Vanderbilt Law Review

Volume 7
Issue 5 *Issue 5 - August 1954*

Article 5

8-1954

Creditors' Rights and Security Transactions -- 1954 Tennessee Survey

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CREDITORS' RIGHTS AND SECURITY TRANSACTIONS—1954 TENNESSEE SURVEY

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MECHANICS' LIENS

Two cases during the Survey period involve priorities between mortgages and mechanics' liens. They are *Southern Blow Pipe & Roofing Co. v. Grubb*,[1] and *First State Bank v. Stacey*.[2] Before giving a detailed consideration of these cases, perhaps it would not be amiss to sketch in a little background by way of the general nature and scope of these mechanics' liens, as well as a few words concerning priorities with other liens. This introductory material may make the cases at hand a little more easily understood.

Origin Nature and Scope of the Lien

The term "mechanics' lien" includes all sorts of liens not only of mechanics, but of laborers, materialmen and other furnishers.[3]

These liens have no likeness at common law; they are a creature of statute.[4] We know when the idea entered into our legislation and the occasion. These liens originated, we are told, with a Maryland statute of 1791, and the motive was to stimulate the building of the City of Washington.[5] So popular did the idea become, that every state now has a mechanic "lien law" of some sort.[6] Because these liens are wholly statutory and because the laws creating them have been extremely varied, generalizations are extremely difficult.[7] Furthermore, case law is not reliable because the decisions are meaningless except with reference to the particular statute under which each arose and the precise language of the statute under which the case arose.

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1. 260 S.W.2d 191 (Tenn. App. E.S. 1953).
2. 261 S.W.2d 245 (Tenn. App. M.S. 1953).
3. The Tennessee legislature has labeled these liens "Mechanics' and Furnishers' Liens." Relevant code sections are contained in TENN. CODE ANN. §§ 7913-7959 (Williams 1934).
4. See 2 GLENN, MORTGAGES § 351 (1943); McDonnell v. Amo, 162 Tenn. 36, 41, 34 S.W.2d 212 (1931).
5. See 2 GLENN, MORTGAGES § 351 (1943). "The origin of such laws in America arose from the desire to establish and improve, as readily as possible, the city of Washington. In 1791, at a meeting of the Commissioners appointed for such a purpose, both Thomas Jefferson and James Madison were present, and a memorial was adopted urging the General Assembly of Maryland to pass an act securing to *master builders* a lien on houses erected and land occupied. The requested law was enacted December 19, 1791." See Moore-Mansfield Construction Co. v. Indianapolis, New Castle and Toledo Ry., 179 Ind. 356, 101 N.E. 296, 301 (1913).
6. See OSBORNE, MORTGAGES § 214 (1951).
7. *Ibid.*

The fundamental idea of the mechanics' lien is that it affords security for the payment of the claims of those who enhance the value of the land to which the lien attaches by labor or materials in construction or improvement.[8] The earlier lien laws furnished protection only to master-builders.[9] But today virtually every segment composing the construction industry is granted liens of varying extent for labor, services, or materials furnished. Included in the protection of the lien statutes are contractors, subcontractors, material dealers and laborers.[10] Although a good many states extend the protection to architects, landscape architects, engineers and surveyors,[11] Tennessee does not extend her protection quite so far. Thus, in Tennessee, architects' services,[12] and the superintendent who merely supervises the work of laborers[13] do not fall within the scope of the lien. Neither does the pale of protection in Tennessee extend to wages of a nightwatchman, and such items as temporary heating, temporary lights, water, stationery for the contractor, sharpening of saws, plate-glass insurance or a tarpaulin to cover materials.[14]

These mechanics' liens are not limited to those with whom the owner dealt with directly; the acts extend the coverage to persons who had no direct dealings with the owner.[15]

Conceivably, under some statutes the claims of the ancillary contractor could exceed the contract price,[16] but the most prevalent type, referred to as the "New York" system, measures the liability of the owner's property by the price stated in the original contract with the general contractor.[17] Tennessee is one of the New York type. The Tennessee statute expressly provides that the claims secured by a lien for labor done and materials furnished shall in no case exceed the amount agreed to be paid by the owner in his contract with the

8. See Chickasaw Hotel Co. v. Construction Co., 135 Tenn. 305, 314-15, 186 S.W. 115 (1916); OSBORNE, MORTGAGES § 214 (1951); TENN. CODE ANN. §§ 7114, 7927 (Williams 1934).

9. OSBORNE, MORTGAGES § 214 (1951).

10. TENN. CODE ANN. §§ 7914, 7927 (Williams 1934); OSBORNE, MORTGAGES § 214 (1951).

11. OSBORNE, MORTGAGES § 214 (1951).

12. Howe v. Kancher-Hodges & Co., 13 Tenn. App. 367 (W.S. 1930); Thompson v. Baxter, 92 Tenn. 305, 21 S.W. 668 (1892).

13. Harris v. Marble, 138 Tenn. 676, 200 S.W. 824 (1917).

14. Variety Fire Door Co. v. Hanson-Worden Co., 10 Tenn. App. 254 (W.S. 1929).

15. "Every journeyman or other person contracted with or employed to work on the buildings, fixtures, machinery, or improvements, or to furnish materials for the same, *whether such journeyman, furnisher, or other person was employed or contracted with by the person who originally contracted with the owner of the premises, or by an immediate or remote sub-contractor,* shall has this lien for his work or material. . . ." (Italics supplied).TENN. CODE ANN. § 7927 (Williams 1934). Code section 7914 provides for the lien when the claimant contracted directly with the owner or his agent.

16. See OSBORNE, MORTGAGES § 214 (1951).

17. See 2 GLENN, MORTGAGES § 351 (1943); 36 YALE L. J. 129 (1926).

original contractor.[18] That statute can be a delusion, however, since the subcontractor may look to the property regardless of payments made by the owner to the contractor.[19] Fortunately, the owner can protect himself against such double liability by an indemnity bond.[20]

To what does the lien attach in Tennessee? It extends only to the interest of the owner in the real property and improvements, existing at the time of the commencement of operations or thereafter acquired.[21] The lien includes the building, structure, fixture, or improvement as well as the lot or land.[22] Any person other than a laborer may, as a part of his contract, waive any part of lien, but a laborer may not waive his right of lien.[23] Likewise, the contractor may be estopped to assert his lien.[24] But the estoppel of the contractor will not necessarily estop a subcontractor who has furnished materials.[25]

When does the lien attach? This is of special concern to a competing lien claimant such as a mortgagee. While the lien attaches at different times in different states,[26] the Tennessee statute provides that the lien relates to and takes effect from the time of visible commencement of operations.[27]

Priority Between Mechanics' Liens and Mortgages

It seems well-established that if the mechanics' lien has attached to the property first it prevails over a subsequent mortgage on the property, both as to the land and the improvement.[28] In this connec-

18. TENN. CODE ANN. § 7937 (Williams 1934); Variety Fire Door Co. v. Hanson-Worden Co., 10 Tenn. App. 354 (Wis. 1929).

19. Under the Tennessee law the subcontractor may look to property regardless of payment by the owner. While subcontractors are chargeable with notice of terms and conditions of the original contract and are bound to make materials and labor furnished by them conform thereto, they may look to the property itself for satisfaction of their liens regardless of whether the owner has paid the contractor the entire amount of the contract price. Richmond Screw Anchor Co. v. Mimter Co., 156 Tenn. 19, 300 S.W. 574 (1927).

20. This is provided for in the code. TENN. CODE ANN. § 7932 (Williams 1934).

21. TENN. CODE ANN. § 7916 (Williams 1934). Thus, a life tenant cannot bind his remainderman. Allen v. Brown, 14 Tenn. App. 405 (E.S. 1932). Nor will a contract with the lessee give a lien on the lessor's interest. Reed v. Estes, 113 Tenn. 200, 80 S.W. 1086 (1904).

22. TENN. CODE ANN. § 7917 (Williams 1934).

23. TENN. CODE ANN. § 7939 (Williams 1934).

24. Green v. Williams, 92 Tenn. 220, 21 S.W. 520 (1893).

25. *Ibid.*

26. There are at least four different points of time when the mechanics' lien fastens to the property for the purpose of priority over other incumbrancers. (1) It begins with the making of the contract between the owner and mechanic. (2) The lien runs from the commencement of the building. (3) The lien of each claimant commences to run from the time he began to perform his labor or furnished the material. (4) There is no mechanics' lien without filing, and priorities are determined solely with reference to the date of filing. See *Priorities between Mortgages and Mechanics' Liens*, 36 YALE L. J. 129, 131-33 (1926); OSBORNE, MORTGAGES § 214 (1951); *Mechanics' Liens in Virginia*, 29 VA. L. REV. 121, 127 (1942).

27. TENN. CODE ANN. § 7915 (Williams 1934).

28. TENN. CODE ANN. 7917 (Williams 1934); Electric Light Co. v. Gas Co., 99 Tenn. 371, 42 S.W. 19 (1889); OSBORNE, MORTGAGES § 215 (1951); *Mechanics' Liens in Virginia*, 29 VA. L. REV. 121, 127 (1942).

tion it is of very considerable importance to be careful to determine when the mechanics' lien does attach, for as we have just seen these liens attach at various stages, depending upon the particular state statute.[29] In Tennessee the lien attaches only from the time of visible commencement of operations;[30] and as to the persons contracting directly with the owner the lien continues for one year after the work is finished or materials are furnished, and until the final decision of any suit that may be brought within that time for its enforcement.[31] Presently we will see that the lien has a shorter duration where the lienor's rights do not grow out of contractual relations directly with the owner.

In order to preserve the lien, however, certain notification and recording requirements may have to be met.

One such requirement concerns notification to the owner. Any laborer or materialman whose contract was not with the owner, but with the original contractor or an immediate or remote subcontractor, shall have his lien only if he notifies the owner in writing 90 days after the demolition or completion of the building or within 90 days after the completion of his performance of his contract or his discharge.[32] In contrast to persons contracting directly with the owner (whose lien lasts one year), these persons whose rights grow out of contractual relations with the original contractor and subcontractor, and not with the owner, have a lien for only 90 days from date of notice, and until the final determination of any suit for enforcement brought within that period.[33]

The Tennessee statute also provides that as the lien applies to the owner it need not be recorded; but as concerns subsequent purchasers and encumbrancers for a valuable consideration without notice, the lien must be recorded within 90 days after the building is completed, or after the contract of the lienor is terminated.[34] The place of recordation is the office of the county register.[35]

But even as concerns subsequent encumbrancers without notice of

29. See note 26 *supra*.
30. TENN. CODE ANN. § 7915 (Williams 1934).
31. TENN. CODE ANN. § 7917 (Williams 1934).
32. TENN. CODE ANN. §§ 7927, 7929 (Williams 1934); Phillips & Buttorff Mfg. Co. v. Campbell, 93 Tenn. 469, 471, 25 S.W. 961 (1894). If the contract is in writing, a recordation of it constitutes notice of the lien. TENN. CODE ANN. § 7918 (Williams 1934).
33. TENN. CODE ANN. §§ 7927, 7929 (Williams 1934). A garnishor of the owner cannot take advantage of the omission of a lien claimant to institute a suit as required by this statute, where the owner was making no resistance to the claim of the lienor, and there was an absence of fraud or collusion between owner and lien claimant. Hamilton Nat'l Bank v. Long, 189 Tenn. 562, 226 S.W.2d 293 (1949).
34. TENN. CODE ANN. § 7919 (Williams 1934). While the lien need not be recorded as to the owner, if there is a written contract it may be recorded, and such recordation shall be notice to all persons of the existence of the lien. *Id.* at § 7918.
35. TENN. CODE ANN. §§ 7918, 7929 (Williams 1934).

the mechanics' lien, the lienor will be protected against such an encumbrancer who became such after the materials have been furnished if the materialman records his lien in the office of the county register within 90 days after the building is completed or the contract of the lienor is terminated. So a mortgagee who takes a mortgage in Tennessee cannot rely upon an examination of the records, but must make investigation outside of them to discover and determine factual matters that frequently are not definite, for the reason that a mechanics' lien relates back to the date of the visible commencement of the work.[36] Here one can see the advantages of the New York type of statute, which relates the lien wholly to the day when the mechanics' lien was recorded.[37] Turning to the other side of the shield, however, when there has been a "visible commencement" of a building, that fact is sufficiently patent to put any prospective mortgagee on notice that a lien might attach to this property for those improvements. Moreover, perhaps there is no great hardship in allowing the mechanics' lien to relate back and be superior to that of the mortgagee. The mechanic or materialman is entitled to no lien until he has augmented the value of the property, and then only to the amount, theoretically at least, of such augmented value. This increased value of his security is directly beneficial to the mortgagee. To save his mortgage, the mortgagee may be required to make an increased investment in the security, but the increased investment is measured by the increased value.[38] In balancing the confiicting interests of the materialmen and the mortgagee, the legislatures incorporating this view in the statute have seen fit to tip the scales slightly in favor of the materialman and laborer.

No constitutional roadblock is thrown up from the fact that the recording of the lien relates it back to the commencement of the work, even though it hurts the intervening mortgagee who advanced the money when the mechanics' lien was not recorded, providing the statute giving the priority antedates the mortgage. The mortgage is presumed to have been executed with reference to existing law.[39] But even under the Tennessee type statute precedence will not be given a mechanics' lien over a subsequent mortgage where the statutory filing requirement has not been complied with; and the fact that actual

36. TENN. CODE ANN. §§ 7919, 7929 (Williams 1934). "The language of the statute is that the claim must be filed within ninety days after the building is completed, etc., but it is provided that during the full ninety day period the lien shall be effective without registration. We think the meaning is clear." Brown v. Brown & Co., 25 Tenn. App. 509, 513, 160 S.W.2d 431 (E.S. 1941). To the same effect: Electric Light Co. v. Gas Co., 99 Tenn. 371, 42 S.W. 19 (1889); Green v. Williams, 92 Tenn. 220, 21 S.W. 520 (1893) (priority over a purchaser).

37. See *Priorities between Mortgages and Mechanics' Liens,* 36 YALE L. J. 129, 133 (1926); *Mechanics' Liens in Virginia,* 29 VA. L. REV. 121, 127 (1942).

38. See Haxtun Steam-Heater Co. v. Gordon, 2 N.D. 246, 254, 50 N.W. 708, 710 (1891).

39. Green v. Williams, 92 Tenn. 220, 21 S.W. 520 (1893).

notice was given in some other manner does not excuse failure to follow the statute.[40]

There have been statutes giving a subsequent mechanics' lien priority over mortgages already existing at the time the mechanics' lien fastened upon the property. Such statutory attempts to make the subsequent mechanics' lien prior as to the property covered by the mortgage already existing at the time the statute was enacted would pretty clearly be unconstitutional, as an impairment of the mortgagee's contract.[41] It is different, however, as to mortgages made subsequently. Then the mortgagee has notice that such a thing is within the possibilities; every mortgage contract is presumed to be executed with reference to existing laws, and subject to such modifications.[42]

Tennessee has a statute that takes a half-way step in this direction. Her statute provides that if the lienor gives ten days' notice to the holder of a mortgage in existence prior to the commencement of operations, the lien shall have priority over the mortgage if the mortgagee consents, and upon failure of the mortgagee to object in writing within ten days after the receipt of the notice, his consent shall be implied.[43] The same rule operates upon the vendor's lien when he has conveyed, expressly reserving a lien, or has only executed a title bond.[44]

So much for an introductory discussion; now let us direct our attention to *Southern Blow Pipe & Roofing Co. v. Grubb*,[45] which is one of the principal cases to be discussed. There the controversies concerned the holder of a deed of trust, who loaned money to the owner of property for the construction of an apartment house, on the one hand, and three materialmen-lienors who furnished material for the apartment house—on the other hand. Athens Federal Savings & Loan Association loaned money to the owner, Grubbs, on three separate occasions for the construction of the apartment house. The first loan was made September 2, 1947; a second loan was made January 21, 1948; and a third on May 28, 1948. Each loan was secured by a deed of trust, which was properly recorded on the date the loan was made.

On December 1, 1947 the owner signed a contract with one of the materialmen's lienors, Southern Blow Pipe and Roofing Company by which the lienor agreed to furnish for the building the necessary work,

40. McDonnell v. Amo, 162 Tenn. 36, 34 S.W.2d 212 (1931); Henderson v. Watson, 25 Tenn. App. 506, 160 S.W.2d 429 (E.S. 1941).
41. Central Savings Bank v. City of New York, 279 N.Y. 266, 18 N.E.2d 151 (1939).
42. 2 GLENN, MORTGAGES § 354 (1943); *cf.* Green v. Williams, 92 Tenn. 220, 21 S.W. 520 (1893).
43. TENN. CODE ANN. § 7924 (Williams 1934). Where mortgagee saw the written contract between materialman and owner, he had the requisite written notice. Neely v. Saunders Co., 169 Tenn. 30, 81 S.W.2d 390 (1935).
44. TENN. CODE ANN. § 7924 (Williams 1934).
45. 260 S.W.2d 191 (Tenn. App. E.S. 1953).

labor and materials for the erection or installation of stucco. This job took about two weeks and was completed sometime between January 15 and March 15, 1948. On August 23, 1948 Roofing Company recorded their lien, and the building was not completed until more than a year later, or December, 1949.

A second materialmen's lien, the McKenzie claim, was for materials purchased by the owner under contract delivered between March 10 and May 27, 1948. This lien was recorded on August 25, 1948.

The third materialman claiming a lien is McLendon, who furnished materials to the owner during February and March, 1948. This lien was not recorded.

Roofing Company's Claim: As to the Roofing Company's claim, the court held that it should be subordinated to all of the Loan Company's deeds of trust, since the recording of Roofing's claim was more than 90 days after the completion of its contract and not within 90 days after the building was completed. It is clear that Roofing recorded its lien long *before* the building was completed, but more than 90 days after it furnished the material.

The statute provides two different filing periods in order for the lien to be valid against subsequent encumbrancers. The lien must be filed within 90 days after the building is completed, or within 90 days after the contract of the lienor is terminated.[46] The Tennessee provisions relating to materialmen are construed by the Tennessee court to be mandatory, and a lien filed after the period allowed by the statute is void.[47] Thus the court concluded that the statutory requirements for recording were not satisfied.

The court concluded that recording by the lienor more than 90 days after furnishing the labor and materials, but *before* completion of the building, is not a proper recording within the purview of either of the two specified periods designated by the statute. Prior Tennessee cases support the court in the instant case in its conclusion that a recordation *before* the work is completed does not satisfy the requirement that the recordation must be within 90 days after the work is completed.[48] The recordation is said to be premature. So the *Grubb* case is in line with Tennessee authority in what the writer thinks is a mechanical, literal and unrealistic interpretation of the statute.

Taking what the writer believes to be a realistic, pragmatic approach to the matter, if a lien is recorded *before* the work is completed and remains of record after it is completed, is not the lien recorded within 90 days after the work is completed? Giving a reasonable interpreta-

46. TENN. CODE ANN. § 7919 (Williams 1934).
47. McDonnell v. Amo, 162 Tenn. 36, 34 S.W.2d 212 (1931); Brown v. Brown & Co., 25 Tenn. App. 509, 160 S.W.2d 431 (E.S. 1941).
48. Bird Brothers v. Southern Surety Co., 139 Tenn. 11, 200 S.W. 978 (1917); Oliver King Sand & Lime Co. v. Sterchi, 7 Tenn. App. 647 (E.S. 1928).

tion to this phrase of the statute, does not the requirement that the lien must be recorded within 90 days after the building is completed simply place a maximum date beyond which a lien cannot be filed and be valid as against encumbrancers? If that is a correct interpretation of the statute, then Roofing did file its lien within the time required by the statute. The chancellor who tried the case in the lower court had so held.

Moreover, the view that a lien filed *before* the work is completed, and which remains of record after it is completed, is much fairer to the third party prospective creditors, whom the statute is designed to protect, than the view which says that it is not a proper recordation. To go back a little, the Tennessee court holds that a mechanics' lien properly recorded within 90 days after the completion of the building relates back to the date of visible commencement of operations and thus takes priority over encumbrancers and other creditors who became such in the interim between the date of visible commencement of operations and the date the lien is recorded.[49] Thus a lien recorded on the 90th day after the building is completed takes priority over a recorded mortgage or deed of trust that was executed between the time the building was started and ninety days after its completion. Now if the lien is recorded *before* the building is completed, then it gives notice to prospective creditors for a much longer time than if it is recorded sometime within the 90 days *after* the building is completed. Thus it is much fairer to those creditors.

There seems to be a somewhat incongruous lesson to be learned from the view of the Tennessee court on this point. Materialmen and laborers must be careful not to give other and prospective creditors too much notice by way of recordation, else the materialmen and laborers will forfeit their liens. That is to say, if they do not file their liens within 90 days after they have furnished the material, they must wait until after the building is completed. To say the least, that seems a bit strange to the writer.

McKenzie Claim: The McKenzie claim was for materials delivered between March 10th and May 27th. The lien was recorded on August 25th, or on the 90th day after the delivery of the last materials. This lien was held to be superior to the deeds of trust of Association recorded January 21, 1948 and May 28, 1948. The McKenzie lien was recorded on the 90th day, which was held to be within 90 days after the commencement of operations. Since, by virtue of the statute, the lien would "relate to and take effect from the time of the visible commencement of operations,"[50] the court held that the lien fastened to the property as of December 1, 1947. Thus, the court concluded that it

49. See note 36 *supra*.
50. TENN. CODE ANN. § 7915 (Williams 1934).

took priority over Association's deeds of trust which were recorded January 21 and May 28, 1948.

There is one feature here that causes the writer some concern. McKenzie never began to deliver materials until March 10th, 1948, yet the court relates the McKenzie lien back to and makes it take effect as of December 1, 1947, the date when the owner of the building started operations. The court thus reached the anomalous decision of giving McKenzie a lien that took effect more than three months before McKenzie ever furnished any materials.

Moreover, this conclusion seems to be unduly prejudicial to the rights of the innocent parties without knowledge (Association with their deeds of trust). There simply is no way in which Association could have protected itself against such a situation. Here a materialman (McKenzie) who has furnished materials between March 10th and May 27th after the execution and recordation of one of Association's deeds of trust (January 21st) is given priority over the deed of trust. Such a construction of the mechanics' lien statute creates a snare to subsequent innocent purchasers and encumbrancers, against which there is no protection. That doctrine will discourage financing of building and construction. What lender will be willing to lay out his money if he knows there is no possible way to protect himself against future liens of potential furnishers, who aren't even in the picture when the loan is made?

Does the Tennessee statute compel any such harsh conclusion? It provides that the lien, if recorded within 90 days after the completion of the contract, shall "relate to and take effect from the time of the visible commencement of operations." What is the "visible commencement of operations" of which the statute speaks? Is it the beginning of the building in which McKenzie (mechanics' lienor) had no part whatsoever, since his claim springs from a separate and independent contract with the owner made more than three months after the building was started by the owner, or does "visible commencement of operations" mean McKenzie's (mechanics' lienor) visible commencement of operations? The writer is of the persuasion that it means the visible commencement of operations of the lienor—the time when the lienor furnished his material.

The writer has found one other case which is closely relevant and it reaches a different result from the Tennessee decision. In *Welch v. Porter & Co.*,[51] the facts were nearly on all fours with the case at hand. The owner made a contract with a builder. Another person (Porter & Co.) contracted with the owner under a separate and independent contract to furnish some materials for the job. But before Porter & Co. had made a contract and before they had furnished any materials,

51. 63 Ala. 225 (1879).

Welch lent the owner money and took a mortgage on the premises. The Alabama statute provided that the materialman's lien "shall attach, and be preferred to all other incumbrances which may be attached to or upon such buildings . . . subsequent to the commencement of such buildings or improvements." Observe that the Alabama statute provides that the mechanics' lien shall attach at the "commencement of such buildings or improvements,"—much the same as the Tennessee statute ("visible commencement of operations"). The Alabama statute, like the Tennessee statute, requires that the lien be recorded within a fixed period after the indebtedness had accrued. Under these recording statutes the Alabama court held that since each lienor had contracted independently with the owner, each lien dated from the commencement of work or furnishing of materials *of the particular contractor.* Consequently the Welch mortgage was given priority over the mechanics' lien of Porter & Co. By that analogy, McKenzie's lien would have attached from the date of the commencement of work or furnishing of materials by McKenzie, and not from the date when the building was started by the owner, which was more than three months before McKenzie had made his contract or furnished any material. In short, the writer believes that "visible commencement of operations" under the Tennessee statute should refer to the visible commencement of operations by the particular independent contractor (McKenzie).

The Alabama court has some language that seems quite pertinent here. The court says:

> "If we were to hold that, because a building had been commenced, a subsequent contractor or material-man could acquire a lien, which would take precedence over an intervening incumbrance, we think we would shock the moral sense of the profession, and fail to carry out the intention of the legislature. Let us show, by an illustration, to what consequences such a doctrine would lead. A mechanic commences a building, but, for some cause, fails to complete it. He has forfeited his claim for compensation, or has been paid, and has no claim which can support a lien. An incumbrance is then created on the property, by mortgage or otherwise. Subsequent to the creation of this incumbrance, another mechanic is employed to complete the work and finish the building. Will his lien date back to the commencement of the building by his predecessor, and thus be preferred to that of the intervening incumbrancer? We suppose no one would contend for such a result as this, and yet we can perceive no difference, in principle, between the claim of such subsequent contractor, and that of a material-man who furnishes materials under a contract made after the creating of the incumbrance."[52]

In the case at hand, the Tennessee court relies on *Brown v. Brown & Co.*,[53] to support their conclusion that the McKenzie mechanics' lien takes priority over the deed of trust, by relating it back to December

52. 63 Ala. 225, 232 (1879).
53. 25 Tenn. App. 509, 160 S.W.2d 431 (E.S. 1941).

1, 1947, as the date of the visible commencement of operations, as contemplated by the statute. That case does not quite stand for that proposition, however. In truth, in the *Brown* case the claim of the mortgagee was given *priority over* the mechanics' lien, for the reason that the mechanics' lien had not been recorded in time. While the *Brown* case is not clear on the point, it also appears that the lien claimant there was the original contractor who had done all the work from the start of the building. A prospective mortgagee would have been put on notice that a lien might attach for these improvements. Consequently, *Brown* dicta needs to be read in light of that fact. For had the *Brown* lien claimant recorded his lien within the proper time, his claim no doubt would have related back to the beginning of visible operations. But in the case at hand, the lien claimant (McKenzie) never came into the picture until more than three months after the building was started, and not until after Association had loaned the money and recorded one deed of trust.

In support of the court's opinion is the idea that the materialman has increased the value of the Association's security, theoretically at least to the value of the lien. The court makes no mention of any such argument, however.

McLendon Claim: McLendon furnished materials to the owner during February and March, 1948, but this lien never was recorded. The court quite properly held that the McLendon lien took priority over the Association's deed of trust dated May 28, 1948. McLendon was furnishing material to the owner before the money secured by this deed of trust was loaned to Owner. McLendon refused to give Owner further credit and Association, knowing that McLendon was furnishing material and was threatening to quit, assured McLendon that the materials, if delivered, would be paid by the Association. The Association expressly told McLendon that it was going to make the owner another loan out of which all bills for labor and materials would be paid. Subsequently McLendon delivered materials to the owner but they were not paid for when the loan secured by the deed of trust dated May 28 was made.

Although McLendon did not record his lien, this did not destroy it as to Association, for the reason that a recordation is necessary only as against a subsequent encumbrancer without notice. Association knew all about McLendon's claim when it advanced the money to Owner. Thus McLendon had a lien against the owner for one year; and as to the owner, recordation is not necessary in order to preserve the lien.[54]

Taking the decision in its broadest aspects, it can be based on estop-

54. TENN. CODE ANN. § 7919 (Williams 1934).

pel, although the court does not so label it. In short, the Association estopped itself to assert its priority.[55]

The other recent case in the field of priorities between deeds of trust and mechanics' liens is *First State Bank v. Stacey.*[56] There Stacey undertook to build a dwelling house. While the house was still under construction, he made a deed of trust to secure a note to the First State Bank in the sum of $10,000. The trust deed was recorded July 1, 1950. Stacey was unable to complete the house as planned and First State Bank foreclosed its deed of trust and the house and lot were sold at public auction for $9,750.

However, during the construction of the building, and before the trust deed was foreclosed, certain furnishers had furnished labor and materials for which they claim mechanics' lien priorities in the proceeds from the foreclosure sale over the deed of trust. These two claimants of liens were Turner and Moore-Handley Hardware Company.

The Turner Claim: Turner contracted with Stacey to furnish the fixtures and wire the house for electricity. Turner began this work in April, 1950 and completed substantially all of it by June 10, 1950. On November 20, 1950 he recorded his lien in the register's office. The court held the deed of trust superior to the Turner claim. It was clear that Turner did not file his claim within 90 days after he had completed his contract, which is the first of two alternative times for filing a lien. The statute[57] fixes two alternative periods for filing: (1) within ninety days after the building is demolished, altered, or completed; or (2) within ninety days after the claimant's contract expires or is terminated or he is discharged. Since Turner did not file within the time allowed within the second alternative time for filing (within 90 days after his contract expired or was terminated), there remained the question of dealing with the first alternative time (within 90 days after the building is completed). Turner's position was that since the house was never finished, the time had not arrived when he was required to file his claim for a lien under this first alternative. The court held against Turner on that point and decided that where the building is not completed, the lien claimant must file his claim within 90 days after his contract is terminated (the second alternative time for filing).

This seems to be the first time this point has been squarely before

55. Ash v. Honig, 62 F.2d 793 (2d Cir.), *cert. denied,* 288 U.S. 614 (1933). There the mortgagee held off recording his mortgage, assuring contractor that the property was clear and that he (mortgagee) would finance construction, whereupon contractor started work. Then mortgage was recorded before notice of lien was filed. The court permitted the contractor to assert priority. For a discussion of some defenses to actions under the Tennessee mechanics' lien statutes, see Anderson, *Defenses to Actions under Mechanics' Lien Statute,* 17 TENN. L. REV. 460 (1942).

56. 261 S.W.2d 245 (Tenn. App. M.S. 1953).

57. TENN. CODE ANN. § 7919 (Williams 1934).

the court. The decision makes it a bit hard on the contractor who intends to file his claim after the building is completed for if the owner is sufficiently unfortunate financially so that he cannot complete the building, then the contractor has taken a risk that has caused him a distinct loss. This case thus makes it plain that the materialman or laborer had better file his claim at the earliest possible date for filing and not dilly-dally, else he may lose his lien. But then it does not impose any great burden on the materialman to require him to be diligent.

The Moore-Handley Hardware Company Claim: There claimant made an oral contract with Stacey in April, 1950 to furnish materials as were required. All the items for which a lien was claimed were furnished between June 1, 1950 and July 17, 1950 except one fixture which was furnished August 10, 1950. Claimant filed his lien in the register's office on January 24, 1951. This clearly was more than ninety days after the delivery of the last item for which a lien was claimed. The court held that the deed of trust took priority over the Moore-Handley claim on the ground that this claim for a lien priority was not filed within the time provided by the statute. It was not filed within ninety days after the completion or termination of claimant's contract.

The comments on the Turner claim regarding the time when a lien must be filed when a building is not finished are pertinent here.

Personal Property Exemption Statutes

The case of *Keen v. Alexander*[58] deals with the steps that must be taken in order for a debtor to secure the protection of the chattel exemption statute.

By way of introduction, perhaps it may be well to point out that the subject of exemptions from claims of creditors is important when a trustee in bankruptcy as a representative of creditors is seeking to collect assets to pay off creditors; and the subject is of equal importance where a single creditor, not in a bankruptcy proceeding, is seeking to satisfy his claim out of the assets of his debtor. Whatever is property in the hands of the debtor is available to his creditors, unless it is exempt by law.[59] In so far as exemptions from claims of creditors are concerned, exemptions given the debtor from the claims of the single creditor by the relevant state law are respected by the National Bankruptcy Act. The Bankruptcy Act expressly recognizes the exemptions granted by the states.[60]

58. 195 Tenn. 564, 260 S.W.2d 297 (1953).

59. "Every debtor's property, except such as may be specially exempt by law, is assets for the satisfaction of all his just debts." Tenn. Code Ann. § 8197 (Williams 1934).

60. § 6 of Bankruptcy Act, 52 Stat. 847 (1938), 11 U.S.C.A. § 24 (Supp. 1953).

The munificent social policy of shielding a debtor and his family from want has grown as a part of our American heritage. The exemption statutes are manifold. They range from the early statutes exempting only personal property such as wearing apparel and the instruments or books necessary to the debtor's avocation to the present day legislation which insulates from claims of creditors all sorts of chattels,[61] a piece of land as a "homestead,"[62] additional widow's support,[63] wages,[64] or allows the debtor to create an estate for his family by means of insurance.[65]

Section 7701 of the Tennessee Code[66] expressly names a great number of specific chattels that are exempt from execution, seizure or attachment in the hands or possession of heads of families, who are bona fide citizens and permanently residing in Tennessee. Then the last paragraph of that code section provides that if "the head of the family does not own sufficient articles" that are specifically exempt by the code section to total $450, then "such head of the family may select additional articles" owned by him to an amount sufficient to total $450. *Keen v. Alexander* gives the lawyer some guidance as to steps that must be taken in Tennessee in order to bring within the protective pale of this chattel exemption statute those chattels that may be selected by reason of the statute as exempt articles, but which are not expressly made exempt from execution by the statute.

In the *Keen* case the sheriff levied on an automobile (which the statute does not expressly exempt). Keen, the debtor, claimed that the fair market value of this automobile, together with the value of all specifically exempt personalty owned by him, did not exceed the sum of $450.00. Therefore, Keen took the position that this automobile was exempt from execution. After the automobile had been seized, Keen executed and filed a supersedeas bond and the sheriff returned the automobile to Keen. Subsequently the trial court directed Keen to return the automobile to the sheriff or a judgment would be entered against Keen and his bondsman.

Keen went to the Tennessee Supreme Court on a petition for certiorari alleging a wrongful levy on exempt property. The Supreme Court denied Keen relief on the grounds that his petition for certiorari did not allege that he had informed the levying officer of his election to claim the automobile as exempt property so as to bring his aggregate exemption up to $450 allowed by the statute and did not

61. For a lengthy list of chattel exemptions in Tennessee, see TENN. CODE ANN. §§ 7707, 7709, 7710, 7712, 7715-7718 (Williams 1934); *Id.* §§ 7701-01.2, 7708, 7711, 7713, 7714, 7714.2-14.7, 7718.1-18.5 (Supp. 1952).
62. TENN. CODE ANN. §§ 7719-7734 (Williams 1934). *Id.* § 7719 (Supp. 1952).
63. TENN. CODE ANN. §§ 8231-8232 (Williams 1934).
64. TENN. CODE ANN. §§ 7711-7712 (Williams 1934).
65. TENN. CODE ANN. §§ 8456, 8458, 6398 (Williams 1934). *Id.* §§ 7718.1-18.5 (Supp. 1952).
66. TENN. CODE ANN. § 7701 (Williams Supp. 1952).

allege that Keen, the debtor, was head of a family. This Tennessee chattel exemption is limited to the head of the family by the express language of the statute, and the case law makes it clear that the burden of proof is upon the one who claims the exemption provided by the statute to prove that he is the head of the family.[67] The debtor's petition did not allege that he was the head of a family.

Where a levy is made on property expressly exempted by the statute, such levy is an abuse of process and will be quashed on a petition for certiorari.[68] However, an automobile is not an article expressly exempted by statute from levy. The statute provides that the debtor "may select additional articles" in the aggregate of $450.00. The debtor's petition for certiorari was silent as to whether he had selected the automobile as exempt property or sought to regain it prior to the filing of his petition for certiorari. Also, the debtor claiming the exemption has the burden of proving that the value of his remaining personalty, in addition to the property expressly exempt, does not exceed $450.[69] Therefore, the court seems properly to have concluded that the levy on the automobile was not an abuse of process in the absence of a showing by the debtor (Keen) that he had elected to claim the automobile as exempt and that the sheriff then arbitrarily refused to surrender it as exempt property.

The Tennessee court draws a fine line with respect to the power of a debtor, who has an exemption, to free the property from the exemption. On the one hand, the court holds that the head of a family may not waive such express exemptions as the homestead exemption, specific chattel exemptions and an additional year's support for the widow.[70] Such restriction is construed not as a restriction on the absolute ownership of the head of the family, but as a restraint placed by the statute upon creditors seeking to collect their debts.[71] Upon that reasoning the court will not permit the head of a family to waive those express exemptions. On the other hand, the debtor has the absolute right to sell or mortgage property expressly exempt from execution, and such sale or mortgage will be enforced, although the property cannot be legally levied on and sold under execution even by

67. Forehand v. Forehand, 28 Tenn. App. 131, 187 S.W.2d 635 (M.S. 1945).
68. Jones v. Williams, 32 Tenn. 105 (1852).
69. Forehand v. Forehand, 28 Tenn. App. 131, 187 S.W.2d 635 (M.S. 1945).
70. McAdams v. McAdams, 177 Tenn. 67, 146 S.W.2d 140 (1941). See American Trust & Banking Co. v. Twinam, 187 Tenn. 570, 576, 216 S.W.2d 314, 317 (1948); Mutual Loan & Thrift Corp. v. Corn, 182 Tenn. 554, 555, 188 S.W.2d 345-46 (1944). However, insurance that is given a statutory exemption from claims of creditors can be freed from the exemption by the insured if he clearly so indicates. Lunsford v. Nashville Savings & Loan Corp., 162 Tenn. 179, 35 S.W.2d 395 (1931); see Adams v. Garraway, 179 Tenn. 93, 96, 162 S.W.2d 1086, 1087 (1942).
71. See Mutual Loan & Thrift Corp. v. Corn, 182 Tenn. 554, 555-56, 188 S.W.2d 345, 346 (1944).

consent.[72] Here the court feels that it is sound public policy to provide that the thrifty and responsible head of a family should have the right to sell or borrow, in an emergency, in order to raise funds for the support of his family.[73] The court does not reckon with the possibility that the debtor might be a wastrel and squander the funds raised by waiving the exemption through mortgage or sale, rather than use the funds for the support of the family.

MOTOR VEHICLE TITLE REGISTRATION LAW

The Tennessee Supreme Court had a second look at the rather involved Tennessee Motor Vehicle Title and Registration Law, which was enacted by the 1951 Legislature.[74] The case before the court was *Memphis Bank & Trust Co. v. Ware*,[75] and it dealt with the question whether a lien had to be recorded upon the application for the certificate of title in order to be constructive notice to subsequent purchasers.

This Title Registration Law requires owners of motor vehicles to register them in the name of the owner with the Motor Vehicle Division of the Tennessee Department of Safety and the owner must procure from it a certificate of title and a title card. An application for a certificate of title is made and later (often months) a title certificate is issued and delivered to the owner if there is no lien or encumbrance appearing thereon. Otherwise, it is delivered to the person holding the first lien shown on the certificate, and it is held by such person until the lien is discharged.[76]

Section 68 of the Act provides:

> "No conditional sales contract, chattel mortgage, or other lien or encumbrance or title retention instrument upon a registered vehicle, other than a lien dependent upon possession entered into after the effective date of this act shall be valid against the creditors of an owner or subsequent purchasers or encumbrances [sic] until the requirements of this article have been complied with, unless such creditor, purchaser, or encumbrancer has actual knowledge of the prior lien."[77]

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72. Mutual Loan & Thrift Corp. v. Corn, 182 Tenn. 554, 188 S.W.2d 345 (1944); cf. American Trust & Banking Co. v. Twinam, 187 Tenn. 570, 216 S.W.2d 314 (1948) (creditor prevailed as to exempt insurance assigned to him).

73. See Mutual Loan & Thrift Corp. v. Corn, 182 Tenn. 554, 557, 188 S.W.2d 345 (1944).

74. TENN. CODE ANN. §§ 5538.101-5538.197 (Williams Supp. 1952). The court had its first look at this statute in City Finance Co. v. Perry, 195 Tenn. 81, 257 S.W.2d 1 (1953), which was the subject of a comment in the 1953 Tennessee Survey, 7 VAND. L. REV. 1049 (1953). In the *Perry* case the court was concerned with priorities between lien claimants as affected by the Title Registration Law. The *Perry* case is also the subject of a comment in 23 TENN. L. REV. 238 (1954).

75. 195 Tenn. 423, 260 S.W.2d 162 (1953). This case also is noted briefly in 23 TENN. L. REV. 238, 242 (1954).

76. TENN. CODE ANN. § 5538.135 (d) (Williams Supp. 1952).

77. *Id.* at § 5538.168.

Section 69 (a) of the Act provides:

> "Such filing and the notation of the lien or encumbrance upon the certificate of title as provided in this act shall constitute constructive notice of all liens and encumbrances against the vehicle described therein to creditors of the owner, to subsequent purchasers and encumbrances [sic] except such liens as may be authorized by law dependent upon possession."[78]

Section 69 (a) further provides that constructive notice of a lien shall date from the "receipt and filing of the request for the notation of said lien or encumbrance upon the certificate of title by the division as shown by the endorsement thereon."[79]

Section 69 (b) provides that this method of giving constructive notice of a lien or encumbrance upon a motor vehicle shall be exclusive, except as to liens dependent upon possession.[80]

In the *Ware* case the owner of an automobile went to the plaintiff bank for a loan which was to be secured by a chattel mortgage on the automobile. At that time his car was unencumbered with liens. Owner showed his application for a title certificate and bill of sale to the bank and obtained a loan, payable in installments. The loan was secured by a chattel mortgage, executed in duplicate. Owner also executed a notice of the bank's lien on a form prescribed by the Motor Vehicle Department. The bank forwarded one of the duplicate originals of the chattel mortgage and the proof of lien to the Motor Vehicle Department but made no notation of its lien on the application for a title certificate. The application for a title certificate was kept by the car owner. Some time later a certificate of title was issued by the department to the owner of the encumbered automobile, with the lien of the bank duly noted thereon. Pursuant to the statute, this title certificate was mailed to the bank. Owner later defaulted in his installment payments and bank elected to declare the entire balance due as provided in the chattel mortgage. Later, and more than two months after the bank had registered its lien with the department, owner sold the automobile to defendants, apparently without notifying the defendants of the bank's lien. The sale was without the bank's knowledge. Defendants ostensibly relied on a copy of the bill of sale, which owner had, showing the sale of the car to him, and also on the application for the certificate of title which owner had in his possession and which carried the statement that there were no liens on the vehicle.

Plaintiff bank sued to replevy the automobile from the defendant purchasers. The Supreme Court of Tennessee held that the bank's mortgage was superior to the claim of the subsequent purchaser

78. *Id.* at § 5538.169(a).
79. *Ibid.*
80. *Id.* at § 5538.169(b).

(defendant) and affirmed a judgment of the Court of Appeals in favor of plaintiff bank.

The court starts with the basic premise that this Motor Vehicle Title Registration Act undertakes to provide the exclusive method of registration of chattel mortgages on automotive vehicles and the bank had fully complied with the Act when it mailed its request for a lien to the Department of Safety. The court then concludes that the bank should prevail since there is nothing in the act that would require the bank to make a notation of its lien on the owner's application for a title certificate. The court was of the opinion that the application for certificate of title simply gave the owner the permission to drive the car temporarily, not exceeding 120 days until the department could decide whether to issue the title certificate.

If the sale to the defendant was made *before* the certificate of title was issued, then there is some difficulty with the court's conclusion that the defendant-purchaser had constructive notice of the bank's lien. The act is not completely clear as to when constructive notice is effective. By the terms of the act constructive notice dates only from the "receipt and filing of the request for the notation of the said lien or encumbrance upon the certificate of title by the division as shown by the endorsement thereon."[81] Does that mean that constructive notice dates from the filing of the request for a lien with the department with the "endorsement thereon," even if no certificate of title has been issued? Or does a certificate of title have to be in existence with the "endorsement thereon" before the filing constitutes constructive notice? If the latter interpretation is given to the act then there simply was no certificate of title upon which the bank's lien could be recorded so as to serve as constructive notice to the purchaser, if the sale was made *before* the certificate of title was issued. The court, in the case at hand, seems to equivocate somewhat on the question whether a lien is constructive notice from the time the request is received, and noted by the department. The court observes that "the defendants made no effort to ascertain the existence of the lien of the Plaintiff by making inquiry to the Department of Motor Vehicles in Nashville." It thus seems to deny defendant's claim, in part at least, on the ground that defendant had not been diligent in trying to find out about plaintiff's lien. If the plaintiff's lien constituted constructive notice to defendant from the time it was received and noted by the department, then defendant's diligence or lack of diligence is immaterial; defendant would be chargeable with constructive notice and that would end the matter. Neither does the case make it clear whether the automobile was sold to the defendant *after* the title certificate was issued by the department or before the title certificate was

81. *Id.* at § 5538.169(a).

issued. If the sale was made after the title was issued, then defendant clearly would have had constructive notice. In light of these ambiguities in the opinion the writer is not completely satisfied with the court's conclusion that the bank fully complied with the recordation features of the act so as to put the purchaser on constructive notice.

Also, what about estoppel? The trial court, which decided in favor of the defendant purchaser, may have been of the opinion that the bank should have made, or caused to be made, some notation on the application for the certificate of title showing its lien on the vehicle and not simply turn the application back to the owner unnoted. In the case at bar the bank did not make a notation of its lien on the application for a certificate of title, and apparently it caused no notation to be made on the copy of the application with the department, although the application has spaces for making notation of liens and the bank used the application as a basis for its loan. Instead, the bank entrusted the unencumbered application to the car owner and thus clothed him with the power to defraud the defendant purchaser who relied on an application free from encumbrances, and who could not check the title certificate for liens, if the certificate had not yet been issued by the department. Under the circumstances the essential elements of an estoppel might be found to be present. There may have been (1) conduct by the bank reasonably calculated to convey the impression that the facts were otherwise than, and inconsistent with, those which the bank afterwards attempted to assert; (2) conduct which at least was calculated to induce a reasonably prudent person to believe such conduct was intended or expected to be relied and acted upon; (3) knowledge by the bank of the real facts; (4) plus an innocent reliance by the purchaser to his prejudice.[82] Moreover, negligent silence may work an estoppel as effectually as an express representation, notwithstanding there was no intention to mislead.[83]

The court decided that there was nothing in the act that would require the bank to make a notation of its lien on the application, and that the bank had fully complied with the act. That could all be true, but that does not prevent the bank from being estopped to assert its claim. Even if we indulge the somewhat questionable assumption that the bank had recorded its lien so as to give purchaser constructive notice, that still does not prevent the application of the doctrine of estoppel against the bank. Even though a claimant of an interest in property has complied with all applicable recording acts, he may still

82. These basic essentials of estoppel are uniformly recognized. Church of Christ v. McDonald, 180 Tenn. 86, 171 S.W.2d 817 (1943); 3 POMEROY, EQUITY JURISPRUDENCE § 805 (5th ed. 1941); 19 AM. JUR., *Estoppel* §§ 42, 46 (1939).

83. See Church of Christ v. McDonald, 180 Tenn. 86, 97, 171 S.W.2d 817 (1943).

be deprived of his interest by estoppel.[84] Compliance with the recording statutes does not make a foolproof claim. Recording statutes simply lay down a certain statutory requirement which must be complied with. They do not close out other ways of losing one's claim.[85]

In light of the fact that the court has now decided that the Motor Vehicle Title Registration Act does not require the notation of a lien on an application for a certificate of title, when coupled with the fact that the title certificate recordation is the exclusive method of recording such liens, it might be well for the legislature to amend the act so as to require some notation of a lien on the application. It would be no great trouble for a creditor to note its lien on the application. As the act now stands, as construed by the decision at hand, one creditor can work an unnecessary hardship on a subsequent creditor or purchaser before the title certificate is issued by the department (for at least 120 days) by failing to note his lien on the application. Of course, after the title certificate has been issued a prospective purchaser or creditor is put on notice that there is the chance of a lien if the owner cannot produce the title certificate, since the act provides that the lienor shall hold the certificate until the lien is discharged. We know that the act provides that the filing of a lien upon the certificate of title shall date from the "receipt and filing of the request for the notation of said lien or encumbrance upon the certificate of title."[86] That clearly takes care of the situation where a certificate of title actually has been issued. But the real "rub" comes during that often long interim after the application for a certificate of title has been filed and before the title certificate is issued.

Of course, if the court construes this act to mean that constructive notice dates from the time the request for a lien reaches the department and the request is noted, rather than when it actually is noted on the certificate of title itself when issued, that would, in part, cure the evil. During this interim before the certificate is issued a prospective purchaser from, or a prospective creditor of, the owner of an automobile should, however, be provided a place certain where he could find out about liens, without unnecessary delay and red tape. On the other hand, if the constructive notice dates only from the date when the lien is noted on the certificate of title itself, which may not be issued for months later, then there is a hole in the act which needs to be plugged.

84. 3 POMEROY, EQUITY JURISPRUDENCE § 810a (5th ed. 1941); 2 MERRILL, NOTICE § 925 (1952).

85. 2 MERRILL, NOTICE § 925 (1952); 3 POMEROY, EQUITY JURISPRUDENCE § 810a (5th ed. 1941). By analogy, the recordation of a fraudulent conveyance will not make the transfer immune to attack as to creditors who became such even *after* the recordation. 1 GLENN, FRAUDULENT CONVEYANCES AND PREFERENCES § 343c (2d ed. 1940).

86. TENN. CODE ANN. § 5538.169(a) (Williams Supp. 1952).

BULK SALES STATUTE

In *Bradas & Gheens, Inc. v. Brewer*,[87] The Tennessee Supreme Court had a look at the question of a purchaser's liability when the Bulk Sales Law is not complied with. But first, a little background before taking up the principal case may make the case more useful to the reader.

In the classic case of a "sale in bulk" a merchant, instead of selling his goods over the counter day by day—in the usual course of business—disposes of the whole stock at one time and to one buyer. This indicates, of course, that the merchant is tired of his business, but the experience of the ages also recognized that often the transaction is a harbinger of travel abroad—the proceeds of sale going with the voyaging merchant to parts unknown.[88]

As the years went on, the sale in bulk presented what might be described as a standard method of defrauding creditors, and a method which called for protection of a preventive nature. So the last decade of the preceding century gave birth to a movement for a statute on the subject.[89] Early in the current century bulk sales laws swept across the country.[90] So rapidly did the movement spread that a bulk sales law is now featured in the statutes of perhaps every state.[91]

The bulk sales statutes give the creditors a chance to be heard before such a transaction has become cold, and also they may protect an honest buyer against belated attacks. Such statutes protect the seller's creditors against a sale of the whole or the major portion of the debtor's chattels by requiring the parties to prepare an inventory of seller's property and also prepare a list of the seller's creditors, plus requiring a notice to such creditors a few days before possession is

87. 195 Tenn. 139, 258 S.W.2d 734 (1953).

88. For the need for bulk sales legislation, see Billig, *Bulk Sales Laws: A Study in Economic Adjustment*, 77 U. OF PA. L. REV. 72, 75-80 (1928), where the author describes outrageous situations involving the transfer by tradesmen of their stock in gross, without making provision for their creditors.

89. *Id.* at 81-85.

90. *Id.* at 85-86.

91. See Miller, *Bulk Sales Laws: Meaning to be Attached to the Quantitative and Qualitative Requirements Phrases of the Statutes*, [1954] WASH. U.L.Q. 282. See also Billig, *Bulk Sales Laws: A Study in Economic Adjustment*, 77 U. OF PA. L. REV. 72 (1928); Note, 168 A.L.R. 735-88 (exhaustive annotations on the businesses or sellers subject to bulk sales statutes, as well as the types of property subject to these statutes). At first there was some question as to the constitutionality of the Bulk Sales Law. The New York Law of 1902 was held unconstitutional as denying merchants the equal protection of the laws as against other classes of persons. Wright v. Hart, 182 N.Y. 330, 75 N.E. 404 (1905). However, *Wright v. Hart* was later overruled and the law sustained in Klein v. Maravelas, 219 N.Y. 383, 114 N.E. 809 (1916). Such laws have been upheld by the United States Supreme Court over objections on federal constitutional grounds. Lemieux v. Young, 211 U.S. 489, 29 Sup. Ct. 174, 53 L. Ed. 295 (1909). Over various grounds of objection, Tennessee has declared her bulk sales statute constitutional. Cantrell v. Ring, 125 Tenn. 472, 145 S.W. 166 (1911); State v. Ausmus Mill Co., 123 Tenn. 399, 131 S.W. 867 (1910); Neas v. Borches, 109 Tenn. 398, 71 S.W. 50 (1902).

taken under such a sale. The principal object is publicity in advance of sale.[92]

The statute may regulate (1) a sale "in bulk," and/or (2) a sale of certain portions of the included property of the business; or it may also regulate (3) any sale out of the ordinary course of trade.[93] The Tennessee bulk sales statute condemns either a sale in bulk or a sale out of the ordinary course of trade, unless the requirements of the statute are met.[94]

The idea of these statutes is that the sale shall not be complete until the statutory conditions are fulfilled. Within the time specified in the statute the seller's creditor must act, if the case is such as to justify action on his part. If the seller's purpose is fraudulent, now is the time to give the purchaser notice, so that he will not have so changed his position as to afford him a defense. At the expiration of the time specified in the statute, the purchaser is safe, unless meanwhile a creditor has attacked. Of course, if the parties have not complied with the essential provisions of the bulk sales statute, the creditor may either go after the property itself, or in some instances he has redress against the purchaser himself.[95]

If a fraudulent merchant will raise cash from his business and then elope to parts unknown, it is by no means unlikely that the rascality may take the form of a loan rather than an outright sale. Thus, to give fuller protection to the seller's creditors, a bulk sales law should provide that a bulk chattel mortgage should be treated the same as a bulk sale. Some states do have statutes that cover the chattel mortgage by express language.[96] More often, however, the legislature has not mentioned chattel mortgages specifically in the bulk sales law, but has left the answer to the courts. The Tennessee statute does not expressly cover chattel mortgages.[97] By numerical weight of authority, unless specifically provided, a bulk sales law does not cover a

92. See Billig, *Bulk Sales Laws: A Study in Economic Adjustment,* 77 U. OF PA. L. REV. 72, 102 (1928).

93. For an exhaustive collection of these statutes and an analysis of the various types, see Miller, *Bulk Sales Laws: Meaning to be Attached to the Quantitative and Qualitative Requirements Phrases of the Statutes,* [1954] WASH. U. L. Q. 282.

94. TENN. CODE ANN. § 7283 (Williams 1934).

95. As to remedies of the creditor in general, see Colonial Milling Co. v. Holt Bros., 3 Tenn. App. 617 (M.S. 1927); Daly v. Drug Co., 127 Tenn. 412, 155 S.W. 167 (1912); 37 C. J. S., *Fraudulent Conveyances* §§ 487-493 (1943). A purchaser of goods in violation of the Bulk Sales Act subjects himself to personal liability for the value of the goods, if sold or disposed of by him or commingled with his own goods. Slaughter v. Cooper Corp., 20 Tenn. App. 241, 97 S.W.2d 648 (E.S. 1936).

96. See Billig and Smith, *Bulk Sales Laws: Transactions Covered by these Statutes,* 39 W. VA. L. Q. 323, 326-27 (1933).

97. TENN. CODE ANN. § 7283 (Williams 1934).

bulk chattel mortgage on a stock of goods.[98] There is some authority to the contrary, however.[99]

The Bulk Sales Acts are applicable only to sales by the owner and are not applicable to court decrees and bona fide court sales.[100] There is also considerable doubt that an auction sale falls within the purview of the Bulk Sales Act.[101] A trustee in bankruptcy of a seller can avail himself of the benefits of the Bulk Sales Act for the benefit of seller's creditors where a sale has been made in disregard of the statute.[102]

The Tennessee statute governing the "Sales of Stocks of Merchandise in Bulk" provides:

> "A sale of any portion of a stock of merchandise otherwise than in the ordinary course of trade in the regular and usual prosecution of the seller's business, or a sale of an entire stock of merchandise in bulk, shall be presumed to be fraudulent and void as against the creditors of the seller, unless the seller and purchaser shall, at least five days before the sale, make a full detailed inventory, showing the quantity, and, so far as possible, with the exercise of a reasonable diligence, the cost price to the seller of each article to be included in the sale; and unless such purchaser shall, at least five days before the sale, in good faith, make full and explicit inquiry of the seller as to the names and places of residence or place of business of each and all of the creditors of the seller, and unless the purchaser shall, at least five days before the sale, in good faith, notify or cause to be notified, personally or by registered mail, each of the creditors of the seller of whom the purchaser has knowledge, or can, with the exercise of reasonable diligence, acquire knowledge, of the purposed sale and of the cost price of the merchandise to be sold, and the price proposed to be paid therefor by the purchaser; and the seller shall, at least five days before such sale, fully and truthfully answer in writing each and all of said inquiries; provided, however, no suit shall be brought or maintained by any creditor against such seller or purchaser within five days after he received notice from any source of the intended sale and purchase,

98. See Billig and Smith, *Bulk Sales Laws: Transactions Covered by these Statutes*, 39 W. VA. L. Q. 323, 327 (1933).

99. *Id.* at 327-28.

100. Schultz, Baujan & Co. v. Bell, 23 Tenn. App. 258, 130 S.W.2d 149 (M.S. 1938); Cooley v. Brennan, 102 Cal. App. 2d 952, 228 P.2d 104 (1951). Both cases held the statute not applicable to a transfer of property under a divorce decree.

101. For authority that auction sales do not fall within the interdiction of the bulk sales statutes, see Lowe v. Fairberg, 245 App. Div. 731, 280 N.Y. Supp. 615 (2d Dept. 1935). See also Goetz v. Michael Tauber & Co., 282 Fed. 869 (7th Cir. 1922).

102. Under § 70e of the present Bankruptcy Act, the trustee is entitled to avoid any transaction which a creditor could have avoided under state law, and concurrent jurisdiction is conferred for that purpose upon state and Bankruptcy Courts. 11 U.S.C.A. § 110 (1953). Applied in Keller v. Fowler Bros. & Cox, 148 Tenn. 571, 256 S.W. 879 (1923). Moreover, the recovery by a trustee in bankruptcy, though based on the rights of certain creditors only, inures to the benefit of all creditors. Creditors who could not have attacked the transaction thus get a "windfall." Moore v. Bay, 284 U.S. 4, 52 Sup. Ct. 3, 76 L. Ed. 133 (1931).

> and any suit so brought shall be dismissed at the cost of the plaintiff in the case."[103]

The next succeeding section of the Code provides that there shall be a conclusive presumption that notice sent by registered mail was received.[104] Under the Tennessee statute actual fraud is not necessary in order for sellor's creditors to have redress. A sale in violation of the statute is not void because of a fraudulent intent and purpose, but because declared so by statute, and so insolvency of the seller is immaterial.[105]

Under the Tennessee statute there are four steps to be taken by the parties in order to comply with the statute. They are: (1) making a full detailed inventory of stock five days before the sale; (2) full and explicit inquiry by the purchaser as to the names, residences, etc. of all the creditors of seller five days before the sale; (3) notice five days before the proposed sale, etc. by the purchaser to each creditor of whom he has knowledge or as to whom he may with the exercise of reasonable diligence acquire knowledge; and (4) the "seller shall, at least five days before such sale, fully and truthfully answer in writing each and all of said inquiries."

In *Bradas & Gheens, Inc. v. Brewer,*[106] the pivotal point concerned the failure of the seller to furnish to the purchaser the name of one of seller's creditors. The plaintiff, Bradas & Gheens, Inc. a creditor of a merchant who sold his goods in bulk to the defendent, Brewer, sued to recover from defendent-buyer because of the omission of plaintiff-creditor's name from the list of creditors furnished to buyer. The Supreme Court of Tennessee found that there was a complete compliance with the other requirements of the Bulk Sales Law. The Supreme Court affirmed the lower court's decision that the plaintiff-creditor was not entitled to recover from defendent-buyer, although there was an omission of creditor's name from the list furnished by seller. The court took the position that it was not the legislative intent that the sale should be considered fraudulent as an unpaid creditor merely because the name of such creditor was omitted by the seller from the list furnished the buyer.

In the *Bradas* opinion the court thought it significant that the statute provides that the sale shall be deemed fraudulent and void as to creditors *unless* (the word used by the statute) there is compliance with each of the first three requirements mentioned; but the word "unless," or its equivalent in meaning, is omitted in the statute pro-

103. TENN. CODE ANN. § 7283 (Williams 1934).
104. TENN. CODE ANN. § 7284 (Williams 1934).
105. Slaughter v. Cooper Corp., 20 Tenn. App. 241, 97 S.W.2d 648 (E.S. 1936).
106. 195 Tenn. 139, 258 S.W.2d 734 (1953).

viding for the fourth (not complied with) requirement, which is that the seller fully and truthfully answer the inquiry as to the names, residences, etc. of creditors. Since the word "unless" expressly precedes each of the first three requirements so as to make the sale fraudulent in the absence of compliance with those requirements, the court concluded that the word "unless" was omitted with reference to the fourth requirement because it was not the legislative intent that the sale be considered fraudulent as to an unpaid creditor merely because the name of such creditor was omitted by the seller from the list furnished the buyer. Moreover, the court felt that the Bulk Sales Act is a statute in derogation of the common law and must be strictly construed.[107]

As Tennessee's highest tribunal points out, its decision in the case at bar probably is sustained by the numerical weight of authority.[108] Also, there is, as the court concludes, a rather pragmatic argument in support of its view in that, if the failure to include a creditor on the list would make the sale void, "no one would ever buy a stock of goods" (which, of course, is an overstatement).

There is one facet of the decision which gives the writer some difficulty, however. Just what is the significance of the failure to include all the creditors on the list? Is that requirement of the statute meaningless? Speaking of legislative intent, as did the court, did not the legislature intend that this requirement have some significance or meaning? If the failure to comply with this requirement does not avoid the sale, just what does it do? No other result flowing from a failure to comply with this requirement suggests itself. Has not the rationale of the court simply read this requirement out of the statute?

There is, moreover, some authority which would have declared the sale fraudulent and void in the case at bar where one creditor was omitted from the list. *Walton v. Walter Fisher Co.*[109] so held, notwithstanding the sale was made in good faith and for value. In the *Walton* case the Mississippi court said: "The purchaser takes the goods at the peril of the statute not having been complied with. He must see that it is complied with. The purpose of the statute was to make the sale of stocks of merchandise in bulk prima facie fraudulent as to the creditors of the seller. Such prima facie case can only be

107. There are two schools of thought as to the interpretation of bulk sales statutes in a case of doubtful application. Some authority favors a strict view, as does the Tennessee Court: Overlin v. Karakapas, 44 Ohio App. 111, 184 N.E. 257 (1932). Other courts favor a liberal view in interpreting bulk sales statutes: *Re* Dederick, 91 F.2d 646 (8th Cir. 1937); First Nat. Bank v. Sharp, 54 F.2d 886 (5th Cir. 1931).

108. See 37 C.J.S. *Fraudulent Conveyances* § 484, p. 1351 (1943); 24 AM. JUR., *Fraudulent Conveyances*, § 252, p. 358 (1939); and Note, 83 A.L.R. 1140 (1933).

109. 146 Miss. 291, 111 So. 364 (1927).

met by the purchaser by showing that the statute was complied with."[110]

The earlier Tennessee case of *Cantrell v. Ring*,[111] should be noticed in this connection. There the seller sued a purchaser who had contracted to buy a stock of merchandise. The purchaser defended, among other grounds, on the ground that seller had omitted the name of a creditor from the list of his creditors. The Tennessee Supreme Court held that the seller could not recover from the purchaser since the seller had omitted the name of a creditor, which was a violation of the Bulk Sales Statute and thereby conclusively fraudulent.[112]

110. 111 So. at 365.
111. 125 Tenn. 472, 145 S.W. 166 (1912).
112. This view expressed by the Supreme Court of Tennessee was later criticized by the court of appeals in Arnold v. May, 10 Tenn. App. 315, 323-25 (E.S. 1929). The court of appeals takes the position in the *Arnold* case that a failure to comply with the Bulk Sales Law will not constitute a sale fraudulent in law unless there are creditors in existence whose rights were affected and prejudiced by the sale.