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COMMERCIAL TRANSACTIONS

by

Peter Winship*

THIS is the eleventh *Annual Survey* of Texas commercial law published by the *Southwestern Law Journal*. The Uniform Commercial Code became effective in Texas in 1966,¹ the year first surveyed by these annual articles. As recently as 1971 the author of the *Annual Survey* noted that, while the number of decisions under the Code had increased, the decisions remained few in number, and only two were of any particular significance.² The *Survey* for 1976, however, reports a number of significant cases decided under the provisions of the Code as it is in force in Texas. The reported decisions illustrate a growing awareness of the Code and increasing sophistication in dealing with the Code's provisions.³ At the same time, many of the decisions reflect limitations in the scope of the Code and indicate that the attorney dealing with commercial matters must continue to be aware of statutes and common law outside the framework of the Uniform Commercial Code.

Several changes from previous *Survey* articles have been made in the scope and format of this *Survey*. In addition to the traditional classification of decisions under the headings of sales, negotiable instruments, secured transactions, and miscellaneous decisions, a new heading collects decisions interpreting the Code's general choice-of-law provision. Texas decisions with respect to creditors' rights are now dealt with in a separate *Survey* article.⁴ A section on legislation is not included because the Texas Legislature did not sit in 1976.⁵

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1. The Uniform Commercial Code [hereinafter referred to as "the Code"] became effective in Texas on July 1, 1966. 1965 Tex. Gen. Laws ch. 721, at 1-316. The Code was incorporated into the Texas Business and Commerce Code as the first ten chapters of this more comprehensive codification. 1967 *id.* ch. 785, § 1, at 2343 (effective Sept. 1, 1967). The Texas Code provisions have since been amended several times and they now generally conform with the Uniform Commercial Code, 1972 Official Text. 1969 *id.* ch. 830, §§ 1-11, at 2466-69; 1971 *id.* ch. 985, §§ 1-5, at 2987-88; 1971 *id.* ch. 1010, §§ 1-2, at 3048-49; 1973 *id.* ch. 400, §§ 1-9, at 997-1036; 1975 *id.* ch. 353, §§ 1-16, at 940-45. The 1977 legislative program of the Texas State Bar proposes several additional amendments. See note 5 *infra*. In this Article textual references are to the Uniform Commercial Code; footnote citations are to the Texas Business and Commerce Code.

2. Teofan, *Commercial Transactions, Annual Survey of Texas Law*, 25 Sw. L.J. 74, 87 (1971).

3. There continue to be cases where the attorneys apparently do not consider the relevance of the Code prior to trial. See, e.g., *Rusk County Elec. Coop. v. Flanagan*, 538 S.W.2d 498 (Tex. Civ. App.—Tyler 1976, writ ref'd n.r.e.) (court decides on common law of contract but notes same result under Code provisions [Query: Is "electricity" a "good" for the purposes of the Code?]); *Christian v. First Nat'l Bank*, 531 S.W.2d 832 (Tex. Civ. App.—Fort Worth 1975, writ ref'd n.r.e.) (Code provisions on repossession apparently not argued to court until rehearings); *Modular Technology Corp., Metal Bd. Div. v. City of Lubbock*, 529 S.W.2d 273 (Tex. Civ. App.—Amarillo 1975, writ ref'd n.r.e.) (relevance of § 2.311 not argued by attorneys but noted by the court).

4. See Dorsaneo, *Creditors' Rights*, p. 213 *infra*.

5. The 1977 legislative program of the Texas State Bar includes proposed amendments to the Code. See 40 TEX. B.J. 63 (1977). The program includes the following proposals: Amendments to Chapters 9 and 11, Business and Commerce Code relating to secured transactions. This would provide an easy means for the secured party to amend a financing statement without the signature of the debtor when (1) the

I. APPLICABILITY OF THE CODE

The Uniform Commercial Code incorporates several choice-of-law provisions. Section 1-105, the Code's general choice-of-law provision, permits parties to a transaction to select the law which will govern their rights and duties as long as the law selected bears a "reasonable relation" to the state or nation whose law is selected. If the parties fail to select the governing law, the same Code section states that "this Act applies to transactions bearing an appropriate relation to this state." This section was initially drafted to ensure the widest possible application of the Uniform Commercial Code at a time when its widespread adoption was in doubt. While the thrust of the section is to apply the law of the forum whenever the parties have not selected the governing law, commentators point to the resulting danger of forum shopping. Most commentators favor reading the "appropriate relation" test to permit the courts to select the governing law by weighing the public policies of the jurisdictions related to the transaction.⁶ Texas state courts have not yet had occasion to interpret the "appropriate relation" test, but in this survey period two federal district courts were faced with fact situations where the test was relevant.⁷

In *Continental Oil Co. v. General American Transportation Corp.*⁸ Judge Bue of the Federal District Court for the Southern District of Texas concluded that, in the absence of a choice of governing law in the parties' agreement, causes of action based on breaches of express and implied warranties were governed by the law of Oklahoma. The court reached this conclusion because "on the basis of the established facts and the case law of other jurisdictions, a Texas court would hold that the nexus between the disputed chain of events and the State of Texas is too slight to justify the use of Texas law."⁹ Having concluded in effect that there was no "appropriate relation" to Texas, the court then followed the traditional choice-of-law rules applied by Texas courts to find that Oklahoma law governed as the place where the contract was entered into when the contract was to be performed in more than one jurisdiction.¹⁰

The court's conclusion in *Continental Oil* is significant for two reasons. First, it implicitly rejects an approach which presumes that the forum's version of the Uniform Commercial Code will govern the transaction unless to do so would violate constitutional due process limitations.¹¹ Second, the

secured party changes his name, or, (2) either the secured party or the debtor changes his address (Uniform Commercial Code Committee of the Corporation Banking and Business Law Section).

Texas State Bar, *Board Approves 1977 Legislative Program*, 5 BAR, Nov. 1976, at 6.

6. See R. NORDSTROM, HANDBOOK OF THE LAW OF SALES 26-39 (1970); R. WEINTRAUB, COMMENTARY ON THE CONFLICT OF LAWS 280-85 (1971); Note, *Conflicts of Laws and the "Appropriate Relation" Test of Section 1-105 of the Uniform Commercial Code*, 40 GEO. WASH. L. REV. 797 (1972).

7. Both decisions are discussed at greater length in Thomas, *Conflict of Laws*, p. 345 *infra*.

8. 409 F. Supp. 288 (S.D. Tex. 1976).

9. *Id.* at 291.

10. It is ironic that while the federal court adopted a flexible approach to the "appropriate relation" test it felt constrained to apply traditional choice-of-law rules rather than a functional or governmental interests approach in the absence of direction from the Code. *Id.* at 291 n.1.

11. In the case before the court there were probably sufficient contacts with Texas—partial delivery in Texas; some repairs in Texas—to meet the constitutional due process test.

court indicates that the forum's non-statutory conflicts rules will apply if there is no appropriate relation between the transaction and the forum. The Code is silent on the applicable law when there is no appropriate relation, and the court's conclusion here is eminently sensible.

An interesting variation on the *Continental Oil* case is found in *Morton v. Texas Welding & Manufacturing Co.*,¹² also decided by the Federal District Court for the Southern District. Faced with a cause of action based in part on breaches of express and implied warranties, Judge Singleton applied Texas law because under Texas conflicts rules a statute of limitations is "procedural" and, therefore, the law of the forum applies. Unlike the plaintiff in *Continental Oil*, however, the plaintiff in *Morton* sought to recover damages for personal injuries which allegedly resulted from the breaches of express and implied warranties. The court therefore proceeded to examine the very important question of whether the enactment of the Uniform Commercial Code in Texas amended the pre-Code Texas case law which held that the personal injury action based on breach of implied warranties was governed by the two-year "tort" statute of limitations. No Texas court had previously examined this question. The federal court concluded that the Code had supplanted the prior rule, and it therefore applied the four-year statute of limitations set out there in section 2-725.¹³

The court in *Morton* does not refer to the appropriate relation test of section 1-105, and the opinion does not give sufficient facts to suggest whether or not the result would be different if the court had examined this issue.¹⁴ The court should have addressed itself to the "appropriate relation" test. The traditional classification of statutes of limitations as "procedural" has been superseded by section 1-105 with respect to transactions which would otherwise fall within the scope of the Code. A precondition to the application of the forum's version of the Code's provisions, whether "substantive" or "procedural," is that the transaction bear an appropriate relation to the forum.¹⁵ If no appropriate relation is found, *Continental Oil* suggests application of the forum's non-statutory conflicts rules. The court in *Morton* failed to examine this issue and on this point the opinion should be viewed with caution.¹⁶

Where the parties themselves choose which law will govern, that law should be applied if the court finds that the transaction bears a "reasonable

12. 408 F. Supp. 7 (S.D. Tex. 1976). For further discussion of this case see notes 68-73 *infra* and accompanying text.

13. The court also applied the section 2-725 limitations period to the claim based on breach of an express warranty. As the court notes, the Code did not change the rule for express warranty actions. 408 F. Supp. at 11.

14. The court simply states:

Defendant sold a propane truck to the National Propane Company on April 21, 1969, who subsequently delivered the truck to Carib Gas, its subsidiary. Plaintiffs, employees of Carib Gas, were severely injured when the truck exploded on June 19, 1969. . . . Defendant falsely assumes in his memorandum that the Virgin Islands statute of limitations is applicable here.

Id. at 8-9.

15. Non-uniform amendments to the Code add significance to the issue of what state's law governs a transaction. In the *Continental Oil* case, Oklahoma's version of section 2-725 set a five-year period of limitations while the Texas version provides for only a four-year period.

16. An interesting problem would result if the court in *Morton* had decided that the Code had not changed the pre-Code rule. Presumably if the court had so decided the Texas two-year statute

relation" to that jurisdiction.¹⁷ In *Three-Seventy Leasing Corp. v. Ampex Corp.*¹⁸ the Fifth Circuit enforced a contract provision choosing California law as the governing law. The court merely stated that section 1.105 of the Texas Business and Commerce Code validated the parties' choice. The court did not discuss whether or not the transaction bore a "reasonable relation" to California, although it notes that the relevant Code provisions in both jurisdictions were similar. The parties themselves attempted to construe the agreement under Texas law and did not present the relevant California law. Presumably, the contacts with California need not be as many or as significant as where an "appropriate relation" test is applied, but a court faced with the situation in *Three-Seventy Leasing* should make a preliminary inquiry and ruling as to the "reasonable relation" between the transaction and the jurisdiction whose law has been chosen by the parties as the governing law.

II. SALES TRANSACTIONS

A. Formation of Contracts

Statute of Frauds. Section 2-201 of the Code sets out a statute of frauds provision which states that "unless there is some writing sufficient to indicate that a contract for sale has been made between the parties and signed by the party against whom enforcement is sought," a contract for the sale of goods at a price of \$500 or more is unenforceable. One of several exceptions to this provision is section 2-201(2) where "between merchants" the requirement of writing is met by a written confirmation of a contract. In *Nelson v. Union Equity Co-operative Exchange*¹⁹ the Fort Worth court of civil appeals examined the question of whether a farmer is a "merchant" for the purposes of this exception. After a thorough survey of decisions from other jurisdictions the Fort Worth court concluded that the fact finder should be entitled to determine the question and that in this case there was sufficient evidence to support the finding that the defendant farmer was a merchant. The Texas Supreme Court has granted a writ of error in this case and no doubt will re-examine the question.²⁰

of limitation would govern. It is not subject to the "appropriate relation" test and as a "procedural" rule the forum's statute of limitations would apply. TEX. REV. CIV. STAT. ANN. art. 5526 (Vernon 1958).

17. TEX. BUS. & COMM. CODE ANN. § 1.105(a) (Vernon Supp. 1976-77).

18. 528 F.2d 993 (5th Cir. 1976).

19. 536 S.W.2d 635 (Tex. Civ. App.—Fort Worth 1976, writ granted), noted in 28 BAYLOR L. REV. 715 (1976). Although not discussed in the text it should be noted that the court interpreted the phrase "a writing in confirmation . . . is received" (TEX. BUS. & COMM. CODE ANN. § 2.201(b) (Vernon 1968)) to be satisfied by evidence that the written confirmation was handled and mailed following plaintiff's usual procedure. 536 S.W.2d at 637. Cf. TEX. BUS. & COMM. CODE ANN § 1.201(26) (Vernon 1968): "A person 'receives' a notice or notification when (A) it comes to his attention; or (B) it is duly delivered at the place of business through which the contract was made or at any other place held out by him as the place for receipt of such communications."

20. The Texas Supreme Court has granted a writ of error on the following two points:

Point 3. The court of civil appeals erred in holding that the evidence was sufficient to support a finding that petitioner was a merchant as that term is defined in § 2.104 of the Texas Business & Commerce Code. Such finding was not supported by sufficient evidence as a matter of law.

Point 4. The court of civil appeals erred in holding that there is evidence of probative force to support the finding of the trial court that petitioner was a merchant as that term is defined in § 2.104 of the Texas Business & Commerce Code.

19 Tex. Sup. Ct. J. 456 (Oct. 2, 1976).

The rules of article 2 of the Uniform Commercial Code apply to all contracts for sale except where the Code specifies that a particular rule applies only to a "merchant" or only to transactions "between merchants." The Code defines these terms.²¹ An official comment to the Code indicates that the special merchant provisions should be read in the context of the underlying policies of the different sections. With specific reference to the statute of frauds section, the comment states:

[Section 2-201 rests] on normal business practices which are or ought to be typical or familiar to any person in business. For purposes of [this section] almost every person in business would, therefore, be deemed to be a 'merchant' under the language 'who . . . by his occupation holds himself out as having knowledge or skill peculiar to the practices . . . involved in the transaction . . .' since the practices involved in the transaction are non-specialized business practices such as answering mail.²²

In other words, the comment suggests that to find that a farmer is a merchant for the purposes of section 2-201(2) does not necessarily mean that the farmer will necessarily be considered a merchant for the purposes of other special merchant provisions. Moreover, many farmers today are "agri-businessmen" who are unlike the stereotype of the relatively unsophisticated and casual seller. Where the Code draftsmen wished to give special benefits to farmers as a class they did so explicitly.²³ There is no reason to permit sophisticated farmers the option of going through with an agreement or avoiding it on the basis of the statute of frauds. The broker or dealer must still prove the terms of the agreement, even if the farmer is denied the defense of the statute of frauds.²⁴

The problem of the farmer as merchant has given rise to a number of recent decisions with eminent judicial authority resolving the issue both ways.²⁵ The Fort Worth court in *Nelson* concluded that "[a] very good reason exists for holding that the fact finder should be entitled to determine the question."²⁶ The court expressed confidence that the fact finder would protect the "ignorant, innocent, and inexperienced farmer" while holding to his agreement the "knowledgeable and experienced trader who happens to be a farmer." The court adds cryptically that "[o]nly in the exceptional case

21. TEX. BUS. & COMM. CODE ANN. §§ 2.104(a), 2.104(c) (Vernon 1968). Section 2.104(a) provides:

'Merchant' means a person who deals in goods of the kind or otherwise by his occupation holds himself out as having knowledge or skill peculiar to the practices or goods involved in the transaction or to whom such knowledge or skill may be attributed by his employment of an agent or broker or other intermediary who by his occupation holds himself out as having such knowledge or skill.

A transaction "between merchants" means that both parties are chargeable with the knowledge or skill of merchants (§ 2.104(c)). See Newell, *The Merchant of Article 2*, 7 VAL. U.L. REV. 307 (1973).

22. TEX. BUS. & COMM. CODE ANN. § 2.104, comment 2 (Vernon 1968).

23. See, e.g., *id.* § 9.307(a) (Vernon Supp. 1976-77).

24. *Id.* § 2.201, comment 3 (Vernon 1968). See generally J. WHITE & R. SUMMERS, HANDBOOK OF THE LAW UNDER THE UNIFORM COMMERCIAL CODE § 2-4 (1972).

25. These judicial opinions are ably discussed in Comment, *The Farmer in the Sales Article of the U.C.C.: "Merchant" or "Tiller of the Soil"?*, 1976 S. ILL. U.L. REV. 237. In addition to the cases discussed by this Comment and by the court in *Nelson*, see the case citations collected in 9 UCC L.J. 185-86 (1976). See also 16 WASHBURN L.J. 230 (1976).

26. 536 S.W.2d at 641.

would circumstances remove the responsibility for factual determination from the fact finder and require the holding that the farmer was not a merchant. . . . That before us on appeal is not such a case."²⁷

The Texas Supreme Court should affirm the *Nelson* decision for the reasons set out above. In doing so the court should spell out for the benefit of trial courts the factors to look to when determining whether or not a farmer is a merchant within the context of section 2-201(2). In the leading case of *Sierens v. Clausen*²⁸ the Illinois Supreme Court suggested the following factors, which might be adopted by the Texas court: (a) the length of time the farmer had farmed; (b) the extent of cultivation; (c) the length of time the farmer had sold similar crops to similar buyers; and (d) the farmer's familiarity with the customs and usages of cash sales and futures contracts. The court should also clearly allocate the burden of proof to the defendant farmer once the plaintiff introduces the written confirmation of the agreement into evidence.²⁹

The possibilities of procedural tactics in a statute of frauds case were featured in *Goodpasture, Inc. v. Skaggs*.³⁰ In addition to a general denial, the defendant entered a special plea that an oral contract under which plaintiff claimed violated sections 2.201 and 26.01 of the Texas Business and Commerce Code. The alleged contract was for the sale of several thousand tons of junk at \$18.00 per ton, well over the \$500 limit of section 2.201. The plaintiff removed some of the junk, which was much less valuable than the remaining junk, before the defendant rescinded the contract. By trial amendment the plaintiff agreed that the contract was unenforceable and sought recovery in quantum meruit. The defendant then filed a "motion for judgment on finding of jury" asserting that the oral contract was enforceable to the extent performed, apparently relying on section 2-201(3)(c) of the Code. This motion was not called to the attention of the court, and the court of civil appeals correctly ruled that the motion was not preserved for review.³¹

Battle of the Forms. Section 2-207 of the Code (Additional Terms in Acceptance or Confirmation) is a favorite of law professors who teach contracts or commercial transactions. There are not many sections of the Code which can boast as much academic comment.³² The First Circuit opinion in *Roto-Lith, Ltd. v. F.P. Bartlett & Co.*³³ is known and reviled by most recent law school

27. *Id.*

28. 60 Ill. 2d 585, 328 N.E.2d 559 (1975).

29. See TEX. R. CIV. P. 94 (statute of frauds an affirmative defense).

30. 532 S.W.2d 384 (Tex. Civ. App.—Waco 1975, no writ).

31. It is possible that plaintiff in *Skaggs* might have been able to take advantage of section 2-201(3)(b). TEX. BUS. & COMM. CODE ANN. § 2.201(c)(2) (Vernon 1968). Under this subsection the oral contract may be enforced to the extent that defendant "admits in his pleading, testimony or otherwise in court" that there was a contract for sale. At least one commentator suggests that this provision spells the end of the statute of frauds. See Yonge, *Unheralded Demise of the Statute of Frauds Welsher in Oral Contracts for the Sale of Goods and Investment Securities: Oral Sales Contracts are Enforceable by Involuntary Admissions in Court Under U.C.C. Sections 2-201(3)(b) and 8-319(d)*, 33 WASH. & LEE L. REV. 1 (1976).

32. For recent surveys of cases see Barron & Dunfee, *Two Decades of 2-207: Review, Reflection and Revision*, 24 CLEV. ST. L. REV. 171 (1975); Shaw, *U.C.C. § 2-207: Two Alternative Proposals for Change*, 13 AM. BUS. L.J. 185 (1975).

33. 297 F.2d 497 (1st Cir. 1962). Even *Roto-Lith* is not without its defenders. See Comment, *A Look at a Strict Construction of Section 2-207 of the Uniform Commercial Code from the Seller's Point of View or What's So Bad About Roto-Lith?*, 8 AKRON L. REV. 111 (1974).

graduates. In this survey period the Texas courts have added another judicial gloss on the statutory provision. In *Hillson Steel Products, Inc. v. Wirth Ltd.*³⁴ buyer followed up an oral conversation with seller by sending a written confirmation, and seller responded with a writing which apparently made price changes and shifted the risk of loss. Buyer refused delivery and seller brought suit to recover damages. Attached to the seller's petition was the buyer's confirmation and seller's "acknowledgment." The trial court entered summary judgment for the seller and granted relief based on the terms of seller's acknowledgment. The appellate court reversed and remanded on the ground that the acknowledgment was a "counter proposal" which was "conditional on assent to the additional or different terms."³⁵

Plaintiff's theory in *Hillson* apparently was that the parties had come to an agreement prior to the sending of buyer's confirmation and that an enforceable contract came into existence when buyer sent the confirmation. If the buyer's confirmation contained additional or different terms, plaintiff would argue, they would be subject to the limitations of section 2-207. The seller's acknowledgment (which, it would be argued, contained the terms of the oral agreement) would be surplusage for the purposes of that section although perhaps necessary for the purposes of section 2-201 (Formal Requirements; Statute of Frauds). Although the appellate court's discussion of these facts in the light of the Code language is not altogether clear, the court is correct in concluding that the plaintiff-seller must produce evidence of the terms of the alleged oral agreement and that the seller's written acknowledgment is insufficient evidence of these terms to support a summary judgment for seller.

B. Warranties

"Products liability" as a distinct conceptual field of law is rapidly absorbing both traditional "contract" warranty and "tort" negligence, and strict liability actions.³⁶ Many cases in the period covered by this survey illustrate both how the traditional concepts overlap, and some of the practical consequences of that overlap. Different statutes of limitation may apply to the different causes of action;³⁷ different measures of damages may govern.³⁸

34. 538 S.W.2d 162 (Tex. Civ. App.—Houston [1st Dist.] 1976, no writ).

35. TEX. BUS. & COMM. CODE ANN. § 2.207(a) (Vernon 1968) (emphasis added):
A definite and seasonable expression of acceptance or a written confirmation which is sent within a reasonable time operates as an acceptance even though it states terms additional to or different from those offered or agreed upon, unless acceptance is expressly made conditional on assent to the additional or different terms.

36. See Note, *Products Liability: Tort or Contract—A Resolution of the Conflict?*, 21 N.Y.L.F. 587 (1976).

37. See, e.g., *Continental Oil Co. v. General Am. Transp. Corp.*, 409 F. Supp. 288 (S.D. Tex. 1976); *Morton v. Texas Welding & Mfg. Co.*, 408 F. Supp. 7 (S.D. Tex. 1976). The court in *Continental Oil* is particularly sensitive to the overlap between tort and contract theories. See, in particular, 409 F. Supp. at 293 n.3. The *Morton* case is discussed in more detail in notes 68-73 *infra* and accompanying text.

38. In *Gorbett Bros. Steel Co. v. Anderson, Clayton & Co.*, 533 S.W.2d 413 (Tex. Civ. App.—Houston [1st Dist.] 1976, no writ), the court held that there was sufficient evidence to support a finding of breach of implied warranties, negligence, and strict liability. On the question of damages the court focused on the theories of negligence and strict liability and held that the proper measure of damages included all damages "the wrongdoer could or should reasonably have foreseen that the injury complained of, or one of the same general character, would

Furthermore, the intervention of regulatory legislation has made warranty questions even more complicated.³⁹ The warranty provisions of the Uniform Commercial Code⁴⁰ are only part of a much larger and rapidly changing picture.

Among the more difficult problems in the field of warranties is whether or not a person other than the buyer may sue the seller (horizontal privity) or whether a buyer may sue a person other than his immediate seller when the party sued is a manufacturer or distributor of the good (vertical privity). The draftsmen of the Uniform Commercial Code offer three alternatives from which state legislatures might choose. The Texas Legislature, however, chose to adopt yet another solution to the problem.⁴¹ Section 2.318 of the Texas Business and Commerce Code states:

Section 2.318. Chapter Neutral on Question of Third Party Beneficiaries of Warranties of Quality and on Need for Privity of Contract.

This chapter does not provide whether anyone other than a buyer may take advantage of an express or implied warranty of quality made to the buyer or whether the buyer or anyone entitled to take advantage of a warranty made to the buyer may sue a third party other than the immediate seller for deficiencies in the quality of the goods. These matters are left to the courts for their determination.

This section has been the subject of differing interpretations by Texas courts.⁴²

In a very important decision the Beaumont court of civil appeals in *Nobility Homes of Texas, Inc. v. Shivers*⁴³ ruled that a consumer could recover damages for economic loss from the manufacturer for breach of an implied warranty of merchantability despite a lack of privity between the consumer and the manufacturer. The consumer purchased a mobile home from an independent dealer who had previously purchased the home from the manufacturer. The dealer was not a party to the suit because he had gone out of business and could not be located. The trial court found, *inter alia*, that the mobile home was defectively constructed and was not fit for the purposes for

probably result from his wrongful conduct." 533 S.W.2d at 419. Damages therefore included the reasonable cost of replacing the collapsed soybean tank designed and constructed by defendant. The court therefore bypasses the question of whether the Code provision on consequential damages would give the same result. TEX. BUS. & COMM. CODE ANN. § 2.715(b) (Vernon 1968).

39. On the federal level, three trade regulation rules promulgated by the Federal Trade Commission under the Magnuson-Moss Warranty Act, 15 U.S.C. §§ 2301-2312 (1970), came into effect during the survey period. 40 Fed. Reg. 60188, 60189, 60215 (1975). These rules govern "Disclosure of Written Consumer Product Warranty Terms and Conditions," "Pre-Sale Availability of Written Terms and Conditions," and "Informal Settlement Procedures."

40. The Code includes four warranty provisions: a warranty of title (TEX. BUS. & COMM. CODE ANN. § 2.312 (Vernon 1968)), express warranty (*id.* § 2.313), implied warranty of merchantability (*id.* § 2.314), and implied warranty of fitness for a particular purpose (*id.* § 2.315). In addition, the Code regulates the exclusion or modification of warranties (*id.* § 2.316) and contractual modification or limitation of remedies (*id.* § 2.719). Vertical and horizontal privity between parties is governed by *id.* § 2.318 which not only is presented in three official alternatives in the 1972 Official Text of the Uniform Commercial Code but also has been subject to numerous non-uniform amendments by the states adopting the Code.

41. For the legislative history of § 2.318 in Texas see Ruud, *The Texas Legislative History of the Uniform Commercial Code*, 44 TEXAS L. REV. 597, 601-02 (1966).

42. Compare *Eli Lilly & Co. v. Casey*, 472 S.W.2d 598, 600 (Tex. Civ. App.—Eastland 1971, writ dismissed), with *Monsanto Co. v. Thrasher*, 463 S.W.2d 25, 27 (Tex. Civ. App.—Amarillo 1970, writ dismissed).

43. 539 S.W.2d 190 (Tex. Civ. App.—Beaumont 1976, writ granted).

which it was sold. The trial court rendered judgment for the plaintiff consumer for the difference between the reasonable market value of the mobile home at the time of purchase and the original contract price. The court of civil appeals affirmed and both a majority opinion and a dissenting opinion have been reported. The Texas Supreme Court has granted a writ of error and will presumably examine in detail the problem of privity in a cause of action based on a theory of breach of an implied warranty of merchantability.⁴⁴

The reasoning of the majority decision of the Beaumont court in *Nobility Homes* proceeds through several steps. The court first interprets section 2-318 as enacted in Texas to be a legislative statement of neutrality on the rules applicable to third parties injured by breaches of warranty. The court then holds, without further citation to the Code, that there was an implied warranty of reasonable fitness in this case and that privity was not required. The court rests its decision on the following points: (a) the interests of equity and justice are best served by its conclusion; (b) economic harm to the public from defective goods placed in the stream of commerce by the manufacturer should be treated in the same way as personal and property damages are now treated; (c) the trend of the law is to reduce the harshness of requiring privity; and (d) the need to avoid wasteful litigation when the dealer in privity with the consumer would ultimately have a right over against the manufacturer. The court rejects the possibility of relying on a theory of strict liability under *Restatement (Second) of Torts* § 402A because that section applies only where there has been physical harm from an inherently dangerous good. A vigorous dissent⁴⁵ points out that the majority decision departs from established Texas precedents, from the prevailing view in other jurisdictions, and from the opinion of some leading scholars. The dissent notes that the premise underlying prior Texas cases denying recovery for consequential economic losses is that an action based on an implied warranty of merchantability is contractual and, therefore, requires privity of contract.

Given the wording and legislative history of section 2-318 as enacted in Texas, the majority opinion's conclusion that the legislature declared itself neutral on questions of privity is persuasive and should be affirmed.⁴⁶ As for the majority's conclusion that an action could be based on implied warranty without having to meet the requirement of privity, the matter is more

44. The Texas Supreme Court has granted a writ of error on the following point: Point No. 1—The court of civil appeals erred in upholding the ruling of the district court allowing the plaintiffs to recover for economic loss on the basis of an implied warranty where the purchaser plaintiffs had no privity of contract with the defendant manufacturer, there being no injury to person or property.

20 Tex. Sup. Ct. J. 49 (Nov. 27, 1976).

45. 539 S.W.2d at 195-97. A later decision by the same court on a related point led to an even sharper dissent from Justice Keith. "'Color me amazed.' . . . [I]f the majority insists on being wrong they should at least strive to be wrong with consistency, and avoid being wrong in a different way and for different reasons each day.'" *Explorers Motor Home Corp. v. Aldridge*, 541 S.W.2d 851, 855 (Tex. Civ. App.—Beaumont 1976, no writ). See also the elaborate and well-reasoned opinion in *Morrow v. New Moon Homes, Inc.*, 548 P.2d 279 (Alas. 1976).

46. One may well deplore the abdication of legislative responsibility. Why courts should be better equipped to resolve the conflicting economic interests is difficult to understand. Moreover, as the official comments to the Uniform Commercial Code indicate, to have a legislative rule does not necessarily mean the end of further case law development. TEX. BUS. & COMM. CODE ANN. § 2.313, comment 2 (Vernon 1968).

problematical. To say that the action is based on contract and that, therefore, privity is required is merely to apply formalistic labels in an area of the law where labels are rapidly becoming outmoded.⁴⁷ On appeal the Texas Supreme Court should go beyond the labels and examine underlying policies. To require the manufacturer to reimburse the ultimate consumer for the difference between the value of a merchantable good and its actual value at the time it leaves the manufacturer would give the manufacturer an incentive to improve quality control of these goods. On the other hand, the consumer can theoretically choose his dealer, can bargain with him for express contractual stipulations as to quality, and can inspect the goods prior to accepting them.

It is respectfully suggested that the Texas Supreme Court should affirm the majority opinion in *Nobility Homes*, but remand on the issue of damages.⁴⁸ Several elements in this case suggest that to allow plaintiff to recover would not be a major departure from prior case law. (1) The plaintiff and ultimate purchaser in this case is a consumer, not a merchant. The plaintiff's ability to bargain for quality protection and to detect defects is attenuated. (2) The plaintiff proved that the mobile home was defective at the time it left the hands of the manufacturer. Many plaintiffs will find it difficult to meet the burden of showing this fact, and that heavy burden will discourage frivolous litigation. (3) The manufacturer has control of the goods and could have prevented the defective good from going on the market. (4) This is not a case where consequential economic damages—such as loss of profits because of the defect—are sought. All that is sought is the difference between the value of the same good without a defect and its value with a defect. The manufacturer received a benefit when he placed the good on the market, and he is not subject to limitless liability for which he cannot plan. (5) The case does not involve an attempt by the manufacturer to disclaim warranties or to limit remedies either to his immediate purchaser or to the ultimate consumer.⁴⁹

Several other reported warranty cases fall within the survey period and are important primarily as illustrations of basic rules sometimes overlooked. Two such cases are worthy of comment. The case of *Simms v. Southwest Texas Methodist Hospital*⁵⁰ illustrates the need to prove not only that there is a warranty but that the breach of the warranty is a producing cause of damage to the plaintiff. The plaintiff in this case sought recovery for personal injuries allegedly resulting from the presence of cornstarch on surgical gloves used by surgeons who operated on her to remove an ovarian cyst. In the lower court

47. See G. GILMORE, *THE DEATH OF CONTRACT* 87 (1974) (footnotes omitted):

Speaking descriptively, we might say that what is happening is that 'contract' is being reabsorbed into the mainstream of 'tort.' Until the general theory of contract was hurriedly run up late in the nineteenth century, tort had always been our residual category of civil liability. As the contract rules dissolve, it is becoming so again.

48. The court apparently may now remand on the damage issue alone. TEX. R. CIV. P. 503 (as amended July 22, 1976). The court of civil appeals affirmed the trial court's award of damages based on "the difference in the reasonable market value thereof at the time of the purchase and the original contract price." 539 S.W.2d at 191. The proper measure should be based not on the time plaintiff purchased but when the good left the hands of the manufacturer. The manufacturer should not bear the risk of depreciation in the hands of an independent dealer.

49. See, however, arguments against the position taken in the text set out in J. WHITE & R. SUMMERS, *supra* note 24, § 11.5.

50. 535 S.W.2d 192 (Tex. Civ. App.—San Antonio 1976, writ ref'd n.r.e.).

the plaintiff relied on theories of negligence, strict tort liability, and breach of express and implied warranties. On appeal from a judgment for defendants based on an adverse jury verdict, the plaintiff relied only on the implied warranty that the surgical gloves were fit for the ordinary purpose for which such gloves are used. The court of civil appeals affirmed the trial court's judgment on the ground that there was some evidence to support the jury's negative answer to a special issue asking whether the "dangerous" condition of the gloves was "a producing cause" of plaintiff's injuries. The opinion made two important points: the plaintiff has the burden of pleading and proving a causal connection between the defect in a good and the damage; and plaintiff must prove that the defect was "a producing cause" but not necessarily that it was "the producing cause."

In a relatively rare reversion to the formalism of magic words the Code in section 2-316(2) requires a seller desiring to exclude or modify the implied warranty of merchantability to mention "merchantability" and, where a writing is used, to make a conspicuous reference to the exclusion or modification. There continue to be cases where the broad language in a contract appears to disclaim liability for all possible contingencies but fails to use the statutory formula. A recent illustration is the language in a contract for the sale of a car in the case of *Bill McDavid Oldsmobile, Inc. v. Mulcahy*.⁵¹ The contract stated: "It is expressly agreed that there are no warranties, expressed or implied, made by either the dealer or the manufacturer other than the manufacturer's warranty against defective materials as stated in the Oldsmobile Owner's Manual." The court correctly concluded that this language excluded all warranties by the dealer except the implied warranty of merchantability because the contract clause failed to follow the requirements of section 2-316. While one may wish to limit the right of a seller to exclude implied warranties, the formalism of section 2-316(2) is unfair because some buyers receive an unexpected windfall when they discover to their surprise that a blanket disclaimer is formally defective. Given, however, the formalism which exists in the Code as presently drafted, an elementary precaution for the attorney drafting a disclaimer clause is to follow the letter of section 2-316.

C. *Acceptance, Rejection, and Revocation of Acceptance*

Several cases in this survey period illustrate the Code rules on acceptance, rejection, and revocation of acceptance.⁵² In *Bill McDavid Oldsmobile, Inc. v. Mulcahy*⁵³ the buyer of an automobile alleged that the battery in his new car was cracked and that the defendant dealer refused to repair or replace the battery as he was required to do under the warranty. The plaintiff sought to revoke his acceptance and to recover damages calculated on the difference

51. 533 S.W.2d 160 (Tex. Civ. App.—Houston [1st Dist.] 1976, no writ).

52. TEX. BUS. & COMM. CODE ANN. §§ 2.601-.608 (Vernon 1968). The best article on this topic and on the general question of Code remedies remains Peters, *Remedies for Breach of Contracts Relating to the Sale of Goods Under the Uniform Commercial Code: A Roadmap for Article Two*, 73 YALE L.J. 199 (1963).

53. 533 S.W.2d 160 (Tex. Civ. App.—Houston [1st Dist.] 1976, no writ). The warranty provision in this case is discussed at text accompanying note 51 *supra*.

between the amount paid for the car less the amount received from the sale of the car on foreclosure. The defendant dealer appealed from an adverse judgment, and the court of civil appeals reversed and rendered judgment that plaintiff take nothing. The appellate court concluded that the plaintiff "accepted" the car within the meaning of the Code.⁵⁴ The court agreed that the defective battery was a non-conformity which breached the implied warranty of merchantability.⁵⁵ The court held, however, that there was no evidence that the non-conformity substantially impaired the value of the car to plaintiff as required by section 2-608 on revocation of acceptance.⁵⁶ Plaintiff's remedy was for damages under the Code formula (the difference at the time and place of acceptance between the value of the car on acceptance and the value it would have had if it had been as warranted).⁵⁷ Nevertheless, he failed to present evidence to support an award for damages under this formula, and the court properly rendered a take-nothing judgment. The lesson for plaintiff in this case is to frame the theory of the case before going to trial in order to organize the evidence to be produced.

The same court was more sympathetic to the buyer in *Askco Engineering Corp. v. Mobil Chemical Corp.*⁵⁸ Buyer contracted to purchase from seller approximately 250,000 pounds of bulk roll, low density, polyethylene film to be reprocessed by buyer into plastic trashcan liners. The court found evidence to support a finding that seller expressly warranted the material to be low density polyethylene film. Before taking delivery, buyer's agent inspected the goods in seller's warehouse. Buyer took delivery but on processing 45,000 pounds of the material found it would not break down properly. Buyer returned the remaining material to seller who refused to accept the return. Buyer then analyzed approximately 75% of the material and discovered that over 80% was not low density polyethylene.

Seller first argued that the plastic film was sold as a lot or "commercial unit" and that acceptance of part of the commercial unit was acceptance of the whole.⁵⁹ The appellate court held that the trial court could reasonably have found that the "commercial unit" was a pound and not a lot. The court noted that the agreed price was not a lot price but a per pound price and that an additional truck load of film was added on a per pound basis. The court then found that buyer had rightfully rejected the non-processed film. The court concluded that the buyer had not accepted the goods because prior to rejection buyer did not have a reasonable opportunity to inspect the film on its

54. The court noted that "[t]he evidence shows that the plaintiff paid to the dealer the full cash purchase price, accepted the automobile, and used it for some three months prior to tendering it back to the dealer." 533 S.W.2d at 163. Later the court also stated: "[I]n this case the contract of sale was complete, and the buyer had received title and possession of the automobile" *Id.* The court does not, however, cite the Code provisions on what constitutes acceptance as a matter of law. TEX. BUS. & COMM. CODE ANN. § 2.606 (Vernon 1968).

55. 533 S.W.2d at 164; TEX. BUS. & COMM. CODE ANN. §§ 2.106(b), .314 (Vernon 1968).

56. TEX. BUS. & COMM. CODE ANN. § 2.608(a) (Vernon 1968).

57. *Id.* § 2.714. The court earlier suggests that the only damage suffered is the cost of replacing the battery. 533 S.W.2d at 162. This statement is made in the context of a reference to the common law rules on damages and should be qualified by the later correct reference to the Code damage formula.

58. 535 S.W.2d 893 (Tex. Civ. App.—Houston [1st Dist.] 1976, no writ).

59. TEX. BUS. & COMM. CODE ANN. §§ 2.105(f), .606(b) (Vernon 1968).

own premises,⁶⁰ and that buyer rejected the film within a reasonable time.⁶¹ The court also rejected the seller's claim that buyer's storage and subsequent disposal of the film was an exercise of dominion over the goods inconsistent with buyer's claim that they belonged to seller.⁶²

In *Sylvester v. Watkins*⁶³ one issue on appeal was whether as a matter of law buyer had revoked his acceptance within a reasonable time.⁶⁴ The court of civil appeals ruled that whether there has been a revocation of acceptance within a reasonable time is a question of fact which was properly submitted to the jury. The court stated: "The criterion is not when the events occurred, but whether, under all of the circumstances, the act of revocation was taken within a reasonable time after [buyer] discovered or should have discovered his grounds for revocation."⁶⁵ To leave the issue to the fact-finder in this way is no doubt correct, but there is the disturbing possibility that strict application of this rule may discourage attempts to negotiate a non-judicial settlement. Presumably, attempts at settlement would be among "all of the circumstances" which the court in *Sylvester* would have the fact-finder consider.

D. Statute of Limitations

Section 2-725 of the Code provides a statute of limitations for actions which arise from sales transactions. Prior to the enactment of the Code in Texas the general rules as to limitations periods for personal actions were set out in articles 5524-5526 of the Revised Civil Statutes. The relation between the Code and these provisions continues to cause problems. Under article 5526(5), for example, actions upon stated or open accounts are subject to a two-year limitations period. It now should be clear that when an account arises from contracts for the sale of goods, the four-year Code limitations period should apply. Two cases⁶⁶ in this survey period so hold and thus follow the lead of the recent supreme court decision in *Big D Service Co. v. Climatrol Industries, Inc.*⁶⁷

A more interesting problem was that faced by the federal district court in *Morton v. Texas Welding & Manufacturing Co.*⁶⁸ In a case of first impression the court considered whether enactment of the Uniform Commercial Code in Texas changed pre-Code Texas rules with respect to the statute of limitations in an action to recover damages for personal injury where the action is based on a theory of a breach of implied warranty.

60. The contract in *Askco* stated in part: "Products purchased hereunder are subject to inspection and approval at Buyer's destination." 535 S.W.2d at 895.

61. TEX. BUS. & COMM. CODE ANN. §§ 2.602(a), .606(a)(1) (Vernon 1968).

62. *Id.* §§ 2.602(b)(1), .606(a)(3).

63. 538 S.W.2d 827 (Tex. Civ. App.—Amarillo 1976, writ ref'd n.r.e.).

64. See TEX. BUS. & COMM. CODE ANN. §§ 1.204, 2.608(b) (Vernon 1968).

65. 538 S.W.2d at 830-31.

66. *Mallory v. Custer*, 537 S.W.2d 141 (Tex. Civ. App.—Austin 1976, no writ); *Kinsey v. Hubby-Reese Co.*, 530 S.W.2d 846 (Tex. Civ. App.—Waco 1975, no writ).

67. 523 S.W.2d 236 (Tex. 1975), *refusing writ of error*, 514 S.W.2d 148 (Tex. Civ. App.—Texarkana 1974). See also *Ideal Builders Hardware Co. v. Cross Constr. Co.*, 491 S.W.2d 228 (Tex. Civ. App.—Houston [1st Dist.] 1972, no writ).

68. 408 F. Supp. 7 (S.D. Tex. 1976). For a discussion of this case with respect to choice-of-law problems, see note 12 *supra* and accompanying text. For recent judicial developments with respect to the Code's statute of limitations, see the case citations collected in 9 UCC L.J. 186-88 (1976).

The first question in *Morton* concerned whether the two-year tort statute of limitations⁶⁹ or the four-year Code provision governed. The pre-Code Texas courts applied the two-year "tort" period.⁷⁰ Section 2-725 of the Code provides a four-year period "for breach of any contract for sale." The district court concluded that the four-year period set out in section 2-725 should apply, and on this point the court's opinion is a model of Code reasoning. The court emphasized the underlying policies of the Code that its provisions apply to all aspects of a commercial transaction and to promote uniformity among the various jurisdictions.⁷¹ The court noted that courts in other jurisdictions have applied section 2-725 to personal injury actions allegedly resulting from a breach of implied warranty and thus have rejected the pre-Code majority rule which treated such claims as tort actions. The court stressed that the Code contemplates recovery of consequential personal and property damages resulting from a breach of warranty.⁷² The court also noted the willingness of Texas courts in sworn account cases, formerly governed by the two-year statute of limitations, to decide that section 2-725 supersedes the pre-Code rule where the account arises from a sale transaction.⁷³

The court in *Morton* is less convincing when it considers the question of when the period of limitations begins to run. Section 2-725(2) provides:

A cause of action accrues when the breach occurs, regardless of the aggrieved party's lack of knowledge of the breach. A breach of warranty occurs when tender of delivery is made, except that where a warranty explicitly extends to future performance of the goods and discovery of the breach must await the time of such performance the cause of action accrues when the breach is or should have been discovered.

Despite the wording of this section, which points to the date tender of delivery is made, the court concluded that the pre-Code Texas rule that the period begins to run from the date a personal injury occurs is unchanged by the enactment of the Code. The court cited the case of *Puretex Lemon Juice, Inc. v. S. Riekes & Sons of Dallas, Inc.*⁷⁴ The court in *Puretex* construed the statutory language "after the cause of action shall have accrued"⁷⁵ to mean that the statute of limitations does not begin to run until the buyer discovers or should discover the injury because it is not until then that the buyer can assert a claim for relief. The *Puretex* court notes, however, that this rule is contrary to the majority rule in other jurisdictions where the courts held that there is a breach of the implied warranty at the time of sale. The Code draftsmen

69. TEX. REV. CIV. STAT. ANN. art. 5526(6) (Vernon 1958).

70. The rule was most recently reaffirmed in the pre-Code cases of *Metal Structures Corp. v. Plains Textiles, Inc.*, 470 S.W.2d 93 (Tex. Civ. App.—Amarillo 1971, writ ref'd n.r.e.), and *Richker v. United Gas Corp.*, 436 S.W.2d 215 (Tex. Civ. App.—Houston [1st Dist.] 1968, writ ref'd n.r.e.).

71. See TEX. BUS. & COMM. CODE ANN. § 1.102 (Vernon 1968). See also *General Comment of National Conference of Commissioners on Uniform State Laws and the American Law Institute, UNIFORM COMMERCIAL CODE*, at ix (1972 Official Text). "This act purports to deal with all the phases which may ordinarily arise in the handling of a commercial transaction, from start to finish." *Id.* at xi.

72. 408 F. Supp. at 11; see TEX. BUS. & COMM. CODE ANN. §§ 2.714, .715(b)(2) (Vernon 1968).

73. See cases cited at notes 66-67 *supra* and accompanying text.

74. 351 S.W.2d 119 (Tex. Civ. App.—San Antonio 1961, writ ref'd n.r.e.).

75. This language appears in the preamble to article 5526. TEX. REV. CIV. STAT. ANN. art. 5526 (Vernon 1958).

adopted the majority rule and this rule is followed in the jurisdictions which have adopted the Code. The district court in *Morton* made no reference here to the need to make the rules uniform between the different jurisdictions and did not discuss underlying policies.⁷⁶ A state court faced with a similar cause of action should, therefore, re-examine this question in detail.

III. NEGOTIABLE INSTRUMENTS

Obligations of accommodation parties and guarantors were the subject of the most important and interesting negotiable instrument cases in this survey period. The survey of creditors' rights in this issue⁷⁷ discusses this topic with special emphasis on the right of a guarantor to raise the claim of usury, and that *Survey* article should be consulted together with the discussion which follows. This part of the survey of commercial transactions examines the non-usury aspects of these accommodation party cases and also notes a number of other cases which illustrate basic Code rules. Not discussed are the considerable number of negotiable instruments cases which are decided on procedural points.⁷⁸

A. Accommodation Parties

The case of *Universal Metals & Machinery, Inc. v. Bohart*⁷⁹ caused the hearts of Texas commercial lawyers and their clients to flutter before the Texas Supreme Court hastily reversed itself on rehearing, withdrew its previous opinion, and gave creditors a sweeping victory. Although the major issue on rehearing was whether the "guarantors" on the note could successfully assert their claim of usury, the opinion also had important implications for the status and liability of the guarantor of payment on a note.

Defendant Boharts signed the following statement on a promissory note:

FOR VALUE RECEIVED, the undersigned — as primary obligor(s), hereby (jointly and severally) unconditionally guarantee(s) the prompt payment of principal and interest on the foregoing promissory note when and as due in accordance with its terms, and hereby waive(s) diligence, presentment, demand, protest, or notice of any kind whatsoever, as well as any requirement that the holder exhaust any right or take any action against the maker of the foregoing promissory note and hereby consent(s) to any extension of time or renewal thereof.

76. Such policies might include maximizing the possibility of adequately protecting plaintiffs with personal injuries, the need to ensure that evidence is preserved, and the need for sellers to face a certain time period during which claims may be made so that they can provide for potential liability by reserves or by insurance.

77. Dorsaneo, *Creditors' Rights*, p. 213 *infra*.

78. The procedural advantages of enforcing obligations represented by negotiable instruments are enhanced by a number of common pleading defects in defendants' pleadings. Rules 93 [certain pleas to be verified] and 94 [affirmative defenses] are sometimes overlooked. *See* TEX. R. CIV. P. 93(h)-(j), 94. Some confusion may result because the Code itself has some rules on pleading, defenses, and burden of proof. *See, e.g.*, TEX. BUS. & COMM. CODE ANN. §§ 1.201(8), .201(31), 3.306, .307 (Vernon 1968).

79. 539 S.W.2d 874 (Tex. 1976), *rev'g* 523 S.W.2d 279 (Tex. Civ. App.—Dallas 1975). The opinion reported in S.W. 2d is the opinion after rehearing. An earlier supreme court opinion was withdrawn at this time. The earlier opinion held that the Boharts were liable on the note but were not barred from raising the usury claim. The earlier opinion is reported at 19 Tex. Sup. Ct. J. 212 (March 13, 1976). For an extended critical review of the court of civil appeals opinion reversed by the supreme court see Henderson, *Commercial Transactions, Annual Survey of Texas Law*, 30 Sw. L.J. 118, 130-33 (1976).

The "maker" of the note was a Mexican company. The note was given in payment for machinery to be delivered by the payee to the Mexican company. The Boharts owned a large part of the stock of the Mexican company and also owned all the stock in another corporation which had exclusive U.S. sales rights to the Mexican company's production.

The majority of the court of civil appeals found the terms "primary obligor(s)" and "guarantor" to be mutually exclusive and ruled that the resulting ambiguity should be resolved in favor of a guaranty, which imposes only secondary liability. Since the jury found that the signature of the authorized representative of the maker was forged, the maker was not liable on the note.⁸⁰ The court of civil appeals held that because the maker was not liable the guarantors were not liable.

Disagreeing with the lower court, the supreme court found no inconsistency between the terms "primary obligor(s)" and "guarantor." The court noted that the liability of a guarantor of payment under section 3-416 of the Code is the same as that of a co-maker.⁸¹ The majority opinion concluded, therefore, that the Boharts were guarantors of payment. Justice Steakley, in his dissenting opinion, suggested that section 3-416 does not apply when the contract of guaranty has stated terms and conditions beyond a simple phrase of guaranty added to a signature.⁸² The lengthy clause in this case, however, adds nothing to what is implicit in a guaranty of payment, and the clause surely consists of "equivalent words" to the phrase "payment guaranteed."⁸³

Having concluded that the Boharts were guarantors of payment, the majority opinion then cited numerous cases for the proposition that a guarantor of payment is liable despite the forged signature of the maker. Unfortunately, with the possible exception of *Newark Finance Corp. v. Acocella*,⁸⁴ the cases cited are not on point. It is respectfully suggested that the court overlooked the key point of whether the plaintiff in this case was a holder in due course of the promissory note. If the plaintiff was a holder in due course, there are several cases which hold that a holder in due course may recover from a co-maker despite the forgery of another co-maker's signature.⁸⁵ Since a guarantor of payment is liable as a co-maker, these cases should be relevant in *Bohart*. On the other hand, if the plaintiff is merely a holder of the note, then under general principles of suretyship law the guarantor should be permitted to raise the principal debtor's defense of forgery.⁸⁶ A payee may

80. TEX. BUS. & COMM. CODE ANN. § 3.401(a) (Vernon 1968).

81. The court cites *id.* § 3.416(a) and the accompanying comment ("the liability of the indorser [who guarantees payment] becomes indistinguishable from that of a co-maker"). 539 S.W.2d at 874.

82. 539 S.W.2d at 881.

83. TEX. BUS. & COMM. CODE ANN. § 3.416(a) (Vernon 1968) states: "Payment guaranteed or equivalent words added to a signature mean that the signer engages that if the instrument is not paid when due he will pay it according to its tenor without resort by the holder to any other party." (Emphasis added.)

84. 115 N.J.L. 388, 180 A. 862 (Sup. Ct. 1935). Compare the treatment of this case by the court of civil appeals. 523 S.W.2d at 284 n.3.

85. See, e.g., *Schmidt v. Archer*, 113 Ind. 365, 14 N.E. 543 (1887); *Wheeler v. Traders' Deposit Bank*, 107 Ky. 653, 55 S.W. 552 (Ct. App. 1900); *Morris Plan Co. v. Adler*, 126 Misc. 237, 213 N.Y.S. 227 (Sup. Ct. 1925). These cases are cited in Peters, *Suretyship Under Article 3 of the Uniform Commercial Code*, 77 YALE L.J. 833, 866 n.142 (1968).

86. See Peters, *supra* note 85, at 838-42, 867-68. The principles of law and equity, including principles of suretyship, supplement the Code's provisions. TEX. BUS. & COMM. CODE ANN. §

qualify as a holder in due course.⁸⁷ It would seem that once defendant "guarantor" raised the defense of forgery, the plaintiff payee would have to establish its status as a holder in due course in order to take the instrument free of the defense.⁸⁸

A second line of defense raised by the Boharts was that there was no consideration for their agreement to guarantee payment. In addition to the recital "value received" on the note itself, the supreme court found sufficient evidence that consideration had been given to support the guaranty agreement between the guarantors and the payee.⁸⁹ The court noted the relationship between the Boharts and the Mexican company and concluded that credit extended to the Mexican company would benefit the Boharts. The promise of a surety is not binding without consideration, but the consideration which supports the promise of the principal debtor will normally also support the guarantor's contract.⁹⁰ If, however, the principal obligor has already received the consideration, a guarantor's subsequent promise must be supported by new consideration. In *Bohart* the machinery was delivered to Mexico after the Mexican company had discussed financing with the Boharts but before the Boharts had signed the promissory note. Apparently the court decided that new consideration for the later signing must be found; otherwise, the guarantors should escape liability under the general surety principles noted above.

In addition, prior to the trial defendants filed a plea in abatement demanding that plaintiff bring action against the principal obligor. The defendants apparently relied on section 34.02 of the Texas Business and Commerce Code.⁹¹ The trial court overruled the plea. The court of civil appeals noted this procedural history but did not comment on the merits.⁹² In apparent reference to this issue, the majority opinion of the supreme court noted that the Boharts waived any right to have the holder of the note exhaust its rights against the maker as a condition precedent to their liability.⁹³ The court's basis is the Code's basic principle that the parties' agreement should be enforced, citing section 1-102 of the Code. This conclusion is consistent with decisions which hold that statutory rights or privileges may be waived where third party interests are not affected.⁹⁴ Although the waiver of the right to have the

1. 103 (Vernon 1968). It is clear that the maker in *Bohart* is not liable on the note. "No person is liable on an instrument unless his signature appears thereon." *Id.* § 3.401(a).

87. TEX. BUS. & COMM. CODE ANN. § 3.302(b)s (Vernon 1968). Section 3.305(b) allows the holder in due course to avoid "all defenses of any party to the instrument with whom the holder has not dealt." Here, however, the payee dealt with both the Mexican company (maker) and the Boharts (guarantors of payment).

88. TEX. BUS. & COMM. CODE ANN. §§ 3.306, .307(c) (Vernon 1968). In response to a special issue the jury found that Universal Metals accepted the instrument without knowledge of the forgery. Counsel for Universal requested this special issue based on 72 C.J.S. *Principal & Surety* §§ 18, 74 (1951). Letter from John H. McElhaney to Peter Winship, Dec. 29, 1976.

89. 539 S.W.2d at 878-79.

90. See generally L. SIMPSON, HANDBOOK ON THE LAW OF SURETYSHIP 26 (1950).

91. For a recent application of this section in the context of negotiable instruments see *First Nat'l Bank v. Hargrove*, 503 S.W.2d 856 (Tex. Civ. App.—Texarkana 1973, no writ).

92. 523 S.W.2d at 281.

93. 539 S.W.2d at 877.

94. See the related discussion of the right to waive a statutory right to have the principal obligor joined in the action by holder against guarantor at notes 208-17 *infra* and accompanying text.

creditor proceed first against the principal obligor is spelled out specifically in the note in *Bohart*, there is precedent for the proposition that guaranteeing payment by itself waives the analogous right to have the principal obligor joined in a proceeding against the guarantor.⁹⁵

A final point on *Bohart* relates to the subrogation rights of the Boharts upon payment of the note. Ordinarily a guarantor who pays a negotiable instrument under these circumstances has the advantage of suing on the instrument. However, the Boharts cannot recover on the note because of the forged signature of maker's authorized representative. Under general suretyship principles⁹⁶ the Boharts should be subrogated not only to payee's rights on the note but also to payee's rights on the underlying transaction. Payee delivered machinery to the Mexican company and would no doubt be entitled to recover the value of this machinery. The Boharts should therefore be able to enforce these rights in an action against the Mexican company.⁹⁷

Subrogation rights of accommodation parties also figured in *Seale v. Hudgens*.⁹⁸ The San Antonio court of civil appeals held in that case that an accommodation party on a note who pays the payee-holder of the note is subrogated to the rights of the payee, including the payee's rights under a written agreement by the accommodated party to pay the notes in a specified county. The court relies on pre-Code law⁹⁹ and section 3-415(5) of the Code.¹⁰⁰ Although the decision relates only to venue, the court's holding suggests that when the accommodation party pays the holder of an instrument he is subrogated not only to the holder's rights on the instrument but also on the underlying obligation. Although this conclusion may stretch the wording of section 3-415(5) ("recourse on the instrument"), it should be approved on the basis of the general suretyship rules applicable by virtue of section 1-103 of the Code.¹⁰¹

Whether defendant maker was an accommodation party for the plaintiff payee and, therefore, not obligated to the payee under section 3-415(5) was an issue in *McPherson v. Longview United Pentecostal Church, Inc.*¹⁰² Pursuant to an agreement between maker and payee, the payee constructed a parking lot for the maker. Maker alleged that it issued the note, which was in the amount of the agreed contract price, to help the payee obtain interim financing. Although the note was negotiated to the bank providing the financing, the bank required the payee to sign his personal note for each

95. *Ganado Land Co. v. Smith*, 290 S.W. 920 (Tex. Civ. App.—Galveston 1927, writ ref'd). The guarantor's right to insist on joinder is set out in TEX. REV. CIV. STAT. ANN. arts. 1986, 1987 (Vernon 1964), discussed at notes 208-17 *infra* and accompanying text.

96. L. SIMPSON, *supra* note 90, § 47.

97. Where the action could be brought and what law would govern the action pose difficult enforcement problems. As Justice Guittard noted in his dissent in the court of civil appeals: "Any suit against the corporation might have to be prosecuted in Mexico, and aside from the inconvenience of such a remedy, the enforceability of such a note under Mexican law may not have been entirely clear." 523 S.W.2d at 292.

98. 538 S.W.2d 459 (Tex. Civ. App.—San Antonio 1976, writ dismissed).

99. *Fox v. Kroeger*, 119 Tex. 511, 35 S.W.2d 679 (1931).

100. TEX. BUS. & COMM. CODE ANN. § 3.415(e) (Vernon 1968): "An accommodation party is not liable to the party accommodated, and if he pays the instrument has a right of recourse on the instrument against such party."

101. L. SIMPSON, *supra* note 90, § 47. See also J. WHITE & R. SUMMERS, *supra* note 24, § 13-16.

102. 540 S.W.2d 424 (Tex. Civ. App.—Tyler 1976, writ ref'd n.r.e.).

advance, and the bank did not credit the advance to the original maker's note. The note was renegotiated to the payee before trial and he sought to enforce it. The jury found that the note was executed to enable the payee to secure interim financing. The appellate court concluded, however, that the maker did not lend its name to the payee *as a surety*, and, therefore, as a matter of law the maker was not an accommodation party. The court reasoned that without a third party on the note when it was issued the issue was for a special purpose or a conditional delivery as to payment, and that evidence of this condition was not, and could not, be introduced to vary the terms of the note.¹⁰³ If this reading of the opinion is correct, the premise is questionable. A maker may be an accommodation party for the payee on a note where the parties contemplate negotiation of the instrument by the payee in order for him to secure credit, as the jury found the parties intended in this case.¹⁰⁴ To find that the maker of the note is an accommodation party does not mean, as payee contended, that the maker then receives a parking lot for nothing. Payee may still enforce his underlying contract rights but without the procedural advantages of suing on a negotiable instrument.

B. Acceleration of Payment

In *Bowie National Bank v. Stevens*¹⁰⁵ the Texas Supreme Court reversed the opinion of the court of civil appeals noted in last year's *Annual Survey*.¹⁰⁶ The maker of the note and his transferee, who had assumed payments on the note, had been allowed by the holders of the note to fall in arrears, although by the terms of the note the holder had the right to accelerate the note on default as to any installment. The bank purchased the note and deed of trust with knowledge that payments were delinquent and took the note for the specific purpose of foreclosing on it. The bank did not demand payment of the delinquent installments; when the obligor on the note sought to pay an installment, the bank's president persuaded him to apply the sum tendered to another note. The supreme court held that "[u]nder these facts, [the obligor] was charged with knowledge that he could no longer rely on the holder to further waive its right to insist upon strict compliance with the note and deed of trust."¹⁰⁷ The waiver no longer being in effect, the obligor had to tender the full amount of the delinquent installments to avoid default and foreclosure. The obligor failed to do so, and the foreclosure was proper. In effect, the court ruled that failure to accelerate when payments on the note are delinquent is not a waiver of a continuing right to accelerate. There may be waiver of a right to accelerate when payment of a late installment is accepted. Where installments continue to be delinquent, however, the right to accelerate is not waived but merely not exercised. Additional circumstances may estop the obligee from enforcing the contract, but this would not be a waiver. The

103. 540 S.W.2d at 430-31.

104. See *Darden v. Harrison*, 511 S.W.2d 925 (Tex. 1974). Oral evidence of the accommodation may be introduced pursuant to § 3-415(3). TEX. BUS. & COMM. CODE ANN. § 3.415(c) (Vernon 1968).

105. 532 S.W.2d 67 (Tex. 1975), *rev'g* 517 S.W.2d 686 (Tex. Civ. App.—Fort Worth 1974).

106. *Henderson*, *supra* note 79, at 128-29.

107. 532 S.W.2d at 68.

supreme court in *Bowie National Bank* came to the correct result but may have confused the issue by speaking of "waiver" and "withdrawing a waiver."

In an important decision last year, the Texas Supreme Court held that in the absence of a clear legislative repeal of the pre-Code rule that notice must be given of an intent to accelerate, the holder must give this notice as a prerequisite to accelerating.¹⁰⁸ In *Sylvester v. Watkins*¹⁰⁹ the Amarillo court of civil appeals approved the prior waiver of this right to receive notice of an intent to accelerate. The note in this case stated that the maker "expressly waives all notices, demands for payment, presentations for payment, notices of intention to accelerate the maturity, protest and notice of protest, as to this note and as to each, every and all installments hereof." The court noted that section 3-511(2)(a) of the Code¹¹⁰ and prior case law supported its conclusion that notice can be expressly waived.¹¹¹ Given that the drafting of instruments is usually in the hands of payee-creditors, one would expect that this right to notice will be waived in most instances. If the harshness of acceleration is as serious as the Texas Supreme Court suggested in the earlier decision, the legislature should deal explicitly with this issue and perhaps limit the instances in which the right to notice of acceleration may be waived.

C. Authorized Signatures

A basic principle of article 3 of the Code is that no person is liable on a negotiable instrument unless his or her signature appears on the instrument.¹¹² An agent or other representative must be careful to indicate on the instrument both the name of the principal and the fact of agency.¹¹³ In *Griffin v. Ellinger*¹¹⁴ the Texas Supreme Court affirmed a decision which held a corporate officer personally liable as the drawer of a check. Defendant Griffin, president of Greenway Building Co., Inc. (Greenway), signed three checks drawn on the Greenway account at the Northeast Bank of Houston. The checks were issued to plaintiff Ellinger in payment for labor and services supplied for a construction project on which Greenway was prime contractor. Payment of the checks was refused because of insufficient funds. Griffin

108. *Allen Sales & Serv. Center, Inc. v. Ryan*, 525 S.W.2d 863 (Tex. 1975), *rev'g* 517 S.W.2d 700 (Tex. Civ. App.—Forth Worth 1974).

109. 538 S.W.2d 827 (Tex. Civ. App.—Amarillo 1976, writ *ref'd n.r.e.*).

110. The section cited by the court does not specifically refer to intent to accelerate. TEX. BUS. & COMM. CODE ANN. § 3.511(b)(1) (Vernon 1968). *See also id.* § 1.208.

111. *Whalen v. Etheridge*, 428 S.W.2d 824 (Tex. Civ. App.—San Antonio 1968, writ *ref'd n.r.e.*); *Interstate Life Ins. Co. v. Turner*, 371 S.W.2d 913 (Tex. Civ. App.—Waco 1963, writ *ref'd n.r.e.*). *See also Justice Mortgage Investors v. C.B. Thompson Constr. Co.*, 533 S.W.2d 939 (Tex. Civ. App.—Amarillo 1976, writ *ref'd n.r.e.*).

112. TEX. BUS. & COMM. CODE ANN. § 3.401(a) (Vernon 1968).

113. *Id.* § 3.403. Section 3.403(b) states:

- An authorized representative who signs his own name to an instrument
- (1) is personally obligated if the instrument neither names the person represented nor shows that the representative signed in a representative capacity;
 - (2) except as otherwise established between the immediate parties, is personally obligated if the instrument names the person represented but does not show that the representative signed in a representative capacity, or if the instrument does not name the person represented but does show that the representative signed in a representative capacity.

114. 530 S.W.2d 329 (Tex. Civ. App.—Austin 1975), *aff'd*, 538 S.W.2d 97 (Tex. 1976). The decision is noted in UCC L. LETTER, Dec. 1976, at 1.

argued that the check showed on its face that it was signed in his representative capacity, and that extrinsic evidence established as a matter of law that the parties understood that his signature was made in a representative capacity. As to the first point, the court ruled that the check itself contained no information as to the capacity in which Griffin signed. The face of the instrument is reproduced in the West reports¹¹⁵ showing the printed name of "Greenway Bldg. Co., Inc." and a check protection imprint showing "Greenway Building Inc." before the amount of the check. Griffin's signature appears, however, with nothing following his name. The court ruled that as between the immediate parties to the check extrinsic evidence is admissible to show the parties understood that the signature was that of an authorized representative and that Griffin had the burden of showing that he disclosed his representative capacity. Disclosure need not be shown to be contemporaneous with the signing of the instrument but may be evidenced by prior dealings between the parties.¹¹⁶ The court concluded that there was sufficient proof to support the trial court's conclusion that Griffin signed in his personal capacity and affirmed judgment for Ellinger on the check.¹¹⁷

D. *Collecting Bank*

The Texas Supreme Court explores the scope of the duties of a collecting bank in *Citizens First National Bank v. Cinco Exploration Co.*¹¹⁸ After initiating collection of a documentary draft the collecting bank in this case received a cashier's check together with a letter instructing the bank not to release the check until its customer had performed the underlying agreement. The supreme court held that the collecting bank owed no duty to the owner of the cashier's check to insure that its customer had performed, and it was, in any case, not bound by the "nebulous" instructions conveyed to it. The collecting bank therefore was entitled to summary judgment in a suit brought against it by the other party to the underlying transaction to recover the amount of the cashier's check which the collecting bank had paid to the account of its customer.

E. *Contemporaneous Writings*

Under section 3-119 of the Code the terms of an instrument may be modified or affected by a contemporaneous writing as between the obligor and his immediate obligee. In *Commerce Savings Association v. GGE Management Co.*¹¹⁹ the appellate court ruled that a separate written agreement between the guarantor of a note and the payee should be enforced between the parties when both the agreement and the note were executed as part of the same transaction. The clause in the agreement limiting the liability of the

115. 538 S.W.2d at 99.

116. *Id.* at 100. On this point the court referred to the more elaborate opinion in *Seale v. Nichols*, 505 S.W.2d 251 (Tex. 1974).

117. See the discussion of the personal liability of an agent in *J. WHITE & R. SUMMERS*, *supra* note 24, § 13-4.

118. 540 S.W.2d 292 (Tex. 1976), *rev'g* 529 S.W.2d 852 (Tex. Civ. App.—Tyler 1975).

119. 539 S.W.2d 71 (Tex. Civ. App.—Houston [1st Dist.] 1976), *aff'd per curiam with modification on another point*, 20 Tex. Sup. Ct. J. 71 (Nov. 27, 1976), *mandate recalled*, 20 Tex. Sup. Ct. J. 233 (March 12, 1977).

guarantor of the note was given effect and the reduced liability meant the obligation was no longer usurious.

F. Conversion

In *Tubin v. Rabin*¹²⁰ the Fifth Circuit affirmed per curiam a district court decision finding a depository bank liable for conversion when it paid the proceeds of a cashier's check to a payee who had forged the signature of a co-payee. The district court decision is noteworthy for two reasons. First, the court allowed the purchaser of the cashier's check, whose name did not appear on the check, to bring suit as "owner" of the check. The bank issuing a cashier's check is both drawer and drawee so that the purchaser of the check is not, in fact, the drawer of the check. The payee of the check was the purchaser's attorney. Given that the payee, as agent of the purchaser, would have had to turn over any recovery from defendant to the purchaser, the court's approval of plaintiff's standing was appropriate. A second, more serious question, however, concerned defendant depository bank's defense under section 3-419(3).¹²¹ The Fifth Circuit's per curiam opinion does not refer to this question, but in its supplemental opinion the district court examined this defense. The district court ruled that section 3-419(3) governed the "true agency situation rather than the typical bank transaction" and, apparently as an alternative holding, that in any case the defendant had failed to prove that it had dealt with the check in a commercially reasonable manner.¹²² While this result is consistent with court decisions on the depository bank's conversion liability, the interpretation overlooked the phrase "including a depository or collecting bank" in section 3-419(3).¹²³ When a state court examines the issue, this interpretation of section 3-419 should be re-examined.

G. Definite Time for Payment

Section 3-104(1)(c) of the Code requires an instrument to "be payable on demand or at a definite time" in order to be a negotiable instrument within article 3 of the Code. Section 3-109(1)(c) indicates that an instrument meets the "definite time" requirement if the instrument states that it is payable "at a definite time subject to any acceleration." In *Caruth v. United States*¹²⁴ the promissory notes were due sixteen years after issuance but could be prepaid if there was sufficient cash flow from a specified partnership. Citing the above Code sections and comment 4 to section 3-109, the federal district court held

120. 533 F.2d 255 (5th Cir. 1976), *aff'g* 382 F. Supp. 193, 389 F. Supp. 787 (N.D. Tex. 1974).

121. TEX. BUS. & COMM. CODE ANN. § 3.419(c) (Vernon 1968) states:

Subject to the provisions of this title concerning restrictive indorsements a representative, including a depository or collecting bank, who has in good faith and in accordance with the reasonable commercial standards applicable to the business of such representative dealt with an instrument or its proceeds on behalf of one who was not the true owner is not liable in conversion or otherwise to the true owner beyond the amount of any proceeds remaining in his hands.

122. 389 F. Supp. at 789-90.

123. See J. WHITE & R. SUMMERS, *supra* note 24, § 15-4. For a recent case which discusses the *Tubin* decision see *Twellman v. Lindell Trust Co.*, 534 S.W.2d 83, 95, 98 (Mo. Ct. App. 1976). See also 41 MO. L. REV. 99 (1976).

124. 411 F. Supp. 604 (N.D. Tex. 1976).

that under state law the notes were definite as to time and, therefore, enforceable negotiable instruments.¹²⁵

H. Discharge

In *Eikel v. Bristow Corp.*¹²⁶ an independent testamentary executor of the estate of an accommodation party on three promissory notes received an assignment of the notes from the payee. The executor continued an action brought by the payee on the notes against the maker and other accommodation endorsers. The other accommodation endorsers argued that they were discharged because the executor was a party who himself had no right of action or recourse on the instrument re-acquired.¹²⁷ The court ruled, however, that the instruments were acquired by the executor, not by the deceased, and the executor, therefore, was not a prior party on the notes. The accommodation parties were liable in their capacity as endorsers of the notes. As an accommodation endorser, decedent was named a defendant in the suit initially brought by the payee. The executor voluntarily answered on suggestion of death being filed. Nevertheless, the court ruled that a foreign executor had no standing to defend the suit and his voluntary action did not operate to continue the suit as to decedent.¹²⁸

I. Material Alteration

In *Sea Hoss Marine Enterprises, Inc. v. Angleton Bank of Commerce*¹²⁹ defendant answered that one of the instruments on which plaintiff sued had been completed by the plaintiff's authorized representative for an amount greater than that authorized by defendant. The court ruled that if defendant carried the burden of showing that plaintiff or his authorized agent had materially altered the instrument without defendant's authorization, then defendant would be discharged.¹³⁰ The court found sufficient evidence to raise fact issues so that an instructed verdict for plaintiff was improper, and the appellate court reversed and remanded on this point.¹³¹ Apparently, the court overlooked the need for defendant to show *both* materiality *and* fraudulent intent before there is a discharge under section 3-407(2)(a) of the Code. Here there was no attempt to show fraud on the part of the plaintiff. The relevant provision would seem to be section 3-407(2)(b), which would have allowed the plaintiff to recover the amount actually authorized by the defendant in this case.

125. *Id.* at 609.

126. 529 S.W.2d 795 (Tex. Civ. App.—Houston [1st Dist.] 1975, no writ).

127. TEX. BUS. & COMM. CODE ANN. §§ 3.208, .601(a)(5) (Vernon 1968).

128. The court noted, but declined to discuss because the matter had not been raised in the trial court, § 324 of the Probate Code. 529 S.W.2d at 801. This section provides that it is unlawful for an executor to purchase any claim against the estate he represents. TEX. PROB. CODE ANN. § 324 (Vernon 1956). Query whether this section could be raised by the other accommodation parties. TEX. BUS. & COMM. CODE ANN. § 3.306(4) (Vernon 1968).

129. 536 S.W.2d 592 (Tex. Civ. App.—Houston [1st Dist.] 1976, writ ref'd n.r.e.).

130. TEX. BUS. & COMM. CODE ANN. §§ 3.115(b), .407(a), .407(b)(1) (Vernon 1968).

131. 536 S.W.2d at 594-95. On a second note defendant pleaded economic duress. While conceding that duress is a matter of degree and generally a question of fact, the appellate court held that "whether established facts will constitute the legal defense of duress is a matter of law to be determined by the court." *Id.* at 596. In this case the court found no factual issue on the defense of duress so that judgment for plaintiff was affirmed.

Defendant maker of a note in *Lawler v. Federal Deposit Insurance Co.*¹³² also asserted that material alterations were fraudulently made to the note which he signed. The appellate court noted correctly that in order to be discharged under section 3-407(2)(a) defendant had to show (a) alteration by the holder, (b) fraudulent intent, and (c) material alteration. The jury in this case had found the alterations material but did not find an intent to defraud; it had not been asked who altered the note. The appellate court therefore affirmed judgment for plaintiff.

J. Right to Recover on Instrument

To recover on a negotiable instrument which does not show how it came into the hands of the plaintiff requires the introduction of additional evidence in order to show that plaintiff is the "owner" of the claim. In *Lawson v. Finance America Private Brands, Inc.*,¹³³ the notes were payable to the order of "GAC Private Brands, Inc." Plaintiff, Finance America Private Brands, Inc., alleged that its former corporate name was GAC Private Brands, Inc. There was, however, no endorsement on the notes and no evidence in the record as to how the change in name took place. Defendant-maker, nevertheless, testified under direct examination that the plaintiff's former name was that of the payee. The appellate court found this admission supplied the missing proof as to plaintiff's right. More importantly, the court ruled that the necessary proof was not supplied by constructive admission under rule 93¹³⁴ because what was involved was proof that the plaintiff was a holder, rather than the capacity of plaintiff. Attorneys, in other words, must be prepared to show how the instrument came into the hands of plaintiff.¹³⁵

K. Third Party Defenses

Section 3-306(d) of the Code provides that except for theft and transfers inconsistent with a restrictive indorsement "[t]he claim of any third person to the instrument is not otherwise available as a defense to any party liable thereon unless the third person himself defends the action for such party." In *Harvey v. Casebeer*¹³⁶ a trustee sought to enforce four promissory notes payable to the trust against the maker of the notes. The trustee had transferred the notes to himself individually for full consideration and sought to enforce the notes as transferee. The maker sought to avoid liability by raising the defense that the transfer was in violation of the Texas Trust Act.¹³⁷ The court of civil appeals correctly held that although the transferee was not a holder in due course because he purchased the notes with knowledge that they were negotiated by a fiduciary in breach of his fiduciary duty,¹³⁸ the maker of the notes cannot raise the claim of a third person (the trust beneficiary in this case) as a defense to his own liability.¹³⁹ Maker's payment of the notes would

132. 538 S.W.2d 245 (Tex. Civ. App.—Beaumont 1976, no writ).

133. 537 S.W.2d 483 (Tex. Civ. App.—El Paso 1976, no writ).

134. TEX. R. CIV. P. 93(i).

135. See TEX. BUS. & COMM. CODE ANN. §§ 3.201, .301 (Vernon 1968).

136. 531 S.W.2d 206 (Tex. Civ. App.—Tyler 1975, no writ).

137. TEX. REV. CIV. STAT. ANN. art. 7425b-12 (Vernon Supp. 1976-77).

138. TEX. BUS. & COMM. CODE ANN. §§ 3.302(a)(3), .304(b)s (Vernon 1968).

139. *Id.* § 3.306(4).

discharge him even if he knew that the holder had acquired the notes in breach of his duty of loyalty to the trust.¹⁴⁰

IV. SECURED TRANSACTIONS

A. *The Rights of Parties Following Default*

When a debtor is in default under a security agreement, the secured party has the rights and remedies provided in part 5 of article 9 and, subject to mandatory provisions in that part, the rights and remedies set out by the parties in the security agreement.¹⁴¹ Numerous cases have passed on the propriety of the conduct of the secured party when he seeks to realize on collateral following default and the remedies of the debtor when the secured party proceeds improperly.¹⁴² Texas courts in 1976 have considered default procedures and have handed down important interpretations of sections 9-504 and 9-507 of the Code.

In *Christian v. First National Bank*¹⁴³ the bank (the secured party) sold the collateral pledged to it and repossessed by it and brought an action to recover the deficiency. Among the defenses raised by the defendant debtors was the issue of whether the private sales conducted by the bank were commercially reasonable. The trial court withdrew the issue from the jury on the ground that no fact question existed and directed a verdict for the plaintiff bank. On appeal, the Fort Worth court of civil appeals emphasized the fiduciary duty of the secured party to sell the collateral in a commercially reasonable manner, and stated that plaintiff did not establish "as a matter of law that the property was sold at its fair market value in a reasonably commercial manner and that its fair market value applied as credits on the notes."¹⁴⁴ The court therefore held that it was reversible error to withdraw from the jury the issue of the commercial reasonableness of the sale. Quoting from *Southwestern Investment Co. v. Neeley*,¹⁴⁵ the court suggested that if the debtors could show that the property was sold unfairly or at "an under price," they would be entitled to have an offset in the amount of the property's full market value when computing the deficiency.

140. *Id.* § 3.603(a).

141. *Id.* §§ 9.501-.507 (Vernon Supp. 1976-77).

142. For cases applying Texas law from prior survey periods see *United States v. Whitehouse Plastics*, 501 F.2d 692 (5th Cir. 1974); *First State Bank v. Northrop*, 519 S.W.2d 161 (Tex. Civ. App.—Waco 1975, no writ). These cases are noted in Henderson, *supra* note 79, at 145-47. See generally J. WHITE & R. SUMMERS, *supra* note 24, §§ 26-9 to -15; Siegel, *Commercially Reasonable Disposition of Collateral*, 80 COM. L.J. 67 (1975). See also 29 OKLA. L. REV. 486 (1976); 7 TEX. TECH L. REV. 702 (1976).

143. 531 S.W.2d 832 (Tex. Civ. App.—Fort Worth 1975, writ ref'd n.r.e.). Defendants in *Christian* also claimed that the bank had not allowed specified credits and payments when the bank set out the sums claimed under the secured notes. The trial court held that the two-year statute of limitations barred these claims. The court of civil appeals reversed. The court reasoned that while the statute barred an affirmative action brought to recover these credits, these same credits might be offset against plaintiff's demand if defendants' claims are not barred by limitations at the time plaintiff's action is brought.

144. 531 S.W.2d at 839.

145. 443 S.W.2d 573 (Tex. Civ. App.—Fort Worth 1969), *remanded on exemplary damage issue*, 452 S.W.2d 705 (Tex.), *on remand*, 455 S.W.2d 785 (Tex. Civ. App.—Fort Worth 1970, writ *dism'd*). That a better price might have been obtained does not necessarily make the sale at the lower price commercially unreasonable. TEX. BUS. & COMM. CODE ANN. § 9.507(b) (Vernon 1968).

On rehearing, the bank contended that the Code required defendants to raise the issue of commercial reasonableness by an independent suit for damages and not by way of defense. The appellate court held, however, that in the absence of a statement in section 9-507(1) of the Code that the remedy provided in that section is exclusive, the court would continue to recognize the pre-Code right of a debtor to raise the secured party's improper sale as a defense or a partial defense to an action to obtain a deficiency judgment. As authority for its conclusion the court cited section 1-103 of the Code and judicial precedents. The court quoted from a Nebraska case where the supreme court of that state ruled that where a debtor filed a general denial and introduced evidence that the property sold had not realized a fair and reasonable price, the secured party had the burden of proving that all offsets had been allowed and the matter was a jury question.¹⁴⁶ For pre-Code Texas law the court quoted liberally from the 1964 Texas case of *Kolbo v. Blair*¹⁴⁷ in which the court held that a commercially reasonable sale is a condition precedent to the entry of a proper deficiency judgment and that the debtor should be given credit for the reasonable market value of the property when computing the deficiency.

In *O'Neil v. Mack Trucks, Inc.*¹⁴⁸ the financing corporation (the secured party) repossessed trucks from the dealer (the debtor) at the dealer's request, sold them, and sued for the deficiency. The defendant answered, *inter alia*, by questioning the commercial reasonableness of the resale. No notice of a private sale to the manufacturer was given, and defendant argued that the sales price was unreasonably low. Plaintiffs answered that notice was unnecessary as the trucks were of a type customarily sold on a recognized market, and defendant waived his right to notice. The appellate court rejected the first argument summarily on the ground that the exception to the requirement that notice must be given should be read "most restrictive[ly]."¹⁴⁹ As authority for this narrow reading the court cited "used car" cases. The quotation from one case suggests that the market must be broad, individual differences between items must be immaterial, haggling must not affect the prices paid, and the prices paid in actual sales of comparable property must be currently quoted. The result may be supported by the policy underlying the giving of notice. The debtor may wish to redeem pursuant to section 9-506 or to participate or find others to participate in the sale so that the "market" price will be reached. This policy is also the underpinning of the court's rejection of the waiver argument: If notice must be given, then the debtor may only waive notice by signing "after default a statement renouncing or modifying his right to notification of sale."¹⁵⁰

Having determined that there had been a violation of section 9-504(3), the court turned to the debtor's remedies. The court sets out two lines of cases:

146. *First Nat'l Bank v. Rose*, 188 Neb. 362, 196 N.W.2d 507 (1972).

147. 379 S.W.2d 125 (Tex. Civ. App.—Corpus Christi 1964, writ ref'd n.r.e.). This case, however, involved a private sale to the secured party himself and is distinguishable from *Christian* on the facts.

148. 533 S.W.2d 832 (Tex. Civ. App.—El Paso 1975), writ granted on another point, 542 S.W.2d 112 (Tex. 1976).

149. 533 S.W.2d at 836.

150. *Id.*; TEX. BUS. & COMM. CODE ANN. § 9.504(c) (Vernon Supp. 1976-77).

(1) prohibition of a deficiency judgment, and (2) the creation of a rebuttable presumption that the value of the collateral equals the amount of the debt so that to recover a deficiency the secured party must prove the fair market value of the goods. The court adopted the reasoning of the Fifth Circuit in *United States v. Whitehouse Plastics*,¹⁵¹ which held that the second line of cases was more consistent with the scheme of the Code. The appellate court in *O'Neil* then affirmed the trial court's finding that the plaintiff had carried the burden of showing the market value of the goods sold. The sales price was the same as the price defendant had voluntarily agreed to nine months earlier, and the manufacturer had resold the trucks in arm's-length transactions for only \$1,789.83 more than the price paid to the secured party.

In *Pruske v. National Bank of Commerce*¹⁵² the defendants, parties to a floor plan agreement for motor homes, answered that the plaintiff secured party had not disposed of the collateral in a commercially reasonable manner and, therefore, was not entitled to any recovery. After noting sections 9-504(3) and 9-507(1) of the Code, the San Antonio court of civil appeals ruled that the burden of proving commercial unreasonableness is on the debtor.¹⁵³ The court stressed that mere inadequacy of consideration does not render a foreclosure sale void.¹⁵⁴ The propriety of the sale is a question of fact to be resolved by the trial court. Here the trial court made no findings of fact, and, in accordance with established procedure, the appellate court presumed that the trial court found all necessary facts in favor of the judgment for plaintiff.

The Texarkana court of civil appeals heard an appeal from a lower court's award of expenses incurred by secured parties in storing, insuring, and preserving repossessed collateral in *Davis v. Small Business Investment Co.*¹⁵⁵ The debtor appellant argued that the plaintiffs were required to show that the expenses were "reasonable" and that plaintiffs had produced no evidence so showing. Section 9-207(2)(a) provides that the secured party is entitled to "reasonable" expenses incurred in the custody, preservation, use, or operation of the collateral unless otherwise agreed.¹⁵⁶ The plaintiffs claimed that the security agreement provided otherwise.¹⁵⁷ The court con-

151. 501 F.2d 692 (5th Cir. 1974).

152. 533 S.W.2d 931 (Tex. Civ. App.—San Antonio 1976, no writ).

153. *Id.* at 935. The court cites Tarrant Sav. Ass'n v. Lucky Homes, Inc., 390 S.W.2d 473 (Tex. 1965); Fryer & Willis Drilling Co. v. Oilwell, Div. of U.S. Steel, 472 S.W.2d 857 (Tex. Civ. App.—Waco 1971), *rev'd on other grounds*, 493 S.W.2d 487 (Tex. 1973). The Texas rule is a minority rule and should be re-examined. A basic purpose of the Uniform Commercial Code is to make uniform the commercial law of the different jurisdictions in the United States. TEX. BUS. & COMM. CODE ANN. § 1.102(b)(3) (Vernon 1968). See generally J. WHITE & R. SUMMERS, *supra* note 24, at 994-95.

154. TEX. BUS. & COMM. CODE ANN. § 9.507(b) (Vernon Supp. 1976-77).

155. 535 S.W.2d 740 (Tex. Civ. App.—Texarkana 1976, writ ref'd n.r.e.).

156. Section 9-207 governs the rights and duties of secured parties in possession of the collateral both before and after default. TEX. BUS. & COMM. CODE ANN. §§ 9.207, .501(a) (Vernon Supp. 1976-77).

157. The security agreement provided:

'Reimbursement of expenses—at secured parties option, secured party may . . . for and in behalf of debtor—pay for the repair, maintenance and preservation of collateral, and all sums so expended, including but not limited to attorney's fees, court costs, agent fees or commissions or any other costs or expenses shall bear interest from the date of payment at the rate of ten per cent per annum and shall be payable at the place designated in the above described note and shall be secured by this security agreement.'

535 S.W.2d at 744.

cluded, however, that in the absence of specific language to the contrary the parties contracted with reference to the statutory standard. It adopted a construction of section 9-207 which rejects the possibility that the parties could contract without regard to the reasonableness of the expenses.¹⁵⁸ Plaintiffs produced evidence that the expenditures were necessary but not that they were reasonable. The appellate court held that the trial court should not have directed a verdict against defendant.

In *Jones v. Garcia*¹⁵⁹ the debtor sought and obtained from the trial court an order temporarily enjoining secured parties from foreclosing on the collateral. The court of civil appeals found that the trial court had authority to issue the temporary injunction and had not abused its discretion by doing so. Plaintiff debtor denied receiving the notice mailed to him. In any case, the trial court found that the notice was defective insofar as it attempted to describe the place of sale. The appellate court referred to section 9-504 of the Code but not to section 9-507. If, as was suggested by the court, there had already been a sale of the collateral even under the dubious facts of this case, then the court decided that the debtor not only had the right to recover losses under section 9-507(1) but also the right to the full panoply of the remedies available to a court of equity. It is possible, however, that defendant secured parties did not have possession of the collateral and that the foreclosure sale was, therefore, incomplete.

B. Priorities

This *Annual Survey* reports the final chapter in the celebrated case of *In re Samuels & Co.*¹⁶⁰ After the writing of last year's *Survey*, the Fifth Circuit, sitting en banc, reversed per curiam its previously reported decision and adopted the dissenting opinion of Judge Godbold. Judge Ainsworth, joined by four other judges, dissented from the per curiam order, while Judge Gee concurred specially. On October 4, 1976, the United States Supreme Court denied certiorari. In effect, the district court judgment is affirmed in its decision that a secured party with a secured interest in after-acquired property prevails over unpaid "cash" sellers.

The facts were not in dispute. Sellers delivered cattle to Samuels & Co., a meatpacking firm. The sales price was not set until after processing when the "grade and yield" could be determined. Samuels & Co. then issued checks to the sellers, but the checks were dishonored for lack of funds. Samuels & Co. promptly filed for bankruptcy, and in the bankruptcy proceedings the sellers and a secured inventory financier both claimed the proceeds from the sale of the processed meat.

Judge Godbold's opinion, now adopted by the Fifth Circuit, held that the secured party was a good faith purchaser under section 2-403(1) of the Code; therefore, even if the seller had "reclamation" rights under sections 2-507

158. See 2 G. GILMORE, SECURITY INTERESTS IN PERSONAL PROPERTY § 44.9.2 (1965).

159. 538 S.W.2d 492 (Tex. Civ. App.—San Antonio 1976, no writ).

160. 526 F.2d 1238 (5th Cir.), cert. denied, 97 S. Ct. 98, 50 L. Ed. 2d 79 (1976). The previous appellate decisions in this case are reported at 483 F.2d 557 (5th Cir. 1973), *rev'd and remanded sub nom.* Mahon v. Stowers, 416 U.S. 100 (1974), *original circuit opinion rev'd on remand*, 510 F.2d 139 (5th Cir. 1975). The Fifth Circuit panel decision, which has now been reversed, is discussed critically in Henderson, *supra* note 79, at 139-41.

and 2-511, the secured party's rights under article 9 would prevail over the sellers' rights under article 2. The opinion noted that the sellers could have protected themselves by perfecting their rights under article 9.¹⁶¹ The dissenting judges emphasized that the sale was intended to be for cash rather than for credit and questioned whether the secured party in this case was a good faith purchaser under section 2-403(1). The concurring opinion stated that "the delayed pricing arrangement transformed the 'cash sale' into a credit transaction for all commercial purposes regardless of how the two parties characterized it."¹⁶²

Meanwhile, the Texas Legislature has resolved similar disputes for the future by prescribing payment procedures for "meat processors" and giving livestock sellers a lien with priority over other conflicting liens or security interests.¹⁶³

The opinion in *Samuels* will no doubt be subject to close scrutiny.¹⁶⁴ The author of last year's *Survey* article stated that the reasoning of Judge Godbold should prevail,¹⁶⁵ and a majority of judges on the Fifth Circuit apparently agree. This commentator would probably have gone off on the narrow point that the sellers failed to exercise in a timely manner their "reclamation" rights under section 2-507. In any case, the implications of the opinion are sufficiently far-reaching to deserve greater legislative attention. In the future all sellers who receive payment by check from a buyer who has a creditor with an after-acquired property clause will bear the risk that the buyer will file for bankruptcy before payment of the check, and, therefore, the secured creditor will have prior claims to the goods supplied by the sellers. Perhaps, as Judge Gee's concurring opinion suggested, the case will be distinguished because of the delayed pricing arrangement in the meatpacking context.

In *Ranchers & Farmers Livestock Auction Co. v. First State Bank*¹⁶⁶ a creditor sought to garnish cattle and proceeds from the sale of cattle in the hands of an auction company with whom the cattle had been deposited by the debtor. The seller of the cattle to the debtor intervened. On November 21 the seller sold cattle to the buyer-debtor, payment being made with a check and seller giving buyer a "purchase sheet" which stated, "[t]his contract constitutes a Bill of Sale to the above described livestock, payment for which is hereby acknowledged." The cattle were shipped to the Tulia livestock auction for resale. On November 23 the bank had a writ of garnishment served

161. 526 F.2d at 1246, 1248. Note that the sellers would not only have to file, which is a simple procedure and relatively inexpensive, but also have to notify the prior secured party of its interest before delivering the cattle to the meatpacking firm. TEX. BUS. & COMM. CODE ANN. § 9.312(c) (Vernon Supp. 1976-77). Judge Godbold states: "The procedure is not unduly complex or cumbersome. But whether cumbersome or not, a lender who chooses to ignore its provisions takes a calculated risk that a loss will result." 526 F.2d at 1248.

162. 526 F.2d at 1249.

163. TEX. REV. CIV. STAT. ANN. art. 6910b (Vernon Supp. 1976-77). The legislation is noted in Henderson, *supra* note 79, at 152.

164. The final Fifth Circuit opinion is noted in UCC L. LETTER, Sept. 1976, at 3. The Second Circuit court opinion is noted in 9 CREIGHTON L. REV. 412 (1975). See also Henderson, *supra* note 79, at 139-41. The original 1973 circuit court opinion is noted in 54 B.U. L. REV. 469 (1974); 52 TEXAS L. REV. 570 (1974). For a recent survey of the rights of a reclaiming seller see Anderson, *The Reclaiming Seller under UCC Section 2-702 vs. His Four Horsemen of the Apocalypse*, 8 ST. MARY'S L.J. 271 (1976).

165. Henderson, *supra* note 79, at 141.

166. 531 S.W.2d 167 (Tex. Civ. App.—Amarillo 1975, writ ref'd n.r.e.).

on the auction company to garnish the indebtedness to the debtor. After November 25 and before November 29 debtor executed a security agreement and financing statement for the benefit of the seller. The seller put in the mail on November 28 a "[d]emand of seller for goods received by buyer on credit while insolvent," claiming a right to return of the livestock under section 2-702 of the Code. The financing statement was filed on November 29. When it intervened in the garnishment proceeding the seller claimed a purchase money security interest. The court pointed out that there had been no security agreement either written or oral until after November 25, so that the security interest did not attach prior to the writ of garnishment. The court also noted that intervenors had not pleaded the right to reclaim or a cause of action under the regulations issued pursuant to the federal Packers and Stockyards Act. The court properly ruled that these claims asserted for the first time on appeal were not properly before it.¹⁶⁷ Under section 9-301 the court held that the garnishment lien creditor prevailed in this case over the secured party whose security interest was unperfected at the time the other claimant became a lien creditor.

In *Kimbell Foods, Inc. v. Republic National Bank*¹⁶⁸ a number of parties laid claim to sums held in escrow by the Republic National Bank (Republic). The sums represented the proceeds of the bulk sales of fixtures, equipment, and inventory owned by a bankrupt supermarket chain. The claim of Kimbell Foods (Kimbell) was based on sales on open account to the supermarket chain, which sales Kimbell alleged were secured by future advance clauses in security agreements between Kimbell and the chain. Republic claimed the total amount in escrow due to a default by the same supermarket chain on a loan for \$300,000 made by Republic and ninety percent guaranteed by the federal Small Business Administration (SBA). The State of Texas and the city of Dallas intervened claiming delinquent taxes.

Kimbell had entered into security agreements in 1966 and 1968 covering equipment and purporting to secure "the payment of all other indebtedness at any time [t]hereafter owing by Debtor to Secured Party." Financing statements were signed and filed with the Texas secretary of state. Republic also had a security agreement and financing statement granting the bank a security interest in the debtor's machinery, fixtures, equipment, and inventory. Financing statements for the bank's security interest were filed on August 7, 1968, and February 18, 1969, with the Texas secretary of state. The debtor used the proceeds of the February 1969 bank loan to pay off the note then outstanding to Kimbell although there was a running balance on open account for inventory purchases from Kimbell. On February 4, 1972, Kimbell obtained judgment for its claim on open account.

The court first held that federal law applied when a debt owed to the United States (in this case the Small Business Administration) is involved.¹⁶⁹ Be-

167. Query whether the seller of the cattle could claim the proceeds of the subsequent resale of these cattle. Judge Godbold in the *Samuels* case seemed to doubt whether the seller does have such a claim. 526 F.2d at 1245.

168. 401 F. Supp. 316 (N.D. Tex. 1975).

169. Cf. *United States v. Yazell*, 382 U.S. 341 (1966) (federal law does not necessarily govern all questions in federal government litigation). See generally P. BATOR, P. MISHKIN, D. SHAPIRO &

tween a federal lien and a state-created lien the applicable federal rule is that the first in time has priority. The court further ruled that a valid lien must meet a test of choateness. In order to be choate the court stated that (a) the identity of the lienor, (b) the property subject to the lien, and (c) the amount of the lien must be certain. The last of these tests is satisfied only when there is "no further opportunity for contesting the amount of the lien."¹⁷⁰ In this case the court held that Kimbell met this test only when it reduced its lien to judgment on February 4, 1972. The SBA had a perfected lien as of the February 18, 1969, filing by Republic because the SBA's participation in the loan was evident from the face of the note. The SBA therefore had priority on the basis of federal law.

The court also found that Kimbell would be subordinated under state law. Relying on pre-Code Texas cases, the court noted that "dragnet clauses" apply only to future indebtedness clearly contemplated by the parties at the time of making the original agreement and only as to indebtedness of the same nature. The court ruled that similar limitations were adopted by section 9-204(5)¹⁷¹ of the Code because a future advance clause can be abused by lenders. After reviewing the relations between Kimbell and the debtor, the court concluded that the parties did not intend purchases on open account to be covered by the broad future indebtedness clauses in the security agreements. The primary indebtedness covered by the security agreements was for specific purposes unrelated to inventory purchases which were the source for the indebtedness on open account.¹⁷²

As to the state and city claims based on delinquent payments of the general sales tax, the court noted that cases construing section 646 of title 15 of the United States Code¹⁷³ have held that these general taxes are not taxes due on specific property. The court held that the state and city did not have a lien on the proceeds of the property because the liens were not extinguished or destroyed by the bulk sale of the property. Further, if the lien is not destroyed, the lienor has no rights to the proceeds and must look instead to the property itself. The court applied this same reasoning to the city's claim for ad valorem taxes. As a result of these rulings the court in *Kimbell Foods* concluded that the SBA was entitled to the entire sum held in escrow.

C. Miscellaneous

In a per curiam opinion the Texas Supreme Court refused a writ of error in *First National Bank v. Lone Star Life Insurance Co.*¹⁷⁴ The Dallas court of civil appeals had found that a non-negotiable certificate of deposit was an "instrument" in which the secured party had a perfected security interest as a

H. WECHSLER, HART & WECHSLER'S THE FEDERAL COURTS AND THE FEDERAL SYSTEM 756-832 (2d ed. 1973).

170. 401 F. Supp. at 322.

171. The court referred to the future advance provision before the 1972 Official Text came into force in Texas. The same provision is now TEX. BUS. & COMM. CODE ANN. § 9.204(c) (Vernon Supp. 1976-77).

172. See generally on the subject of "dragnet clauses" 2 G. GILMORE, *supra* note 158, §§ 35.1-.5.

173. 15 U.S.C. § 646 (1970).

174. 529 S.W.2d 67 (Tex. 1975), *aff'g per curiam* 524 S.W.2d 525 (Tex. Civ. App.—Dallas 1975). For a casenote about the court of civil appeals decision see 7 ST. MARY'S L.J. 895 (1976).

result of taking possession of the certificate. The bank which had issued the certificate of deposit sought to set off against the amount of the certificate an amount owing to it under previous indebtedness of the debtor. The majority interpreted section 9-104(i) to mean that a claimant of the right of set-off need not comply with the Code and not that the set-off can be successfully asserted against a party who has perfected a security interest under article 9. The majority opinion also ruled on rehearing that a non-negotiable certificate of deposit is *as a matter of law* an "instrument" within the definition of section 9-105(1)(i) and that a security interest can be perfected in it only by taking possession in accordance with section 9-304(1). The concurring opinion considered the primary question to be whether the bank was entitled to a set-off against the certificate of deposit and would affirm the trial court's opinion based on established precedent rather than on the Texas Business and Commerce Code.

In its cryptic *per curiam* affirmance, the Texas Supreme Court refused a writ of error but stated that "[i]n taking such action, we do not approve the holding that Chapter 9 of the Texas Business and Commerce Code controls the right of a bank to assert a set-off against the funds of a depositor."¹⁷⁵ With respect, it is suggested that this statement leaves the issue in even greater confusion. The court of civil appeals recognized that article 9 does not affect a right of a bank to a set-off.¹⁷⁶ The holding of the appellate court was that a perfected security interest in the certificate of deposit—perfected pursuant to article 9—would prevail over the bank's right to set off. The problem with this decision is that the appellate court never clearly explained the source of authority for its conclusion that an article 9 perfected security interest prevails over the non-Code right to set off. The brief supreme court opinion does not help resolve this problem.

Although the Uniform Commercial Code made significant changes in the terminology used in secured transactions, with few exceptions the Code did not seek to amend the existing patterns of financing. Floor plans by which the inventory of motor vehicle dealers are financed—a form of financing which has a long and interesting history—were not prohibited by the Code. The court in *American Fiber Glass, Inc. v. General Electric Credit Corp.*¹⁷⁷ makes the straightforward point that trust receipts used in such financing arrangements are not abolished although the terminology has been changed. The court quite properly cites section 9-102(2)¹⁷⁸ and quotes liberally from the comments to section 9-101.

The court in *Citizens State Bank v. J.M. Jackson Corp.*¹⁷⁹ held as a matter of law that a notation at the bottom of an invoice did not reasonably identify the rights assigned. The notation stated: "Make all checks payable to Citizens State Bank and Jetero Underground Utility Contractors, Inc." Section 9-318(3) states in part: "The account debtor is authorized to pay the assignor

175. 529 S.W.2d at 68.

176. 524 S.W.2d at 528.

177. 529 S.W.2d 298 (Tex. Civ. App.—Fort Worth 1975, writ ref'd n.r.e.).

178. "This chapter applies to security interests created by contract including . . . trust deed . . ." TEX. BUS. & COMM. CODE ANN. § 9.102(b) (Vernon Supp. 1976-77).

179. 537 S.W.2d 120 (Tex. Civ. App.—Houston [14th Dist.] 1976, no writ).

until the account debtor receives notification that the account has been assigned and that payment is to be made to the assignee. A notification which does not reasonably identify the rights assigned is ineffective.¹⁸⁰ An account debtor which had received an invoice with the above notation paid the invoice with a check payable to Jetero only. The secured party, with a security interest in the accounts, sought to recover from the account debtor. The court held that the secured party failed to give the account debtor the notification required by section 9-318(3). The obvious lesson for the attorney advising a secured party with a security interest in accounts is to conform as closely as possible with the terms of section 9-318.

V. MISCELLANEOUS DECISIONS

Much of the discussion in the previous sections of this *Survey* article focuses on decisions construing the Uniform Commercial Code as adopted in Texas. There remains each year a fairly large residue of commercial cases which do not fit within the framework of the Code yet are of importance to the commercial lawyer. This section collects decisions on accord and satisfaction, arbitration, bailment, conversion, and guaranty agreements. Other topics which in past years might have appeared in this section may now be found in the *Survey* article on creditors' rights.¹⁸¹

A. *Accord and Satisfaction*

In *Wilkes v. Mason*¹⁸² the payee endorsed and accepted the proceeds of a check with an uncompleted printed notation stating that the check was given in full satisfaction of an unspecified claim. The Amarillo court of civil appeals held that the payee did not as a matter of law necessarily accept the check in satisfaction of his claim against the drawer of the check. The check bore the following printed notation in very small capital letters: "THIS CHECK IS IN FULL SETTLEMENT AS SHOWN HERE. ACCEPTANCE BY ENDORSEMENT CONSTITUTES RECEIPT IN FULL." Four lines on which the purpose for which the check was drawn could be noted were left incomplete. In his affidavit the payee stated that when he told defendants that he would not accept partial payment the defendants said "Well, this will help you to clean up the place and get the place cleaned up." The court distinguished a prior case¹⁸³ because the printed notation on the check in the earlier case was conspicuous, the notation was followed by a typed indication of the purpose for which the check was drawn, payee solicited the check, and the payee did not object to the lesser amount tendered. As this was a summary judgment case, the *Wilkes* court properly ruled that a fact issue existed as to whether there had been an offer of accord or satisfaction. Drawer, as movant for summary judgment, had the burden of establishing conclusively the affirmative defense of accord and satisfaction.

180. The provision cited in the text is from the pre-1972 version of the Code. Minor amendments to this section were made in the 1972 Official Text. TEX. BUS. & COMM. CODE ANN. § 9.318(c) (Vernon Supp. 1976-77).

181. See Dorsaneo, *Creditors' Rights*, p. 213 *infra*.

182. 529 S.W.2d 255 (Tex. Civ. App.—Amarillo 1975, no writ).

183. *Avent v. Stinnett*, 513 S.W.2d 89 (Tex. Civ. App.—Amarillo 1974, no writ). For a casenote on this decision see 8 ST. MARY'S L.J. 359 (1976).

The *Wilkes* opinion should not be read as reversing the traditional substantive law rule that by cashing a check tendered with clear language indicating that it is offered in full payment of a disputed claim the payee has accepted an offer of accord or satisfaction.¹⁸⁴ Some commentators suggest that section 1-207 of the Code, not mentioned by the court in *Wilkes*, has reversed the traditional rule at least where the payee adds words of protest to his endorsement.¹⁸⁵ While this commentator favors this suggested reading of section 1-207, a court faced with this question should re-examine the whole matter in depth.

B. Arbitration

Despite references to arbitration in early Texas constitutions and legislation, commercial arbitration apparently has never been widely used in Texas.¹⁸⁶ Article 224 of the Texas Revised Civil Statutes unfortunately makes it even less likely that arbitration agreements will be enforced because this article requires the signatures of parties' counsel on the arbitration agreement before the agreement is enforceable.¹⁸⁷ While there is a danger that "fine-print, printed forms" may be used without parties realizing that they are agreeing to an arbitration provision, there is also a high likelihood that a bona fide agreement will be unenforceable because of the extra formality. The case of *Withers-Busby Group v. Surety Industries, Inc.*¹⁸⁸ illustrates this problem with respect to an agreement to arbitrate disputes which may arise in the future. The court held that "under the plain provisions of the statute" the arbitration provision was unenforceable without the signatures of counsel.¹⁸⁹ The court rejected an argument that the signatures are unnecessary because article 225B allows a stay of arbitration proceedings on a showing that there is "no agreement to arbitrate" without a reference to invalidity under article 224. The court stated that when both articles are read together there is no doubt that counsel's signature is required in order to enforce the provision.

If a contract which includes an arbitration clause involves interstate commerce, the Federal Arbitration Act may apply.¹⁹⁰ In the *Withers-Busby* case the court of civil appeals affirmed the lower court's finding that the joint

184. See 6 A. CORBIN, CORBIN ON CONTRACTS § 1279 (2d ed. 1962).

185. See J. WHITE & R. SUMMERS, *supra* note 24, at 452-54. Note that in *Wilkes* the court did not indicate whether or not payee did more than protest orally that he was not accepting the check in full payment.

186. See generally Carrington, *The 1965 General Arbitration Statute of Texas*, 20 SW. L.J. 21 (1966).

187. TEX. REV. CIV. STAT. ANN. art. 224 (Vernon 1973):

A written agreement concluded upon the advice of counsel to both parties as evidenced by counsels' signatures thereto to submit any existing controversy to arbitration or a provision in a written contract concluded upon the advice of counsel to both parties as evidenced by counsels' signatures thereto to submit to arbitration any controversy thereafter arising between the parties is valid, enforceable and irrevocable, save upon such grounds as exist at law or in equity for the revocation of any contract.

188. 538 S.W.2d 198 (Tex. Civ. App.—Dallas 1976, no writ).

189. *Id.* at 199. The court noted that the agreement was prepared by appellee's counsel, who assured the representatives of the appellant that the agreement was valid. The court noted also that the attorney's representation might give rise to an action for damages but that the representation does not make the invalid provision enforceable. *Id.* at 200.

190. 9 U.S.C. § 1 (1970). The Convention on the Recognition and Enforcement of Foreign Arbitral Awards is now incorporated into title 9 of the United States Code.

venture agreement in that case did not involve "commerce between the states" as defined by the federal act.¹⁹¹

C. Bailment

Following the suggestion of the Texas Supreme Court last year in *Buchanan v. Byrd*,¹⁹² several courts of civil appeals have re-examined a Texas exception to the rule that the bailor makes a presumptive case of negligence by proving a bailment and a failure of the bailee to return the goods bailed. The exception in Texas allowed the bailee to rebut the presumption of negligence by merely showing that loss occurred because of theft or fire without further evidence that the bailee exercised due care. The Houston [14th District] court of civil appeals rejected this "fire and theft" exception in *Classified Parking Systems v. Dansereau*.¹⁹³ Aside from references to the "modern" view and "enlightenment," the court noted that the presumption of negligence is necessary to aid the bailor to prove his case and to allow the bailee to rebut this presumption by merely showing theft or fire undercuts this aid to the bailor. The court also held that the bailor need not plead negligence. In *Jalco, Inc. v. Tool Traders, Inc.*¹⁹⁴ the Houston [1st District] court of civil appeals adopted the holding in *Classified Parking*.¹⁹⁵

Reversal of the former Texas exception should be approved. The best policy support for the new rule remains the language adopted in the *Buchanan v. Byrd* decision.¹⁹⁶ In allocating risks between bailors and bailees a court should consider that a bailee usually has control of the evidence, the bailee is usually in a better position to insure against fire and theft, the bailee can adjust charges to cover these risks, and the bailee will use greater caution in the care of goods left with him.

D. Conversion

The primary difficulty in the conversion cases during this survey period is not in identifying the conversion but in determining the proper measure of damages. The basic rule is that the plaintiff may recover the value of the converted good at the time and place of conversion.¹⁹⁷ Recent Texas cases suggest qualifications to this rule where fluctuating markets are involved.

In two very similar cases, the Amarillo court of civil appeals found that the purchase of cotton which belonged in part to a landlord¹⁹⁸ made the purchaser

191. 538 S.W.2d at 199. The definition of "commerce" for the purposes of the Federal Arbitration Act is found in 9 U.S.C. § 1 (1970). For a federal court decision construing the federal act with respect to a transaction in which a Texas business was involved, see the per curiam decision in *Southwest Indus. Import & Export, Inc. v. Wilmod Co.*, 524 F.2d 468 (5th Cir. 1975).

192. 519 S.W.2d 841, 844 (Tex. 1975).

193. 535 S.W.2d 14 (Tex. Civ. App.—Houston [14th Dist.] 1976, no writ).

194. 535 S.W.2d 898 (Tex. Civ. App.—Houston [1st Dist.] 1976, no writ).

195. The Eastland court of civil appeals had earlier come to a similar conclusion in a theft case. *Central Trailer Sales, Inc. v. Gay*, 533 S.W.2d 476 (Tex. Civ. App.—Eastland 1976, no writ). Unfortunately in this case the appellate court had no findings of fact or conclusions of law to deal with, and the court merely affirmed the implied findings of the trial court without discussing the burden of proof or underlying policies.

196. 519 S.W.2d at 844.

197. See generally D. DOBBS, *HANDBOOK ON THE LAW OF REMEDIES* § 5.14 (1973); W. PROSSER, *HANDBOOK OF THE LAW OF TORTS* § 15 (4th ed. 1971).

198. The court refers to the landlord's lien. TEX. REV. CIV. STAT. ANN. art. 5222 (Vernon 1962). Under the lease agreements involved in these cases the landlord was to receive one-fourth

a converter without regard to the purchaser's actual knowledge of the landlord's ownership. It is incumbent, in other words, on the buyer to inquire carefully into the authority of the seller to sell the entire crop. The two cases, however, suggest different measures for damages. In *Keaton McCrary Cotton Co. v. Herron*¹⁹⁹ the court calculated damages as the difference between the price of cotton at the time of trial (stipulated to by the parties) and the price per pound contracted for by the unauthorized seller and the purchaser. In *Dill v. Graham*,²⁰⁰ on the other hand, the court affirmed jury findings as to the fair market value of two lots of converted cotton (a) by using the lowest per pound market price between two dates for one lot, and (b) the average per pound market price (stipulated to by the parties) during the time when the second lot of the cotton was harvested and ginned. The court found that the uncontroverted evidence and the stipulations showed the fair market value at the time when the cotton normally would have been available for delivery to the landlord by the lessee.

These converted cotton cases pose difficult practical problems. Not only does the market for ginned cotton fluctuate but the date of conversion of fungible goods subject to processing will in most cases be virtually impossible to prove. The Amarillo court has taken advantage of party stipulations and jury findings to end the dispute between the parties, but the court gives little guidance to the parties as to what they should stipulate or what issues should be submitted to the jury.

A more traditional conversion case is *Romano v. Dempsey-Tegler & Co.*²⁰¹ where plaintiff sued his securities broker for conversion of bonds in plaintiff's margin account. Plaintiff alleged that defendant firm failed to transfer these bonds to another broker as he had requested. The trial court entered judgment n.o.v. for the defendant. The appellate court reversed and remanded. The court noted sufficient evidence to support a jury finding of conversion but no support for the finding of the date of conversion. The jury had found the date of conversion to be after the date on which suit had been filed but before trial. Citing a prior Texas case,²⁰² the court of civil appeals stated that the proper measure of damages for the conversion of goods which fluctuate widely in value is the highest intermediate value between the date of conversion and the filing of suit, or the trial where the suit is promptly tried after filing.

*Metal Window Products Co. v. Nored*²⁰³ illustrates the problems of proof for a plaintiff seeking to show fair market value of a converted good. The Beaumont court of civil appeals found the following evidence insufficient to

of the cotton crop raised by the tenant as rent. The court indicates that the tenant owns the entire crop prior to harvest but on harvesting the landlord "has the fixed right to become owner of his share." The court further suggests that the landlord in the cases under review has the option of either following the cotton and foreclosing the lien or suing the purchaser for conversion. It is difficult to find in article 5222, however, the suggested right to foreclose the lien on property transferred to a good faith purchaser. Liens normally do not survive transfer.

199. 529 S.W.2d 630 (Tex. Civ. App.—Amarillo 1975, no writ).

200. 530 S.W.2d 157 (Tex. Civ. App.—Amarillo 1975, writ ref'd n.r.e.).

201. 540 S.W.2d 538 (Tex. Civ. App.—Houston [14th Dist.] 1976, no writ).

202. *Security State Bank v. Spinnler*, 78 S.W.2d 275 (Tex. Civ. App.—Amarillo 1935, no writ).

203. 535 S.W.2d 711 (Tex. Civ. App.—Beaumont 1976, no writ).

support a jury finding of market value on the date of conversion: the purchase price of the new car nine months earlier (allowing for fleet discount), the purchase price of the used car by plaintiff one month before conversion, and testimony that the car was in "perfect running condition" at the time of conversion. The court noted that no witness testified directly as to the reasonable cash market value of the car on the date of conversion. It is suggested that the court's slighting of evidence as to purchase price be limited to the facts of this case. Frequently, it will be difficult to determine the date of conversion, let alone to find a witness who could qualify as an expert on the reasonable market value of the converted good.

E. Guaranty Agreements

Texas decisions in this survey period leave the guarantor in an unenviable position. The guarantor may guarantee payment of a note and thereby become in effect a co-maker of the note.²⁰⁴ The guarantor may validly waive his statutory right to have the principal obligor sued first²⁰⁵ or at least to have the principal obligor joined in the action.²⁰⁶ Despite his primary liability the guarantor has been held to be outside the protection of the usury statutes.²⁰⁷ Under the format adopted in this year's *Survey* issue these cases are scattered between this *Survey* article and the survey of creditors' rights.

An important pair of cases considers whether or not the guarantor may insist on the joinder of the principal obligor in an action brought against the guarantor by the creditor. Articles 1986 and 1987 of the Texas Revised Civil Statutes,²⁰⁸ as well as rule 31 of the Texas Rules of Civil Procedure,²⁰⁹ suggest that the guarantor may require joinder.

In *Cook v. Citizens National Bank*²¹⁰ the Beaumont court of civil appeals held that the principal borrower must be joined with the guarantor when the

204. *Universal Metals & Mach., Inc. v. Bohart*, 539 S.W.2d 874 (Tex. 1976); TEX. BUS. & COMM. CODE ANN. § 3.416(a) (Vernon 1968); see note 79 *supra* and accompanying text.

205. *Universal Metals & Mach., Inc. v. Bohart*, 539 S.W.2d 874, 877 (Tex. 1976); TEX. BUS. & COMM. CODE ANN. § 34.02 (Vernon 1968); see note 92 *supra* and accompanying text.

206. See the *Cook* and *Yandell* cases, notes 211, 216 *infra* and accompanying text.

207. *Universal Metals & Mach., Inc. v. Bohart*, 539 S.W.2d 874, 879 (Tex. 1976); *Hartnett v. Adams & Holmes Mortgage Co.*, 539 S.W.2d 181 (Tex. Civ. App.—Texarkana 1976, no writ) (guarantor not an "obligor" for the purposes of art. 5069-1.06); TEX. REV. CIV. STAT. ANN. arts. 5069-1.06 (Vernon 1971), 1302-2.09 (Vernon Supp. 1976-77).

208. TEX. REV. CIV. STAT. ANN. arts. 1986, 1987 (Vernon 1964). These articles provide:
Art. 1986. Several obligors to contract

The acceptor of a bill of exchange, or a principal obligor in a contract, may be sued either alone or jointly with any other party who may be liable thereon; but no judgment shall be rendered against a party not primarily liable on such bill or other contract, unless judgment be also rendered against such acceptor or other principal obligor, except where the plaintiff may discontinue his suit against such principal obligor as hereinafter provided.

Art. 1987. Parties conditionally liable

The assignor, indorser, guarantor and surety upon a contract, and the drawer of bill which has been accepted, may be sued without suing the maker, acceptor or other principal obligor, when the principal obligor resides beyond the limits of the State, or where he cannot be reached by the ordinary process of law, or when his residence is unknown and cannot be ascertained by the use of reasonable diligence, or when he is dead, or actually or notoriously insolvent.

209. TEX. R. CIV. P. 31: "No surety shall be sued unless his principal is joined with him, or unless a judgment has previously been rendered against his principal, except in cases otherwise provided for in the law and these rules."

210. 538 S.W.2d 460 (Tex. Civ. App.—Beaumont 1976, no writ).

creditor brought suit against the guarantor of payment. The court felt itself bound by the texts of rule 31 and articles 1986 and 1987 as construed by the decision of the commission of appeals in *Wood v. Canfield Paper Co.*²¹¹ Noting that the guaranty agreement should be given effect when possible and that the *Wood* case does not distinguish between absolute and conditional guarantors, the court ruled that the trial court's severance of the action against the principal obligor was improper. The court also held that the principal obligor, which was in chapter XI proceedings, did not come within the article 1987 exception by being "actually or notoriously insolvent." The court cited judicial construction²¹² of article 1987 which adopted a bankruptcy test of insolvency,²¹³ and the court noted that the principal obligor's assets were almost twice as large as its liabilities. The court quoted, but did not discuss, the waiver provision in the guaranty agreement which provided that "it shall not be necessary for the bank . . . to first institute suit or exhaust its remedies against the Borrower" ²¹⁴

The holding of the *Cook* case was not followed in *Yandell v. Tarrant State Bank*.²¹⁵ The guaranty agreement stated explicitly: "Guarantor waives any right to have Customer joined with Guarantor in any suit brought against Guarantor on this guaranty, and further waives any right to require Bank to forthwith sue Customer to collect the Obligations as a prerequisite to Bank's taking action against Guarantor under this Guaranty." The Fort Worth court of civil appeals held that there was insufficient evidence as a matter of law to uphold the entry of summary judgment on the insolvency of the principal obligor. The court went on to hold, however, that the guarantor could validly waive the legal right to have the principal obligor joined in the suit. The court interpreted articles 1986 and 1987, together with rule 31, to be solely for the benefit of the surety. The court then cited Texas precedents for the proposition that rights conferred by the constitution and legislation could be waived where third party rights were not affected.²¹⁶ While agreeing with the Beaumont court that the *Wood* case is still binding, the court refused to follow the holding in *Cook*. Apparently the court distinguished the *Wood* case because the guarantor in that case had not purported to waive his right to have the principal obligor joined. It is suggested that the Fort Worth court's reasoning should be followed in the absence of more explicit legislation. It is consistent with the basic principle of Anglo-American commercial law that there is a presumption that the parties' agreement should be enforced in the absence of

211. 117 Tex. 399, 5 S.W.2d 748 (1928).

212. *Texas Baptist Univ. v. Patton*, 145 S.W. 1063 (Tex. Civ. App.—Dallas 1912, no writ).

213. 11 U.S.C. § 1(19) (1970):

A person shall be deemed insolvent within the provisions of this title whenever the aggregate of his property, exclusive of any property which he may have conveyed, transferred, concealed, removed, or permitted to be concealed or removed, with intent to defraud, hinder, or delay his creditors, shall not at a fair valuation be sufficient in amount to pay his debts.

214. 538 S.W.2d at 462.

215. 538 S.W.2d 684 (Tex. Civ. App.—Fort Worth 1976, writ ref'd n.r.e.).

216. *United Benefit Fire Ins. Co. v. Metropolitan Plumbing Co.*, 363 S.W.2d 843 (Tex. Civ. App.—El Paso 1962, no writ); *Zurich Gen. Accident & Liab. Ins. Co. v. Fort Worth Laundry Co.*, 63 S.W.2d 236 (Tex. Civ. App.—Fort Worth 1933, no writ); *Young v. Colorado*, 174 S.W. 986 (Tex. Civ. App.—Fort Worth 1915, writ ref'd).

an over-riding public interest.²¹⁷

The case of *Hargis v. Radio Corp. of America, Electronic Components*²¹⁸ illustrates the rules as to the consideration which will support a guaranty agreement. When the creditor confers a benefit on the principal whose obligation is guaranteed this will support a guaranty contract without the need for additional consideration passing to the guarantor.²¹⁹ The court noted that in *Hargis* each delivery of merchandise after the guaranty agreement was entered into was a new extension of credit or new consideration. In addition, the total amount of credit extended grew after the signing of the guaranty agreement. The court, therefore, had no difficulty in holding that the guaranty agreement was supported by consideration.

Of the several construction bond cases during the survey period one is important for its urging the Texas Supreme Court to re-examine the rule that the compensated corporate surety has the advantage of the traditional suretyship rule that the surety's contract is strictly construed in favor of the surety. In *United States Fidelity & Guaranty Co. v. Borden Metal Products Co.*²²⁰ the Beaumont court of civil appeals affirmed a judgment for a materialman suing the corporate surety on a construction payment bond. The surety challenged the sufficiency of the evidence to support the trial court's finding that the contract between the principal and the obligee was not "substantially or materially changed, modified or altered." The appellate court found sufficient evidence in the record and concluded that in essence the surety was arguing that because the principal was successful in overreaching the obligee, the overreaching would operate as a release of the surety. The court refused to approve this position, noting that to approve it would be "equivalent to saying that the surety may reap advantage by the default of the very party against whose failure he has undertaken to indemnify the obligee."²²¹ In his opinion for the court Justice Keith urged the supreme court to reconsider the favored position of the compensated corporate surety.²²² He noted that the Texas rule is a minority rule and that the *Restatement of Security* had distinguished the liability of the compensated corporate surety. For the purposes of the *Borden Metal* case, however, he agreed that he was bound by the rule of law urged by the surety and affirmed instead on the sufficiency of the evidence point.

217. Cf. TEX. BUS. & COMM. CODE ANN. § 1.102(c) (Vernon 1968).

218. 539 S.W.2d 230 (Tex. Civ. App.—Austin 1976, no writ).

219. See generally L. SIMPSON, *supra* note 90, § 26. See also the discussion of consideration in the *Bohart* case, *supra* notes 89-90 and accompanying text.

220. 539 S.W.2d 170 (Tex. Civ. App.—Beaumont 1976, no writ).

221. *Id.* at 174 n.6.

222. *Id.* at 173-74.

