INS AND OUTS OF DEED OF TRUST FORECLOSURES

Practical Tips for the Practitioner

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Ins and Outs of Deed of Trust Foreclosure
Practical Tips for the Practitioner
by William H. Locke, Jr.

The following article is not intended to be an all inclusive discussion of the law or the practice relating to foreclosure under deeds of trust in Texas. The topics covered are a collection of both some basic topics encountered in all foreclosures (for example, where to conduct the sale and what needs to be included in the notice) and other unusual but all too frequently encountered topics (what if the debtor is in the military?, what if the debtor is deceased at the time of sale?, what happens if the debtor does not pay its property taxes?, what do you do if the debtor calls and advises before the foreclosure sale that it has a contract to sell the property that will blow up if you do not postpone the sale?, how long due you have to give a bidder to come up with the cash?). These materials are a "work in progress" as they are taken from the draft of the Texas Foreclosure Manual (2005) to be published later this year by the State Bar of Texas. This work in progress began in the 1980's when we represented various financial institutions in the Gulf Coast region of Texas. As lending decreased and loan defaults increased, our practice shifted in part from negotiating and drafting loan documents to loan workouts and foreclosures. I recall the feelings I had as I drove the streets of the business sector of my home town and knew of or had a story about many of the properties I passed. Out of this experience grew a degree of "expertise," the kind I guess that the executioner had in France at the time of the fall of the monarchy. The idea about putting this experience in written form grew from our experience in not finding a good source that connected the law, as explained in Texas Jurisprudence, with the practice, as documented in the Bar Forms Manuals. This article does not have attached to it the "forms." For those you will have to purchase the Texas Foreclosure Manual.

1. Status of the Secured Loan

1.1 Contract Rights Restricted by Statute.

Although the deed of trust reads as if it were a conveyance of the title to the mortgaged property and perhaps the collateral to the trustee "in trust," Texas law recharacterizes the transaction as creating merely a nonpossessory lien on the mortgaged property in favor of the mortgagee. The mortgagee is granted a power of sale exercisable through the trustee. Neither the trustee nor the mortgagee is deemed to have any present right of possession or legal title to the mortgaged property or collateral. *Johnson v. Snell,* 504 S.W.2d 397 (Tex. 1973); *Humble Oil & Refining Co. v. Atwood*, 244 S.W.2d 637 (Tex. 1951). Additional authority on the nature of the deed of trust includes *Carroll v. Edmondson*, 41 S.W.2d 64 (Tex. Comm'n App. 1931, judgm't adopted); *Armenta v. Nussbaum*, 519 S.W.2d 673 (Tex. Civ. App.—Corpus Christi 1975, writ ref'd n.r.e.); *Tarrant Savings Association v. Lucky Homes, Inc.*, 379 S.W.2d 386 (Tex. Civ. App.—Fort Worth 1964), rev'd on other grounds, 390 S.W.2d 473 (Tex. 1965); *Pioneer Building & Loan Association v. Cowan*, 123 S.W.2d 726 (Tex. Civ. App.—Waco 1938, writ dism'd judgm't cor.); *Texas Loan Agency v. Gray*, 34 S.W. 650 (Tex. Civ. App. 1896, writ ref'd). The deed of trust is regarded as a contract binding the mortgagor, the trustee, and the mortgagee, also referred to as the beneficiary. The deed of trust usually is executed by the mortgagor only and not the trustee and the beneficiary. The deed of trust typically contains numerous covenants by the mortgagor (*e.g.*, payment of taxes, maintenance of insurance), the conditions permitting the mortgagee to cause the mortgaged property to be sold (*e.g.*, definitions of default), and the procedures to be followed (*e.g.*, acceleration, notices, waivers, substitutions of trustees, and advertisement of sale). Texas law does not condone extra-judicial seizure of mortgaged real property by the mortgagee, unless the property is voluntarily relinquished by the mortgagor. In other words, Texas does not recognize "self-help repossession" of real estate. The Texas Property Code instead provides an orderly means for resolving disputes. Sometimes security agreements contain provisions authorizing the secured creditor to go on to a debtor's property to take possession of personal property collateral if this can be done without a breach of the peace. In the absence of a similar provision as to real property mortgaged as collateral, absent grounds for a receivership or injunction preforeclosure, the mortgagee's remedy is to seek nonjudicial or judicial foreclosure of its mortgage lien. *Lighthouse Church of Cloverleaf v. Texas Bank*, 889 S.W.2d 595 (Tex. App.—Houston [14th Dist.] 1994, writ denied). The procedures set forth in section

51.002 of the Texas Property Code are generally mandatory and nonwaivable. *See* Tex. Prop. Code Ann. § 51.002 (Vernon Supp. 2004). If the deed of trust conflicts with the statute, the statute controls. The conditions to exercising the power of sale and the manner of exercising the sale may be made more restrictive or burdensome by contract than the statute provides. *See Ford* v. *Emerich,* 343 S.W.2d 527 (Tex. Civ. App.—Houston 1961, writ ref'd n.r.e.); *Faine v. Wilson,* 192 S.W.2d 456 (Tex. Civ. App.—Galveston 1946, no writ). Foreclosure transfers title from the debtor to another party, but it does not put the new owner in possession; it gives him a right to possession. If a debtor remains on the property, most deeds of trust treat him as a tenant by sufferance. To remove a tenant at sufferance, the new owner must file a forcible detainer suit.

1.2 Identifying the Secured Debt

The deed of trust may secure a variety of obligations.

There appear to be no Texas cases on whether or not a deed of trust can secure contingent obligations. One commentator has argued that Texas courts will uphold the validity and superior priority of such liens. Danilowicz, *Validity of a Deed of Trust Securing Contingent Obligations (Mortgages for Future Advances and Standby Letters of Credit),* 50 Tex. B. J. 1086 (1987). The court in *Taylor v. Transcontinental Properties,* 739 S.W.2d 873 (Tex. App.—Tyler 1987, no writ), held that a note and deed of trust given to secure a mortgagor's performance of obligations under a contract were supported by adequate consideration as a matter of law. Taylor had contracted with Transcontinental to purchase notes generated in Transcontinental's time–share sales program. In the note sales agreement, Transcontinental agreed to execute a deed of trust "[t]o guarantee [its] performance under the commitment and to assure SMSC that all taxes, insurance and maintenance costs are timely paid." *Taylor*, 739 S.W.2d at 877. Transcontinental executed a deed of trust to ensure its performance of the note sales agreement "and to further ensure the endorsement of all notes sold by Grantors [Transcontinental] to Beneficiary [Taylor]." *Taylor*, 739 S.W.2d at 877.

1.3 Payment Terms and Payment Default

There are at least three common forms of debt instruments: demand note, term note, and installment note. See M. Baggett, 15 Texas Practice, *Texas Foreclosure Law and Practice* § 1.01 *et seq.* (2001 & Supp. 2004).

1.3:1 Payable on Demand

Section 3.108(a) of the Texas Business and Commerce Code defines payable on demand:

> (a) A promise or order is "payable on demand" if it: (1) states that it is payable on demand or at sight, or otherwise indicates that it is payable at the will of the holder; or (2) does not state any time of payment.

Tex. Bus. & Comm. Code Ann. § 3.108(a) (Vernon 2002). A demand note is matured on demand by the holder. However, one case has held that "[a] demand note is due from the moment of execution and actionable immediately without demand." *Stavert Properties v. RepublicBank of Northern Hills,* 696 S.W.2d 278, 281 (Tex. App.—San Antonio 1985, writ ref'd n.r.e.). A note containing "on demand" language may be construed as not being a demand note, if the acceleration language contains explicit conditions of default. *Bank One, Texas, N. A. v. Taylor*, 970 F.2d 16 (5th Cir. 1992).

Formal demand for payment and failure to pay must occur on a demand note before commencement of the foreclosure process. The demand feature of the note involves a number of issues that have not been extensively dealt with by state and federal courts. In *Conte v. Greater Houston Bank,* 641 S.W.2d 411 (Tex. App.—Houston [14th Dist.] 1982, writ ref'd), the court held that language providing for payment on demand, but if no demand was made, in monthly installments with a fixed maturity date was payable in full at time of demand, notwithstanding the provisions concerning monthly payments. *Conte* was followed by *Stavert Properties, Inc. v. RepublicBank of Northern Hills*, 696 S.W.2d 75 (Tex. App.—Dallas 1983, writ ref'd n.r.e.), the court interpreted the phrase "on demand and if no demand is made, then on December 1, 1922" as making the note a demand instrument.

However, a subsequent Fifth Circuit case has distinguished and declined to follow the *Conte* case. In *Bank One Texas, N. A. v. Taylor,* 970 F.2d 16 (5th Cir. 1992), the Fifth Circuit interpreted a promissory note which stated,

> This obligation is, as an alternative to the above recited payment schedule, due and payable on demand.

The note also contained default provisions and acceleration clauses whereby the bank could accelerate the note on the occurrence of an event of default. In addition, the security interests securing the note listed various events of default which would allow the bank to declare the entire obligation immediately due and payable. The lender argued, citing *Conte* that this instrument was a demand note. The Fifth Circuit distinguished *Conte* on the grounds that, first, the note in *Conte* did not contain an acceleration clause and apparently was not accompanied by an underlying security agreement or terms which would modify the right of demand.

> [H]ere, in contrast, the existence of explicit conditions of demand in the acceleration clause, as well as the related security agreements, shows a clear intention that the note be payable on demand only in the event Taylor failed to meet the installment obligation or the obligations imposed by the security agreement.

Citing to the opinion of the First Circuit in *Reid v. Key Bank of Southern Maine, Inc.*, 821 F.2d 9 (1st Cir. 1987), the Fifth Circuit held that the presence of such conditions in the documents qualified the demand provision and that,

> Based upon the testimony and our reading of the loan documents, we determine that although these notes profess to be demand instruments, a fair reading of the notes and related security agreements demonstrates an intention that these installment notes be payable on demand only in the event of default. This construction comports with the common expectation that a promissory note with an installment feature and an acceleration clause is a time obligation and that the bank does not have the right to demand payment in the absence of default.

In view of the conflict between the state and federal case law, the terms of the entire loan transaction should be reviewed before making demand on a "demand" note.

Some commentators have raised a question as to the breadth of the language in Tex. Prop. Code Ann. § 51.002(d) (Vernon Supp. 2004) that

> the debtor must be given at least 20 days to cure the default before the entire debt is due and notice of sale is given.

Unquestionably, this provision overrides any waiver or express demand feature without notice contained in a deed of trust encumbering a debtor's residence.

Giving maker and mortgagor advance notice of the mortgagee's intention to demand payment of a demand note may be advisable. The trend in some jurisdictions is to find a special relationship between the parties or an implied contractual obligation of "good faith and fair dealing." For example, the Sixth Circuit, applying New York law, upheld a jury verdict for $7,500,000 against Irving Trust Company for its breach of an implied obligation of good faith and fair dealing in refusing to advance additional credit under a line–of–credit note that was payable on demand. *K.M.C. Co. v. Irving Trust* Co., 757 F.2d 752 (6th Cir. 1984). The Sixth Circuit found support for its position in chapter 2 of the UCC, which deals with sales agreements. (See Tex. Bus. & Comm. Code Ann. § 2.309 comment (Vernon 1994) for the equivalent section of the Texas UCC.) The Sixth Circuit held that

> the application of principles of good faith and sound commercial practice normally call for such notification of the termination of a going contract relationship as will give the other party reasonable time to seek a substitute arrangement.

K.M.C., 757 F.2d at 759.

1.4 Default - Insecurity.

Texas Business and Commerce Code § 1.309 provides that when a contract allows a party to accelerate payment of a note "when he deems himself insecure," the lender may do so only

> if he in good faith believes that the prospect of payment or performance is impaired. The burden of establishing lack of good faith is on the party against whom the power has been exercised.

Tex. Bus. & Comm. Code Ann. § 1.309 (Vernon Supp. 2004). The comments to the Section, however, clearly state that the good faith requirement is not applicable to a demand note:

> Obviously, this section has no application to demand instruments or obligations whose very nature permits call at any time with or without reason. This section applies only to an agreement or to paper which in the first instance is payable at a future date.

Under Texas Business and Commerce Code § 1.201(20), *good faith* means "honesty in fact and the observance of reasonable commercial standards of fair dealing." Tex. Bus. & Comm. Code Ann. § 1.201(20) (Vernon Supp. 2004). The Texas Supreme Court has held that the obligation of good faith imposed under Texas UCC § 1.203 (the predecessor to Texas UCC § 1.201(20)) may be breached only by a showing of dishonesty by the creditor, and that the test for "honesty in fact" under Texas UCC § 1.108(19) (now Texas UCC § 1.201) did not include diligence or negligence. *FDIC v. Coleman*, 795 S.W.2d 706 (Tex. 1990). Texas does not recognize a common law duty of good faith and fair dealing in every contract, and such duty arises only if there is a "special relationship" between the parties. *Arnold v. National County Mut. Fire Ins. Co.,* 725 S.W.2d 165 (Tex. 1987).

Where a security instrument authorizes a creditor to accelerate maturity when the creditor deems itself insecure, the insecurity may be found as to the debt itself or as to the collateral. *Jack M. Finley, Inc. v. Longview Bank & Trust Co.,* 705 S.W.2d 206 (Tex. Civ. App.—Texarkana 1986, writ ref'd n.r.e.). Texas courts generally state that "good faith" must be decided on a case by case basis after acceleration has occurred. *American Bank of Waco v. Waco Airmotive, Inc.,* 818 S.W.2d 163 (Tex. App.—Waco 1991, writ denied), citing to *Ford Motor Credit Co. v. Powers,* 613 S.W.2d 30 (Tex. Civ. App.—Corpus Christi 1981, no writ) and cases cited therein. These cases suggest that the question is decided by fact issues, but in the *Finley* case, the court granted summary judgment on the good faith issue to the lender by finding that "uncontroverted sworn evidence" that the debtor had threatened bankruptcy, was a sufficient basis to establish the Bank's good faith in exercising an insecurity clause, notwithstanding that the $750,000 loan at 11% interest was secured by a $750,000 CD bearing 9% interest.

In *American Bank of Waco v. Waco Airmotive, Inc.,* 818 S.W.2d 163 (Tex. App.—Waco 1991, writ denied), the court stated that insecurity clauses are to be used only to protect the creditor from actions by the debtor which jeopardize or impair the security, and not offensively for the commercial advantage of the creditor. *Id.* at 72, citing to *Brown v. Avemco,* 603 F.2d 1367 (9th Cir. 1979). In this case, the borrower and the lender entered into a promissory note combining and renewing several loans held by the lender at a time when the borrower was delinquent on several installments on a separate SBA loan also held by the lender. Two weeks later, notwithstanding that no material change had occurred to the borrower's financial situation and that the lender had just agreed to consider the borrower's proposal for restructuring the delinquent SBA loan, the lender accelerated the delinquent SBA loan under an insecurity clause, cross-defaulted the renewal note, and then offset the borrower's checking account to pay off the renewal note in full and the delinquent installments on the SBA note. The court in *Airmotive* found the lender's acceleration of the note's maturity and offsetting of borrower's checking account was wrongful and found lender's reliance on an insecurity clause to be misplaced.

1.5 Identifying the Security

Before writing the first demand letter or notice of intent–to–accelerate letter, the types of collateral securing the obligations should be identified. This first step is to verify perfection of security interests, to determine if the loan is secured by the intended mortgaged property and collateral, and to avoid the assertion of impermissible claims on homestead–exempt assets.

1.5:1 Personal Property

The deed of trust may expressly encumber both real property and personal property. The *Texas Real Estate Forms Manual* contains at Clause 15-9-9 suggested language for inclusion in the

deed of trust as to the creation of a lien as to such mixed collateral. Clause 15-9-9 provides

> In addition to creating a deed-of-trust lien on all the real and other property described above, Grantor also grants to Lender a security interest in all of the above-described personal property pursuant to and to the extent permitted by the Texas Uniform Commercial Code.

See below for additional language suggested in the *Texas Real Estate Forms Manual* specifying that Lender may elect to proceed as to both the real property and personal property in a unified deed of trust lien foreclosure sale.

The Texas Uniform Commercial Code, as set out in the Texas Business and Commerce Code, provides an option to the lender if the deed of trust covers both real and personal property. Texas UCC § 9.604(a) (Vernon 2002). A lender may proceed against the personal property under the personal property foreclosure provisions of the Texas UCC as if there is no real property involved, or the lender may elect to foreclose on both real and personal property pursuant to section 51.002 of the Texas Property Code. If the personal property is foreclosed under section 51.002, then the provisions of subchapter F of the Texas UCC covering default do not apply.

Comment 2 of §9.604 states:

> In the interest of simplicity, speed and economy, subsection (a) like former Section 9.501(4), permits, (but does not require), the secured party to proceed as to both real and personal property in accordance with its rights and remedies in respect of the real property. Subsection (a) also makes clear that a secured party who exercises rights under Part 6 with respect to personal property does not prejudice any rights under real property law.

Tex. Bus. & Comm. Code Ann. § 9.604 comment 2 (Tex. UCC) (Vernon 2002).

This election between real property and personal property foreclosure procedures is set out in Clause 15-9-9 to the form of Deed of Trust in *Texas Real Estate Forms Manual* Ch. 15, p. 15-50 immediately following the above-quoted language as to dual deed of trust and security interest liens in mortgaged property. This clause provides:

> [If the security agreement covers nonfixtures and other personalty, continue with the following.]
>
> In the event of a foreclosure sale under the deed of trust, Grantor agrees that all the Property may be sold as a whole at Lender's option and that the Property need not be present at the place of sale.

Other states, most notably California, have attempted to reconcile seemingly conflicting real property and personal property foreclosure rules. California replaced the one–sentence provision of former U.C.C. § 9–501(d) with a seven–paragraph treatment of what had become known in California as the "mixed collateral problem." Cal. Comm. Code § 9501(4); see Hetland & Hansen, *The "Mixed Collateral" Amendments to California's Commercial Code—Covert Repeal of California's Real Property Foreclosure and Antideficiency Provisions or Exercise in Futility?,* 75 Calif. L. Rev. 185–216 (1987); Hirsh, Arnold, Rabin & Sigman, *The U.C.C. Mixed Collateral* Statute—Has *Paradise Really Been Lost?, 36* UCLA L. Rev. 1–81 (1988). In *Van Brunt v. BancTexas Quorum, N. A.,* 804 S.W.2d 117 (Tex. App.—Dallas 1990, no writ) the court relied upon this section of the Texas UCC to justify not extending the rule announced in *Tanenbaum v. Economics Laboratory, Inc.*, 628 S.W.2d 769 (Tex. 1982) eliminating deficiencies after a defective personal property foreclosure sale to bar a subsequent real property foreclosure sale or suit for deficiency after the subsequent real property foreclosure sale.

> In a case of first impression in Texas, we find that, as both real and personal property secured the note, [Lender] had the option under section 9.501(d) [now § 9.604 of the Texas Uniform Commercial Code] to proceed under that Code as to the personal property, and later proceed under the Texas Property Code as to the real property, without being adversely affected by any defects in its personal property foreclosure proceedings.

Van Brunt, 804 S.W.2d at 127.

> We hold that any defect in [Lender's] foreclosure under the Code has no effect on its rights under the real property mortgage, including its right to seek a deficiency.

Van Brunt, 804 S.W.2d at 129-30. The defect in *Van Brunt* was the failure of the lender to re-notify the debtor that the lender would sell the collateral at a private sale after the lender held a public sale but rejected the highest bid and later sold to the highest bidder at private sale for a higher price. Additionally, the debt in *Van Brunt* was a series of notes each guaranteed by a guarantor and secured by separate security agreements granting a security interest in accounts, inventory and equipment to secure all indebtedness of the borrower to the lender. One of the notes of the borrower expressly stated that it was secured by a deed of trust but did not refer to any of the security agreements.

Complicating this issue as regards to real property foreclosures is the fact that the *Tanenbaum* rule appears to have been overturned in non-consumer personal property foreclosure cases by Texas legislature's adoption of the revised chapter 9 to the Uniform Commercial Code. Texas Business and Commerce Code § 9.626 provides that in non-consumer transactions, a secured party need not prove compliance with the provisions of subchapter F ("Default") relating to collection, enforcement, disposition, or acceptance unless the debtor or a secondary obligor places the secured party's compliance in issue. Tex. Bus. & Comm. Code Ann. § 9.626(a)(1) (Vernon 2002). If the secured party's compliance is placed in issue, the secured party has the burden of establishing that the collection, enforcement, disposition, or acceptance was conducted in accordance with subchapter F. Tex. Bus. & Comm. Code Ann. § 9.626(a)(2) (Vernon 2002). Except as otherwise provided in Section 9.628, if a secured party fails to prove that the collection, enforcement, disposition, or acceptance was conducted in accordance with the provisions of subchapter F, the liability of a debtor or a secondary obligor for a deficiency is limited to an amount by which the sum of the secured obligation, expenses, and attorney's fees exceeds the greater of: (i) the proceeds of the collection, enforcement, disposition, or acceptance; or (ii) the amount of proceeds that would have been realized had the noncomplying secured party proceeded in accordance with the provisions of subchapter F. Tex. Bus. & Comm. Code Ann. § 9.626(a)(3) (Vernon 2002). For this purpose, the amount of proceeds that would have been realized is deemed equal to the sum of the secured obligation, expenses, and attorney's fees unless the secured party proves that the amount is less than that sum. Tex. Bus. & Comm. Code Ann. § 9.626(a)(4) (Vernon 2002). If a deficiency or surplus is calculated under § 9.615(f), the debtor or obligor has the burden of establishing that the amount of proceeds of the disposition is significantly below the range of prices that a complying disposition to a person other than the secured party, a person related to the secured party, or a secondary obligor would have brought. Tex. Bus. & Comm. Code Ann. § 9.626(a)(5) (Vernon 2002). Section 9.626 further provides that its limitation to transactions other than consumer transactions is intended to leave to the court determination of the proper rules in consumer transactions, but that "the court may not infer from that limitation the nature of the proper rule in consumer transactions and may continue to apply established approaches." Tex. Bus. & Comm. Code Ann. § 9.626(b) (Vernon 2002). *See also Huddleston v. Texas Commerce Bank—Dallas,* 756 S.W.2d 343 (Tex. App.—Dallas 1988, writ denied) (court refused to require mortgagee to prove that its deed of trust lien foreclosure sale on real property was conducted in commercially reasonable manner, citing (former) section 9.104(10) that excepts from chapter 9 of Texas Business and Commerce Code "creation or transfer of an interest in or lien on real estate").

If the security includes personal property, such as equipment or consumer goods (stoves, furniture), a UCC search should be conducted to determine initial perfection, continued perfection, priority, and junior security–interest holders to be notified. The secured creditor is required to notify other secured creditors with security interests in the same collateral of the proposed personal property foreclosure sale. Tex. Bus. & Comm. Code Ann. § 9.611 (Vernon 2002). The presence of personal property may also affect the type of requests in the initial communication to the debtor (*e.g.*, request for inspection of the collateral, for assembly of collateral, or for voluntary turnover to lender for foreclosure sale).

Commercially Reasonable Sale Requirements: If the lender decides to proceed against the personal property separately, the

lender must repossess the collateral in order to conduct a commercially reasonable sale. Section 9.610(b) of the Texas UCC requires that every aspect of a secured party's disposition of personal property collateral in foreclosure of its security interest be "commercially reasonable," including the method, manner, time, place, and terms of sale. Prior to its revision in 1999, the Texas UCC did not define "commercially reasonable," but revised Texas UCC § 9.627(b) provides rules that assist in the determination of "*commercially reasonable*" and, in certain circumstances, provide a safe harbor for certain actions.

Inadvertent Omissions from Collateral and Mortgaged Property: Use of the mortgaged property may require the continuation after the foreclosure sale of a variety of contracts, franchises, licenses, permits, leases, and other interests that may not be described by the phrase "TO HAVE AND TO HOLD the above described property, together with the rights, privileges, and appurtenances thereto belonging . . ." in an earlier version of the *Texas Real Estate Forms Manual's* deed of trust. (at 7B (1976 & Supp. 1982)), or the phrase "property (including any improvements)" in the current version of the deed of trust, at ch. 15, form 15-1. Unless the mortgagee is in some manner a party or a legally recognized third–party beneficiary to the contract, franchise, license, permit, lease, or other interest, the mortgagee may not have the benefits or the burdens of such matters. Some permits necessary to continue operation of the mortgaged property may be personal to the mortgagor. See, *e.g.*, Tex. Alco. Bev. Code Ann. §§ 11.03, .05 (Vernon 1995).

Including Unwanted Property: The deed of trust may include an omnibus description of mortgaged property (i.e., "all agreements affecting or benefiting the mortgaged property"). There is no way of knowing at the time of the execution of the deed of trust which present or future agreements will be assets and which will be liabilities. Whether the mortgagee or the purchaser can pick and choose at the foreclosure sale or whether the foreclosure sale documents can specifically exclude undesirable agreements are unsettled issues. Even if they can be excluded, the undesirable agreements may not be identifiable as such at the time of foreclosure.

1.5:2 Real Property

Identifying the real property may not be as easy as it first sounds. Sometimes not enough care is taken at the time of the loan to verify the property's description. If the description is by metes and bounds, a survey should be considered if one was not obtained at the time the loan was made.

Changes In the Security: Since the loan was originally made, the description of the mortgaged property may have changed through platting, replatting, partial release of liens, and condominium declaration. Failure to verify the description may result in clouding the title, inadequately advertising the sale; may be considered as additional evidence of the fraudulent conduct of the lender; and may result in failure to convey title to the lender of portions of the security.

Homestead: If the mortgaged property is the debtor's homestead or the debtor's residence, additional considerations should be given to cure rights, consumer debt–collection laws, and limitations on secured debt.

Two cases emphasize that "a lien cannot be 'estopped' into existence" over the homestead exemption. In *Hruska v. First State Bank*, 747 S.W.2d 783, 785 (Tex. 1988), the debtors misrepresented to the lender, subsequent to the funding of a construction loan on a homestead, that mechanic's lien documents had been prepared. The Texas Supreme Court found that these misrepresentations would not retroactively create a lien by estoppel. In *In re Niland*, 825 F.2d 801 (5th Cir. 1987), the Fifth Circuit held that a mortgagor's misrepresentations in a recorded homestead affidavit and designation identifying another residential property as the debtor's homestead did not estop the debtor from claiming a foreclosed residence as a homestead against a purchaser for value at a foreclosure sale. *But see Templin v. Weisgram*, 867 F.2d 240 (5th Cir. 1989) (borrower's homestead claim, made following simulated sale, barred by 12 U.S.C.A. § 1823(e) (West 1989).

Additionally, the lender's attorney should ensure that the lender is not attempting to claim that the mortgaged property serves as collateral for debts not permitted to be secured by the homestead. The lender may also be asserting erroneously that the homestead loan, although

not otherwise in default, is in default because of a default on another loan. This problem can occur if the homestead loan documents do not clearly state that a default on other indebtedness is a default on the homestead loan. For example, the homestead loan documents may recite that a default on "any debt secured hereby" is a default permitting acceleration but fail to recite that a default on debt "not secured hereby" is a default permitting acceleration of the homestead loan.

Improvements and Fixtures. The *Texas Real Estate Forms Manual's* form for deed of trust provides for the description of the mortgaged real property by calling for the insertion of a description following the heading "Property (including any improvements):" *Texas Real Estate Forms Manual*, ch. 15, form 15-1. A frequent practice is to insert a description of the land without further reference to the "improvements" encumbered or to "*fixtures*" and "*appurtenances*." Although a better practice is to include at least a general description of the improvements and fixtures, this practice in most cases should suffice. Court's have given liberal construction to the scope of the "property" conveyed by deeds merely identifying the property conveyed by description of the land. The general rule is that "[d]eeds are construed to convey to the grantee the greatest estate possible." *Reeves v. Towery*, 621 S.W.2d 209, 212 (Tex. Civ. App.—Corpus Christi 1981, writ ref'd n.r.e.) (citing *Waters v. Ellis*, 312 S.W.2d 231 (Tex. 1958)). A deed that does not except property owned by the grantor conveys the grantor's entire estate. *See Waters v. Ellis*, 312 S.W.2d 231, 234 (Tex. 1958). Reservations must be by clear language. *See Reeves*, 621 S.W.2d at 212 (citing *State v. Black Bros.*, 297 S.W. 213 (Tex. 1927)). No exception or reservation exists absent a manifest intent expressed in the instrument. *See Garvin v. Hudson*, 353 S.W.2d 508, 510 (Tex. Civ. App.--Texarkana 1962, writ ref'd n.r.e.).

The term "*improvement*" generally includes anything that permanently enhances the value of such real property. *See Karisch v. Allied-Signal, Inc.*, 837 S.W.2d 679, 680 (Tex. App.—Corpus Christi 1992, no writ). The term "improvement" covers a broader range of items than does the term "*fixture*." *See Logan v. Mullis*, 686 S.W.2d 605, 607 (Tex. 1985); *Cantrell v. Broadnax*, 306 S.W.2d 429, 432 (Tex. Civ. App.--Dallas 1957, no writ). Items which have been held under Texas law to be improvements include: (i) a building (*see Producers Lumber & Supply Co. v. Olney Bldg. Co.*, 333 S.W.2d 619, 624 (Tex. Civ. App.—San Antonio 1960, writ ref'd n.r.e.)); (ii) a house (*see Dennis v. Dennis*, 256 S.W.2d 964, 966 (Tex. Civ. App.—Amarillo 1952, no writ)); (iii) a fence (*see Jarrell v. Boedeker*, 146 S.W.2d 293, 295 (Tex. Civ. App.—Fort Worth 1940, no writ)); (iv) oil wells (*see Jenkins v. Pure Oil Co.*, 53 S.W.2d 497, 503 (Tex. Civ. App.—Dallas 1932, no writ)); (v) underground petroleum storage tanks (*see Big West Oil Co.*, 836 S.W.2d at 803); and (vi) a heat exchanger bolted to a concrete structure (*see Karisch*, 837 S.W.2d at 681). The permanent aspect of an improvement requires that it be placed on the land so that it is impossible to remove it or carry it away without injuring the real property or that the improvement be annexed to the soil as part of the freehold. *See Big West Oil Co. v. Willborn Bros. Co.*, 836 S.W.2d 800, 803 (Tex. App.--Amarillo 1992, no writ) Many of these examples indicate the difference between a fixture, which must be chattel, and an improvement which encompasses any permanent betterment.

If the property is leased, there are likely to be trade fixtures (items annexed to property that enable a tenant or occupant to carry on a trade or business) affixed to the property. The general rule is that a tenant's trade fixtures can be removed by a tenant if they may be done without injury to the property. *See Sonnier v. Chisolm-Ryder Co.*, 909 S.W.2d 475, 479 (Tex. 1995); *Reames v. Hawthorne-Seving, Inc.*, 949 S.W.2d 758, 761 (Tex. App.—Dallas 1997, writ denied).

"***Fixtures***" are broadly described under Texas law as items of property that are personal in nature and have been annexed to realty so as to become a part of the realty. *See Houston Bldg. Serv., Inc. v. American Gen. Fire and Cas. Co.*, 799 S.W.2d 308, 311 (Tex. App.--Houston [14th Dist.] 1990, writ denied); *Fenlon v. Jaffe*, 553 S.W.2d 422, 428 (Tex. Civ. App.—Tyler 1977, writ ref'd n.r.e.); *Ruby v. Cambridge Mut. Fire Ins. Co.*, 358 S.W.2d 943, 945 (Tex. Civ. App.--Dallas 1962, no writ). Generally, the term "fixture" includes all chattels or structures attached to realty that cannot be removed without materially damaging the property. *See Melendez v. State*, 902 S.W.2d 132, 137-38 (Tex. App.--Houston [1st Dist.] 1995, no writ). *See* TEX. BUS & COMM. CODE ANN. § 9.313(9)(1) (Vernon 2002).

More specifically, a three part test has been developed to determine whether an item of personal property has become a fixture: (i) did the person who annexed the chattel to the realty intend for it to become a fixture? (ii) was the mode and sufficiency of annexation adequate to attach the chattel to the realty? and (iii) has the chattel been adapted to the use of the realty? *See Logan v. Mullis*, 686 S.W.2d 605, 607 (Tex. 1985); *House the Homeless, Inc. v. Widnall*, 94 F.3d 176, 181-82 (5th Cir. 1996). Absent any evidence to the contrary, an owner who affixes improvements onto land is assumed to have intended for such improvements to become fixtures. *See McDaniel v. Pettigrew*, 536 S.W.2d 611, 615 (Tex. Civ. App.—Dallas 1976, writ ref'd n.r.e.); *Clark v. Clark*, 107 S.W.2d 421, 424 (Tex. Civ. App.—Texarkana 1963, no writ). If there was intent that the improvement be temporary in nature, however, such improvements will not be deemed a fixture. *See O'Neil v. Quilter*, 234 S.W. 528, 529 (Tex. 1921). Secret intentions will not be dispositive of an intent for the issue of permanent annexation. *See Ruby*, 358 S.W.2d at 946; *C.D. Shamburger Lumber Co. v. Bredthauer*, 62 S.W.2d 603, 604 (Tex. Civ. App.—Fort Worth 1933, writ dism'd w.o.j.). The second and third prongs of the fixture test are typically used as further evidence of the question of intent. *See Hutchins v. Masterson*, 46 Tex. 551, 554 (Tex. 1887); *Logan*, 686 S.W.2d at 607; *Fenlon*, 553 S.W.2d at 42.

Appurtenances. "***Appurtenance***" means a real property interest that is annexed to, incident to or necessarily connected with the use and enjoyment of a tract of real property. BLACK'S LAW DICTIONARY (West 1999). "*Appurtenance*" includes improvements and easements. *Angelo v. Biscamp*, 441 S.W.2d 524 (Tex. 1969); *Pine v. Gibraltar Savings Association*, 519 S.W.2d 238 (Tex. Civ. App.—Houston [14th Dist.] 1974, writ ref'd n.r.e.) Under the common law, the conveyance of a tract of real property includes appurtenances, unless the deed provides otherwise. *Pollock v. Lowry*, 345 S.W.2d 587 (Tex. Civ. App.—San Antonio 1961, writ ref'd n.r.e.). "***Appurtenance***" does not, however, normally include personal property. *Ogden v. Jones*, 37 S.W.2d 777 (Tex. Civ. App.—Austin 1931, writ dism'd w.o.j.).

The *Texas Real Estate Forms Manual's* form for deed of trust does not attempt to describe the variety of appurtenances or agreements that give value to the mortgaged property, nor does it refer to "appurtenances" but merely describes the mortgaged property as "Property (including any improvements)." *Texas Real Estate Forms Manual*, ch. 15, form 15-1. Prior to foreclosing on the deed of trust lien, a reexamination should be made to determine whether there are valuable rights associated with the property and whether these rights are appurtenances that pass to the foreclosure sale purchaser with title to the mortgaged property.

Water Rights. Water rights have been held to be included as part of the mortgaged property when the deed of trust did not expressly reserve or except water rights. *Graham v. Kuzmich,* 876 S.W.2d 446 (Tex. App.—Corpus Christi 1994, no writ). The obligation of a municipal utility district to lease and later purchase water, sanitary sewer and drainage facilities installed by the mortgagor have been held to be an appurtenance passing at a foreclosure sale. *Olmos v. Pecan Grove Municipal Utility District,* 857 S.W.2d 734 (Tex. App.—Houston [14th Dist.] 1993, no writ).

Peanut Allotment.

A federal peanut allotment has been held to be appurtenant to farm land. *Lindsey v. FDIC,* 960 F.2d 567 (5th Cir. 1992).

Parking Garage Lease.

A garage parking lease has been held not to be appurtenant to an office building where the leasehold interest in the parking garage was not necessary to the intended function of the building because other parking was available near the building and not every tenant in the building leased parking space in the garage. *Law Offices of C. Kendall Harrell, P.C. v. Commerce Savings Association,* 824 F.Supp. 1159 (W. D. Tex. 1993).

1.5:3 Crops, Crop Rent, and Farm Tenants

The purchaser at a foreclosure sale will take title to crops and crop rent only if there has not been an actual or constructive severance of the crops and rent from the land. This severance may be created by harvest, sale, assignment, or mortgage. Lease of the land creates a severance of the crops under the proper