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Security Devices

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SECURITY DEVICES

*Thomas A. Harrell**

Suretyship

In *Prime Time Television, Inc. v. Coastal Computer Systems, Inc.*,[1] the court properly rejected the argument that a contract of suretyship cannot be confected until after the principal obligation arises. This proposition occasionally has been advanced because Louisiana Civil Code article 3035 defines suretyship as an accessory promise by which one binds himself for "another already bound." Furthermore, the text of the article was not found in the Code of 1808, but was added, without comment, by the redactors of the Code of 1825, so that its antecedents and purpose are not entirely clear.[2]

The Code of 1808 contained no definition of the contract of suretyship, and the most likely explanation for the addition of article 3035 in 1825 is simply that the redactors intended to correct that omission. The article obviously is a definition: it was inserted as the first article in the Title, it adds nothing of substantial importance to the Code, and every other title in the Code regulating a nominate contract contains such a definition.

A comparison of article 3035 with other articles simultaneously inserted by the redactors of the Code of 1825 further supports the conclusion that the reference to one "already bound" serves only to emphasize the accessory nature of the contract, rather than to establish the rules regulating when and under what circumstances suretyship can be established.[3] One such article is article 1764,[4] which defines accessory

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1. 484 So. 2d 780 (La. App. 1st Cir. 1986).

2. Professor Batiza suggests, in his work on the sources of the Code of 1825, that the article was "substantially influenced" by Pothier. See Batiza, The Actual Sources of the Louisiana Projet of 1823: A General Analytical Survey, 47 Tul. L. Rev. 1, 100 (1972).

3. Professor Denis's observations concerning the definitions of pledge in the Louisiana Civil Code are probably worth repeating in this context:

> I do not propose to define the contract of pledge. There are already numerous definitions of it. Many are defective; very few are instructive or useful. Definitions at best seldom convey information or knowledge, and they sometimes create confusion. As the Latin maxim says: Omnia definitio in lege periculosa est.

H. Denis, A Treatise on the Law of the Contract of Pledge 2 (1898).

4. Article 1771 of the Louisiana Civil Code of 1870.

contracts "such as suretyship, mortgage and pledge" in terminology similar to article 3035: "An accessory contract is made for assuring the performance of a prior contract . . . ." Also adopted was article 3259,[5] which expressly declares that a mortgage may be given for an obligation "which has not yet risen into existence." The absence of comment by the redactors to these additions indicates a lack of intention to work any great change in the law, which before the Code clearly permitted creation of contracts of suretyship and mortgage for future obligations.[6]

The civil law has never experienced any theoretical difficulty in creating security for future obligations.[7] Suretyship could be given for such obligations under Roman law[8] and under the Spanish law prevailing in Louisiana before the Code of 1808.[9] Furthermore, the Civil Code provides that pledge and mortgage can be contracted for future obligations.[10] Despite all of this, support for an interpretation of article

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5. Article 3292 of the Louisiana Civil Code of 1870.

6. As to suretyships, see infra note 9. As to mortgages, see Roussel v. Dukeylus' Syndics, 4 Mart. (o.s.) 218 (La. 1816), approving the validity of a mortgage "to secure the plaintiff, among other things, against future endorsements." Edward Livingston, one of the 1825 redactors, was the attorney for the plaintiff in that case, and although it cannot be established with certainty, the first clause of article 3292 appears to paraphrase a section of Pothier relied upon by Livingston in his argument. Pothier declared: "One can give a mortgage for a debt which is not yet contracted, but only to be contracted." Pothier, des Hypotheques, sec. 3. The second clause of article 3292, providing, "as when a man grants a mortgage by way of security for indorsements, which another promises to make for him," seems to be taken directly from the *Roussel* case. It would be difficult to support the proposition that Livingston, at least, saw any conceptual difficulties with security created in anticipation of the principal obligation.

7. A similar question could be raised as to mortgage if the matter is limited solely to the definitional articles. La. Civ. Code art. 3285 provides: "[I]t is essentially necessary to the existence of a mortgage, that there shall be a principal debt to serve as a foundation for it." That this does not limit a mortgage to existing obligations is made clear by the previously mentioned article 3292: "A mortgage may be given for an obligation which has not yet risen into existence . . . ."

8. "A surety may bind himself either previously or subsequently to the contraction of the obligation." Scott, Corpus Juris Civilis, The Civil law, Vol. 2, The Enactments of Justinian, Title XX, Concerning Sureties, (3), 113. "Fideiussion . . . was the sole means of creating suretyship by stipulation in Justinian's time, and which must have dated back at least to 81 B. C. . . . . Further, the main obligation . . . might even be guaranteed by anticipation." Pritchard, Leagues Roman Private Law 344 (3d ed. 1961).

9. "We may give security [suretyship] not only for a present obligation, or one already contracted, but also for an obligation to be contracted . . . ." Part I, Book III, Tit. IV, § I, No. 1853 (1808).

10. La. Civ. Code arts. 3158, 3292. The priority of real security given under such conditions vis-à-vis security created before the principal obligation arises is a different question. It might also be noted that, if the creation of security for a debt not yet in existence violates the "accessory nature" of security, so should the creation of security over property not yet owned by the person creating the contract. There is no difficulty with creating such security however. See La. Civ. Code arts. 3288, 3304.

3035 that would preclude suretyship from arising until the debt is formed has been found in the commonly stated proposition that an accessory obligation cannot exist without a principal one.[11] Such an interpretation confuses the question of when a contract can be confected with the questions of when and under what conditions its obligations can be enforced. An accessory obligation obviously cannot be *enforced* in the absence of a principal obligation (which is what statements concerning the necessity for a principal obligation mean). Nevertheless, there is not, and has never been, any doubt in the civil law that an accessory contract can be made before the principal obligation arises, the creation of the latter being merely a suspensive condition to the enforcement of the former.[12] In fact, the accessorial nature of contracts of security is nothing more than a recognition that such contracts are given upon a particular kind of suspensive condition that distinguishes them from "direct" or "principal" obligations. The enforcement of every accessory obligation is dependant upon the existence of another, unperformed obligation.

The accessory character of security was also at issue in *Desonnier v. Golden Gulf Marine Operators, Inc.*[13] The plaintiff in that case entered into an employment contract with the defendant corporation that was guaranteed by the defendant's principal shareholders (one of whom was also a defendant in the action). When the defendant corporation prematurely terminated the contract, the plaintiff claimed that his discharge was without cause and that Civil Code article 2749 permitted him to collect his salary for the contract's remaining term.[14] The court concluded that the discharge was in fact without just cause and awarded the plaintiff the full amount of his unpaid salary in accordance with the article. The contract contained a rather complicated compensation structure, one of the items of which required the employer to pay certain premiums for disability, life and health insurance. The court noted that article 2749 is penal in nature and limits the employee to collection only of his unearned salary. It then rejected the employee's claim for future insurance premiums on the ground that they were not part of his "salary"

11. Compare La. Civ. Code arts. 3285 & 3292, supra note 7.

12. La. Civ. Code art. 1767: "A conditional obligation is one dependent upon an uncertain event. If the obligation may not be enforced until the uncertain event occurs, the condition is suspensive . . . ." La. Civ. Code art. 1775: "Fulfillment of a condition has effects that are retroactive to the inception of the obligation . . . ." It is also possible to make an offer to form a suretyship contingent upon an acceptance by act of extending the credit or agreeing to extend the credit to the debtor. The matter is one of contract, not imperative law.

13. 474 So. 2d 1314 (La. App. 5th Cir. 1985).

14. "If, without any serious ground of complaint, a man should send away a laborer whose services he has hired for a certain time, before that time has expired, he shall be bound to pay to such laborer the whole of the salaries which he would have been entitled to receive, had the full term of his services arrived." La. Civ. Code art. 2749.

within the meaning of article 2749. Nevertheless, the court held the surety liable for those amounts, declaring: "The liability of the guarantor differs from that of the company. The promise is to guarantee not only payment but 'performance of all obligations of the Company under this Agreement.' . . . Therefore, the judgment against [the guarantor] consists of his virile share of salary, bonus, and life and health insurance."[15]

In effect, the court cast the surety for amounts that it held were not owed by the principal obligor. This is clearly erroneous for several reasons. First, it is contrary to Civil Code article 3037, which provides: "The suretyship cannot exceed what may be due by the debtor, nor be contracted under more onerous conditions. . . . The suretyship which exceeds the debt or which is contracted under more onerous conditions shall not be void, but shall be reduced to the conditions of the principal obligation."[16] Secondly, the surety is not an insurer. He is entitled to recover what he pays the principal creditor from the debtor. He is thus subrogated to the claim of the principal creditor and has a direct right of indemnification against the debtor.[17] More importantly, these rules and the limitations of article 3037 flow from the essential nature of suretyship as an accessory contract.[18] It is given to guarantee performance of the unfulfilled obligation of another.[19] The surety is released or discharged to the extent the principal obligation is discharged and may plead any defense to the principal obligation that the debtor may plead.[20] Consequently, the law leaves no doubt whatsoever that an indispensable allegation of a suit against a surety is that the debtor is indebted to the plaintiff for the sum he seeks from the surety. To the extent the court held the surety for more than the employer owed to the employee, it distorted the purpose and misconstrued the nature of suretyship.

15. 474 So. 2d at 1319.

16. La. Civ. Code art. 3037.

17. La. Civ. Code art. 3052. "The surety may oppose to the creditor all exceptions belonging to the principal debtor, and which are inherent in the debt . . . ." La. Civ. Code art. 3060.

18. "A contract is accessory when it is made to provide security for the performance of an obligation. Suretyship . . . [is an example] . . . of such a contract." La. Civ. Code art. 1913. "The obligation of the surety towards the creditor is to pay him in case the debtor should not himself satisfy the debt . . . ." La. Civ. Code art. 3045.

19. There is little doubt of the nature of the guaranty in this case. Even though the parties bound themselves solidarily "with the Company," they did so to "absolutely guarantee to [the] Employee prompt and complete payment and performance of all obligations of the Company under this Agreement." 474 So. 2d at 1315. If the judgment sought against the guarantor cannot be obtained against the company, it is difficult to see how it can be an obligation of the company under the contract, the performance of which is guaranteed.

20. La. Civ. Code art. 3060.

Hardware Wholesalers, Inc. v. Guilbeau[21] illustrates a trap into which owners of closely-held corporations (or their attorneys) may easily fall. The defendants were the sole shareholders of a corporation engaged in the retail hardware business. The plaintiff was a wholesale hardware cooperative. As a prerequisite to the retail corporation purchasing merchandise from the plaintiff, defendants were required to buy stock in the plaintiff's cooperative and to guarantee the debts of the retailer. The defendants later sold their interest in the retailer to their daughters and sons-in-law. Defendants also transferred their stock in plaintiff's cooperative to these purchasers, and thus the plaintiff apparently was aware of the change in the ownership of the retail corporation. About three years later, the retail corporation defaulted on its account to the plaintiff. Plaintiff then demanded that the defendants pay the account in accordance with their guaranty.

The defendants argued that they only intended to guarantee the debts of the retail corporation while they were its owners. This, combined with the plaintiff's awareness that they had sold all of their stock in the retail corporation, claimed the defendants, terminated their liability under the guaranty. Nevertheless, because the guaranty agreement expressly provided that it would continue until written notice of termination was received from the guarantors, the court held that the contract continued in full force and effect until such notice was given. The court found the testimony of the defendants as to their intention to be irrelevant, absent a showing that such an intention was understood and shared by the plaintiff.

The decision appears to be correct.[22] There is no particular reason to believe that the transfer of stock in a corporation of itself denotes a termination of the interest of the former shareholders in its success, or a willingness to guarantee its debts. This would seem to be particularly true when the transfer is to the children of the guarantors. Whether the plaintiff would have continued to extend credit to the corporation without the guaranty of the defendants is a matter of speculation.

It must also be observed that in the case at hand, and in the cases the court relied upon in deciding it, the sureties never directly notified the creditor that they were unwilling to continue guaranteeing the future debts of the principal obligor. Whether a verbal notice from the surety, followed by some indication of the creditor that he recognizes the unwillingness of the surety to guarantee future obligations, is sufficient

21. 473 So. 2d 108 (La. App. 3d Cir. 1985).

22. The court relied upon two earlier cases as authority for its proposition: Magnolia Petroleum Co. v. Harley, 13 So. 2d 84 (La. App. 2d Cir. 1943), and Bonura v. Christiana Bros. Poultry Co., 336 So. 2d 881 (La. App. 4th Cir. 1976), cert. denied, 339 So. 2d 11 (La. 1976), 339 So. 2d 26 (La. 1976).

to terminate a suretyship that otherwise requires written notice to do so, was not before the courts. There is little reason, however, for a court to hold that the suretyship continues in such a case. If clear and convincing evidence is presented that the surety communicated his desire to terminate the agreement and that the creditor acquiesced in or accepted the communication, what more is required? After all, the creditor cannot refuse the request, he can only require that it be put in writing. If he chooses not to do so, that should end the matter.[23] Furthermore, few sureties are likely to demand a written release from the creditor or to send an express written notice of termination if they receive a positive indication from the creditor that he has received and understands the revocation and does not expect to receive a written confirmation of it.

Perhaps the most important lesson to be drawn from the case is that when one represents shareholders of closely-held corporations or partners of partnerships who are disposing of all or even a substantial part of their interest in the business, deliberate, explicit and careful inquiry must be made as to the existence of contingent obligations undertaken by the seller that might require cancellation or modification.[24]

Mortgages

A well known requirement for the availability of executory process is that the mortgage upon which execution is sought must substantially describe the note paraphed for identification with it. Any deviation between the terms of the note presented by the plaintiff and that described in the mortgage is fatal, even if the note bears the paraph of the notary before whom the mortgage is executed. The rule itself is

23. This is not to say that the surety's burden of proof should not be great, or that uncertainty or doubt should not be resolved against him. The purpose of a writing obviously is to give certainty to the obligation. Having that means available to terminate his liability, the surety should run the risk of any misunderstanding or ambiguity. The question is, however, one of degree, not of substance. If there is no doubt that he communicated his revocation and the creditor accepted it without the necessity of a confirming writing, the revocation should be effective.

24. These may exist in a variety of forms other than express guarantees of the corporate or partnership obligations. For example, contributions of property to the enterprise by the owners may have entailed the assumption of unreleased obligations of the shareholders or partners. Direct guarantees, however, are probably the most common. Utilities, service companies, suppliers of equipment and fixtures, wholesalers, franchisers, key employees and even customers may require guarantees by shareholders or partners of the current and future obligations of the enterprise. These kinds of obligations are frequently overlooked or forgotten by the shareholders or partners at the time they sever their connection with the business. Such persons are also sometimes unaware of the continuing nature of their obligations, assuming, as the defendants in this case apparently did, that since they have severed their connection with the busines, they are automatically relieved of any responsibility for its future activities.

not found in the Code of Civil Procedure, which merely requires that the plaintiff submit "authentic evidence of: (1) The note, bond or other instrument evidencing the obligation secured by the mortgage or privilege."[25] The existence of the rule is obliquely given legislative recognition by the last sentence of this article, which provides: "A variance between the recitals of the note and of the mortgage regarding the obligation to pay attorney's fees shall not preclude the use of executory process."[26]

The rule and its exception were both the subject of litigation this year. In *Bank of St. Charles v. Eris*,[27] the court held that executory process was not available where the mortgage and note were both dated September 25, 1981, but the notarial paraph on the note stated that it was "in conformity with an act of collateral mortgage passed before me this day September 30, 1981."[28]

In *Colonial Financial Services, Inc. v. Stewart*,[29] the court reversed a lower court's order enjoining issuance of executory process where there was a discrepancy between the attorney's fees stipulated in the note presented and their description in the mortgage,[30] and where the plaintiff had acquired the note by an authentic act of assignment in which the notary did not paraph the note. The court noted that Code of Civil Procedure article 2635, referred to above, expressly provides that a discrepancy in the attorney's fees stipulated in the note and the mortgage does not preclude use of executory process. As to the lack of paraph of the note with the assignment, the court observed that no statute or jurisprudence required a notary to paraph a note with an authentic act of assignment or endorsement. Moreover, after noting that Louisiana Revised Statutes (La. R.S.) 9:5305 declares "notes . . . need not be paraphed if the act of mortgage identifies them by date, number, amount and date when payable," the court stated:

> The courts have consistently interpreted this statute as authority for the proposition that a note need not be paraphed if it can be identified in all respects with the act of mortgage so that there can be no doubt that the two instruments are in fact related and that one stands as security for the other . . . .[31]

Although the court's decision may be correct as to the necessity for a paraph of the note in the case of an assignment, its reliance upon

25. La. Code Civ. P. art. 2635.
26. Id.
27. 477 So. 2d 847 (La. App. 5th Cir. 1985).
28. Id. at 849.
29. 481 So. 2d 186 (La. App. 1st Cir. 1985).
30. The opinion does not reveal the nature or extent of the discrepancy.
31. 481 So. 2d at 189 (citing Pepper v. Dunlap, 16 La. 163 (1840); Babin v. Winchester, 7 La. 460 (1834); U-Finish Homes, Inc. v. Lanzl, 202 So. 2d 339 (La. App. 1st Cir. 1967)).

the authorities cited is certainly misplaced. La. R.S. 9:5305 is an exceptional statute, dealing exclusively with conventional mortgages that secure several obligations.[32] The provision quoted obviously was intended to negate any inference that mortgages of that kind are subject to the provisions of Civil Code article 3384, which makes it "the duty" of every notary before whom a mortgage securing negotiable notes has been passed to paraph the notes with the act of mortgage. The cases relied upon as "interpreting the act in question" in fact have nothing to do with either the act or executory process. Rather, they recognize the well-settled principle that a failure to comply with the provisions of article 3384 does not affect the intrinsic validity of the mortgage itself. To be valid a mortgage need only be in writing,[33] identify the property encumbered,[34] and state the amount of the debt it secures.[35] Consequently, the failure of the notary to paraph the note as required of him, or to comply with any requirement for the authenticity of the mortgage, can only render the mortgage a private act, which is all the law requires for its validity. Such a mortgage is certainly not in authentic form and entitled to enforcement by executory process.

The jurisprudence is unvarying in its insistence that, for a debt in negotiable form to be enforced by executory process, it must be accurately described in the mortgage and carry the paraph of the notary before whom the mortgage is executed.[36] Nevertheless, it does not necessarily follow that the court is incorrect in its conclusion. The source of the "variance" rule is, as noted, not found directly in the Code of Civil Procedure or the statutes. It is evidentiary. The plaintiff in an executory proceeding is, in theory, proceeding upon a confessed judgment. His right is limited to executing upon property securing the obligation as to which the debtor has confessed judgment.[37] When the plaintiff presents that judgment for execution, he must accompany it with evidence in authentic form demonstrating his right to assert the

32. The provisions have their genesis in Act 72 of 1914, the obvious purpose of which was to permit the issuance of multiple or bond mortgages and the appointment of a trustee for the benefit of the creditors.

33. La. Civ. Code art. 3305. Obviously, if a private writing will suffice, a lack of paraph could hardly be said to affect its validity.

34. La. Civ. Code art. 3306.

35. La. Civ. Code art. 3309.

36. See Myrtle Grove Packing Co. v. Mones, 226 La. 287, 76 So. 2d 305 (1954), and the cases cited therein.

37. "Executory proceedings are those . . . to enforce a mortgage or privilege . . . evidenced by an authentic act importing a confession of judgment." La. Code Civ. P. art. 2631. "An act . . . imports a confession of judgment when the obligor therein acknowledges the obligation . . . and confesses judgment thereon . . . ." La. Code Civ. P. art. 2632.

judgment and seize the debtor's property.[38] The Code of Civil Procedure describes what evidence is authentic or is to be considered authentic. It also prescribes evidence that must be "included" in that which is presented by the petitioner.[39] The Code does not prescribe whether the evidence presented by a particular petitioner is sufficient to establish his right to proceed. When a note is presented, ostensibly securing a mortgage and paraphed for identification with it, and that note or the declarations of the notary or parties in connection with it vary in some material respect from each other, doubt is created as to whether the note is in fact the one the mortgage secures. In an ordinary proceeding, the plaintiff may cure this uncertainty by introducing evidence that a mistake was made in the recitals of the parties and that the note is in fact the one that the mortgagor executed and that the mortgage secures. In an executory proceeding, however, no evidence may be introduced that is not in authentic form. Furthermore, unless the petitioner introduces such evidence (as he might, through an act of correction, or certificate from the notary that one document or the other contains a clerical error[40]), he simply has not sufficiently proven his case to warrant issuing an ex parte order to seize and sell the debtor's property.

The case of *Myrtle Grove Packing Co. v. Mones*,[41] contains an excellent discussion of the rule, the reasons for its existence and the authorities supporting it. The court in that case refused to direct issuance of executory process where there was a discrepancy between the paraphed note and its description in the mortgage. The court summarized its reasons as follows:

> We still fail to see how the presence of the paraph cures the discrepancy between the recitals of the note and the one described in the act of sale and mortgage because it is essential that evidence, other than authentic, must be introduced to establish that the latter represents the same obligation upon which suit is brought. For executory process to issue, all of the evidence must be authentic.[42]

This statement explains and confirms the holding of the court in the *Bank of St. Charles* case. The court there held that, even though

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38. This rule has a long history. See Chambliss v. Atchinson, 2 La. Ann. 488 (1847), which also suggests that the notary's paraph may not be sacrosanct. See also McMahon, The Historical Development of Executory Procedure in Louisiana, 32 Tul. L. Rev. 555 (1958), for an excellent summary of the development of the process and its Spanish antecedents.

39. See La. Code Civ. P. art. 2635.

40. La. R. S. 13:4104 (1968) permits the notary to certify as to such an error on the note or mortgage with authentic effect.

41. 226 La. 287, 76 So. 2d 305 (La. 1954).

42. Id. at 307.

the note and mortgage conformed to each other, the statement of the notary that the note was paraphed for identification with a mortgage executed before him on a different day from the one presented would dictate, in light of the strictness of proof required for executory process, that some evidence be offered that the paraph was in error and that the note was in fact the one secured by the mortgage. Even if one postulates that a paraph is not necessary, the solemn declaration of the notary that the note in question is secured by a mortgage bearing a date different from the one attached to the petition should call for some explanation. If it does, that explanation must be given by evidence in authentic form.

Therefore, whether an act of assignment that transfers a mortgage note must contain a reference to a paraph of the note depends, to some extent, upon the terms of the documents. If, for example, the notary states that he has paraphed the note, but the note presented does not evidence such a paraph, some explanation should be forthcoming before the court could justifiably conclude that the note presented is the note that was assigned to the petitioner. On the other hand, the notary may declare in the act of assignment that the assignor has presented the note described in the mortgage, and mention its paraph and description. If, in addition, the assignor acknowledges that the note presented is in fact the one endorsed or transferred by him, then the presentation of the note (the authenticity of which is affirmed by the mortgage and paraph), endorsed in the manner described in the act of assignment, should provide the court with sufficient evidence to order issuance of executory process.[43]

Somewhat the same observation may be made concerning Code of Civil Procedure article 2635, which declares that a discrepancy between the attorney's fees stipulated in the note and those described in the mortgage does not preclude executory process. There is little doubt that this article renders such a discrepancy insufficient to require introduction of evidence that the note is the one described in the mortgage. Furthermore, the article clearly justifies the ordering of executory process

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43. It would seem to be indispensable for the notary to declare that the note has been exhibited to him with sufficient particularity to satisfy the court that the person signing the act of assignment was in fact the owner and holder of the note at that time. See, e.g., Bornes v. Vernon, 64 So. 2d 18 (La. App. 1st Cir. 1953), refusing to accept an act of release executed by one who only declared he was the "holder" of the note, rather than "the holder and owner." The presence of the notary's paraph on the note provides almost conclusive evidence that the note presented to him is the one secured by the mortgage and upon which execution is sought. The case in question may be correct, but sound practice would dictate, if only for the protection of the notary, that he paraph any mortgage note presented to him for identification with any act he executes modifying or affecting rights dependent upon it.

by the court in *Colonial Financial Services* for the enforcement of the principal and interest due on the note. But what of the attorney's fees? Permitting executory process where there is a variance in the documents "regarding the obligation to pay attorney's fees" says nothing about which document, if either, is presumed to be correct. To enforce the obligation to pay attorney's fees by executory process, the petitioner must still prove his right to collect such fees, the amount secured by the mortgage and the mortgagor's confession of judgment upon them.

Consider a mortgage in which the mortgagor confesses judgment upon his note and the obligations it contains, including that regarding attorney's fees, and also declares that such fees are secured by the mortgage. Suppose, however, he also declares that the note provides for attorney's fees of ten percent. Would the court be justified in issuing a writ directing the sheriff to seize and sell the property to satisfy the petitioner's claim for attorney's fees, if the note presented by the petitioner, although paraphed for identification with the mortgage and otherwise corresponding to it, in fact stipulates attorney's fees of 25 percent? The only evidence before the court is that an error exists with respect to the fees. Without additional evidence as to the nature of the error, is the court justified in concluding that either amount is correct? The author suggests petitioner has not made his case for including the fees in the description of the amount for which the property is to be sold under the writ of seizure and sale. Nevertheless, this may not be ultimately fatal to the plaintiff's case. It may be possible that he can assert and prove his claim for the fees out of the proceeds in the sheriff's hands after the sale, by a rule or motion directed to the sheriff.[44] There are cases, however, holding that a petitioner who prays for recognition of his mortgage in an ordinary action is not entitled to assert it if the judgment does not recognize it.[45] Thus, the defendant can argue that where the writ of seizure and sale does not authorize the sheriff to satisfy the claim for attorney's fees, the petitioner is precluded from recovering them until he establishes his right to them by an action for a deficiency judgment. The answer to the problem is by no means clear.

Brian v. The Jock Shop, Inc.[46] concerns the intractable problem of correlating the rules pertaining to the accessory nature of a mortgage with its status as a real right, regulated by the laws of registry. The

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44. The Code of Civil Procedure apparently only contemplates that third persons will assert such claims by intervention, and a case can be made that insofar as the proceeds of the sale by executory process is concerned, the petitioner would be limited to recovering the amount which the writ directs the property be sold to satisfy. See La. Code Civ. P. art. 2643.

45. See Houma Steel & Supply, Inc. v. Allied Towing Servs., Inc., 468 So. 2d 637 (La. App. 4th Cir. 1985), and cases cited therein.

46. 479 So. 2d 398 (La. App. 1st Cir.), cert. denied, 481 So. 2d 1349 (La. 1986).

debt secured by a mortgage is not a real right and is obviously not recorded. Consequently, its transfer or extinction cannot be determined from the public records. Civil Code article 2645, which provides that the "sale or transfer of a credit includes every thing which is an accessory to the same; as . . . mortgages,"[47] has been held to effect an implicit assignment of the mortgage when the note it secures is negotiated.[48] More importantly, third persons dealing with the mortgaged property are bound by such an assignment. As a result, the "mortgagee," who at any given moment may modify, release, enforce or otherwise exercise the rights granted by the mortgage, is the person entitled to enforce the principal obligation which the mortgage secures, even though there is nothing of record to reveal that person's identity.[49] This causes difficulty in cases of releases, amendments or other modifications of the mortgage, since third persons, finding such documents in the public records, must independently determine that the person purporting to act as the mortgagee was the creditor of the secured obligation.[50]

A corollary to this problem is created when the holder of the mortgage note executes an act modifying the mortgage, but negotiates the note before recording the act. Is the new holder of the note bound by the unrecorded act? It can be argued that he is on the grounds that an assignee can enforce no greater rights than his assignor possessed. Alternatively, it can be maintained that, although the assignee becomes a party to the mortgage by virtue of the assignment, an act or release or amendment to the mortgage is a different contract, which, because it affects a real right, is ineffective as to him unless recorded. This would preclude the person asserting that the assignor's rights were diminished by the release or amendment from introducing the agreement into evidence against the assignee.

In *Brian* the plaintiff was a surety for a corporation's obligations to the Fidelity bank. Plaintiff gave the bank a continuing guaranty agreement in which he bound himself in solido with the corporation for its debts to the bank "precisely as if the same had been contracted

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47. La. Civ. Code art. 2645.

48. A mortgage can, of course, secure any kind of obligation, but for pragmatic reasons conventional obligations are almost invariably cast in negotiable form when mortgage security is desired, and for convenience it will be assumed the mortgage debt is represented by a negotiable instrument.

49. The most obvious and notable consequences of this rule are the imposition of liability upon the recorder for cancelling a mortgage without evidence that the person granting the release is the holder of the note, and the rule permitting execution by executory process only upon evidence that the petitioner is the holder of the note secured by the mortgage.

50. It is safe to say this is one of the very few instances where a person may not affirmatively rely upon the records as evidencing the ownership of real rights transferable by agreement.

and was due or owing" by him. Further, he bound himself to the terms of any note of the debtor to the bank as "a party thereto."

The notes of the corporation to the bank were also secured by the pledge of a collateral mortgage note, that was in turn secured by a mortgage upon what was referred to as the Camelia Street property. The property was owned by one of the shareholders of the corporation, who was, not coincidentally, the brother-in-law of the plaintiff. The brother-in-law had independently executed and pledged the mortgage note and mortgage for the corporation's notes to the bank. When the corporation defaulted on its notes to the bank, the plaintiff apparently paid the bank under the guaranty agreement, and the bank assigned him the corporation's notes, as well as the collateral mortgage note.

After the assignment, the plaintiff attempted to execute upon the mortgage. The defendant sued to enjoin the action, alleging that, before the corporation defaulted on its obligations, the bank had verbally represented to a prospective purchaser of the Camelia Street property that nothing was owed upon the collateral mortgage note, and that the bank would release the mortgage upon request. The purchaser had in fact thereafter bought the property in reliance upon those representations, and later sold the property to the defendant, who was unaware that the mortgage had not been released. No act of release was ever actually executed or recorded, and it was upon the basis of the public records doctrine that the plaintiff asserted his right to enforce the mortgage.

The lower court enjoined the plaintiff on the grounds the the bank, and plaintiff as its successor, were estopped to assert the mortgage. The first circuit agreed with the plaintiff that the question of estoppel was not properly before the court, because the defendant had not expressly pleaded it. It then held, however, that the release of the mortgage was binding upon the bank and that the plaintiff could not raise the lack of recordation, because he was a "party" to the "transaction" under the terms of his guaranty agreement: "[F]or the purposes of the public records doctrine, Brian by executing a continuing guaranty on the debt of the Jock Shop, became a party to the note and mortgage by agreement and as such is bound by all agreements whether or not they are recorded."[51] The decision, although understandable,[52] is questionable if not clearly wrong on both points. A verbal agreement to release a mortgage, absent estoppel or confession, should be no more binding than any other verbal agreement affecting a real right.[53]

51. 479 So. 2d at 400.

52. The court was convinced that the plaintiff was aware that the bank did not consider the mortgage binding, and that his brother-in-law (the mortgagor) sold the property as being free of the mortgage.

53. The lower court had held the release binding upon grounds of estoppel. The

The court's conclusion that the terms of the guaranty made the surety "a party" to the mortgage and the note securing it also appears to be erroneous. The corporation, whose debts he guaranteed, was not a "party" to the mortgage and the mortgage note. The mortgage note was executed by a third person and was secured by a mortgage upon that third person's land. If the surety was, by virtue of his guaranty, "a party to" the note, in what capacity was he made a party? Was he maker? Payee? Endorser?[54]

This does not mean, however, that the decision is necessarily incorrect. Support for the court's action can be found in a line of cases holding that, while a mortgage note may be negotiable, the mortgage securing it is not. Consequently, a person acquiring a mortgage note, even as a holder in due course, only succeeds to the rights of the transferor of the note by virtue of the tacit assignment granted by article 2645. This assignee acquires no greater rights to the mortgage than his assignor possessed.[55] As applied to the present case, the rule would mean that the bank, having in fact released the mortgage, was no longer entitled to enforce it and could assign no rights in it to the plaintiff. Another line of cases, based upon the same principles, also indicates that (absent some contractual agreement to the contrary) the bank, by assigning the mortgage note (even "without recourse"), impliedly warrants the existence of the mortgage under the provisions of Civil Code article 2505.[56]

South Louisiana Bank v. Miller,[57] held that a chattel mortgage witnessed by only one witness and proven before the notary by the affidavit of the witness was invalid as to third persons. Louisiana Revised Statutes 9:5353 provides: "In order to affect third persons, every chattel mortgage shall be by authentic act, or by private act, duly authenticated in any manner provided by law."[58] The court went on to observe that several Civil Code articles "clearly provide that both an authentic act and an act under private signature require at least *two* witnesses."[59] The

court of appeal said this was erroneous, because the plaintiff in the injunction had not pleaded estoppel. The court gave no reasons whatsoever for its holding that "[t]he release of the mortgage by Fidelity [the bank], though not recorded, is effective between Fidelity, Fortier [the mortagor] and Brian [the plaintiff] . . . ."

54. The court's conclusion would be equivalent to saying that if a third person had pledged United States Bonds to secure the corporation's obligations, the plaintiff, as surety, became a "party to" the bonds with the United States. This is a conclusion which the writer (and I suspect the losing attorney) finds somewhat astounding.

55. See Adams v. Webster, 25 La. Ann. 117 (La. 1873).

56. See Lemoine v. City of Shreveport, 184 La. 221, 165 So. 873 (La. 1936), and Citizens Bank & Trust Co. v. Cook, 121 So. 306 (La. App. 2d Cir. 1928).

57. 479 So. 2d 461 (La. App. 1st Cir. 1985).

58. La. R.S. 9:5353 (1981).

59. 479 So. 2d at 463 (emphasis in original).

court also noted (by way of dicta) that "[a]ctual knowledge by a third person of the existence of a recorded chattel mortgage dispenses with the necessity of complying with statutory requirements."[60] The court relied upon *All State Credit Plan, Inc. v. Fournier*,[61] as authority for this proposition. *Fournier* contains substantially the same statement (also by way of dicta) relying, in turn, upon *Southern Enterprises v. Foster*,[62] a Louisiana Supreme Court decision. In *Southern Enterprises*, the court said that the requirements prescribed by the chattel mortgage regulations then in effect were essential only to make the mortgage effective as to "innocent third persons" without notice. Unfortunately, however, the Chattel Mortgage Act[63] construed by the court in that case expressly provided that the requirements for both authenticity and recordation were necessary to "affect third persons without notice."[64] The act was amended in 1944 (the source of the present provisions) to read: "in order to affect third persons every chattel mortgage," etc.[65] Consequently, the dicta by the court relative to lack of actual notice would ordinarily not merit comment. A few years after enactment of the present provision, however, the second circuit held that the 1944 revision was not intended to change its substance, and that actual notice of a chattel mortgage not only cured defects of form, but rendered lack of recordation itself irrelevant.[66]

The court's conclusion in *South Louisiana Bank* that an act under private signature requires two witnesses is also incorrect. The term "act under private signature" is synonymous with "written act" and simply refers to a writing signed by one or both of the parties. The most recent revision of the Civil Code sets forth the requirements of an act under private signature as follows: "An act under private signature need not be written by the parties, but must be signed by them."[67]

Although there were, and still are, references in the Civil Code to witnesses to a private act, there is not, and never has been, any requirement that such an act be witnessed to be valid. It cannot be said, however, that the court was incorrect in rejecting the act in question as not having been "authenticated" in a "manner provided by law." The parties attempted to authenticate the mortgage by the affidavit of the witness, as permitted by La. R.S. 13:3720, which provides that an act may be made "self proving" by the affidavit of "one of the

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60. Id. n.4.
61. 175 So. 2d 707 (La. App. 1st Cir. 1965).
62. 203 La. 133, 13 So. 2d 491 (La. 1943).
63. 1918 La. Acts No. 198, § 2, as amended by 1936 La. Acts No. 174.
64. Id.
65. 1944 La. Acts No. 172.
66. First Nat'l Bank v. Lawrence, 207 So. 2d 907 (La. App. 2d. Cir. 1968).
67. La. Civ. Code art. 1837.

witnesses" to the act stating that the witness saw the "other witness" and parties execute the same. The section obviously contemplates there are two or more witnesses to the act, and its provisions are probably unavailable where the act has only one witness. Nevertheless, there are a number of other ways of authenticating documents that do not contemplate or require witnesses to the basic act. For example, article 1836 of the Civil Code allows authentication by the acknowledgement of a party before a notary and two witnesses. La. R.S. 35:511 provides an alternative method of acknowledgement by permitting a party to acknowledge his signature before a notary alone. The decision in question would render such acknowledgements invalid unless the original act also was witnessed by two witnesses. Apart from the absence of any positive provision of law mandating such witnesses, it is difficult to see what value they would have, since the law declares a later acknowledgement by the parties in a form that does not involve those witnesses sufficient to give the act "authenticity" and make it self-proving.

The Private Works Act

In *Morgan v. Audobon Construction Co.*,[68] the court held that a statement of claim or privilege of a subcontractor signed "Yantley Erectors, Inc by: Wayne Morgan," was valid, although "Yantly Erectors" was a trade name under which Mr. Morgan did business. The Private Works Act requires that the statement of claim be signed by the person asserting the same "or his representative."[69] The comments to that section say:

> The purpose of the statement . . . is to give notice to the owner (and contractor) of the existence of the claim and to give notice to persons who may deal with the owner that a privilege is claimed on the property. . . . Technical defects in the notice should not defeat the claim as long as the notice is adequate to serve the purposes intended.[70]

The court found that the comments were supported by *Central Lumber Co. v. Douglas*,[71] and *Alside Supply Co. v. Gervais*,[72] and held that since there was no evidence that the contract or surety were misled or did not in fact know of the claim, the notice was sufficient.

The decision appears to be correct. Insofar as the owner is concerned, the recordation of the notice is almost irrelevant, since the act requires

68. 485 So. 2d 529 (La. App. 5th Cir. 1986).
69. La. R.S. 9:4822 E(2) (1983).
70. Official Comments to La. R.S. 9:4822 (1983).
71. 12 La. App. 680, 127 So. 43 (2d Cir. 1930).
72. 303 So. 2d 584 (La. App. 4th Cir. 1974).

delivery of a copy of the statement to the owner. As far as the contractor is concerned, the recordation has nothing to do with the establishment of a real right or the protection of third persons relying upon an independent examination of the records. The function of notice to the contractor is simply to protect him in paying his subcontractors and to establish a method by which he can be assured that the subcontractors have satisfied those persons who can claim the protection of the act. The matter is, as to the contractor, exclusively one of notice. He has no interest in the land, nor is he acquiring any interest in it. There is thus no reason to apply the ordinarily rather strict rules of construction developed to protect persons relying upon the public records pertaining to immovables and to give integrity to those records.

C.J. Richard Lumber Co. v. Melancon,[73] held that, for purposes of the Private Works Act, a supplier of materials may include the sales taxes in the price of the materials. Again, this seems to be correct. The act gives a privilege to the seller of goods "for the price" of the materials.[74] The sales tax act requires a seller to "add the amount of the tax, to the sale price or charges, which shall be a debt from the purchaser or consumer to the dealer, until paid."[75] It can hardly be said that the court was unjustified in reading the word "price" in the Private Works Act in pari materia with the sales tax. Certainly, the purpose of both acts is better served by the decision.

The act gives privileges to: "contractors" (and "subcontractors"), for "the price of their work"; "laborers" and "employees," for the "price of work performed at the job site"; "sellers," for the "price of movables . . . that become component parts of the immovable . . .; and "lessors," for the "rent of movables used at the site . . . leased by a written contract." After noting the specific and careful language used by these provisions of the act in defining the persons given rights under it, and the kinds of obligations they may assert, the court in *Cirlot Co. v. Lake Forest, Inc.*[76] rejected the claim of a person who entered into a contract "to supply equipment and drivers" to a contractor, to be directed by the latter. The court concluded the contract was neither one of employment nor the lease of movables, but was instead an innominate one that did not fall within any of the categories protected by the act.

The decision is probably correct, although there is little logic in excluding contracts of the type described from the protection of the

73. 476 So. 2d 1018 (La. App. 3d Cir. 1985).
74. La. R.S. 9:4801 (1983).
75. La. R.S. 47:304 (e) (Supp. 1986).
76. 475 So. 2d 799 (La. App. 4th Cir. 1985).

act. Certainly, the same arrangement could have been made in such a manner as to come within the terms of the act. On the other hand, the obvious purpose of the act is to give greater certainty to the status of persons involved in the construction process and to contractors, sureties, owners, lenders and others who must deal with the intricate contractual and property relationships involved in modern construction projects. There can be little doubt, reading the act as a whole, that the language of the classifications was intended to be both technical and precise. The penalty one usually pays for such precision is a certain degree of arbitrariness and unfairness arising from the inability to predict the multitude of contractual arrangements that modern industry may develop to take advantage of changing technology and economic conditions.