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Security Deposits With Utilities — Debts or Pledges?

Following the general practice of utility companies, Central Power and Light Company of Corpus Christi requires from its customers a five dollar security deposit as a condition precedent to service. Although the money is not kept separate from other funds of the company, the amount is credited to the individual accounts of the customers. In accordance with both the civil and penal statutes, interest is paid on the money. When service is terminated, the customer’s account is settled, and the deposit, plus any interest, less deductions for any unpaid bills, is returned to him. Over a period of years the company accumulated a number of unclaimed and apparently abandoned deposits, which it treated as debts owed to its customers. After a deposit remained unclaimed for a period of five years, the company credited it to unearned income and paid taxes on it, relying upon the four-year statute of limitations for debts. However, all deposits are returned upon demand.

The state of Texas sought to escheat deposits more than seven years old as abandoned property, urging that the deposits were in the nature of pledges, and therefore the company’s plea of limitations could not bar recovery to the state. The trial court found that the deposits were pledges and escheated to the state. Held, reversed: Customer security deposits with utilities are in the nature of debts owed by the company to its former customers, barred from enforcement by the general four-year statute of limitations on debts, and thus not subject to escheat claims by the state. Alternatively, even if the deposits are pledges, they are barred by laches if the former customers have failed to make demand within a reasonable time of the date of discontinuance of service and thus still not subject to escheat. Central Power & Light Co. v. State, 410 S.W.2d 18 (Tex. Civ. App. 1966) error ref. n.r.e.

I. Statutory Provisions

Of principal importance in Central Power & Light Co. v. State is the characterization of security deposits as either debts or pledges as defined by the common law. Nevertheless, the court’s discussion must be understood in the context of independent but interrelated statutes.

Two Texas statutes relate specifically to the utility company practice

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4 Another holding of the court of civil appeals which will not be discussed in the body of the Note concerned certain unpaid dividends owed to persons whose last known addresses were out-of-state. The state of Texas contended that they should escheat to the state of the debtor. Central Power and Light relied upon Texas v. New Jersey, 379 U.S. 674 (1965), where the United States Supreme Court held that the situs of a debt is in the creditor, and any escheat must be to the state of the creditor’s last known address if that state has applicable escheat laws. (All of the last known addresses of the creditors to whom Central Power and Light owed dividends were in states having applicable escheat laws.) The state countered by arguing that no other state could get jurisdiction over the debtor to enforce payment, since Central Power and Light only did business in Texas. The argument seems plausible, but the same argument was rejected by the Supreme Court in denying a motion for rehearing in Texas v. New Jersey, 381 U.S. 931 (1965) (mem.). The court of civil appeals apparently was correct in holding for Central Power and Light on this issue.
of requiring a deposit as a condition precedent to service. Article 1440 requires utilities demanding security deposits to pay interest on them at the rate of six per cent per annum, and to return the deposits to their former customers, together with any unpaid interest, less any unpaid bills, when service is discontinued. Article 1054 of the Penal Code provides a fine or imprisonment, or both, for anyone violating the terms of article 1440. The deposit is not a prepayment, and the company may discontinue service without resorting to the deposit any time a customer fails to make his payments.

Escheat of abandoned personal property by the state of Texas is governed by article 3272a. The statute provides for escheat of unclaimed personal property, tangible or intangible, when the owner has been unknown for at least seven years. In order for property to be considered abandoned, the owner must assert no act of ownership during the period, and no will may be recorded or probated affecting the property. The statute is custodial in nature, because the rightful owner or his heirs may, at any time, recover from the state the property or the proceeds from its sale. Corporations holding security deposits are specifically included within the statute’s operation.

There are two statutes of limitations in Texas relating to debts: the two-year statute applying to debts evidenced orally, and the four-year statute applying to debts evidenced in writing. Ordinarily, however, unless expressly provided by statute, limitations may not be pleaded against an action by the state, including an action of escheat. Nevertheless, this may be avoided by pleading limitations against the claim which the state wishes to escheat. In Southern Pacific Transport Co. v. State the state of Texas sought to escheat unpaid wages which were unclaimed for a period of over seven years. The company pleaded limitations. The court of civil appeals held that the state could only escheat whatever right the former
employees had. As their claims were barred by the statute of limitations, the state could only recover stale claims impossible to collect. Since the state must wait at least seven years to escheat an abandoned debt, the four-year statute of limitations will always have run, making collection of an escheated debt impossible.

II. PLEDGE OR DEBT

As a pledge is not subject to limitations statutes, it is important to distinguish between a pledge and a debt. A pledge is a bailment of goods or other personal property as security for a debt or other obligation. In order for a pledge to exist in Texas there must be: (1) a pledgor and pledgee, (2) a debt or obligation, and (3) a contract of pledge. Possession of the pledged property must pass from the pledgor to the pledgee or someone for him, although legal title remains in the pledgor. The pledgee must have a lien on the property; the pledgor the right of redemption. In case of improper use of the pledged property by the pledgee, an action of conversion is the usual but not exclusive remedy of the pledgor. The pledgee may also sue for the proceeds if the chattel has been wrongfully sold, or may sue for damages for breach of contract. The remedy of the pledgor, in case of default on the principal obligation by the pledgor, is a sale of the property and satisfaction out of the proceeds, with any excess held in trust for the pledgor.

Special problems have arisen when fungibles have been bailed and under certain circumstances courts have allowed the bailor to maintain an action of conversion even when his fungibles have been mixed with like fungibles. However, from early common law money could be the subject of a bailment only if it were kept in a separate container and returned intact to the bailor. The same rule applies generally to bank deposits.

Debt, on the other hand, usually means an exchange of cash for a promise to return with interest. The term is loosely used, and a pledgee has

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19 Although limitations do not apply directly to pledges, limitations may act to bar a remedy which a pledgor would have to recover his property. See text accompanying note 22 infra for discussion of remedies. For the possible practical effects on this case of limitations barring a pledgor's remedies, see the discussion accompanying footnote 36 infra.
20 See definitions, 72 C.J.S. Pledges § 1, at 1 (1951).
24 Parks & 46th St. Corp. v. State Tax Comm'n, 295 N.Y. 173, 65 N.E.2d 763 (1946). For other definitions see 26 C.J.S. Debt § 1, at 3 (1956). In Texas it has been broadly said to be that which one person is bound to pay to another. Montgomery v. Phillips Petroleum Co., 49 S.W.2d 967 (Tex. Civ. App. 1932) error ref.
even been described as a debtor, although in Texas the distinction between a debtor and a bailee is preserved. Whether an exchange of money creates a debt or some other relationship depends primarily upon the intent of the parties, particularly as manifested by the way in which the money is to be handled. Where the transferee of money is to have unrestricted use of it, being liable to repay only a similar amount, the intent to create a debt is shown. Likewise, the payment of interest is strong but not conclusive evidence that a debtor-creditor relationship was intended by the parties making the transfer.

III. Central Power & Light Co. v. State

Central Power & Light Co. v. State is a case of first impression in Texas. In reaching its conclusion that the security deposits were debts, the court of civil appeals relied upon three arguments: (1) courts of other states hold that customer service deposits are in the nature of debts; (2) the language of the contracts between the company and its customers, as well as the language of the statutes relating to customer security deposits with utilities, shows that the intent of the parties was to create a debtor-creditor relationship; and (3) the deposits do not meet the requirements of pledges.

The court relied principally upon New Jersey v. Atlantic City Electric Co., the facts of which are nearly identical to those of Central Power & Light Co. v. State. The New Jersey court concluded that the commingling of the deposited money with the other funds of the company, plus the payment of interest as required by regulation, showed that the relationship of the company to its customers was that of debtor to creditors. The court was influenced by the reasoning that intent that the deposits be considered debts could be inferred from the state requirement of interest. Since in Texas payment of interest is required by both criminal and civil statutes, this is a stronger indication that intent to create a debtor-creditor relationship should be imputed to the parties.

The court of civil appeals also relied upon Commonwealth v. Kentucky Power & Light Co., where the company was tried under a penal statute requiring utilities to pay interest on the security deposits at the end of each year. The company had been accruing interest on the deposits. Affirming a verdict of not guilty, the court characterized the deposits as demand loans. Thus interest would not be due until the loan was demanded, and the accrual method would be an acceptable method of treating interest. The

29 Thomas v. Waters, 142 Pa. 125, 18 A.2d 872 (1941).
33 Janner v. Langdeau, 317 S.W.2d 787 (Tex. Civ. App. 1958) error ref. n.r.e. See Restatement (Second) of Trusts § 12, comment g at 37 (1959).
35 Id.
36 257 Ky. 66, 77 S.W.2d 395 (1934).
reason for characterizing the deposits as demand loans was that a depositor could have his deposit returned to him at any time. Of course, this is true, but only upon severance of service. The reasoning in Kentucky Power & Light seems weak, since even if the deposits were termed pledges, a customer would be entitled to a return of his deposit upon severance of service.37

After consideration of out-of-state decisions the court of civil appeals turned its attention to the intent of Central Power and Light and its customers regarding their security arrangements. The court found that “the intent shown is that the customer would have a matured right to a refund of an amount of money equivalent to the deposit, or the balance of it, after discontinuance of service and settlement of the account. Under these conditions, the obligation of the company is nothing more than to pay a simple debt.”38 In the contracts between the company and its customers, and in the statutes relating to the deposits, the time for settlement of a customer’s account is the time of discontinuance of service. Looking at the relationship of the parties at that time, the obligation of the company would simply be to pay the customer an amount of money equal to his deposit, plus interest, less any unpaid bills. The obligation of a debtor on the date the money becomes due is nothing more than to pay money plus any interest due, so the court apparently felt that the relationship of the parties fell squarely into the category of debtor to creditor.

The key word in the portion of the court’s opinion quoted above is the word “amount.” By agreeing to accept an amount of money at termination of service, the customers implicitly authorized Central Power and Light to commingle their deposits with other funds of the company and to use the money as its own (while of course paying interest). The manifest intention expressed by so agreeing was that a debtor-creditor relationship be established.39 That the subjective intent of the parties was not to create a loan arrangement is immaterial, for when money is commingled with other money, its identity disappears, and a debtor-creditor relationship is formed.40

As the court in Central pointed out, the terms of the statutes relating to the transactions between the parties would by operation of law be incorporated into the contracts between them.41 The intent of the legislature regarding the character of the deposits is therefore important, though difficult, to determine. Legislative requirement of interest payments on the deposits is evidence of a debt.42 Yet in Texas article 1054 of the Penal Code provides that violation of article 1440, requiring return of the de-

37 The state of Texas relied heavily upon Brooklyn Borough Gas Co. v. Bennett, 154 Misc. 106, 277 N.Y.S. 203 (Sup. Ct. 1935), a New York trial court decision holding that a security deposit with a utility was not a debt and escheated to the state unaffected by limitations. However, nowhere in the opinion is the deposit termed a pledge.
38 Central Power & Light Co. v. State, 410 S.W.2d 18, 23 (Tex. Civ. App. 1966) error ref. n.r.e.
41 Winder Bros. v. Sterling, 118 Tex. 268, 12 S.W.2d 127 (1929).
42 See text accompanying note 34 supra.
deposits (with interest), can result in a jail sentence for the transgressor. Since article I, section 18 of the Constitution of Texas prohibits a jail sentence for failure to pay a debt, it logically follows that the legislature could not intend for the deposits to be characterized as debts. Interest payments not being conclusive evidence of a debt relationship, the most consistent interpretation of legislative "intent" is that the deposits are something other than debts. While in all likelihood the legislature never considered the problem, this interpretation is the only way to reconcile the statutes with the constitution. Thus there is apparently an irreconcilable conflict between legislative "intent" and applicable case law regarding the nature of the deposits.

Finally, the court of civil appeals decided that the deposits did not meet the requirements of pledges. Because of the commingling of the deposits with other funds of the company, title to the money had passed, there was no lien on the specific money, and the remedy of conversion was not available to the depositors. The court relied upon the case of Story v. Palmer, which held that money, unlike other fungibles, can be the subject of conversion only when it can be described or identified as a specific chattel. From its nature the title to money passes upon delivery, its identity lost by being changed into other money or its equivalent. The court of civil appeals thereby preserved the common law notion that money may not be the subject of a pledge unless kept separate and identifiable from other money.

But even should the deposits be pledges, the court reasoned, still the state should not be allowed to escheat them. Limitations, said the court, do not begin to run on each customer's deposit until his cause of action against the company for the return of his deposit is complete. The court reasoned that each customer's cause of action was not complete until demand had been made. Nevertheless, in such a case a plaintiff may not unduly delay the start of the running of the statutes of limitations by neglect or procrastination. Unreasonable delay is generally held to be the period of the statutes of limitations. Failure to make demand within this period, then, would serve to bar the customer's right of recovery. This would, in turn, serve to bar the recovery of the state in escheat proceedings.

The reasoning of the court in arriving at its alternative holding appears to be in error, although the rule of law cited is correct: if demand by the plaintiff is the only act necessary to perfect his cause of action such demand

44 See text accompanying note 33 supra.
45 Possibly the courts will continue to ignore the conflict of article 1054 of the Penal Code with article I, § 18 of the Texas Constitution until a case arises under the statute. No case has arisen yet. If a court is again called upon to characterize security deposits, constitutional implications may be avoided on the ground that the statute provides the alternative of a fine instead of imprisonment, and so is not conclusive of legislative intent.
48 Jackson v. Tom Green County, 208 S.W.2d 115 (Tex. Civ. App. 1948) error ref. n.r.e.
50 See text accompanying note 17 supra.
must be made within a reasonable time after the obligation becomes due. However, the requirement of demand for the return of pledged property is satisfied by performance or tender of performance of the principal obligation. If at that time the pledgee refuses or is unable to return the pledged property, the pledgor’s cause of action is complete. Since in this case all the customers had either fully performed or had their obligations satisfied out of their deposits, it would seem their causes of action are complete.

In the alternative holding the court has taken the law of demand loans and applied it to pledges. Although it does not say so, the court has transformed a pledge arrangement into a debt arrangement at the time of termination of service. This cannot be done. If a customer made his deposit as a pledge at commencement of service, whatever was due him at termination of service was also a pledge. No authority has been found for the proposition that a pledge may be transformed into a debt. Even the excess of a sale of the pledged property—an amount of money—is not a debt owed by the pledgee to the pledgor, but is an amount of money held in trust for him. If limitations are to bar recovery of a pledge by the state, it must be for some other reason than that demand was unreasonably delayed.

The concept of a pledge of money commingled with other money is contrary to general common law principles. Assuming that the commingling does not automatically amount to conversion of the pledged property, perhaps by analogy with cases involving bailments of fungibles, recovery by the state might still be barred. Although there is no statute of limitations applying to suits to recover pledged property, there are statutes of limitations applying to the causes of action a pledgor may pursue for wrongful use of his pledge. Thus it might be found that Central Power and Light had converted the deposits when it failed to return them upon termination of service. As each cause of action for conversion arose, the customer affected would have had to bring his suit within two years. Should a customer have elected to sue on the contract, he would have had to bring his action within four years from the date of breach. And if by some
stretch of the imagination the company could be deemed to have wrong-
fully "sold" the deposits to itself, a customer would have had to sue for the
"proceeds" within a reasonable time measured from the date of the "sale."\textsuperscript{56}
As each deposit was at least seven years old measured from discontinuance
of service, limitations or laches could properly be held to bar recovery by
the customers, and the state would again only escheat stale claims.\textsuperscript{59}

IV. Conclusion

The court of civil appeals has probably reached the best solution to the
problems presented by this case. The decision is in line with authority in
other jurisdictions, including the very similar New Jersey decision. It also
follows the long line of cases holding that money which is mixed with
other money is the subject of a debtor-creditor relationship. Enforcing
limitations against the state also prevents the unlikely avoidance of the
limitations statutes: a former customer, denied his claim by the utility
company four years after severance of service, could wait until the state
escheated his deposit and recover it under article 3272a. In addition, to
force a company to pay from present funds money which as long ago as
forty years was put into operations may be regarded by some as a harsh
remedy.

The court’s opinion would have been strengthened had it dealt in some
manner with the constitutional question. Are deposits with utilities debts
which must be paid in order to avoid a possible jail sentence? Perhaps the
court should simply have admitted that the deposits are hybrids, partaking
of some elements of a pledge and some elements of a debt. More problems
would probably be raised than solved, however, since there is no law dealing
with such a creation. The best solution seems to be the one the court
reached: declare the deposits to be debts, and let the constitutional ques-
tions be dealt with whenever a case arises under article 1054.\textsuperscript{60}

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date of conversion. See note 55 supra. Should date of breach be considered the date the accounts
were credited to unearned income, any account less than nine years old would not yet be barred by
limitations, and would thus escheat to the state. The number of accounts affected would be small,
and how a court would decide whether to apply conversion limitations or contract limitations is
unknown.\textsuperscript{58}


The state made two other arguments: (1) The company was under an absolute duty, under
the language of the statute, to return the deposits to its customers upon termination of service, and
limitations could not relieve the company of the duty. The court of civil appeals dismissed this
argument on the ground that the legislative history of art. 3272a showed that there was no such
duty in an escheat case, and that limitations could be pleaded to bar recovery of the claims which
the state was trying to escheat. Central Power & Light Co. v. State, 410 S.W.2d 18 (Tex. Civ. App.
1966) error ref. n.r.e. Another argument is that limitations apply unless the duty of return is
strictly statutory in origin. In this case the company would have a duty to return the deposits
861 (1957). (2) By returning some deposits to former customers after limitations had run, the
company waived limitations as to the other deposits, and showed that its plea of limitations against
the state was merely a subterfuge to circumvent the provisions of article 3272a. The court of civil
appeals rejected the argument for the reason that it would engraft an exception onto the statutes
of limitations, and exceptions to statutes of limitations are not to be implied. It also seems clear
that each customer’s claim was a separate cause of action, and would not affect the causes of action
of the customers whose deposits have not been returned. Central Power & Light Co. v. State, 410
S.W.2d 18 (Tex. Civ. App. 1966) error ref. n.r.e.

See note 45 supra.