

CATTLE OWNERSHIP

Prepared for

Texas Cattle Feeders Association

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CATTLE OWNERSHIP

I. BASIC PROPOSITIONS

A. Unifying Rule

1. Priority in disputes does not necessarily turn on the concept of “title” or the concept of “ownership.” Similarly, “possession,” “brands,” and “bills of sale” do not necessarily govern outcome. In order to prevail, one must have rights which are superior to the competitors. Those superior rights are allocated with the express recognition that some party worthy of sympathy may still lose.
2. Generally, a party who has acquired his claim in good faith (honestly), for value in a transaction within the scope of ordinary business, and has done so without actual, or in some cases constructive, knowledge will prevail if the party conducted its transaction with one who had the power to convey superior rights.

B. Business Customs and Identity of the “Owner”

1. Very common practices in the cattle business create problems of legal ambiguity.
 - a) Cattle are bought and sold by telephone often with no inspection by either buyer or seller.
 - b) The “Code of the West” says that the buyer does not ask the identity of the seller.
 - c) Often the only proof of ownership is the seller’s word that the seller is actually the owner.

2. Different business entities are often created by cattlemen.

- a) “Semi” partnership arrangements.

- b) “Cowboy partnerships”

- c) Joint Ventures

- d) These entities usually are based on the need to share capital costs, and typically do not create a separate legal entity but instead involve some form of joint ownership.

3. Different capacities used by cattlemen.

- a) Operators may work as an “order buyer,” a cattle feeder, and operate a production business at the same time.

- b) Each of these involves different lending needs and may create different lending problems.

- c) For example, cattle in the possession of an “order buyer” may be classified as “inventory” while the same cattle may be “farm products” in the hands of a production operation.

II. PURCHASE CONTRACTS

A. General Requirements

1. To be enforceable by either buyer against seller or seller against buyer, a sales contract must be in writing and signed by the party against whom enforcement is sought (or by his authorized agent or broker).

2. To be enforceable, it is not required that the writing be formal or legalistic, nor is it required that it describe every detail of the transaction.
3. If the party against whom enforcement is sought is a “merchant” (and feedyards, middlemen, and probably most producers, would qualify as “merchants”), and that party receives a contract or purchase confirmation and does not object to it in ten (10) days, that party will be bound to its terms even if it was never signed.
4. Exceptions to Necessity for a Writing

If an oral contract is formed, it may be enforceable if payment has been made and/or delivery has been accepted under the oral contract.

B. Warranties in General

Whether it says so or not, a contract for sale carries a number of warranties which are given by Seller to Buyer. If Seller wants to avoid the warranties, exclusion must be explicit.

1. Implied Warranties Concerning Sale of Livestock
 - a) Several states have modified or excluded implied warranties concerning livestock.
 - (1) Texas has excluded the implied warranties of merchantability and fitness concerning the sale of livestock in all instances.
 - (2) Oklahoma law says that the implied warranties of merchantability and fitness do

not apply to the sale of livestock, if the seller “offers sufficient evidence that all state and federal regulations pertaining to the health of such animals were complied with,” and says that implied warranties do apply to the sale or barter of horses.

- (3) Kansas says that there are no implied warranties concerning the sale of livestock, “other than the sale of livestock for immediate slaughter.”
- (4) It does not appear that either Colorado or New Mexico have enacted an exclusion of implied warranties in the sale of livestock. In those states, a sale of cattle will carry an implied warranty.

b) In determining whether a warranty of health has been breached, the following factors may come into play:

- (1) A properly crafted written agreement in favor of the purchaser will contain an explicit warranty of health.
- (2) Even if a written contract is signed, if the contract does not contain a health warranty, the law which governs the contract will determine whether an implied warranty exists. This question involves a concept known as “conflicts of law” and is determined on a case-by-case basis.

2. Risk of Death or Loss

The contract may specify when risk of loss passes. If it does not specify, generally risk of loss passes to the buyer when he receives the cattle.

C. The Importance of Delivery

1. The concept of delivery of possession is crucial to understand the relationship between buyer and seller to cattle.
2. The UCC says that despite any agreements between the parties to the contrary, ownership to goods passes no later than delivery of possession. This means that the idea that “title does not pass until the check clears” is not a relevant legal concept when the rights of third parties are involved.
3. In fact, under the Code, title passes even if a check is given which eventually bounces so long as delivery has been made.
4. Ownership can transfer even before delivery if the parties make such an agreement.

D. Buyer’s Rights if Seller Fails to Deliver

[For purposes of these statements, it is assumed that the contract in question identifies specific cattle to be purchased.]

1. The existence of a contract to purchase gives the buyer an insurable interest in the cattle, even if they are still in the hands of seller.
2. If a seller is insolvent, a buyer may attempt to “reclaim” the purchased goods from seller if buyer has paid

all or a part of the purchase price. (See discussion below).

3. Generally, however, the fact that the buyer has a contract with the seller and has made a down payment, will not allow that buyer to take the cattle away from a second buyer who has obtained possession of the cattle, so the disappointed first buyer is left to sue seller for damages.

E. Seller’s Rights if Buyer Fails to Perform

GENERAL RULE: If the seller has delivered cattle or other goods and has not been paid (or the buyer’s check has not cleared) when an insolvency arises, the seller must seek legal help immediately and its lawyer generally must take certain steps very quickly. This is not the time for “Doing It Yourself.”

1. Assurance of Performance. If the seller believes the buyer is not going to perform when delivery time occurs, the seller can protect itself by requiring assurance of performance by the buyer before a seller relinquishes possession.
2. Stoppage of Transit. If the goods are actually in transit at the time Seller discovers the insolvency of the buyer, the seller can instruct the carrier to stop delivery.
3. Seller’s Right to Reclaim Cattle Delivered But Not Paid For
 - a) There is a right to “reclamation” (a right to regain possession of delivered goods) recognized by the law, but there are a number of limitations.

- (1) Except where buyer has given seller a false representation of solvency within three months before delivery, the seller must give written demand for reclamation within ten days of delivery.
 - (2) The seller's right to reclaim generally will be good only as against his buyer and is not useful as against subsequent buyers and claimants further down the chain of title if they qualify as "good faith purchasers," or "lien creditors."
- b) Nevertheless, where cattle have been sold to a party who files bankruptcy or suddenly disappears, reclamation is the first remedy the seller should consider.
4. The seller can seek to recover a judgment against the buyer for damages. Generally, the seller will be obligated to try to cover as much of his loss as reasonably possible by re-selling.

III. COMPETITION BETWEEN UNPAID SELLERS AND MULTIPLE BUYERS

A. Beware of the Middleman

The most common crisis of insolvency in the cattle industry is the insolvency of a middleman who operates in a number of capacities such as producer, pasture operator, pasture lessee, pasture lessor, cattle dealer and cattle broker.

B. Some Basic Rules of Competition Under the Uniform Commercial Code

1. Determination of superior rights is the issue. All competing parties may have some rights which are worthy of sympathy and, absent the crisis of insolvency, might be enforceable. Priorities are determined, however, on the basis of superior rights, not necessarily "title," "ownership," or "possession."
2. An agreement between a seller and a buyer may not be binding on third parties. For example, an attempt by a seller to "reserve title" until full payment, is, after delivery has occurred, no more than a security interest. (If the security interest is unperfected, it does not bind one who purchases in good faith from the insolvent party.)
3. The Effect of Possession in Ownership Disputes
 - a) A contract to buy, coupled with delivery of possession, gives the buyer the ability to transfer superior rights to others. In the law this is known as the "shelter provision."
 - b) A party who acquires cattle under a transaction of purchase (a contract) has the power to transfer superior rights to its own lender or a downstream purchaser even though:
 - (1) the delivery was in exchange for a dishonored check; or
 - (2) the delivery was procured through fraud; or
 - (3) the transferor was deceived as to the identity of the purchaser.

- c) A party who acquires possession of cattle under a transaction of “entrustment” has the power to transfer superior rights to a downstream buyer (but not its own lender). The issue of “entrustment” is a fertile ground for argument between two relatively innocent parties.
 - d) The concept of “entrustment” is viewed from an objective standpoint and focuses primarily on the apparent business of the seller as a dealer or merchant in goods of the kind entrusted. However, only a “buyer in ordinary course of business” from the trustee may benefit from the concept of entrustment. (A lender cannot be a “buyer in ordinary course.”)
- a) How has the alleged principal described his relationship with the middleman, both to the middleman and to third parties?
 - b) What has the middleman said?
 - c) Whose credit did the third party rely on?
 - d) What is the true nature of the business of the middleman? For example, does he take an ownership position, or is he just a broker? Does he always make the same profit, or does he sometimes make a larger profit or sustain a loss?
 - e) Although not every relationship described by the participants as a “partnership” or “joint venture” is a legal partnership or joint venture, the existence of a legal partnership or joint venture or the characterization of such relationship by the parties may be a relevant factor.

C. Agency Principles

1. Agency law is primarily a product of case law. It deals with the power of one party to bind another, and is highly fact-dependent.
2. A finding of agency may create a result different from what would occur otherwise under the UCC rules described above. An argument that the insolvent middleman is the agent of the disappointed seller may benefit the ultimate buyer; and conversely, an argument that the insolvent middleman is the agent of the buyer may benefit the disappointed seller.
3. In the cattle business, the broke middleman is often alleged to be someone’s agent, which allegations raise complicated factual issues. However, some factors which may influence agency questions are:

D. Brands And Bills Of Sale

1. Brands

- a) Brand laws and the effect of brands differ among states. Brands have proven impractical as a means to settle title and ownership disputes because modern husbandry practices do not consistently use brands for the purpose of settling such disputes.
- b) A Texas law enacted in 1848 attempted to suggest that a brand was some evidence of ownership when it said:

“No brand, except as . . . [properly recorded] shall be recognized in law as any evidence of ownership.”

This statute was repealed in 1929. Since then, one case has stated that brands are “some evidence” of ownership, but it appears that Texas law would permit the true owner to show ownership even if its brand was not on cattle in dispute.

- c) In some states, the presence of a recorded brand may be considered “prima facie” evidence of ownership rebuttable by other showings of fact.
- d) Brands may be material to the argument in disputes involving questions of knowledge or lack of knowledge and the buyer’s and seller’s respective abilities to convey good title.

2. Bills of Sale

- a) A Texas statute dating to 1866, still on the books, states that sales of cattle must be accompanied by a “written transfer” describing the number of head and identifying marks and brands.

Early cases under the statute established that a sale of cattle accompanied by delivery and payment was not rendered unenforceable by the statute if there was no bill of sale. Those early cases are believed to be still good law.

- b) The Colorado Supreme Court has stated that the “majority of jurisdictions that have construed

similar statutes” hold that livestock bill of sale laws, even those which state that they establish “prima facie ownership,” are still subject to the general rules concerning ownership established by the Uniform Commercial Code.

3. “Bill of Sale” Drafts

- a) A carefully written bill of sale draft can accomplish many objectives from the purchaser’s standpoint.

(1) A bill of sale draft can contain a promise by the seller that no liens against the cattle exist.

(2) The same document can also require that if there are any liens, the lienholder’s execution of the draft constitutes a release of those liens.

(3) This same document can serve as evidence of the transfer of ownership from the buyer to the seller.

- b) A “bill of sale draft” may be helpful to the purchaser’s lender in tracing collateral.

- c) A “bill of sale” draft may give the purchasers some helpful, but not determinative, points of argument as to third parties. However, if the purchaser has a bill of sale from someone who is not the owner, the bill of sale is not much help.

IV. TIPS FOR PURCHASING FARM PRODUCTS IN TEXAS

A. Cattle Purchased from Dealers

1. If the seller is clearly and unambiguously a dealer, such as a cattle aggregator, the cattle are arguably “inventory” and the Feedyard will be a “buyer in ordinary course of business.”
2. If the cattle are “Inventory” and the feedyard is a “Buyer in Ordinary Course of Business”, the Feedyard will take free of the dealer’s lender’s liens.

B. Cattle from “Cattle Jockeys”

1. Cattle may or may not be the seller’s inventory. If cattle are not “inventory” they are “farm products” and the seller’s lender’s lien may carry over and the Feedyard may purchase subject to the lien.
2. The feedyard should follow the same protective procedure as with purchases from cattle producers.

C. Cattle from Producers

1. The feedyard is very likely to take subject to producer’s lender’s lien.
2. The feedyard should honor any actual notices received from lenders requiring joint payment.
3. The feedyard should honor notice received by virtue of the “newspaper,” that is, the publication of lien filings by the central notification system incorporated.
4. The feedyard should honor any UCC financing statements discovered by a search. The feedyard’s safety is enhanced by conducting a UCC search.

5. Note: After July 1, 2001, UCC search procedures need to be changed to take into account changes in new Article 9.

D. Grain or Hay Purchased from Merchandisers

1. If the merchandiser is clearly a merchandiser and not a producer, the feedyard should qualify as a “buyer in ordinary course of business.”
2. If the feedyard is a “buyer in ordinary course of business”, it will take free of the seller’s lender’s lien, and the feedyard is safe not to check filings.
3. Any explicit notice from the merchandiser’s lender, however, should be heeded, or at least investigated because merchandiser’s lender may realize upon accounts receivable of the merchandiser by giving such a notice.

E. Grain, Ensilage or Hay Purchased from a Producer

1. The feedyard is very likely to take subject to the producer’s lender’s lien unless the feedyard takes precautions.
2. The feedyard should honor actual notices received from lenders.
3. The feedyard should honor notice received by virtue of the “newspaper,” the publication of Central Notification System, Inc.
4. The feedyard should honor any UCC financing statements discovered by a search.

5. After July 1, 2001, the feedyard may need to alter search procedures to comply with the new provisions of Article 9 of the Uniform Commercial Code.

BIOGRAPHICAL SKETCH
OF
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John Huffaker graduated from Texas Tech University with a B.S. and later received his J.D. from The Texas Tech University School of Law in 1974. While at The Texas Tech University School of Law, he served as Editor in Chief of The Texas Tech Law Review, and graduated Order of the Coif. His practice areas include general commercial litigation, agricultural law, bankruptcy and creditors' rights, employment law, and representation of public entities. He has served as Chair of the State Bar of Texas Committee on Agricultural Law. He is a member of the Texas Association of Bank Counsel and frequently speaks on issues arising in lender liability, risk avoidance, and agricultural law. He is a current member of the Texas Bar Foundation and the College of the State Bar of Texas. Mr. Huffaker is Board Certified in Civil Trial Law.

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OF
DAVID L. LEBAS

David LeBas was born in Kassel, Germany, in 1957. He graduated from the University of Texas with a B.A. in 1979 and a J.D. in 1982. He is Board Certified in Civil Trial Law, and he practices in the areas of business litigation, concentrating in areas of agriculture, lending, construction law, probate, and intellectual property. Bar associations include Amarillo Area Young Lawyers Association (President 1988-1990), Texas Young Lawyers Association (Director 1988-1990), Texas Bar Foundation (Life Fellow), Texas Association of Defense Counsel, and the State Bar's Agricultural Law Committee (Chair 1998-1999).

Mr. LeBas' recent bibliography includes:

1. "The Recovery of Expectancy Damages in Misrepresentation Cases" (Spring 1996 and Summer 1997, TADC).
2. "Recent (and Relevant) Texas Supreme Court Cases" (Winter 1997, TADC meeting).
3. "Insurance Code Art. 21.21 and Art. 21.55 Highlights" (Spring 2000, TADC).
4. "Texas Livestock Law" (1992, 1995, 1996, 1998 Agricultural Law Seminar).
5. "Creating and Protecting Agricultural Loans" (1999 State Bar Agricultural Law Seminar).
6. "Risks to Lenders in the Use of Forward Contracts by Borrowers" (1999 Texas Tech Agricultural Lending School).
7. "Creating and Protecting Agricultural Liens" (Fall 2000 Texas Assoc. of Bank Counsel Annual Convention).