NEW MEXICO LAW REVIEW

Volume 21
Issue 3 *Summer 1991*

Summer 1991

Commercial Law

Ruben III Arvizu

Esther Marie Garduno

COMMERCIAL LAW

I. INTRODUCTION

During the past year,[1] New Mexico's appellate courts handed down a number of rulings which affected New Mexico's commercial laws. The first section of this survey article examines cases affecting punitive damages and prejudgment interest. This section also examines cases concerning statutes of limitation, attorney's fees, modifications of real estate contracts, and government contracts.[2] The second part of the survey article examines cases dealing with bulk transfers, secured transactions, and notes.[3] The third part of the survey article examines cases which clarified certain aspects of agency, partnership, director indemnification, unfair trade practice, and New Mexico tax law.[4]

II. CONTRACTS

A. Punitive Damages

Historically, American courts did not allow recovery of punitive damages in contract cases.[5] At least six exceptions emerged permitting punitive damages in a contract cause of action.[6] The first two exceptions were a marriage contract[7] and a public service contract.[8] Recently, punitive damages have been recovered when the breach of contract was accom-

---

1. The survey period ran from September 30, 1989 to August 31, 1990.
2. *See infra* notes 5-176 and accompanying text.
3. *See infra* notes 177-336 and accompanying text.
4. *See infra* notes 337-513 and accompanying text.
5. RESTATEMENT (SECOND) OF CONTRACTS § 355 (1981); John, *Formulating Standards for Awards of Punitive Damages in the Borderland of Contract and Tort*, 74 CALIF. L. REV. 2033 (1987). Courts did not want to disturb the allocation of risks and benefits agreed to by the parties.
6. John, *supra* note 5, at 2043; McCubbin, *Punitive Damages in Contract Actions-Are the Exceptions Swallowing the Rule?*, 20 WASHBURN L.J. 86 (1980).
7. John, *supra* note 5, at 2043; McCubbin, *supra* note 6, at 94 (citing Smith v. Hawkins, 120 Kan. 518, 520, 243 P. 1018, 1019 (1926) (where defendant's conduct was fraudulent); Osmun v. Winters, 30 Or. 177, 46 P. 780 (1896) (where the defendant's conduct was malicious); Sneve v. Lunder, 100 Minn. 5, 110 N.W. 99 (1907) (where the defendant's conduct was ruthless)). This exception was very similar to intentional infliction of mental distress and rested more in tort than contract. *Id.* (citing *Osmun*, 30 Or. at 182, 46 P. at 782; D. DOBBS, HANDBOOK ON THE LAW OF REMEDIES § 3.9 n.1 (1973)).
8. John, *supra* note 5, at 2043; McCubbin, *supra* note 6, at 94 (citing Williams v. Western Union Telegraph Co., 138 S.C. 281, 136 S.E. 218 (1927) (involving a telephone company); Davis v. Atlantic Coast Line R. Co., 104 S.C. 63, 88 S.E. 273 (1916) (involving a common carrier); Woody v. National Bank of Rocky Mount, 194 N.C. 549, 140 S.E. 150 (1927); Birmingham Waterworks Co. v. Keiley, 2 Ala. App. 629, 56 So. 838 (Civ. App. 1911); Southwestern Gas & Elec. Co. v. Stanley, 45 S.W. 2d 671 (Tex. Civ. App. 1931), *aff'd*, 123 Tex. 157, 70 S.W.2d 413 (1934)).

panied by fraud,[9] an independent tort,[10] breach of fiduciary duty,[11] or breach of an implied covenant of good faith and fair dealing.[12] Punitive damages are also allowed when a building or construction contract has been breached.[13]

In determining whether to apply punitive damages to a breach of contract, New Mexico courts must consider whether the defendant's conduct was committed maliciously, intentionally, fraudulently, oppressively, recklessly, or with wanton disregard for a plaintiff's rights.[14] New Mexico also allows punitive damages under a breach of contract suit when the breach is accompanied by fraud,[15] an independent tort,[16] or a breach of good faith.[17] In the past year the New Mexico Supreme Court addressed whether punitive damages should be allowed in a cause of action for breach of contract accompanied by a breach of fiduciary duty.[18] The court also addressed an award of punitive damages with regard to employment contracts[19] and building contracts.[20] Finally, in *Romero v. Mervyn's*, the supreme court may have eliminated the specific exceptions in favor of one general exception.[21]

In *Romero v. Mervyn's*,[22] the plaintiff, Lucy Romero, fell while shopping at Mervyn's Department Store ("Mervyn's"). The store manager allegedly told Romero that Mervyn's would pay her medical bills. When Mervyn's refused to pay the medical bills, Romero brought an action for negligence and breach of contract.[23]

The trial court granted summary judgment in favor of Mervyn's on the contract claim. The jury absolved Mervyn's of liability under the negligence claim.[24] The supreme court upheld the negligence verdict but

---

9. *See* Thompson v. Home Security Life Ins., 271 S.C. 54, 244 S.E.2d 533 (1978); Powers v. Martinson, 313 N.W.2d 720 (N.D. 1981) (punitive damages properly awarded where defendant committed fraud in sale of building).

10. Ramsey v. Culpepper, 738 F.2d 1092, 1099 (10th Cir. 1984); Stanback v. Stanback, 297 N.C. 181, 254 S.E.2d 611 (1979).

11. PSG Co. v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 417 F.2d 659 (9th Cir. 1969), *cert. denied*, 397 U.S. 918 (1970); Mulder v. Mittelstadt, 120 Wis. 2d 103, 352 N.W.2d 223, 230 (Ct. App. 1984).

12. Seaman's Direct Buying Serv. v. Standard Oil Co., 36 Cal. 3d 752, 686 P.2d 1158, 206 Cal. Rptr. 354 (1984); Phillips v. Aetna Life Ins. Co., 473 F. Supp. 984 (D. Vt. 1979).

13. Annotation, *Recovery of Punitive Damages for Breach of Building or Construction Contract*, 40 A.L.R.4TH 110, 116-21 (1985).

14. Hood v. Fulkerson, 102 N.M. 677, 681, 699 P.2d 608, 612 (1985) (citing Loucks v. Albuquerque Nat'l Bank, 76 N.M. 735, 747, 418 P.2d 191, 199 (1966)). In order to sustain an award of punitive damages, a plaintiff must only prove one of the terms. Romero v. Mervyn's, 109 N.M. 249, 255, 784 P.2d 992, 998 (1989) (citing Green Tree Acceptance, Inc. v. Layton, 108 N.M. 171, 174, 769 P.2d 84, 87 (1989)).

15. Curtiss v. Aetna Life Ins. Co., 90 N.M. 105, 560 P.2d 169 (Ct. App. 1976); Stewart v. Potter, 44 N.M. 460, 104 P.2d 736 (1940).

16. Jessen v. National Excess Ins. Co., 108 N.M. 625, 776 P.2d 1244 (1989).

17. *Curtiss*, 90 N.M. 105, 560 P.2d 169.

18. *See* Kueffer v. Kueffer, 110 N.M. 10, 791 P.2d 461 (1990).

19. *See* McGinnis v. Honeywell, Inc., 110 N.M. 1, 791 P.2d 452 (1990).

20. *See* Foley v. Horton, 108 N.M. 812, 780 P.2d 638 (1989).

21. *See* Romero v. Mervyn's, 109 N.M. 249, 784 P.2d 992 (1989).

22. 109 N.M. 249, 784 P.2d 992 (1989).

23. *Id.* at 251, 252, 784 P.2d at 994, 995.

24. *Id.* at 252, 784 P.2d at 995.

held the summary judgment on the contract claim improper and remanded it for trial.[25] On remand, the jury returned a verdict in favor of Romero on the contract claim and awarded Romero punitive damages.[26] Mervyn's appealed.[27] The supreme court affirmed, allowing punitive damages as possible relief in all cases of breach of contract where the award would serve important social ends.[28]

In general, recovery is limited to compensatory damages in contract cases because courts are unwilling to disturb the allocation of risks and benefits agreed to by the parties.[29] The *Romero* court noted that punitive damages may be awarded when one of the exceptions discussed above[30] is found.[31] The court stated that malicious or overreaching conduct is not good for business[32] and violates community standards of decency[33] and thus punitive damages should apply to such conduct.[34] Thus, the court set out the following rule: in cases where parties overreach or act maliciously, it is appropriate for a jury to determine "whether 'the public interest will be served by the deterrent effect punitive damages will have upon future conduct.'"[35] The court qualified punitive damages, however, by stating that the New Mexico rule was never intended to allow for punitive damages in every instance of breach of contract.[36]

The *Romero* court went on to apply its newly formulated rule to the facts before it. Under the new rule the court found that a jury could have believed that when the store manager made the contract with Romero to cover her medical bills, he knew Mervyn's would not honor it.[37] The court also found that a jury could also believe that the store manager acted maliciously when he promised that Mervyn's would pay Romero's medical expenses.[38] The *Romero* court therefore concluded that the trial court's jury instructions were supported by substantial evidence.[39]

---

25. *Id.* (citing Romero v. Mervyn's, 106 N.M. 389, 744 P.2d 164 (1987)).
26. *Romero*, 109 N.M. at 252, 784 P.2d at 995.
27. *Id.* at 258, 784 P.2d at 1001.
28. *Id.* at 257, 784 P.2d at 1000. The court cited Seaman's Direct Buying Serv. v. Standard Oil Co., 36 Cal. 3d 752, 769-70, 686 P.2d 1158, 1167, 206 Cal. Rptr. 354, 363 (1984), as an example of serving important social ends. In *Seaman's*, a California court awarded punitive damages against a party who adopted a "see you in court" position without a belief in the existence of a defense. *Id.* The California court justified its position stating, "Such conduct goes beyond the mere breach of contract. It offends accepted notions of business ethics. Acceptance of tort remedies in such a situation is not likely to intrude upon the reasonable expectations of the contracting parties." *Id.*
29. *Romero*, 109 N.M. at 257, 784 P.2d at 1000.
30. *Id.*; *see supra* notes 11-17 and accompanying text.
31. *Romero*, 109 N.M. at 257, 784 P.2d at 1000.
32. *Id.* at 258, 784 P.2d at 1001. Thus, the court implied that an award of punitive damages would promote good business.
33. *Id.*
34. *Id.*
35. *Id.* (quoting Vernon Fire & Casualty Ins. Co. v. Sharp, 264 Ind. 599, 608, 349 N.E.2d 173, 180 (1976)).
36. *Id.* at 256, 784 P.2d at 999.
37. *Id.* at 258, 784 P.2d at 1001.
38. *Id.*
39. *Id.*

Future applications of the *Romero* punitive damages rule are unclear. Should the new rule not be as sweeping as it seems, courts will still award punitive damages in certain specific instances, including cases where a breach of contract involves a breach of fiduciary duty, an employment contract, or a contract to build a home.

In *Kueffer v. Kueffer*,[40] Kathleen Kueffer sued William C. Kueffer and Santa Fe Design Associates, Inc. for breach of contract and breach of fiduciary duty. The Kueffers had divorced and divided their community assets in a written contract.[41] The contract provided that Mr. Kueffer would act as manager of the couple's interests in a contract with a third party.[42] Thus, Mr. Kueffer was acting as Ms. Kueffer's fiduciary.[43] The contract also stipulated that Ms. Kueffer was to be held harmless from any debts incurred by Santa Fe Design Associates, Inc. after July 1987.[44] Ms. Kueffer sued for breach of contract and breach of fiduciary duty when Mr. Kueffer's accountant incorrectly deducted some of Santa Fe Design Associates, Inc.'s debts from Ms. Kueffer's share of the proceeds from the sale of the Kueffer's community property after their divorce.[45]

The trial court ruled in favor of Ms. Kueffer on the breach of contract claim.[46] The trial court based its ruling on Mr. Kueffer's improper deduction of debts from Ms. Kueffer's portion of some net sale proceeds realized by way of a third party contract.[47] In addressing the breach of fiduciary duty claim, the trial court ruled in favor of Mr. Kueffer.[48] The trial court based its ruling on the ambiguity in the Kueffer contract and the fact that Mr. Kueffer had acted in good faith.[49] The trial court refused Ms. Kueffer's claims for punitive damages, prejudgment interest, costs, and fees.[50] Ms. Kueffer appealed.[51]

The supreme court held that because the Kueffer marriage contract was ambiguous, substantial evidence did not support an award of punitive damages.[52] The court noted that Mr. Kueffer interpreted the marriage contract as only exempting Ms. Kueffer from liability arising after the marriage contract was signed.[53] The evidence did not show that Mr. Kueffer's "interpretation of the contract was intentional, malicious, oppressive, reckless, or in wanton disregard of Ms. Kueffer's rights."[54]

---

40. 110 N.M. 10, 791 P.2d 461 (1990).
41. *Id.* at 11, 791 P.2d at 462.
42. *Id.* The Kueffers shared a 64% interest in the net proceeds from a contract between Santa Fe Design Associates, Inc. and John Conron. *Id.* The Kueffer marriage contract provided that this 64% interest would be divided equally between the Kueffers. *Id.*
43. *Id.* at 13, 791 P.2d at 464.
44. *Id.* at 11, 791 P.2d at 462.
45. *Id.*
46. *Id.* at 12, 791 P.2d at 463.
47. *Id.*; *see infra* note 79.
48. *Kueffer*, 110 N.M. at 12, 791 P.2d at 463.
49. *Id.*
50. *Id.*
51. *Id.*
52. *Id.* at 13, 791 P.2d at 464.
53. *Id.*
54. *Id.*

Thus, when a contract is ambiguous, the supreme court will not award punitive damages.

In addition to exploring an award of punitive damages where a breach of contract is accompanied by a breach of fiduciary duty, the supreme court considered the circumstances where breach of an employment contract warrants punitive damages in *McGinnis v. Honeywell, Inc.*[55] Shirley McGinnis had been employed as a secretary by Honeywell, Inc. ("Honeywell").[56] When McGinnis applied for her job, she signed an employment agreement which provided that either McGinnis or Honeywell could terminate the employment agreement at any time.[57] In 1982, McGinnis was promoted to benefits administrator in Honeywell's Human Resources Department.[58] In 1986, McGinnis was laid off.[59] At the time McGinnis was laid off, Honeywell operated under a work force realignment guide, which provided McGinnis with the option of resuming her job as a secretary in the event of a lay off.[60] This option was not offered to McGinnis.[61]

McGinnis sued Honeywell and alleged that she had been terminated in violation of Honeywell's policies and procedures.[62] She sought punitive and compensatory damages from Honeywell for breach of an implied employment contract and retaliatory discharge.[63] The trial court found in favor of McGinnis on the breach of employment contract and awarded compensatory damages. The trial court also granted Honeywell a directed verdict on the claims for retaliatory discharge and punitive damages.[64] Both Honeywell and McGinnis appealed.[65]

The New Mexico Supreme Court refused to award punitive damages for breach of an employment contract where there was no substantial evidence of a culpable mental state on the part of the employer's agents.[66] In order to collect punitive damages, McGinnis needed to show bad faith by Honeywell during the course of her employment.[67] Alternatively, McGinnis needed to show bad faith in the manner and method used by Honeywell to fire her.[68] McGinnis also needed to show a culpable mental state on the part of Honeywell's agents in laying off McGinnis.[69] The

---

55. 110 N.M. 1, 791 P.2d 452 (1990).
56. *Id.* at 2, 791 P.2d at 453.
57. *Id.*
58. *Id.* at 3, 791 P.2d at 454.
59. *Id.*
60. *Id.*
61. *Id.*
62. *Id.*
63. *Id.* at 2, 791 P.2d at 453. Ms. McGinnis' retaliatory discharge claim was based on her charge that she had been terminated because she had exposed potential fraud at Honeywell and refused to ignore accounting inconsistencies. *Id.* at 3-4, 791 P.2d at 454-55.
64. *Id.* at 2, 791 P.2d at 453.
65. *Id.*
66. *Id.* at 9, 791 P.2d at 460.
67. *Id.*
68. *Id.* (citing Newberry v. Allied Stores, 108 N.M. 424, 432, 773 P.2d 1231, 1239 (1989)).
69. *Id.* (citing Gonzales v. Sansoy, 103 N.M. 127, 130, 703 P.2d 904, 907 (Ct. App. 1984)). The *McGinnis* court also cited Patton v. Mid-Continent Sys., Inc., 841 F.2d 742, 750 (7th Cir.

court noted that McGinnis failed to introduce evidence of a culpable mental state and added that breach of an employment contract did not necessitate an award of punitive damages.[70]

In addition to establishing a standard for awarding punitive damages for breach of an employment contract, the court considered an award of punitive damages for breach of a contract to build a home. In *Foley v. Horton,*[71] Herbert and Roberta Horton ("the Hortons") entered into a contract with James and Maureen Foley ("the Foleys") to build the Foleys' home. The trial court found that the Hortons failed to build the home in a workmanlike manner.[72] The trial court pointed out that the home was structurally unsafe and contained building code violations.[73] The court went on to award both compensatory and punitive damages to the Foleys.[74] The Hortons appealed.[75]

The supreme court held that where a builder uses inferior materials and violates building codes, punitive damages may be awarded.[76] The court pointed out the following facts: (1) by erecting and locking a gate at the building cite, the Hortons tried to deprive the Foleys of the protection of state building code inspection; (2) although the Hortons were not licensed to install wiring, they installed it and exposed the Foleys to unnecessary risks; and (3) the Hortons used green timbers, which became dry and warped and made the house unsafe for its occupants.[77] Thus, the supreme court found that the facts supported the trial court's award of punitive damages.[78]

B. Prejudgment Interest

New Mexico awards prejudgment interest for breach of contract as a matter of right when the amount due is "ascertainable by a mathematical calculation from a standard fixed in the contract or from established

---

1988) for the proposition that "the mere breach of a contract does not itself create a right to punitive damages: even if deliberate, the breach may be justified in some sense if the promisee can be fully compensated for the loss and the benefit to the promisor from the breach may provide society with a net gain, *i.e.*, the breach may be 'efficient.'" *McGinnis*, 110 N.M. at 9, 791 P.2d at 460.

70. *Id.*

71. 108 N.M. 812, 780 P.2d 638 (1989).

72. *Id.*

73. *Id.*

74. *Id.* at 812-13, 780 P.2d at 638-39.

75. *Id.* at 813, 780 P.2d at 639.

76. *Id.* at 814, 780 P.2d at 640. In addition to focusing on punitive damages, the *Foley* court considered whether estoppel and waiver prohibited the Foleys from suing the Hortons for breach of contract. *Id.* at 813, 780 P.2d at 639. In addressing the waiver issue, the *Foley* court followed the principles set out in Pillsbury v. Blumenthal, 58 N.M. 422, 272 P.2d 326 (1954) and Clear v. Patterson, 80 N.M. 654, 459 P.2d 358 (Ct. App. 1969), and held that acceptance of a house with latent defects does not bar a cause of action for waiver. *Foley*, 108 N.M. at 813, 780 P.2d at 639. The *Foley* Court also held that the homeowners were not estopped from suing the builder where the builder failed to rely on the homeowner in breaching a contract. *Id.*

77. *Foley*, 108 N.M. at 814, 780 P.2d at 640.

78. *Id.*

market prices."[79] Furthermore, where indebtedness can be ascertained by the calculation method, the injured party has the right to collect interest at the legal rate.[80]

In *Kueffer v. Kueffer*,[81] discussed previously,[82] the trial court denied Ms. Kueffer's claim for prejudgment interest. The supreme court pointed out that the Kueffers' contract set out a mathematical standard when it defined net proceeds.[83] The Kueffers' marital settlement contract defined net proceeds as the proceeds limited to land or money received from a third party contract less any claim the third party had been paid as a result of a certain development project.[84] The supreme court applied the New Mexico standard for awarding prejudgment interest, holding that the trial court erred by not awarding Ms. Kueffer prejudgment interest of 15% annually under New Mexico statute section 56-8-3(B).[85] The court reasoned that Mr. Kueffer could have subtracted the appropriate costs from the sale proceeds from the third party contract.[86] The court noted that to rule otherwise would encourage Mr. Kueffer to avoid prejudgment interest by contesting the amount owed.[87]

C. *Choice of Law/Statute of Limitations*

In New Mexico, statutes of limitation are procedural and not substantive for choice of law purposes. Under the substance-procedure dichotomy, procedural matters are governed by the law of the forum.[88] New Mexico also allows parties to choose the law that governs their agreement, including time to sue provisions.[89] For example, parties may include a shorter time to sue provision in a contract than is available under New

---

79. Grynberg v. Roberts, 102 N.M. 560, 562, 698 P.2d 430, 432 (1985) (amount is ascertainable where agreements between parties set out exact percentages of working interests and costs each defendant owed and where documents filed with court listed dates, invoice numbers, exact amounts due per invoice, and total amounts due for each defendant); B. McCarthy Const. v. Seegee Eng'g, 106 N.M. 781, 783, 784, 750 P.2d 1107, 1109, 1110 (1988) (where invoices to Seegee met *Grynberg* requirements); RESTATEMENT OF CONTRACTS § 337(a) (1932).

80. *Grynberg*, 102 N.M. at 562, 698 P.2d at 432. In New Mexico, when there is no written contract the legal rate of interest is 15% annually on: (1) "money due by contract;" (2) "money received to the use of another and retained without the owner's consent expressed or implied;" and (3) "money due upon the settlement of matured accounts from the day the balance is ascertained." N.M. STAT. ANN. § 56-8-3 (Repl. Pamp. 1986).

81. 110 N.M. 10, 791 P.2d 461 (1990).

82. *See supra* notes 40-53 and accompanying text.

83. *Kueffer*, 110 N.M. at 12, 791 P.2d at 463.

84. *Id.* at 11, 791 P.2d at 462. The third party was an individual named John Conron. *Id.* The Kueffer's owned a 64% interest in the net proceeds from a contract between Santa Fe Design Associates, Inc. and John Conron. *Id.* The Conron contract concerned the Conron Property Development Project. *Id.*

85. *Id.* at 12, 791 P.2d at 463. Section 56-8-3(B) prohibits an interest rate of more than 15% annually, unless a written contract fixes a different rate, "on money received to the use of another and retained without the owner's consent express or implied." N.M. STAT. ANN. § 56-8-3(B) (Repl. Pamp. 1986).

86. *Kueffer*, 110 N.M. at 12, 791 P.2d at 463.

87. *Id.*

88. Slade v. Slade, 81 N.M. 462, 463, 468 P.2d 627, 628 (1970); Sierra Life Ins. Co. v. First Nat'l Life Ins. Co., 85 N.M. 409, 413, 512 P.2d 1245, 1249 (1973).

89. Jim v. CIT Fin. Servs. Corp., 87 N.M. 362, 364, 533 P.2d 751, 753 (1975).

Mexico statutes of limitation.[90] However, the shorter time to sue provision may not conflict with New Mexico public policy.[91]

In *Nez v. Forney*,[92] Jimmy and Elizabeth Nez ("the Nezes") entered into a retail installment contract with an auto dealer in El Paso, Texas.[93] The contract was for the purchase of a Ford truck.[94] The installment contract listed an El Paso address for the Nezes.[95] The auto dealer assigned the contract to M Bank, an El Paso bank.[96] The contract contained a clause which stated that Texas law would govern the contract.[97] After the Nezes moved to the Navajo reservation in New Mexico, an employee of Max Forney repossessed the truck.[98] Forney and his employee were acting as agents for M Bank.[99] The Nezes sued for conversion, wrongful repossession, an unfair trade practice violation, and violation of Navajo Tribal Code section 607.[100] They asked for punitive damages under the conversion count.[101] The trial court granted summary judgment in favor of Forney and M Bank, and the Nezes appealed.[102]

On appeal, the supreme court held that "choice of law provisions *must* specifically describe remedial limitations, if such aspects are to be covered in addition to substantive aspects of the contract."[103] The court also held that a New Mexico statute of limitations should have been applied by the trial court.[104] In arriving at this holding, the court addressed two issues. First, the court addressed the issue of whether parties to a contract have a right to include remedial law in a choice of law agreement.[105] Second, the court considered whether the district court should have applied the New Mexico or the Texas statute of limitations.[106]

After setting out the established New Mexico law for choice of law purposes,[107] the court noted that the choice of law provision only set out that the retail installment contract would be governed by Texas law.[108] The court also noted that the contract did not include a specific statute

---

90. *See, e.g.* Turner v. New Brunswick Fire Ins. Co., 45 N.M. 126, 112 P.2d 511 (1941) (holding that a contract with a one year statute of limitations, which shortened a six year limitations period, was not void).

91. Sandoval v. Valdez, 91 N.M. 705, 707, 580 P.2d 131, 133 (Ct. App. 1978).

92. 109 N.M. 161, 783 P.2d 471.

93. *Id.*

94. *Id.*

95. *Id.*

96. *Id.*

97. *Id.*

98. *Id.*

99. *Id.*

100. *Id.* at 162, 783 P.2d at 472.

101. *Id.*

102. *Id.*

103. *Id.* at 163, 783 P.2d 473.

104. *Id.*

105. *Id.*

106. *Id.*

107. *See supra* notes 57-60. After setting out the law of New Mexico, the court stated that New Mexico's law was consistent with Sun Oil Co. v. Wortman, 486 U.S. 717 (1988), where the Supreme Court held that statutes of limitation are procedural. *Nez*, 109 N.M. at 162, 783 P.2d at 472.

108. *Nez*, 109 N.M. at 162, 783 P.2d at 472.

of limitations/time to sue provision.[109] Finally, the court limited the Nezes' choice of law provision to substantive matters.[110] The court concluded that the trial court should have applied the New Mexico statute of limitations "because New Mexico courts should apply the forum state's statute of limitations."[111]

D. Attorney's Fees

Under New Mexico law, litigants are responsible for their own attorney's fees unless statutory or other authority, such as contract terms, provide otherwise.[112] When contracting parties allocate fees in their contract, the contract controls the award of attorney's fees if a dispute arises.[113] Thus, contract interpretation determines what fees are authorized.[114]

In *Montoya v. Villa Linda Mall, Ltd.*,[115] David and Elizabeth Montoya ("the Montoyas") agreed to lease retail space from Villa Linda Mall ("the Mall").[116] The Montoyas occupied the space from July 1985 until June 1986.[117] The Montoyas alleged that prior to entering the lease agreement, the Mall misrepresented the projected occupancy of the mall and mall promotional activities.[118] The Mall subsequently relet the space.[119] The lease contract contained an article which provided that if either party sued on the lease, the losing party would pay attorney's fees.[120]

---

109. *Id.*

110. *Id.* Faced with two applicable statutes of limitation, the court held that Mr. and Mrs. Nez were not barred from filing suit under either statute. *Id.* at 163, 783 P.2d at 473. In a concurring opinion, Justice Montgomery disagreed with the majority opinion's rationale. *Id.* at 164, 783 P.2d at 474 (Montgomery, J., concurring). Although Justice Montgomery agreed that *Sun Oil* stands for the proposition that statutes of limitation are procedural, he pointed out that *Sun Oil* also stands for the notion that statutes of limitation may be procedural and substantive, under differing contexts. *Id.* Justice Montgomery wrote that the Supreme Court stated that statutes of limitation can be substantive or procedural depending on whether the issue concerns conflict of laws, full faith and credit, or the *Erie* doctrine. *Id.* Justice Montgomery wrote that the differences between substance and procedure should decide the Nez case. *Id.* Justice Montgomery might have proposed a relation test as the criteria for deciding which forum's statute of limitations is appropriate. *Id.* Furthermore, Justice Montgomery did not agree that a choice of law provision needed to describe remedial limitations. *Id.* Justice Montgomery opined that the statement "this contract shall be governed by the laws of the State of Texas" should govern all disputes under the contract. *Id.* Justice Montgomery also stated that Mr. and Mrs. Nez should be given the benefit of New Mexico law because they were New Mexico residents suing in New Mexico court for violations of New Mexico law. *Id.* at 165, 783 P.2d at 475.

111. *Id.* at 163, 783 P.2d at 473.

112. McClain Co., Inc., v. Page & Wirtz Constr. Co., 102 N.M. 284, 694 P.2d 1349 (1985). *McClain* does not stand for the proposition that a breaching party who prevails at trial cannot be awarded attorney's fees. Montoya v. Villa Linda Mall, 110 N.M. 128, 131, 793 P.2d 258, 261 (1990).

113. *See* Dennison v. Marlowe, 108 N.M. 524, 526-27, 775 P.2d 726, 728-29 (1989).

114. *Id.*

115. 110 N.M. 128, 793 P.2d 258 (1990).

116. *Id.* at 128-29, 793 P.2d 258-59.

117. *Id.* at 129, 793 P.2d 259.

118. *Id.*

119. *Id.*

120. *Id.* The specific article reads as follows:

> In the event that at any time during the term of this lease either Landlord or Tenant shall institute any action or proceeding against the other relating to the

The Montoyas sued the Mall for negligent misrepresentation and constructive fraud.[121] The Mall counterclaimed for past rent based on a breach of the lease.[122] At trial, the Montoyas did not pursue any claims based on the lease.[123] The district court ruled in favor of the Montoyas on the negligent misrepresentation and constructive fraud claims and awarded the Montoyas $42,825 in attorney's fees to be paid by the Mall.[124] The court denied the Mall's claim for $5,000 in attorney's fees.[125] The Mall appealed the district court's award of attorney's fees.[126]

The New Mexico Supreme Court upheld the district court's award of attorney's fees under the lease.[127] The court stated that where one party to a contract acts such that it precipitates a breach, a court has discretion to allow the prevailing party to recover attorney's fees despite its breach.[128]

The court then considered whether this particular contract provision authorized attorney's fees for an action sounding in tort.[129] An interpretation of the contractual provision authorizing attorney's fees to a prevailing party was essential to determining the case.[130] The court pointed out that the language of the contractual provision included suits based on tort claims which related directly to the contract.[131] Although the Montoyas' claims were in tort, the claims directly related to the leased space.[132] The court based its rationale on the portion of the lease's attorney's fees article that stated, "relating to the provisions of this lease, or any default hereunder."[133] The court specifically pointed to the use of the word "or" and stated that it ordinarily has disjunctive meaning.[134] Thus, the court stated that attorney's fees could be awarded for causes of action relating to the lease "or" to default under the lease.[135]

E. Government Contracting

During the past year, the New Mexico Supreme Court ruled on two cases where private entities entered into contracts with governments. *Scott*

---

provisions of this lease, or any default hereunder, then, and in that event, the unsuccessful party in such action or proceeding agrees to reimburse the successful party for the reasonable expenses of attorney's fees and disbursements incurred therein by the successful party.

Id.

121. *Id.* at 128, 793 P.2d at 258.
122. *Id.*
123. *Id.* at 129, 793 P.2d at 259.
124. *Id.*
125. *Id.*
126. *Id.*
127. *Id.* at 131, 793 P.2d at 261.
128. *Id.*
129. *Id.* at 129, 793 P.2d at 259.
130. *Id.*
131. *Id.*
132. *Id.*
133. *Id.* at 130, 793 P.2d at 260.
134. *Id.* (citing First Nat'l Bank v. Bernalillo County Valuation Protest Bd., 90 N.M. 110, 112, 560 P.2d 174, 176 (Ct. App. 1977)).
135. *Id.*

v. Board of Commissioners of the County of Los Alamos[136] considered whether the assessment of liquidated damages, pursuant to a contract, for untimely performance provided the basis for a claim under the Civil Rights Act. In *Gardner-Zemke Co. v. State*,[137] the New Mexico Supreme Court considered whether the trial court properly ruled that a soil report made part of a contract was unambiguous as a matter of law. The *Gardner-Zemke* court interpreted a changed condition clause.

1. Due Process and Government Contracting

The Civil Rights Act[138] provides a cause of action to people who are wrongly deprived of property by another person under the guise of a federal, state or municipal law.[139] In order for a cause of action to exist under the Civil Rights Act, a court must determine whether the following elements are present: "(1) whether the conduct complained of was committed by a person acting under color of state law; and (2) whether this conduct deprived a person of rights, privileges, or immunities secured by the Constitution or laws of the United States."[140]

In *Scott v. Board of Commissioners of the County of Los Alamos*,[141] Marc Scott contracted with the Board of Commissioners of the County of Los Alamos ("the Commissioners") and others to build a new entrance to the municipal annex building in Los Alamos.[142] The contract was to be completed on October 9, 1986, 120 days from June 11, 1986, its date of receipt.[143] The contract provided for damages of $250 per day for every day construction extended beyond the scheduled completion day.[144] The project was substantially completed seventeen days late and the county assessed damages of $8,000.[145]

Scott sued for various tort and contract claims, including a substantive due process claim under section 1983 of the Civil Rights Act.[146] The district court granted summary judgment in favor of the Commissioners.[147]

---

136. 109 N.M. 310, 785 P.2d 221 (1989).
137. 109 N.M. 729, 790 P.2d 1010 (1990).
138. 42 U.S.C. § 1983 (1981).
139. 42 U.S.C. § 1983 reads:

> [E]very person who, under color of any statute, ordinance, regulation, custom, or usage, of any State or territory or the District of Columbia, subjects, or causes to be subjected, any citizen of the United States or other person within the jurisdiction thereof to the deprivation of any rights, privileges, or immunities secured by the constitution and laws, shall be liable to the party injured in an action at law, suit in equity, or other proper proceeding for redress.

140. Parratt v. Taylor, 451 U.S. 527, 535 (1981), *overruled on other grounds*, Daniels v. Williams, 474 U.S. 327 (1986).
141. 109 N.M. 310, 785 P.2d 221 (1989).
142. *Id.* at 311, 785 P.2d at 222.
143. *Id.*
144. *Id.*
145. *Id.*
146. *Id.*
147. *Id.* at 310, 785 P.2d 221.

The district court found that section 1983 did not apply to a breach of contract claim.[148] Scott appealed.[149]

The Supreme Court of New Mexico upheld the trial court, finding that Scott's contract claim involved liquidated damages, which clearly would not rise to the level of a deprivation of a civil right that may be remedied by section 1983.[150] The court reasoned that Scott had a cognizable property interest under state law.[151] The court stated that possession of a cognizable property interest does not give a party the right to sue under the Civil Rights Act.[152] The court noted that the Civil Rights Act does not give a remedy for all wrongs committed under state law.[153] The court went on to state that deprivation of property without procedural due process by state officials is not an applicable cause of action if state law can remedy the breach.[154] Otherwise, every breach of contract suit would become a constitutional case if deprivation of property without due process were alleged.[155] Thus, the court held that procedural due process was not an issue because the state provided a remedy for Scott's cause of action.[156]

The court then considered whether Scott had a substantive due process claim. For a substantive due process claim to exist, a plaintiff must allege a deprivation of a state-created property interest and a violation of another constitutional right.[157] The court noted that Scott failed to allege that Los Alamos County's action affected one of Scott's liberty interests.[158] Thus, the court stated that a claim for liquidated damages could not be classified as a deprivation of a civil right under the Civil Rights Act.[159] As a result of the court's ruling, causes of action under the Civil Rights Act can no longer be brought against the state for breach of contract.

2. Reporting Discrepancies to Government

In New Mexico, pre-bid documents integrated into a contract are interpreted under accepted rules of contract law. For example, misleading pre-bid documents are a breach of the implied warranty of correctness.[160] Moreover, whether a contract must be adjusted because of a change in conditions is a question of law.[161]

148. *Id.* at 311, 785 P.2d at 222.
149. *Id.* at 310, 785 P.2d at 221.
150. *Id.* at 313, 785 P.2d at 224.
151. *Id.* at 312, 785 P.2d at 223 (citing Logun v. Zimmerman Brush Co., 455 U.S. 422 (1982)).
152. *Id.*
153. *Id.*
154. *Id.*
155. *Id.*
156. *Id.*
157. *Id.* at 313, 785 P.2d at 224.
158. *Id.*
159. *Id.*
160. *See* Vinnell Corp. v. State, 85 N.M. 311, 512 P.2d 71 (1973).
161. *See* T.F. Scholes, Inc. v. United States, 357 F.2d 963 (Ct. Cl. 1966).

In *Gardner-Zemke Co. v. State*,[162] the Gardner-Zemke Company ("Gardner-Zemke") entered into a contract with the State of New Mexico to help build the Las Cruces Medium Security Facility.[163] The bid documents sent to Gardner-Zemke contained a soil report.[164] Defendant Fox & Associates, Inc. prepared the soil report.[165] Gardner-Zemke relied in part on the soil report in calculating its bid.[166] Gardner-Zemke interpreted the report to state that the soil consisted primarily of sand.[167] Because portions of the soil actually contained limestone and caliche rather than sand, the trenching costs incurred by Gardner-Zemke were higher than expected.[168] As a result, Gardner-Zemke sued for its excess costs under the contract's changed condition clause.[169] The district court granted summary judgment in favor of the state and Gardner-Zemke appealed.[170]

On appeal, the New Mexico Supreme Court held that because Gardner-Zemke failed to notice the contradictions between the narrative and technical sections of the soil report and failed to report the discrepancy to the government, Gardner-Zemke's claim could not prevail.[171] The court found that the pre-bid documents, including the soil report, were part of the contract.[172] The court then explained that success on a changed

---

162. 109 N.M. 729, 790 P.2d 1010 (1990).
163. *Id.* at 730, 790 P.2d at 1011.
164. *Id.*
165. *Id.*
166. *Id.*
167. *Id.*
168. *Id.* at 731, 790 P.2d at 1012.
169. *Id.* The clause provided that the contract could be equitably adjusted if subsurface conditions differed materially from what the contractor reasonably expected. *Id.*
170. *Id.* at 730, 790 P.2d at 1011.
171. *Id.* at 735, 790 P.2d at 1016 (citing Beacon Constr. Co. v. United States, 314 F.2d 501 (Ct. Cl. 1963)).
172. *Id.* at 733, 790 P.2d at 1014. As part of the contract, the court stated that the pre-bid documents should be interpreted under the following canons of contract construction:

> 1. Interpretation of a contract to determine whether a condition encountered is a changed condition allowing an equitable adjustment of the contract is a question of law. *Id.* (citing T.F. Scholes, Inc. v. United States, 357 F.2d 963 (Ct. Cl. 1966)).
> 2. Whether an ambiguity exists is a question of law. *Id.* (citing Levenson v. Mobley, 106 N.M. 399, 744 P.2d 174 (1987)).
> 3. If the contract is found to be ambiguous, the meaning of the ambiguous terms is a question of fact. *Id.* (citing Segura v. Molycorp, Inc., 97 N.M. 13, 636 P.2d 284 (1981)).
> 4. The drafter of a document must use language conveying its intent. If the language has more than one interpretation, it is interpreted against the drafter. *Id.*. (citing Smith v. Tinley, 100 N.M. 663, 674 P.2d 1123 (1984)).
> 5. The rule stated in *Smith* applies only where courts cannot otherwise ascertain the intent of the parties. *Id.* (citing El Paso Natural Gas Co. v. Western Bldg. Assocs., 675 F.2d 1135 (10th Cir. 1982)).
> 6. A contract is not automatically ambiguous where a disagreement over the meaning of specification exists. A contract must be susceptible to various interpretations and the contractor's interpretation has to be reasonable. *Id. See Levenson*, 106 N.M. at 401, 744 P.2d at 176; *see also* Major v. Bishop, 462 F.2d 1277 (10th Cir. 1972).
> 7. A reasonable interpretation is consistent with the language of the contract. Courts must consider the language of the entire contract and cannot depend on selected portions of the contract to support a finding of ambiguity. *Gardner-Zemke Co.*, 109 N.M. at 734, 790 P.2d at 1015 (citing Lindbeck v. Bendziunas, 84 N.M. 21, 498 P.2d 1364 (Ct. App. 1972)).

condition claim requires a showing that the contractor was "reasonably unaware" the condition existed.[173] A contractor is "reasonably unaware" of a changed condition if: (1) the contractor relied on representations made about the site; or (2) was the victim of a hidden condition.[174] The court noted that Gardner-Zemke failed to read the whole contract.[175] Thus, the court ruled that Gardner-Zemke could not argue it was reasonably unaware of conditions set out in the unread portion of the contract.[176]

III. BULK TRANSFERS

The Bulk Transfers Act ("the Act")[177] is necessary to help prevent fraudulent transfers of commercial property.[178] The notice requirement included in the Act[179] is essential to avert fraudulent transfers because it allows creditors to investigate transfers to determine whether the creditors should take action to protect their interests.[180] When the seller of commercial property has not followed the notice requirement in the Act,[181] the Act provides that the "transfer" is "ineffective" as to creditors of

---

173. *Gardner-Zenke Co.*, 109 N.M. at 734, 790 P.2d at 1015.

174. *Id.* (citing J. MCBRIDE & I. WACHTEL, GOVERNMENT CONTRACTS § 29.20 (Rev'd 1989)).

175. *Id.*

176. *Id.*

177. Bulk Transfers Act, N.M. STAT. ANN. §§ 55-6-101 to -110 (Supp. 1991).

178. *Id.* § 55-6-101, official comment 2.

179. N.M. STAT. ANN. § 55-6-104 (Cum. Supp. 1991) is the notice requirement within the Bulk Transfers Act. It states as follows:

(1) Except as provided with respect to auction sales (Section 6-107 [55-6-107 NMSA 1978]), a bulk transfer subject to this article is ineffective against any creditor of the transferor unless:

(a) the transferee requires the transferor to furnish a list of his existing creditors prepared as stated in this section; and

(b) the parties prepare a schedule of the property transferred sufficient to identify it;

(c) the transferee preserves the list and schedule for six months next following the transfer and permits inspection of either or both and copying therefrom at all reasonable hours by any creditor of the transferor, or files the list and schedule in the office of the secretary of state and, in addition, if the debtor has a place of business in only one county of this state, also in the office of the county clerk of such county, or, if the debtor has no place of business in this state, but resides in the state, also in the office of the county clerk of the county in which he resides.

(2) The list of creditors must be signed and sworn to or affirmed by the transferor or his agent. It must contain the names and business addresses of all creditors of the transferor, with the amounts when known, and also the names of all persons who are known to the transferor to assert claims against him even though such claims are disputed. If the transferor is the obligor of an outstanding issue of bonds, debentures or the like as to which there is an indenture trustee, the list of creditors need include only the name and address of the indenture trustee and the aggregate outstanding principal amount of the issue.

(3) Responsibility for the completeness and accuracy of the list of creditors rests on the transferor, and the transfer is not rendered ineffective by errors or omissions therein unless the transferee is shown to have had knowledge.

180. *Id.* § 55-6-101, official comment 3.

181. *Id.* § 55-6-104.

the seller.[182] In other words, creditors of the seller may execute against the property of the buyer after the sale has been made.

During the survey period, the supreme court addressed the issue of proper notice pursuant to the Bulk Transfers Act and interpreted language in the Act in favor of future creditors. In *Professional Insurors, Inc. v. Buck Scott & Son Motor Co., Inc.*,[183] Professional Insurors, Inc. ("Professional Insurors") brought suit against Buck Scott & Son Motor Company ("Buck Scott Motors"), Buck and Claravon Scott ("the Scotts"), and Richard Blanken to recover for insurance premiums owed by Buck Scott Motors following a bulk transfer of the corporate assets to Blanken.[184]

In July 1986, Buck Scott Motors agreed to sell its corporate assets to Blanken.[185] In October 1986, Blanken sent notice to the creditors of Buck Scott Motors according to the Bulk Sales Act; however, there was some question as to the accuracy of this notice.[186] The notice listed Buck Scott Motors' total debt as $495,000, but the actual amount of the debt exceeded one million dollars.[187] The notice also listed the consideration to be paid by Blanken to Buck Scott Motors as $562,000, even though Blanken actually paid $778,000 in consideration.[188] The discrepancies resulted from the omission of $801,380 owed to one of Buck Scott Motors' creditors, Barclays American/Financial, Inc. ("Barclays").[189] On the notice sent to the creditors, the amount owed to Barclays was listed as "unknown."[190]

After the sale, Buck Scott Motors immediately paid Barclays the total $778,000 received from Blanken from the sale of the assets.[191] Therefore, no funds were available from the proceeds of the sale to pay any of the other creditors listed on the notice.[192] Professional Insurors was one of the other creditors listed on the notice.[193]

Professional Insurors brought suit against Buck Scott Motors and Blanken to recover the debt.[194] The district court granted Blanken summary judgment on Professional Insurors' claim of defective notice under the Act.[195] Professional Insurors appealed the judgment.[196]

The New Mexico Supreme Court broke down the major issue of whether proper notice was given into two issues.[197] The first issue involved determining whether Blanken actually knew the amount of the "unknown"

182. *Id.* § 55-6-105.
183. 110 N.M. 299, 795 P.2d 991 (1990).
184. *Id.* at 300, 795 P.2d at 992.
185. *Id.*
186. *Id.*
187. *Id.*
188. *Id.*
189. *Id.*
190. *Id.*
191. *Id.*
192. *Id.*
193. *Id.*
194. *Id.*
195. *Id.*
196. *Id.*
197. *Id.* at 301, 795 P.2d at 993.

debt to Barclays.[198] The second issue was the determination of whether the Act was properly followed.[199]

In addressing the first issue, the court stated that the Act requires the amount of the debt owed to any creditor to be listed when the amount is known.[200] The court determined that Blanken admittedly had notice that Barclays was a creditor and that he had knowledge of the relative size of the debt.[201] Blanken argued that he was required to know the precise amount of the debt.[202] The court decided that "[t]his burden . . . would be too exacting. He (transferee) may not have had knowledge of the exact amount of the debt, but we find that to be irrelevant."[203] Because Blanken had knowledge of the relative size of the debt, he was obligated to provide a reasonable estimate of the debt.[204] Blanken could not hide behind the claim that the exact amount of the debt was unascertainable.[205]

In addressing the second issue, the court determined that the notice was improper and ineffective.[206] Rather than giving the creditor warning that steps might need to be taken in order to protect its interest, the notice lulled the creditor into a false sense of security.[207] The notice gave the appearance that debts would be payable out of the proceeds of the transaction and induced the creditor to sit by passively.[208] Therefore, the court held that "a transferee cannot turn a blind eye to the circumstances surrounding the transaction to the detriment of creditors, and we believe the principle regarding sufficiency of notice applies to this case."[209] Thus, the court reversed the summary judgment of the district court and remanded the case for trial in accordance with the above principles.[210]

IV. SECURED TRANSACTIONS

A. Commercially Reasonable Disposition of Secured Collateral

The New Mexico Supreme Court addressed the commercial reasonableness of a sale of secured collateral when a debtor has defaulted in *First National Bank of Dona Ana County v. Ruttle*.[211] The *Ruttle* court

198. *Id.*
199. *Id.*
200. *Id.*; *see supra* note 158.
201. *Buck Scott*, 110 N.M. at 301, 795 P.2d at 993.
202. *Id.* at 302, 795 P.2d at 994.
203. *Id.*
204. *Id.* at 304, 795 P.2d at 996.
205. *Id.* at 303, 795 P.2d at 995.
206. *Id.* at 303-04, 795 P.2d at 995-96.
207. *Id.* at 304, 795 P.2d at 996.
208. *Id.*
209. *Id.*
210. *Id.*
211. 108 N.M. 687, 778 P.2d 434 (1989).

evaluated the reasonableness of a foreclosure sale based on factors previously established in *Villella Enterprises, Inc. v. Young*.[212]

In *Ruttle*, the First National Bank of Dona Ana County ("First National") secured six pieces of equipment belonging to John Ruttle in return for Ruttle's promise to pay a promissory note.[213] Ruttle did not pay the promissory note and First National repossessed the six pieces of equipment.[214] First National then sold five of the six pieces of equipment at a public auction.[215] First National sold the sixth piece of equipment, a tractor, at a private sale to a company in the business of buying and selling new and used equipment.[216] The amounts received from the above sales were not enough to sufficiently cover the balance of the promissory note owed by Ruttle.[217] Therefore, First National sued Ruttle for the deficiency.[218] The district court entered a deficiency judgment in favor of First National.[219] Ruttle appealed the trial court's finding that the equipment was sold for commercially reasonable amounts.[220] In his appeal, Ruttle argued that First National failed to provide written notice of the sale of the equipment.[221]

The supreme court acknowledged that failure to provide written notice is not an absolute bar to a deficiency judgment.[222] New Mexico law requires "reasonable notification" of the time and place of a public sale or of the date after which a private sale is to be made.[223]

---

212. 108 N.M. 33, 766 P.2d 293 (1988). The court in *Villella* established that "every aspect of the disposition of the collateral, including the method, manner, time, place, and terms must be commercially reasonable, and that reasonable notification of the time and place of any public sale shall be sent by the secured party to the debtor." *Id.* at 35, 766 P.2d at 295. Furthermore, the court stated that in determining commercial reasonableness, "each case will turn on its particular facts; but, generally, in response to a motion for summary judgment, evidence adduced by the debtor as to any aspect of the sale . . . will be pertinent." *Id.*

213. *Ruttle*, 108 N.M. at 688, 778 P.2d at 435.

214. *Id.*

215. *Id.*

216. *Id.*

217. *Id.*

218. *Id.*

219. *Id.*

220. *Id.* at 689, 778 P.2d at 436.

221. *Id.* Ruttle also argued that First National sold the equipment at a value that was below the equipment's market value, and that the means of the disposition was not in accordance with N.M. STAT. ANN. § 55-9-504(3). *Id.* Furthermore, Ruttle complained that First National had: (1) insufficiently advertised prior to the auction; (2) failed to negotiate over the auctioneer's fee; (3) failed to wash or paint the equipment sold at auction in order to secure the best price; and (4) would only accept cash or a certified check at the time of sale. *Id.*

The court examined the evidence and decided that there was substantial evidence that the price received for the collateral was commercially reasonable, and the disposition of the collateral was commercially reasonable. *Id.* at 690, 778 P.2d at 437.

222. *Id.* at 689, 778 P.2d at 436.

223. N.M. STAT. ANN. § 55-9-504(3) (1978) provides:

> Unless collateral is perishable or threatens to decline speedily in value or is of a type customarily sold on a recognized market, reasonable notification of the time and place of any public sale or reasonable notification of the time after which any private sale or other intended disposition is to be made shall be sent by the secured party to the debtor, if he has not signed after default a statement renouncing or modifying this right to notification of sale.

In this case, First National did not give the proper notice.[224] Nevertheless, despite First National's non-compliance with the notice provision,[225] First National could still secure a deficiency judgment if First National proved the market value of the collateral.[226] Ruttle did not argue that First National failed to prove the market value of the collateral by introduction of appropriate independent evidence.[227] Rather, he argued that failure to give proper notice rendered the sale commercially unreasonable and requested a conclusion of law that First National was barred from asserting any deficiency because of the commercially unreasonable sale.[228] The court ruled that Ruttle waived the right to raise on appeal the absence of proof of the fair market value of the collateral.[229]

In effect, the court decided that arguing insufficient compliance with the notice provision is not enough.[230] The debtor must also assert and provide evidence that the secured party sold the collateral property for less than the market value of the collateral.[231] To merely argue the first tier of the improper notice requirement will not suffice when trying to prove that a secured party has not complied with the notice provision.[232]

Ruttle did not properly make his argument to the court concerning the notice requirement, and by applying the standards first provided in *Villella Enterprises, Inc. v. Young*,[233] the *Ruttle* court concluded that there was substantial evidence of commercial reasonableness as to each aspect of the sale on which Ruttle purportedly adduced evidence to the contrary.[234] Therefore, the court affirmed the district court's ruling.[235]

B. Classification of Capital Retains in UCC and Proper Description in a Financing Statement

During the survey period, the supreme court determined that a capital retains account should be classified as a "general intangible" when determining priority between two subordinate lienholders.[236] The court also adopted the rule that the description of collateral in a financing statement which states "all accounts and contract rights arising from the

---

224. Ruttle argued that the sale of the six pieces of equipment at issue did not comply with N.M. STAT. ANN. § 55-9-504(3) because he was not notified at all as to the private sale of the tractor, nor given written notice of the sale of the other equipment at auction. *Ruttle*, 108 N.M. at 689, 778 P.2d at 436. Ruttle did testify that although he knew his property was being stored by the auction company and heard about the auction on the radio several days in advance, he never received notice from the bank that his property was among that to be sold. *Id.*

225. *Id.*

226. *Id.* (citing Clark Leasing Corp. v. White Sands Forest Prods., Inc., 87 N.M. 451, 456, 535 P.2d 1077, 1082 (1975)).

227. *Id.* at 690, 778 P.2d at 437.

228. *Id.*

229. *Id.*

230. *Id.*

231. *Id.*

232. *Id.*

233. *Villella*, 108 N.M. at 35, 766 P.2d at 295.

234. *Ruttle*, 108 N.M. at 691, 778 P.2d at 438.

235. *Id.*

236. Valley Fed. Sav. Bank v. Stahl, 110 N.M. 169, 172, 793 P.2d 851, 854 (1990).

sale or other disposition of . . . dairy products" is sufficient to put third parties on inquiry notice of a prior encumbrance on capital retains.[237]

In *Valley Federal Savings Bank v. Stahl*,[238] Vernon and Marcia Stahl were members of the Associated Milk Producers ("the Cooperative"), a cooperative association.[239] The Stahls had accumulated a balance of over $100,000 in their capital retains account.[240] The Stahls also owed the Cooperative over $70,000 for equipment purchased in July of 1984.[241] Because the Stahls owed the Cooperative $70,000, the Cooperative's bylaws reserved to the Cooperative a first lien upon the Stahls' capital retains to the extent of any claim the Cooperative had against them.[242] To further evidence the Cooperative's interest in the equipment, the Stahls signed a security agreement with the Cooperative.[243] The security interest was perfected by the Cooperative's filing of financing statements on August 20, 1984.[244] The description of the collateral included: "All equities issued or to be issued by [Associated Milk Producers]."[245] The Cooperative claimed that the description describes the Stahls' capital retains account.[246]

The Stahls also owed money to the Bank of America ("the Bank"), and incident to the loan agreements between the Stahls and the Bank, the Stahls granted to the Bank a security interest in collateral described in the financing statement as "all accounts and contract rights arising from the sale or other disposition of . . . dairy products."[247] This security interest was also perfected by way of filing financing statements with the county clerk on December 7, 1983.[248]

The Stahls subsequently defaulted on their debts.[249] A third party[250] induced the original action against the Stahls to collect money due and to foreclose on a real estate mortgage and personal property liens.[251] The district court originally held that the Bank's security interest had priority over the Cooperative's interest.[252]

---

237. *Id.* at 173, 793 P.2d at 855.
238. 110 N.M. 169, 793 P.2d 851 (1990).
239. *Id.* at 170, 793 P.2d at 852. For purposes of this article, the terms "cooperative association" or "cooperative" refer to a combination of persons, either natural or artificial, organized on a cooperative basis for the mutual benefit of its members. Members are also entitled to the association's net earnings or net proceeds in proportion to the volume of business transacted by each of the members.
240. *Id.* In other words, the Stahls were entitled to over $100,000 of the cooperative's past net profits.
241. *Id.*
242. *Id.*
243. *Id.*
244. *Id.*
245. *Id.*
246. *Id.*
247. *Id.* at 170-71, 793 P.2d at 852-53.
248. *Id.* at 171, 793 P.2d at 853.
249. *Id.* at 170, 793 P.2d at 852.
250. The third party originally bringing this action was Valley Federal Savings Bank. *Id.* at 169, 793 P.2d at 851.
251. *Id.*
252. *Id.*

The trial court based its decision on the fact that the Bank perfected its security interest on December 7, 1983, whereas the security interest of the Cooperative was perfected at the later date of August 20, 1984.[253] The Cooperative appealed the trial court's grant of priority in the capital retains to the Bank.[254] The supreme court considered the issue of priority in the capital retains account between the two lienholders, Associated Milk Producers and Bank of America.[255]

The Cooperative first argued that the trial court incorrectly concluded that the Stahls had rights in and to their capital retains that could be made subject to a lien (*i.e.*, the Cooperative argued that capital retains were not property of the Stahls in which they could grant a security interest).[256] The supreme court disagreed with the Cooperative's logic.[257] The court stated that capital retains are income to the member in the form of an equity interest, and that capital retains are subject to the claims of creditors.[258] The capital retains account was classified as a "general intangible."[259]

The Cooperative then asserted that its security agreement was first in priority because "accounts and contract rights" as used in the Bank's financing statement of December 7, 1983 did not adequately describe the capital retains account.[260] The court weighed this argument by considering the questions of attachment,[261] perfection,[262] and priority[263] of the two liens as governed by article 9 of the Uniform Commercial Code.[264] The court determined that the Bank's interest in the capital retains had attached.[265] Furthermore, the court concluded that the Bank would have

253. *Id.* at 171, 793 P.2d at 853.
254. *Id.* at 169, 793 P.2d at 851.
255. *Id.* at 170, 793 P.2d at 852.
256. *Id.* at 171, 793 P.2d at 853.
257. *Id.*
258. *Id.* The court stated that a member's right to payment of the capital retains is governed by the bylaws of the Association. *Id.* (citing *In re* Shiflett, 40 Bankr. 493, 495 (W.D. Va. 1984)). Furthermore, the court stated that the Cooperative's bylaws allowed the Cooperative to "retain from the proceeds received with respect to the sale of products marketed for each patron an amount which is fixed without reference to net earnings" and which "shall be considered a capital contribution." *Id.* From this the court deduced that the capital retains were a property interest to the Stahls. *Id.*
259. *Id.* A general intangible is "any personal property (including things in action) other than goods, accounts, chattel paper, documents, instruments and money." N.M. STAT. ANN. § 55-9-106 (Repl. Pamp. 1987).
260. *Stahl*, 110 N.M. at 171, 793 P.2d at 853.
261. *Id.* at 172, 793 P.2d at 854. A security agreement is enforceable against the debtor once the agreement has attached and then been perfected. *Id.* For a security agreement to attach, the debtor must have rights in the collateral. N.M. STAT. ANN. § 55-9-203(1)(c) (Repl. Pamp. 1987). Thus, because the court held capital retains to be property, the debtor may grant a security interest in capital retains.
262. *Stahl*, 110 N.M. at 172, 793 P.2d at 854. Perfection of any security interest is dependent upon an adequate filing. N.M. STAT. ANN. §§ 55-9-302(1) to -305 (Repl. Pamp. 1987).
263. *Stahl*, 110 N.M. at 172, 793 P.2d at 854. Priority pertains to the question of who attached and perfected their interest in the property first. *Id.*
264. *Id.* Article 9 of the Uniform Commercial Code specifically applies to general intangibles. *See* N.M. STAT. ANN. § 55-9-103(3) (Repl. Pamp. 1987).
265. *Stahl*, 110 N.M. at 172, 793 P.2d at 854.

priority if the financing statement was adequately filed.[266] Therefore, the main issue before the court was whether the Bank's description of the collateral was proper so as to put third parties on inquiry notice of the existence of a security agreement.[267]

The court stated that whether the description of the collateral was adequate was a question of law and not a question of fact.[268] The court determined that the description in the financing statement sufficiently put third parties on inquiry notice of a prior encumbrance on capital retains.[269] The court rationalized that under the bylaws of the Cooperative, the Stahls had a "contractual right," in a non-technical sense, to the capital retains.[270] Therefore, the Bank's financing statement adequately gave notice to the public because it mentioned "contract rights arising from the sale or other disposition of dairy products" in the description of the collateral.[271] Thus, the supreme court affirmed the district court's judgment.[272]

V. NOTES

A. Status of Guarantors

During the survey period, the supreme court ruled that a personal guarantor, by terms of an "assumption of indebtedness" agreement, did not become a co-maker or co-debtor with the original note maker.[273] Under this rule, a subsequent release of the guarantors did not release the original makers of the note to the extent of their right of contribution.

In *Sunwest Bank of Farmington v. Kennedy*,[274] Don, Sharon, Edith and Troy Kennedy ("the Kennedys") borrowed $165,000 from Sunwest Bank of Farmington ("Sunwest") in September of 1982.[275] The use of the funds was for Kennedy, Inc., a corporation owned by the Kennedys.[276] The corporation and the Kennedys were primarily liable for the note; in addition, the Kennedys also each signed an "unconditional and continuing guaranty" obligating them to "pay any and all liabilities, obligations or indebtedness, of any kind or nature" of Kennedy, Inc.[277]

In December 1984, the Kennedys sold their interest in Kennedy, Inc. to James Copeland, James Clark, Charlie Craven, and Santex, Inc., the

---

266. *Id.*
267. *Id.*
268. *Id.*
269. *Id.* at 173, 793 P.2d at 855.
270. *Id.*
271. *Id.*
272. *Id.*
273. Sunwest Bank of Farmington v. Kennedy, 109 N.M. 400, 785 P.2d 740 (1990).
274. *Id.*
275. *Id.* The Kennedys actually borrowed the money from Valley Bank, the predecessor of Sunwest Bank. *Id.* The note's original term was one year; however, Valley Bank and the Kennedys contemplated annual renewals allowing the note to be repaid over a ten-year period. *Id.* The note was extended twice, in September of 1983 and September of 1984. *Id.* at 401, 785 P.2d at 741.
276. *Id.* Kennedy, Inc.'s principal line of business was the operation of a car dealership. *Id.*
277. *Id.* at 400, 401, 785 P.2d at 740, 741.

other defendants in the action.[278] The Kennedys remained both primarily liable and liable as guarantors on the note.[279] Copeland, Clark and Craven also executed personal guaranties on the payment of the note.[280] Copeland and Clark eventually bought out the interests of Craven and Santex, Inc.[281] Sunwest subsequently released Craven from his personal guaranty.[282] The release of Craven's personal guaranty was done without any notice to the Kennedys.[283] The parties subsequently defaulted on the note, and Sunwest brought suit to collect the amount of over $100,000 still owed.[284] The district court granted summary judgment to Sunwest Bank.[285] The Kennedys appealed.[286]

The issue on appeal was whether Sunwest Bank, by releasing Craven from his personal guaranty of the note without notice to the Kennedys, effected a discharge of the Kennedys' liability on the note.[287] The Kennedys argued that such a release by the holder of a note operates to discharge the obligations of subsequent parties and co-debtors who are jointly and severally bound, absent the maker's approval.[288] The court decided the Kennedys' release from the note depended upon the elevation of Craven and Santex to the status of co-maker or co-debtor.[289]

The Kennedys argued that a maker of a note is a party who "engages that he will pay the instrument according to its tenor at the time of his engagement."[290] The Kennedys further asserted that Copeland and Craven, when they assumed the indebtedness, became makers by agreeing to be co-equal with the Kennedys.[291] The court decided, however, that because neither Craven nor Santex was a party to the original agreement executed between Sunwest and the Kennedys, neither Craven nor Santex was a co-maker.[292]

Thus, the court stated, "[i]t is apparent . . . that the Kennedys' argument that Craven and Santex were co-makers fails."[293] The court determined that "[S]unwest's release of their [Craven and Santex] obligations is irrelevant to the Kennedys' on-going liability."[294]

---

278. *Id.* at 401, 785 P.2d at 741.
279. *Id.*
280. *Id.*
281. *Id.*
282. *Id.* Sunwest released Craven from his personal guarantee in August 1985. *Id.* At the same time, Kennedy, Inc., now doing business as Copeland-Craven Pontiac, Oldsmobile-Nissan, Inc., executed a modification of the note which contemplated amortizing the note over three years. *Id.*
283. *Id.*
284. *Id.*
285. *Id.* at 400, 785 P.2d at 740.
286. *Id.*
287. *Id.* at 401, 785 P.2d at 741.
288. *Id.*; *see* Wood v. Eminger, 44 N.M. 636, 641, 107 P.2d 557, 560 (1940).
289. *Kennedy*, 109 N.M. at 401, 785 P.2d at 741.
290. *Id.* The Kennedys were quoting N.M. STAT. ANN. § 55-3-413(1) (1978).
291. *Kennedy*, 109 N.M. at 401, 785 P.2d at 741.
292. *Id.* at 402, 785 P.2d at 742.
293. *Id.*
294. *Id.*

B. *Materially Altered Obligation*

An original maker of a note may be discharged from his obligation if a material alteration is made in the renewal of the note without the original maker's consent.[295] During the survey period, the supreme court shed new light on the "material alteration" rule.

In addition to the argument in the preceding section in *Sunwest Bank of Farmington v. Kennedy*,[296] the Kennedys argued that Sunwest Bank, by releasing co-guarantors and by extending the time period for payment of the note,[297] had materially altered the terms of the note without the Kennedys' consent, thus discharging the Kennedys' obligation.[298]

The Kennedys contended that because Copeland and Clark extended the note after the sale of Kennedy, Inc., the Kennedys should be discharged from their liability.[299] The court distinguished this case from *First National Bank in Albuquerque v. Abraham*,[300] the case that first stated the "material alteration" rule. *Abraham* involved a renewal rather than an extension.[301] The court determined that the Kennedys should not be discharged from their obligation because Copeland and Clark merely extended the note as opposed to renewing it.[302] Thus, the court affirmed the district court's grant of summary judgment to Sunwest Bank.[303]

C. *Extent of Unwritten Condition on Guarantor's Liability*

When dealing with a bank or savings and loan, individuals and businesses secure all agreements in writing. Under the Federal Deposit Insurance Act:[304]

> No agreement which tends to diminish or defeat the . . . interest of the [Federal Deposit Insurance] Corporation ("the FDIC") . . . shall be valid against the Corporation unless such agreement (1) shall be in writing, (2) shall have been executed by the bank and the person or persons claiming an adverse interest thereunder . . . , (3) shall have been approved by the board of directors of the bank or its loan committee, which approval shall be reflected in the minutes of said board or committee, and (4) shall have been, continuously, from the time of execution, an official record of the bank.[305]

The above rule allows both federal and state bank examiners to rely completely on a bank's records when evaluating its assets pursuant to liquidation of assets or providing financing for purchases of assets and

---

295. *Id.*
296. 109 N.M. 400, 785 P.2d 740 (1990).
297. *See supra* notes 249-56 and accompanying text.
298. *Kennedy*, 109 N.M. at 402, 785 P.2d at 742.
299. *Id.* at 403, 785 P.2d at 743.
300. 97 N.M. 288, 639 P.2d 575 (1982).
301. *Id.* at 291, 639 P.2d at 578.
302. *Kennedy*, 109 N.M. at 403, 785 P.2d at 743.
303. *Id.*
304. 12 U.S.C. §§ 1811-1833 (1989).
305. *Id.* § 1823(e).

liabilities by another bank.[306] Usually, these evaluations must be made with great speed in order to preserve the ongoing concern value of the failed bank and avoid an interruption in banking services.[307] If unwritten agreements were allowed, examiners' evaluations would not be accurate because of the uncertainty involved in each transaction.[308] In short, the FDIC "does not simply step into the private shoes of the local bank . . . ."[309] So, in effect, an oral agreement between a bank officer and an individual is not considered to be any agreement at all between the FDIC and the individual.

In *FDIC v. Alto Construction Co., Inc.*,[310] George Cliff, Thomas Deason, George Slaughter, and Hal Cliff were the four shareholders of Alto Construction Company, Inc. ("Alto").[311] Hal Cliff was the president and ran the day-to-day operations of the corporation.[312] George Cliff, Deason, and Slaughter executed unlimited guaranties in favor of First City National Bank ("First City") guaranteeing the indebtedness of Alto.[313]

Purportedly without the knowledge of the other shareholders of Alto, Hal Cliff entered into a partnership on behalf of the corporation with several other individuals and business entities.[314] The resulting general partnership was called the "Westsun Group" ("Westsun").[315] Westsun borrowed $178,000 from First City in return for a mortgage on a parcel of land Westsun purchased.[316] Hal Cliff and other Westsun partners gave personal guaranties on the note.[317] George Cliff, Deason, and Slaughter did not directly participate in these transactions, nor did they give guaranties specifically to secure the Westsun note.[318]

Westsun and Alto subsequently defaulted on various notes held by First City.[319] Deason and Slaughter met with the president of First City to discuss the Westsun loan and the other outstanding obligations of Alto.[320] At this meeting, Deason and Slaughter acknowledged that the Westsun note was an obligation of Alto, but the bank stated that it intended to seek repayment only from those persons who signed guaranties on behalf of Westsun.[321] Deason and Slaughter entered into an agreement with the bank to restructure the three remaining notes and entered into

306. FDIC v. Alto Constr. Co., Inc., 109 N.M. 165, 168, 783 P.2d 475, 478 (1989).
307. *Id.*
308. *Id.*
309. *Id.* (quoting FDIC v. Tito Castro Constr. Co., 548 F. Supp. 1224, 1226 (D.P.R. 1982), *aff'd*, 741 F.2d 475 (1st Cir. 1984)).
310. 109 N.M. 165, 783 P.2d 475 (1989).
311. *Id.* at 166, 783 P.2d at 476.
312. *Id.*
313. *Id.*
314. *Id.*
315. *Id.*
316. *Id.*
317. *Id.*
318. *Id.*
319. *Id.*
320. *Id.*
321. *Id.*

new guaranties to cover those notes.[322] The Westsun note was not covered under this agreement or the new guaranties.[323]

Subsequently, the FDIC closed the bank and began liquidating its assets.[324] The FDIC brought suit against the partners of Westsun, including Alto Construction Company, George Cliff, Deason, and Slaughter for foreclosure on the Westsun property and any deficiency remaining after the foreclosure sale.[325] The district court granted FDIC's motion for summary judgment on the individual liability of defendants George Cliff, Deason, and Slaughter.[326] George Cliff, Deason, and Slaughter appealed.[327]

The supreme court addressed whether George Cliff, Deason, and Slaughter intended the guaranties executed prior to the formation of Westsun to secure Alto's obligations as one of Westsun's partners.[328] George Cliff, Deason, and Slaughter framed their argument in two ways. First, they stated that they intended the guaranties to cover only those obligations of Alto that related to its home building activities.[329] Because guaranties are a species of contract, they argued, if there was no meeting of minds over the subject of financial obligations unrelated to Alto's home building activities, then the guaranties did not cover such activities and the FDIC was precluded from enforcing the guaranties.[330] Second, George Cliff, Deason, and Slaughter alleged that the bank understood and agreed that the guaranties would only cover Alto's home building activities.[331] The court did find that the bank understood and agreed that the guaranties would only cover Alto's home building activities; however, the court applied the applicable federal law under the Federal Deposit Insurance Act[332] and concluded that summary judgment was proper.[333]

The court found that under the Federal Deposit Insurance Act, the resulting unwritten condition alleged by George Cliff, Deason, and Slaughter, whether a secret agreement with the bank or their own unilateral understanding, did not provide a defense against the FDIC.[334] The court reasoned that to do so would "tend to diminish or defeat the interest of FDIC and mislead banking authorities as to the true status of a bank's assets."[335] Thus, the court affirmed the judgment of the trial court.[336]

---

322. *Id.*
323. *Id.*
324. *Id.*
325. *Id.* at 167, 783 P.2d at 477.
326. *Id.* Hal Cliff was not a party to the appeal. *Id.* at 166, 783 P.2d at 476.
327. *Id.* at 166, 783 P.2d at 476.
328. *Id.* at 167, 783 P.2d at 477.
329. *Id.*
330. *Id.*
331. *Id.*
332. 12 U.S.C. § 1823(e) (1989).
333. *Alto Construction Co.*, 109 N.M. at 168, 783 P.2d at 478.
334. *Id.*
335. *Id.*
336. *Id.* at 169, 783 P.2d at 479.

VI. AGENCY

A. Limitation on Attorney's Capacity to Pay Witness Fees

When an agent's authority from her principal is limited and that limitation is communicated to a third person, the principal is not liable to the third person for the agent's acts in excess of the limitation.[337] In addition, a person dealing with an agent is required to use reasonable diligence and prudence in ascertaining the limits of the agent's authority.[338] In *Comstock v. Mitchell*,[339] the court addressed issues concerning limitations on an attorney's capacity to pay witness fees.

In *Comstock*,[340] Josephine Mitchell hired Ed Yudin to represent her in a divorce action.[341] Mitchell and Yudin hired Frederick Comstock, an accountant, to testify on Mitchell's behalf.[342] Through Yudin, Mitchell paid Comstock $2,500 for his expert testimony.[343] Subsequently, Comstock billed Mitchell for nearly an additional $2,500.[344] Mitchell refused to pay Comstock the additional fee.[345] Comstock sued Mitchell in metropolitan court to recover the additional fee.[346]

The metropolitan court held that Mitchell did not have to pay Comstock the additional fee.[347] The metropolitan court found that Comstock had failed to prove that Yudin, as Mitchell's agent, acted within the scope of Mitchell's actual, express, implied, apparent or ostensible authority.[348] The court also found that Mitchell's testimony established that Yudin acted outside the scope of his authority.[349] In addition, the court found that Comstock failed to make any inquiry into the extent of Yudin's authority, even though Comstock knew or should have known that Comstock's initial fees were paid by someone other than Mitchell.[350] Comstock appealed the metropolitan court's decision.[351] The district court affirmed the lower court's decision.[352] On appeal to the supreme court, Comstock claimed error in the metropolitan court's findings and judgment.[353]

---

337. Chevron Oil Co. v. Sutton, 85 N.M. 679, 515 P.2d 1283 (1973).
338. *Id.*
339. 110 N.M. 131, 793 P.2d 261 (1990).
340. *Id.*
341. *Id.* at 132, 793 P.2d at 262.
342. *Id.*
343. *Id.*
344. *Id.*
345. *Id.*
346. *Id.*
347. *Id.*
348. *Id.*
349. *Id.*
350. *Id.*
351. *Id.*
352. *Id.*
353. *Id.*

The supreme court addressed the issue of whether an agent, who had indisputable authority to obligate the principal to pay witness fees of $2,500, likewise had authority to pay fees to a witness in excess of that sum.[354] Before addressing this issue, the court stated that a limitation of the agent's authority by the principal, when communicated to a third person, is effective to excuse the principal from liability to that third person for acts by the agent in excess of the limit prescribed.[355] While Mitchell may have shown that, insofar as Mitchell and Yudin were concerned, Yudin had exceeded his authority, Mitchell failed to show that she communicated to Comstock that Yudin's authority was limited to $2,500.[356]

The court then addressed whether Comstock knew or should have known that Mitchell and Yudin had agreed not to pay Comstock more than $2,500, and whether Comstock acted undiligently and imprudently in ascertaining what limits, if any, Mitchell imposed on Yudin.[357] The supreme court held that Comstock was not obligated to prove that Yudin did not exceed the limitation on Yudin's authority.[358] Rather, Mitchell was obligated to prove that Yudin exceeded the limitation and that Comstock knew or should have known through the exercise of due diligence that Yudin exceeded the limitation.[359] The supreme court rested its holding on two bases. First, the court explained that it is within the implied authority of an attorney to bind his client for the fees of an expert witness.[360] The court then explained that a person dealing with an agent must use reasonable diligence and prudence to ascertain whether the agent is acting within the scope of his powers.[361] Thus, the court remanded the case to the district court to determine whether Comstock knew or through the exercise of due diligence should have known that Yudin exceeded his authority in contracting with Comstock for witness fees in excess of $2,500.[362]

B. Agent Exoneration/Settlement

When claims of negligent or fraudulent misrepresentation and breach of quasi-contract are based on agents' and principals' actions, agency issues of tort, contract and vicarious liability may arise. In *Gallegos v.*

---

354. *Id.*
355. *Id.* (quoting 3 AM. JUR. 2D *Agency* § 82 (1986)).
356. *Id.* at 133, 793 P.2d at 263.
357. *Id.*
358. *Id.*
359. *Id.*
360. *Id.* (citing Klein v. Boylan, 115 N.J.L. 295, 179 A. 638 (1935); Herfurth v. Horaine, 266 Ky. 19, 98 S.W.2d 21 (1936); Portnow v. Berg, 593 S.W.2d 843 (Tex. Ct. App. 1980)).
361. *Id.*
362. *Id.* at 134, 793 P.2d at 264. The court stated that if the answer was yes, then the metropolitan court's judgment in Mitchell's favor was affirmed. However, if the answer was no, then the court would answer the following question: Were Comstock's fees above $2,500 reasonable? If the answer was no, then the court would enter judgment in an amount found to be reasonable. If the answer was yes, then the court would enter judgment in favor of Comstock for the excess fees he charged. *Id.* at 133, 793 P.2d at 263.

Citizens Insurance Agency,[363] Max Sanchez and Amadeo Tenorio were equal partners in Citizens Insurance Agency ("Citizens").[364] Prior to May 1984, Robert Gonzales began soliciting insurance on behalf of Citizens.[365] Gonzales procured an auto insurance application and a premium check from Fernando and Frances Gallegos on May 12, 1984.[366] One month after the transaction, Emilio Aragon acquired the entirety of Tenorio's partnership interest in Citizens.[367] Meanwhile, the Gallegoses never received their policy or proof of financial responsibility from Citizens and were involved in two auto accidents.[368] Citizens informed the Gallegoses that Citizens had not procured an insurance policy for the Gallegoses and that the Gallegoses were uninsured.[369] Although Citizens offered to reimburse the Gallegoses the full amount of their premium, the premium was never refunded.[370]

The Gallegoses brought an action against the insurance agency, the partners (Sanchez and Tenorio or Aragon), and the agent (Gonzales).[371] Following a jury trial, the jury found in favor of Gonzales.[372] The Gallegoses settled with Tenorio.[373] The trial court entered judgment against Sanchez in the sum of $2,000 for compensatory damages and $8,000 for punitive damages.[374] Judgment was also entered against Aragon for the same amounts of compensatory and punitive damages.[375] Aragon appealed.[376]

The supreme court addressed the preliminary question of whether Gonzales was an agent for Citizens at the time he negotiated the contract with the Gallegoses.[377] The court held that there was substantial evidence that Gonzales acted on behalf of Citizens as either its actual agent or under its apparent authority and that a contract existed between the Gallegoses and Citizens.[378]

The court then addressed issues dealing with the liability of the agent for failing to issue a policy. First, the court addressed whether exoneration of an agent extinguished the principal's liability.[379] Aragon asserted that his liability was extinguished by virtue of the jury verdict in favor of

---

363. 108 N.M. 722, 779 P.2d 99 (1989).
364. *Id.* at 724, 779 P.2d at 101.
365. *Id.*
366. *Id.* at 725, 779 P.2d at 102.
367. *Id.*
368. *Id.*
369. *Id.*
370. *Id.*
371. *Id.* at 725, 726, 779 P.2d at 102, 103. The Gallegos' claims were breach of an automobile insurance contract and retention of an insurance premium (unjust enrichment), or quasi-contract, and claims of negligent or fraudulent misrepresentation. *Id.*
372. *Id.* at 727, 779 P.2d at 104.
373. *Id.* at 730, 779 P.2d at 107.
374. *Id.* at 727, 779 P.2d at 104.
375. *Id.*
376. *Id.* at 728, 779 P.2d at 105.
377. *Id.* at 729, 779 P.2d at 106.
378. *Id.*
379. *Id.*

Gonzales.[380] Aragon relied upon the theory that exoneration of the servant operates in tort to exonerate the principal of vicarious liability.[381] In resolving the issue of Aragon's liability, the court found that the evidence supported the contention that Aragon was directly, not vicariously, responsible for the failure to provide the Gallegoses with the automobile insurance they purchased.[382] Further, the court applied agency theories for contracts and found Aragon liable even though a jury had exonerated Gonzales.[383] The court held that under breach of contract, it was not inconsistent to place liability upon the principal and to exonerate the agent.[384] Furthermore, the court held that an agent is not liable for the disclosed principal's breach of contract unless he expressly was made a party to the contract or unless his conduct indicated an intent to be bound.[385]

The court also addressed whether the Gallegoses' settlement with Tenorio extinguished Aragon's tort liability.[386] Aragon asserted that the settlement between the Gallegoses and Tenorio extinguished his liability.[387] In resolving the settlement issue, the court held that the settlement with Tenorio for any alleged tortious conduct on his part would have no effect upon the tort liability of Aragon as a consequence of Aragon's own actions.[388] The court reasoned that if Tenorio's liability was joint and several under New Mexico's release statute,[389] a release would not discharge other tortfeasors unless the release so provided.[390] The issue of release, however, was not previously raised and preserved.[391]

VII. JOINT VENTURE/PARTNERSHIP

During the survey period, the concept of a joint venture was developed to expand partnership law principles to organizations which fail to meet

---

380. *Id.* at 730, 779 P.2d at 107.

381. *Id.*; *see also* Harrison v. Lucero, 86 N.M. 581, 525 P.2d 941 (Ct. App. 1974).

382. *Gallegos*, 108 N.M. at 730, 779 P.2d at 107.

383. *Id.*

384. *Id.*; *see* Barnes v. Sadler Assocs., Inc., 95 N.M. 334, 622 P.2d 239 (1981).

385. *Gallegos*, 108 N.M. at 730, 779 P.2d at 107; *see* Otero v. Wheeler, 102 N.M. 770, 701 P.2d 369 (1985).

386. *Gallegos*, 108 N.M. at 730, 779 P.2d at 107.

387. *Id.*

388. *Id.*

389. Under N.M. STAT. ANN. § 41-3-4 (Repl. Pamp. 1989), a release by the injured person of one joint tortfeasor, whether before or after judgment, does not discharge the other tortfeasors unless the release so provides; but it reduces the claim against the other tortfeasors in the amount of the consideration paid for the release, or in any amount or proportion by which the release provides that the total claim shall be reduced, if greater than the consideration paid.

390. *Gallegos*, 108 N.M. at 730, 779 P.2d at 107.

391. *Id.* The court refused to address whether it would follow the common law treatment of joint contract liability that a release of one joint obligor on a contract operates to release all obligers, or whether it would follow the modern approach to the treatment of joint contract liability that where two or more obligors are jointly liable for breach, a release of one does not necessarily release the other. *Id.* In addition, the court refused to address joint contract liability because Aragon's motion to dismiss the action was premised on the ground that Tenorio was an indispensable party and not on the ground that Tenorio's settlement operated to discharge all joint obligors. *Id.*

the technical requirements of a partnership.[392] A joint venture is usually limited to carrying out a single transaction or a series of related transactions, while a partnership is formed for the purpose of carrying on a continuous business.[393] The current trend is to include joint ventures as a recognized type of partnership, rather than a separate but analogous business organization.[394] In *In re Groff v. Citizens Bank of Clovis*,[395] the court applied partnership law to a joint venture in continuation of that trend.

In *In re Groff*,[396] to secure a debt, Lee and Gwen Groff gave Citizens Bank of Clovis ("Citizens Bank") a security interest in specified cattle owned by the Groffs, as well as all cattle the Groffs later acquired.[397] Without Citizens Bank's knowledge, Lee Groff entered into a cattle-feeding venture with Ed Pickering.[398] Groff and Pickering purchased cattle from Agri-Tech Services, Inc., with Morgan County Feeders, Inc. providing the purchase money financing.[399] Subsequently, the Groffs filed for bankruptcy.[400] A priority dispute ensued and an action was brought to determine the priority of the Groffs' creditors to the Groff-Pickering cattle.[401]

The bankruptcy court held that Groff and Pickering were involved in a joint venture and that the cattle were property of the joint venture.[402] The bankruptcy court also held that New Mexico partnership law applies to joint ventures and, under New Mexico law, Citizens Bank, as a creditor of the Groffs in their individual capacity only, did not hold an interest in the Groff-Pickering cattle.[403] The bankruptcy court concluded that the Groffs' bankruptcy estate did not contain the Groff-Pickering cattle; the estate contained only the Groffs' interest in the Groff-Pickering joint venture as determined under New Mexico partnership law.[404] Citizens Bank appealed to the United States District Court.[405] The trial court affirmed the decision of the bankruptcy court.[406] Citizens Bank appealed.[407]

The United States Court of Appeals for the Tenth Circuit examined the issue of whether the rules governing partners' interests in partnership

392. A. BROMBERG & L. RIBSTEIN, BROMBERG AND RIBSTEIN ON PARTNERSHIP § 1.01(b), at 1:5 (1988).
393. *Id.* at §§ 2.06(a), 2:42-43.
394. H. REUSCHLEIN & W. GREGORY, HANDBOOK ON THE LAW OF AGENCY AND PARTNERSHIP § 266, at 446 (1979).
395. 898 F.2d 1475 (10th Cir. 1990).
396. *Id.*
397. *Id.*
398. *Id.*
399. *Id.*
400. *Id.* at 1476.
401. *Id.*
402. *Id.*
403. *Id.*
404. *Id.*
405. *Id.*
406. *Id.*
407. *Id.*

assets also apply to joint ventures.[408] The court of appeals, applying New Mexico partnership law, held that a creditor with a security interest in a debtor's presently owned and after-acquired cattle had no interest in the cattle subsequently acquired by the debtor's joint venture with a third party.[409]

The court of appeals rested its holding on three bases. First, the history of a joint venture was discussed.[410] The American judiciary developed the concept of a joint venture in order to extend principles of partnership law to organizations that fail to meet the technical requirements of a partnership.[411] Second, the court discussed the current trend in the treatment of joint ventures.[412] The current trend is to include joint ventures as a recognized type of partnership rather than a distinct but similar business entity.[413] Third, the court applied New Mexico partnership law.[414] Under the Uniform Partnership Act,[415] the partnership owns property as an entity separate and distinct from the partners.[416] Individual partners can only assign their residual interests in the entire partnership.[417]

VIII. DIRECTOR INDEMNIFICATION

Stockholders may obtain relief in equity against fraud or breach of trust by officers or directors who wrongfully deal with property to the injury of the stockholders.[418] In *Petty v. Bank of New Mexico Holding Co.*,[419] the court addressed whether a minority shareholder may seek relief for a claim of breach of fiduciary duty against the directors and officers of a corporation for an alleged wrongful indemnification.

In *Petty*, Ralph Petty purchased fifty shares, less than one percent of the total outstanding shares, in the Bank of New Mexico Holding Company ("the Holding Company") on September 23, 1987.[420] One week later, Petty sent a written protest to the Holding Company demanding that the Holding Company refrain from incurring any further litigation expenses in a separate, pending lawsuit.[421] The litigation involved a suit

---

408. *Id.*
409. *Id.* at 1478.
410. *Id.* at 1476.
411. *Id.*
412. *Id.* at 1477.
413. *Id.*; *see supra* note 364.
414. *In re Groff*, 898 F.2d at 1477.
415. N.M. STAT. ANN. §§ 54-1-1 to -43 (Repl. Pamp. 1988).
416. *In re Groff*, 898 F.2d at 1477. N.M. STAT. ANN. § 54-1-8 (Repl. Pamp. 1988) states in pertinent part:

> A. All property originally brought into the partnership stock or subsequently acquired by purchase or otherwise, on account of the partnership, is partnership property.
>
> B. Unless the contrary intention appears, property acquired with partnership funds is partnership property.

417. *In re Groff*, 898 F.2d at 1477.
418. 19 AM. JUR. 2D *Corporations* § 2262, at 161 (1986).
419. 109 N.M. 524, 787 P.2d 443 (1990).
420. *Id.* at 526, 787 P.2d at 445.
421. *Id.*

by a minority shareholder, Lanford, against the president and chief executive officer of the Holding Company, against other shareholders of the Holding Company, and against the Holding Company itself, for a determination of the price at which shares of stock in the corporation should be bought and sold pursuant to the buy-sell and voting trust agreement.[422] Petty was not a party to the Lanford litigation because he was not a shareholder at that time.[423] On October 1, 1987, subsequent to Petty's purchase of stock, the Holding Company authorized reimbursement of its officers and directors for their legal fees, costs and expenses incurred in the defense of the litigation.[424] Petty filed a derivative suit against the Holding Company and its officers and directors.[425] Petty alleged that the use of any Holding Company funds to defend the litigation was improper, that litigation expenses could not be reimbursed by the Holding Company, and that any judgment against the directors in the litigation could not be reimbursed to any defendant.[426] The trial court dismissed the complaint for failure to state a claim upon which relief could be granted.[427] Petty appealed.[428]

The supreme court addressed two issues. First, the court considered whether Petty's complaint was sufficient to state a cause of action on behalf of the corporation for the allegedly wrongful indemnification of the officers and directors.[429] The supreme court held that Petty's complaint alleged sufficient facts to state a claim against the officers and directors for breach of their fiduciary duty.[430] The court rested its holding on two bases. First, the defendants were adequately apprised of the nature of the corporation's claim, asserted derivatively through Petty.[431] Defendants were notified, by virtue of Petty's allegations, that defendants had breached their fiduciary duty, or otherwise acted wrongfully, in authorizing the officers' and directors' indemnification by the corporation of their litigation expenses.[432] Second, an action on behalf of the corporation to seek reimbursement for distributions by the corporation resulting from the defendants' breach of their fiduciary duty, or other duty owed to the corporation and the minority shareholders, does exist.[433]

The second issue addressed by the supreme court, an issue of first impression in New Mexico, was whether the corporation had the power to indemnify its directors.[434] The supreme court held that New Mexico's

---

422. *Id.*
423. *Id.*
424. *Id.*
425. *Id.*
426. *Id.*
427. *Id.* at 525, 787 P.2d at 444.
428. *Id.*
429. *Id.* at 526, 787 P.2d at 445.
430. *Id.*
431. *Id.* at 527, 787 P.2d at 446.
432. *Id.*
433. *Id.*
434. *Id.*

indemnification statute,[435] which empowers a corporation to indemnify any person made a party to a proceeding by reason of his status as director, was inapplicable to the Holding Company's action with respect to the defendants in the litigation.[436] The court rested its holding on two bases. First, the indemnification statute did not apply to the Holding Company's actions indemnifying the directors because the defendants were not made parties to the litigation as a result of the defendants' status as directors of the corporation.[437] Rather, the defendants were made parties to that suit because they were shareholders in the Holding Company and signatories to the buy-sell and voting stock agreement.[438] Second, the indemnification statute is an enabling statute which operates to empower corporations to indemnify their directors and other agents.[439] The indemnification statute, however, does not confer on the indemnified director an unquestionable right to indemnification.[440]

IX. UNFAIR TRADE PRACTICE

In *Thompson v. Youart*,[441] Ernest Thompson, a furniture designer-manufacturer, began selling his furniture in 1982 to Schelu, a gallery which sells southwestern-style furniture owned by Tim and Jai Youart ("the Youarts").[442] In 1988, the Youarts decided to carry a new line of furniture in place of Thompson's furniture line because of alleged problems with receiving special orders from Thompson, and because of Thompson's placement of advertisements which competed with Schelu's advertisements.[443] The new line of furniture sold by Schelu was similar to Thompson's.[444] Schelu announced the new furniture line in a radio advertisement.[445] Thompson filed a petition, complaint and order to show cause why the gallery owners should not be enjoined from selling the new line.[446] In a letter ruling, the trial court held that Thompson's furniture designs had aesthetic value which belonged to Thompson and which deserved some degree of protection.[447] The trial court communicated its

435. Under N.M. STAT. ANN. § 53-11-4.1(B) (Supp. 1991), a corporation shall have the power to indemnify any person made a party to any proceeding by reason of the fact that the person is or was a director, if three conditions are met.

436. *Petty*, 109 N.M. at 529, 787 P.2d at 448.

437. *Id.* at 528, 787 P.2d at 447.

438. *Id.*

439. *Id.* at 530, 787 P.2d at 449.

440. *Id.* The court remanded the case to consider whether the directors had breached their fiduciary duty to the corporation or had otherwise failed to adhere to the various standards of conduct required of corporate directors in the management of their corporations. *Id.* at 531, 787 P.2d at 450. In addition, the court commented that the directors' claim that this action was premature was predicated on the applicability of the indemnification statute, and if the statute did not apply, then the case might be ripe and not premature. *Id.* at 533, 787 P.2d at 452.

441. 109 N.M. 572, 787 P.2d 1255 (Ct. App. 1990).

442. *Id.* at 574, 787 P.2d at 1257.

443. *Id.*

444. *Id.*

445. *Id.*

446. *Id.*

447. *Id.*

intent to grant a temporary restraining order prohibiting the gallery owners from selling furniture which was deceptively similar to Thompson's furniture line.[448] The trial court based its decision on the court's duty to prevent trade practices that are unfair and overreaching.[449] The trial court certified the order for interlocutory appeal.[450]

The court of appeals addressed whether a furniture designer-manufacturer has a right to prevent a gallery from selling furniture similar to the furniture line of the designer-manufacturer where no furniture copyright exists and no exclusive contract to sell the designer-manufacturer's furniture line exists.[451] The court held that the gallery owners did not misrepresent the source of the new furniture line so as to confuse the public; rather, Schelu announced the switch in furniture lines.[452] The court applied the Unfair Practices Act to Thompson's claim.[453] The court stated that it could not distinguish Thompson's common law claim of unfair competition from a claim under the Unfair Practices Act.[454] Under the Act, none of the elements[455] for an unfair practice claim were present.[456] The court also held that the designs used by Thompson were in the public domain and could be copied freely absent protection by a patent or copyright.[457] The court reasoned that the mere inability of the public to tell two identical articles apart is not enough to support an injunction against copying that federal patent law permits.[458] If no exclusive right to a product or to the use of designs exists, mere copying by another does not constitute unfair competition.[459]

The court also addressed whether the designer-manufacturer's claim was preempted by federal law.[460] The court held that Thompson's claim, which sought protection against copying designs, was preempted by federal law and came under the exclusive jurisdiction of the federal courts.[461] The court reasoned that the right to prevent copying is a right protected by federal copyright laws.[462] Those rights governed by federal copyright laws are under the exclusive jurisdiction of the federal courts.[463]

---

448. *Id.* at 575, 787 P.2d at 1258.
449. *Id.*
450. *Id.*
451. *Id.*
452. *Id.* at 576, 787 P.2d at 1259.
453. *Id.* at 575, 787 P.2d at 1258.
454. *Id.*
455. Under N.M. STAT. ANN. § 57-12-2(C) (Supp. 1991), the relevant elements for a claim under the Unfair Practices Act are: (1) a false or misleading representation; (2) knowingly made; (3) in connection with the sale of goods or services; (4) in the regular course of trade or commerce; (5) which may, tends to or does deceive or mislead any person.
456. *Thompson*, 109 N.M. at 576, 787 P.2d at 1259.
457. *Id.* at 577, 787 P.2d at 1260.
458. *Id.* (citing Sears, Roebuck & Co. v. Stiffel Co., 376 U.S. 225, 232 (1964)).
459. *Id.* at 576, 787 P.2d at 1259 (quoting Gardenia Flowers, Inc. v. Joseph Markovits, Inc., 280 F. Supp. 776 (S.D.N.Y. 1968)).
460. *Id.* at 575, 787 P.2d at 1258.
461. *Id.* at 577, 787 P.2d at 1260.
462. *Id.*
463. *Id.*

X. GROSS RECEIPTS TAX

The gross receipts tax in effect operates as a tax on the sale of goods and services.[464] The gross receipts tax and a retail sales tax are both collected by the seller; however, the gross receipts tax is imposed on the seller and is customarily passed to the buyer, while the sales tax is imposed directly on the buyer.[465]

In *El Centro Villa Nursing Center v. Taxation and Revenue Department of New Mexico*,[466] El Centro Villa Nursing Center ("El Centro") received payments from the Department of Human Services in December 1983 and November 1984 and failed to inquire as to El Centro's tax liability from these payments.[467] El Centro failed to pay gross receipts tax on these payments.[468] El Centro admitted that the cause of its failure to pay tax was an inadvertent error.[469] El Centro appealed the penalty assessment for its failure to pay the gross receipts tax applicable to these payments.[470]

The decision and order of the hearing officer of the Taxation and Revenue Department ("the Department") upheld the penalty assessed against El Centro for failure to pay gross receipts tax.[471] The hearing officer held that El Centro's failure to pay the tax was negligent.[472] The hearing officer based his holding on the presumption that the Department's determination that a penalty should be assessed under New Mexico's gross receipts penalty statute[473] was correct.[474] El Centro appealed.[475]

The court of appeals addressed two issues. The first issue the court addressed was whether there was substantial evidence to support a penalty assessment against El Centro under section 7-1-69(A) for failure to pay gross receipts tax due to El Centro's negligence.[476] The court held that there was sufficient evidence to find that El Centro's failure to pay tax was due to El Centro's negligence.[477] The court rested its decision on three bases. First, under New Mexico's administrative regulations,[478] a penalty may be imposed upon a taxpayer for inadvertent failure to pay

---

464. United States v. New Mexico, 455 U.S. 720, 721 (1982).

465. Yesley, *Out of Sight But Not Out of Mind: New Mexico's Tax on Out-of-State Services*, 20 N.M.L. REV. 501, 502 n.6 (1990).

466. 108 N.M. 795, 779 P.2d 982 (Ct. App. 1989).

467. *Id.* at 796, 779 P.2d at 983.

468. *Id.* at 795, 779 P.2d at 982. New Mexico's gross receipts tax is imposed under the Gross Receipts and Compensating Act, N.M. STAT. ANN. §§ 7-9-1 to -82 (Supp. 1991).

469. *El Centro*, 108 N.M. at 798, 779 P.2d at 985.

470. *Id.* at 795, 779 P.2d at 982.

471. *Id.*

472. *Id.*

473. Under N.M. STAT. ANN. § 7-1-69(A) (Supp. 1991), in the case of a failure due to negligence or disregard of rules and regulations, but without intent to defraud, to pay when due any amount of tax required to be paid, or to file by the date required regardless of whether any tax is due, a penalty, specified in the statute, is applied.

474. *El Centro*, 108 N.M. at 795, 779 P.2d at 982.

475. *Id.*

476. *Id.*

477. *Id.* at 796, 779 P.2d at 983.

478. N.M. Tax Reg. 69:3(3) (1990) states, "[t]axpayer 'negligence' under Section 7-1-69(A) means: inadvertence, indifference, thoughtlessness, carelessness, erroneous belief or inattention."

tax.[479] El Centro admitted that the cause of its failure to pay the tax was inadvertent error, thereby admitting that the cause was negligent as defined by administrative regulations.[480] Second, under New Mexico's administrative regulations,[481] a penalty may be imposed upon a taxpayer for his inaction if action would reasonably be required.[482] El Centro's failure to specifically bring the unusual and large payments to its accountant's attention constituted inaction.[483] Third, under New Mexico's administrative regulations,[484] a penalty may be imposed for a taxpayer's failure to act with ordinary business care and prudence under the circumstances.[485] El Centro's efforts to exercise ordinary business care and prudence by setting up and actively participating in an accounting system failed to account for large and unusual increases in gross receipts and, therefore, was inadequate under the circumstances.[486]

The second issue addressed by the court of appeals was whether El Centro's failure to pay tax was due in part to El Centro's accountant's negligence in implementing El Centro's accounting system.[487] The court held that although there was sufficient evidence to support the finding that El Centro's failure to pay tax was due as much to El Centro's inattention as to the negligence of its accountant, the court was not inclined to hold that a taxpayer can abdicate its responsibility merely by appointing an accountant as an agent in tax matters.[488] The court followed the decision in *Tiffany Construction Co. v. Bureau of Revenue,*[489] which held that "every person is charged with the reasonable duty to ascertain the possible tax consequences of his action [or inaction]."[490]

XI. COMPENSATING TAX

In *Phillips Mercantile Co. v. Taxation and Revenue Department of New Mexico,*[491] Phillips Mercantile Company ("Phillips") contracted with the *Albuquerque Journal/Tribune* and the *Santa Fe New Mexican* to distribute newspaper inserts.[492] The inserts were shipped directly from the

479. *El Centro,* 108 N.M. at 797, 779 P.2d at 984.
480. *Id.* at 798, 779 P.2d at 985.
481. N.M. Tax Reg. 69:3(2) (1990) states, "[t]axpayer 'negligence' under Section 7-1-69(A) means: inaction by taxpayers where action is required."
482. *El Centro,* 108 N.M. at 798, 779 P.2d at 985.
483. *Id.*
484. N.M. Tax Reg. 69:3(1) (1990) states, "[t]axpayer 'negligence' under Section 7-1-69(A) means: failure to exercise that degree of ordinary business care and prudence which reasonable taxpayers would exercise under like circumstances."
485. *El Centro,* 108 N.M. at 798, 779 P.2d at 985.
486. *Id.*
487. *Id.*
488. *Id.* at 799, 779 P.2d at 986.
489. 90 N.M. 16, 558 P.2d 1155 (1976).
490. *El Centro,* 108 N.M. at 799, 779 P.2d at 986 (quoting Tiffany Constr. Co. v. Bureau of Revenue, 90 N.M. 16, 17, 558 P.2d 1155, 1156 (Ct. App. 1976)).
491. 109 N.M. 487, 786 P.2d 1221 (Ct. App. 1990).
492. *Id.* at 488, 786 P.2d at 1222.

printers to the newspapers.[493] Phillips also contracted with a mailing service in Albuquerque to address and mail catalogs to New Mexico residents.[494] Phillips had ninety percent of the catalogs shipped to the Albuquerque mailing service and ninety-nine percent of the newspaper inserts shipped to the New Mexico newspapers.[495] The remainder of the catalogs and inserts were shipped to Phillips' retail stores for use in those stores.[496] The Taxation and Revenue Department of New Mexico ("the Department") assessed a compensating tax on Phillips.[497]

The Secretary of the Department issued a decision and an order upholding the assessment of the compensating tax against Phillips on the value of catalogs and newspaper inserts purchased by Phillips.[498] Phillips appealed the decision and order.[499]

The court of appeals addressed two issues. The court addressed whether Phillips' contracting for the distribution of the catalogs and newspaper inserts was a taxable "use"[500] of them.[501] The court of appeals analyzed Phillips' transaction under New Mexico's statute on compensating tax.[502] The court held that Phillips had used the advertising materials distributed in New Mexico within the meaning of section 7-9-7.[503] The court rested its decision on two bases. First, Phillips had a contractual relationship with the Albuquerque mailing service used to address and mail the catalogs to New Mexico residents.[504] Second, Phillips had a contractual relationship with the New Mexico newspapers through which it directed the manner and timing of the distribution of its newspaper inserts to New Mexico residents.[505] Thus, by exercising control over the catalogs and inserts through its contractual relationships with the mailing service and the newspapers in New Mexico, Phillips used the advertising material within the meaning of section 7-9-7.[506]

The court also addressed whether Phillips should be allowed a deduction from gross receipts tax under New Mexico's deduction from gross receipts statute.[507] The court held that Phillips' newspaper inserts were advertising and did not constitute newspapers.[508] Thus, the deductions from gross

493. *Id.*
494. *Id.*
495. *Id.*
496. *Id.*
497. *Id.* at 487, 786 P.2d at 1221.
498. *Id.*
499. *Id.*
500. Under N.M. STAT. ANN. § 7-9-3(L) (Supp. 1991), for the purposes of the Gross Receipts and Compensating Act, "use" or "using" includes use, consumption or storage, other than storage for subsequent sale in the ordinary course of business, or for use solely outside of New Mexico.
501. *Phillips*, 109 N.M. at 488, 786 P.2d at 1222.
502. *Id.* at 488-489, 786 P.2d at 1222-23. Under N.M. STAT. ANN. § 7-9-7 (Supp. 1991), for the privilege of using property in New Mexico, there is imposed an excise tax equal to five percent of the value of the property under certain circumstances.
503. *Phillips*, 109 N.M. at 489, 786 P.2d at 1223.
504. *Id.*
505. *Id.*
506. *Id.*
507. *Id.* Under N.M. STAT. ANN. § 7-9-63 (Supp. 1991), receipts from publishing newspapers or magazines, except from selling advertising space, may be deducted from gross receipts.
508. *Phillips*, 109 N.M. at 489, 786 P.2d at 1223.

receipts tax allowed by New Mexico's statute did not operate to shield Phillips from the compensating tax.[509] The court based its decision on a New Mexico gross receipts regulation[510] which provides that, as used in section 7-9-63, the term "newspaper" is limited to publications commonly understood to be newspapers and printed and distributed periodically at daily, weekly, or other short intervals for the dissemination of news of a general character and of a general interest.[511] In addition, advertising is not considered to be news of a general character and of a general interest.[512] Therefore, the taxpayer's contracting for the distribution of catalogs and newspaper inserts was a taxable use of the catalogs and inserts.[513]

RUBEN ARVIZU III
ESTHER MARIE GARDUNO
JOSEPH F. STRELITZ

509. *Id.* at 490, 786 P.2d at 1224.
510. N.M. Gross Receipts Reg. 64:1 (1989) states:
> As used in Sections 7-9-63 and 7-9-64, the term 'newspaper' is limited to those publications which are commonly understood to be newspapers and which are printed and distributed periodically at daily, weekly, or other short intervals for the dissemination of news of a general character and of a general interest. The term does not include handbills, circulars, flyers, or the like, unless printed and distributed as a part of a publication which otherwise constitutes a newspaper within the meaning of this paragraph. Neither does the term include any publication which is issued to supply information on certain subjects of interest to particular groups, unless such publication otherwise qualifies as a newspaper within the meaning of this paragraph. Advertising is not considered to be news of a general character and of a general interest.

511. *Phillips*, 109 N.M. at 489-90, 786 P.2d 1223-24.
512. *Id.* at 489, 786 P.2d at 1223.
513. *Id.* at 489-90, 786 P.2d at 1223-24.