

# SMU Annual Texas Survey

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## Commercial Transactions

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# COMMERCIAL TRANSACTIONS

*John Kraemer\**

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## I. INTRODUCTION

The last Commercial Transactions Survey included cases decided under the Texas Uniform Commercial Code (UCC) through the end of 2013.<sup>1</sup>

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1. The Texas version of the Uniform Commercial Code appears as the first nine chapters in the Texas Business and Commerce Code (the Code). *See* TEX. BUS. & COM. CODE ANN. §§ 1.101–9.809 (West 2015). The Code first became effective in Texas on July 1, 1966, as a separate statute. *See* Act issued Sept. 27, 1965, 59th Leg., ch. 721, § 1-316, 1965 Tex. Gen. Laws 1951. It was reenacted in 1967 as part of the Business and Commerce Code, the first of the codes promulgated under the Texas Codification Act. In that process, the designation of “Article” in the Official Text was changed to “Chapter,” subsections were designated by letters rather than numbers, and a period instead of a dash was used to designate sections. Thus, for example, § 2-204(1) in the Official Text became § 2.204(a) in the Texas codification. Revisions of the Code that have taken place since 1967 still substitute “Chap-

This Survey discusses cases decided through the end of 2015. During the last two years, cases dealing with the sale of goods and negotiable instruments under Chapters 2 and 3 predominated, while only a relative few cases dealt with bank deposits and collections or secured transactions under Chapters 4 and 9.

## II. DEFINITIONS AND GENERAL PROVISIONS

### A. CONSPICUOUSNESS & FAIR NOTICE

Under Texas law, it is clear that the definition of “conspicuous” in § 1.201(b)(10) of the Texas Business and Commerce Code (Code) is to be applied in both Code and non-Code cases.<sup>2</sup> A clause is conspicuous if it appears in larger type, in contrasting color, or is stated in some other way that it would call attention to itself.<sup>3</sup> In addition, if a clause attempts to disclaim liability for negligence, the clause must specifically indicate that such liability is being disclaimed.<sup>4</sup> However, if the affected party has actual knowledge of the terms of a disclaimer, the disclaimer will be enforceable whether or not it is conspicuous.<sup>5</sup>

The same standards of conspicuousness and fair notice apply to indemnity agreements as illustrated by the decision in *In re H & M Oil & Gas, LLC*.<sup>6</sup> In that case, the U.S. Bankruptcy Court for the Northern District of Texas held that an indemnity clause was not conspicuous when the part of the agreement in which it was contained had the heading “Miscellaneous,” was not in a contrasting font or type style, and was one of twelve sections appearing under the same heading.<sup>7</sup> But the indemnity provision was enforceable even though it was not conspicuous, because the indemnitor had actual knowledge of the provision.<sup>8</sup>

In *J.C. Penney Purchasing Corp. v. Welco, Inc.*,<sup>9</sup> an indemnity clause appeared as one of several printed clauses in light grey print and in a small font on the reverse side of a purchase order, which was printed on thin paper and made the text hard to read.<sup>10</sup> In addition, the clause was

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ter” for “Article,” and still use a period instead of a dash, but now use the Official Text system for designating subsections. *See, e.g.*, Act issued Sept. 8, 1995, 74th Leg., ch. 921, § 1, 1995 Tex. Gen. Laws 4582 (effective on January 1, 1996). As currently enacted, Chapter 2 is the only chapter of the Code that retains the older non-uniform system to designate subsections. In the grand scheme of things, this is a minor point, but it can be confusing when doing Code research and in correlating the text of the Official Comments (which have not been adopted in Texas as part of the Code itself) to the statutory provisions. It can also affect searching on WestLaw and LEXIS if the searcher is trying to track case interpretations of particular sections of the Code because of the variation in section and subsection designations over the years.

2. *See Dresser Indus. v. Page Petroleum*, 853 S.W.2d 505, 509 (Tex. 1993).

3. *Id.*; *see also Littlefield v. Schaefer*, 955 S.W.2d 272, 274–75 (Tex. 1997).

4. *See Littlefield*, 955 S.W.2d at 274.

5. *See Cate v. Dover Corp.*, 790 S.W.2d 559, 561 (Tex. 1990).

6. 514 B.R. 790, 833–34 (Bankr. N.D. Tex. 2014).

7. *Id.* at 834–35.

8. *Id.*

9. No. 4:13-CV-684, 2014 WL 6787787 (E.D. Tex. Dec. 2, 2014).

10. *Id.* at \*3.

not in contrasting type and there was no distinctive heading that would draw attention to the clause. Because the clause was not conspicuous, and there was no showing that the indemnitor knew about the clause, the U.S. District Court for the Eastern District of Texas held that the indemnity provision was unenforceable.<sup>11</sup> The district court reached a similar result in *Plasma Fab, LLC v. BankDirect Capital Finance, LLC*,<sup>12</sup> where a limitation of liability clause in a premium financing agreement appeared in the same size font in the sixteenth paragraph of a two-column, multi-page agreement and was not identified by a distinctive heading or other indication that it limited liability.<sup>13</sup> In fact, the heading identified the clause with the word “Liability,” instead of “Limitation of Liability.”

In *Grijalva v. Bally Total Fitness Corp.*,<sup>14</sup> the membership agreement for a fitness center contained a clause releasing the center from liability for injuries that might result from use of the equipment or negligence on the part of the center or its employees.<sup>15</sup> The clause was printed in capital letters in the membership agreement and included a notice appearing just above the signature line to alert the signer that the agreement contained a “Waiver and Release” of liability. The plaintiff admitted that he had signed the agreement. The First Houston Court of Appeals held that because the clause was conspicuous and gave fair notice to the signer, it was effective to bar the plaintiff from recovering for an injury that he suffered at the fitness center.<sup>16</sup>

In *Matador Production Co. v. Weatherford Artificial Lift Systems, Inc.*,<sup>17</sup> the Texarkana Court of Appeals also addressed the issue of whether a disclaimer of liability and indemnity clause was conspicuous, but in a somewhat different context.<sup>18</sup> In this case, the clause appeared in six-point type at the end of a six-page price estimate and directed the reader to the service provider’s website for a statement of the terms and conditions where the disclaimer and indemnity terms were conspicuous. The seller argued this made the clause effective. The court of appeals, however, rejected this argument because the statement in the price estimate itself was not conspicuous and did not indicate that the website contained significant limitation of liability provisions.<sup>19</sup> The result in *Matador* provides an interesting counterpoint to the decision in *One Beacon Insurance Co. v. Crowley Marine Services, Inc.*,<sup>20</sup> where the U.S. Court of Appeals for the Fifth Circuit held that a clause in a repair service order that incorporated the terms on the purchaser’s website and included the URL

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11. *Id.* at \*5–6.

12. 468 S.W.3d 121 (Tex. App.—Austin 2015, pet. granted).

13. *Id.* at 129.

14. No. 01–14–00217–CV, 2015 WL 1544582 (Tex. App.—Houston [1st Dist.] Apr. 2, 2015, no pet.).

15. *Id.* at \*1–2.

16. *Id.* at \*5–6.

17. 450 S.W.3d 580 (Tex. App.—Texarkana 2014, pet. denied).

18. *Id.* at 593.

19. *Id.* at 594.

20. 648 F.3d 258 (5th Cir. 2011).

for the website was effective to invoke the conspicuous indemnity provisions contained on the website.<sup>21</sup> The lesson to be drawn from a comparison of these two cases is clear: terms on a website can be incorporated as part of a written agreement, but the incorporation must itself be conspicuous, and the website to which a clause refers should be made readily available and conspicuously state any disclaimers, limitations of liability, or indemnity provisions applicable to the contract.

## B. ACCELERATION CLAUSES

Under the Code, parties can agree to permit acceleration of a payment obligation upon default, “at will,” or when a party “deems itself insecure.”<sup>22</sup> As developed in Texas case law, unless waived, the party against whom a debt is accelerated must be given notice of intent to accelerate and a notice of the acceleration, followed by presentment and a demand for payment of the accelerated amount.<sup>23</sup> To be effective, a waiver must be “clear and unequivocal” and must specifically state the rights being waived.<sup>24</sup>

In *Schuhardt Consulting Profit Sharing Plan v. Double Knobs Mountain Ranch, Inc.*,<sup>25</sup> the holder of a note and mortgage attempted to accelerate payment due to a default by the mortgagor.<sup>26</sup> After the mortgagor made several late payments on the note, the mortgagee sent a written notice stating that payments were due on the first of each month and that the note would be strictly enforced. This was followed a month later by a text message, the content of which was not put into evidence. The San Antonio Court of Appeals held that the written notice and the text message were insufficient to give the mortgagor notice of default or of intent to accelerate.<sup>27</sup>

In *Murphy v. HSBC Bank USA*,<sup>28</sup> the focus was not on the content of the notice of acceleration, but on whether the party who invoked an acceleration clause had later abandoned the acceleration.<sup>29</sup> The U.S. District Court for the Southern District of Texas held that an issue of material fact existed as to whether the note holder had abandoned its earlier acceleration and could send another notice of acceleration to remain within the four-year limitations period applicable to notes secured by real property when a note holder seeks to foreclose on the property securing the note.<sup>30</sup> The district court reversed its earlier summary judg-

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21. *Id.* at 270.

22. TEX. BUS. & COM. CODE ANN. §§ 1.309, 3.308 (West 2015).

23. *See, e.g.*, *Ogden v. Gibraltar Sav. Ass'n.*, 640 S.W.2d 232, 233 (Tex. 1982); *Shumway v. Horizon Credit Corp.* 801 S.W.2d 890, 893 (Tex. 1991).

24. *See Shumway*, 801 S.W.2d at 893.

25. 468 S.W.3d 557 (Tex. App.—San Antonio 2014, pet. denied).

26. *Id.* at 564.

27. *Id.* at 571–72.

28. 95 F. Supp. 3d 1025 (S.D. Tex. 2015).

29. *Id.* at 1039.

30. *Id.* at 1040. On this point, the district court noted that, “When a cause of action accrues is a question of law for the court, while whether a holder has accelerated a note is a

ment in favor of the mortgagor and addressed the issue of fact about abandonment of the first acceleration.<sup>31</sup>

More than thirty years ago, the Texas Supreme Court admonished creditors to include a savings clause in their contracts to avoid problems of usury that may result from careless use of an acceleration clause.<sup>32</sup> In *Franch v. HP Locate, LLC*,<sup>33</sup> the creditor took this lesson to heart and included a savings clause that expressly limited the interest due on a note to an amount that did not exceed the maximum rate allowed in Texas. The U.S. District Court for the Northern District of Texas held that this clause effectively defeated the makers' claim of usury, and the creditor was entitled to recover the accelerated principal due on the note along with an order compelling turnover of collateral securing the note and the recovery of attorney fees.<sup>34</sup>

### III. SALE OF GOODS

#### A. SCOPE OF CHAPTER 2

Chapter 2 of the Code applies to the sale of goods. A sale is defined as “the passing of title from the seller to the buyer for a price.”<sup>35</sup> Goods are defined as “all things (including specially manufactured goods) which are movable at the time of identification to the contract for sale.”<sup>36</sup> If a contract calls for both the sale of goods and the rendition of service, the usual approach is to apply what is called the “predominate purpose test” to determine whether the sale or the service was the principal purpose of the contract.<sup>37</sup> By their very nature, distributorship contracts contain a

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question of fact.” *Id.* In the context of this case, as stated by the district court, “unless the first acceleration was effectively abandoned, continued, or waived, and therefore a new, independent acceleration invoked in June 2012, HSBC’s second suit, *i.e.*, the instant action, was outside the four-year limitations period and is time-barred.” *Id.* at 1029 n.8.

31. *Id.* at 1040; *see also* *Ward v. Stanford*, 443 S.W.3d 334, 346 (Tex. App.—Dallas 2014, pet. denied) (addressing a similar issue and reaching a similar conclusion).

32. *See* *Jim Walter Homes, Inc. v. Schuenemann*, 668 S.W.2d 324, 333 n.6 (Tex. 1984). In no uncertain terms, the supreme court stated:

[W]e fail to understand why acceleration clauses are drafted which do not include a sentence expressly disavowing any intention to collect excessive unearned interest or finance charges in the event the obligation is accelerated. To leave the matter open to doubt is to invite litigation and risk the harsh penalties of article 5069 [now Tex. Fin. Code. § 305.001 (West 2006)].

*Id.*

33. No. 3:14-CV-3247-L, 2015 WL 7251678 (N.D. Tex. Nov. 16, 2015).

34. *Id.* at \*12.

35. TEX. BUS. & COM. CODE ANN. § 2.106(a) (West 2015).

36. *Id.* § 2.105(a).

37. *See, e.g.*, *Structural Metals, Inc. v. S & C Elect. Co.*, No. SA-09-CV-984-XR, 2012 WL 4959465, at \*9–10 (W.D. Tex. Oct. 16, 2012) (determining the essence of the contract was the purchase of AVC power units not design services for the installation of the units); *Cont’l Casing Corp. v. Siderca Corp.*, 38 S.W.3d 782, 787–88 (Tex. App.—Houston [14th Dist.] 2001, no pet.) (determining that the dominate feature of distributorship contract containing a mix of sales and service was for the sale of goods but contract was unenforceable for failure to comply with statute of frauds under § 2.201 of the Code); *Westech Eng’g, Inc. v. Clearwater Constructors, Inc.*, 835 S.W.2d 190, 197 (Tex. App.—Austin 1992, no writ) (determining predominate purpose of construction subcontract was for the sale of goods where subcontractor was to provide equipment for construction project).

mix of sales and service, but it now appears that Texas law has reached the point where distributorship contracts are routinely treated as contracts for the sale of goods under Chapter 2.<sup>38</sup>

In *Joniback Management Trust v. Wartburg Enterprises, Inc.*,<sup>39</sup> the U.S. District Court for the Southern District of Texas had no difficulty in reaching this conclusion in a contract of indefinite duration entered into between a South African seller and an American buyer calling for the distribution of plastic baby seats in the United States.<sup>40</sup> However, two other issues involved in this case required further proceedings. First, there was a significant dispute about whether an oral agreement between the parties restricted the ability of the American buyer to sell to whomever it chose. Second, it was not clear whether the seller or the buyer was the first to cancel or terminate the agreement and whether the cancellation or termination complied with the reasonable notice requirements of § 2.106 of the Code.<sup>41</sup> Because of these disputed issues of material fact, summary judgment was denied and the case continued for further proceedings.<sup>42</sup>

#### B. WARRANTY OF GOOD TITLE

Two cases decided during this Survey period provide an excellent illustration of the proof required to prevail under § 2.312 of the Code for breach of the implied warranty of good title.<sup>43</sup> In *City Direct Motor Cars, Inc. v. Expo Motors, L.L.C.*,<sup>44</sup> a car dealer purchased a vehicle from another dealer. The purchasing dealer sold the car to a retail buyer. Approximately three months after these transactions occurred, a secured party asserted that it had a prior lien on the vehicle and sued the selling dealer, the purchasing dealer, and the retail buyer for conversion. The purchasing dealer repurchased the vehicle from the retail buyer and filed

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38. The seminal case for this approach is *E. Hill Marine, Inc. v. Rinker Boat Co.*, where the Fort Worth Court of Appeals noted that “the overwhelming majority of jurisdictions that have considered the question have concluded that distributorship agreements are subject to the UCC.” *E. Hill Marine, Inc. v. Rinker Boat Co.*, 229 S.W.3d 813, 819 (Tex. App.—Fort Worth 2007, pet. denied). And the court of appeals decided to follow the majority rule. *Id.* at 19–20; see also John Krahmer, *Commercial Transactions*, 61 SMU L. REV. 657, 662–63 (2008) (discussing *E. Hill Marine*, 229 S.W.3d 813); D & M Edwards, Inc. v. Bio-Cide Int’l, Inc., No. 3:08-CV-0670-L, 2009 WL 102732, at \*2–3 (N.D. Tex. Jan. 14, 2009) (parties conceded that contract for distribution of food processing equipment was governed by Chapter 2 of the Code).

39. 136 F. Supp. 3d 792 (S.D. Tex. 2015).

40. *Id.* at 810.

41. Section 2.106(c)–(d) of the Code provide for termination or cancellation of a sales contract of indefinite duration like the contract involved in the case at bar. TEX. BUS. & COM. CODE ANN. § 2.106(c)–(d) (West 2015).

42. *Joniback Mgmt. Trust*, 136 F. Supp. 3d at 821–23.

43. Section 2.312 of the Code provides, in part, that “there is in a contract for sale a warranty by the seller that (1) the title conveyed shall be good, and its transfer rightful; and (2) the goods shall be delivered free from any security interest or other lien or encumbrance of which the buyer at the time of contracting has no knowledge.” TEX. BUS. & COM. CODE ANN. § 2.312.

44. No. 14-13-00122-CV, 2014 WL 2553484 (Tex. App.—Houston [14th Dist.] June 5, 2014, pet. denied) (mem. op).

a cross action against the selling dealer for breach of the warranty of good title. Though it was later determined that the secured party did not have a valid lien, the Fourteenth Houston Court of Appeals held that the title dispute interfered with the ability of the purchasing dealer to resell the vehicle, and that this constituted an encumbrance on the vehicle.<sup>45</sup> The court of appeals, therefore, upheld a jury finding in favor of the purchasing dealer.<sup>46</sup>

In contrast to the result in *City Direct*, the Austin Court of Appeals in *Green Tree Servicing, LLC v. ICA Wholesale, Ltd.*<sup>47</sup> reasoned that Texas law requires a buyer to show an interference with the buyer's right to quiet possession of the goods as a part of the buyer's claim for breach of the warranty of title.<sup>48</sup> Unlike the situation in *City Direct* where the purchasing dealer had to repurchase the vehicle and defend an action for conversion, the buyer of a manufactured home in *Green Tree* had suffered no interference with its claim of ownership and introduced no evidence that its right of quiet possession had been disturbed. The judgment of the trial court was reversed and judgment rendered in favor of the seller.<sup>49</sup>

### C. WARRANTIES OF QUALITY

The Code provides for three different warranties of quality. The first is creation of express warranties by the seller's affirmation, promise, description, or sample of the goods.<sup>50</sup> The second is an implied warranty of merchantability that generally means the goods will pass without objection in the trade, are of fair average quality, and fit for their ordinary purposes.<sup>51</sup> The third is a warranty that the goods are fit for the buyer's particular purpose.<sup>52</sup> This warranty differs from the warranty of merchantability by requiring that the seller know of the particular purpose for which the goods are to be used, and the buyer must rely on the seller's skill and judgment in selecting or furnishing goods suitable for the buyer's purpose.<sup>53</sup>

Until the significant decision in *Man Engines & Components, Inc. v. Shows*,<sup>54</sup> Texas law had held that implied warranties of quality do not arise in the sale of used goods.<sup>55</sup> In *Man Engines*, the engines on a yacht

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45. *Id.* at \*3.

46. *Id.*

47. 439 S.W.3d 657 (Tex. App.—Austin 2014, no pet.).

48. *Id.* at 660–61.

49. *Id.* at 662.

50. See TEX. BUS. & COM. CODE ANN. § 2.313 (West 2015).

51. See *id.* § 2.314.

52. See *id.* § 2.315.

53. Compare *id.* § 2.315, with *id.* § 2.314.

54. 434 S.W.3d 132 (Tex. 2014).

55. See, e.g., *Bren-Tex. Tractor Co. v. Massey Ferguson, Inc.*, 97 S.W.3d 155, 159 n.8 (Tex. App.—Houston [14th Dist.] 2002, no pet.); *Bunting v. Fodor*, 586 S.W.2d 144, 145–46 (Tex. Civ. App.—Houston [1st Dist.] 1979, no writ); *Chaq Oil Co. v. Gardner Mach. Corp.*, 500 S.W.2d 877, 878 (Tex. Civ. App.—Houston [14th Dist.], no writ).



were replaced in 2000. In 2002, the yacht was sold by the then-current owner to the plaintiff who purchased the yacht with knowledge that the yacht and engines were used goods. In 2004, one of the engines failed and was repaired. A year later, the engine failed again and could not be repaired. The plaintiff sued the engine manufacturer for breach of the implied warranty of merchantability. The jury found in favor of the plaintiff, but the trial court granted the defendant's motion for judgment notwithstanding the verdict, relying on the then-existing rule dealing with implied warranties in the sale of used goods.<sup>56</sup> On appeal by the buyer, the court of appeals reasoned that while several appellate court cases had held that no warranties arise in the sale of used goods, the Texas Supreme Court had never ruled on this issue.<sup>57</sup> The court of appeals distinguished these cases on the ground that the plaintiff in *Man Engines* was not suing the immediate seller for a breach of an implied warranty that arose when the plaintiff purchased the yacht from his immediate seller, but instead, the suit was against the engine manufacturer for breach of an implied warranty that arose when the new engines were sold to a previous owner and installed in the yacht.<sup>58</sup> The judgment of the trial court was reversed.<sup>59</sup>

On further appeal by the engine manufacturer, the Texas Supreme Court affirmed the ruling of the court of appeals and held that a remote purchaser was entitled to the benefit of any implied warranty against defects that came into existence in the sale of new goods to the original purchaser.<sup>60</sup> The supreme court rather colorfully stated, "The defect doesn't rub off with use."<sup>61</sup> In reaching this decision, the supreme court disapproved the holding in *Chaq Oil Co. v. Gardner Machinery Corp.*,<sup>62</sup> but specifically noted that it was not addressing the issue of whether a seller of used goods would be liable for breach of an implied warranty when selling the goods to a subsequent buyer.<sup>63</sup> The supreme court tempered its decision by pointing out that the buyer has a duty of inspection, and an implied warranty would not exist for defects that would be revealed by a reasonable inspection.<sup>64</sup> In the case at bar, however, the buyer had made a reasonable inspection, and the defect was one not revealed by the inspection.<sup>65</sup> The supreme court also stated that the rights of a remote buyer would be no greater than those of the original purchaser, and if implied warranties had been effectively disclaimed in the original sale, the remote buyer would be bound by the disclaimer.<sup>66</sup> Be-

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56. *Man Engines & Components, Inc.*, 434 S.W.3d at 134–35.

57. *Shows v. Man Engines & Components, Inc.*, 364 S.W.3d 348, 352 & n.3 (Tex. App.—Houston [14th Dist.] 2012), *aff'd* by 434 S.W.3d 132 (Tex. 2014).

58. *Id.* at 353.

59. *Id.* at 355.

60. *Man Engines & Components, Inc.*, 434 S.W.3d at 138.

61. *Id.*

62. 500 S.W.2d 877 (Tex. App.—Houston [14th Dist.] 1973, no writ).

63. *Man Engines & Components, Inc.*, 434 S.W.3d at 138.

64. *Id.*

65. *Id.*

66. *Id.* at 140.

cause it had not been raised at trial, the supreme court did not reach the issue of whether an “as is” sale by the original purchaser to a remote buyer inured to the benefit of the manufacturer.<sup>67</sup>

In *Becker v. Continental Motors, Inc.*,<sup>68</sup> a buyer purchased an airplane engine from a manufacturer for installation in an aircraft owned by the buyer. The manufacturer provided a “New Engine Warranty” as part of the transaction that stated the manufacturer, at its option, would repair or replace the engine or its components for defects in material or workmanship for a period of thirty-six months. A separate twenty-four month warranty was provided for the engine cylinders. Both warranties limited the remedies to repair or replacement and disclaimed any incidental or consequential damages.<sup>69</sup>

Some seventeen months after the purchase, it became apparent that the engine had major problems, and the buyer contacted the manufacturer to discuss repair. During the next few months, the manufacturer attempted to repair the engine, but these attempts failed. When it became apparent that the manufacturer would not attempt further repairs, the buyer sued for breach of express warranty under the Code and under the Texas Deceptive Trade Practices Act (TDTPA).<sup>70</sup> The U.S. District Court for the Northern District of Texas held that the manufacturer had breached its express warranty by failing to repair the engine and that the buyer was entitled to recover damages for the cost of replacing the engine.<sup>71</sup> In addition, the buyer was entitled to recover attorney’s fees under both § 38.001 of the Texas Civil Practice and Remedies Code and under the TDTPA.<sup>72</sup> The buyer also sought recovery for damages resulting from loss of use of the aircraft during the time it was out of service. The district court, however, denied recovery for these damages on the ground that the terms of the warranty effectively limited the buyer’s remedies and excluded recovery of incidental or consequential damages.<sup>73</sup>

While *Becker* involved the application of a limitation of remedies provision, *Luig v. North Bay Enterprises, Inc.*<sup>74</sup> concerned the interpretation of a contract that included both an express warranty and a disclaimer of

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67. *Id.* at 141.

68. No. 4:13-CV-520-BJ, 2015 WL 6742104 (N.D. Tex. Nov. 2, 2015).

69. *Id.* at \*1–2.

70. *Id.* at \*5. The TDTPA appears as Chapter 17 in the Code. See TEX. BUS. & COM. CODE ANN. §§ 17.4–.63 (West 2015). Section 17.50(a)(2) of the TDTPA provides, *inter alia*, that “[a] consumer may maintain an action . . . [for] breach of an express or implied warranty.” *Id.* § 17.50(a)(2).

71. *Becker*, 2015 WL 6742104, at \*8.

72. *Id.* at \*13. The recovery of attorney’s fees in actions for breach of contract is permitted under § 38.001 of the Code and the TDTPA. TEX. CIV. PRAC. & REM. CODE ANN. § 38.001; *id.* § 17.50(d). In *Medical City Dallas, Ltd. v. Carlisle Corp.*, the Texas Supreme Court held that breach of express warranty claims are founded in contract for the purpose of recovery of attorney’s fees. *Med. City Dall., Ltd. v. Carlisle Corp.*, 251 S.W.3d 55, 63 (Tex. 2008).

73. *Becker*, 2015 WL 6742104, at \*10.

74. 55 F. Supp. 3d 942 (N.D. Tex. 2014), *rev’d in part, vacated in part*, 817 F.3d 901 (5th Cir. 2016).

warranties.<sup>75</sup> In this case, the buyer purchased a helicopter under a contract representing that it would be airworthy, but the contract also stated that the helicopter was sold “as is,” and the buyer had made pre-purchase inspections of the helicopter.<sup>76</sup> The U.S. District Court for the Northern District of Texas held that under § 2.316 of the Code, this language and the buyer’s inspection were effective to disclaim any implied warranties.<sup>77</sup>

The express warranty, however, presented a different problem because of the conflict between the terms creating an express warranty and the terms disclaiming warranties. On this issue, the district court reasoned that the contract should be construed as a whole to give effect to both terms as directed by § 2.316(a).<sup>78</sup> Using this approach, the district court concluded that the specific statement creating an express warranty survived the general language disclaiming warranties, thus indicating that the parties had intended the express warranty to not be disclaimed.<sup>79</sup> The seller’s motion for summary judgment was denied, and the buyer’s claim for declaratory judgment in its favor was upheld.<sup>80</sup>

Under § 2.607 of the Code, the failure of a buyer to notify the seller of a breach of warranty within a reasonable time after the breach was or should have been discovered bars the buyer from any remedy.<sup>81</sup> In *Barocio v. General Electric Co.*,<sup>82</sup> a fire destroyed a home. It was unclear whether the fire was caused by improper installation of the wiring for the heating system or by a defective blower fan in the heating unit. Although one of the homeowners had given notice to the manufacturer of the heating unit, no notice was given to the manufacturer of the blower fan until suit was filed against the fan manufacturer some two years and eight months after the fire.<sup>83</sup> The Amarillo Court of Appeals held that the

75. *Id.* at 950–93.

76. Section 2.316(c)(1) of the Code permits disclaimer of all implied warranties “by expressions like ‘as is’, ‘with all faults’ or other language which in common understanding calls the buyer’s attention to the exclusion of warranties and makes plain that there is no implied warranty. TEX. BUS. & COM. CODE ANN. § 2.316(c)(1) (West 2015). Section 2.316(c)(2) of the Code provides that there is no implied warranty regarding defects that should have been discovered by the buyer through examination. *Id.* § 2.316(c)(2).

77. *Luig*, 55 F. Supp. at 950.

78. TEX. BUS. & COM. CODE ANN. § 2.316(a) (providing “Words or conduct relevant to the creation of an express warranty and words or conduct tending to negate or limit warranty shall be construed wherever reasonable as consistent with each other; but subject to the provisions of this chapter on parol or extrinsic evidence (Section 2.202) negation or limitation is inoperative to the extent that such construction is unreasonable”).

79. *Luig*, 55 F. Supp. at 952–53.

80. *Id.* at 955.

81. TEX. BUS. & COM. CODE ANN. § 2.607(c)(1).

82. No. 07-12-00311-CV, 2014 WL 31255 (Tex. App.—Amarillo Jan. 3, 2014, no pet.) (mem. op.).

83. It should be noted that there is a conflict in Texas law about whether notice given to one of the sellers in a distribution chain is effective against sellers further up the chain. Compare *Vintage Homes, Inc. v. Coldiron*, 585 S.W.2d 886 (Tex. Civ. App.—El Paso, 1979, no writ), with *Wilcox v. Hillcrest Mem’l Park of Dall.*, 696 S.W.2d 423 (Tex. App.—Dallas, writ ref’d n.r.e.). In *Wilcox*, the Texas Supreme Court recognized the split, but declined to resolve it. *Wilcox*, 696 S.W.2d at 425. In *U.S. Tire-Tech, Inc. v. Boren*, the First Houston Court of Appeals reasoned that later decisions of the supreme court on the purpose of notices under the Code generally indicated that notice should be given directly to the party

homeowners' claim against the fan manufacturer failed on two grounds.<sup>84</sup> First, because of conflicting evidence on the cause of the fire, the homeowners had failed to show that the blower fan was the cause-in-fact of the fire.<sup>85</sup> Second, because of the failure to give notice to the fan manufacturer within a reasonable time, the action was barred by the terms of § 2.607.<sup>86</sup> The court of appeals affirmed the take-nothing summary judgment in favor of the defendants.<sup>87</sup>

In *Massey v. Novartis Pharmaceuticals Corp.*,<sup>88</sup> a plaintiff alleged harm due to a drug prescribed for her cancer treatment. The plaintiff filed suit shortly before she died, and the suit was continued by her husband as executor of her estate. The U.S. District Court for the Western District of Texas granted summary judgment on the strict liability and negligence claims for failure to overcome the presumption that the manufacturer's warnings about the drug were adequate.<sup>89</sup> In addition, no pre-suit notice was given to the manufacturer, and this barred any breach of warranty claims.<sup>90</sup> On this point, the district court rejected an argument that the manufacturer was aware of problems with the drug because of "adverse event" reports received from other claimants.<sup>91</sup> Citing *U.S. Tire-Tech, Inc. v. Boeran*,<sup>92</sup> the district court ruled that under the Texas interpretation of § 2.607, notice must be received from the specific plaintiff who is asserting the breach of warranty claim.<sup>93</sup>

#### D. REJECTION AND ACCEPTANCE

Chapter 2 of the Code provides a fairly stark dividing line to establish the rights of the parties to a contract of sale following the rejection or acceptance of goods. After a rightful rejection, the buyer has a right to recover damages for the seller's breach under § 2.711.<sup>94</sup> If goods have

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who might ultimately be liable for a breach of warranty, such as the remote manufacturers of component parts. *U.S. Tire-Tech, Inc. v. Boren*, 110 S.W.3d 194, 198–99 (Tex. App.—Houston [1st Dist.] 2003, pet. denied).

84. *Barocio*, 2014 WL 31255, at \*4–5.

85. *Id.* at \*4.

86. *Id.* at \*4–5.

87. *Id.* at \*5.

88. 46 F. Supp. 3d 688 (W.D. Tex. 2014).

89. *Id.* at 691–92.

90. *Id.* at 692.

91. *Id.*

92. 110 S.W.3d 194 (Tex. App.—Houston [1st Dist.] 2003, pet. denied).

93. *Massey*, 46 F. Supp. 3d at 692.

94. Section 2.711(a) of the Code provides:

- (a) Where the seller fails to make delivery or repudiates or the buyer rightfully rejects or justifiably revokes acceptance then with respect to any goods involved, and with respect to the whole if the breach goes to the whole contract (Section 2.612), the buyer may cancel and whether or not he has done so may in addition to recovering so much of the price as has been paid
- (1) "cover" and have damages under the next section as to all the goods affected whether or not they have been identified to the contract; or
  - (2) recover damages for non-delivery as provided in this chapter (Section 2.713).

TEX. BUS. & COM. CODE ANN. § 2.711(a) (West 2015).

been accepted, absent proper revocation or breach of warranty, the buyer is liable for the price under § 2.607.<sup>95</sup> *National Oilwell Varco, L.P. v. Flowsolve Corp.*,<sup>96</sup> and *Genender v. USA Store Fixtures, LLC*,<sup>97</sup> nicely illustrate application of these sections. In *National Oilwell*, a buyer purchased motors to power pumps in a water treatment plant.<sup>98</sup> After delivery and installation, the buyer discovered substantial oil leakage from the motors, and the seller's attempts to cure the problem proved to be fruitless. The buyer rejected the motors, purchased replacements from another source, and sued for breach of contract and fraud. The jury awarded damages to the buyer on both claims. The trial court rendered judgment in favor of the buyer on the breach of contract claim. On appeal by the seller, the First Houston Court of Appeals had no difficulty in concluding that the buyer properly rejected the goods and dismissed arguments by the seller that the rejection was in bad faith or based on grounds other than the oil leakage.<sup>99</sup> The court of appeals affirmed the judgment in favor of the buyer.<sup>100</sup>

In *Genender*, a buyer purchased shelving for use in her store and charged the purchase to a credit card.<sup>101</sup> After the shelving was delivered, the buyer had the credit card company charge-back the amount of the purchase to the seller, but the buyer retained the goods. The seller sued for breach of contract and attorney's fees. Referring to § 2.607, the Fourteenth Houston Court of Appeals held that the evidence was sufficient to support the jury's verdict in favor of the seller, and the buyer was required to pay at the contract rate for the accepted goods.<sup>102</sup> The seller also sought to recover attorney's fees. The court of appeals, however, held that the seller had failed to prove that it had made a proper presentment of its demand for attorney's fees as required by § 38.001 of the Civil Practices & Remedies Code.<sup>103</sup> On this issue, therefore, the court of appeals reversed the trial court's award of attorney's fees, but affirmed the judgment for damages in favor of the seller.<sup>104</sup>

#### E. DAMAGES FOR FAILURE TO DELIVER

Some cases never die.<sup>105</sup> In *Citgo Petroleum Corp. v. Odfjell*

95. *Id.* § 2.607(a) (providing "The buyer must pay at the contract rate for any goods accepted").

96. No. 01-13-00388-CV, 2015 WL 1967490 (Tex. App.—Houston [1st Dist.] Apr. 30, 2015, no pet.) (mem. op.).

97. 451 S.W.3d 916 (Tex. App.—Houston [14th Dist.] 2014, no pet.).

98. *Nat'l Oilwell*, 2015 WL 1967490, at \*1.

99. *Id.* at \*6–9.

100. *Id.* at \*9.

101. *Genender*, 451 S.W.3d at 919.

102. *Id.* at 923–24.

103. *Id.* at 928; see also TEX. CIV. PRAC. & REM. CODE ANN. § 38.001 (West 2015) (providing, in part, that "the claimant must present the claim [for attorney's fees] to the opposing party, or to a duly authorized agent of the opposing party").

104. *Genender*, 451 S.W.3d at 928.

105. As a teacher of Contract Law, students sometimes ask why some of the cases in the casebook are so old. *Citgo Petroleum* provides a good answer to that question.

*Seachem*,<sup>106</sup> a buyer purchased a large quantity of cyclohexane to be delivered by a designated vessel to Freeport, Texas, from Argentina between April 15th and April 20th of 2005. The vessel suffered an engine failure, and the goods were not delivered until June of 2005. Because of the delay in delivery, the buyer had to purchase cyclohexane elsewhere to fulfill its own commitments to downstream buyers. The buyer sued to recover damages in lost profits and costs associated with obtaining the chemical from another source.<sup>107</sup> The seller moved for summary judgment because the buyer failed to show the loss was in the contemplation of the parties at the time the contract was made. Quoting extensively from *Hadley v. Baxendale*,<sup>108</sup> the U.S. District Court for the Southern District of Texas held that the test of foreseeability announced in *Hadley* had been approved by the Texas Supreme Court, by the U.S. Court of Appeals for the Fifth Circuit, and had been incorporated into the Restatement (Second) of Contracts.<sup>109</sup> Applying this test, the district court held that the buyer had the burden of raising an issue of fact about the seller's awareness that the buyer intended to resell the cyclohexane and might lose profit or suffer other damages for a delay in delivery.<sup>110</sup> Because the buyer failed to carry this burden, the court of appeals granted the seller's motion for summary judgment.<sup>111</sup>

#### IV. NEGOTIABLE INSTRUMENTS

##### A. INTERPRETATION OF TERMS IN AN INSTRUMENT

Chapter 3 of the Code states some very formal requirements for negotiable instruments.<sup>112</sup> One of the most direct statements is contained in § 3.114, which states, *inter alia*, that if there are contradictory terms in an instrument, “words prevail over numbers.”<sup>113</sup> In *Charles R. Tips Family Trust v. PB Commercial*,<sup>114</sup> a note was issued in the numerical amount of \$1,700,000. Unfortunately for the lender, the amount stated in words was “ONE MILLION SEVEN THOUSAND DOLLARS AND NO/100 (\$1,700,000.00) DOLLARS.”<sup>115</sup> Applying the rule in § 3.114, the First Houston Court of Appeals held that words prevailed over numbers and

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106. No. H-07-2950, 2014 WL 7004049 (S.D. Tex. Dec. 10, 2014).

107. *Id.* at \*6–7.

108. (1854) 156 Eng. Rep. 145 (Exchequer Ct.).

109. *Citgo Petroleum*, 2014 WL 7004049, at \*6–7 (citing *Mead v. Johnson Grp., Inc.*, 615 S.W.2d 685 (Tex. 1981); *Hector Martinez & Co. v. S. Pac. Transp. Co.*, 606 F.2d 106 (5th Cir. 1979); RESTATEMENT (SECOND) OF CONTRACTS § 351 (Tent. Draft No. 14, 1979) (now RESTATEMENT (SECOND) OF CONTRACTS § 351 (1981))).

110. *Id.* at \*8.

111. *Id.*

112. See generally TEX. BUS. & COM. CODE ANN. § 3.104 (West 2015); *id.* §§ 3.105–.116 (further elucidating the requirements briefly listed in § 3.104).

113. See TEX. BUS. & COM. CODE ANN. § 3.114 (“If an instrument contains contradictory terms, typewritten terms prevail over printed terms, handwritten terms prevail over both, and words prevail over numbers.”). There are not very many one-sentence sections anywhere in the Code.

114. 459 S.W.3d 147 (Tex. App.—Houston [1st Dist.] 2015, no pet.).

115. *Id.* at 150.

the note was payable in the lower amount despite the large difference of some \$693,000 (six hundred ninety-three thousand dollars).<sup>116</sup> An expensive lesson which demonstrates the need for careful review of loan documents.

In *McAllen Hospitals, LP v. State Farm Mutual Insurance Co.*,<sup>117</sup> two people were injured in an auto accident and treated at a hospital. The hospital filed a lien to secure payment for the hospital's medical services. The tortfeasor's insurance company settled the claims with the victims and issued checks made jointly payable to the respective victims and to the hospital. The checks, however, were indorsed only by the individual victims and paid by the payor bank without the indorsement of the hospital. When the hospital discovered that the checks had been issued and paid, it sought recovery from the insurer. The Texas Supreme Court held that the insurer, as drawer of the checks, remained liable because the checks had not been indorsed by the holder and, therefore, were never paid.<sup>118</sup> The supreme court reasoned that under § 3-110(d) of the Code, all persons named as payees on jointly payable checks, taken together, are deemed to be the holder of the instrument and indorsement by all payees was required for proper payment.<sup>119</sup> In reaching this conclusion, the supreme court rejected a contrary holding reached in *Benchmark Bank v. State Farm Lloyds*.<sup>120</sup>

The result in *McAllen Hospitals* was later followed in *Viewpoint Bank v. Allied Property & Casualty Insurance Co.*,<sup>121</sup> a similar case where an insurance company made a check jointly payable to a mortgagor and a mortgagee, but only the mortgagor indorsed the check and received payment. Therefore, the Dallas Court of Appeals rendered judgment against the insurer in favor of the mortgagee.<sup>122</sup>

## B. LIABILITY OF MAKERS

Under § 3.412 of the Code, the maker of a note is obligated to pay according to its terms at the time it was issued.<sup>123</sup> Texas law is well settled

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116. *Id.* at 155.

117. 433 S.W.3d 535 (Tex. 2014).

118. *Id.* at 536–37.

119. *Id.* at 539–40. On this point, the supreme court quoted a portion of the comment to § 3-110, which states:

If an instrument is payable to X and Y, neither X nor Y acting alone is the person to whom the instrument is payable. Neither person, acting alone, can be the holder of the instrument. The instrument is 'payable to an identified person.' The 'identified person' is X and Y acting jointly. . . . Thus . . . X or Y, acting alone, cannot be the holder or the person entitled to enforce or negotiate the instrument because neither, acting alone, is the identified person stated in the instrument.

*Id.* at 539; see TEX. BUS. & COM. CODE ANN. § 3.110 cmt. 4 (West 2015).

120. 893 S.W.2d 649 (Tex. App.—Dallas 1994, no writ).

121. 439 S.W.3d 626 (Tex. App.—Dallas 2014, pet. denied).

122. *Id.* at 638.

123. TEX. BUS. & COM. CODE ANN. § 3.412 (further providing that a maker is obligated to pay an unissued instrument according to its terms when it first comes into the possession of a holder or, if an instrument is incomplete, according to its terms as completed in accor-

on the elements required for a plaintiff to recover the amount due on a note. These include proof that the plaintiff is the owner or holder of the note, the terms of the note, and the balance due and owing on the note.<sup>124</sup> In *Jim Maddox Properties, LLC v. WEM Equity Capital Investments, Ltd.*,<sup>125</sup> *Roth v. JPMorgan Chase Bank, N.A.*,<sup>126</sup> *Thu Binh Si Ho v. Saigon National Bank*,<sup>127</sup> and *Lujan v. Navistar Financial Corp.*,<sup>128</sup> the courts of appeals used almost identical language to state the requirements for recovery.<sup>129</sup> In three of the cases, the courts of appeals rejected defenses raised by the makers,<sup>130</sup> but in *Thu Binh Si Ho*, the Fourteenth Houston Court of Appeals held that the maker raised an issue about the plaintiff's ownership of the note and reversed the summary judgment that had been entered in favor of the plaintiff.<sup>131</sup> In *In re Brooks*,<sup>132</sup> the U.S. District Court for the Southern District of Texas also upheld a challenge to the ownership of a note on the ground that the lender failed to show that the note had been indorsed or assigned to the lender.<sup>133</sup> Challenges to ownership or the right to enforce a note were ruled ineffective in a number of other cases.<sup>134</sup>

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dance with the rules governing completion or alteration as provided in §§ 3.115 and 3.407 of the Code).

124. See TEX. BUS. & COM. CODE ANN. §§ 3.301, 3.305(b), 3.308, 3.309, 3.401, 3.412 (establishing the requirements for a plaintiff to recover the amount due on a note).

125. 446 S.W.3d 126 (Tex. App.—Houston [1st Dist.] 2014, no pet.).

126. 439 S.W.3d 508 (Tex. App.—El Paso 2014, no pet.).

127. 438 S.W.3d 871 (Tex. App.—Houston [14th Dist.] 2014, no pet.).

128. 433 S.W.3d 699 (Tex. App.—Houston [1st Dist.] 2014, no pet.).

129. *Jim Maddox Properties, LLC*, 446 S.W.3d at 128; *Roth*, 439 S.W.3d at 510; *Lujan*, 433 S.W.3d at 701.

130. *Jim Maddox Properties, LLC*, 446 S.W.3d at 132; *Roth*, 439 S.W.3d at 512; *Lujan*, 433 S.W.3d at 705.

131. *Thu Binh Si Ho*, 438 S.W.3d at 873–74 (further holding that attaching a photocopy of the note within alleging and providing testimony of ownership was insufficient to prove a right to recover). In *Jim Maddox*, the First Houston Court of Appeals rejected claims that the plaintiff failed to show breach or waiver of the plaintiff's right to recover. *Jim Maddox Properties, LLC*, 446 S.W.3d at 133–35. In *Roth*, the El Paso Court of Appeals held that the maker had waived a claim for offset by failing to plead an affirmative defense of payment at the trial level. *Roth*, 439 S.W.3d at 513–14. In *Lujan*, the First Houston Court of Appeals held that the maker failed to prove any element of a claim that the loan agreement had been signed under duress. *Lujan*, 433 S.W.3d at 708.

132. No. 09–38232, 2014 WL 4796937 (S.D. Tex. Sept. 25, 2014).

133. *Id.* at \*7.

134. See, e.g., *Skelton v. Urban Trust Bank*, 516 B.R. 396, 405 (N.D. Tex. 2014) (transfer by holder without indorsement gave non-holder right to enforce note); *Blizzard v. Select Portfolio Serv.*, No. 03–13–00716–CV, 2015 WL 5096710, at \*3 (Tex. App.—Austin Aug. 27, 2015, no pet.) (mem. op.) (blank indorsement effective to transfer note to holder); *Passeur v. Wells Fargo Bank, N.A.*, No. 03–14–00376–CV, 2015 WL 5096534, at \*3 (Tex. App.—Austin Aug. 25, 2015, pet. filed) (mem. op.) (transfer of note to holder allowed holder to enforce note); *Deubler v. Bank of New York Mellon*, No. 07–13–00221–CV, 2015 WL 3750312, at \*4 (Tex. App.—Amarillo June 15, 2015, pet. denied) (mem. op.) (documents showing assignment effective to transfer ownership of note); *DeWeese v. Ocwen Loan Servicing, L.L.C.*, No. 01–13–00861–CV, 2014 WL 6998063, at \*4 (Tex. App.—Houston [1st Dist.] Dec. 11, 2014, no pet.) (mem. op.) (transfer by indorsement gave holder right to enforce note); *Das v. Deutsche Bank*, No. 05–12–01612–CV, 2014 WL 1022385, at \*3 (Tex. App.—Dallas Mar. 5, 2014, pet. denied) (mem. op.) (note was properly transferred to holder by blank indorsement).



## C. LIABILITY OF DRAWERS

Under § 3.414 of the Code, the drawer of a check is obligated to pay the holder if a check is dishonored by the drawer's bank.<sup>135</sup> In *1/2 Price Checks Cashed v. United Automobile Insurance Co.*,<sup>136</sup> the Texas Supreme Court held that actions against a drawer were actions in contract allowing recovery of attorney's fees.<sup>137</sup> In *Statewide Hydraulics, Inc. v. EZ Management GP, LLC*,<sup>138</sup> the Fourteenth Houston Court of Appeals addressed both the liability of a drawer for issuing dishonored checks and the evidence needed for recovery of attorney's fees.<sup>139</sup> In *Statewide Hydraulics*, a check cashing store routinely processed checks for a drawer. The parties had an arrangement for the drawer to repay any checks that were dishonored by the drawer's bank. In May of 2010, the store hired an auditor to review its records. The auditor discovered two checks that the drawer had not repaid. After the store demanded payment, the drawer provided two payments against the outstanding balance, but even after those payments, the drawer still owed a balance of \$19,695.03. The drawer allegedly made a third payment against the balance, but the check cashing store had no record of that payment. The check cashing store sued the drawer. The trial court awarded damages to the check cashing store for the unpaid amount and also awarded attorney's fees to the store for both trial and appeal. On appeal by the drawer, the court of appeals upheld the damage recovery, but denied recovery of attorney's fees for the appeal because such fees had not been requested by counsel for the check cashing store and there was no evidence in the record to show the reasonableness or necessity of the fees.<sup>140</sup> The court of appeals reversed the trial court's judgment awarding attorney's fees for appeal and affirmed the remainder of the judgment.<sup>141</sup>

It is elementary commercial law that to become a holder in due course, the holder must take an instrument for value, in good faith, and without notice of any claims or defenses to the instrument.<sup>142</sup> In *RR Maloan Investments, Inc. v. New HGE, Inc.*,<sup>143</sup> the Fourteenth Houston Court of Appeals addressed the issue of whether a holder can act in good faith

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135. TEX. BUS. & COM. CODE ANN. § 3.414(b) (West 2015) (providing "If an unaccepted draft is dishonored, the drawer is obliged to pay the draft (i) according to its terms at the time it was issued or, if not issued, at the time it first came into possession of a holder, or (ii) if the drawer signed an incomplete instrument, according to its terms when completed, to the extent stated in Sections 3.115 and 3.407. The obligation is owed to a person entitled to enforce the draft or to an indorser who paid the draft under Section 3.415.").

136. 344 S.W.3d 378 (Tex. 2011).

137. *Id.* at 388.

138. No. 14-13-01049-CV, 2015 WL 167160 (Tex. App.—Houston [14th Dist.] Jan. 13, 2015, no pet.) (mem. op.).

139. *Id.* at \*5–9.

140. *Id.* at \*9–10.

141. *Id.* at \*10.

142. See TEX. BUS. & COM. CODE ANN. § 3.302 (West 2015).

143. 428 S.W.3d 355 (Tex. App.—Houston [14th Dist.] 2014, no pet.).

when the holder takes a post-dated check.<sup>144</sup> The majority held that post-dating, in and of itself, will not prevent a holder from becoming a holder in due course.<sup>145</sup> In reaching this conclusion, the majority relied on cases decided under the pre-1990 version of the Code and the former text of § 3-304(d)(1), which provided, “Knowledge of the following facts does not of itself give the purchaser notice of a defense or claim . . . that the instrument is antedated or postdated.”<sup>146</sup> In the view of the majority, omission of this provision in the current version of the Code did not change the law.<sup>147</sup> The dissent, however, argued that the definition of good faith as it now appears in § 1-201(b)(20) of the Code requires both “honesty in fact [a subjective element] and observance of reasonable commercial standards of fair dealing [an objective element].”<sup>148</sup> In the view of the dissent, post-dating requires a holder to inquire about the validity of an instrument to satisfy the objective element of good faith.<sup>149</sup> Because no inquiry had been made, the dissent reasoned that the holder failed take the instrument in good faith.<sup>150</sup> Because of its ruling that the holder became a holder in due course despite the post-dating, the drawer’s defenses were not effective to prevent recovery by the holder.<sup>151</sup>

Under both the common law and the Code, a check can be used as the basis for an accord and satisfaction of a disputed debt to discharge a drawer from further liability on the debt.<sup>152</sup> In *Baeza v. Hector’s Tire & Wrecker Service, Inc.*,<sup>153</sup> the El Paso Court of Appeals addressed both the common law and statutory requirements needed to prove that an accord and satisfaction had been reached between the parties. The court of appeals pointed out that under either theory, the drawer was required to

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144. *Id.* at 360–61.

145. *Id.* at 363–64.

146. Act of Sept. 1, 1967, 60th Leg., ch. 785, § 3.304(d), 1967 Tex. Gen. Laws 2343, amended by Act of Jan. 1, 1996, 74th Leg., ch. 921, § 1, 1996 Tex. Gen. Laws 3823, 4592.

147. *RR Maloan Investments, Inc.*, 428 S.W.3d at 361–62.

148. *Id.* at 364–66 (Christopher, J. dissenting) (quoting TEX. BUS. & COM. CODE ANN. § 1.201(b)(20) West 2009)).

149. *Id.* at 366.

150. *Id.* at 364. The dissent succinctly explained its reasoning by stating, “With the change in the good-faith definition, no longer may the holder of an instrument act with a ‘pure heart and an empty head and still obtain holder in due course status’” *Id.* at 366 (citing *Any Kind Checks Cashd, Inc. v. Talcott*, 830 So.2d 160, 165 (Fla. Dist. Ct. App. 2002) (quoting *Maine Family Fed. Credit Union v. Sun Life Assurance Co. of Can.* 727 A.2d 335 (Me. 1999))).

151. *RR Maloan* is a good example of the uncertain effect the revised definition of good faith can have on a transaction. This uncertainty is not limited to checks, but has also played a part in the context of secured transactions and wire transfers. *See, e.g., In re Jersey Tractor Trailer Training, Inc.*, 580 F.3d 147 (3rd Cir. 2009) (addressing whether the factoring company that purchased accounts acted in good faith where secured party had perfected a security interest in accounts by filing a UCC-1); *Experi-metal, Inc. v. Comerica, Inc.*, No. 09-14890, 2010 WL 2720914 (E.D. Mich. July 8, 2010) (addressing whether the bank acted in good faith when it failed to stop fraudulent wire transfers after receiving notice of suspicious activity).

152. *See Lopez v. Munoz, Hockema & Reed, L.L.P.*, 22 S.W.3d 857, 863 (Tex. 2000) (accord and satisfaction is a contract by which the parties agree to settle a disputed debt); *see also* TEX. BUS. & COM. CODE ANN. § 3.311 (West 2015).

153. 471 S.W.3d 585 (Tex. App.—El Paso 2015, no pet.).

clearly communicate that a check was being tendered in full satisfaction of a disputed debt.<sup>154</sup> In this case, there was no evidence in the record showing that two checks sent to the payee were intended to be in full payment of the debt.<sup>155</sup> The court of appeals, therefore, held that the drawer's attempt to prove discharge by accord and satisfaction failed both at common law and under the Code.<sup>156</sup>

In *Leach v. Wilbur-Ellis Co.*,<sup>157</sup> the maker of a note sent a check to a creditor that was conspicuously marked as being in full payment of the debt. The creditor cashed the check but later demanded payment of the outstanding balance. The drawer of the check (maker of the note) filed a declaratory judgment action asserting that an accord and satisfaction discharged him from further liability. The terms of the note, however, expressly stated that any check sent in full payment of the debt was to be sent to an office specified in the note and that checks sent directly to the lender would not be effective as an accord and satisfaction.<sup>158</sup> Because the check was not sent to the designated office, the Amarillo Court of Appeals held that the accord and satisfaction failed.<sup>159</sup>

#### D. LIABILITY OF GUARANTORS

Guaranty agreements are very common in loan transactions. Such agreements can take two principal forms: (1) The guaranty can be part of the note itself; or (2) it may be contained in a separate agreement of guaranty. If it is part of the note, § 3.605 of the Code contains an elaborate set of provisions dealing with discharge of “secondary obligors,” the terminology used by the Code to include guarantors as well as other secondary parties such as indorsers.<sup>160</sup> If the guaranty is in a separate agree-

154. *Baeza*, 471 S.W.3d at 393–95.

155. *Id.* at 592–95.

156. *Id.* The court of appeals did point out that under the Code, there is a slight difference from the common law approach: The Code requires an instrument on which a claim of accord and satisfaction is based must be sent in good faith. *Id.* at 593–94. Although the trial court may have erred in excluding evidence of good faith intent on the part of the drawer, this was harmless error because of the failure to clearly notify the claimant that the checks were intended to be in full satisfaction of the debt. *Id.* at 594.

157. No. 07–14–00022–CV, 2014 WL 4553204 (Tex. App.—Amarillo Sept. 15, 2014, no pet.) (mem. op.).

158. Section 3.311(c)(1) of the Code provides:

Subject to Subsection (d), a claim is not discharged under Subsection (b) if either of the following applies:

(1) The claimant, if an organization, proves that:

(A) within a reasonable time before the tender, the claimant sent a conspicuous statement to the person against whom the claim is asserted that communications concerning disputed debts, including an instrument tendered as full satisfaction of a debt, are to be sent to a designated person, office, or place; and

(B) the instrument or accompanying communication was not received by that designated person, office, or place.

TEX. BUS. & COM. CODE ANN. § 3.311(c)(1) (West 2015).

159. See *Leach*, 2014 WL 4553204, at \*3.

160. See TEX. BUS. & COM. CODE ANN. § 3.605. Indorsers, like guarantors, are included because, by indorsing, they also agree to pay the holder of a dishonored instrument following, among others, presentment and notice of dishonor. See *id.* § 3.605 cmt. 3.

ment, the law of suretyship will apply.<sup>161</sup> In general, there is considerable overlap between § 3.605 and the law of suretyship. Under both the Code and the law of suretyship, a guarantor can waive defenses that would otherwise be available to the guarantor.<sup>162</sup>

In *Moayedi v. Interstate 35/Chisam Road, L.P.*,<sup>163</sup> the Texas Supreme Court announced a very important rule governing waivers in guaranty agreements. In that case, the supreme court held that a general waiver of defenses was effective to waive ordinary common law defenses as well as a statutory defense of offset based on § 51.003 of the Texas Property Code.<sup>164</sup> In reaching this conclusion, the supreme court and the court of appeals both emphasized that the terms of the waiver included a waiver of “any,” “each,” and “every” defense.<sup>165</sup> In *Holmes v. Graham Mortgage Corp.*,<sup>166</sup> and in *Hometown 2006-1 1925 Valley View, LLC v. Prime Income Asset Management, LLC*,<sup>167</sup> the courts referred to *Moayedi* and

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161. *Id.* § 3.605 cmt. 1 (“[The rules of this section] essentially parallel modern interpretations of the law of suretyship and guaranty that apply when a secondary obligor is not a party to an instrument. See generally Restatement of the Law, Third, Suretyship and Guaranty (1996). . . . In the event that a situation is presented that is not resolved by this section (or the other related sections of this Article), the resolution may be provided by the general law of suretyship because, pursuant to Section 1-103, that law is applicable unless displaced by provision of this Act.”).

162. *Id.* § 3.605(f) (“A secondary obligor is not discharged under this section if the secondary obligor consents to the event or conduct that is the basis of the discharge, or the instrument or a separate agreement of the party provides for waiver of discharge under this section specifically or by general language indicating that parties waive defenses based on suretyship or impairment of collateral. Unless the circumstances indicate otherwise, consent by the principal obligor to an act that would lead to a discharge under this section constitutes consent to that act by the secondary obligor if the secondary obligor controls the principal obligor or deals with the person entitled to enforce the instrument on behalf of the principal obligor.”); *see also* Restatement (Third) of Suretyship & Guaranty § 48 (1996) (stating a similar rule).

163. 438 S.W.3d 1 (Tex. 2014).

164. *Id.* at 8; *see* TEX. PROP. CODE ANN. § 51.003 (West 2015) (allowing a right of offset in certain circumstances where property is sold at foreclosure for an amount less than its fair market value). The waiver clause addressed by the supreme court stated the following:

7. Guarantor further agrees that this Guaranty shall not be discharged, impaired or affected by (a) the transfer by the Borrower of all or any portion of the real estate or improvements thereon, or of any security or collateral described in the Deed of Trust or in any other security document, or (b) any defense (other than the full payment of the indebtedness hereby guaranteed in accordance with the terms hereof) that the Guarantor may or might have as to Guarantor’s respective undertakings, liabilities and obligations hereunder, each and every such defense being hereby waived by the undersigned Guarantor.

*Moayedi*, 438 S.W.3d at 3. The guarantor argued that the clause should have specifically mentioned the waiver of rights under § 51.003. *Id.* at 3.

165. *Id.* at 8. The language used by the supreme court clearly emphasizes that general waivers are effective. Near the end of the opinion, the supreme court stated:

Just because a waiver is all encompassing does not mean that it is unclear or vague. To waive all possible defenses seems to very clearly indicate what defenses are included: all of them. Indeed, a waiver provision such as this one may be more descriptive to a layperson than a waiver referencing Property Code section numbers.

*Id.*

166. 449 S.W.3d 257 (Tex. App.—Dallas 2014, pet denied).

167. 595 F. App’x 306 (5th Cir. 2014).

reached the same result where the guarantors attempted to raise a defense of offset in the face of a general waiver of defenses clause.<sup>168</sup>

In *Berry v. Encore Bank*,<sup>169</sup> three guarantors signed a guaranty to enable a borrower to purchase a yacht. The guaranty in this case did not include a general waiver of defenses, but instead provided that the guarantors were liable as primary obligors and that no demand for payment need be made on the borrower before the lender asserted a claim against the guarantors.<sup>170</sup> The guaranty also specifically provided that the lender would not be liable to the guarantors for failure to secure the collateral (the yacht). As matters developed, when the loan and guaranty transactions occurred, a shipyard was repairing the yacht and held a first priority maritime lien on the vessel. When the borrower defaulted, the guarantors raised a defense of impairment of collateral due to the lender's failure to obtain priority over the maritime lien. Based on the specific language of the guaranty agreement, the First Houston Court of Appeals rejected this defense.<sup>171</sup> The guarantors also defended on the ground that limitations had run against the borrower. The court of appeals rejected this argument because the guaranty did not require the lender to first proceed against the borrower.<sup>172</sup> Judgment was affirmed in favor of the lender.<sup>173</sup>

## V. BANK DEPOSITS AND COLLECTIONS

### A. DEPOSIT OR PAYMENT OF ITEMS BEARING FORGED INDORSEMENTS

In *Coastal Agricultural Supply, Inc. v. JP Morgan Chase Bank*,<sup>174</sup> a bookkeeper opened a bank account in a name substantially similar to that of the company at which he was employed. During the next few years, he wrongfully deposited more than nine hundred checks made payable to the company into this account.<sup>175</sup> When his defalcation was discovered, the company settled its suit against the bookkeeper and sued the bank where the fraudulent account had been established on claims of conversion, negligence, and for money had and received. The bank asserted an affirmative defense to these claims under § 3.405 of the Code and obtained summary judgment in its favor on all but eighty-two of the

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168. *Holmes*, 449 S.W.3d at 265–66; *Prime Income Asset Mgmt., LLC*, 595 Fed. Appx. at 309–12.

169. No. 01-14-00246-CV, 2015 WL 3485970 (Tex. App.—Houston [1st Dist.] June 2, 2015, pet. denied) (mem. op.).

170. *Id.* at \*2.

171. *Id.* at \*8.

172. *Id.* at \*5; see also *Bank of Am., N.A. v. Alta Logistics, Inc.*, No. 05–13–01633–CV, 2015 WL 505373, at \*3 (Tex. App.—Dallas Feb. 6, 2015, no pet.) (mem. op.) (the guarantor was successful in raising a limitations defense because suit was not brought within the four year limitations period applicable to the guaranty).

173. *Berry*, 2015 WL 3485970, at \*14.

174. 759 F.3d 498 (5th Cir. 2014).

175. *Id.* at 502.

checks.<sup>176</sup> The bank also sought a reduction in its liability due to the settlement reached between the employer and the bookkeeper.<sup>177</sup> The employer argued that the § 3.405 defense did not apply to its common law claim for money had and received on the eighty-two disputed checks and that any settlement credit should be applied to the entire amount of the settlement and not limited to the amount of the bank's liability. The trial court granted partial summary judgment in favor of the bank on both issues. A limited interlocutory appeal was granted to the employer on both of these issues.

The U.S. Court of Appeals for the Fifth Circuit affirmed the district court on both issues.<sup>178</sup> The Fifth Circuit reasoned that the Code did not displace the common law action for money had and received, but that it did modify the common law by creating an affirmative defense under § 3.405.<sup>179</sup> The Fifth Circuit held that any conflict between the common law and the Code could be harmonized by allowing the employer to assert the common law claim, but also allowing the bank to assert the affirmative defense provided in § 3.405.<sup>180</sup> On the issue of proper allocation of the settlement credit, the Fifth Circuit held that under the "one-satisfaction rule," the credit should be applied only to the amount of the bank's liability and not to the entire amount of the employer's settlement with the bookkeeper because that amount included a sum for punitive damages for which the bank would not be liable.<sup>181</sup> Because the interlocutory appeal was limited to two specific issues, the Fifth Circuit did not address the issue of whether attorney's fees could be recovered on a

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176. See TEX. BUS. & COM. CODE ANN. § 3.405(b) (West 2015) (providing, in part, "For the purpose of determining the rights and liabilities of a person who, in good faith, pays an instrument or takes it for value or for collection, if an employer entrusted an employee with responsibility with respect to the instrument and the employee or a person acting in concert with the employee makes a fraudulent indorsement of the instrument, the indorsement is effective as the indorsement of the person to whom the instrument is payable if it is made in the name of that person. If the person paying the instrument or taking it for value or for collection fails to exercise ordinary care in paying or taking the instrument and that failure contributes to loss resulting from the fraud, the person bearing the loss may recover from the person failing to exercise ordinary care to the extent the failure to exercise ordinary care contributed to the loss").

177. The district court adopted the determination of the magistrate judge that the bank was protected by § 3.405(b) of the Code as to the checks that had been deposited in person at the bank. *Coastal Agric. Supply, Inc.*, 759 F.3d at 503–04. The eighty-two checks in dispute had been deposited at ATM machines. *Id.*

178. *Coastal Agric. Supply, Inc.*, 759 F.3d at 502.

179. *Id.* at 505–06.

180. *Id.* at 507–08. In reaching this conclusion, the U.S. Court of Appeals for the Fifth Circuit referred to its own prior decision in *Peerless Insurance Co. v. Tex. Commerce Bank–New Braunfels*, and to a decision of the Texas Supreme Court in *Bryan v. Citizens National Bank in Abilene*, both of which resolved conflicts between the Code and the common law by allowing the provisions of the Code to modify, but not displace, the common law. *Id.*; see *Peerless Ins. Co. v. Tex. Commerce Bank–New Braunfels, N.A.*, 791 F.2d 1177, 1180 (5th Cir. 1986) ("any inconsistencies between the various elements of the common law action and the particular provisions of the code be resolved in the Code's favor."); *Bryan v. Citizens Nat'l Bank in Abilene*, 628 S.W.2d 761, 764 (Tex. 1982).

181. *Coastal Agric. Supply, Inc.*, 759 F.3d at 512 (reasoning that the application of the one-satisfaction rule in *Crown Life Insurance Company v. Casteel* was squarely in point on the allocation of settlement credits among joint tortfeasors).

claim for money had and received.<sup>182</sup>

In *Contractors Source, Inc. v. Amegy Bank N.A.*,<sup>183</sup> a company hired a bookkeeper in July of 2007. In January of 2008, the bookkeeper began stealing funds from the company by submitting the company's checking account number and routing information to third-party websites with instructions to withdraw funds from the company's checking account for the bookkeeper's personal use. In September of 2010, the bookkeeper forged two checks on the company's account and obtained payment from the payor bank. The company discovered the forged checks when it reviewed the September 2010 statement and notified the bank. The bank reccredited the company's account for one of the checks, but refused to recredit the company for the amount of the other check or for any of the funds paid from the account through third-party websites.<sup>184</sup> In an action by the company against the bank, the bank asserted the "same wrongdoer" rule contained in § 4.406 of the Code as a defense.<sup>185</sup> The First Houston Court of Appeals held that § 4.406 applies not only to checks, but also to "items."<sup>186</sup> Noting that the term, item, was to be broadly construed under the decision in *American Airlines Employees Federal Credit Union v. Martin*,<sup>187</sup> the court of appeals held that the non-check draw requests made through third-party websites were akin to "remotely created items" defined in § 3.103(a)(16).<sup>188</sup> Based on this reasoning, the court of appeals held that because the bank had provided the company with monthly statements for more than two years showing payments from the company account, the company had failed to notify the bank of unauthorized payments within the thirty-day "same wrongdoer rule" as required by § 4.406(d).<sup>189</sup> The court of appeals also rejected a claim that the bank had failed to act in good faith or with a lack of ordinary care.<sup>190</sup>

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182. *Id.* at 508.

183. 462 S.W.3d 128 (Tex. App.—Houston [1st Dist.] 2015, no pet.).

184. *Id.* at 137.

185. *Id.* at 133.

186. *Id.* at 135. Section 4.406(d) of the Code provides:

If the bank proves that the customer failed, with respect to an item, to comply with the duties imposed on the customer by Subsection (c), the customer is precluded from asserting against the bank:

- (1) the customer's unauthorized signature or any alteration on the item, if the bank also proves that it suffered a loss by reason of the failure; and
- (2) the customer's unauthorized signature or alteration by the same wrongdoer on any other item paid in good faith by the bank if the payment was made before the bank received notice from the customer of the unauthorized signature or alteration and after the customer had been afforded a reasonable period of time, not exceeding 30 days, in which to examine the item or statement of account and notify the bank.

TEX. BUS. & COM. CODE ANN. § 4.406(d) (West 2015).

187. 29 S.W.3d 86 (Tex. 2000).

188. *Contractor's Source*, 462 S.W.3d at 134–35; see TEX. BUS. & COM. CODE ANN. § 3.103(a)(16) ("Remotely-created item' means an item that is created by a third party, other than the payor bank, under the purported authority of the drawer of the item for the purpose of charging the drawer's account with a bank and that does not bear a handwritten signature purporting to be the signature of the drawer.").

189. *Contractor's Source*, 462 S.W.3d at 134–35.

190. *Id.* at 135–37.

Summary judgment in favor of the bank was affirmed.<sup>191</sup>

In *Compass Bank v. Nacim*,<sup>192</sup> the El Paso Court of Appeals also gave a broad reading to the term, item, and held that debit memos used by a dishonest bank employee in 2007 and 2008 to withdraw funds from a customers' account for his personal use were items for purposes of § 4.406.<sup>193</sup> Although the customers' claims for withdrawals made in 2007 were barred by limitations, the court of appeals held that the claims for withdrawals made in July and August of 2008 were not barred by the same wrongdoer rule for two reasons.<sup>194</sup> First, the court of appeals ruled that the bank was not protected by the rule because it failed to show it suffered a loss due to the customers' delay in reporting the loss for some thirty-three days after the statement of account had been sent to the customers—three days beyond the thirty-day period provided in the deposit agreement.<sup>195</sup> On this point, the court of appeals reasoned that the bank had not suffered a loss due to the delay because it had discharged the dishonest employee before the thirty-day time period had run.<sup>196</sup> Consequently, the failure of the customers to notify the bank within the prescribed time period did not deprive the bank of an opportunity to pursue recovery from the wrongdoer because it already had the information necessary to pursue such a claim.<sup>197</sup>

The court of appeals also ruled that the deposit agreement was ambiguous about the date triggering the customers' duty to report.<sup>198</sup> The first sentence of the relevant provision stated, "You agree that you will carefully examine each account statement or notice you *receive* and report any exceptions to us promptly after you receive the statement or notice."<sup>199</sup> But the last sentence of the same provision stated, "[I]f you do not report exceptions to us within thirty (30) days after we *send* the statement or notice to you, we will not reimburse you for any loss you suffer . . . ."<sup>200</sup> The court of appeals reasoned that this ambiguity created a situation in which the thirty-day period could expire before an account statement was received by the customers.<sup>201</sup> This, in fact, is what happened in *Nacim* because the customers never received the relevant statement due to the bank's error in failing to change the address to which statements should be mailed. The court of appeals, therefore, upheld the trial court's ruling that actual receipt was required to trigger the duty to report.<sup>202</sup>

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191. *Id.* at 140.

192. 459 S.W.3d 95 (Tex. App.—El Paso 2015, no pet.).

193. *Id.* at 105.

194. *Id.* at 109.

195. *Id.* at 104–09.

196. *Id.* at 107.

197. *Id.*

198. *Id.* at 107–09.

199. *Id.* at 108 (emphasis added).

200. *Id.* (emphasis added).

201. *Id.*

202. *Id.* at 109.



## VI. SECURED TRANSACTIONS

## A. PERFECTION OF SECURITY INTERESTS

Although not decided under Texas law, *Official Committee of Unsecured Creditors of Motors Liquidation Co. v. JPMorgan Chase Bank, N.A. (In re Motors Liquidation Co.)*<sup>203</sup> is an important decision showing how a lack of attention to details can have disastrous results for a secured party. *In re Motors Liquidation Co.* arose out of the General Motors bankruptcy reorganization involving loans made to the bankruptcy debtor (old GM) that was restructured into a new corporation (new GM). The restructuring plan called for the payoff and the termination of perfection of a \$300 million finance lease made by a lending group to old GM in 2001.<sup>204</sup> In 2006, a different lending group made a \$1.5 billion secured loan to old GM. The same bank (lead bank) served as administrative agent for both lending groups and perfected both the finance lease and the secured loan by filing proper financing statements in Delaware.<sup>205</sup> An associate at the law firm charged with making the closing arrangements to pay off and terminate perfection of the lease transaction did a UCC filing search and located three financing statements, two of them covering the finance lease and one of them covering the secured loan.<sup>206</sup>

The associate prepared a closing list and draft documents, including UCC-3 termination statements for all of the loans. No one at the law firm, at the lead bank, at the law firm representing the lead bank, or at General Motors realized that the termination statements covered not only the \$300 million finance lease, but also the \$1.5 billion secured loan.<sup>207</sup> After the termination statements were filed, the Committee of Unsecured Creditors (Committee) filed an action in bankruptcy court seeking a determination that the filed termination statements rendered the \$1.5 billion dollar loan unperfected, thereby causing the lead bank and the lending group to lose priority and become unsecured creditors. The bankruptcy court held that although the termination statement covering the secured loan was filed by mistake, it was an unauthorized filing and did not cause a loss of perfection.<sup>208</sup> Because of the importance of the case, the bankruptcy court approved a direct appeal to the Second Circuit.

The Second Circuit determined that the issue of the effectiveness of a mistaken filing was one of state law and certified the question to the Delaware Supreme Court.<sup>209</sup> The supreme court answered that a filing made intentionally, although with a mistaken understanding about its legal ef-

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203. 777 F.3d 100 (2d Cir. 2015).

204. *Id.* at 101.

205. *Id.*

206. *Id.* at 102.

207. *Id.*

208. *In re Motors Liquidation Co.*, 486 B.R. 596, 647–48 (Bankr. S.D.N.Y. 2013), *rev'd*, 777 F.3d 100 (2d Cir. 2015).

209. *In re Motors Liquidation Co.*, 755 F.3d 78, 84 (2d Cir. 2014).

fect, was an authorized filing that would terminate perfection.<sup>210</sup> After receiving an answer to the certified question, the Second Circuit held that the lead bank knew that the termination statements accompanying the documents in the closing list were going to be filed, and after reviewing those documents, it authorized the filing.<sup>211</sup> It made no difference if the lead bank did not intend to terminate perfection of the secured loan and mistakenly granted authorization for the filing.<sup>212</sup> The case was remanded to the bankruptcy court with instructions to grant partial summary judgment in favor of the Committee.<sup>213</sup> The net result was the loss of perfection for a \$1.5 billion loan.

## B. PRIORITIES

In *Inwood National Bank v. Wells Fargo Bank*,<sup>214</sup> the Dallas Court of Appeals dealt with the relative priorities of a garnishing creditor and a bank that had a perfected security interest in funds held in a deposit account.<sup>215</sup> The court of appeals recognized that under § 9.317 of the Code, a perfected security interest generally primes the claim of the garnishing creditor.<sup>216</sup> In this case, however, the court of appeals had to address the priority of the bank and the lien creditor in regard to future advances under § 9.323 of the Code. This issue arose because the bank had the debtor sign a renewal note more than 45 days after the garnishment was served on the bank. The trial court reasoned that this was a future advance that was not made pursuant to commitment, and therefore, was not protected under the terms of § 9.323.<sup>217</sup>

On appeal by the garnishing creditor, the court of appeals disagreed.<sup>218</sup> Instead, the court held that a note given in renewal and extension of an earlier loan was not a future advance, but simply a continuation of a debt that pre-dated the garnishing creditor's lien on the account.<sup>219</sup> The court of appeals reasoned that the renewal note was not a novation and did not provide new credit to the debtor that would disadvantage the lien creditor by increasing the amount of the bank's secured claim.<sup>220</sup> The judgment of the trial court was reversed and judgment was rendered in favor

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210. *In re Motors Liquidation Co.*, 103 A.3d 1010, 1017–18 (Del. 2014).

211. *In re Motors Liquidation Co.*, 777 F.3d at 105.

212. *Id.*

213. *Id.* at 105–06.

214. 463 S.W.3d 228 (Tex. App.—Dallas 2015, no pet.).

215. *Id.* at 238.

216. *Id.* at 235; see TEX. BUS. & COM. CODE ANN. § 9.317(a)(2) (West 2015) (a lien creditor is subordinate to a security interest that is perfected before the lien arises).

217. Under § 9.323(b) of the Code, a lien creditor is subject to future advances made during a 45-day period after the lien arises, but is protected from future advances made after that time unless they are made pursuant to an earlier commitment. *Id.* § 9.323(b). Referring to this rule, the court of appeals noted, “The purpose of section 9.323(b) is to protect a judgment lien creditor who has successfully levied on a valuable equity subject to a security interest from being ‘squeezed out’ by a later enlargement of the security interest by an addition advance.” *Inwood Nat'l Bank*, 463 S.W.3d at 235.

218. *Id.* at 238–40.

219. *Id.* at 238.

220. *Id.*

of the secured party.<sup>221</sup>

### C. DISPOSITION OF COLLATERAL

If collateral has been successfully repossessed, a secured party may have the option of retaining the collateral in full or partial satisfaction of the debt or selling it at a public or private sale.<sup>222</sup> If the secured party decides to sell the collateral, Chapter 9 of the Code contains several sections dealing with the giving of notice and accounting for the proceeds of sale.<sup>223</sup> Under § 9.610, a sale must be conducted in a commercially reasonable manner.<sup>224</sup> In *Plains Capital Bank v. Jani*,<sup>225</sup> a secondary obligor challenged the commercial reasonableness of a secured party's disposition of accounts securing a loan. In commercial cases, when such a challenge is made, § 9.626(a)(2) of the Code requires the secured party to prove that the disposition was commercially reasonable.<sup>226</sup> If the secured party fails to carry this burden, the liability of the debtor or secondary obligor is limited to an amount calculated under the formula stated in § 9.626(a)(3).<sup>227</sup> The jury returned a verdict pursuant to instructions drafted in accordance with § 9.626, and the trial court offset the amount found by the jury against the damages claimed by the secured party, re-

221. *Id.* at 241–42.

222. *See* TEX. BUS. & COM. CODE ANN. § 9.620 (West 2015) (In commercial cases, the secured party always has the option of keeping collateral in full or partial satisfaction of a debt (strict foreclosure). In consumer cases, the option of keeping collateral in partial satisfaction is not available and, if more than sixty percent of the price has been paid, neither is keeping the collateral in full satisfaction and the collateral must be sold).

223. *See, e.g., id.* §§ 9.610–.616.

224. *Id.* § 9.610(b) (providing, in part, “Every aspect of a disposition of collateral, including the method, manner, time, place, and other terms, must be commercially reasonable.”)

225. No. 02-14-0149-CV, 2015 WL 7303934 (Tex. App.—Fort Worth Nov. 19, 2015, pet. denied).

226. Section 9.626(a)(2) of the Code provides:

(a) In an action arising from a transaction, other than a consumer transaction, in which the amount of a deficiency or surplus is in issue, the following rules apply:

...

(2) If the secured party's compliance is placed in issue, the secured party has the burden of establishing that the collection, enforcement, disposition, or acceptance was conducted in accordance with this subchapter.

TEX. BUS. & COM. CODE ANN. § 9.626(a)(2).

227. Section 9.626(a)(3) of the Code provides:

(3) Except as otherwise provided in Section 9-628, if a secured party fails to prove that the collection, enforcement, disposition, or acceptance was conducted in accordance with the provisions of this subchapter relating to collection, enforcement, disposition, or acceptance, the liability of a debtor or a secondary obligor for a deficiency is limited to an amount by which the sum of the secured obligation, expenses, and attorney's fees exceeds the greater of:

(A) the proceeds of the collection, enforcement, disposition, or acceptance;

or

(B) the amount of proceeds that would have been realized had the noncomplying secured party proceeded in accordance with the provisions of this subchapter relating to collection, enforcement, disposition, or acceptance.

*Id.* § 9.626(a)(3).

sulting in a net judgment of zero. The trial court entered a take-nothing judgment against both parties.<sup>228</sup> On appeal, the Fort Worth Court of Appeals found no error in the trial court's application of Chapter 9 and affirmed the judgment.<sup>229</sup>

## VII. CONCLUSION

As usual, Texas has contributed its share of cases to Code learning, a few of which have settled previously open questions. It is somewhat surprising that relatively few secured transaction cases were decided under Chapter 9 during the Survey period, but this may be because attorneys have adjusted to the changes made to Chapter 9 in 2001 and in 2013 that clarified many of the issues that led to problems under the former version.

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228. *Plains Capital Bank*, 2015 WL 7303934, at \*3.

229. *Id.* at \*4-5.

