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COMMERCIAL TRANSACTIONS

*John Kraemer**

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I. INTRODUCTION

THIS Survey concentrates on a discussion of recent cases interpreting the Uniform Commercial Code adopted in Texas as part of the Texas Business and Commerce Code.¹ In addition, during the Sur-

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1. The Texas version of the Uniform Commercial Code is contained in the first eleven chapters of the Texas Business and Commerce Code (the "Code"). See TEX. BUS. & COM. CODE ANN. §§ 1.101-11.108 (West 2009). These chapters are designated as follows:

- Chapter 1: General Provisions
- Chapter 2: Sales
- Chapter 2A: Leases
- Chapter 3: Negotiable Instruments
- Chapter 4: Bank Deposits and Collections

vey period, the American Law Institute and the National Conference of Commissioners on Uniform State Laws approved several amendments to the Official Text of article 9 dealing with secured transactions. These amendments have been introduced during the 2011 Texas legislative session and, if adopted, will be discussed in next year's Survey. Readers who would like additional information about these changes may wish to consult the sources in the accompanying footnote.²

II. GENERAL PROVISIONS

A. CONSPICUOUSNESS

Various provisions in the Code require certain terms to be "conspicuous."³ As defined in section 1.201, conspicuousness includes setting off headings or content in capital letters, larger font size, or contrasting color such that a reasonable person ought to notice it.⁴ Whether a term is "conspicuous" is determined as a matter of law by the court.⁵ In *Bergholtz v. Southwestern Bell Yellow Pages, Inc.*, an advertiser refused to pay for an ad in the yellow pages that allegedly contained various errors and sought recovery from the publisher for breach of contract, negligence, and violations of the Texas Deceptive Trade Practices Act.⁶ Citing *Dresser Industrials, Inc. v. Page Petroleum, Inc.*,⁷ the advertiser argued a clause in the publication contract limiting the publisher's liability to the amount paid for the ad was not conspicuous and therefore ineffective. In addressing this issue, the Texas Supreme Court pointed out that although

Chapter 4A: Funds Transfers
 Chapter 5: Letters of Credit
 Chapter 7: Documents of Title
 Chapter 8: Investment Securities
 Chapter 9: Secured Transactions
 Chapter 10: [Reserved for Expansion]
 Chapter 11: 1973 Transition Provisions

2. The Official Text of the proposed amendments is available for \$20.00 from the American Law Institute website, Am. Law Inst. & Nat'l Conference of Comm'rs on Unif. State Laws, *UCC Art. 9 2010 Amendments to the Original Comments*, Aug. 25, 2010, available at <http://extranet.ali.org/directory/files/2010AmendmentstoOfficialComments.pdf>. The amendments were introduced as companion bills HB 1617 and SB 782. Am. Bar Assoc., *UCC: Legislative Enactment of Revised Article 9*, <http://apps.americanbar.org/dch/committee.efm?com=CL10043> (last visited May 15, 2011). The progress of these bills can be tracked at <http://www.capitol.state.tx.us>. The amendments are discussed in detail in a four part series appearing in *82nd Legislative Regular Session*, TEXAS LEGISLATURE ONLINE, <http://www.capitol.state.tx.us> (last visited May 20, 2011).

3. See, e.g., TEX. BUS. & COM. CODE ANN. §§ 2.316(b), 2A.214(b), 3.104(d), 8.204(l) (West 2009).

4. See *id.* § 1.201(b)(10).

5. *Id.*

6. 324 S.W.3d 195, 197 (Tex. App.—El Paso 2010, no pet.). The deceptive trade practices claim was based on the Texas Deceptive Trade Practices Act (DTPA). TEX. BUS. & COM. CODE ANN. §§ 17.41–63 (West 2009). The opinion does not identify the particular sections on which the advertiser based the DTPA claims.

7. 853 S.W.2d 505 (Tex. 1993). In *Dresser*, the court interpreted the definition of "conspicuous" as it then appeared in TEX. BUS. & COM. CODE ANN. § 1.201(10) (West 1994). The definition was expanded and revised in what is now TEX. BUS. & COM. CODE ANN. § 1.201(b)(10) (West 2009).

Dresser broadly held that the Code definition of “conspicuous” applicable to non-Code contracts, this holding was subsequently limited to releases or exculpatory clauses that completely shifted the risk of loss caused by negligence, rather than clauses that merely shifted the risk of economic loss.⁸ Because the limitation of liability clause only affected the advertising cost, it was not necessary to determine whether the clause was conspicuous.⁹

Although most cases involving the conspicuousness of contract clauses deal with traditional printed forms, terms contained on websites are beginning to find their way into reported cases. For example, in *One Beacon Insurance Co. v. Crowley Marine Services, Inc.*,¹⁰ the owner of a fleet of vessels sent a printed Repair Service Order (RSO) to a marine repair company. The RSO contained a notice in capital letters with, *inter alia*, the URL for a website showing the terms and conditions governing the RSO, including a term that required vendors of repair services to provide defense and indemnity insurance covering any liability to the fleet owner for injuries suffered by employees during the course of repairs. When an employee was injured while making repairs to a barge, the fleet owner filed a claim against the repair service and its insurer. Coverage was denied and the fleet owner sued. The repair service and its insurer argued the requirement for defense and indemnity was not conspicuous because it did not appear in the RSO, and the website link was in a printed form and not a hyperlink that could be “mouse-clicked.”

The court held inclusion of the URL was sufficient to put the repair service on notice that the RSO was subject to the terms and conditions displayed on the website, particularly because the same parties dealt with each other on twenty-three prior occasions and the president of the repair service admitted knowing he could have gone to the fleet owner’s website to see the terms and conditions.¹¹ The court concluded a reasonable person would be able to access the website and find the insurance provisions governing the RSO.¹² In reaching this conclusion, the court noted the small font used on the website could be enlarged by the viewer to any

8. *Id.* In reaching this conclusion, the court noted that *Green Intern., Inc. v. Solis*, 951 S.W.2d 384, 387 (Tex. 1987) clarified the scope of the decision in *Dresser*.

9. *Id.* Interestingly enough, the portion of the contract reprinted in *Bergholtz* shows that the limitation of liability did appear in capital letters. The court applied the narrowest possible reading of *Dresser*, and this holding seems to conflict with some other decisions that have applied the conspicuousness requirement in cases that did not involve indemnity or release clauses. *See, e.g.*, *Hartford v. Lyndon-DFS Warranty Serv., Inc.*, No. 01-08-00398-CV, 2010 WL 2220443, at *12 (Tex. App.—Houston [1st Dist.] May 28, 2010 no pet.) (mem. op.) (not designated for publication) (disclaimer of warranty of good and workman-like repair was conspicuous but not enforceable under rule of *Melody Home Mfg. Co. v. Barnes*, 741 S.W.2d 349, 355 (Tex. 1987)); *Mickens v. Longhorn DFW Moving, Inc.*, 264 S.W.3d 875, 877, 879 (Tex. App.—Dallas 2008, pet. denied) (limitation of liability for loss or damage to goods was conspicuous); *Drug Test USA, L.L.C. v. Buyers Shopping Network*, 154 S.W.3d 191 (Tex. App.—Waco 2004, no pet.) (choice of law clause required by TEX. BUS. & COM. CODE § 35.53(b) (current version at § 273.002) had to be conspicuous).

10. No. H-08-2059, 2010 WL 1463451 (S.D. Tex., Apr. 12, 2010).

11. *Id.* at *5.

12. *Id.*

desired size font; furthermore, the Texas definition of “conspicuous” did not control because the case arose under maritime law, which does not invalidate contracts simply because they are contracts of adhesion that do not display particular terms in a conspicuous font or color.¹³

III. SALE OF GOODS

A. FORMATION OF CONTRACT

One purpose of chapter 2 is to eschew the formalism that often surrounds common law rules dealing with contract formation, and instead substitute a legal regime allowing courts to find an existing contract despite absence of a formal offer and acceptance.¹⁴ In *Bro-Tech Corporation v. Purity Water Company of San Antonio*,¹⁵ a water purification company ordered resin from a chemical manufacturer to use in a water filtration project. The resin, together with invoices, was shipped in three lots in response to purchase orders sent by the buyer. When the buyer refused to pay for the third shipment, the seller brought an action to recover the balance due. The buyer argued the seller failed to produce any documents showing the existence of a contract. The court easily determined that the shipments were sent in response to the purchase orders and that this was an effective mode of acceptance.¹⁶ The seller also sought recovery of interest based on a provision in its invoices that interest of one and a half percent would be charged on past due balances, contending this provision had become part of the contract under the “Battle of the Forms” rules in section 2.207 of the Code.¹⁷ On this point, the court recognized a term providing for interest would normally be per-

13. *Id.* at *12. On this point, the court referred to both Texas law under TEX. BUS. & COM. CODE § 1.201(b)(10) (West 2009) and to general maritime law as described in *Brown v. Pacific Life Insurance Co.*, 462 F.3d 384, 397 (5th Cir. 2006). While Texas law is concerned with conspicuousness, maritime law focuses on whether enforcement of an agreement is reasonable between the parties. In *One Beacon*, the court noted that both parties were sophisticated commercial entities who had dealt with each other on several occasions. Because the terms were readily available on the fleet owner’s website, maritime law did not require the terms to meet the Texas requirement of conspicuousness. For cases arising under Texas law, a website owner should comply with the Texas requirements; an easy task because of the ability to change fonts or colors with the appropriate coding. See TEX. BUS. & COM. CODE ANN. § 1.201(10) (West 2009). The need for such state law compliance is nicely illustrated by the decision in *Fieldtech Avionics & Instruments, Inc. v. Component Control.Com, Inc.*, where a disclaimer on a website failed the Texas requirement that warranty disclaimers be conspicuous. 262 S.W.3d 813 (Tex. App.—Ft. Worth 2008, no pet.).

14. The Code provides: “A contract for the sale of goods may be made in any manner sufficient to show agreement, including conduct by both parties which recognizes the existence of such a contract.” TEX. BUS. & COM. CODE ANN. § 2.204(a) (West 2009).

15. 681 F. Supp. 2d 791 (W.D. Tex. 2010).

16. *Id.* at 801. The court did, however, make a minor adjustment because of a discrepancy between the amount of 13,000 thousand pounds shown on one purchase order and the amount of 13,480 pounds shown on the related invoice. *Id.* at 802–03.

17. *Id.* at 802. Section 2.207 of the Code rejects the common law “mirror image” rule and allows a contract to be formed even though the documents exchanged between the parties contain varying terms so long as: (1) the offer does not expressly limit acceptance to the terms of the offer; (2) the varying terms do not materially alter the contract; or (3) no objection is made to the varying terms.

mitted under section 2.207, but only in contracts between merchants.¹⁸ Although it was clear the seller was a merchant, the seller failed to produce any evidence that the buyer was also a merchant, and the court deferred a ruling on this issue pending a pretrial conference on the matter.¹⁹

In *Parker Drilling Company v. Romfor Supply Company*,²⁰ a prospective buyer of oil field equipment was unsuccessful in showing the existence of a contract where an email from a purported seller so materially changed the buyer's order that the court could not deem it to be an acceptance.²¹ A statement in the email that the seller intended to sell the equipment to another buyer was particularly important in reaching the conclusion that the email constituted a rejection of the buyer's offer.²² A take nothing judgment was rendered against the plaintiff buyer.²³

In *Contractor's Source, Inc. v. Hanes Companies, Inc.*,²⁴ the court also addressed application of section 2.207 where the seller shipped the goods before sending an invoice that included a term limiting the recovery of consequential damages. The court held the act of shipping the goods constituted acceptance of the buyer's order and the subsequent mailing of the invoice came too late to make its damages limitation part of the contract.²⁵

In *J.D. Fields & Company, Inc. v. United States Steel International, Inc.*,²⁶ much of the dispute centered on whether a seller's emails amounted to a firm offer or merely a price quotation inviting the buyer to make an offer. In a carefully reasoned opinion, the court balanced the factors on both sides of the issue. Factors favoring the buyer included the detailed nature of the emails, the use of statements that "I can offer" and "[w]e can offer," and the absence of language indicating confirmation by the seller was required. Factors favoring the seller included a lack of shipping terms, delivery dates, the references to orders of any specific quantity, and the fact the goods were manufactured as specialty items and not goods provided out of inventory. Beyond the content of the emails, the court also considered industry custom and prior course of dealing between the parties.²⁷ Based on these considerations, the court concluded the emails did not create a firm offer but only a price quotation.²⁸ Having reached this conclusion, the court also addressed promissory estoppel and fraud claims asserted by the buyer. On both these issues the court held

18. *Bro-Tech*, 681 F. Supp. 2d at 803 (citing TEX. BUS. & COM. CODE ANN. § 2.207 cmt. 5).

19. *Id.*

20. 316 S.W.3d 71 (Tex. App.—Houston [14th Dist.] 2010, pet. denied).

21. *Id.* at 74–75.

22. *Id.*

23. *Id.* at 78.

24. No. 09-CV-0069, 2009 WL 6443116 (S.D. Tex. Dec. 29, 2010).

25. *Id.* at *9. The opinion also contains an extensive choice of law discussion in which the court concluded that Texas law should be applied because Texas had the most significant relationship to the transaction. *See id.* at *1–5.

26. 690 F. Supp. 2d 487 (S.D. Tex. 2009).

27. *Id.* at 500–02.

28. *Id.* at 502–03.

the buyer failed to show any specific statements by the seller amounting to a promise or representation upon which the buyer was entitled to rely.²⁹ In addition to the disputed issues about contract formation, the seller asserted a right to recover damages because of the buyer's failure to pay the balance due on a previous shipment made under an earlier admitted contract.³⁰ On this issue, the court determined that while the seller had a right to recover damages because of the buyer's breach on the earlier contract, the amount could not be determined without trial because of discrepancies in the documents evidencing the earlier contract.³¹

B. STATUTE OF FRAUDS

In addition to issues surrounding formation of a contract, the exchange of emails and invoices can also raise questions about the satisfying the Statute of Frauds. In *Barrington Group Limited, Inc. v. Classic Cruise Holdings S. De R.L.*,³² a manufacturer sought payment for six invoices allegedly sent to a purchaser for goods specially manufactured for the buyer. After goods were delivered pursuant to three purchase orders, the buyer sent an email cancelling further orders because the quality of the goods it received was below the quality the buyer desired. The seller viewed this email as a repudiation, but the buyer claimed it had no records showing the existence of any agreement to purchase the goods shown on the other three invoices and the seller was unable to produce any documents beyond these three invoices. Because the invoices were prepared by the seller, there was no writing signed by the buyer to satisfy the basic Statute of Frauds requirement in section 2.201 of the Code.³³ To avoid this statutory bar to enforcement, the seller pointed to three exceptions in section 2.201. First, because the buyer admitted receiving all six invoices (although no related purchase orders were found for three of them), the seller claimed the "merchant's exception" to the Statute of Frauds allowed enforcement despite absence of a signed writing. Under this exception, if a merchant receives a signed writing that purports to confirm existence of a contract and the buyer does not object to it within a reasonable time after receipt, the Statute of Frauds does not bar enforcement of the alleged contract.³⁴ Based on the timing of the invoices

29. *Id.* at 503–06.

30. The buyer had asserted a right to deduct damages on the disputed contract from the amount due on the earlier contracts. This self-help remedy is permitted by TEX. BUS. & COM. CODE ANN. § 2.717 (West 2002).

31. *J.D. Fields & Co., Inc.*, 690 F. Supp. 2d at 507–09.

32. No. 3:08-CV-1813-B, 2010 WL 184307 (N.D. Tex., Jan. 15, 2010).

33. The basic Statute of Frauds rule in TEX. BUS. & COM. CODE ANN. § 2.201(a) (West 2009) provides that a contract for the sale of goods with a price of \$500 or more is not enforceable unless there is a writing sufficient to show a contract was made and signed by the party against whom enforcement is sought.

34. *Id.* § 2.201(b). It is important to note that the merchant's exception only avoids the Statute of Frauds as a bar to enforcement. It does not prove the existence of a contract, but merely allows a party to go forward with the introduction of evidence to show a contract actually exists.

and the buyer's email canceling further orders, the court held the merchant's exception applied to two of the disputed invoices and the buyer's motion for summary judgment was denied on these invoices.³⁵ The seller also contended the statutory exception in section 2.201 for goods received and accepted by the buyer applied to four of the six invoices.³⁶ The court agreed this exception applied to three invoices, but goods covered by the fourth invoice were placed in storage by the seller and never delivered to the buyer. Therefore, the seller was not entitled to summary judgment as to these goods.³⁷ The third exception urged by the seller was grounded in the "specially manufactured goods" provision in section 2.201.³⁸ The buyer disputed application of this exception because the "special manufacturing" relied on by the seller merely consisted of marks or logos on the goods that could be removed or covered up to make the goods suitable for sale to others. Furthermore, the seller failed to show it made a substantial beginning to manufacture or taken steps to procure the goods when the cancellation notice was received. Summary judgment was denied on the two invoices for which this exception was urged.³⁹ Beyond the Statute of Frauds issues, the buyer also claimed its payment for three invoices excused non-payment of the fourth invoice because of the seller's failure to deliver these goods on time. Because of a disputed issue of fact as to whether the buyer breached its payment obligations, summary judgment could not be rendered on the damages issue. The court ultimately held that summary judgment should be granted in favor of the seller on the Statute of Frauds issue for four of the six invoices, but fact issues remained about applying of the Statute of Frauds to the other two invoices and for the issue of damages on all six invoices.⁴⁰

C. PAROL EVIDENCE

Application of the parol evidence rule can be difficult. On one hand, the rule serves the worthwhile purpose of preventing an aggrieved party from using prior oral or written statements to vary the express terms of a final written contract he or she has signed. On the other hand, it is always possible a person was persuaded to sign because of false representations about what the agreement contained or what the terms meant. In the latter situation, evidence of fraud can be introduced as an exception to

35. *Barrington Group*, 2010 WL 184307, at *7.

36. *Id.* at *7-8. TEX. BUS. & COM. CODE ANN. § 2.201(c)(3) provides that the Statute of Frauds does not apply to goods for which payment was made or to goods received and accepted.

37. *Barrington Group*, 2010 WL 184307, at *8.

38. Under TEX. BUS. & COM. CODE ANN. § 2.201(c)(1), a seller of goods that are specially manufactured for a buyer and not suitable for sale to others can avoid the Statute of Frauds if the seller has begun manufacture of the goods or made commitments for their procurement, and the circumstances reasonably indicate the goods are intended for the buyer.

39. *Barrington Group*, 2010 WL 184307, at *8.

40. *Id.* at *10.

the parol evidence rule despite the written contract. However, it is always possible to allege a person was induced to enter into a contract because of the other party's fraud and the exception would too easily overcome the rule.

In *LeTourneau Technologies Drilling Systems, Inc. v. Nomac Drilling, LLC*,⁴¹ the court addressed a situation where a buyer signed two separate agreements to purchase oil field drilling equipment, one for ninety million dollars and the other for ten million dollars. Both contracts contained merger clauses expressly stating the contract constituted the final agreement between the parties. The equipment did not live up to the buyer's expectations and the buyer demanded return of its down payment. In an ensuing action by the seller, the buyer counterclaimed to rescind the contract and recover the down payment on grounds of contract breach and fraudulent inducement. The seller moved for partial summary judgment on the fraud claim. After noting tension between the parol evidence rule and the fraud exception, the court discussed prior Texas cases in which justifiable reliance was used to determine if evidence of fraud should be allowed.⁴² The court pointed out the critical issue was whether the contract and the circumstances surrounding contract formation indicated that reliance on prior oral or written communications was reasonable. While the merger clause in one contract provided some indication that reliance was not reasonable, the merger clause alone was not determinative. Other factors considered were circumstances of the negotiation, sophistication of the parties, and availability of legal counsel. Even without considering the merger clause, after discussing application of these factors to facts of this case, the court held the buyer's alleged reliance on representations preceding the written agreement was not justified because both parties were large companies that routinely dealt in major transactions.⁴³ In addition, to the extent the buyer required the equipment to meet certain specifications, the length of the contract was such that these specifications could have been easily included in the final document, particularly when the value of the goods was ninety million dollars. As to the ten million dollar contract, the court discussed the same factors and reached the same result.⁴⁴ Partial summary judgment on the fraudulent inducement claim was granted in favor of the seller.⁴⁵

D. REVOCATION OF ACCEPTANCE

Unless otherwise agreed, a buyer has a right to inspect goods prior to accepting them.⁴⁶ If the buyer decides to reject the goods, then rejection

41. 676 F. Supp. 2d 534 (S.D. Tex. 2009).

42. The principal Texas case the court discussed was *Schlumberger Tech. Corp. v. Swanson*, 959 S.W.2d 171 (Tex. 1997).

43. *LeTourneau Techs. Drilling Sys.*, 676 F. Supp. 2d at 545–46.

44. *Id.* at 546–47.

45. *Id.* at 547.

46. See TEX. BUS. & COM. CODE ANN. § 2.513 (West 2009). In *Romero v. Scoggin-Dickey Chevrolet-Buick, Inc.*, No. 07-09-0086-CV, 2010 WL 456910, at *2 (Tex. App.—

must take place within a reasonable time.⁴⁷ Even if goods have been accepted, a buyer may revoke acceptance if the defects in the goods were not discovered until they were put to use.⁴⁸ All these rules figured in *Courey International v. Designer Floors of Texas, Inc.*,⁴⁹ where the buyer, a tile company, purchased a substantial quantity of floor tiles for distribution to flooring contractors. When the buyer began receiving complaints from its customers about the tile's failure to adhere to floor surfaces, it contacted the seller. The seller recommended using a different adhesive but tests using this adhesive yielded the same results. Between July and October of 2003, the buyer reinstalled another brand of tile in several floors for customers who complained about the original installation. On October 23, 2003, the buyer notified the seller it would discontinue selling this tile brand, asked for reimbursement of costs incurred during reinstallation, and credit for unused tile to be returned to the seller from the buyer's warehouse. The seller refused these requests and sued for the balance due on the contract. The buyer produced evidence the tile failed to properly adhere to floor surfaces and when installed, the tile showed an imprint shaped like a cutout in the boxes used to ship the tile. The trial court granted judgment in favor of the buyer.⁵⁰ On appeal, the court held the evidence showed a breach of the warranty of merchantability sufficient to justify rejection of unused tile and revocation of acceptance of installed tile.⁵¹ The court also held the delay in notifying the seller was not unreasonable because of the difficulty in discovering the defects coupled with the buyer's attempt to correct the problem by following the seller's advice about the use of a different adhesive.⁵² The judgment of the trial court was affirmed.⁵³

E. REMEDIES

An interesting pair of recent cases addressed the effect of clauses prohibiting recovery of consequential damages by buyers of natural gas. In *Cherokee County Cogeneration Partners, L.P. v. Dynege Marketing and Trade*,⁵⁴ a buyer had a long-term supply contract for gas purchased to operate a cogeneration facility. The contract included a clause allowing the buyer to use the gas to operate the facility or to resell the gas to third parties, as well as a clause disclaiming the buyer's right to recover consequential damages. Following disruptions in the gas industry caused by

Amarillo Feb. 9, 2010, no pet.) (mem. op.) the court applied section 2.513 to hold a contract for sale was not completed until the seller gave the buyer an opportunity to inspect the goods.

47. TEX. BUS. & COM. CODE ANN. § 2.602(a) (West 2009).

48. *Id.* § 2.608.

49. No. 03-09-0059-CV, 2010 WL 143420 (Tex. App.—Austin Jan. 15, 2010, no pet.) (mem. op.).

50. *Id.* at *1.

51. *Id.* at *6–7.

52. *Id.* at *6.

53. *Id.* at *8.

54. 305 S.W.3d 309 (Tex. App.—Houston [14th Dist.] 2009, no pet.).

the 2005 hurricanes Katrina and Rita, the seller was unable to deliver the required quantity of gas and the buyer sued for damages based on the difference between the amount it would pay for gas under the contract and the amount it would receive by sale of gas to third parties. The seller argued this damage formula allowed recovery of lost profits in violation of the clause prohibiting recovery of consequential damages. The buyer contended the contract specifically allowed for the resale of gas to third parties, and the damages sought were direct damages rather than consequential damages. The trial court granted summary judgment for the seller.⁵⁵

On appeal, the court noted the contract's failure to define the term "consequential damage" raised the question of whether to use the Code definition, which treats profits on resale contracts as consequential damages, or the common law definition, which allows recovery of such profits as direct damages if they are "conclusively foreseen" as a consequence of breach.⁵⁶ Because the contract did not define the term, the court presumed it was used in its ordinary sense and applied the common law definition reasoning that the resale of gas as a specific right of the buyer in the contract made recovery of profits lost by resale a direct damage and not a consequential damage.⁵⁷ The judgment of the trial court was reversed and the case was remanded.⁵⁸

In *Wolf Hollow I, L.P. v. El Paso Marketing, L.P.*,⁵⁹ as in *Cherokee*, the contract contained *force majeure* and disclaimer of consequential damages clauses. In this case, however, another contract existed, through assignment, between the seller and a pipeline company that provided transportation services between the seller and the buyer. Over time, disruptions in supply were caused by various equipment and computer errors. In addition, some of the delivered gas was allegedly contaminated with liquid hydrocarbons, resulting in damage to the buyer's electrical generation facility. Faced with the buyer's complaints, the seller sought a declaratory judgment that it had no liability to the buyer under the *force majeure* and disclaimer of liability clauses, and subsequently filed a third party action against the pipeline company for contribution and indemnity. The buyer counterclaimed for breach of contract and breach of warranty, and filed a cross-claim against the pipeline company for negligence. The trial court granted summary judgment on all issues in favor of the seller and pipeline company.⁶⁰ On appeal, the court determined it was not necessary to consider the *force majeure* issue and instead addressed the buyer's contract claims against the seller and the negligence claim

55. *Id.* at 311.

56. *Id.* at 314.

57. *Id.* at 315.

58. *Id.* at 316. The *force majeure* issue was not before the court on this appeal. *See id.* at 312 n.3.

59. 329 S.W.3d 628 (Tex. App.—Houston [14th Dist.] Oct. 28, 2010, pet. filed).

60. *Id.* at 631.

against the pipeline company.⁶¹

On the contract claim, the court held the principal purpose of the contract was the sale of gas, which is governed by the Code and not by common law.⁶² Applying section 2.713 of the Code, the court reasoned the buyer was not seeking damages for the contract or market difference in the price of gas caused by the delivery interruptions, but for the purchase of replacement power needed to satisfy its customers when unable to operate its cogeneration facility. Because the circumstances in which the seller was liable for the purchase of replacement power were addressed in the contract and none of them applied in this case, the damages sought by the buyer were consequential damages as defined in section 2.715 and not direct damages resulting from a breach of contract.⁶³ On the breach of warranty claim asserted against the seller for delivery of contaminated gas, the court also concluded that purchasing replacement power was not a “special circumstance” within the meaning of section 2.714 of the Code that would permit such recovery in the face of the other contract provisions and the disclaimer of consequential damages.⁶⁴ Summary judgment in favor of the seller was affirmed on all of these issues.⁶⁵

The buyer fared better, however, on its negligence cross-claim against the pipeline company. On this issue, the pipeline company argued the buyer was trying to convert a contract action into a tort claim. Reviewing the terms by which the transportation contract was assigned to the pipeline company, the court concluded the buyer and the company were not in privity.⁶⁶ The court reasoned that under these circumstances, the pipeline company had a duty to perform its contract obligations with reasonable care to avoid injury to property of a non-contracting party, and a negligence claim would lie against the company for delivering contaminated gas.⁶⁷ In a final attempt to avoid liability, the pipeline company asserted the buyer was precluded from recovery under the economic loss rule.⁶⁸ Under this rule, damages are not recoverable if a defective product causes harm only to itself rather than causing harm to a person or to other property. The court held the buyer’s allegations of physical harm to the turbines and other equipment in the cogeneration plant took the case out of the economic loss rule.⁶⁹ The summary judgment in favor of the

61. *Id.* at 634 n.2.

62. *Id.* at 637. Because of this determination, the court distinguished *Cherokee* because it was based on common law definitions of direct damages and consequential damages rather than the Code definitions. *See id.* at 638 n.6.

63. *Id.* at 638. TEX. BUS. & COM. CODE ANN. § 2.714(b) (West 2009) provides, “[t]he measure of damages for breach of warranty is the difference at the time and place of acceptance between the value of the goods accepted and the value they would have had if they had been as warranted, unless special circumstances show proximate damages of a different amount.”

64. *Wolf Hollow I*, 329 S.W.3d at 640–41.

65. *Id.* at 637–40.

66. *Id.* at 643.

67. *Id.* at 644.

68. *Id.*

69. *Id.* at 645.

pipeline company was reversed and remanded.⁷⁰

IV. NEGOTIABLE INSTRUMENTS

A. FORM OF INSTRUMENT

In *Financial Freedom Senior Funding Corp. v. Horrocks*,⁷¹ the court had to decide if two negotiable notes were demand notes or notes payable at a definite time. The issue arose because of language in two apparently inconsistent paragraphs contained in the notes.⁷²

Following the death of the maker's wife, who inherited the property collateralizing the note after the maker's death, her estate administrator sent notice to the payee bank that claims against the estate had to be filed within four years after the date of her death. For some reason, the bank did not file a claim but sent a notice of acceleration more than four years later. The administrator sued to quiet title to the property. The bank argued the statute of limitations on the notes did not begin to run until notice of acceleration was given because the notes did not state a definite time of payment. The administrator contended the notes were demand notes and the limitations period began running on the date they were signed. The court agreed with the bank that the notes were not demand notes, but disagreed that the notes lacked a definite time of payment.⁷³ Pointing out that paragraph 4 referred to the conditions stated in paragraph 7, the court reasoned that a cause of action to enforce the lien securing the notes would accrue upon occurrence of one of the conditions in paragraph 7.⁷⁴ According to the court, therefore, the notes were payable at a definite time under section 3.108 of the Code and that time began

70. *Id.*

71. 294 S.W.3d 749 (Tex. App.—Houston [14th Dist.] 2009, no pet.).

72. The two paragraphs in question provided:

4. MANNER OF PAYMENT

(A) Time

Borrower shall pay all outstanding principal and accrued interest to Lender upon receipt of a notice by Lender requiring immediate payment in full, as provided by Paragraph 7 of this Note. . . .

7. IMMEDIATE PAYMENT IN FULL

(A) Death or Sale

Lender may require immediate payments in full of outstanding principal and accrued interest if:

(i) All Borrowers die, or

(ii) All of a Borrower's title in the Property (or his beneficial interest in a trust owning all or part of the Property) is sold or otherwise transferred and no other Borrower retains (a) title to the Property in fee simple, (b) a leasehold under a lease for less than 99 years which is renewable or a lease having a remaining period of not less than 50 years beyond the date of the 100th birthday of the youngest Borrower (or retaining a beneficial interest in a trust with such an interest in the Property), or (c) a life estate in the Property.

Id. at 751–52.

73. *Id.* at 754.

74. *Id.*

to run on March 21, 2003, upon the death of the wife.⁷⁵ Since the suit was not commenced for more than four years after that date, the liens were unenforceable.⁷⁶

B. LIABILITY OF PARTIES

In the last Survey, the author criticized two cases in which the courts held actions to collect a check amount from the drawer were not actions founded in contract.⁷⁷ During this Survey period, the Dallas Court of Appeals reached the same result in *United Automobile Insurance Co. v. 1/2 Price Checks Cashed*.⁷⁸ A petition for review was granted in *United*. The Supreme Court recognized that a drawer's liability is one founded on contract and reversed the lower court.⁷⁹

C. CONVERSION

In *Ross v. Bank of America*,⁸⁰ an office manager forged her employer's endorsement and deposited a number of checks payable to her employer into her personal bank account at a location other than where the employer had an account. The employer sued the depository bank for conversion and for money had and received. The depository bank moved to dismiss the claim for money had and received on the ground that section 3.420 preempts such claims.⁸¹ Reviewing earlier Texas cases, the court concluded section 3.420 did not completely preempt the common-law claim, but that recovery on such claims was limited to the face amounts of the checks.⁸²

75. *Id.* at 756. TEX. BUS. & COM. CODE ANN. § 3.108(b) (West 2011) states, *inter alia*, that an instrument is payable at a definite time if it is payable "at a time or times readily ascertainable at the time the promise or order is issued" after the instrument is issued.

76. *Id.*

77. John Krahrmer, *Commercial Transactions*, 63 SMU L. REV. 425, 438 n.87 (2010). See *Zamora v. The Money Box*, No. 04-08-00549-CV, 2009 WL 2050207 (Tex. App.—San Antonio July 15, 2009, pet. denied) (mem. op.); *Time Out Grocery v. Vanguard Group, Inc.*, 187 S.W.3d 41 (Tex. App.—Dallas 2005, no pet.), *abrogated by 1/2 Price Checks Cashed v. United Auto Ins. Co.*, No. 10-0434, 2011 WL 2517036 (Tex. June 24, 2011).

78. 310 S.W.3d 197 (Tex. App.—Dallas 2010, pet. granted), *rev'd*, 2011 WL 2517036 (Tex. 2011).

79. *1/2 Price Checks Cashed v. United Auto. Ins. Co.*, No. 10-434, 2011 WL 2517036 (Tex. June 24, 2011).

80. 693 F. Supp. 2d 692 (S.D. Tex. 2010).

81. *Id.* at 693. The extent to which provisions in chapter 3 preempt common law claims has been the subject of several Texas decisions. See, e.g., *Sw. Bank v. Info. Support Concepts, Inc.*, 149 S.W.3d 104 (Tex. 2004) (comparative fault rules of chapter 3 preempt comparative responsibility rules applicable under other statutes); *Bryan v. Citizens Nat'l Bank in Abilene*, 628 S.W.2d 761 (Tex. 1982) (common law claim of mistake not preempted by chapter 3); *Mazon Assoc., Inc. v. Comerica Bank*, 195 S.W.3d 800 (Tex. App.—Dallas 2006, no pet.) (common law conversion claims brought by persons who had not received delivery of checks preempted by section 3.420(a)(2)).

82. *Ross*, 693 F. Supp. 2d at 696. Questions regarding the preemptive effect of section 3-420 are discussed at length in Phillip E. Cleary, *Statutory Overkill: Why Section 3-420(a) of the Uniform Commercial Code May Not Really Mean What It Says About the Issuer's Cause of Action for Conversion of a Negotiable Instrument*, 39 UCC L.J. 1 (2007). As to actions for money had and received, Cleary notes that:

V. BANK DEPOSITS AND COLLECTIONS

A. RELATIONSHIP BETWEEN PAYOR BANKS AND THEIR CUSTOMERS

Under section 4.401 of the Code, a payor bank is entitled to pay any “properly payable” item drawn on a customer’s account.⁸³ If it fails to pay an item otherwise properly payable, the bank runs the risk of being liable for wrongful dishonor.⁸⁴ The difficulty lies in distinguishing between those items that are properly payable and those that are not.⁸⁵

In *Wilcots v. Wiggins*,⁸⁶ an incarcerated inmate inherited funds from his mother and signed a limited power of attorney authorizing his sister to open an account for him at a credit union and deal with some of his financial matters. Acting in accordance with his instructions, his sister opened a Power of Attorney account in her name. She immediately withdrew \$3,500 of the funds and disbursed them pursuant to her brother’s instructions. During the next few weeks, she withdrew the rest of the money for her personal use. The brother sued his sister, the credit union, and one of its employees for improperly allowing the withdrawals. During pendency of this action, his sister died and the claim against her was dismissed for want of prosecution; the claim against the credit union continued with the trial court ultimately granting summary judgment in favor of the credit union and its employee.⁸⁷ On appeal, the court reviewed the terms of the power of attorney under which the account was opened and held it granted the sister authority to draw checks and withdraw funds.⁸⁸ Based on the power of attorney, the account agreement, and the signature card, the court concluded the funds were properly disbursed by the credit union and summary judgment was affirmed.⁸⁹

Section 3-118(g) states, “[u]nless governed by other law regarding claims for indemnity or contribution, an action (i) for conversion, for money had and received, or like action based on conversion, (ii) for breach of warranty, or (iii) to enforce an obligation, duty, or right arising under this Article and not governed by this section must be commenced within three years after the [cause of action] accrues. . . .”

[T]he specific mention of an “action . . . for money had and received” in § 3-118(g) shows that the cause of action has not been displaced by the Code. *Id.* at 433–34. The decision in *Ross* is consistent with the Cleary article.

83. TEX. BUS. & COM. CODE ANN. § 4.401(a) (West 2011) (“A bank may charge against the account of a customer an item that is properly payable from that account even though the charge creates an overdraft. An item is properly payable if it is authorized by the customer and is in accordance with any agreement between the customer and the bank.”).

84. *Id.* § 4.402.

85. Whether an item is properly payable presents a bank with issues of both law and fact. See Official Comment to U.C.C. § 4-203 (2002) (“Payor banks always have the problem of making proper payment of an item; whether such payment is proper should be based upon all of the rules of Articles 3 and 4 and all of the facts of any particular case, and should not be dependent entirely upon instructions from or an agreement with a person presenting an item.”). TEX. BUS. & COM. CODE ANN. § 4.203 (West 2011). Also note section 4.203 is identical to U.C.C. § 4-203.

86. 306 S.W.3d 947 (Tex. App.—Dallas 2010, no pet.).

87. *Id.* at 948–49.

88. *Id.* at 951.

89. *Id.*

Another issue that can arise from payment of an item not properly payable is whether the customer reported the improper payment within the one year time limit provided in section 4.406 of the Code or stated in the deposit agreement.⁹⁰ In *Lenk v. Jefferson State Bank*,⁹¹ discussed in the last Survey, a county clerk fraudulently named himself as administrator of several decedents' estates by forging letters of appointment and then withdrew funds from the decedents' bank accounts. The court of appeals held that sending account statements to the fraudster did not trigger the statutory time limit or bar a lawfully appointed administrator from suing the bank to recover funds improperly paid from the account.⁹² During this Survey period, the Texas Supreme Court reversed the court of appeals and ruled the time limit for reporting unauthorized transactions began running when the lawful administrator was appointed because the bank retained statements of account available to the administrator upon her appointment.⁹³ Because the administrator delayed reporting the improper payments for almost two years after her appointment, the administrator's claim was barred.⁹⁴

While the Texas Supreme Court's opinion is clear on the point that the one year time limit in section 4.406 begins to run from the date an administrator is lawfully appointed, it is less than clear on whether the court was applying the statutory time limit in section 4.406 or applying the sixty day time limit stated in the deposit agreement.⁹⁵ If the former is the holding of the court, an administrator would have one year after appointment to locate a decedent's bank records. If the latter is the holding, an administrator would have only the time period stated in the deposit agreement to locate the records, a time period which might be much shorter (e.g., ten days). If the shorter time period applies, even a diligent administrator dealing with the estate of a decedent who kept good records might be hard-pressed to discover any unauthorized transactions. On the facts described in *Lenk*, these seemingly conflicting statements might be reconciled because the administrator did become aware of the

90. See TEX. BUS. & COM. CODE ANN. § 4.406(f) (West 2011). Under the general rule of this section, if a bank sends or makes available a statement of account to its customer, the customer must examine the statement with "reasonable promptness" and notify the bank of any alterations or forgeries of the customer's signature. See *In Re Estate of Berry*, 280 S.W.3d 478, 480 (Tex. App.—Dallas 2009, no pet.). The outside time limit for reporting alterations is one year. *Id.* As a practical matter, virtually all deposit agreements specify a time limit for reporting such improper payments; although agreements vary, a common time limit is thirty days.

91. 323 S.W.3d 199 (Tex. App.—San Antonio Mar. 11, 2009, pet. granted) *rev'd*, 323 S.W.3d 146 (Tex. 2010).

92. See *id.* at 202–03; Krahmer, *supra* note 77, at 444–45.

93. *Jefferson State Bank v. Lenk*, 323 S.W.3d 146, 147 (Tex. 2010).

94. *Id.* at 147, 150.

95. Compare *id.* at *Lenk*, 323 S.W.3d at 147 (“[w]e thus hold that the statute of repose in Section 4.406 begins to run once a court appoints an administrator. In this case, the repose period had expired before the administration brought suit almost two years later.”) with *Lenk*, 323 S.W.3d at 150 (“[t]he statute of repose in Section 4.406 of the Business and Commerce Code bars [the administrator’s] claims because she failed to notify the Bank of any unauthorized transactions within sixty days of being appointed estate administrator.”).

existence of the bank accounts by at least February 2004, but did not notify the bank about improper transactions until June 2005. Once aware of the existence of an account, it seems reasonable to require notice of improper payments within the time limit stated in the deposit agreement—which the administrator did not do. Absent knowledge of the existence of an account, however, it seems unreasonable to apply a time limit contained in a deposit agreement and better to use, instead, the one year limit in section 4.406(f)—a time limit with which *Lenk* also failed to comply. The uncertainty created by this opinion will no doubt be the subject of litigation in some future case.

VI. SECURED TRANSACTIONS

A. PERFECTING A SECURITY INTEREST

Chapter 9 contains two distinct rules governing perfection of security interests in motor vehicles. While vehicles are in possession of a seller who is in the business of selling goods of that kind (i.e., cars in the hands of a car dealer), perfection is accomplished by filing a financing statement covering the seller's inventory.⁹⁶ Once a vehicle is sold and a certificate of title is issued, a security interest is perfected by complying with the certificate of title law determined by the jurisdiction issuing the certificate.⁹⁷ In Texas, the certificate of title law governing motor vehicles requires application for a certificate of title containing a notation of the security interest on the certificate of title.⁹⁸ In *In re Moye*,⁹⁹ a creditor asserted that it had a perfected security interest in several used cars held for sale by a dealer because the creditor had taken physical possession of the certificates of title that were issued for the cars. After rejecting various procedural objections raised by the creditor, the court acknowledged that filing a financing statement covering inventory is the proper method of perfecting security interests for cars held for sale by a car dealer even if the cars are used cars covered by a certificate of title, and that physical possession of a title does not perfect a security interest in cars held for sale by car dealers.¹⁰⁰

B. ASSIGNMENT OF SECURITY INTERESTS

In *In re Clark Contracting Services, Inc.*,¹⁰¹ the federal district court reversed a controversial decision previously rendered by a bankruptcy court, which brought the rules governing assignment of security interests perfected by notation on a certificate of title back into line with the Code's general rule dealing with continued perfection of security interests

96. See TEX. BUS. & COM. CODE ANN. §§ 9.311(a), 9.311(d) (West 2011).

97. See *id.* § 9.311(a)(2).

98. See TEX. TRANSP. CODE ANN. § 501.111, 501.114 (West 2007).

99. No. H-09-2747, 2010 WL 3259386 (S.D. Tex. Aug. 17, 2010).

100. *Id.* at *11–12, *13.

101. 438 B.R. 913 (Bankr. W.D. Tex. 2010).

following an assignment.¹⁰² Under the general rule, an assignee may, but is not required, to file a record of the assignment.¹⁰³ The bankruptcy court had reasoned that the Texas Certificate of Title Act required an assignee to obtain a new certificate of title showing the name of the assignee as the secured party.¹⁰⁴ Soon after this decision was reported, the Texas legislature amended the Certificate of Title Act making it clear that an assignee was not required to record an assignment to continue perfection of a security interest.¹⁰⁵ On appeal, the district court held the terms of the Texas Certificate of Title Act, both before and after the amendment, did not mandate recordation of an assignment to continue perfection.¹⁰⁶

A somewhat different certificate of title issue was addressed in *Nxcess Motor Cars, Inc. v. JPMorgan Chase Bank, N.A.*,¹⁰⁷ where a perfected secured creditor sued the purchaser of a car for conversion. The purchaser had acquired the car under a “clean” certificate of title issued by the Texas Department of Motor Vehicles. Unbeknownst to both the seller and the purchaser, a previous owner of the car had forged a release of lien and applied for a certified copy of the original certificate of title indicating no liens existed on the vehicle. The purchaser, a car dealer, argued it qualified as a buyer in the ordinary course of business and therefore took the car free of the secured party’s claim.¹⁰⁸ The court rejected this argument on the ground that forging a release of lien breaks

102. *Id.* at 925.

103. TEX. BUS. & COM. CODE ANN. § 9.310(c) (West 2011) (“If a secured party assigns a perfected security interest or agricultural lien, a filing under this Chapter is not required to continue the perfected status of the security interest against creditors of and transferees from the original debtor.”).

104. See *In re Clark*, 399 B.R. 789, 804 (Bankr. W.D. Tex. 2008). This decision was criticized by both courts and commentators. See, e.g., *In re Scott*, 427 B.R. 123, 128 (Bankr. S.D. Ind. 2010); CLARK’S SECURED TRANSACTIONS, *Red Flag: Texas Court Requires Assignees of Vehicle Contracts to Get Lien Noted on New Certificates of Title* (February 2009); Alvin C. Harrell, Note, *Clark Contracting Services, Inc. v. Wells Fargo—Does an Assignee of a CT Lien Entry Become Unperfected?*, 62 CONSUMER FIN. L.Q. REP. 274 (2008).

105. See Act of June 19, 2009, 81st Leg., ch. 814, § 4–5, 2009 Tex. Sess. Law Serv. 2049 (current version at TEX. TRANSP. CODE ANN. §§ 501.113–114 (West Supp. 2010)). The same Act made similar changes in the certificate of title provisions governing utility security interests, boats, and boat motors. See Act of June 19, 2009, 81st Leg., R.S., ch. 814, §§ 1–2, 2009 Tex. Sess. Law Serv. 2047 (current version at TEX. BUS. & COM. CODE ANN. § 261.012 (West Supp. 2011)) (utility security interests); Act of June 19, 2009, 81st Leg., R.S., ch. 814, § 3, 2009 Tex. Sess. Law Serv. 2047 (current version at TEX. PARKS AND WILDLIFE CODE ANN. § 31.052 (West Supp. 2011)) (boats & boat motors).

106. *Clark Contracting Servs.*, 438 B.R. at 925. In reaching this conclusion, the court reasoned the amendment was declaratory of legislative intent, and coupled with the legislative history of the Act, its relation to the Code and public policy, and the terms of the Act itself, the bankruptcy court had erred in reaching a contrary result. *Id.*

107. 317 S.W.3d 462 (Tex. App.—Houston [1st Dist.] 2010, pet. denied).

108. *Id.* at 466–67. The Code defines a buyer in ordinary course of business as one who buys goods in good faith from a person in the business of selling goods of that kind, without knowledge that the sale violates the rights of another person holding the goods. TEX. BUS. & COM. CODE ANN. § 1.201(b)(9) (West 2009). Although the principal defendant was the dealer, an individual who purchased the car from the dealer was also named as a defendant and the arguments discussed by the court were the same for both defendants. *Nxcess*, 317 S.W.3d at 464–65, 467.

the chain of title and prevents a subsequent purchaser from acquiring ownership of a vehicle because such break.¹⁰⁹ The purchaser also argued it was protected by the good faith purchase provisions in section 2.403 of the Code.¹¹⁰ Under that section, a seller with voidable title can transfer good title to a good faith purchaser for value.¹¹¹ The court rejected this argument as well, pointing out that the forged release of lien rendered the title void and not merely voidable.¹¹² Under these circumstances, the secured party whose lien was noted on the original certificate of title had the superior claim to the car.¹¹³

Issues involving assignments can go beyond determination of rights acquired by an assignee to directly address whether security interests can even be created or assigned in certain types of collateral.¹¹⁴ In *Texas Lottery Commission v. First State Bank of DeQueen*,¹¹⁵ a lottery winner assigned his last two annual payments to a bank, but the Lottery Commission asserted the Texas Lottery Act prohibited the assignment.¹¹⁶ The plaintiffs argued that the prohibition in the Lottery Act was ineffective under section 9.406 of the Code. The supreme court agreed with the plaintiffs that lottery winnings are “accounts” under section 9.102 and that assignments of accounts are authorized by section 9.406.¹¹⁷ Judgment was affirmed in favor of the plaintiffs.¹¹⁸

C. PRIORITIES

Section 9.332 of the Code protects transferees of deposit account funds from claims of parties asserting a security interest in the deposit account unless the transferee has colluded with the debtor to violate the rights of the secured party.¹¹⁹ Under this rule, a transferee paid with a check issued by a debtor may cash the check and retain the funds against the claim of a creditor with a security interest in the bank account unless the transferee and debtor acted in concert to deprive the creditor of his or

109. On this point, the court cited *Drake Ins. Co. v. King*, 606 S.W.2d 812, 817 (Tex. 1980) and *Lee v. The Bank, N.A.*, 23 S.W.3d 129, 131 (Tex. App.—Austin 2000, no pet.), both holding the purchaser of a motor vehicle acquires no rights in the vehicle following the forgery of a release of lien.

110. *Nxcoss*, 317 S.W.3d at 469–70.

111. TEX. BUS. & COM. CODE ANN. § 2.403(a) (West 2009).

112. *Nxcoss*, 317 S.W.3d at 471.

113. *Id.*

114. The Code contains a number of provisions dealing with a debtor’s ability to create security interests in, and a secured party’s ability to assign rights in, *inter alia*, accounts, chattel paper, payment intangibles, promissory notes, leases, and letters of credit. TEX. BUS. & COM. CODE ANN. §§ 9.406–.409 (West 2011).

115. 325 S.W.3d 628 (Tex. 2010).

116. *Id.* at 631. The provisions on which the Texas Lottery Act relied appear in TEX. GOV. CODE ANN. §§ 466.406, 466.410 (West 2009).

117. *Texas Lottery Comm’n*, 325 S.W.3d at 635. See TEX. BUS. & COM. CODE ANN. § 9.102(a)(2) (West 2010) (defining “accounts”); TEX. BUS. & COM. CODE ANN. § 9.406(f) (West 2011) (provides that accounts are assignable despite the existence of a “rule of law, statute, or regulation” that “prohibits, restricts, or requires the consent of the government, governmental body, or official.”).

118. *Tex. Lottery Comm’n*, 325 S.W.3d at 631.

119. TEX. BUS. & COM. CODE ANN. § 9.332 (West 2011).

her right to the funds. The result is not so clear, however, when a bank acting upon the request of its customer, applies funds in the customer's account to repay loans it made to the customer when another creditor has a security interest in the those funds.¹²⁰ This issue was discussed, but not decided in *City Bank v. Compass Bank*.¹²¹ In this case, one bank had a security interest in collateral proceeds deposited in an account maintained at another bank and the depository bank was asked by its depositor to apply one million dollars of those funds to a debt the customer owed to the depository bank. When the debtor defaulted on debts owed to both these banks, a flurry of lawsuits began including a bankruptcy filing by the debtor. Because of the complex factual circumstances and other pending lawsuits, the opinion addresses a number of issues, but for purposes of this article, the most interesting portion is the court's discussion of the Code sections dealing with relative priorities of competing claims to bank accounts.¹²² While the opinion helpfully summarizes the interpretive difficulties surrounding such claims, the court declined to resolve the dispute because of the pending bankruptcy case in which these same issues were bound up with a fraudulent transfer claim.¹²³ The proceedings were stayed pending a decision by the bankruptcy court.¹²⁴ Although the opinion does not authoritatively answer certain issues before the court, it is a case worth watching for further developments on these issues, specifically the interpretation of section 9.332.

D. DEFAULT AND DISPOSITION OF COLLATERAL

"Default" is not defined in the Code itself. Instead, what constitutes a default under a security agreement depends upon the terms of the agreement. In *Grohman v. Kahlig*,¹²⁵ a husband and wife entered into a divorce settlement which included a security agreement requiring the husband to provide collateral to secure his performance of the settlement. The collateral consisted of controlling stock held by the husband two corporations. A few years later, he reorganized the corporations by converting the corporations to limited partnerships. When his ex-wife discovered the conversion, she sued for breach of the security agreement based on the condition that her ex-husband would "not sell, transfer, lease, or otherwise dispose of the Collateral" and would "not allow the Collateral to become wasted or destroyed."¹²⁶ She also asserted claims for fraud, negligence, and gross negligence. The trial court entered judgment in favor of the ex-husband on all claims.¹²⁷ The court of appeals

120. See *id.* at cmt. 2. ("[T]his section does not cover . . . the case in which a bank debits an encumbered account and credits another account it maintains for the debtor.")

121. 717 F. Supp. 2d 599 (W.D. Tex. 2010).

122. See *id.* at 614–20. See TEX. BUS. & COM. CODE ANN. §§ 9.327, 9.332, 9.341 (West 2011).

123. *City Bank*, 717 F. Supp. 2d at 617, 619.

124. *Id.* at 626.

125. 318 S.W.3d 882 (Tex. 2010).

126. *Id.* at 884–85.

127. *Id.* at 884.

upheld the ruling of the trial court on the tort claims, but reversed the contract claim because converting the corporations to limited partnerships was a disposition of the collateral resulting in destruction of the stock.¹²⁸

On further appeal, the Texas Supreme Court held the security agreement was to be considered as a whole and not by reference to only one part of the agreement.¹²⁹ Because the term “collateral” was defined in the security agreement to mean the shares of stock in the corporations “and all replacements, additions and substitutions therefor[sic] now owned or hereafter acquired by [debtor],” the conversion to limited partnerships did not dispose of the shares in a manner that caused default under the agreement; it merely substituted the shares for an interest in partnership units.¹³⁰ Furthermore, no transfer of shares occurred because the ex-husband retained an equivalent ownership interest in the partnerships.¹³¹ The judgment of the appellate court was reversed on this issue.¹³²

In *Holman Street Baptist Church v. Jefferson*,¹³³ a note was secured by the transfer of shares of stock to the payee. The final note payment was scheduled for December 31, 1992. However, the maker failed to make payments on the note and in 2006, the maker sued to compel return of the stock on the ground that the statute of limitations expired on December 31, 1996 because the security interest became unenforceable. The payee asserted: (1) the maker reaffirmed the debt numerous times over a period of several years; (2) by seeking return of the stock, the maker sought affirmative relief waiving the right to assert limitations; and (3) even if an action on the debt was barred, the debt still existed and did not bar enforcement of security interest. The court held that by seeking return of the stock, the maker sought affirmative relief thereby reviving the payee’s action on the debt under the Texas Civil Practice and Remedies Code.¹³⁴ In addition, under the terms of the note the security interest continued for “four (4) years from the date of payment of Debtor’s last Obligation to Secured Party.”¹³⁵ The court interpreted this language to mean the security interest was still effective because the maker did not make any payments on the note.¹³⁶ The stated time period, therefore, never began to run and had not expired. As to enforcement of the security interest, the court held that under Texas law even if an action on the debt is barred by limitations, the security interest continues to exist and

128. *Id.*; see *Grohman-Kahlig v. Kahlig*, 319 S.W.3d 28 (Tex. App.—San Antonio 2008, pet. granted), *rev’d*, 318 S.W.3d 882 (Tex. 2010).

129. *Grohman*, 318 S.W.3d at 887.

130. *Id.* at 887–88.

131. *Id.* at 888.

132. *Id.*

133. 317 S.W.3d 540 (Tex. App.—Houston [14th Dist.] 2010, pet. denied).

134. *Id.* at 546. See TEX. CIV. PRAC. & REM. CODE § 16.069(a) (West 2008).

135. *Id.* at 549.

136. *Id.*

the secured party may still proceed against the collateral.¹³⁷ The case was remanded for the entry of judgment in favor of the secured party.¹³⁸

What does “if” mean? This was the question in *Regal Finance Company, Ltd. v. Tex Star Motors, Inc.*,¹³⁹ where a jury charge included the statement that a disposition of collateral following repossession was commercially reasonable “if it conforms to reasonable commercial practices among dealers in the type of property that was the subject of the sale.”¹⁴⁰ The evidence introduced at trial described the method and manner by which the sale of repossessed collateral, used cars, was conducted but did not include evidence of the practices used by car dealers. The jury found the sales were made in a commercially reasonable manner and judgment was entered in favor of the dealer who conducted the sales.¹⁴¹ The Houston Court of Appeals reversed the judgment by reasoning that the word “if” meant “only if,” and that the jury verdict could not be upheld on the issue of commercial reasonableness because of the lack of evidence about car dealers’ practices in selling repossessed cars.¹⁴² On further appeal, the Texas Supreme Court disagreed with the conclusion that “if” meant “only if” because the jury instruction read as a whole included a paragraph indicating that a disposition could be commercially reasonable whether or not it complied with the practices used by dealers.¹⁴³ In the supreme court’s view, the statement about dealer practices was “merely an example of one method for determining commercial reasonableness.”¹⁴⁴ The judgment of the court of appeals was reversed and remanded for that court to determine if the evidence introduced about commercial reasonableness was factually sufficient to support the jury verdict.¹⁴⁵ A strong dissenting opinion argued that the grammatical structure of the charge was such that the jury was bound to measure commercial reasonableness of the sale against the practices used by dealers, and lack of evidence regarding those practices was fatal to the verdict.¹⁴⁶

VII. CONCLUSION

Issues surrounding contract formation and interpretation figured rather prominently in the cases reported during this Survey period. An increasing number involved electronic communication, whether by information

137. *Id.* at 546. The court distinguished enforcement of a consensual security interest against collateral from cases holding that statutory or equitable liens on real estate are extinguished by the running of a statute of limitations. *See id.* at 546 n.4.

138. *Id.* at 550.

139. No. 08-0148, 2010 WL 3277132 (Tex. Aug. 20, 2010).

140. *Id.*, at *3-4.

141. *Id.*, at *1.

142. *Id.*, at *4; *Tex Star Motors, Inc. v. Regal Fin. Co., Ltd.*, 246 S.W.3d 745, 750-51 (Tex. App.—Houston [14th Dist.] 2008, pet. granted), *rev’d*, 2010 WL 3277132 (Tex. 2010).

143. *Regal Finance Co.*, 2010 WL 3277132, at *4-5.

144. *Id.* at *5.

145. *Id.* at *7. The court of appeals did not reach this issue because it concluded that the jury verdict could be supported “only if” there was evidence of dealer practice in the sale of repossessed cars. *Id.*

146. *Id.* at *11.

contained on websites or sent by email.¹⁴⁷ This trend is likely to continue and, to the extent such communication is sometimes treated more informally than printed communication, discerning the meaning of the parties may become more difficult. Even when contracts are in printed form, disputes about the meaning of terms can still arise, as illustrated by the results reached in *Cherokee County Cogeneration Partners, L.P. v. Dynegey Marketing and Trade*¹⁴⁸ and *Wolf Hollow I, L.P. v. El Paso Marketing, L.P.*¹⁴⁹

Beyond issues of contract formation, *United Automobile Insurance Co. v. ½ Price Checks Cash*¹⁵⁰ has settled the question of whether checks are contracts allowing the recovery of attorney's fees in actions brought against the drawer following dishonor.

Two decisions of the Texas Supreme Court reported during the Survey period deserve special note. In *Jefferson State Bank v. Lenk* the court discussed the circumstances in which a bank might be liable for sending account statements to the wrong person following the death of a customer, and the time limits within which an estate administrator must act in reporting alterations or forgeries under section 4.406 of the Code.¹⁵¹ Unfortunately, the opinion is not entirely clear about when the time limits begin to run and this issue may arise again. In *Texas Lottery Commission v. First State Bank of DeQueen*, however, the court very clearly determined that lottery winnings are accounts in which a security interest can be created.¹⁵²

Finally, the decision in *In re Clark Contracting Services, Inc.* made it clear that the Code rules dealing with the continued perfection of a security interest following assignment govern over the Texas Certificate of Title Act whether the assignment of the security interest occurred before or after the amendments to that Act.¹⁵³

147. See, e.g., *One Beacon Ins. Co. v. Crowley Marine Servs., Inc.*, No. H-08-2059, 2010 WL 1463451 (S.D. Tex. Apr. 12, 2010) (not designated for publication) (printed link in contract from sufficient to make disclaimer of warranty conspicuous); *Barrington Group Ltd. v. Classic Cruise Holdings S. De R.L.*, No. 3:08-CV-1813-B, 2010 WL 184307 (N.D. Tex. Jan. 15, 2010) (interpretation of email as a repudiation of sales contract); *J.D. Fields & Co. v. U.S. Steel Int'l, Inc.*, 690 F. Supp. 2d 487 (S.D. Tex. 2009) (construction of emails as firm offers or mere price quotations).

148. 305 S.W.3d 309, 315–16 (Tex. App.—Houston [14th Dist.] 2009, no pet.) (failure to define “consequential damages” in contract meant common law definition applied).

149. *Wolf Hollow I, L.P. v. El Paso Mktg.*, 329 S.W.3d 628 (Tex. App.—Houston [14th Dist.] 2010, pet. filed) (holding that because principal purpose of contract was sale of gas, Code definition of consequential damages applied).

150. 310 S.W.3d 197 (Tex. App.—Dallas 2010, pet. granted), *rev'd*, 2011 WL 2517036 (Tex. 2011).

151. See *Jefferson State Bank v. Lenk*, 323 S.W.3d 146, 148–50 (Tex. 2010).

152. See *Texas Lottery Comm'n v. First State Bank of DeQueen*, 325 S.W.3d 628, 635–37 (Tex. 2010).

153. See *In re Clark Contracting Servs., Inc.*, 438 B.R. 913, 925 (W.D. Tex. 2010).