years, a new section 1250(d)(10)473 has been added to the Code to require property owners whose property has been foreclosed or reconveyed to the mortgagee after default under the deed of trust to recapture the accelerated depreciation as of the date the foreclosure proceeding was begun, or on the date the operation of the agreement (e.g., deed in lieu of foreclosure) began. If the complexity and impact of the new rules for depreciation recapture are not reason enough to discourage clients from using accelerated depreciation methods, consider the fact that accelerated depreciation is a tax preference item for purposes of determining the minimum tax on individuals under Code sections 56, 57, and 58,474 and that it will reduce the already reduced benefit of the maximum tax on personal service income.475

The Act attempts to codify some of the case law regarding prepaid interest. Cash method taxpayers may deduct interest only in the taxable year in which and to the extent that interest represents a charge for the use or forebearance of borrowed money.476 After December 31, 1975,477 prepaid interest must be capitalized and deducted ratably over the term of the loan. This rule also applies to “points,” except that points paid by a cash basis taxpayer on a home mortgage (principal residence only) may be deducted in full in the year in which they are paid, provided (1) the payment of points is an established business practice in the area, and (2) the amount of the points does not exceed the amount generally charged in the area.478 Additionally, Code section 163(d)479 has been amended to limit to $10,000 plus the amount of net investment income (and certain lease expenses) the amount of investment interest a taxpayer other than a corporation can deduct in a taxable year.480

The maximum amount of losses in excess of gains which are deductible against ordinary income has been increased from $1,000 to $2,000 for tax years beginning after December 31, 1976, and to $3,000 for years beginning

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472. Act § 202(a).
474. Act § 301 is generally applicable to tax preferences for taxable years after Dec. 31, 1975.
476. Act § 208, adding I.R.C. § 461(g).
477. This limitation is not applicable to prepayments made before Jan. 1, 1977, if made pursuant to a binding contract which was in effect on Sept. 16, 1975.
478. Both of these conditions must be satisfied. Furthermore, the points must be “interest” and not payment for the lender's services. I TAX REFORM ACT OF 1976, at 51 (ALI-ABA 1976).
479. Act § 209.
480. An additional $15,000 is permitted for interest paid on indebtedness incurred to acquire stock in a corporation or an interest in a partnership by a family which has acquired or is acquiring at least 50% of that business. Excess interest can be carried forward. The House bill also sought to apply this limitation to personal expenses, such as residential mortgages, but the final version covers only investment interest.
after 1977.\textsuperscript{481} But the holding period required in order to get long-term capital gains treatment is increased from six months to nine months for tax years beginning after December 31, 1976, and to twelve months for tax years beginning after 1977.\textsuperscript{482} The treatment of gain on the sale of depreciable property transferred between related parties as ordinary income rather than capital gain under section 1239 of the Code has been extended to sales or exchanges between corporations controlled by the same individual.\textsuperscript{483} The time for replacing involuntarily converted property with like-kind property in order to defer the recognition of gain has been increased from two to three years.\textsuperscript{484} Additionally, new rules for involuntary conversion now allow taxpayers whose outdoor advertising displays are condemned to elect to treat them as real property.\textsuperscript{485}

Extensive changes were made in the limitations and requirements for real estate investment trusts (REIT).\textsuperscript{486} These changes include an increase in the percentage of gross income that must be derived from passive sources from ninety to ninety-five percent,\textsuperscript{487} a change in the definition of "rents from real property," an increase in the distribution requirement from 90% to 95%,\textsuperscript{488} a change whereby a REIT which voluntarily disqualifies itself cannot requalify for five years,\textsuperscript{489} and a change allowing corporations to qualify as REITs.\textsuperscript{490} The most significant aspect of the REIT changes is the new deficiency dividend procedure which eliminates disqualification as the penalty for inadvertent failure to meet the income qualification tests.\textsuperscript{491} The Act also removes the prohibition against holding property for sale to customers.\textsuperscript{492} Additionally, a REIT is now permitted a net operation loss deduction for loss carryovers (but not carry backs),\textsuperscript{493} and may apply ordinary losses to reduce

\textsuperscript{481} Act § 1401, amending I.R.C. § 1211(b).
\textsuperscript{482} Act § 1402, amending I.R.C. § 1222(1), (2), (3), (4).
\textsuperscript{483} Act § 2129, amending I.R.C. § 1239.
\textsuperscript{484} Act § 2140, adding I.R.C. § 1033(g)(1). The new three-year time period applies to any disposition of converted property after Dec. 31, 1974, unless the condemnation proceeding was started before Oct. 4, 1976.
\textsuperscript{485} Act § 2127, amending I.R.C. § 1033(g).
\textsuperscript{486} Act § 1604, adding I.R.C. §§ 856(f), (g), 860, and amending I.R.C. §§ 856(a), (c), (d), and 857(a)(1).
\textsuperscript{487} Act § 1604(a), amending I.R.C. § 856(c).
\textsuperscript{488} Act § 1604(b), amending I.R.C. § 856(d). Rents from real property now include amounts received for customary services, even if separate charges are made for such services, and amounts attributable to personal property incidental to rental of real property, if the amount allocable to personal property is less than 15% of total rent. Also, where a prime tenant under a percentage lease subleases to a subtenant under a percentage sublease, only a portion of the rent received from the prime tenant fails to qualify as rents from real property.
\textsuperscript{489} Act § 1604(i), amending I.R.C. § 857(a)(1).
\textsuperscript{490} Act § 1604(k), adding I.R.C. § 856(g).
\textsuperscript{491} Act § 1604(f), amending I.R.C. § 856(a).
\textsuperscript{492} Act § 1601, adding I.R.C. §§ 316(b)(3), 859, 6697, and amending I.R.C. § 857(b)(3)(c). Very generally, qualifying distributions may now be made in subsequent years under certain circumstances. New rules for failure to meet the income source tests are embodied in Act § 1602, adding I.R.C. § 856(c)(7), redesignating I.R.C. § 857(b)(5) as I.R.C. § 857(b)(7) and adding I.R.C. §§ 857(b)(5), 857(b)(2)(E). Under the new law failure to meet the income source tests will not disqualify a REIT if (1) the REIT sets forth the source and nature of its gross income on its return; (2) any incorrect information is not due to fraud with intent to evade tax; and (3) the failure to meet the income source requirements is due to a reasonable cause and not willful neglect. A 100% tax is imposed on the net income attributable to the greater amount by which the REIT fails the 75% or 90% requirements.
\textsuperscript{493} Act § 1603, deleting I.R.C. § 856(a)(4) and adding I.R.C. § 857(b)(6).
\textsuperscript{494} Act § 1606, adding I.R.C. §§ 172(b)(1)(I), 172(d)(7).
net capital gains if the alternative tax on net capital gains is not used. 495

Finally, for tax years beginning after 1979, the Act imposes an excise tax on a REIT to the extent it fails to distribute seventy-five percent of the income it is required to distribute during the year the income is earned. 496

There were several changes in partnership tax law which will affect real estate investments. One of the more notable changes, providing that the adjusted basis of a partner’s interest will not include any portion of any partnership liability with respect to which the partner has no personal liability, expressly excepts real estate partnerships other than those involved in certain farming operations and oil and gas exploration. 497 For tax years beginning after December 31, 1976, fees paid in connection with the organization of a partnership must be capitalized, and after December 31, 1976, all organizational and syndication expenses are subject to this rule. 498 Other changes include a limitation to $2,000.00 in the aggregate on the amount of additional first-year depreciation which a partnership can pass through to the partners in any tax year, 499 an allocation to a partner of income or losses only for the portion of the year he is a member of the partnership, 500 and the disallowance of any special allocation of a partner’s distributive share of gain, loss, deduction, or credit which lacks substantial economic effect. 501

Other real estate related provisions include a reinstatement of the special five-year amortization (and an increase in the maximum amount per unit that can qualify) for low-income housing, 502 changes allowing an elderly taxpayer to exclude from income the entire gain on the sale of his principal residence if the adjusted sales price is less than $35,000, 503 and changes exempting from income tax, dues, and assessments received by electing qualified homeowners associations, if the dues and assessments are paid by property owners who are members of the association and are used for the maintenance and improvement of association property, and allowing a lending institution which obtains stock in a cooperative housing corporation through foreclosure to be treated as a tenant-stockholder for up to three years. 504 Effective December 31, 1975, the Act sets forth an objective test to be applied in determining the allowable deductions for expenses related to vacation homes. 505 If a taxpayer uses the home more than fourteen days or ten percent of the number of days in the year during which the home is rented, whichever is greater, the deduction is limited to the amount by which the gross rental income exceeds expenses otherwise deductible (for example, interest, taxes

496. Act § 1605, adding I.R.C. § 4981.
500. Act § 213(c), amending I.R.C. § 706(c)(2).
503. Act § 1404, amending I.R.C. § 121(b)(1). The former limit was $20,000.
505. Act § 601, adding I.R.C. § 280A.
and casualty loss). Deductible rental related expenses are further limited to an amount based on the ratio the number of days the home is rented bears to the total number of days during the year the home is used for either personal or rental purposes. If the home is rented out less than fifteen days during the year, no income or loss is included in the taxpayer's return. For taxable years beginning after 1975, no deduction is allowed for an office in the home unless the portion of the home is used as the principal place of business for meeting or dealing with clients or customers in the normal course of business, exclusively and on a regular basis.\textsuperscript{506} If the taxpayer is an employee, the exclusive use must be for the convenience of his employer. In any event, the deductions allocated to the business use may not be more than the amount by which gross income derived from the business use exceeds the deductions allocated to such use otherwise allowable (for example, taxes, interest, and casualty losses).

The Act severely curtails special farm tax rules for farming syndications in which a substantial portion of the interest is held by taxpayers who are motivated by a desire to shelter other income.\textsuperscript{507} This amendment requires farming syndicates to deduct expenses for seed, feed, and fertilizer only when consumed, and to deduct expenses for purchased poultry only for their useful life (in case of inventory, only when disposed of). Additionally, the Act requires that in the case of a farming syndicate, amounts attributable to planting, cultivation, maintenance, or development of a grove, orchard, or vineyard incurred prior to the tax year in which the grove, orchard, or vineyard commences production in commercial quantities must be capitalized and recovered through depreciation.\textsuperscript{508} Finally, the Act adds a new provision requiring that corporations (other than certain family owned corporations and Subchapter S corporations) and certain partnerships use the accrual method of accounting for farm operations. This provision also requires such entities to capitalize their productive period expenses of growing or raising crops or animals.\textsuperscript{509}

C. The Uniform Land Transactions Act and Other Uniform Acts

In August 1975 the National Conference of Commissioners on Uniform State Laws approved the Uniform Land Transactions Act and recommended it for enactment in all states.\textsuperscript{510} The Act in its present form would codify many aspects of real property law in the areas of contracts, the remedies for breach of those contracts, security agreements affecting real property, usury, and the rights of the creditor and debtor upon default.\textsuperscript{511} The Act's stated

\textsuperscript{506} Act § 601, adding I.R.C. § 280A.
\textsuperscript{507} Act § 207(a), amending I.R.C. § 464 (effective for amounts paid in tax years beginning after Dec. 31, 1975, except for syndicates in existence on that date in which there was no change in membership during 1976, which come within the amendment after Dec. 31, 1976).
\textsuperscript{508} Act § 207(b), amending I.R.C. § 278 (effective for tax years beginning after Dec. 31, 1975, except for groves, etc., planted on or before that date).
\textsuperscript{509} Act § 207(c), adding I.R.C. § 447 (effective for tax years beginning after Dec. 31, 1976).
\textsuperscript{510} The Act with comments has been published by West Publishing Co.
purposes are to provide uniformity among the states in real property law, to modernize and simplify real property laws, and to provide special protection to homeowners. Some of the provisions of the Act are in conformity with existing Texas law, but many provisions would bring both uncertainty and drastic change to Texas real property law. The Act and the official comments thereto are derived in a very general way from the Uniform Commercial Code, which leads to the Act's most apparent shortcoming. The flexibility that may be important to parties who are dealing with personal property is not so important in a real property context. Further, this added flexibility, and the resulting uncertainty could lead to litigation in many situations where, at least in Texas, the rights of parties have been well defined for many years. The Texas Bar Section of Real Property, Probate, and Trust Law indicated its interest and concern by organizing a new committee under which real property practitioners in Houston and Dallas have been formed to study the Act.

The Section of Real Property, Probate and Trust Law of the American Bar Association has announced its opposition to the Act. The National Conference of Commissioners has requested the Section to propose written modifications to the Act by August 1977, and has agreed to consider any suggested changes. The proposed revision of Article 2 of the Act has been assigned to the Houston Real Estate Lawyers Council, and Article 1 has been assigned to a group of Dallas real estate lawyers. The reader should also be aware of other uniform acts which are in various stages of drafting, including the Uniform Simplification of Land Transfers Act and a uniform condominium act, both of which formed part of the working draft of the Uniform Land Transactions Act, but were deleted from the final draft, a uniform eminent domain code, and a uniform act for historic preservation and easements.

D. Other

By way of brief summary, some additional developments at the federal level are deserving of mention. The Federal Trade Commission has been showing signs of increased activity in the area of land sales. Its regulatory power having been expanded by the Federal Trade Commission Improvement Act, the agency will soon issue broad proposed rules defining unfair and deceptive practices in land sales and spelling out the available remedies. The proposed rules will cover sellers already subject to the Interstate Land Sales Full Disclosure Act and the filing requirements of the Office of Interstate Land Sales Registration. In addition, the Federal Insurance Administration has promulgated new regulations, effective January 1, 1976, which contain sweeping and substantive changes in the National...
Flood Insurance Program.\textsuperscript{518}

SEC Guide 60\textsuperscript{519} was finally promulgated, effective April 20, 1976. Guide 60 is intended to aid in the preparation of registration statements relating to interests in real estate limited partnerships. Several changes are made from Proposed Guide 60,\textsuperscript{520} which was originally published for comment on March 1, 1974. These changes are basically aimed at clarifying the Guide and making the information requested more concise. The necessity for obtaining an appraiser's consent has been clarified. If a specific appraisal is used in the registration statement, the appraiser would have to be named as an expert. The management section has been revised to include a description of any substantial reliance on a non-affiliate in running partnership operations, as well as information concerning the experience and compensation of the non-affiliate. These changes make it clear that in certain circumstances (e.g., an unspecified property fund), it is inappropriate to make any statement as to anticipated cash returns.

The Guide has also been amended to require specific disclosure about property only at such time as there is a reasonable probability that it will be acquired. The undertakings relating to filing information when specific properties are to be acquired by a nonspecific fund have also been changed. Finally, published for comment along with Guide 60 is proposed undertaking 21(C) under which the registrant must undertake to provide limited partners the financial statements required by Form 10-K for the first full year of operations of the partnership.

