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Commerical Transactions

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COMMERCIAL TRANSACTIONS

*John Kraemer**

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THIS article discusses case and statutory developments affecting the Uniform Commercial Code as enacted in Texas as part of the Texas Business and Commerce Code (the “Code”).¹ The time period covered by this 2003 Survey runs from approximately December 1,

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1. The Texas enactment 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 (Vernon 1994, 2002 & Supp. 2003). 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

Chapter 4A: Funds Transfers

Chapter 5: Letters of Credit

Chapter 7: Warehouse Receipts, Bills of Lading and Other Documents of Title

Chapter 8: Investment Securities

Chapter 9: Secured Transactions; Sales of Accounts and Chattel Paper

2002 through November 30, 2003. As usual, the organization of the Survey parallels the organization of the Code.

I. GENERAL PROVISIONS

Perhaps the most important development in Texas Commercial Law during the Survey period was the revision of Chapter 1 of the Code through the adoption of much of the revised Article 1 promulgated by the National Conference of Commissioners on Uniform State Laws.² The possible adoption of revised Article 1 in Texas was noted in last year's Survey.³ However, one major non-uniform amendment was made in the Texas enactment that deserves particular attention.

The Official Text of revised Article 1 substantially changed the default choice-of-law rules contained in the former Article 1. As a general proposition, except in consumer cases, the rules in the Official Text permit the parties to a transaction to choose the law of any jurisdiction to govern their transaction.⁴ The consumer exception limits this open-ended choice of law when the choice of applicable law would deprive a consumer of legal protections afforded to the consumer by the law of the state or nation where the consumer resides or where the consumer contracts for or takes delivery of goods.⁵ Under the former Article 1, the choice of applicable law had to bear a "reasonable relation" to the state or nation whose law was chosen to govern the transaction.⁶

As enacted during the 2003 legislative session, the Texas Legislature rejected the new choice-of-law rules and retained the choice-of-law provisions existing under the former law.⁷ That such a change might occur in jurisdictions considering enactment of revised Article 1 was not unforeseen and, in fact, adoption of revised Article 1 has been slow.⁸ While

2. The text approved by the National Conference of Commissioners on Uniform State Laws may be found in UNIFORM COMMERCIAL CODE, 2002 OFFICIAL TEXT WITH COMMENTS app. XVII (West 2002) [hereinafter OFFICIAL TEXT]. The Texas enactment appears as Act of June 20, 2003, 78th Leg., R.S., ch. 542, §§ 1-21 (codified as TEX. BUS. & COM. CODE ANN. §§ 1.101-310 (Vernon Supp. 2004)).

3. See John Kraemer, *Commercial Transactions*, 56 SMU L. REV. 1255, 1257-58 (2003).

4. See OFFICIAL TEXT, *supra* note 2, § 1-301(b).

5. See OFFICIAL TEXT, *supra* note 2, § 1-301(e).

6. See the former OFFICIAL TEXT, § 1-105, enacted in Texas as TEX. BUS. & COM. CODE § 1.105(a) (Vernon 1994).

7. See TEX. BUS. & COM. CODE ANN. § 1.301 (Vernon Supp. 2004).

8. As of January, 2004, in addition to Texas, only Virginia and the Virgin Islands have adopted revised Article 1. See VA. CODE ANN. §§ 8.1A-101 to -309 (Michie Supp. 2003) and V.I. CODE ANN. §§ 1-101 to -309 (Supp. 2003). Like Texas, Virginia rejected the revised § 1-301 and retained the former choice-of-law rules instead. Only the Virgin Islands adopted revised § 1-301 as it appears in the OFFICIAL TEXT. See V.I. CODE ANN. § 1-301 (Supp. 2003). In January of 2003, Professors Henning and Miller noted that "significant opposition to Article 1's choice-of-law rule in revised § 1-301 had been voiced. NCCUSL has not yet made a concerted effort to enact the article and thus it remains to be seen whether the expressed concerns will lead some to support a non-uniform amendment to § 1-301 or even to oppose enactment altogether; however, the potential is there." William H. Henning & Fred H. Miller, *The State of the Uniform Commercial Code*, 48 UCC BULLETIN 1 (West, January, 2003).

revised Article 1 will no doubt be introduced in other jurisdictions during their 2004 legislative sessions, it appears that misgivings about the open-ended choice-of-law rule in the Official Text may result in the non-uniform amendment of this rule as occurred in Texas or, perhaps, even in the refusal to enact revised Article 1. If non-uniform amendment or the refusal to enact is widespread, it would not be surprising to find that the National Conference of Commissioners revises the Official Text within the next year or two.

Because Chapter 1 was substantially reorganized and renumbered, conforming amendments were made in other Chapters of the Code to update citations to Chapter 1 that are contained in those other Chapters. The following table and accompanying footnotes may be helpful in correlating and understanding the changes made by revised Chapter 1.

Former Chapter 1	Revised Chapter 1
1.101	1.101 ⁹
No similar section	1.102 ¹⁰
1.102(a)-(b) & 1.103	1.103 ¹¹
1.102(c)-(d) & 1.204(a)	1.302 ¹²
1.102(e)	1.106 ¹³
1.104	1.104 ¹⁴
1.105	1.301 ¹⁵
1.106	1.305 ¹⁶
1.107	1.306 ¹⁷
1.108	1.105 ¹⁸

9. **SHORT TITLES.** Derived from former TEX. BUS. & COM. CODE ANN. § 1.101 (Vernon 1994). Subsection (a) unchanged; new subsection (b) adds short title for Chapter 1.

10. **SCOPE OF CHAPTER.** New section intended to make it clear that substantive provisions in Chapter 1 apply to transactions to the extent those transactions are governed by one of the other chapters of the Code.

11. **CONSTRUCTION OF TITLE TO PROMOTE ITS PURPOSES AND POLICIES; APPLICABILITY OF SUPPLEMENTAL PRINCIPLES OF LAW.** Except for stylistic changes and renumbering, the substance has not been changed, but the provisions dealing with variation of Code rules by agreement have been moved to TEX. BUS. & COM. CODE ANN. § 1.302 (Vernon Supp. 2004).

12. **VARIATION BY AGREEMENT.** This section combines rules stated in other sections of the former Chapter 1, but without change in substance.

13. **USE OF SINGULAR AND PLURAL; GENDER.** Except for minor stylistic changes, this section is the same as the former TEX. BUS. & COM. CODE ANN. § 1.102(e) (Vernon 1994).

14. **CONSTRUCTION AGAINST IMPLIED REPEAL.** Substantively unchanged from the former TEX. BUS. & COM. CODE ANN. § 1.104 (Vernon 1994).

15. **TERRITORIAL APPLICABILITY; PARTIES' POWER TO CHOOSE APPLICABLE LAW.** This section states the rules governing the applicability of the Code and the ability of the parties to choose the law of a given state or nation. The Texas version of this section is significantly different from that of the OFFICIAL TEXT.

16. **REMEDIES TO BE LIBERALLY ADMINISTERED.** Except for renumbering and minor stylistic change, this section is the same as the former TEX. BUS. & COM. CODE ANN. § 1.106 (Vernon 1994).

17. **WAIVER OR RENUNCIATION OF CLAIM OR RIGHT AFTER BREACH.** This section has been modified to permit a party to waive or renounce rights by electronic means.

18. **USE OF SINGULAR AND PLURAL; GENDER.** Except for minor stylistic changes, this section is the same as the former TEX. BUS. & COM. CODE ANN. § 1.102(e) (Vernon 1994).

1.109	1.107 ¹⁹
No similar section	1.108 ²⁰
1.201	1.201 ²¹
1.201(25)-(27)	1.202 ²²
1.201(31)	1.206 ²³
1.201(37)	1.203 ²⁴
1.201(44)	1.204 ²⁵
1.202	1.307 ²⁶

19. SECTION CAPTIONS. Renumbered with no change in substance.

20. RELATION TO ELECTRONIC SIGNATURES IN GLOBAL AND NATIONAL COMMERCE ACT. New. The federal Electronic Signatures in Global and National Commerce Act, 15 U.S.C. § 7001 *et. seq.*, permits a state to modify, limit, or supersede the federal law. However, TEX. BUS. & COM. CODE ANN. § 1.108 cmt. 2 (Vernon 2002) notes that this section “does not modify, limit, or supersede Section 101(c) of the Electronic Signatures in Global and National Commerce Act (requiring affirmative consent from a consumer to electronic delivery of transactional disclosures that are required by state law to be in writing); nor does it authorize electronic delivery of any of the notices described in Section 103(b) of that Act.”

21. GENERAL DEFINITIONS. Except for minor stylistic changes, most of the definitions are the same as those appearing in the former TEX. BUS. & COM. CODE ANN. § 1.201 (Vernon 1994). However, some definitions have been changed, a few new definitions have been added, and some definitions have been relocated. The following list summarizes these modifications:

Bill of Lading. Definition of “airbill” omitted as unnecessary.

Conspicuous. “Safe harbor” rules added to determine if a term is “conspicuous.”

Consumer. New term; adopted from TEX. BUS. & COM. CODE ANN. § 9.102(a)(25) (Vernon 2002).

Good Faith. Revised to include both subjective and objective elements. Conforming changes made in other chapters of the Code.

Knowledge, Notice, Notifies. Deleted from former TEX. BUS. & COM. CODE ANN. § 1.201(25), (26), (27) (Vernon 1994); moved to TEX. BUS. & COM. CODE ANN. § 1.202 (Vernon Supp. 2004).

Present Value. Formerly contained within the definition of “security interest.” Now stated as a separate definition; portions of security interest definition dealing with determining nature of a lease moved to TEX. BUS. & COM. CODE ANN. § 1.203 (Vernon Supp. 2004).

Record. New term defined to cover both written media as well as electronic or other media.

Send. Revised to include sending a “record” by electronic means.

State. New term. Derived from standard definition used by NCCUSL.

Surety. Revised to make it clear that the term includes all secondary obligors.

Value. Deleted from former TEX. BUS. & COM. CODE ANN. § 1.201(44) (Vernon 1994) and moved to TEX. BUS. & COM. CODE ANN. § 1.204 (Vernon Supp. 2004).

22. NOTICE; KNOWLEDGE. This new section places the rules about notice, knowledge, and the giving or sending of notice to persons or organizations into a single section.

23. PRESUMPTIONS. The definitions of “presumption” and “presumed” have been moved to this section.

24. LEASE DISTINGUISHED FROM SECURITY INTEREST. This new section states the rules for determining whether a lease is a “true” lease or a disguised security interest. The provisions were derived from the test previously stated in the definition of “security interest” in the former TEX. BUS. & COM. CODE ANN. § 1.201(37) (Vernon 1994).

25. VALUE. This new section contains the provisions for determining when a person gives “value.” It is derived from the former TEX. BUS. & COM. CODE ANN. § 1.201(44) (Vernon 1994).

26. PRIMA FACIE EVIDENCE BY THIRD-PARTY DOCUMENTS. Except for renumbering, this section has not been substantively changed.

1.203	1.304 ²⁷
1.204(b)-(c)	1.205 ²⁸
1.205, 2.208 & 2A.207	1.303 ²⁹
1.206	Omitted ³⁰
1.207	1.308 ³¹
1.208	1.309 ³²
1.209	1.310 ³³
1.210	

II. SALE OF GOODS

A. STATUTE OF FRAUDS

The statute of frauds in Section 2.201 of the Code does not contain a promissory estoppel exception.³⁴ In contrast, however, the parallel provision in Section 2A.201 governing leases does contain such an exception and the 2003 amendments to the Official Text of Section 2-201 (not yet adopted in Texas) permit the use of promissory estoppel to avoid the requirement of a writing.³⁵ In the meantime, the status of promissory estoppel as an exception to the statute of frauds is unclear. Perhaps the most extreme use of promissory estoppel occurred in *Frost Crushed Stone Co., Inc. v. Odell Geer Construction Co., Inc.*,³⁶ where the court allowed the plaintiff to use promissory estoppel as an affirmative cause of action and not merely as a means to counter a statute of frauds defense. Although the case involved a contract for a supplier to produce and haul rock for a highway construction project, the court did not discuss whether this was a sales or a service transaction and did not indicate whether it was specifi-

27. OBLIGATION OF GOOD FAITH. Except for renumbering, this section has not been substantively changed, but note that the definition of “good faith” has been changed in revised TEX. BUS. & COM. CODE ANN. § 1.201(b)(2) (Vernon Supp. 2004).

28. REASONABLE TIME; SEASONABLENESS. The rules for determining when action is taken in a “reasonable” or “seasonable” time have been moved to this section.

29. COURSE OF PERFORMANCE, COURSE OF DEALING, AND USAGE OF TRADE. Rules concerning these subjects were previously divided between TEX. BUS. & COM. CODE ANN. § 1.205 (Vernon 1994), TEX. BUS. & COM. CODE ANN. § 2.208 (Vernon 1994), and TEX. BUS. & COM. CODE ANN. § 2A.207 (Vernon 1994). They are now covered in a single section. The former TEX. BUS. & COM. CODE ANN. §§ 2.208, 2A.207 (Vernon 1994) have been repealed.

30. STATUTE OF FRAUDS FOR KINDS OF PERSONAL PROPERTY NOT OTHERWISE COVERED. This section has been omitted. There is, therefore, no longer a general statute of frauds covering transactions not covered by another chapter of the Code.

31. PERFORMANCE OR ACCEPTANCE UNDER RESERVATION OF RIGHTS. Except for renumbering, this section has not been substantively changed.

32. OPTION TO ACCELERATE AT WILL. Except for renumbering, this section has not been substantively changed.

33. SUBORDINATED OBLIGATIONS. Except for renumbering, this section has not been substantively changed.

34. TEX. BUS. & COM. CODE ANN. § 2.201 (Vernon 1994).

35. See TEX. BUS. & COM. CODE ANN. § 2A.201(d)(4) (Vernon 1994). See also Linda J. Rusch, *Is the Saga of the Uniform Commercial Code Article 2 Revisions Over? A Brief Look at What NCCUSL Finally Approved*, 6 DEL. L. REV. 41, 55 (2003).

36. *Frost Crushed Stone Co., Inc. v. Odell Geer Constr. Co., Inc.*, 110 S.W.3d 41 (Tex. App.—Waco 2002, no pet.).

cally addressing the use of promissory estoppel under Section 2.201. A strong dissenting opinion criticized the majority for creating “a new cause of action not previously recognized by the Texas Supreme Court or this court.”³⁷

B. BATTLE OF THE FORMS

A continuing problem arising between sellers and buyers is the exchange of forms that agree on fundamental aspects of a sale (price, quantity, delivery dates, and the like), but disagree on issues affecting the rights and responsibilities of the respective parties (scope of warranty coverage, limitation of remedy, right to arbitrate disputes, and other matters of this kind). This problem is commonly termed the “Battle of the Forms.” Section 2.207 of the Code provides a complex series of provisions attempting to deal with the exchange of mis-matched forms, but the difficulties with this section have been described as “legion.”³⁸

In *Wade & Sons, Inc. v. American Standard, Inc.*,³⁹ a Section 2.207 issue arose in conjunction with the exchange of forms between a buyer of commercial air-conditioning units and the seller who manufactured the units. After delays occurred in installation of the air-conditioning units under a construction contract, the buyer was terminated as the subcontractor for that portion of the contract. The buyer sued the seller for damages resulting from its termination. The seller defended by asserting provisions limiting its liability that were contained in a page of “Standard Terms and Conditions” allegedly attached to the original proposal it had sent to the buyer. The buyer contended that the terms and conditions had not been included in the original proposal and that the terms and conditions were proposals for addition to the contract because the seller’s acceptance of the buyer’s purchase order (which was sent to the seller after the seller’s proposal had been received) operated as an effective acceptance of the buyer’s terms. The proposed additions to the contract, therefore, materially altered the terms of the buyer’s purchase order and did not become part of the contract.⁴⁰

The trial court, sitting without a jury, found that the evidence supported the seller’s contention that the terms and conditions were attached to the seller’s original proposal.⁴¹ Because the buyer’s purchase order indicated that the order was for air-conditioning units “as specifically detailed in the proposal,” the terms and conditions attached to the seller’s acknowledgement of the buyer’s purchase order were not proposals for additions to the contract, but were incorporated by reference in the

37. *Id.* at 48.

38. Rusch, *supra* note 35, at 56-57. Section 2-207 is another of the sections that has been revised in the 2003 Official Text of the Code and discussed in the cited article. *Id.*

39. *Wade & Sons, Inc. v. Am. Standard, Inc.*, No. 04-02-00857-CV, 2003 WL 22955938 (Tex. App.—San Antonio, December 17, 2003, pet. filed) (Opinion not yet released for publication.).

40. *Id.* at *1-3.

41. *Id.* at *2.

buyer's purchase order and were part of the original contract that came into existence upon the seller's acknowledgement and acceptance of the purchase order.⁴² On appeal, the court ruled that the evidence supported the factual determination of the trial court that the terms and conditions were not proposals for additional terms, but were part of the initial contract.⁴³ The court, therefore, did not need to reach the issue of whether the limitation of liability terms materially altered the contract.⁴⁴

C. OPEN PRICE TERMS

In *HRN, Inc. v. Shell Oil Co.*,⁴⁵ several hundred retail gas station operators who leased stations from Shell sued Shell for allegedly forcing them out of business by raising the price of gasoline to a level that prevented them from effectively competing with gas stations owned and operated by the seller. The dealers argued that Section 2.305 of the Code governing open-price terms includes a duty that a price set by the seller must be a price set in good faith. The trial court rejected this argument and granted summary judgment in favor of the seller. On appeal, the court discussed *Mathis v. Exxon Corp.*,⁴⁶ where the court held that Section 2.305 requires that prices set under an open price term must satisfy both subjective and objective duties of good faith.⁴⁷ The court approved the reasoning in *Mathis* and adopted the same interpretation of Section 2.305. The judgment of the trial court was reversed and the case was remanded as to those dealers whose claims had been effectively preserved on appeal.⁴⁸

D. OUTPUT, REQUIREMENTS, AND EXCLUSIVE DEALINGS

Chapter 2 of the Code applies to transactions in goods.⁴⁹ In *Natural*

42. *Id.* at *1.

43. *Id.* at *4.

44. *Id.*

45. *HRN, Inc. v. Shell Oil Co.*, 102 S.W.3d 205 (Tex. App.—Houston [14th Dist.] 2003, pet. granted).

46. *Mathis v. Exxon Corp.*, 302 F.3d 448 (5th Cir. 2002).

47. TEX. BUS. & COM. CODE ANN. § 2.103(a)(2) (Vernon 1994) provides that “‘Good Faith’ in the case of a merchant means honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade.” The “honesty in fact” branch of this definition is regarded as a subjective test of good faith while the “observance of reasonable commercial standards” branch is regarded as stating an objective test. Revised Chapter 1 now incorporates both tests. See TEX. BUS. & COM. CODE ANN. § 1.201(b)(20) (Vernon Supp. 2004). The definition in former Chapter 1 only required “honesty in fact.” See TEX. BUS. & COM. CODE ANN. § 1.201(19) (Vernon 1994). Because both *Mathis* and *Shell* involved interpretation of the provisions of Chapter 2, both the subject and objective parts of the test of good faith were applicable in those cases. *Mathis* is discussed in John Krahmer, *Commercial Transactions*, 56 SMU L. REV. 1255, 1260-61 (2003).

48. *HRN, Inc.*, 102 S.W.3d at 213-14, 219. Among the several hundred dealers who were plaintiffs in this case, twenty-seven had signed releases and eight dealers had not responded to discovery requests. As to these dealers, the court upheld the judgment of the trial court in favor of the seller. See *id.* at 219.

49. TEX. BUS. & COM. CODE ANN. § 2.102 (Vernon 1994) provides, in part, that “this chapter applies to transactions in goods.” “Goods” are defined in TEX. BUS. & COM. CODE ANN. § 2.105 (Vernon 1994) as “all things (including specially manufactured goods) which

Gas Clearinghouse v. Midgard Energy Co.,⁵⁰ a natural gas processor sued a gathering system operator for breach of a contract to supply natural gas. The contract required the system operator to supply a specified quantity of gas, including all constituents, for a period of five years. After the system operator sold its rights in the system to another company, the operator ceased delivery of gas. The court held that the sale of natural gas and its constituents is a sale of goods governed by Chapter 2.⁵¹ The system operator contended that the obligation to deliver gas was dependent upon its continued ownership of the gathering system. The court disagreed, stating that nothing in the contract tied the duty to deliver to the continued ownership of the gathering system. The court analogized this case to one "in which Farmer X agrees to deliver to Buyer Y 1000 bushels of wheat. Farmer X cannot then deliver the bushels to Z and profess immunity from suit by Y because he no longer had the wheat when it came time to deliver it to Y."⁵² The court rejected an argument by the system operator that this case was controlled by the decision in *Northern Natural Gas Co. v. Conoco, Inc.*⁵³ The court distinguished *Northern* on the ground that the contract in *Northern* contemplated that the gas supply could vary from time to time and there was no requirement that the supplier buy additional gas from other suppliers to meet any of the delivery requirements under the contract at issue in that case.

E. NOTICE OF TERMINATION

Contracts between distributors and manufacturers for the distribution of goods are governed by Chapter 2.⁵⁴ Although distributorship contracts may provide that a distributorship will continue for a specified period of time, many distributorship contracts are terminable at will. Section 2.309 of the Code requires that termination by one party be by reasonable notification given to the other party.⁵⁵

In *Coburn Supply Co. v. Kohler Co.*,⁵⁶ a manufacturer notified a distributor that the distributorship would be terminated at the end of the year. During the 105 days that remained between the time notice was

are movable at the time of identification to the contract for sale other than the money in which the price is to be paid, investment securities, (Chapter 8) and things in action."

50. *Natural Gas Clearinghouse v. Midgard Energy Co.*, 113 S.W.3d 400 (Tex. App.—Amarillo 2003, pet. filed).

51. *Id.* at 408, n.3.

52. *Id.* at 409.

53. *N. Natural Gas Co. v. Conoco, Inc.*, 939 S.W.2d 676 (Tex. App.—El Paso, 1996), *aff'd in part, rev'd in part*, 986 S.W.2d 603 (Tex. 1998).

54. *See, e.g.*, *Cont'l Casing Corp. v. Siderca Corp.*, 38 S.W.3d 782, 788 (Tex. App.—Houston [14th Dist.] 2001, no pet.); *Glenn Thurman, Inc. v. Moore Const., Inc.*, 942 S.W.2d 768, 771 (Tex. App.—Tyler 1997, no writ).

55. TEX. BUS. & COM. CODE ANN. § 2.309(c) (Vernon 1994). The Official Comment to that section provides, in part, that "application of principles of good faith and sound commercial practice normally call for such notification of the termination of a going contract relationship as will give the other party reasonable time to seek a substitute arrangement." TEX. BUS. & COM. CODE ANN. § 2.309 cmt. 8 (Vernon 1994).

56. *Coburn Supply Co. v. Kohler Co.*, 342 F.3d 372 (5th Cir. 2003).

given and the end of the year, the distributor successfully arranged a new distributorship agreement with another manufacturer. Despite obtaining this new arrangement, the distributor sued for breach of an obligation to give reasonable notice of termination and for negligent misrepresentation that the distributorship would continue. The jury found that the manufacturer had breached its duty to give reasonable notice of termination, but awarded zero damages for lost profits following the termination.⁵⁷ Damages in excess of two million dollars were awarded, however, for other damages proximately caused by the termination.⁵⁸ Judgment was entered on the jury verdict. The court of appeals reversed, ruling that no reasonable jury could find that 105 days notice was inadequate when the distributor was able to arrange an alternate source of supply within six weeks after receiving notice of termination.⁵⁹

F. WARRANTIES

In a series of cases decided in the 1970s, the Texas Supreme Court made it clear that claims for economic loss are governed by contract law and not by the standards of tort law applied in strict liability actions. The seminal case in this series was *Nobility Homes of Texas, Inc. v. Shivers*,⁶⁰ where the purchaser of a mobile home sued a remote manufacturer for defects in the home on theories of negligence, strict liability in tort, and breach of implied warranty. As stated by the supreme court, "The important issues in this case are whether Section 402A of the Restatement (Second) of Torts or the implied warranties of the Uniform Commercial Code allow a consumer to recover his economic loss against a manufacturer with whom the consumer is not in privity."⁶¹ The supreme court held that damages for economic loss were not recoverable under the strict liability rule of Section 402A, but were recoverable without regard to privity for breach of implied warranty.⁶²

Within a year, the Texas Supreme Court revisited this issue in two cases decided on the same day and reported "back-to-back" in the reports. In *Mid Continent Aircraft Corp. v. Curry County Spraying Service, Inc.*,⁶³ the supreme court held that a product defect that damages only the product itself could not be maintained as a strict liability action, but, in *Signal Oil & Gas Co. v. Universal Oil Products*,⁶⁴ the supreme court, referring to the decision in *Mid Continent*, stated,

[W]here only the product itself is damaged, such damage constitutes economic loss recoverable only as damages for breach of an implied

57. *Id.* at 374.

58. *Id.*

59. *Id.* at 377.

60. *Nobility Homes of Tex., Inc. v. Shivers*, 557 S.W.2d 77 (Tex. 1977).

61. *Id.* at 78.

62. *Id.*

63. *Mid Continent Aircraft Corp. v. Curry County Spraying Serv., Inc.*, 572 S.W.2d 308 (Tex. 1978).

64. *Signal Oil & Gas Co. v. Universal Oil Prods.*, 572 S.W.2d 320 (Tex. 1978).

warranty under the Code. In the instant case [the plaintiff] has alleged property damages in the form of damages to the product itself, *as well as to other surrounding property* To the extent that the product itself has become part of the accident risk or the tort by causing collateral property damage, it is properly considered as part of the property damages, rather than as economic loss.⁶⁵

The supreme court went on to hold that, even though a claim in strict liability was proper due to the allegations of damage to other property, the plaintiff failed to obtain favorable jury findings on causation and judgment against the plaintiff was affirmed on the strict liability issue.⁶⁶

In *Murray v. Ford Motor Co.*,⁶⁷ the court addressed an issue raised by these cases that had been lying dormant for almost thirty years: If a defective product damages both itself as well as other property, does a strict liability claim lie for both the damage to the product as well as the damage to other property, or is the claim limited to the damage caused to other property? In *Murray*, the issue arose when a pickup truck caught fire due to an electrical failure. The fire destroyed the truck as well as personal property worth \$453.25 that was in the truck at the time of the fire. While a breach of warranty claim was barred by the statute of limitations, a strict liability claim was still timely.⁶⁸

The plaintiffs argued that *Signal Oil* permitted a tort action for all damages when "other property" was damaged by a defective product. In reviewing the *Nobility Homes*, *Mid Continent*, and *Signal Oil* trilogy, however, the court reasoned that the statement made by the court in *Signal Oil*, which seemingly permitted such recovery, was mere dicta because the jury had failed to find causation and judgment had been entered against the plaintiff on the strict liability claim. The remarks about "other property" were, therefore, unnecessary to the decision. Since there were apparently no Texas cases on point, the court turned to two United States Supreme Court cases⁶⁹ and one Fifth Circuit case⁷⁰ to determine that when a defective product damages both itself as well as other property, the economic loss doctrine still bars recovery in tort for any damage to the product itself. Under this rule, therefore, the plaintiffs could maintain a tort claim for the damage to the \$453.25 worth of other property, but were limited to bringing a breach of warranty claim for damage to the truck itself. Since the warranty claim was barred by limita-

65. *Id.* at 325 (emphasis added).

66. *Id.* at 325-26.

67. *Murray v. Ford Motor Co.*, 97 S.W.3d 888 (Tex. App.—Dallas 2003, no pet.)

68. *Id.* at 890. Under TEX. BUS. & COM. CODE ANN. § 2.725 (Vernon 1994), a limitations period of four years begins to run upon tender of the goods, but under TEX. CIV. PRAC. & REM. CODE § 16.003 (Vernon Supp. 2004) a tort claim can be brought within two years after the tort injury takes place. Because the truck had been purchased more than four years before the fire occurred, the breach of warranty claim was barred, but an action in tort could be brought within two years after the fire. *Murray*, 97 S.W.3d at 890.

69. *Saratoga Fishing Co. v. J.M. Martinac & Co.*, 520 U.S. 875 (1997); *E. River S.S. Corp. v. Transamerica Delaval, Inc.*, 476 U.S. 858 (1987).

70. *McDermott, Inc. v. Clyde Iron*, 979 F.2d 1068 (5th Cir. 1992), *rev'd in part on other grounds*, 511 U.S. 202 (1994).

tions, the trial court's judgment against the plaintiffs was affirmed on that cause of action, but the judgment was reversed and remanded on the claim for damage to the other property.⁷¹ Whether the court's interpretation of *Signal Oil* is correct must ultimately await a decision by the Texas Supreme Court.

In another case involving an issue on which the Texas Supreme Court has not authoritatively spoken, the court in *U.S. Tire-Tech, Inc. v. Boeran, B.V.*⁷² reviewed two lines of authority that have developed in Texas on whether privity of contract is required in actions brought by a buyer against a remote manufacturer for breach of express warranty. The court noted that, while it was clear that *Nobility Homes* permitted actions for breach of implied warranty without regard to privity, there was disagreement among the courts of appeal on whether the same rule applied to actions for breach of express warranty. An older line of cases requires privity.⁷³ A more recent line of cases holds that privity is not required.⁷⁴ Based on the reasoning in the more recent line of cases, and on the policy underlying *Nobility Homes* to prevent unscrupulous manufacturers from being insulated from liability while still making representations about the performance of their products, the court held that privity of contract was not required in the buyer's action for breach of express warranty.⁷⁵

The same court also addressed the question of whether a buyer is required to give notice of breach to the remote manufacturer to avoid the bar imposed by Section 2.607(c)(1) of the Code.⁷⁶ The court noted that the Texas Supreme Court had recognized a split between the lower courts on this issue and had expressly reserved judgment on the matter in *Wilcox v. Hillcrest Memorial Park of Dallas*⁷⁷ but had never revisited the issue. The court reasoned that, to be consistent with its rejection of a

71. *Murray*, 97 S.W.3d at 893. The economic loss rule as applied in *Murray* has been followed in *Equistar Chems., L.P. v. Dresser-Rand Co.*, 123 S.W.3d 584, 591-92 (Tex. App.—Houston [14th Dist.] 2003, no pet. h.); *Plunkett v. Toyota Motor Sales, U.S.A., Inc.*, No. 05-02-00867-CV, 2003 WL 352038, at *1 (Tex. App.—Dallas, Feb. 18, 2003, no pet.).

72. *U.S. Tire-Tech, Inc. v. Boeran, B.V.*, 110 S.W.3d 194 (Tex. App.—Houston [1st Dist.] 2003, pet. denied).

73. The cases cited by the court for this proposition were as follows: *Tex. Processed Plastics, Inc. v. Gray Enters. Inc.*, 592 S.W.2d 412, 415 (Tex. Civ. App.—Tyler 1979, no writ); *Henderson v. Ford Motor Co.*, 547 S.W.2d 663, 667 (Tex. Civ. App.—Amarillo 1977, no writ); *Pioneer HiBred Int'l, Inc. v. Talley*, 493 S.W.2d 602, 607-08 (Tex. Civ. App.—Amarillo 1973, no writ); and *Eli Lilly & Co. v. Casey*, 472 S.W.2d 598, 600 (Tex. Civ. App.—Eastland 1971, writ dism'd).

74. The court cited the following cases on this point: *Edwards v. Schuh*, 5 S.W.3d 829, 833 (Tex. App.—Austin 1999, no pet.); *Church & Dwight Co. v. Huey*, 961 S.W.2d 560, 568 (Tex. App.—San Antonio 1997, pet. denied); *Nat'l Bugmobiles, Inc. v. Jobi Props.*, 773 S.W.2d 616, 622 (Tex. App.—Corpus Christi 1989, writ denied); and *Indust-Ri-Chem Lab., Inc. v. Par-Pak Co., Inc.*, 602 S.W.2d 282, 287-88 (Tex. Civ. App.—Dallas 1980, no writ).

75. *U.S. Tire-Tech*, 110 S.W.3d at 197-98.

76. TEX. BUS. & COM. CODE ANN. § 2.607(c)(1) (Vernon 1994) provides that "the buyer must within a reasonable time after he discovers or should have discovered any breach notify the seller of breach or be barred from any remedy."

77. *Wilcox v. Hillcrest Mem'l Park*, 701 S.W.2d 842, 843 (Tex. 1986). In *Wilcox*, the supreme court acknowledged that the El Paso Court of Appeals had reached a contrary result in *Vintage Homes, Inc. v. Coldiron*, 585 S.W.2d 886, 888 (Tex. Civ. App.—El Paso 1979, no writ).

privity requirement to permit warranty actions against a remote manufacturer, the manufacturer should be entitled to notice of breach.⁷⁸ Because the buyer failed to give such notice, judgment was rendered against the buyer.⁷⁹

G. REMEDIES FOR BREACH

In *Neal v. SMC Corp.*,⁸⁰ the court also considered the question of notice to a remote manufacturer, but in the context of revocation of acceptance rather than in the context of breach of warranty.⁸¹ The court characterized the issue as “[w]hether a manufacturer is a ‘seller’ under Section 2.608 of the UCC” and noted that this was an issue of first impression in Texas.⁸² Reasoning that revocation of acceptance is a contract claim rather than a breach of warranty claim, the court held that privity of contract was required between the buyers and the manufacturer.⁸³ Because there was no privity between the buyers and the manufacturer, revocation of acceptance was effective only between the buyers and their immediate seller but not against the remote manufacturer.⁸⁴

In *McManus v. Fleetwood Enterprises, Inc.*,⁸⁵ the focus was on the damages recoverable for breach of the warranty of merchantability in the certification of a class action against a seller of motor homes. The defendant contended that the class should not be certified because the measure of damages could vary from one plaintiff to another. The court pointed out, however, that the class representatives were seeking damages based on the difference between the actual value of the motor homes as delivered and the value they would have had if they had been delivered as warranted. Because this measure of damage would not vary from plaintiff to plaintiff, class certification was proper under Federal Rule of Procedure 23(b)(3).⁸⁶

78. *U.S. Tire-Tech*, 110 S.W.3d at 198-99.

79. *Id.* at 203.

80. *Neal v. SMC Corp.*, 99 S.W.3d 813 (Tex. App.—Dallas 2003, no pet.).

81. TEX. BUS. & COM. CODE ANN. § 2.608 (Vernon 1994) permits a buyer to revoke acceptance of goods for non-conformities that substantially impair the value of the goods. Notice of revocation must be given within a reasonable time after the buyer discovers or should have discovered the grounds for revocation.

82. *Neal*, 99 S.W.3d at 815.

83. *Id.* at 817-18.

84. *Id.* at 818.

85. *McManus v. Fleetwood Enters., Inc.*, 320 F.3d 545 (5th Cir. 2003).

86. *Id.* at 546. Although the court held that certification was proper under Fed. R. Civ. Proc. 23(b)(3) for breach of the implied warranty of merchantability, the court also held that certification was not proper in regard to the plaintiffs' claim for breach of express warranty because individual proof of reliance would be required for each class member. Certification under Fed. R. Civ. Proc. 23(b)(2) was also denied on the plaintiffs' claim for injunctive relief because damage recovery under Rule 23(b)(3) would be the superior remedy since it would preserve the notice and opt-out protections for members of the class who might be able to prove damages in excess of the benefit of the bargain measure sought for breach of the implied warranty of merchantability. *Id.* at 552-54.

III. LEASES OF GOODS

Chapter 2A of the Code governs leases of goods.⁸⁷ Many of the provisions in Chapter 2A parallel those of Chapter 2. For example, both contain a statute of frauds, similar provisions on contract formation and construction, and warranties.⁸⁸ As with Chapter 2, however, there is a penumbra surrounding Chapter 2A where case law may have an effect on a commercial transaction that goes beyond the statute. Under Chapter 2, one example is the decision in *Melody Home Manufacturing Co. v. Barnes*,⁸⁹ where the Texas Supreme Court created a warranty of good workmanship in the repair or modification of existing tangible goods or property. Although this warranty is not one that exists under Chapter 2 itself, it has an obvious effect on the repair of goods, whether or not such repairs are made under a warranty that accompanied the goods at the time of sale. In *Anthony Equipment Corp. v. Irwin Steel Erectors, Inc.*,⁹⁰ the court addressed the question of whether a similar warranty should be implied in the lease of a construction crane. The transaction involved the lease of the crane itself along with the services of a crane operator from the same lessor for the purpose of putting a large steel truss in place during construction of a roof for an arena. When the truss reached the correct level, the operator released his end of the truss without being instructed to do so. The truss fell some eighty feet to the ground and damaged both the arena and the crane. The lessee sued the lessor for, *inter alia*, negligence and breach of an implied warranty to perform in a good and workmanlike manner.

The lessee succeeded on the negligence claim but, on the warranty claim, citing and discussing *Melody Home*, the court held that there was no compelling need to create an implied warranty that the services of the operator would be performed in a good and workmanlike manner because other adequate remedies were available to the lessee, including negligence, an issue on which this very lessee had prevailed.⁹¹ As to *Melody Home* itself, the court noted that it was not controlling in this case because the services of the crane operator were for the purpose of lifting the truss, not for the repair or modification of tangible goods or property.⁹²

87. TEX. BUS. & COM. CODE ANN. § 2A.101 to .532 (Vernon 1994).

88. Compare TEX. BUS. & COM. CODE ANN. § 2.201 (Vernon 1994), with TEX. BUS. & COM. CODE ANN. § 2A.201 (Vernon 1994) (Statute of Frauds); TEX. BUS. & COM. CODE ANN. § 2.202-210 (Vernon 1994), with TEX. BUS. & COM. CODE ANN. § 2A.202-221 (Vernon 1994) (contract formation and construction); and TEX. BUS. & COM. CODE ANN. § 2.312-315 (Vernon 1994), with TEX. BUS. & COM. CODE ANN. § 2A.210 to .213 (Vernon 1994) (warranties).

89. *Melody Home Mfg. Co. v. Barnes*, 741 S.W.2d 349 (Tex. 1987).

90. *Anthony Equip. Corp. v. Irwin Steel Erectors, Inc.*, 115 S.W.3d 191 (Tex. App.—Dallas 2003, pet. dism'd).

91. *Id.* at 209.

92. *Id.*

IV. NEGOTIABLE INSTRUMENTS AND BANK TRANSACTIONS

A. FORM OF INSTRUMENTS

Under Chapter 3 of the Code, the form of an instrument is critical. Unless the formal requirements of Section 3.104 are met, the instrument is not negotiable and is not governed by Chapter 3.⁹³ As a general matter, Section 3.104 requires instruments to be payable to bearer or order, be payable on demand or at a definite time, contain an unconditional promise to pay a fixed amount of money and, with three exceptions, contain no other promises by the obligor to perform any act other than the payment of money.⁹⁴ One of the exceptions permits the waiver of any law intended for the advantage or protection of the obligor.⁹⁵

In *In re Wells Fargo Bank Minnesota, N.A.*,⁹⁶ the makers signed a note waiving the right of trial by jury and providing that Louisiana law would govern the rights of the parties under the note. Suit was brought in Texas. The court was thus faced with the questions of whether Louisiana law or Texas law would apply and whether the contractual waiver of the right to jury trial was enforceable. Reviewing both Louisiana law and Texas law, the court found that both jurisdictions enforced contractual jury waivers.⁹⁷ There was, therefore, no conflict that the court needed to resolve. On the issue of the enforceability of the waiver, the court determined that the waivers had been signed by the obligors knowingly and voluntarily.⁹⁸ A writ of mandamus was conditionally granted instructing the trial court to remove the case from the jury docket.⁹⁹

B. ENFORCEMENT OF INSTRUMENTS

In *Parker v. Dodge*,¹⁰⁰ a debtor borrowed some \$120,000 evidenced by a note calling for repayment at the rate of \$1,000 per month with a balloon payment at the end of ten years. The note was issued in 1990 and the debtor made one payment in December of that year. No further payments on the note were ever made. In 2001, the creditor sued on the note and obtained a summary judgment for installments and interest that had not been paid during the preceding six years. The debtor appealed, arguing that the limitations period on the note under Section 3.118(b) was ten years and that the creditor's action was, therefore, barred.¹⁰¹ The court correctly pointed out that, while the limitations period on a demand note

93. See TEX. BUS. & COM. CODE ANN. §§ 3.102, 3.104 (Vernon 2002).

94. See TEX. BUS. & COM. CODE ANN. § 3.104(a) (Vernon 2002).

95. *Id.*

96. *In re Wells Fargo Bank Minn., N.A.*, 115 S.W.3d 600 (Tex. App.—Houston [14th Dist.] 2003, no pet.).

97. *Id.* at 606-08.

98. *Id.* at 610.

99. *Id.* at 612.

100. *Parker v. Dodge*, 98 S.W.3d 297 (Tex. App.—Houston [1st Dist.] 2003, no pet.).

101. TEX. BUS. & COM. CODE ANN. § 3.118 (Vernon 2002) states the limitation periods applicable to various types of negotiable instruments.

is ten years, the note on which the suit was based was a note payable at a definite time at the rate of \$1,000 per month.¹⁰² Actions on notes payable at a definite time are governed by the six-year limitations period in Section 3.118(a). The creditor, therefore, was entitled to recover payments due within six years of the date of the filing of the petition, but recovery of payments due more than six years earlier was barred.¹⁰³

The debtor argued that the equitable doctrine of laches should apply. While the court noted that this argument might have some merit based on unreasonable delay in filing suit if the note were a demand note with no demand and with no payments being made since 1990, this note was a note payable at a definite time with the date of the last payment (the balloon payment) due in 2000.¹⁰⁴ Suit was filed in 2001, well within the limitations period. The court rejected the defense of laches as well as a defense of inadequate consideration and upheld summary judgment in favor of the creditor.¹⁰⁵

In *Sixth RMA Partners, L.P. v. Sibley*¹⁰⁶ and *Nowak v. DAS Investment Corp.*,¹⁰⁷ the enforcement issues before the courts were largely procedural in nature. In *Sibley*, the Texas Supreme Court ruled that an objection to use of a supplemental pleading instead of an amendment to the original pleading to substitute the plaintiff noteholder's legal name was waived where the defendant maker failed to file a special exception.¹⁰⁸ The supreme court also ruled that the failure of the noteholder to file an assumed name certificate was not fatal to enforcement of the note when the defendant did not raise the failure to file in any pleading or motion in the trial court.¹⁰⁹

In *Nowak*, the noteholders sued for recovery on a demand note that had been issued in 1990. Demand was first made for payment in 2000 and suit was filed in 2001. The defendant filed a no-evidence summary judgment motion on the ground that the action was barred because it had been brought more than four years after the note was executed. The noteholders argued that their claim accrued at the time of demand rather than at the time of execution. The court held that the defendant's no-evidence motion did not properly raise the limitations issue because limitations is an affirmative defense that must be shown by the moving party.¹¹⁰ The court pointed out that a no-evidence motion shifts the burden of proof to the opposing party and that proof that no affirmative defense exists is not part of a plaintiff's cause of action.¹¹¹ Summary judgment of the trial

102. *Parker*, 98 S.W.3d at 300-01.

103. *Id.* at 301.

104. *Id.*

105. *Id.* at 301-02.

106. *Sixth RMA Partners, L.P. v. Sibley*, 111 S.W.3d 46 (Tex. 2003).

107. *Nowak v. DAS Inv. Corp.*, 110 S.W.3d 677 (Tex. App.—Houston [14th Dist.] 2003, no pet.).

108. *Sibley*, 111 S.W.3d at 54-55.

109. *Id.* at 56.

110. *Nowak*, 110 S.W.3d at 679-80.

111. *Id.* at 680.

court in favor of the defendant was reversed and the case was remanded.

V. BANK TRANSACTIONS

In *Carson Energy, Inc. v. Riverway Bank*,¹¹² a depositor sought to avoid the rule of Section 3.420 prohibiting conversion actions by the issuer of an instrument by asserting claims for breach of a bailment contract, breach of a deposit agreement, and negligence.¹¹³ The deposit account in question was established to hold contributions of working-interest owners in oil and gas wells. The funds were not to be released to the driller until work was completed on the specific project for which the account was established. Under the account agreement with the bank, two signatures were required for the withdrawal of funds and faxed instructions were not to be honored by the bank. Despite these requirements, the bank permitted the withdrawal of funds by faxed instructions that contained only one of the two required signatures.¹¹⁴

The court held that the deposit agreement did not state that the funds were to be held as a "special deposit." Absent a clear direction that the funds were to be so held, and absent agreement by the bank that it would so hold the funds, the deposit was a mere "general deposit" that would not give rise to a claim for breach of a bailment contract.¹¹⁵ Furthermore, the deposit agreement did not indicate that the non-signing party was an intended beneficiary of the deposit agreement or that this party was a representative of the named depositor. Without such indication, the non-signer was not in privity with the bank, nor a third-party beneficiary who had standing to object to the bank's handling of the account.¹¹⁶ As to the negligence claim, the court held that Texas law requires the violation of a duty imposed by law independent of any contract. Citing *Southwestern Bell Telephone Co. v. DeLanney*,¹¹⁷ the court stated, "Where the only duty between parties arises from a contract, a breach of this duty will ordinarily sound only in contract, not in tort."¹¹⁸ Summary judgment in favor of the bank was upheld.¹¹⁹

In *Jureczki v. Banc One Texas, N.A.*,¹²⁰ an arbitration provision in a deposit agreement was held to be enforceable against a depositor, not only by the bank in which the account was maintained, but by affiliates of the bank that were not signatories to the agreement. The court noted that non-signatories can compel arbitration under an equitable estoppel the-

112. *Carson Energy, Inc. v. Riverway Bank*, 100 S.W.3d 591 (Tex. App.—Texarkana 2003, pet. denied).

113. TEX. BUS. & COM. CODE ANN. § 3.420(a) (Vernon 2002) provides, in part, that "[a]n action for conversion of an instrument may not be brought by (i) the issuer or acceptor of the instrument."

114. *Riverway Bank*, 100 S.W.3d at 596-97.

115. *Id.* at 597-99.

116. *Id.* at 600.

117. *S.W. Bell Tel. Co. v. DeLanney*, 809 S.W.2d 493 (Tex. 1991).

118. *Riverway Bank*, 100 S.W.3d at 601.

119. *Id.*

120. *Jureczki v. Banc One Tex.*, 252 F. Supp. 2d 368 (S.D. Tex. 2003).

ory in two circumstances. First, when a signatory must rely on the terms of the written contract in asserting its claims against the non-signatory. Second, when the signatory asserts claims of interdependent and concerted misconduct by the non-signatory and one or more of the other signatories to the contract.¹²¹ The court found that the non-signatories met both circumstances because the plaintiffs' claims were all based on the allegedly wrongful withdrawal of funds from a deposit account and the allegations included assertions that the defendants had acted in concert.¹²² The defendants' motion to compel arbitration was granted.¹²³

In *Fetter v. Wells Fargo Bank Texas, N.A.*,¹²⁴ a customer sought injunctive relief against a bank to prohibit the bank from paying checks in a "highest to lowest" order. The customer contended that the bank had breached its duty of good faith under Sections 4.303 and 1.203 of the Code because the high to low posting was not done for any legitimate business purpose other than to maximize fees.¹²⁵ In making this argument, the customer referred to the Texas State Bar Committee's Comment to UCC Section 4.303 which, in part, states that while a bank has great discretion under subsection (b), the bank must continue to act in good faith in establishing policies.¹²⁶ This Comment includes an example specifically relating to high to low posting used simply to increase fees and opines that this practice would be inappropriate. The customer also contended that by failing to perform its duties in good faith, the bank breached the account agreement which governed the relationship between the bank and the customer. The bank moved for summary judgment on the ground that the customer's claim failed as a matter of law because Section 4.303 allows posting in any order, and the account agreement itself also authorized high to low posting.¹²⁷

The court held that the posting of checks from highest to lowest dollar amount was specifically permitted by the Code and by the account agreement and, therefore, it did not violate the duty of good faith.¹²⁸ In regard to the State Bar Committee Comment, the court concluded there was no evidence that this Comment was written prior to the enactment of Section 4-303.¹²⁹ The plain language of the statute allows high to low posting, and there was no indication that the legislature did not realize the broad

121. *Id.* at 376 (citing *Grigson v. Creative Artists Agency, L.L.C.*, 210 F.3d 524, 527 (5th Cir. 2000)).

122. *Id.*

123. *Id.* at 380.

124. *Fetter v. Wells Fargo Bank Tex., N.A.*, 110 S.W.3d 683 (Tex. App.—Houston [14th Dist.] 2003, no pet.).

125. TEX. BUS. & COM. CODE ANN. § 4.303 (Vernon 2002) governs the order in which checks may be paid and TEX. BUS. & COM. CODE ANN. § 1.203 (Vernon 2002) (now TEX. BUS. & COM. CODE ANN. § 1.304 (Vernon 2004)) provides that a duty of good faith applies to every contract or duty within the scope of the Code.

126. TEX. BUS. & COM. CODE ANN. State Bar Committee Comment § 4.303 (Vernon 2002).

127. *Fetter*, 110 S.W.3d at 684-86.

128. *Id.* at 687-88.

129. *Id.* at 688-89.

language of the statute when it was enacted. The court, therefore, declined to view the Comment as persuasive authority.¹³⁰ The court also declined to find that the bank breached the account agreement.¹³¹ The trial court's decision granting summary judgment in favor of the bank was affirmed.¹³²

In *Texas Commerce Bank v. Grizzle*,¹³³ several trusts had been created by court order for the benefit of minors who were entitled to receive payments from the settlement of lawsuits. A mother, suing as next friend of a trust beneficiary, charged that banks serving as trustees of the trusts had engaged in self-dealing by merging and liquidating trust funds that caused the trusts to suffer losses. Several issues concerning the trusts were resolved in the lower courts. However, one of the principal issues concerned the effect of an exculpatory clause.¹³⁴

On appeal to the Texas Supreme Court, the plaintiff argued that this clause did not absolve a trustee from liability for self-dealing by liquidating trust assets and investing in its own stock. The supreme court held that Section 113.059 of the Texas Trust Code applied, not only to trusts voluntarily created by a settlor, but also to trusts created by court decree to manage funds for a minor's benefit. Under the Trust Code, an exculpatory clause was effective to relieve a corporate trustee from liability for self-dealing.¹³⁵

The supreme court also considered the question of whether the trustees' actions amounted to gross negligence, bad faith, or fraud. The beneficiary argued that the failure of the banks to notify beneficiaries of a proposed merger, and a delay in reinvesting trust funds, fell within these categories. The supreme court held otherwise, noting that the trust instrument contained no provisions requiring disclosure of proposed mergers.¹³⁶ In addition, a delay of no more than "several days" in reinvesting the trust funds, did not give rise to liability, particularly where the funds were held in an interest-bearing account during that time.¹³⁷

The supreme court concluded by stating, "In short, [the beneficiary] failed to create a fact issue that [the banks] acted or failed to act as a result of gross negligence, bad faith, or fraud. We accordingly hold that

130. *Id.* at 688.

131. *Id.* at 691.

132. *Id.*

133. *Tex. Commerce Bank v. Grizzle*, 96 S.W.3d 240 (Tex. 2002).

134. *Id.* at 244, 247. The exculpatory clause provided; "This instrument shall always be construed in favor of the validity of any act or omission of any Trustee, and a Trustee shall not be liable for any act or omission except in the case of gross negligence, bad faith, or fraud." *Id.* at 243.

135. *Id.* at 248-49.

136. *Id.* at 253.

137. On this point, the supreme court quoted with approval from *New England Trust Co. v. Paine*, 59 N.E.2d 263, 272 (Mass. 1945), where the court stated, "At most, these [delays] were no more than failures to exercise the degree of judgment required in the circumstances. They did not amount to bad faith or to intentional breaches of trust or to reckless indifference to the interest of the beneficiaries." *Grizzle*, 96 S.W.3d at 253.

[the banks] are entitled to judgment as a matter of law. . . ."¹³⁸

VI. SECURED TRANSACTIONS

A. SCOPE OF CHAPTER 9

In addition to security interests in personal property and fixtures, Chapter 9 also covers agricultural liens, sales of accounts, chattel paper, payment intangibles, promissory notes, consignments, and statutory security interests arising under other Chapters of the Code.¹³⁹ Certain transactions falling within these general categories are, however, excluded from Chapter 9 as situations that do not generally involve commercial financing transactions. *Texas Development Co. v. Exxon Mobil Corp.*,¹⁴⁰ is one example of such an exclusion. In *Texas Development*, the issue before the court was whether the transaction involved the assignment of a single account in satisfaction of a preexisting indebtedness or whether the assignment was to secure future performance. The court held that if the assignment was for a preexisting indebtedness, it would not be within the scope of Chapter 9 but, if it secured future performance, it was covered by Chapter 9.¹⁴¹ Because this was an issue of material fact on which neither party had presented evidence, summary judgment was reversed and the case was remanded.¹⁴² Although the case arose under the former Chapter 9, the court noted that the same exclusion still applies under revised Chapter 9 as well.¹⁴³

B. CREATION OF SECURITY INTERESTS

Unless a security interest comes into existence by operation of law under a provision contained in another chapter of the Code, a security agreement is necessary to create a security interest.¹⁴⁴ In *Alan Acceptance Corp. v. East Texas National Bank of Palestine*,¹⁴⁵ a dentist purchased dental equipment from a dental equipment company. The dentist used the equipment as collateral for a bank loan. A security agreement was signed and a financing statement was filed. The dentist later sought funds from another lender under a purported "sale and lease-back"

138. *Grizzle*, 96 S.W.3d at 255.

139. See TEX. BUS. & COM. CODE ANN. § 9.109(a)(1)-(6) (Vernon 2002).

140. *Tex. Dev. Co. v. Exxon Mobil Corp.*, 119 S.W.3d 875 (Tex. App.—Eastland 2003, no pet.)

141. *Id.* at 882-83.

142. *Id.* at 885.

143. *Id.* at 882.

144. See TEX. BUS. & COM. CODE ANN. § 9.203 (Vernon 2002). TEX. BUS. & COM. CODE ANN. §§ 2.401, 2.505, 2.711(c), 2A.509(e), 4.210, 5.118 (Tex. 1994 & 2002) are the provisions contained in other Chapters of the Code that automatically create security interests effective under Chapter 9.

145. *Alan Acceptance Corp. v. E. Tex. Nat'l Bank of Palestine*, 109 S.W.3d 511 (Tex. App.—Tyler 1998, no pet.). There is no indication in the opinion as to why a case decided in 1998 was published in 2003 in Volume 109 of the Southwestern Reporter. The facts of the case do, however, point up the need for a security agreement and this would remain so under revised Chapter 9.

agreement. When the dentist defaulted on both the bank loan and the lease, the lessor-lender repossessed some of the equipment, including some items not covered by the lease agreement. The bank sued the lessor-lender for conversion.¹⁴⁶

The trial court, sitting without a jury, found that the "sale" part of the "sale and lease-back" transaction never took place and that the lessor-lender never obtained a security interest in the equipment. On appeal, the court reviewed the record for factual sufficiency and determined that the trial court had made a correct finding. On this basis, judgment was affirmed in favor of the bank¹⁴⁷

C. ENFORCEMENT OF SECURITY INTERESTS

In *Morgan Buildings & Spas, Inc. v. Turn-Key Leasing, Ltd.*,¹⁴⁸ the court held that a waiver of a debtor's right to notice and commercially reasonable disposition of collateral was ineffective under the former Chapter 9. In its discussion, the court noted that revised Chapter 9 also prohibits the waiver of these rights and that, at most, an agreement can establish the standards for the disposition of collateral. Even if the agreement in question simply established such standards, the standards contained in the agreement were "manifestly unreasonable" under the former Sections 9.504 and 9.505 as well as revised Section 9.603.¹⁴⁹

146. *Id.* at 513-14.

147. *Id.* at 514-17.

148. *Morgan Bldgs. & Spas, Inc. v. Turn-Key Leasing, Ltd.*, 97 S.W.3d 871 (Tex. App.—Dallas 2003, pet. denied).

149. *Id.* at 880-81.