



January 1984

Commercial Transactions

John Krahrmer

Recommended Citation

John Krahrmer, *Commercial Transactions*, 38 Sw L.J. 207 (1984)
<https://scholar.smu.edu/smulr/vol38/iss1/10>

This Article is brought to you for free and open access by the Law Journals at SMU Scholar. It has been accepted for inclusion in SMU Law Review by an authorized administrator of SMU Scholar. For more information, please visit <http://digitalrepository.smu.edu>.

COMMERCIAL TRANSACTIONS

by
John Kraemer*

SIGNIFICANT activity occurred in the area of commercial transactions during the last survey period on both the legislative and judicial fronts. Of particular importance is the legislative adoption of the 1978 Official Text of Article 8 of the Uniform Commercial Code dealing with investment securities.¹ This Article discusses this development, as well as others of a less comprehensive nature. The survey subjects are treated in the same order as the subject matters appear in the Texas Business and Commerce Code.

I. GENERAL PROVISIONS

A. Legislative Changes

Definitional Amendments. Section 1.201 of the Code contains definitions that are applicable to the entire Code.² The revision of chapter 8 creates two main types of investment securities, the certificated security³ and the uncertificated security.⁴ While both types of securities have technical definitions, the primary distinction between them is that a certificated security is represented by an instrument that can be physically transferred from hand to hand, while transfer of an uncertificated security is represented only by entry on the books of the issuing corporation.⁵ The distinction is similar to the distinction between a certificate of title to a motor vehicle that is signed over to a buyer at the time of sale, thereby immediately evidencing the sale and protecting the buyer against third parties, and the

* B.A., J.D., University of Iowa; LL.M., Harvard University. Professor of Law, Texas Tech University.

1. The new article 8 was adopted by Act of Sept. 1, 1983, ch. 442, 1983 Tex. Gen. Laws 2511-83 (codified at TEX. BUS. & COM. CODE ANN. §§ 8.101-408 (Tex. UCC) (Vernon Supp. 1984)).

The Uniform Commercial Code first became effective in Texas on July 1, 1966. Uniform Commercial Code, ch. 721, §§ 1—101 to 10—105, 1965 Tex. Gen. Laws 1-316. In 1967 it became part of the Texas Business and Commerce Code. Act of Sept. 1, 1967, ch. 785, §§ 1-6, 1967 Tex. Gen. Laws 2343-2782. As amended, the Texas version of the Uniform Commercial Code now conforms closely to the 1978 Official Text. In this Article all references are to the Uniform Commercial Code as enacted in chapters 1 through 11 of the Texas Business and Commerce Code (hereinafter referred to as the Code), TEX. BUS. & COM. CODE ANN. §§ 1.101-11.108 (Tex. UCC) (Vernon 1968 & Supp. 1984).

2. *Id.* § 1.201 (Vernon 1968 & Supp. 1984).

3. *Id.* § 8.102(a)(1) (Vernon Supp. 1984).

4. *Id.* § 8.102(a)(2). Compare *id.* § 8.102(a)(2) (definition of uncertified security) with *id.* § 8.102(a)(3) (distinctions between certified and uncertified security).

5. *Id.* §§ 8.102(a)(2)-(3).

delivery of a deed to real property to a buyer that must be recorded before various third-party claims can be defeated. Because the bulk of stock transactions take place through brokers and stock exchanges, uncertificated securities will facilitate the exchange process by eliminating the need for physical transfer of stock certificates through several hands whenever shares are bought or sold. Section 1.201 contains several conforming amendments that reflect the revision of chapter 8 by adding the word "certificated" to those definitions dealing with the holding or transferring of securities.⁶ The uncertificated security is defined only in the new chapter 8.⁷ Section 1.201 needed no conforming amendments to reflect this new type of security.

Besides these conforming amendments, the legislature modified the definition of bank in section 1.201.⁸ This modification leaves no doubt that the rules of chapters 3 and 4 of the Code dealing with commercial paper, bank deposits, and bank collections⁹ cover savings and loan associations, credit unions, and other institutions that offer checking account services.¹⁰ The federal adoption of the Depository Institutions Deregulation and Monetary Control Act of 1980 prompted this change.¹¹

B. Choice of Law

Choice of Law by Agreement. In *Mostek Corp. v. Chemetron Corp.*¹² the parties to a sales contract specified that Illinois law governed the interpretation and performance of their agreement. In a suit alleging negligence, breach of warranty, and strict liability in tort, the court held that the state of Illinois bore a reasonable relation to the transaction and that the choice of Illinois law by agreement of the parties was valid.¹³ Applying Illinois law, the court found that the seller effectively disclaimed liability for negligence and breach of warranty, but that Illinois disallowed disclaimer of strict liability in tort.¹⁴ The court remanded the case for trial on the strict liability issue.¹⁵ The *Mostek* decision joins a growing list of cases upholding a consensual choice of law provision under the reasonable relation test of section 1.105.¹⁶

6. *Id.* §§ 1.201(5) (bearer), 1.201(14) (delivery), 1.201(20) (holder).

7. *Id.* § 8.102(a)(3).

8. *Id.* § 1.201(4).

9. Chapter 3 of the Code, *id.* §§ 3.101-.805 (Vernon 1968), is entitled "Commercial Paper." Chapter 4, *id.* §§ 4.101-.504, is entitled "Bank Deposits and Collections."

10. *Id.* § 1.201(4) (Vernon Supp. 1984).

11. Pub. L. No. 96-221, §§ 101-902, 94 Stat. 132-93 (1980) (codified at scattered sections of 12 U.S.C. (1982)).

12. 642 S.W.2d 20 (Tex. App.—Dallas 1982, no writ).

13. *Id.* at 24.

14. *Id.* at 26.

15. *Id.* at 27.

16. TEX. BUS. & COM. CODE ANN. § 1.105 (Tex. UCC) (Vernon 1968); *see, e.g.*, First Commerce Realty Investors v. K-F Land Co., 617 S.W.2d 806 (Tex. Civ. App.—Houston [14th Dist.] 1981, writ ref'd n.r.e.); Walker v. Associates Fin. Servs. Corp., 588 S.W.2d 416 (Tex. Civ. App.—Eastland 1979, writ ref'd n.r.e.); Hi Fashion Wigs Profit Sharing Trust v. Hamilton Inv. Trust, 579 S.W.2d 300 (Tex. Civ. App.—Eastland 1979, no writ).

C. Acceleration Clauses

A typical acceleration clause permits a creditor to accelerate the entire remaining balance of an installment obligation upon the occurrence of a particular event or whenever the creditor deems himself insecure.¹⁷ One fact situation that arises with some frequency in acceleration cases involves a debtor who has made several late installment payments and a creditor who has accepted the payments despite their lateness. When the creditor finally tires of receiving late payments and tries to accelerate, the debtor argues that the creditor has waived acceleration rights by the prior acceptance of late payments.

During the survey period debtors successfully raised the waiver argument in three cases,¹⁸ and only in *Slivka v. Swiss Avenue Bank*¹⁹ was the creditor able to avoid the defense. In *Slivka* the creditor notified the debtor, both orally and in writing, that further late payments would not be acceptable. When the debtor's next payment was late, the creditor's attorney gave prompt notice of acceleration. The court, in reaching its decision that the right of acceleration had not been waived, quoted and applied the following rule from the earlier case of *McGowan v. Pasol*:²⁰

[W]here, as is the case here, the holder of the note has accepted late payments on numerous occasions in the past, he is precluded from accelerating the maturity of an installment note because of a single late payment unless he has, prior to the late payment for which default is claimed, notified the maker that in the future he will not accept late payments.²¹

The lesson of *Slivka* is clear. If a creditor intends to accelerate after having previously accepted late payments, he must notify the debtor that no further late payments will be acceptable. A failure to give such notice will likely result in a waiver of the right to accelerate.

II. SALES TRANSACTIONS

A. Scope of Chapter 2

Insurance Coverage for Destroyed Goods. In *Custom Controls Co. v. Rogers Insurance*²² a seller agreed to manufacture and sell twelve custom control panels. After four panels were completed, but not yet delivered, they were destroyed by fire without fault of either party. The seller sought recovery from its insurer for the fair market value of the destroyed panels. The insurer paid an amount to the seller based on the cost of remanufacturing

17. E.g., 1 F. ELLIOTT & M. RUUD, VERNON'S TEXAS CODE FORMS ANNOTATED § 1.208 (Forms 1 & 2) (1968).

18. *Bodiford v. Parker*, 651 S.W.2d 338 (Tex. App.—Fort Worth 1983, no writ); *Dhanani Invs., Inc. v. Second Master Bilt Homes, Inc.*, 650 S.W.2d 220 (Tex. App.—Fort Worth 1983, no writ); *Highpoint of Montgomery Corp. v. Vail*, 638 S.W.2d 624 (Tex. App.—Houston [1st Dist.] 1982, no writ).

19. 653 S.W.2d 939 (Tex. App.—Dallas 1983, no writ).

20. 605 S.W.2d 728 (Tex. Civ. App.—Corpus Christi 1980, no writ).

21. 653 S.W.2d at 942.

22. 652 S.W.2d 449 (Tex. App.—Houston [1st Dist.] 1983, no writ).

the panels that was \$158,000 less than the seller's fair market value claim. In an action against the insurer, the seller contended that chapter 2 of the Code did not apply to the issue of insurance coverage. The court held that the definition of goods in section 2.105²³ brought the insurance transaction within the scope of chapter 2 for the purpose of determining coverage under the insurance policy.²⁴ The policy covered sold property on the basis of the "[n]et selling price of the Assured."²⁵ The court examined several provisions of chapter 2 to determine if title to the goods had passed, or if either the buyer or seller had the right to seek specific performance or bring an action for the price at the time the goods were destroyed.²⁶ The court concluded that the goods had not become sold goods under chapter 2 for purposes of insurance coverage and that the insurer was liable only for the cost of remanufacture, not for the fair market value.²⁷ Although not mentioned by the court, section 2.509 dealing with risk of loss supports the decision and provides a more direct route to the same result.²⁸

B. Enforceability of Sales Contracts

Statute of Frauds—Drafting a Valid Confirmation Between Merchants. Section 2.201 of the Code contains the statute of frauds requirements for the sale of goods.²⁹ The basic rule provides that contracts for the sale of goods for \$500 or more are not enforceable unless evidenced by a writing signed by the party against whom enforcement is sought.³⁰ One of the exceptions to this rule concerns confirmations between merchants. In section 2.201(b) the Code makes certain sales contracts enforceable:

Between merchants if within a reasonable time a writing in confirmation of the contract and sufficient against the sender is received and the party receiving it has reason to know its contents, it satisfies the requirements of Subsection (a) against such party unless written notice of objection to its contents is given within ten days after it is received.³¹

In *Great Western Sugar Co. v. Lone Star Donut Co.*³² the seller sent a letter agreement to the buyer that concluded, "This letter is a written confirmation of our agreement. Please sign and return to me the enclosed

23. TEX. BUS. & COM. CODE ANN. § 2.105(a) (Tex. UCC) (Vernon 1968) defines "goods" as "all things (including specially manufactured goods) which are movable at the time of identification to the contract for sale other than the money in which the price is to be paid, investment securities (Chapter 8) and things in action."

24. 652 S.W.2d at 452.

25. *Id.* at 453.

26. *Id.* at 452-53. The court reviewed the rules of TEX. BUS. & COM. CODE ANN. §§ 2.105-.106, .401, .709, .711, .717 (Tex. UCC) (Vernon 1968).

27. 652 S.W.2d at 453.

28. *See* TEX. BUS. & COM. CODE ANN. § 2.509 (Tex. UCC) (Vernon 1968) (risk of loss in absence of breach).

29. *Id.* § 2.201.

30. *Id.* § 2.201(a).

31. *Id.* § 2.201(b).

32. 567 F. Supp. 340 (N.D. Tex. 1983).

counterpart of this letter signalling your acceptance of the above agreement."³³ The buyer never sent an objection to this letter agreement, nor did he ever sign and return the counterpart. In ruling on the buyer's motion for summary judgment, the court reasoned that the letter agreement was only an offer by the seller because the concluding paragraph specifically requested the signing and return of the counterpart as the method of acceptance.³⁴ Because the counterpart was not signed and returned, the court granted the motion for summary judgment in favor of the buyer.³⁵ Based on the decision in this case, the careful drafter, to avoid the construction of a confirmation as an offer, should delete any language in the confirmation that requires a buyer to perform some indicated act as an expression of acceptance.³⁶

Unconscionability as a Claim. Under the Code unconscionability is an affirmative defense available to invalidate a contract in whole or in part.³⁷ The Texas Deceptive Trade Practices Act (TDTPA),³⁸ however, permits a party to assert unconscionability as an affirmative claim for the recovery of damages or injunctive relief.³⁹ The Code and the TDTPA also differ on the basic meaning of the term "unconscionability." Under the Code a contract must be unconscionable, if at all, "at the time it was made."⁴⁰ Under the TDTPA a contract may be unconscionable at the time of formation or during the course of performance.⁴¹ *North Star Dodge Sales, Inc. v. Luna*⁴² nicely illustrates this difference in the meanings of unconscionability. In *North Star* the purchaser bought a car under a warranty program that permitted a dissatisfied purchaser to return a vehicle for a full refund of the purchase price within thirty days after purchase or before the car had been driven 1000 miles, whichever came first. Soon after the purchase the buyer complained to the seller about mechanical defects, particularly steering column vibration. The seller never corrected the steering column defect.

33. *Id.* at 342.

34. *Id.* at 343.

35. *Id.* at 345.

36. The most scrupulous drafting will not, of course, solve the cases in which parties exchange forms that do not form a contract and yet, despite the mismatch, deal with each other as if a contract existed. In such cases TEX. BUS. & COM. CODE ANN. § 2.207(c) (Tex. UCC) (Vernon 1968) recognizes a contract based upon the conduct of the parties. No statute of frauds problem exists because of the partial performance exception found in *id.* § 2.201(c)(3).

37. *Id.* § 2.302.

38. *Id.* §§ 17.41-.63 (Vernon Supp. 1984).

39. *Id.* § 17.50(a)(3).

40. *Id.* § 2.302 (Tex. UCC) (Vernon 1968).

41. *Id.* § 17.45(5) (Vernon Supp. 1984) provides:

"Unconscionable action or course of action" means an act or practice which, to a person's detriment:

(A) takes advantage of the lack of knowledge, ability, experience, or capacity of a person to a grossly unfair degree; or

(B) results in gross disparity between the value received and consideration paid, in a transaction involving transfer of consideration.

42. 653 S.W.2d 892 (Tex. App.—San Antonio 1983, writ requested).

The buyer testified at trial that she made numerous requests for refund prior to expiration of the warranty period, but was met with a variety of excuses about why a refund could not be made (the contract was not yet processed; the proper party was not available to make the refund; the vibration would be corrected). The former service manager of the seller testified that he knew that most cars of the particular model purchased by the buyer had steering column vibration and acceded to the statement that he would have a customer return repeatedly for service rather than acknowledge the problem as irreparable. The court held that the buyer presented sufficient evidence of an unconscionable act or course of action to support a jury finding of unconscionability.⁴³

The buyer in *North Star* also asserted claims for deceptive acts or practices under the TDTA "laundry list"⁴⁴ and for violation of the Texas Consumer Credit Code (Motor Vehicle Installment Sales).⁴⁵ The latter violation was posited on a clause in the sales contract that provided:

Seller [sic] his agents or representatives, may enter the premises where the property may be and take immediate possession of the property including any equipment or accessories, and Seller may take possession of any other items in the property at the time of the repossession, and hold them without liability until demanded by Buyer⁴⁶

The court held that this clause violated article 5069—7.07(7) because the clause did not require the seller to give notice regarding return of the buyer's personal property not covered by a security interest at the time of the repossession.⁴⁷ The court assessed a \$2000 statutory penalty for this

43. *Id.* at 901.

44. TEX. BUS. & COM. CODE ANN. § 17.46(b) (Vernon Supp. 1984) contains a list of several acts or practices that are declared to be deceptive. The buyer sought recovery under *id.* § 17.46(b)(5), (7), (12), which provide:

(b) Except as provided in Subsection (d) of this section, the term "false, misleading, or deceptive acts or practices" includes, but is not limited to, the following acts:

(5) representing that goods or services have sponsorship, approval, characteristics, ingredients, uses, benefits, or quantities which they do not have or that a person has a sponsorship, approval, status, affiliation, or connection which he does not;

(7) representing that goods or services are of a particular standard, quality, or grade, or that the goods are of a particular style or model, and they are of another;

(12) representing that an agreement confers or involves rights, remedies, or obligations which it does not have or involve, or which are prohibited by law;

45. TEX. REV. CIV. STAT. ANN. arts 5069—7.01 to .10 (Vernon Supp. 1984).

46. 653 S.W.2d at 900. The wording of this clause may be usefully compared to the clause litigated in *Zapata v. Ford Motor Credit Co.*, 615 S.W.2d 198 (Tex. 1981). In *Zapata* a similar clause was held to violate TEX. REV. CIV. STAT. ANN. art. 5069—7.07(4) (Vernon Supp. 1984). *Zapata* and similar cases are discussed in Kraemer, *Commercial Transactions, Annual Survey of Texas Law*, 36 Sw. L.J. 201, 220 (1982).

47. 653 S.W.2d at 900; see TEX. REV. CIV. STAT. ANN. art. 5069—7.07(7) (Vernon Supp. 1984).

violation,⁴⁸ but denied a claim for the recovery of damages for mental anguish because of a failure of proof.⁴⁹

C. Warranties

Deceptive Trade Practices and the Warranty of Title. Besides permitting claims for deceptive trade practices and unconscionable acts or courses of action, the TDTPA permits actions on breach of warranty claims.⁵⁰ An advantage to joining a TDTPA claim to a Code warranty claim is that the Code only permits the recovery of actual damages,⁵¹ while the TDTPA mandates the multiplication of actual damages⁵² and provides for the recovery of attorney's fees.⁵³ These features of the TDTPA provided the plaintiff with a sizable recovery in *Saenz Motors v. Big H. Auto Auction, Inc.*⁵⁴ based on a breach of warranty of title for two automobiles purchased from the defendant auction company. After the buyer purchased the cars the Department of Public Safety seized the cars as stolen vehicles and never returned them. The court had no difficulty finding a breach of the warranty of title under the Code,⁵⁵ despite a complete lack of proof that the cars actually were stolen.⁵⁶ The court based its conclusion on the official comments to section 2.312, which state that disturbance of quiet possession is one way to show that the warranty of title has been breached.⁵⁷ The seizure of the vehicles clearly disturbed the buyer's quiet possession. Due to the breach of warranty, the plaintiff recovered both treble damages and attorney's fees.⁵⁸

Express and Implied Warranties in Construction Contracts. Although the Code limits warranties to transactions involving the sale of goods,⁵⁹ the Texas Supreme Court has developed a series of warranty standards in con-

48. 653 S.W.2d at 900.

49. *Id.* at 898.

50. TEX. BUS. & COM. CODE ANN. § 17.50(a) (Vernon Supp. 1984) provides that "[a] consumer may maintain an action where any of the following constitute a producing cause of actual damages: . . . (2) breach of an express or implied warranty"

51. *Id.* § 2.714 (Tex. UCC) (Vernon 1968).

52. Prior to 1979 the TDTPA provided for the trebling of actual damages, but in that year it was amended to provide:

In a suit filed under this section, each consumer who prevails may obtain:

(1) the amount of actual damages found by the trier of fact. In addition the court shall award two times that portion of the actual damages that does not exceed \$1,000. If the trier of fact finds that the conduct of the defendant was committed knowingly, the trier of fact may award not more than three times the amount of actual damages in excess of \$1,000.

Id. § 17.50(b) (Vernon Supp. 1984).

53. *Id.* § 17.50(a).

54. 653 S.W.2d 521 (Tex. App.—Corpus Christi 1983, writ ref'd n.r.e.).

55. See TEX. BUS. & COM. CODE ANN. § 2.312 (Tex. UCC) (Vernon 1968).

56. 653 S.W.2d at 525.

57. TEX. BUS. & COM. CODE ANN. § 2.312 comment 1 (Tex. UCC) (Vernon 1968), provides: "Disturbance of quiet possession, although not mentioned specifically, is one way, among many, in which the breach of the warranty of title may be established."

58. 653 S.W.2d at 525-26. Treble damages were awarded because the case arose prior to the 1979 amendments to the TDTPA.

59. TEX. BUS. & COM. CODE ANN. § 2.102 (Tex. UCC) (Vernon 1968) provides that

struction cases that parallel the Code.⁶⁰ In *Austin Co. v. Vaughn Building Corp.*⁶¹ the court permitted recovery for breach of a one-year express warranty covering the construction of a commercial building. The warranty did not specify a time by which the owner was required to give notice of defects. The court held that notice by the owner one year and eleven days after final acceptance of the building was timely in the absence of any showing of prejudice to the contractor and in light of the undisputed fact that the defect existed when the building was completed.⁶² The court, however, specifically declined to address the question of whether a commercial construction contract contains an implied warranty of fitness.⁶³

In two other construction cases⁶⁴ the Texas Supreme Court reaffirmed the rule that implied warranties of fitness do exist in the construction of residential dwellings.⁶⁵ These cases differ, however, on the level of consistency of underlying policy. In the last survey the author suggested that the lower Texas courts had adopted a purely mechanical approach to the issue of whether implied warranties exist in the sale of used goods or used homes.⁶⁶ The author reasoned that "a better jurisprudential approach would be to recognize that implied warranties can exist in such sales and focus judicial consideration on whether particular defects should fall within the scope of such an implied warranty."⁶⁷

In *Gupta v. Ritter Homes, Inc.*⁶⁸ the court adopted a rule extending the implied warranty of habitability to the buyer of a used home for "latent defects not discoverable by a reasonably prudent inspection of the building at the time of sale."⁶⁹ In support of the rule extending implied warranty protection to the buyer of a used home, the court held:

As between the builder and owner, it matters not whether there has been an intervening owner. The effect of the latent defect on the subsequent owner is just as great as on the original buyer and the builder is no more able to justify his improper work as to a subsequent owner than to the original buyer. The public policy upon which the *Humber* decision was based applies equally to both situations. . . .

. . . We hold that the implied warranty of habitability and good workmanship is implicit in the contract between the builder/vendor and original purchaser and is automatically assigned to the subse-

chapter 2 "applies to transactions in goods." "Goods" are defined in *id.* § 2.105(a) (quoted *supra* note 23).

60. See *Kamarath v. Bennett*, 568 S.W.2d 658 (Tex. 1978); *Humber v. Morton*, 426 S.W.2d 554 (Tex. 1968).

61. 643 S.W.2d 113 (Tex. 1983).

62. *Id.* at 115.

63. *Id.*

64. *Gupta v. Ritter Homes, Inc.*, 646 S.W.2d 168 (Tex. 1983); *G-W-L, Inc. v. Robichaux*, 643 S.W.2d 392 (Tex. 1982).

65. See *Humber v. Morton*, 426 S.W.2d 554, 555 (Tex. 1968).

66. *Krahmer, Commercial Transactions, Annual Survey of Texas Law*, 37 Sw. L.J. 145, 150-52 (1983).

67. *Id.* at 152.

68. 646 S.W.2d 168 (Tex. 1983).

69. *Id.* at 169.

quent purchaser.⁷⁰

The court noted that the rule adopted in *Gupta* involved an implied warranty running from the builder to a subsequent purchaser, but did not create an implied warranty running from a nonbuilder owner to a purchaser.⁷¹ The court also disapproved *Thornton Homes, Inc. v. Greiner*,⁷² which denied the existence of implied warranties from a builder in the sale of a used home.⁷³ The *Gupta* rule has the distinct benefit of concentrating judicial energy on the fact issues of when latent defects exist in the sale of used homes, rather than on denying relief on a questionable doctrinal basis.

In the other construction warranty case decided during the survey period, *G-W-L, Inc. v. Robichaux*,⁷⁴ the Texas Supreme Court considered the question of whether the following clause in a promissory note was sufficient to waive the implied warranty of habitability in the sale of a new home:

This note, the aforesaid Mechanic's and Materialmen's Lien Contract and the plans and specification signed for identification by the parties hereto constitute the entire agreement between the parties hereto with reference to the erection of said improvements, there being no oral agreements, representations, conditions, warranties, express or implied, in addition to said written instruments.⁷⁵

The Beaumont court of appeals previously ruled that the clause was insufficient to operate as a waiver of the implied warranty of fitness because its language was not "clear and free from doubt."⁷⁶ The Texas Supreme Court agreed with this standard, but disagreed with the lower court's application.⁷⁷ In reversing the court of appeals the Texas Supreme Court held that the language used was fully adequate to disclaim the warranty of fitness.⁷⁸ In a vigorous dissent Justice Spears stated:

The warranty of habitability is implied in law to protect innocent consumers, and to hold builders accountable for their work. To effectuate the public policies underlying the implied warranty, a court should not consider the warranty waived except by very express and specific language which clearly reflects that the buyer knew the implied warranty did not attach to the sale of his home.⁷⁹

This author agrees with the Spears dissent. It is anomalous for a court to adopt a forward-looking approach to the creation of an implied warranty of fitness in the sale of new and used homes closely paralleling the

70. *Id.*

71. *Id.*

72. 619 S.W.2d 8 (Tex. Civ. App.—Eastland 1981, no writ).

73. 646 S.W.2d at 169.

74. 643 S.W.2d 392 (Tex. 1982).

75. *Id.* at 393.

76. *G-W-L, Inc. v. Robichaux*, 622 S.W.2d 461, 464 (Tex. App.—Beaumont 1982).

77. 643 S.W.2d at 393.

78. *Id.*

79. *Id.* at 395.

implied warranties under the Code,⁸⁰ and then adopt a standard for disclaimers that permits the warranty to be disclaimed in a manner that is likely to go unnoticed by the parties it is designed to protect. As urged by the buyer, applying the Code disclaimer standards by analogy is a better means to insure that the implied warranty of fitness has real meaning.⁸¹ The court, however, sidestepped this issue and indicated that the Code does not apply to the sale of homes.⁸² This determination is unpersuasive because it does not respond to the question of whether the Code disclaimer standards should apply to home sales. Interestingly enough, the court noted that section 2.107 covers the sale of a structure to be removed from realty.⁸³ Given the large number of manufactured homes built in Texas, the existence of separate disclaimer standards for site-built and manufactured homes is even less appropriate. Since the court has recognized the symmetry of policies underlying the need for warranties of quality in the areas of goods and homes, it should recognize the same symmetry of policies underlying the need for clear, express, and conspicuous disclaimers in both areas.

Warranties in the Sale of Goods. The Amarillo court of appeals applied the Code's disclaimer standards in *Balderson-Berger Equipment, Inc. v. Blount*.⁸⁴ In *Blount* the seller gave an express oral warranty, but the written contract clearly and conspicuously disclaimed all warranties, express and implied, other than the warranties contained in the written contract. The buyer denied any knowledge of the disclaimers and testified that he did not read the contract before signing it. The court held that the disclaimers met the requirements of the Code and that the buyer was therefore bound by them.⁸⁵ The fact that the buyer signed the contract without reading it did not constitute a valid defense to the effectiveness of the disclaimers.⁸⁶

D. Bona Fide Purchase

Bona Fide Purchase from a Person with Voidable Title. Since the decision in *Samuels & Co. v. Mahon*,⁸⁷ section 2.403 of the Code has created problems for cattle sellers. Under section 2.403 one who sells goods in exchange for a check that is later dishonored loses the right to recover the

80. The Code warranties of quality appear in TEX. BUS. & COM. CODE ANN. §§ 2.314-.315 (Tex. UCC) (Vernon 1968).

81. The Code requires disclaimers to be not only clear and specific, but also to be conspicuous. *Id.* § 2.316(b).

82. 643 S.W.2d at 394.

83. *Id.* TEX. BUS. & COM. CODE ANN. § 2.107(a) (Tex. UCC) (Vernon 1968) provides: "A contract for the sale of . . . a structure or its materials to be removed from realty is a contract for the sale of goods . . ."

84. 653 S.W.2d 902 (Tex. App.—Amarillo 1983, no writ).

85. *Id.* at 908. The Code disclaimer standards are set out in TEX. BUS. & COM. CODE ANN. § 2.316 (Tex. UCC) (Vernon 1968).

86. 653 S.W.2d at 908.

87. 526 F.2d 1238 (5th Cir. 1976), *cert. denied sub nom.* Stowers v. Mahon, 429 U.S. 834 (1976).

goods from a bona fide purchaser from the original defaulting buyer.⁸⁸ An unfortunately common situation for cattle sellers concerns delivery of cattle to a broker in exchange for a rubber check. By the time the check bounces, the broker has resold the cattle to a packing company. Unless the cattle seller can show that the broker acted as an agent for the packing company, thereby defeating bona fide purchaser status, the original buyer loses the right to recover the cattle. In the latest of a series of cases involving Iowa Beef Processors and an insolvent cattle broker,⁸⁹ the Fifth Circuit Court of Appeals held that the cattle sellers failed to prove an agency relationship between the broker and Iowa Beef.⁹⁰ Due to the failure of proof, the cattle sellers could not recover against the processor, a bona fide purchaser.⁹¹

Bona Fide Purchase of Automobiles. In stark contrast to the cases involving cattle or other ordinary goods, the purchaser of an automobile who does not acquire the original certificate of title as part of the purchase may be compelled to return the car to the true owner.⁹² This result obtains because the Certificate of Title Act requires a specified manner of transfer for automobile titles. Unless the bona fide purchaser obtains a valid certificate of title, the original owner is entitled to reclaim the vehicle.⁹³ For example, in *Everett v. United States Fire Insurance Co.*⁹⁴ the court allowed the original owner to reclaim the vehicle even though a chain of subsequent purchasers had purchased the car under a certified copy of the certificate of title. The court held that the certified copy conveyed no rights in the car as against the holder of the original title.⁹⁵

E. Performance Disputes

The Perfect Tender Rule in the Sale of Goods. In contracts for the sale of goods, the Code adopts the pre-Code "perfect tender" rule.⁹⁶ Under this rule a buyer is entitled to reject goods that do not conform to the contract

88. TEX. BUS. & COM. CODE ANN. § 2.403 (Tex. UCC) (Vernon 1968).

89. *Rufenacht v. Iowa Beef Processors, Inc.*, 656 F.2d 198 (5th Cir. 1981), *cert. denied*, 455 U.S. 921 (1982); *Lubbock Feed Lots, Inc. v. Iowa Beef Processors, Inc.*, 630 F.2d 250 (5th Cir. 1980); *Valley View Cattle Co. v. Iowa Beef Processors, Inc.*, 548 F.2d 1219 (5th Cir. 1977), *cert. denied*, 434 U.S. 855 (1977).

90. *Brumley Estate v. Iowa Beef Processors, Inc.*, 704 F.2d 1351, 1361-62 (5th Cir. 1983). As in *Rufenacht v. Iowa Beef Processors, Inc.*, 656 F.2d 198 (5th Cir. 1981), *cert. denied*, 455 U.S. 921 (1982), the plaintiff attempted to apply collateral estoppel to avoid relitigating the agency issue. For the reasons discussed in *Rufenacht*, the court held that collateral estoppel could not be used on the facts of this case. *Brumley Estate v. Iowa Beef Processors, Inc.*, 704 F.2d 1351, 1356 (5th Cir. 1983). The collateral estoppel aspects of *Rufenacht* are discussed in Krahrmer, *Commercial Transactions, Annual Survey of Texas Law*, 35 Sw. L.J. 191, 203 (1981).

91. *Brumley Estate v. Iowa Beef Processors, Inc.*, 704 F.2d 1351, 1362 (5th Cir. 1983).

92. *See, e.g., Drake Ins. Co. v. King*, 606 S.W.2d 812 (Tex. 1980); *Pfluger v. Colquitt*, 620 S.W.2d 739 (Tex. Civ. App.—Dallas 1981, writ ref'd n.r.e.).

93. TEX. REV. CIV. STAT. ANN. art. 6687—1 (Vernon 1977 & Supp. 1984).

94. 653 S.W.2d 948 (Tex. App.—Fort Worth 1983, no writ).

95. *Id.* at 950-51.

96. TEX. BUS. & COM. CODE ANN. § 2.601 (Tex. UCC) (Vernon 1968).

no matter how slight the deviation.⁹⁷ Also, when the goods comprise several commercial units, the buyer may reject the defective units and accept the rest.⁹⁸ In *Texas Imports v. Allday*⁹⁹ the buyer rejected 22 of 49 cattle as nonconforming under the sales contract. The buyer attempted to tender payment for the 27 accepted cattle, but the seller rejected the tender. The buyer then returned all 49 cattle to the seller under an agreement providing that both parties retained their legal rights as they existed at the time of tender, pending the outcome of litigation. In a carefully reasoned opinion the Tyler court of appeals discussed the application of the perfect tender rule in sales cases and its relation to other Code provisions. The court concluded that the buyer was entitled to reject the nonconforming cattle and accept those that did conform.¹⁰⁰ The seller did not assert a right to cure under section 2.508. The case is worth examination because it is the first Texas decision discussing the operation of the Code provisions on tender of goods, rather than erroneously using the general contract law of substantial performance.¹⁰¹

Revocation of Acceptance. While the Code adopts the perfect tender rule as the operative standard for cases of initial tender,¹⁰² other Code provisions limit the apparent harshness of the rule in a variety of circumstances.¹⁰³ One of these limitations, section 2.508, provides two distinct rules granting the seller a right to cure defects in the tendered goods. First, if the time for performance has not passed, the seller may seasonably notify the buyer that the defects will be cured and may make a conforming tender within the contract time.¹⁰⁴ Second, if the time for performance has passed and the buyer rejects a nonconforming tender that the seller reasonably believed would be acceptable, the seller may seasonably notify the buyer and have a further reasonable time to substitute a conforming tender.¹⁰⁵ Operation of the perfect tender rule is also limited when the buyer initially accepts the goods but later attempts to revoke the acceptance. In this circumstance section 2.608 prevents the buyer from revoking acceptance unless the nonconformity substantially impairs the value of the goods.¹⁰⁶

In a case of first impression in Texas, *Gappelburg v. Landrum*,¹⁰⁷ both

97. *Id.* The seller is protected against surprise rejection by the right to cure granted in *id.* § 2.508.

98. *Id.* § 2.601.

99. 649 S.W.2d 730 (Tex. App.—Tyler 1983, writ ref'd n.r.e.).

100. *Id.* at 737-38.

101. *Del Monte Corp. v. Martin*, 574 S.W.2d 597 (Tex. Civ. App.—San Antonio 1978, no writ), provides a good contrast to *Texas Imports* because it invokes the general contract rule of substantial performance.

102. TEX. BUS. & COM. CODE ANN. § 2.601 (Tex. UCC) (Vernon 1968).

103. *See, e.g., id.* §§ 2.508 (cure by seller of improper tender or delivery), 2.512 (payment by buyer before inspection), 2.608 (revocation of acceptance in whole or in part).

104. *Id.* § 2.508(a).

105. *Id.* § 2.508(b).

106. *Id.* § 2.608(a).

107. 654 S.W.2d 549 (Tex. App.—Dallas 1983), *rev'd*, 27 Tex. Sup. Ct. J. 260 (Feb. 29, 1984).

the Dallas court of appeals and the Texas Supreme Court confronted the issue of how the buyer's right to revocation and the seller's right to cure should be read together when both rights arise out of the same transaction. In this case the buyer purchased an expensive big screen television that failed to work properly. The seller repaired some of the defects during the next two weeks. Three weeks after the sale, the set stopped working completely and the buyer notified the seller of the problem. The seller's service representative told the buyer that the set would have to be taken to the repair shop, but no one came to pick it up despite several calls to the seller. Within a few days the buyer asked for his money back and the seller responded with an offer of a replacement. The buyer maintained his position that a replacement would not be acceptable, and sued to recover the price paid for the television. Both parties agreed that the buyer properly revoked acceptance of the set, thus squarely raising the issue of whether the seller had a right to cure after a proper revocation.¹⁰⁸

The court of appeals recognized the novelty of the issue and carefully reviewed cases from other jurisdictions, as well as numerous secondary authorities.¹⁰⁹ The court reasoned that the right to cure by repair ended when the buyer properly revoked acceptance under section 2.608.¹¹⁰ As to whether a right to cure by replacement survived the revocation of acceptance, however, the court noted that an underlying policy of the Code encourages parties to work out their differences and to minimize losses resulting from defective performance.¹¹¹ The court viewed the right to cure under section 2.508 as a means of avoiding injustice by reason of a surprise rejection by the buyer.¹¹² The court concluded that a seller's right to cure by replacement survived a buyer's revocation of acceptance after a sequence of unsuccessful repair attempts.¹¹³ On appeal the Texas Supreme Court reversed the court of appeals and held that a better policy view was to terminate the right to cure after revocation of acceptance, whether the proposed cure was by repair or by replacement.¹¹⁴ Despite their opposite resolution of the narrow issue presented by the case, both of the *Gappelberg* opinions are worth reading on the subjects of revocation of acceptance and the right to cure as a valuable review of the policy issues underlying these important areas of commercial law.

Substituted Performance. One of chapter 2's most important functions is

108. *Id.* at 551.

109. *Id.* at 552-53. The authorities cited in the opinion are a good compendium on the issues presented by the case.

110. *Id.* at 551-52; *see* TEX. BUS. & COM. CODE ANN. § 2.608 (Tex. UCC) (Vernon 1968).

111. 654 S.W.2d at 552 (citing J. WHITE & R. SUMMERS, HANDBOOK OF THE LAW UNDER THE UNIFORM COMMERCIAL CODE § 8-2, at 299 n.23 (2d ed. 1980)).

112. 654 S.W.2d at 552 (citing TEX. BUS. & COM. CODE ANN. § 2.508 comment 2 (Tex. UCC) (Vernon 1968)).

113. 654 S.W.2d at 552.

114. *Gappelberg v. Landrum*, 27 Tex. Sup. Ct. J. 260, 262 (Feb. 29, 1984).

filling gaps in sales contracts by statutorily providing omitted terms.¹¹⁵ Because an underlying tenet of the Code is to permit freedom of contract to significant degree,¹¹⁶ parties are generally free to contract as they wish on subjects covered by the gap-filling provisions. *Jon-T Chemicals, Inc. v. Freeport Chemical Co.*¹¹⁷ illustrates both the Code's gap-filling function and the parties' freedom to contract. The parties in *Jon-T* agreed to buy and sell chemicals under a contract containing a comprehensive *force majeure* clause excusing the seller's performance on occurrence of various contingencies. The contract also provided that all deliveries were to be "by rail 'unless otherwise agreed.'"¹¹⁸ Because of extreme weather conditions during the winter of 1978-1979, the seller failed to deliver 598 short tons of acid ordered by the buyer. In an action by the buyer for damages for nondelivery, the court held that the parties agreed to make all deliveries by rail unless they mutually agreed to some other method.¹¹⁹ The seller's performance was therefore excused under the contract's *force majeure* clause because of the adverse weather conditions.¹²⁰ The buyer argued that section 2.614 of the Code established a gap-filling rule that required the seller to make deliveries by alternate means such as by truck.¹²¹ Although the Code does provide this rule, the court held that the parties' agreement superseded section 2.614 and that the seller was required only to make delivery as specified in the contract.¹²²

F. Remedies

Cost of Cover as General Damages. One of the Code's innovations is its establishment of certain damage rules providing both sellers and buyers with an efficient means of fixing damages while simultaneously minimizing losses caused by a default.¹²³ Of these rules, the most notable is section 2.712, which creates the buyer's right to cover.¹²⁴ Under section 2.712, an aggrieved buyer may cover by purchasing goods in substitution for those originally due from the defaulting seller.¹²⁵ The substitute purchase, however, must be made in good faith, without unreasonable delay, and on reasonable terms.¹²⁶ Once the purchase is properly made, the buyer's damages are calculated as the difference between the cost of cover and the contract price, plus any incidental or consequential damages caused by the

115. This function of the Code, along with numerous examples, is discussed at length in J. WHITE & R. SUMMERS, *supra* note 111, § 3-4 to -9.

116. See TEX. BUS. & COM. CODE ANN. § 1.102(c) (Tex. UCC) (Vernon 1968).

117. 704 F.2d 1412 (5th Cir. 1983).

118. *Id.* at 1415 (emphasis in original).

119. *Id.* at 1415-17.

120. *Id.*

121. See TEX. BUS. & COM. CODE ANN. § 2.614 (Tex. UCC) (Vernon 1968).

122. 704 F.2d at 1416-17.

123. The seller is provided with the remedy of resale under TEX. BUS. & COM. CODE ANN. § 2.706 (Tex. UCC) (Vernon 1968), while the buyer is entitled to cover by obtaining substitute goods under *id.* § 2.712.

124. *Id.*

125. *Id.* § 2.712(a).

126. *Id.*

seller's breach.¹²⁷ A distinct advantage of the cover remedy is its avoidance of the cumbersome process of proving market value at the time of breach.¹²⁸

In *Hess Die Mold, Inc. v. American Plasti-Plate Corp.*¹²⁹ a manufacturer of die molds failed to manufacture and deliver a mold within the time specified by the sales contract. When it became apparent that the seller would be unable to supply the mold, the buyer entered into a contract with another manufacturer to obtain a substitute mold costing \$24,000 more than that originally contracted for. In the buyer's action to recover its down payment and the cost of cover, the seller contended that the cover damages were special damages not contemplated by the parties at the time the contract was signed and therefore not recoverable. The court reviewed the Code provisions on cover damages¹³⁰ and on consequential damages¹³¹ and concluded that cover damages constituted an item of general damages recoverable from any defaulting seller regardless of whether they were contemplated by the parties at the time the contract was signed.¹³²

Statute of Limitations in Sales Cases. An earlier survey noted that *Garcia v. Texas Instruments, Inc.*¹³³ introduced a serious element of confusion into the question of when the four-year statute of limitations begins to run in claims for personal injuries based on a breach of warranty under the Code.¹³⁴ In *Garcia* the Texas Supreme Court clearly held that implied warranty actions for personal injuries are within the section 2.725 four-year statute of limitations rather than the two-year general tort statute of limitations.¹³⁵ In its opinion, however, the court referred to two different starting points for the statute of limitations, the date of the accident¹³⁶ and the date of sale.¹³⁷ Nowhere in the opinion did the court clarify which date applies.

This confusion already has caused one possibly erroneous decision¹³⁸ and now has led to a second decision, *Garvie v. Duo-Fast Corp.*,¹³⁹ that may also be incorrect. In *Garvie*, however, the Fifth Circuit faced the additional problem of dealing with its own federal precedent¹⁴⁰ as well as

127. *Id.* § 2.712(b).

128. The Code rules on proof of market value and admissibility of market quotations give some idea of the difficulties of proof involved in this issue. *See id.* §§ 2.723-.724.

129. 653 S.W.2d 927 (Tex. App.—Tyler 1983, no writ).

130. TEX. BUS. & COM. CODE ANN. § 2.712 (Tex. UCC) (Vernon 1968).

131. *Id.* § 2.715.

132. 653 S.W.2d at 929-30.

133. 610 S.W.2d 456 (Tex. 1980).

134. Krahmer, *supra* note 46, at 208-09; *see* TEX. BUS. & COM. CODE ANN. § 2.725 (Tex. UCC) (Vernon 1968).

135. 610 S.W.2d at 458-63; *see* TEX. REV. CIV. STAT. ANN. art. 5526(4) (Vernon Supp. 1984).

136. 610 S.W.2d at 457.

137. *Id.* at 465.

138. Cleveland v. Square-D Co., 613 S.W.2d 790 (Tex. Civ. App.—Houston [14th Dist.] 1981, no writ).

139. 711 F.2d 47 (5th Cir. 1983).

140. Clark v. DeLaval Separator Corp., 639 F.2d 1320 (5th Cir. 1981).

Garcia, the applicable Texas law. Because of *Garcia's* lack of clarity, the court considered itself bound by federal precedent, which recognizes the date of sale as triggering the statute of limitations.¹⁴¹ While this decision is a practical response to the *Garcia* problem, a state court clarification of *Garcia* would be desirable.¹⁴²

III. COMMERCIAL PAPER

A. Form of Negotiable Instruments

Time of Maturity. One important distinction between demand instruments and time instruments concerns the accrual date of a cause of action. Section 3.122 of the Code provides: "(a) A cause of action against a maker or an acceptor accrues (1) in the case of a time instrument on the day after maturity; (2) in the case of a demand instrument upon its date or, if no date is stated, on the date of issue."¹⁴³ In *Loomis v. Republic National Bank*¹⁴⁴ a debtor executed a note payable "on demand or if no demand is made 1-31-77."¹⁴⁵ The holder of the note filed suit more than four years after the note was issued, but less than four years after January 31, 1977. Whether the suit was within the limitation period depended entirely on classification of the note as a demand instrument or a time instrument.¹⁴⁶ The court found no Texas authority or Code provision dealing with this issue. The court did find a pre-Code Oklahoma case that discussed the precise problem.¹⁴⁷ The *Loomis* court adopted the Oklahoma court's rationale, which construed the note as a time instrument.¹⁴⁸ The cause of

141. 711 F.2d at 48.

142. A judicial clarification must, of course, work within the confines of existing legislation. Based solely on the ordinary methods of statutory interpretation, the reading of TEX. BUS. & COM. CODE ANN. § 2.725 (Tex. UCC) (Vernon 1968) by the federal court in *Clark v. DeLaval Separator Corp.*, 639 F.2d 1320, 1324-25 (5th Cir. 1981), is sound: cause of action based on breach of implied warranty accrues when tender of delivery is made because an implied warranty by its very nature does not extend to the future performance of the goods. Unless a court is willing to hold that implied warranty actions for personal injuries somehow extend to future performance, but other implied warranties do not (a distinction of dubious theoretical merit, although probably responsive to a felt need), a legislative clarification may be desirable. In a concurring opinion in *Garvie*, Judge Rubin stated, "Although I was a member of the panel that decided *Clark*, I write separately to state that, on further reflection, the result in that case seems unjust: a plaintiff's cause of action may have accrued and been extinguished before the plaintiff is injured." 711 F.2d at 49. Judge Rubin's statement may point up a need for reevaluating the function of TEX. BUS. & COM. CODE ANN. § 2.725 (Tex. UCC) (Vernon 1968) as a commercial statute of limitations in contrast to its developing use as a de facto tort statute of limitations in cases of personal injury or property damage. One must remember that this provision of the Code antedates the development of strict liability in tort as a separate cause of action and that the way of viewing injury and property claims in tort is vastly different today than when the Code was written. As needs change, statutes should be revised.

143. *Id.* § 3.122(a).

144. 653 S.W.2d 75 (Tex. App.—Dallas 1983, writ ref'd n.r.e.).

145. *Id.* at 77.

146. TEX. REV. CIV. STAT. ANN. art. 5527(1) (Vernon Supp. 1984) (four-year statute of limitations for promissory notes).

147. *First Nat'l Bank v. Bell*, 140 Okla. 24, 282 P. 147 (1929).

148. 653 S.W.2d at 78.

action, therefore, could be maintained.¹⁴⁹

B. Enforcement of Commercial Paper

Rights Acquired Absent Due Negotiation. If an instrument is transferred for value, the transferee acquires the specifically enforceable right to have the transferor's unqualified indorsement.¹⁵⁰ Until the indorsement is made, however, the transferee does not qualify as a holder because the instrument has not been duly negotiated, and no presumption exists that the transferee is the owner of the instrument.¹⁵¹ A transferee who takes an instrument without simultaneously obtaining a proper indorsement runs the risk of having to prove proper ownership, instead of avoiding the issue by raising a presumption of ownership on a motion for summary judgment.

This precise situation occurred in *First State Bank v. Hughes*.¹⁵² The payor bank, as successor to the rights of the transferee, learned that its failure to return the instrument for lack of a proper indorsement, and the failure of the transferee to obtain such an indorsement, forced a full trial on the merits to prove the issues surrounding the instrument's transfer.¹⁵³ The case would not have arisen if the instrument had been properly indorsed. Needless to say, the lesson was a time consuming and expensive one. Payor banks should examine instruments presented for payment with greater care.

Rights Acquired When Instrument Is Duly Negotiated. When a transferee acquires an instrument by due negotiation, the transferee qualifies as a holder and is entitled to recover on the instrument, unless the effectiveness of a necessary signature is put in issue or the defendant establishes a defense.¹⁵⁴ In many instances the mere production of an instrument that is duly issued or negotiated to the holder is a sufficient basis for recovery on a motion for summary judgment.¹⁵⁵ In *Zarges v. Bevan*¹⁵⁶ the Texas Supreme Court reaffirmed the principle that a photocopied instrument, sworn to be true and correct, is proper evidence to support a summary judgment. In cases involving the production of photocopies, however, a court may require security indemnifying the defendant against loss due to later claims made on the instrument.¹⁵⁷

149. *Id.*

150. TEX. BUS. & COM. CODE ANN. § 3.201(c) (Tex. UCC) (Vernon 1968).

151. *Id.*

152. 654 S.W.2d 31 (Tex. App.—Tyler 1983, no writ).

153. *Id.* at 32-33.

154. TEX. BUS. & COM. CODE ANN. § 3.307 (Tex. UCC) (Vernon 1968).

155. *See, e.g., Zarges v. Bevan*, 652 S.W.2d 368 (Tex. 1983); *Jackson T. Fulgham Co. v. Stewart Title Guar. Co.*, 649 S.W.2d 128 (Tex. App.—Dallas 1983, writ ref'd n.r.e.); *Tyra v. Dowell*, 644 S.W.2d 558 (Tex. App.—El Paso 1983, writ ref'd n.r.e.).

156. 652 S.W.2d 368 (Tex. 1983) (reaffirming *Life Ins. Co. v. Gar-Del, Inc.*, 570 S.W.2d 378 (Tex. 1978)).

157. *See* TEX. BUS. & COM. CODE ANN. § 3.804 (Tex. UCC) (Vernon 1968).

C. Defenses to Enforcement of Commercial Paper

Garnishment as a Defense. If a holder acquires an instrument for value, in good faith, and without notice that it is overdue or of any defense against it, the holder qualifies as a holder in due course.¹⁵⁸ The holder in due course takes the instrument free of many possible defenses assertable against the assignee of a simple contract.¹⁵⁹ *William v. Stansbury*¹⁶⁰ illustrates the high degree of protection accorded to a holder in due course. In *Williams* a holder purchased an instrument without knowledge of the instrument's prior subjection to garnishment proceedings. The jury found that the holder was unaware that the note was in default or subject to garnishment proceedings at the time of purchase. The Texas Supreme Court properly held that the holder in due course took the note free of any defenses or claims arising from the garnishment proceedings.¹⁶¹ The court would have reached the opposite result if a simple debt had been involved, or if the party had not been a holder in due course.¹⁶²

IV. BANK TRANSACTIONS

A. Bank Deposits

Limitations on Right of Set-Off. United States courts have adopted two distinct rules governing a bank's right to set-off the account of a depositor against debts owed to the bank. The first rule permits set-off unless the bank has actual or constructive notice that the account is held by the depositor in trust for another.¹⁶³ The second rule prohibits set-off when the bank has actual or constructive notice that the depositor is holding funds in trust, but also requires the bank to show a detrimental change of position in reliance on the set-off to avoid liability to the equitable owner even if the bank has no initial knowledge of the trust.¹⁶⁴

Texas follows the latter rule, referred to as the equitable set-off or federal set-off rule.¹⁶⁵ Two cases reported during the survey period applied

158. *Id.* § 3.302.

159. Compare *id.* § 3.305 (rights of a holder in due course) with *id.* § 3.306 (rights of one not a holder in due course).

160. 649 S.W.2d 293 (Tex. 1983).

161. *Id.* at 296.

162. *Id.* at 296 n.2.

163. See, e.g., *Keeney v. Bank of Italy*, 33 Cal. App. 515, 165 P. 735 (1917); *Clemmer v. Drover's Nat'l Bank*, 157 Ill. 206, 41 N.E. 728 (1895); *First Nat'l Bank v. Eastern Trust & Banking Co.*, 108 Me. 79, 79 A. 4 (1911); *Wagner v. Citizens' Bank & Trust Co.*, 122 Tenn. 164, 122 S.W. 245 (1909).

164. The following states have adopted the equitable set-off rule: Colorado, Indiana, Michigan, Minnesota, Nebraska, Oklahoma, Pennsylvania, South Carolina, South Dakota, and Wisconsin. See *Cox v. Metropolitan State Bank, Inc.*, 138 Colo. 576, 336 P.2d 742 (1959); *Peoples State Bank v. Caterpillar Tractor Co.*, 213 Ind. 235, 12 N.E.2d 123 (1938); *Burnett v. First Nat'l Bank*, 38 Mich. 630 (1878); *Berg v. Union State Bank*, 186 Minn. 529, 243 N.W. 696 (1932); *Allen Dudley & Co. v. First Nat'l Bank*, 122 Neb. 443, 240 N.W. 522 (1932); *Brady v. American Nat'l Bank*, 120 Okla. 162, 250 P. 1006 (1926); *Sherts v. Fulton Nat'l Bank*, 342 Pa. 337, 21 A.2d 18 (1941); *Peurifoy v. Boswell*, 162 S.C. 107, 160 S.E. 156 (1931); *Thompson v. Commercial & Sav. Bank*, 50 S.D. 154, 208 N.W. 780 (1926); *Commercial Discount Corp. v. Milwaukee W. Bank*, 61 Wis. 2d 671, 214 N.W.2d 33 (1974).

165. The Texas Supreme Court adopted this rule in *National Indem. Co. v. Spring*

the first portion of the equitable rule.¹⁶⁶ In each case the set-off was disallowed when the depositor demonstrated that the bank had notice that the funds were held in trust for another.¹⁶⁷

B. Bank Collections

Time Allowed for Paying Documentary Drafts. The midnight deadline applicable to the handling of checks and other demand items by a payor bank¹⁶⁸ does not cover the handling of documentary drafts.¹⁶⁹ With documentary drafts a payor bank is required to follow the instructions of its transferor regarding the time allowed for acceptance or payment. A failure to follow instructions may result in liability for the payor bank.¹⁷⁰ If a documentary draft is "payable at" a named bank, the Code makes the named bank a payor bank for purposes of determining its rights and responsibilities concerning the draft and accompanying documents.¹⁷¹ In *Hamby Co. v. Seminole State Bank*¹⁷² the Texas Supreme Court reversed the appellate court decision, which held that two drafts designated as payable at the Seminole bank made that bank a mere collecting bank responsible only for making seasonable collection of the drafts.¹⁷³ Instead, the supreme court ruled that the Seminole bank was a payor bank and thus required to follow the instructions of its transferor concerning the time for payment or, failing payment, the time for returning the draft.¹⁷⁴ The transferor presented the drafts and accompanying invoices to the bank on April 4, 1980, and instructed the bank not to hold the drafts after the maturity date of April 10, 1980, unless otherwise instructed. On April 14, 1980, the transferor inquired into the status of the drafts. The bank, having not yet paid the drafts, returned them the same day. The supreme court concluded that the payor bank became accountable for the drafts under section 4.302 of the Code by failing to dishonor and return the drafts on April 10, 1980, in accordance with the instructions.¹⁷⁵

Branch State Bank, 162 Tex. 521, 348 S.W.2d 528 (1961), and has been followed in Texas since that time. See, e.g., *Continental Nat'l Bank v. Great Am. Management & Inv., Inc.*, 606 S.W.2d 346 (Tex. Civ. App.—Fort Worth 1980, writ ref'd n.r.e.); *First Nat'l Bank v. Lone Star Life Ins. Co.*, 524 S.W.2d 525 (Tex. Civ. App.—Dallas 1975, writ ref'd n.r.e.).

166. *Reed v. Valley Fed. Sav. & Loan Co.*, 655 S.W.2d 259 (Tex. App.—Corpus Christi 1983, writ ref'd n.r.e.); *Collin County Sav. & Loan v. Miller Lumber Co.*, 653 S.W.2d 114 (Tex. App.—Dallas 1983, no writ).

167. *Reed v. Valley Fed. Sav. & Loan Co.*, 655 S.W.2d 259, 261-64 (Tex. App.—Corpus Christi 1983, writ ref'd n.r.e.); *Collin County Sav. & Loan v. Miller Lumber Co.*, 653 S.W.2d 114, 117 (Tex. App.—Dallas 1983, no writ).

168. The midnight deadline is midnight of the next banking day following the day of receipt of an item or other relevant notice. TEX. BUS. & COM. CODE ANN. § 4.104(a)(8) (Tex. UCC) (Vernon 1968).

169. *Id.* § 4.301.

170. *Id.* § 4.302.

171. *Id.* § 3.121.

172. 652 S.W.2d 939 (Tex. 1983).

173. *Hamby Co. v. Seminole State Bank*, 649 S.W.2d 81, 82-83 (Tex. App.—El Paso 1982). The seasonable time standard for collecting banks appears in TEX. BUS. & COM. CODE ANN. § 4.202 (Tex. UCC) (Vernon 1968).

174. 652 S.W.2d at 941.

175. *Id.* at 941; see TEX. BUS. & COM. CODE ANN. § 4.302(2) (Tex. UCC) (Vernon 1968).

C. Letters of Credit

Limits on the Use of a Letter of Credit. The letter of credit is an extremely versatile, widely accepted financing device¹⁷⁶ because it amounts to an almost iron-clad guarantee to pay the letter's beneficiary.¹⁷⁷ By comparison, a negotiable instrument is an I.O.U. written on the back of a matchbook. Despite its security, the letter of credit is still not acceptable for some purposes, as demonstrated in *Heritage Housing Corp. v. Ferguson*.¹⁷⁸ In *Heritage* the appellant sought leave to file a letter of credit in lieu of the surety bond required under Texas Rule of Civil Procedure 14(c).¹⁷⁹ The court denied the motion and properly held that a letter of credit is not a negotiable instrument and therefore does not qualify as a proper form of bond under rule 14(c).¹⁸⁰ As a practical matter, a letter of credit is as secure as the negotiable bank obligations required by rule 14(c). The rule could be appropriately amended to include letters of credit as an approved form of surety bond.

V. INVESTMENT SECURITIES

A. Enforcement of Securities Contracts

Statute of Frauds. Section 8.319 of the Code contains a statute of frauds provision that requires enforceable contracts for the sale of securities to be in writing unless one of the limited exceptions is met.¹⁸¹ In *Consolidated Petroleum Industries, Inc. v. Jacobs*¹⁸² the Eastland court of appeals held that an oral contract to sell securities was not enforceable because no written agreement existed and none of the statutory exceptions applied.¹⁸³ The plaintiff urged, however, that the common law doctrine of promissory estoppel created an additional exception to section 8.319. The court agreed that promissory estoppel is available as a statute of frauds exception in securities cases, but ruled that promissory estoppel did not apply in this case because the plaintiff presented no proof that the defendants orally

176. See, e.g., *East Girard Sav. Ass'n v. Citizens Nat'l Bank & Trust Co.*, 593 F.2d 598 (5th Cir. 1979) (letter of credit used to guarantee credit of contractor on construction project); *Cypress Bank v. Southwestern Bell Tel. Co.*, 610 S.W.2d 185 (Tex. Civ. App.—Houston [1st Dist.] 1980, writ ref'd n.r.e.) (standby letter of credit used to guarantee payment of telephone charges); *Siderius, Inc. v. Wallace Co.*, 583 S.W.2d 852 (Tex. Civ. App.—Tyler 1979, no writ) (letter of credit used in sale of goods transaction).

177. See TEX. BUS. & COM. CODE ANN. § 5.114 (Tex. UCC) (Vernon 1968).

178. 651 S.W.2d 272 (Tex. App.—Dallas 1983, no writ).

179. TEX. R. CIV. P. 14(c).

180. 651 S.W.2d at 273.

181. TEX. BUS. & COM. CODE ANN. § 8.319 (Tex. UCC) (Vernon 1968).

182. 648 S.W.2d 363 (Tex. App.—Eastland 1983, no writ).

183. *Id.* at 366. Under TEX. BUS. & COM. CODE ANN. § 8.319 (Tex. UCC) (Vernon 1968) the statutory exceptions are: (1) that there be some writing signed by the party to be charged showing the quantity and price of the securities involved in the contract, *id.* § 8.319(1); (2) that delivery or payment is made, *id.* § 8.319(2); (3) that the party to be charged receives a written confirmation of the oral agreement and makes no objection within 10 days after receipt, *id.* § 8.319(3); and (4) that the party against whom enforcement is sought admits in pleadings, testimony, or otherwise in court, that the contract was made, *id.* § 8.319(4).

promised to sign a written contract.¹⁸⁴

In *Mortgageamerica Corp. v. American National Bank*¹⁸⁵ the plaintiff successfully met one of the section 8.319 exceptions by showing that the defendant received written confirmations of the contracted sale without objection, thereby making the contract enforceable even without a written agreement.¹⁸⁶ Although the defendant did not receive the confirmations until three months after the oral agreement, the defendant failed to request a special issue at trial on whether this delay was reasonable.¹⁸⁷ The court held that the defendant's failure precluded raising the issue on appeal.¹⁸⁸

B. Shareholder's Rights Against Issuer

Replacement of Lost Shares. In a case of first impression the Fifth Circuit Court of Appeals in *Glaser v. Texon Energy Corp.*¹⁸⁹ held that a shareholder is precluded from compelling an issuer to replace lost share certificates if the shareholder fails to provide reasonable information to the issuer about the lost shares pursuant to the issuer's request under section 8.405 of the Code.¹⁹⁰ In *Glaser* the issuer requested the shareholder to provide a variety of information about the lost shares, apparently because the stock transfer records showed that all shares owned by the shareholder had been cancelled several years before. The shareholder never responded to this request and eventually filed suit to compel the issuance of replacement shares. The shareholder claimed an inability to meet the issuer's request for the numbers of the lost certificates. The court, however, noted that the issuer had a legitimate need for this information to avoid overissue under the Texas Business Corporation Act.¹⁹¹ Furthermore, the court recognized a need to identify the lost shares if the shares should ever be presented to the issuer for transfer.¹⁹²

184. 648 S.W.2d at 367. As adopted in Texas, the promissory estoppel exception to the statute of frauds requires the party against whom enforcement is sought to have explicitly promised to sign and deliver a written contract meeting the requirements of the statute of frauds. See, e.g., *Nagle v. Nagle*, 633 S.W.2d 796 (Tex. 1982); "*Moore*" *Burger, Inc. v. Phillips Petroleum Co.*, 492 S.W.2d 934 (Tex. 1972).

185. 651 S.W.2d 851 (Tex. App.—Austin 1983, writ ref'd n.r.e.).

186. See TEX. BUS. & COM. CODE ANN. § 8.319(3) (Tex. UCC) (Vernon 1968).

187. See *id.*

188. 651 S.W.2d at 856-57.

189. 702 F.2d 569 (5th Cir. 1983).

190. *Id.* at 572. TEX. BUS. & COM. CODE ANN. § 8.405(b) (Tex. UCC) (Vernon 1968) (amended 1983) provided:

(b) Where the owner of a security claims that the security has been lost, destroyed or wrongfully taken, the issuer must issue a new security in place of the original security if the owner

(1) so requests before the issuer has notice that the security has been acquired by a bona fide purchaser; and

(2) files with the issuer a sufficient indemnity bond; and

(3) satisfies any other reasonable requirements imposed by the issuer.

This section has been amended since the decision in *Glaser*, but the revision has no effect on the validity of the case. See *id.* § 8.405(b) (Tex. UCC) (Vernon Supp. 1984).

191. 702 F.2d at 572; see TEX. BUS. CORP. ACT ANN. arts. 2.12-.16 (Vernon 1980).

192. 702 F.2d at 572.

C. Legislative Changes

The New Chapter 8. The 68th Legislature adopted a completely revised chapter 8 for the Business and Commerce Code.¹⁹³ A comprehensive review of the new chapter 8 is beyond the scope of this Article, but four main areas of the revision deserve particular mention.¹⁹⁴

First, the revision creates a new form of corporate share ownership, the uncertificated security.¹⁹⁵ This new form of security necessitated the conforming changes in chapter 1 of the Code that were described earlier in the discussion of chapter 1.¹⁹⁶

Second, because the uncertificated security does not have a tangible existence, no share certificate can be seized by attachment or levy. A judgment creditor can reach uncertificated securities registered in the name of a judgment debtor only by legal process at the issuer's chief executive office in the United States.¹⁹⁷ Both the new and the old chapter 8 specifically provide that a creditor attempting to levy on securities is entitled to the aid of a court of appropriate jurisdiction in reaching the securities.¹⁹⁸

Third, the creation of a security interest in investment securities will be governed by section 8.321 instead of section 9.203, whether or not the shares are certificated.¹⁹⁹ If a lender has established procedures for acquiring a security interest in shares of stock, these procedures do not have to be changed because the substance of section 8.321 is identical to the former section 9.203.²⁰⁰ The new chapter 8 does not compel the issuance of uncertificated securities. An issuer is free to choose whether a particular issue will be entirely certificated, uncertificated, or a mixture of both.²⁰¹ If the latter choice is made, the holder is entitled to exchange a certificated security for one that is uncertificated or vice versa.²⁰² A secured lender who prefers not to deal with uncertificated shares, therefore, is entitled to have certificated shares issued in the name of the lender, unless the particular stock issue is completely uncertificated.²⁰³

A secured loan against uncertificated securities is made and simultane-

193. Act of Sept. 1, 1983, ch. 442, 1983 Tex. Gen. Laws 2511-83 (codified at TEX. BUS. & COM. CODE ANN. §§ 8.101-408 (Tex. UCC) (Vernon Supp. 1984)).

194. For those interested in a comprehensive discussion of the new chapter 8 and its effect on Texas law, see Special Project, *Uncertificated Securities, Articles 8 and 9 of the U.C.C., and the Texas Business Corporation Act: A New System to Accommodate Modern Securities Transactions*, 11 TEX. TECH L. REV. 813 (1980). The article includes the full text of the article 8 revision. A limited number of reprints of the article are available and, within the limits of availability, the author of this *Survey* Article will be happy to supply copies upon request.

195. TEX. BUS. & COM. CODE ANN. § 8.102(a)(2) (Tex. UCC) (Vernon Supp. 1984).

196. See *supra* notes 4-7 and accompanying text.

197. TEX. BUS. & COM. CODE ANN. § 8.317(b) (Tex. UCC) (Vernon Supp. 1984).

198. *Id.* § 8.317(f).

199. *Id.* § 8.321.

200. Compare *id.* (enforceability, attachment, perfection, and termination of security interests) with *id.* § 9.203 (Vernon Supp. 1982-1983) (amended 1983) (attachment and enforceability of security interests).

201. *Id.* § 8.407 (Vernon Supp. 1984).

202. *Id.*

203. *Id.*

ously perfected by registration of the pledge on the books of the issuer or transfer agent.²⁰⁴ If the debtor signs a written security agreement describing the security, the security interest arises and is perfected at the time the secured party gives new value.²⁰⁵ This security interest becomes unperfected, however, after twenty-one days unless perfected by transfer within that time.²⁰⁶ An advantage to lending on uncertificated securities is that the security is not subject to loss or theft and the secured party is insulated from liability for such loss under the duty of care rules stated in section 9.207.²⁰⁷

Fourth, under the new chapter 8, a second secured party can obtain a perfected security interest in shares merely by notifying the first secured party of the creation of the second security interest.²⁰⁸ Perfection by notice is available for either a certificated or an uncertificated security.²⁰⁹ This change corrects a problem that existed under the former version of section 9.305, which required an acknowledgment from the first secured party that he was willing to act as bailee for the benefit of the second secured party.²¹⁰

VI. SECURED TRANSACTIONS

A. Creation of Security Interests

Classification of Collateral. The primary purpose of collateral classification under chapter 9 is to determine the proper method of perfection and, when a filing is necessary, where the filing should be made.²¹¹ In one instance, however, collateral classification is especially important because it may act as a direct limitation on the validity of a security interest, rather than merely as a means to perfect the security interest. For example, section 9.204 provides that no security interest attaches to consumer goods under an after-acquired property clause if the goods are acquired more than ten days after the secured creditor gives value under the security agreement.²¹²

In *Citizens National Bank v. Baggerly*²¹³ a creditor attempted to foreclose on a security interest claimed under an after-acquired property clause in two automobiles owned by the debtor. The debtor defended on

204. *Id.* § 8.313(a)(2).

205. *Id.* § 8.313(a)(9).

206. *Id.* § 8.321(b). Section 8.321(b) is the new chapter 8 equivalent of the old rule in TEX. BUS. & COM. CODE ANN. § 9.304(d) (Tex. UCC) (Vernon Supp. 1982-1983) (amended 1983) that permitted automatic perfection in an instrument, including share certificates, for a period of 21 days from the time new value was given under a written security agreement. Section 9.304 was amended to allow automatic perfection of certificated securities only under section 8.321. Act of Sept. 1, 1983, ch. 443, § 19, 1983 Tex. Gen. Laws 2511, 2580-81.

207. *See* TEX. BUS. & COM. CODE ANN. § 9.207 (Tex. UCC) (Vernon Supp. 1984).

208. *Id.* § 8.313(a)(8).

209. *Id.*

210. *See* 1 F. ELLIOTT & M. RUUD, *supra* note 17, § 9.305 (Supp. 1983).

211. *See* TEX. BUS. & COM. CODE ANN. §§ 9.302, .401-.402 (Tex. UCC) (Vernon Supp. 1984).

212. *Id.* § 9.204(b).

213. 649 S.W.2d 812 (Tex. App.—Austin 1983, no writ).

the ground that the cars were consumer goods²¹⁴ and therefore were protected from foreclosure under section 9.204.²¹⁵ The Austin court of appeals held that the use to which the cars were put was a material issue of fact that was not litigated at trial.²¹⁶ The court remanded the case to determine if the cars were used primarily for personal, family, or household purposes or in a manner that classified the goods as equipment²¹⁷ or inventory.²¹⁸ In reaching this decision, the court stated, "In making such proof, 'the principle use to which the property is put should be considered as determinative' in establishing whether the property is 'consumer goods,' 'equipment,' 'farm products,' or 'inventory.'" ²¹⁹ Section 9.109 classifies goods as consumer goods or equipment if they are "used or bought for use" as consumer goods or equipment.²²⁰ One problem with the court's decision is its failure to discuss the possibility that the cars were bought for use as consumer goods or equipment and later converted to another classification. This problem of the collateral's transmutation is difficult and deserves more consideration than it received in *Baggerly*.²²¹

B. Priorities in Secured Collateral

Buyers of Livestock. While a buyer in the ordinary course of business normally takes free of a security interest created by the seller, a person buying farm products from one engaged in farming operations remains subject to claims asserted by the seller's secured creditors.²²² In *Cox v. Bancoklahoma Agri-service Corp.*²²³ a buyer purchased cattle from a person claiming to be a cattle trader. After the purchase, the seller's secured creditor sued the buyer for conversion of the cattle. The buyer raised two primary defensive issues: first, that he had purchased the cattle from a cattle trader and not from someone engaged in farming operations; and second, that the bank had waived its security interest in the cattle by permitting the debtor to sell cattle on prior occasions without the written con-

214. See TEX. BUS. & COM. CODE ANN. § 9.109(a) (Tex. UCC) (Vernon Supp. 1984).

215. *Id.* § 9.204(b). Section 9.109(a) defines goods as consumer goods if "they are used or bought for use primarily for personal, family or household purposes . . ." *Id.* § 9.109(a).

216. 649 S.W.2d at 813-14.

217. TEX. BUS. & COM. CODE ANN. § 9.109(b) (Tex. UCC) (Vernon Supp. 1984) defines goods as equipment if "they are used or bought for use primarily in business . . ."

218. *Id.* § 9.109(d) defines goods as inventory if "they are held by a person who holds them for sale or lease . . ."

219. 649 S.W.2d at 814 (quoting TEX. BUS. & COM. CODE ANN. § 9.109 comment 2 (Tex. UCC) (Vernon Supp. 1984)).

220. TEX. BUS. & COM. CODE ANN. § 9.109(a)-(b) (Tex. UCC) (Vernon Supp. 1984).

221. Transmutation of collateral is discussed at some length in J. WHITE & R. SUMMERS, *supra* note 111, § 23-13. Although the collateral involved in *Baggerly* was automobiles, the Certificate of Title Act, TEX. REV. CIV. STAT. ANN. art. 6687-1 (Vernon 1977), was not in issue because no third-party claimants contested the validity of the security interest's perfection. As between a secured creditor and a debtor, a security interest is effective without perfection. TEX. BUS. & COM. CODE ANN. § 9.201 (Tex. UCC) (Vernon Supp. 1984).

222. TEX. BUS. & COM. CODE ANN. § 9.307(a) (Tex. UCC) (Vernon Supp. 1984).

223. 641 S.W.2d 400 (Tex. App.—Amarillo 1982, no writ).

sent of the bank, despite language in the security agreement requiring such written consent.

On the first issue, the Amarillo court of appeals held that the buyer failed to establish that the seller was not engaged in farming operations.²²⁴ On the second issue, the court ruled that the buyer failed to show his reliance on the bank's prior conduct permitting the sale of cattle without written consent.²²⁵ Absent such a showing, the buyer was not entitled to a favorable ruling on the waiver issue.²²⁶

C. Proceedings After Default

Improper Repossession as Conversion. In two cases reported during the survey period a debtor alleged that a secured creditor converted the debtor's property while repossessing collateral after a default. In *Dolenz v. National Bank*²²⁷ a bank repossessed three large trailers. The bank was unaware that one of the trailers contained restaurant equipment. Several weeks passed before the bank was able to determine the ownership of the equipment. After learning that the equipment was probably owned by the debtor, the bank offered to return the property upon proof of ownership. The debtor never responded to the bank's offer, but later filed a conversion action. The court noted that conversion requires the intentional repudiation of an owner's right to the property and held that the bank took the restaurant equipment without knowledge or intent to exercise dominion or control over the property.²²⁸ Furthermore, the bank offered to return the property upon locating the apparent owner.²²⁹ The judgment of the trial court ruling in favor of the bank as a matter of law was affirmed.²³⁰

In *First National Bank v. Brown*²³¹ a bank erroneously failed to list one of the two cars owned by the debtor as collateral on the security agreement. When the debtor defaulted, both cars were repossessed. In a subsequent action by the debtor for conversion of the car not covered by the security agreement, the court held that a conversion had occurred because the bank failed to refer to the security agreement before the repossession.²³² Since the bank had the means of knowing that the repossession of both cars was improper under the security agreement, the court upheld a jury finding of willful and malicious conversion and an award of punitive damages.²³³

224. *Id.* at 403.

225. *Id.* at 404.

226. *Id.*

227. 649 S.W.2d 368 (Tex. App.—Fort Worth 1983, writ ref'd n.r.e.).

228. *Id.* at 370.

229. *Id.*

230. *Id.*

231. 644 S.W.2d 808 (Tex. App.—Corpus Christi 1982, writ ref'd n.r.e.).

232. *Id.* at 810.

233. *Id.* at 810-11.

D. Legislative Changes

Certificates of Title. The last legislature amended section 9.302 of the Code to include an accurate list of cross references to other certificate of title legislation that controls the perfection of security interests in various items of collateral.²³⁴ The legislature also amended the Parks and Wildlife Code to clarify the fact that chapter 9 of the Business and Commerce Code governs the resolution of priority disputes involving motorboats and outboard motors.²³⁵

Security Interests in Oil and Gas. The legislature added a new section 9.319, dealing with security interests in oil and gas, to chapter 9 of the Code.²³⁶ This new section protects persons owning an entire or fractional interest in oil and gas production and persons who have a right to receive payments based on production. These persons are provided with a security interest in the production to secure payment of the purchase price by the first purchaser.²³⁷ The security interest is perfected automatically and continues as a perfected security interest without a time limit, the signing of a security agreement, or the filing of a financing statement.²³⁸ The first purchaser's sale of oil or gas production to a buyer in the ordinary course of business cuts off the security interest in the oil and gas sold. The security interest continues, however, in the sales proceeds received by the first purchaser.²³⁹

Section 9.319 contains its own set of priority rules, which give security interests created by the section a special priority status over other security interests.²⁴⁰ The section also provides special rules concerning statutory liens and tax liens.²⁴¹ No portion of the section, however, correlates its provisions with other Code sections that deal with security interests in oil and gas.²⁴²

Section 9.319 in its present form is an unfortunate addition to the Code

234. Act of Aug. 29, 1983, ch. 290, 1983 Tex. Gen. Laws 1530. TEX. BUS. & COM. CODE ANN. § 9.302 (Tex. UCC) (Vernon Supp. 1984) now provides:

(c) The filing of a financing statement otherwise required by this Chapter is not necessary or effective to perfect a security interest in property subject to

(2) the following statutes of this state; the Certificate of Title Act, as amended (Article 6687-1, Vernon's Texas Civil Statutes); Subchapter B-1, Chapter 31, Parks and Wildlife Code, as amended, relating to the certificates of title for motorboat and outboard motors; the Texas Manufactured Housing Standards Act, as amended (Article 5221(f), Vernon's Texas Civil Statutes)

235. Act of Aug. 29, 1983, ch. 636, 1983 Tex. Gen. Laws 4062 (amending TEX. PARKS & WILD. CODE ANN. §§ 31.052-.055).

236. Act of Aug. 29, 1983, ch. 807, 1983 Tex. Gen. Laws 4657-65 (codified at TEX. BUS. & COM. CODE ANN. § 9.319 (Tex. UCC) (Vernon Supp. 1984).

237. TEX. BUS. & COM. CODE ANN. § 9.319(a) (Tex. UCC) (Vernon Supp. 1984).

238. *Id.* § 9.319(a)-(b).

239. *Id.* § 9.319(c), (e), (m).

240. *Id.* § 9.319(f)-(i).

241. *Id.* § 9.319(d), (f)-(h).

242. See, e.g., *id.* §§ 9.103, .401-.403.

because the section creates secret liens on oil and gas production. The entire concept of notice filing assures a simplified and readily accessible public record that reveals any security interests filed against a particular debtor. Section 9.319 will increase the cost of financing oil and gas production purchases by making the financing transactions bear the cost of a real estate title search, instead of a much less expensive financing statement records inquiry.²⁴³ At a minimum, the section should be amended to simplify the search procedure.

Filing and Search Fee Amendments. The legislature increased the fee for filing financing statements, termination statements, and release of collateral statements in the standard form prescribed by the secretary of state from three dollars to five dollars.²⁴⁴ The charge for filings in nonstandard form was increased to fifteen dollars from six dollars.²⁴⁵ The basic search fee remains ten dollars, unless a search certificate issued by a county filing officer contains listings for more than ten financing statements. An additional fifty cents will be charged for each listing over ten.²⁴⁶ A county filing officer is required only to provide information about financing statement filings and not information from the real estate records of the county.²⁴⁷

VII. CONTRACTS OF GUARANTY

Corporate Loan Not Usurious to Guarantors. In *RepublicBank Dallas v. Shook*²⁴⁸ the Texas Supreme Court held that an individual guarantor could not recover on a claim for usury regarding a loan made to a corporation owned by the guarantor, even though the corporation was established at the request of the lender for the sole purpose of permitting a loan at the higher corporate rate.²⁴⁹ After a lengthy review of cases in both Texas and other jurisdictions, the court aligned itself with the majority view. This view holds that corporate loans are not usurious unless the loan is actually made for a personal, family, or household purpose, rather than for a business or commercial purpose.²⁵⁰ The court found that the present loan was made to further a business enterprise and, therefore, was not usurious.²⁵¹

In *Stanley v. Conner Construction Co.*²⁵² the El Paso court of appeals reached a similar result, holding that a corporate loan guarantor could not assert a usury claim in regard to a loan made to the corporation.²⁵³ A

243. A Code financing statement search costs \$10. Few lawyers are willing to search a real estate title for that price. See *id.* § 9.407.

244. Act of Sept. 1, 1983, ch. 69, 1983 Tex. Gen. Laws 310.

245. *Id.*

246. Act of Aug. 29, 1983, ch. 562, 1983 Tex. Gen. Laws 3253.

247. *Id.*

248. 653 S.W.2d 278 (Tex. 1983).

249. *Id.* at 279-82.

250. *Id.* at 281.

251. *Id.* at 282.

252. 651 S.W.2d 34 (Tex. App.—El Paso 1983, no writ).

253. *Id.* at 38-39.

major issue in *Stanley* was whether the person asserting the usury claim was actually a principal obligor on the instrument or a guarantor. The court admitted parol evidence to show the intent of the parties and concluded that the individual should be classified as a guarantor.²⁵⁴ The court also held that whether the individual was technically termed an accommodation party, a guarantor of payment, or a guarantor of collection did not affect the person's inability to assert a usury claim.²⁵⁵

Consideration for Contract of Guaranty. In *Reed v. First National Bank*²⁵⁶ the court held that independent consideration was not necessary to bind a guarantor.²⁵⁷ A loan made to the principal was sufficient consideration to create a valid contract of guaranty.²⁵⁸

254. *Id.*

255. *Id.* at 39.

256. 645 S.W.2d 843 (Tex. App.—Dallas 1982, writ ref'd n.r.e.).

257. *Id.* at 845.

258. *Id.*