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COMMERCIAL TRANSACTIONS

John Krahmer*

THIS Article discusses cases arising under the Texas Business and Commerce Code during the 1992 Survey period as well as some cases of a similar nature arising under other statutes or at common law. Because of the proliferation of cases involving actions by and against the FDIC and the RTC, cases whose resolution turns primarily on the application of federal banking law have been included in the Banking Law Survey in this volume rather than in this Article.

I. GENERAL PROVISIONS

A. GOOD FAITH AND FAIR DEALING

Article One of the Code contains several provisions applicable to all commercial transactions covered by the Code. One of the provisions that has been prominent during the last few years is Section 1.203, which provides, “Every contract or duty within this title imposes an obligation of good faith in its performance or enforcement.” This statutory duty parallels the common law implied duty of good faith and fair dealing which is often asserted as an alternative claim. In Pack v. First Federal Savings & Loan Associa-
tion, the court held that a financial institution had fulfilled its duty of good faith to the purchasers of a house when the institution fully disclosed its knowledge about the possible existence of another contract to sell the same house to another purchaser. The court treated the disclosure as adequate to fulfill both the statutory duty and the common law duty of good faith.

In *Cockrell v. Republic Mortgage Insurance Co.*, the maker of a note asserted breach of the common law duty of good faith and fair dealing as a counterclaim in a deficiency action. The court rejected the counterclaim on the now familiar ground that such a claim can exist only in cases involving a "special relationship" between the parties. The court held that a lender-borrower relationship did not qualify as a special relationship giving rise to an implied duty of good faith and fair dealing.

B. ACCELERATION AND USURY

A perennial problem facing creditors under Texas law after default by a debtor is the need to give sufficient notice of an intent to accelerate followed by sufficient notice of the actual acceleration if the debtor does not cure the default. While section 1.208 of the Code authorizes the acceleration itself, the notice requirements have been developed by Texas caselaw. A closely related problem is the need for the creditor to avoid possible usury violations by erroneously claiming unearned interest when a debt is accelerated. In *Sumrall v. Navistar Financial Corp.*, the creditor gave proper notice of intent to accelerate and notice of acceleration, but made a major error by asserting an interest claim of more than ten thousand dollars when...
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in fact, no interest was due at all.18 The debtor sued for wrongful repossession and usury. The court upheld an award of mental anguish damages and attorney's fees rendered in favor of the debtor on the claim for wrongful repossession and remanded the case for calculation of additional damages for the usury violation.19

In contrast to Sumrall, where the interest claim was both clearly erroneous and clearly substantial, the court refused to find a usury violation in HSAM, Inc. v. Gatter.20 In Gatter, the error consisted of providing an early payoff quote to the debtor that included a late charge of seventeen dollars and ninety-five cents when the late charge was not actually due until five days later.21 The court calculated that the interest overcharge for this five day period would have amounted to slightly more than two cents.22 The court also noted that the payoff quote had been requested following an offer made to the debtors for "free legal services" in a letter from an attorney directed to owners of manufactured homes in Bexar County.23 The jury found that the payoff quote had been requested for the purpose of creating a cause of action.24 Based on the small amount of the interest overcharge and the circumstances surrounding the request for the payoff quote, the court applied the doctrine of de minimis non curat lex to hold that the creditor was not liable for a usury violation.25

In transactions not governed by the Texas Credit Code, a creditor may require a prepayment penalty from the debtor in the event of acceleration or prepayment.26 In Affiliated Capital Corp. v. Commercial Federal Bank,27 the court held that a prepayment penalty based on the amount of time by which the initial loan was shortened was not a charge for unearned interest.28 According to the court, the prepayment penalty was not usurious because of a savings clause in the note disclaiming any intent to charge usurious interest and the spreading doctrine, which allows a one-time charge to be spread over the life of a loan to determine if the rate exceeds the maximum rate permitted by law.29 Summary judgment was upheld in favor of

18. No interest was due for two reasons. First, the creditor erroneously calculated that the debtor owed $149,398.38 more than was actually due. Second, the "contract between the parties contained no provision for interest charges." 818 S.W.2d at 559.
19. Id. at 560.
20. 814 S.W.2d 887 (Tex. App.—San Antonio 1991, writ dism'd by agr.).
21. Id. at 892.
22. Id.
23. Id. at 888-89.
24. Id. at 889.
25. Id. at 892.
27. 834 S.W.2d 521 (Tex. App.—Austin 1992, n.w.h.).
28. Id. at 525.
29. Id. at 525-26. The court calculated the total interest charged under the loan, including the prepayment penalty, to be $3,559,119.19. At the highest lawful rate, the creditor could have charged up to $4,200,350.82. Thus, under the spreading doctrine, the amount charged did not exceed the lawful rate. Id. at 524 n. 4.
Another usury issue of considerable importance decided during the Survey period was whether a demand for prejudgment interest contained only in a pleading constitutes a charge of usurious interest. This issue first arose in Moore v. Sabine National Bank, where the Austin court of appeals held that a charge of usurious interest could be found when a bank claimed excessive interest in its notice of intention to repossess, in its original petition, and in its sequestration affidavit. Subsequent cases interpreted Moore to hold that simply filing a pleading claiming excessive interest amounted to a charge of usurious interest.

During the Survey period, the Texas Supreme Court affirmed the decision of the Dallas court of appeals in George A. Fuller Co. v. Carpet Services, Inc. that a demand for prejudgment interest asserted only in a pleading did not amount to a charge of usurious interest. The court reached this conclusion on the theory that a pleading is addressed to the court rather than to the debtor and that a demand for excessive interest directed to the court does not amount to a demand on the debtor. The court also disapproved Hagar v. Williams to the extent of its holding that usury could be found if a creditor unilaterally placed an interest charge on an account in its internal records, even if this charge was never communicated to the debtor. The net result in Carpet Services is that an unlawful charge of usurious prejudgment interest does not occur until the creditor communicates a claim to the debtor for such interest in some form other than a demand in a pleading.

C. IMPLIED CONTRACT TO PAY INTEREST

In Tubelite v. Risica & Sons, Inc., a supplier of fabricated construction materials entered into a contract with a subcontractor to supply materials for a construction project. The original contract did not contain a provision for interest. The supplier thereafter sent a notice to the subcontractor that interest on late payments would be charged at the rate of one and one-half percent per month. The subcontractor never objected to this notice, but never paid any of the late charges claimed by the supplier in its invoice statements for overdue amounts. When the supplier sued for payment of the outstanding balance, the subcontractor counterclaimed for usury violations

31. 527 S.W.2d 209 (Tex. Civ. App.—Austin 1975, writ ref'd n.r.e.).
32. Id. at 211.
34. 823 S.W.2d 603 (Tex. 1992).
35. Id. at 605.
36. 593 S.W.2d 783 (Tex. Civ. App.—Amarillo 1979, no writ).
37. Carpet Svcs., Inc., 823 S.W.2d at 605.
38. 819 S.W.2d 801 (Tex. 1991).
based on the invoices assessing interest at the rate of eighteen percent.\textsuperscript{39} The supplier argued that a course of dealing between the parties created an implied agreement to pay interest.\textsuperscript{40} The supreme court held that the subcontractor neither expressly nor impliedly assented to the payment of interest and that the unilateral charging of interest by the supplier amounted to usury.\textsuperscript{41} The court also noted that the failure of the subcontractor to formally object to the addition of the late charge was not evidence that would support a finding of implied modification of the original contract.\textsuperscript{42}

II. SALES OF GOODS

A. Statute of Frauds

The basic premise of section 2.201 of the Code is that a contract for the sale of goods at a price of more than five hundred dollars must be in writing and signed by the party against whom enforcement is sought.\textsuperscript{43} While the writing can be rudimentary, there must be at least some writing that reflects the existence of a contract.\textsuperscript{44} An important exception to this rule is the "merchants' exception."\textsuperscript{45} Under this exception, when a contract for the sale of goods is between merchants, the statute of frauds is satisfied if one party sends a confirmation of the contract to the other party and the other party has reason to know the contents of the writing, and makes no objection to the confirmation within ten days. In such a case the sender of the confirmation can enforce the contract against the recipient despite the lack of a writing signed by the recipient. For this exception to apply, however, the writing must be in confirmation of an existing contract. Thus, in \textit{Baker

\textsuperscript{39} Id. at 802.

\textsuperscript{40} Id. at 803. The standards for determining if a course of dealing results in a contract modification are found in \textit{Tex. Bus. & Com. Code Ann. §§ 1.205 & 2.208} (Tex. UCC) (Vernon 1968),

\textsuperscript{41} Id. at 805.

\textsuperscript{42} Id.

\textsuperscript{43} Tex. Bus. & Com. Code Ann. § 2.201(a) (Tex. UCC) (Vernon 1968) provides: Except as otherwise provided in this section a contract for the sale of goods for the price of $500 or more is not enforceable by way of action or defense 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 or by his authorized agent or broker. A writing is not insufficient because it omits or incorrectly states a term agreed upon but the contract is not enforceable under this paragraph beyond the quantity of goods shown in such writing. Id.

\textsuperscript{44} See the second sentence of \textit{Tex. Bus. & Com. Code Ann. § 2.201(a)} (Tex. UCC) (Vernon 1968) quoted supra note 43.

\textsuperscript{45} \textit{Tex. Bus. & Com. Code Ann. § 2.201(a)} (Tex. UCC) (Vernon 1968) begins with the statement, "Except as otherwise provided in this section." The merchants' exception is one such circumstance where the section otherwise provides. \textit{Tex. Bus. & Com. Code Ann. § 2.201(b)} (Tex. UCC) (Vernon 1968). The other exceptions in the section are: (1) specially manufactured goods; (2) admission in pleadings, testimony or otherwise in court that a contract exists; and (3) goods for which payment has been made and accepted or which have been received and accepted. An important exception to section 2.201 created by caselaw is for promissory estoppel. This exception is applicable if the promisor promises to sign a written agreement and then fails to sign under circumstances where the promisee changes its position in reliance on the promise to sign. \textit{Adams v. Petrade Int'l, Inc.}, 754 S.W.2d 696 (Tex. App.—Houston [1st Dist.] 1988, writ denied).
Hughes, Inc. v. Schwarz,\textsuperscript{46} the court held that an offer contained in a letter could not operate as a confirmation of a contract that had not yet been formed.\textsuperscript{47} The court also held that a letter from the offeree merely acknowledged receipt of the offer, and did not amount to either an acceptance of the offer or to a confirmation of the contract.\textsuperscript{48} Because no writing existed to satisfy the statute of frauds requirement, the court held the alleged oral contract to be unenforceable under section 2.201 of the Code.\textsuperscript{49}

\textbf{B. ADDITIONAL TERMS CONTAINED IN AN ACCEPTANCE}

Section 2.207 of the Code abandons the common law mirror image rule and permits a contract to be formed even if an acceptance contains terms in addition to those contained in the offer.\textsuperscript{50} The offeree can prevent a communication containing additional terms from operating as an acceptance by expressly conditioning the acceptance on assent to the additional terms.\textsuperscript{51} In Westech Engineering, Inc. v. Clearwater Constructors, Inc.,\textsuperscript{52} a subcontractor submitted a bid to a general contractor, who was bidding on a wastewater treatment plant project, and offered to supply some of the equipment for the project. The general contractor used this bid in preparing its own bid submission and was subsequently awarded the project. A few weeks later, the general contractor sent a letter of intent to contract to the subcontractor, followed a month later with an unsigned purchase order form containing typed-in details of equipment specifications and contract requirements. The purchase order contained some additional terms and some different terms than those contained in the subcontractor's bid proposal. The subcontractor signed and returned this form several weeks later along with a letter listing several items of difference from the bid proposal. The general contractor signed the purchase order two months later and returned a copy to the subcontractor.\textsuperscript{53}

Faced with this exchange of correspondence extending over several months, the court concluded that the parties formed a contract and treated the additional terms and different terms in the purchase order as proposals for addition to the contract.\textsuperscript{54} The court noted that these proposals become part of a contract under section 2.207 unless (1) the offer limits acceptance to its exact terms, or (2) the proposals materially alter the original offer, or

\textsuperscript{46} 833 S.W.2d 292 (Tex. App.—Houston [14th Dist.] 1992, writ denied).
\textsuperscript{47} Id. at 295.
\textsuperscript{48} Id.
\textsuperscript{49} Id.
\textsuperscript{50} TEX. BUS. & COM. CODE ANN. § 2.207(a) (TEX. UCC) (Vernon 1968).
\textsuperscript{51} Id.
\textsuperscript{52} 835 S.W.2d 190 (Tex. App.—Austin 1992, n.w.h.).
\textsuperscript{53} The court summarizes the series of correspondence in a convenient tabular form in its opinion. Id. at 197-98.
\textsuperscript{54} Id. at 199. Although not mentioned by the court, further support for its finding that the parties had formed a contract, despite the difficulty of determining exactly when the contract formation occurred, could be found in TEX. BUS. & COM. CODE ANN. § 2.204(b) (Tex. UCC) (Vernon 1968) which provides, “An agreement sufficient to constitute a contract for sale may be found even though the moment of its making is undetermined.”
(3) the offeree objects to the proposals. Applying these rules to the case in hand, the court held that the subcontractor assented to all of the proposals contained in the purchase order except for those listed as items of difference in the subcontractor's letter that was returned with the purchase order.

The court then reviewed the bid proposal, purchase order form, and the subcontractor's letter that accompanied the returned form to determine which terms became part of the contract between the parties. To assist in this analysis, the court applied a rule of construction giving more weight to the typed-in terms than to the preprinted terms. Under this analysis, the subcontractor was responsible for providing equipment that would pass inspection by the engineering firm representing the city in overseeing the wastewater treatment plant project. When some of the equipment furnished by the subcontractor failed to obtain approval by the engineering firm, the subcontractor was, therefore, liable for the general contractor's cover costs incurred in purchasing substitute equipment from other suppliers.

C. Tender of Payment

Although Article 2 of the Code is directly applicable only to the sale of goods, many of its provisions influenced the drafting of the Restatement (Second) of Contracts and, through the Restatement, these provisions now represent a source of authority in the general law of contracts. A good example of this catalytic effect is TSB Exco, Inc. v. E.N. Smith, III Energy Corp., where a lessee under an oil and gas lease tendered a check as payment under a lease extension clause instead of tendering cash. The lessors did not cash the checks and, when the lease expired, they returned the checks to the lessee. The lessors then executed a new lease with another party. The lessee claimed that its tender of a check effectively extended the lease and that the court should declare the new lease invalid. The lessors argued that the terms of the lease called for "payment" of a designated amount and that this term was equivalent to a demand for cash rather than a check. Terming the "modern and better rule" to be that found in section 249 of the Restatement (Second) of Contracts, the court noted the genesis of the Restatement rule was section 2-511(b) of the Code. As contained in

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56. Id.
58. 835 S.W.2d at 204.
60. 818 S.W.2d 417 (Tex. App.—Texarkana 1991, no writ).
61. Id. at 420.
62. Id. Tex. Bus. & Com. Code Ann. § 2.511(b) (Tex. UCC) (Vernon 1968) provides: "Tender of payment is sufficient when made by any means or in any manner current in the ordinary course of business unless the seller demands payment in legal tender and gives any extension of time reasonably necessary to procure it."
the Restatement, tender of payment by check is permitted in any contract unless the agreement otherwise provides or unless the obligee demands payment by legal tender and permits a reasonable time for the obligor to obtain cash. The court specifically adopted section 249 of the Restatement as the rule applicable to contracts calling for the payment of money. Applying this rule, the court rendered judgment in favor of the lessee because: (1) the lease only called for "payment" and did not specify cash as the exclusive means of payment; and (2) the lessors waited until after expiration of the lease before notifying the lessee that its tender by check was rejected (thus not providing a reasonable time for the lessee to obtain cash).

D. REJECTION OF GOODS TO BE DELIVERED IN INSTALLMENTS

In Superior Derrick Services v. Anderson, four workover rig masts used in the oil and gas industry were to be delivered in four installments at the rate of one mast per installment. The buyer discovered various defects with each of the first three masts, but the seller either cured these defects by making repairs or by deducting an allowance from the purchase price to permit the buyer to make the necessary repairs. The buyer canceled the contract before delivery of the fourth mast. In an action by the seller for the unpaid purchase price of all four masts, the court applied section 2.612 of the Code governing contracts for goods to be delivered in installments. In such a contract the buyer can reject an individual installment if a non-conformity substantially impairs the value of that installment and cannot be cured. A cure can take the form of an allowance against the price. Cancellation of an installment contract can take place only if the non-conformity of one or more installments substantially impairs the value of the whole contract. The court held that the defects in the installments could be cured and did not substantially impair the value of the whole contract. The court rendered judgment in favor of the seller on its claim for the first three masts. As to the fourth mast, however, the court noted that the seller had chosen to maintain the action as a suit on a sworn account. In such an action the seller must prove that the goods have been delivered or that title has passed to the buyer. Because the seller never delivered the fourth mast and because title did not pass to the buyer, the court denied recovery of the price for this fourth mast. The court rejected the seller's argument that an action on a sworn account was equivalent to a breach of contract action.

63. 818 S.W.2d at 421.
64. Id. at 423.
65. 831 S.W.2d 868 (Tex. App.—Houston [14th Dist.] 1992, writ denied).
67. 831 S.W.2d at 872.
68. Id. at 876.
69. Id. at 873.
70. Id. at 876.
71. Id. at 873.
E. Warranty Claims in a Consumer Context

Much of the litigation involving the sale of goods in recent years has involved breach of warranty claims. Because of the interaction in Texas between the Code, the common law of warranty, and the Deceptive Trade Practices Act (DTPA), warranty claims asserted only under Article 2 have become rare in any case where the plaintiff can meet the definition of "consumer" as contained in the DTPA.\(^{72}\) Cases reported during this Survey period were no exception.

In *Johnson Roofing, Inc. v. Staas Plumbing Co., Inc.*,\(^{73}\) the plaintiff sued for negligent installation of a roof, for breach of an express warranty against defects in workmanship and materials, and for breach of an implied warranty of good and workmanlike performance under the DTPA. The court held that, while there was sufficient evidence to support a jury finding that neither the express nor the implied warranty had been breached, there was also sufficient evidence to support a finding that the defendant was eighty percent negligent in the installation of the roof.\(^{74}\) The court remanded the case with instructions to enter a judgment in favor of the plaintiff based on the jury findings.\(^{75}\) The interesting aspect to this case is that the trial court had entered a judgment notwithstanding the verdict based on a breach of warranty under the DTPA and had included recovery of the plaintiff's attorney's fees as part of the judgment. The defendant was the party seeking entry of a judgment against it for negligence to avoid the larger damage award under the DTPA and to avoid the recovery of attorney's fees by the plaintiff.\(^{76}\)

In *Selig v. BMW of North American, Inc.*,\(^{77}\) and in *Lujan v. Tampo Manufacturing Co.*,\(^{78}\) the plaintiffs were also unable to show a breach of warranty. In both cases the plaintiffs failed to effectively rebut expert testimony showing there were no defects in the products involved and summary judgments were entered against the plaintiffs. In *Selig* the court also upheld a decision by the trial court that the suit was groundless and brought in bad faith and affirmed recovery of costs and attorneys' fees in favor of the defendant.\(^{79}\) In *Lujan* the court not only held that the defendant did not breach an implied warranty, but further held that the plaintiff, who had been injured by the

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\(^{72}\) The Texas Deceptive Trade Practices Act appears as *Tex. Bus. & Com. Code Ann.* §§ 17.41-.63 (Vernon 1987 & Supp. 1993). A "consumer" is defined in the DTPA as, "an individual, partnership, corporation, this state, or a subdivision or agency of this state who seeks or acquires by purchase or lease, any goods or services, except that the term does not include a business consumer that has assets of $25 million or more, or that is owned or controlled by a corporation or entity with assets of $25 million or more." This definition is much broader than the more common definition of a consumer as a person who purchases goods for personal, family or household purposes. *See, e.g.*, *Tex. Bus. & Com. Code Ann.* sec. 9.109(a) (Tex. UCC) (Vernon 1991).

\(^{73}\) 832 S.W.2d 783 (Tex. App.—Waco 1992, n.w.h.).

\(^{74}\) *Id.* at 789-90.

\(^{75}\) *Id.* at 791.

\(^{76}\) *Id.*

\(^{77}\) 832 S.W.2d 95 (Tex. App.—Houston [14th Dist.] 1992, n.w.h.).

\(^{78}\) 825 S.W.2d 505 (Tex. App.—El Paso 1992, n.w.h.).

\(^{79}\) *Selig*, 832 S.W.2d at 104.
product in question, was only a bystander who was not in privity with either the manufacturer or with the buyer so as to have standing to assert a breach of express warranty claim.80 Associated negligence and strict liability claims were found to have been waived in part and negated in part by the failure to raise a negligent design claim on appeal and by the failure to rebut the expert testimony regarding design of the product.81

Whether a business breached a warranty was also the subject of dispute in Sears, Roebuck and Co. v. Nichols.82 In Sears, the plaintiff asserted a DTPA claim based on an alleged breach of the Melody Home Manufacturing Co. v. Barnes83 implied warranty of good and workmanlike repair rather than breach of an express warranty. The court held that the Melody Home warranty did not cover a repair transaction where a knowledgeable consumer was fully advised of the need for making certain repairs to a lawnmower and of the consequences of failing to make the repairs.84 Despite having this information and despite having specific knowledge about the repair and servicing of the mower in question, the consumer told the defendant service provider not to make the recommended repairs.85

Characterizing the case as one raising a novel issue under Texas law, the court held that the defendant had met its duty under Melody Home by performing the authorized work in a good and workmanlike manner and by giving accurate and complete advice about the need for additional repairs.86 The court noted that it would be a “bizarre result” to hold a service provider liable for failing to make repairs after a customer has specifically instructed that the repairs not be made.87

The Melody Home warranty of good and workmanlike repair also figured in a DTPA claim brought in Milt Ferguson Motor Co. v. Zeretzke.88 In this case the court found misrepresentation of the quality of an automobile as well as breach of the Melody Home implied warranty.89 The misrepresentation claim was based on representations made by the manufacturer in its advertising and other sales literature and by statements made by the sales personnel about the high quality of the car.90 The court held that the representations contained in the literature and the statements made by the sales-

80. Lujan, 825 S.W.2d at 511.
81. Id. at 510.
82. 819 S.W.2d 900 (Tex. App.—Houston [14th Dist.] 1991, writ denied).
83. 741 S.W.2d 349 (Tex. 1987). In this very significant opinion, the Texas Supreme Court announced two very important rules affecting Texas warranty law: (1) there is a warranty of good and workmanlike repair in every contract involving the repair or modification of tangible goods or property; and (2) this warranty cannot be waived or disclaimed. Id. at 354-55. Some of the ramifications of Melody Home are discussed in John Krahmer, Commercial Transactions, Annual Survey of Texas Law, 42 Sw. L.J. 217, 222-25 (1988).
84. Nichols, 819 S.W.2d at 904-05.
85. Id. at 905.
86. Id.
87. Id. at 906.
88. 827 S.W.2d 349 (Tex. App.—San Antonio 1991, no writ).
89. Id. at 355-56.
90. Id. at 354.
person were misrepresentations of material facts. The court also held that the dealer breached the Melody Home implied warranty by repeatedly failing to repair defects in the vehicle. The inadequacy of the repair efforts was rather dramatically demonstrated when an independent mechanic found cracks in the engine block that seemed to be of manufacturer's origin. The dealer had either never discovered the cracks or, if discovered, had never reported them to the plaintiffs. The court upheld an award of damages based on both the misrepresentation and the breach of warranty. The majority allowed recovery for mental anguish as part of the damages suffered by the plaintiff, but a strong dissenting opinion argued that mental anguish damages are recoverable in DTPA actions only if the defendant "knowingly" misrepresents the quality of the vehicle or the quality of the repairs. The dissent would have disallowed the award of damages for mental anguish because the trial court had made no finding that the defendants' acts were committed "knowingly."

In Bowe v. General Motors Corp., a manufacturer and an automobile dealer were also sued for breach of the warranty of good and workmanlike repair. The dealer urged, as one of its principal defenses, that it had disclaimed all warranties by a direct and separate disclosure. The court held that the disclaimer was effective only as to warranties associated with the sale of the vehicle, but did not purport to disclaim any warranties associated with repair services. The court noted, moreover, that the supreme court had expressly held in Melody Homes that the implied warranty of good and workmanlike repair could not be waived or disclaimed. Summary judgment in favor of the defendants was reversed and the case remanded for trial on the merits.

An interesting question as to the ownership of a breach of warranty claim arose in Dowler v. Delta Investment House, Inc. Following the purchase of a mobile home under a security agreement, various defects appeared and the sellers ineffectually attempted to repair the defects. The purchasers subsequently defaulted on their payments for the mobile home and the home was repossessed and resold. The defendants argued that the plaintiffs no longer had standing to assert a breach of warranty claim based on defective repairs because the foreclosure effectively transferred the cause of action to the purchaser at the foreclosure sale. The court rejected this argument, holding that the foreclosure transferred only the title to the mobile home, but did not
transfer any cause of action the purchasers may have had against the sellers that arose prior to foreclosure.\textsuperscript{104}

Another interesting claim that defies ordinary commercial transaction classification was asserted in \textit{Dan Boone Mitsubishi, Inc. v. Ebrom.}\textsuperscript{105} In that case the plaintiff alleged that a car dealer failed to deliver the certificate of title for an automobile the plaintiff had purchased. Despite repeated attempts by the buyer to obtain the title and repeated assurances by the dealer that the title would be forthcoming, more than a year later, the buyer still had not received a title for the vehicle.\textsuperscript{106} In an action brought under the DTPA, the court allowed recovery for mental anguish damages alone without proof of any other actual damage.\textsuperscript{107} In addition, because the action had been brought under the DTPA, and because the trial court found the misrepresentations about delivery of the title had been committed knowingly, the court allowed trebling of the mental anguish damages for a total recovery of ninety thousand dollars plus attorney’s fees.\textsuperscript{108}

\textbf{F. WARRANTY CLAIMS IN A COMMERCIAL CONTEXT}

\textit{GT & MC, Inc. v. Texas City Refining, Inc.,}\textsuperscript{109} was one of the few cases during the Survey period involving a non-DTPA warranty claim. A contract of sale for an oil storage tank contained express warranties covering design, materials and workmanship. The contract also contained a limitation of remedy for defects in materials or workmanship, but did not mention any limitation for design defects.\textsuperscript{110} The court held that an express warranty that the Everfloat tank roof was designed to withstand wind loads of one-hundred-twenty-five miles per hour and rainfall of up to ten inches in a twenty-four hour period was breached when the Everfloat roof failed to live up to its name and sank under a wind and rain load of less than the warranted limits.\textsuperscript{111} The court further held that, because the contract did not limit remedies for design defects, damages were recoverable for loss of use of the tank along with damages for the loss of oil from the tank.\textsuperscript{112}

In \textit{Transoil Ltd. v. Belcher Oil Co.}\textsuperscript{113} and \textit{HCI Chemicals v. Henkel

\begin{footnotesize}
\begin{enumerate}
\item 104. \textit{Id.} at 128-29.
\item 105. 830 S.W.2d 334 (Tex. App.—Houston [14th Dist.] 1992, writ denied).
\item 106. \textit{Id.} at 335.
\item 107. \textit{Id.} at 337. In this non-jury trial, the record was replete with evidence that the dealer did not have title to the vehicle when it was sold and that it consistently promised to deliver the title even when it became apparent that it was unable to do so. \textit{Id.}
\item 108. \textit{Id.} The evidence in support of damages for mental anguish included fear that the plaintiff might be stopped by the police and face a charge of motor vehicle theft since the title was in someone else’s name, the need to drive the vehicle with an illegally obtained license sticker because a legal sticker could not be obtained without the title, and possible embarrassment and loss of reputation a police charge might cause because the plaintiff had to use the car to transport customers in her business.
\item 109. 822 S.W.2d 252 (Tex. App.—Houston [1st Dist.] 1991, writ denied).
\item 110. \textbf{TEX. BUS. \\ & COM. CODE ANN.} § 2.719 (Tex. UCC) (Vernon 1968) permits the contractual limitation of remedies for breach of warranty.
\item 111. 822 S.W.2d at 256-57.
\item 112. \textit{Id.}
\item 113. 950 F.2d 1115 (5th Cir. 1992).
\end{enumerate}
\end{footnotesize}
the disputes centered on the proper method of calculating damages for the delivery of nonconforming goods. In both cases the court first had to resolve the question of whether the buyers had effectively rejected the goods so the court could determine the proper Article 2 provisions to calculate damages. In Transoil the court resolved this question on a procedural ground by finding that the buyer never requested jury instructions based on a theory of rejection or revocation of acceptance of the goods. By failing to properly raise this issue at trial, the court found that the buyer waived its right to seek damages based on a theory of non-acceptance and was limited to seeking damages on a breach of warranty theory. In HCI Chemicals the court concluded that the buyer did not give the seller timely notice of rejection and, failing such notice, the buyer was deemed to have accepted the goods and was limited to recovery for breach of warranty.

On the damage calculation issue, the two cases present an interesting contrast. In HCI Chemicals, the court held the buyer was entitled to recover the difference between the value the goods would have had if they had conformed to the contract and the value of the nonconforming goods as accepted. Because the seller had introduced no evidence to the contrary, the court concluded that the contract price could be used as the value of conforming goods and the price received for the goods on resale could be used as the value of the nonconforming goods. The buyer was entitled to recover the difference between these two amounts and was also entitled to recover consequential damages for lost profits when it was unable to fulfill a contract with one of its own customers because of the nonconformity. Incidental damages for shipping and storage were also allowed. In contrast to the result in HCI Chemicals, the court in Transoil refused to use a “contract price less resale price” differential. While the contract price of $19.40 per barrel for the oil to be delivered under the contract closely matched the spot market price of $20.00 per barrel at the time of delivery, the court found that the resale price of $11.00 per barrel that the buyer received some two months later bore little or no resemblance to the value of the oil at the time of delivery because of a collapse in the market between January and March of 1986. The only evidence in the record as to the value of the nonconformity was the spot market price of $20.00 per barrel at the time of delivery.
forming oil showed that it could have been sold in some markets at a price higher than the contract price. Because there was no evidence of damage, the buyer could not recover for breach of warranty.

III. COMMERCIAL PAPER

A. FORM OF NEGOTIABLE INSTRUMENTS

Amberboy v. Societe de Banque Privee was by far the most important commercial paper decision handed down during the Survey period. In Amberboy the Texas Supreme Court held that a note requiring interest to be paid at a “bank’s published prime rate” could satisfy the “sum certain” requirement of section 3.104 of the Code to qualify as a negotiable instrument. It is important to note that this opinion was issued in response to a certified question from the federal Fifth Circuit Court of Appeals and is necessarily limited in scope. The court was careful to point out that “published prime rate” means only “those rates which are public, either known to or readily ascertainable by any interested person.” The court also noted that it did not require any particular method of publication so long as the goal of commercial certainty was achieved by making the rate readily available to the public.

The court reached its conclusion in Amberboy in three ways: (1) by reference to the stated policy of the Code to “simplify, clarify and modernize the law governing commercial transactions;” (2) by a comprehensive review of prior cases that had considered the issue of the negotiability of variable rate notes; and (3) by noting the widespread legislative adoption of amendments to Article 3 to make variable rate notes negotiable, including

124. Id. at 1122.
125. Id.
126. 831 S.W.2d 793 (Tex. 1992).
127. TEX. BUS. & COM. CODE ANN. § 3.104(a)(2) (Tex. UCC) (Vernon 1968) states the requirement that a writing must contain a promise or order to pay a “sum certain” to qualify as a negotiable instrument under Chapter 3 of the Code. TEX. BUS. & COM. CODE ANN. § 3.106 (Tex. UCC) (Vernon 1968), further defines this requirement with examples of instruments that contain a “sum certain” even though the amount to be paid is not stated as a single dollar figure. The examples include instruments payable in installments, instruments payable with interest at a stated rate, instruments payable with a stated discount or addition, instruments payable with allowance for exchange, and instruments that include costs of collection, including attorney’s fees.
128. Amberboy, 831 S.W.2d at 797-98.
129. Id.
130. Id.
131. TEX. BUS. & COM. CODE ANN. § 1.102 (Tex. UCC) (Vernon 1968) states the rules of construction, purposes and policies of the Code.
132. 831 S.W.2d at 794-95. The authorities cited in Amberboy included numerous cases decided in other jurisdictions as well as earlier decisions by lower Texas courts. There is no need to repeat those citations here, but it should be noted that the court expressly disapproved the holdings in Lexington Insurance Co. v. Gray, 775 S.W.2d 679 (Tex. App.—Austin 1989, writ denied) and Dillard v. NCNB Texas National Bank, 815 S.W.2d 356 (Tex. App.—Austin 1991, no writ) to the extent those decisions conflicted with the holding in Amberboy. 831 S.W.2d at 797.
133. Amberboy, 831 S.W.2d at 795-96. The court cited statutes from nineteen states that had legislatively changed the definition of “sum certain” to include variable rate notes.
the revision of Article 3 by the National Conference of Commissioners on Uniform State Laws in the 1990 Official Text of the Uniform Commercial Code. Based on its review of these authorities, the court decided that the purposes of the Code could best be served by adopting a rule of commercial certainty rather than a rule of mathematical certainty.

While the decision in Amberboy clearly states the standards for determining what constitutes a "bank's published prime rate," it does leave open the question of the negotiability of notes that call for the calculation of interest based on references to other types of rates, such as a consumer price index or treasury bill rate. While these are "published" rates readily ascertainable by interested persons, they are neither prime rates nor are they rates established by a bank. These questions remain after Amberboy.

Another formal requirement for negotiability is that an instrument must be signed by the maker or drawer. As with other contracts, a signature may be made by an agent or other representative. If the signature is made in proper representative form, the agent will not be personally liable for payment of the instrument. In Mestco Distributing, Inc. v. Stamps the court held that four promissory notes in a series of seven notes had been signed in proper representative form to absolve the agent from personal liability.

As to the other three notes, although the signatures did not clearly disclose representative capacity, the agent was able to avoid personal liability by establishing that the immediate parties to the transaction understood that the agent was signing on behalf of a corporate principal.

B. PROOF OF CLAIMS AND DEFENSES

In Jones v. RTC the court held that an affidavit of a bank officer submitted contemporaneously with the bank's motion for summary judgment on a promissory note was sufficient to prove that the bank was the owner and holder of the note in question, that maker signed the note and was in

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134. Id. at 795-96. The 1990 Official Text of the Uniform Commercial Code includes modification of the "sum certain" requirement as only one part of a comprehensive revision of Article 3.

135. 831 S.W.2d at 796. The court cited Tanenbaum v. Agri-Capital, Inc., 885 F.2d 464 (8th Cir. 1989), with approval for this view. A dissenting opinion by four of the justices argued that the majority went beyond construction of the Code and had simply created a new rule of law. The dissent also contended that even under the rationale of the majority, the notes in question did not refer to a readily ascertainable prime rate.

136. The 1990 revision of the Official Text of the Uniform Commercial Code permits reference to any external rate. If the amount of interest cannot be determined from the description in the instrument, interest is payable at the judgment rate. U.C.C. § 3-112(b) (1990). In Pruitt v. Franklin Federal Bancorp, 824 S.W.2d 798 (Tex. App.—Austin 1992, n.w.h.), the notes based the interest rate on the yield of United States Treasury securities. Pruitt is discussed in the text, infra, at note 145.


138. Id. § 3.403(a) (Tex. UCC) (Vernon 1968).

139. Id. §§ 3.401(a) & .403(b) (Tex. UCC) (Vernon 1968).

140. 824 S.W.2d 678 (Tex. App.—Houston [14th Dist.] 1992, n.w.h.).

141. Id. at 680.

142. Id. at 681.

143. 828 S.W.2d 821 (Tex. App.—Fort Worth 1992, writ denied).
default, and that a sum certain was due and owing on the instrument. The court rejected arguments that the affidavit was insufficient because the affiant had not been employed by the bank when the transaction first originated and that the affidavit had not been physically attached to the motion for summary judgment.

In Pruitt v. Franklin Federal Bancorp the bank fared less well in supporting its motion for summary judgment. The affidavit submitted in support of this motion neither stated the amount of interest due on the notes nor the information necessary to calculate the amount of interest. The court held that the bank had failed to present sufficient evidence to uphold a summary judgment in its favor.

A holder who does not qualify as a holder in due course takes an instrument subject to all defenses of any party which would be available on a simple contract. One such defense that might be urged against a holder who does not qualify as a holder in due course is fraud in the inducement. Under Texas law, however, this defense requires the maker to show that he or she was induced to sign the note by trickery, artifice, or device and by a promise that the maker would not be liable for payment. In three cases decided during the Survey period, the makers failed to overcome the parol evidence rule, and the court excluded evidence of collateral agreements alleged to relieve the makers of liability. In a fourth case, the maker was allowed to introduce parol evidence that he was liable for only one-half the face amount of the note based on a prior course of dealing between the parties. The court held that the collateral agreement could be shown in this case because it was based on a routine practice of the parties and not on a single representation that the maker would only be liable for one-half the face amount of the note. A dissenting opinion argued that the course of dealing only amounted to a representation that the maker would be partially relieved of liability and there was no extrinsic evidence of trickery, artifice, or device to satisfy the other branch of the fraud in the inducement test.

In Rea v. Sunbelt Savings the maker generally alleged payment as an
affirmative defense to a motion for summary judgment, but did not file an
account distinctly stating the nature of the payment and did not plainly and
particularly describe the payment in his plea so as to give notice of the char-
acter of the payment. The court held that the failure to adequately plead
the defense of payment precluded the maker from introducing evidence on
this issue.

IV. BANK DEPOSITS AND COLLECTIONS

A. SETOFF

In *FDIC v. Projects American Corp.* a corporation set up a pension fund
trust plan for its officers and employees in a bank that subsequently failed.
The initial funding for the pension trust was obtained by a loan from the
bank to the corporation. After the FDIC took over the bank, the corporation
sued for a declaratory judgment to setoff the amount still owing on the loan
against the uninsured amount of the pension fund trust account. In essence,
the corporation wanted to satisfy its liability on the note with some of the
pension funds not covered by FDIC insurance since the trust might never
recover from the assets of the failed bank. The court held that, while the
 corporation was liable for the debt on the loan transaction, it was not the
owner of the pension plan account as that account was held as a trust ac-
to account for the employees as beneficiaries of the trust and the trustee was, in
effect, a separate creditor of the failed bank. Because the plan was estab-
lished as a trust account, it could not be held liable for corporate debts, thus,
there was no mutuality of obligation between the corporate debt owing on
the loan and the debt of the FDIC owing to the trust account. The court
held that the setoff claim by the corporation should not be allowed.

In *Bandy v. First State Bank* a bank setoff funds it held in a checking
account and eight certificates of deposit against debts owed to it by the insol-
vent estate of a deceased depositor. The bank exercised the setoff without
following the claims procedure described in the Texas Probate Code. In a
lengthy opinion, the Texas Supreme Court reviewed the common law right
of setoff and the treatment of this right under the Texas Probate Code. The
court concluded that the Probate Code did not abolish the common law
right of setoff and, in fact, specifically recognized it. The court further

155. These requirements for pleading an affirmative defense of payment appear in Tex. R.
Civ. P. 95 (Vernon 1979).
156. 822 S.W.2d at 372.
158. Id. at 773.
159. Id. at 774. The court rested part of its decision on D'Oench, Duhme & Co. v. FDIC,
315 U.S. 447 (1942) and on 12 U.S.C. § 1823(e) (1988) to rebut the argument that there was an
unwritten understanding between the trustees and the bank that the pension funds could be
used as security for repayment of the corporate loan.
160. 835 S.W.2d 609 (Tex. 1992).
against estates.
162. 835 S.W.2d at 617-21.
163. Id. at 618 (quoting Tex. Prob. Code Ann. § 449 (Vernon 1980)).
held that the right of setoff could be exercised by a bank, whether the estate was solvent or insolvent, because all creditors would be paid in full by asserting a claim against the bank if it were later determined that the estate was solvent when the setoff was exercised. The court ruled that the bank had not converted the funds in all but one of the certificate of deposit accounts by exercising its right of setoff, but, because of an incomplete record, the court remanded the case for determination of the right of setoff as to one certificate of deposit account and of the checking accounts.

B. Garnishment

In *Bank One, Texas, N.A. v. Sunbelt Savings, F.S.B.*, a writ of garnishment was issued on a personal judgment obtained against the sole shareholder of a closely-held corporation. The writ named only the individual as the judgment debtor and did not name the corporation as the owner of any funds of the individual although there was evidence that the individual had commingled his funds with funds held in a corporate bank account. In a per curiam opinion, the Texas Supreme Court held that a bank is entitled to rely on its deposit agreements to determine the ownership of funds held on deposit in an account. Because the bank had no accounts in the name of the individual, and because the writ did not name the corporation as a judgment debtor, the bank was not required to freeze the corporate account and was not liable for a subsequent withdrawal of funds from that account. The court pointed out that the judgment creditor should have sought a writ of garnishment in the name of the nominal owner of the funds so the court could exercise its judicial function of determining true ownership of the funds in the corporate account. The court properly noted that failing to name the correct person in the writ improperly shifted the burden of determining ownership of the funds to the garnishee.

In *Esquivel v. Watson* the drawer of a check sued the payee for malicious prosecution and abuse of process following the dismissal of criminal charges against the drawer that had been filed by the payee. The drawer obtained a favorable jury verdict against the payee, but the trial court entered a judgment notwithstanding the verdict in favor of the payee and this judgment was upheld by the court of appeals. The principal ground for this holding was an admission by the drawer that she knew the account had insufficient funds when she wrote the check. On further appeal to the Texas Supreme Court, the court held that this admission was not fatal to the malicious prosecution and abuse of process claims because this was not an admis-
sion that she had issued an insufficient funds check. This distinction was important because the drawer believed that by the time she delivered the check to the payee her employer had deposited sufficient funds in her account to cover the check. The court held there was some evidence from which the jury could conclude that the criminal complaint against the drawer was not supported by probable cause and the basis for upholding a judgment notwithstanding the verdict could not rest on the ground that she had failed to prove this element of her malicious prosecution and abuse of process claims.

V. LETTERS OF CREDIT

It is elementary commercial law that a letter of credit creates an independent obligation on the part of the issuer to honor documents drawn under the credit if they conform to the terms of the credit. It is equally elementary that an injunction against honor will not issue unless there is such fraud, forgery or other defect in the transaction as will vitiate the entire transaction. In Goldome Credit Corp. v. University Square Apartments, the court carefully reviewed the standards for injunctive relief in letter of credit transactions and held that these standards were met in a peculiar fact situation when there was a substantial likelihood that the beneficiary of the letter of credit no longer existed and that an attempted presentment under the credit was being made by an unknown party. The named beneficiary was a holding company which apparently ceased to exist when a subsidiary savings bank it owned was declared insolvent and placed into receivership. The disappearance of the beneficiary had been admitted by counsel in an earlier, unrelated bankruptcy proceeding and the non-existence of the beneficiary became part of an order in the bankruptcy court. Because payment by the issuer to a beneficiary who no longer existed might constitute an erroneous payment leaving the customer liable both to the issuer and to the actual beneficiary on the underlying contract, the court held that a temporary injunction was proper until the identity of the party making the presentment could be determined.

VI. INVESTMENT SECURITIES

In Beta Drilling, Inc. v. Durkee the court held that an oral agreement to sell stock was unenforceable for failure to comply with the statute of frauds

171. Id. at 590. TEX. PENAL CODE § 32.41 (Vernon 1974) makes it an offense to issue an insufficient funds check.
172. Id. at 591.
174. Id.
175. 828 S.W.2d 505 (Tex. App.—Amarillo 1992, n.w.h.).
176. Id. at 507-08.
177. The bankruptcy order and its surrounding circumstances are described in a footnote to the opinion. Id. at 508 n.4.
178. Id. at 511.
179. 821 S.W.2d 739 (Tex. App.—Houston [14th Dist.] 1992, writ denied).
While it was clear there was no written agreement for the sale of the securities, the court had to consider whether the statute of frauds covered a sale that was to be made in exchange partly for services and partly in money. On this issue, the court concluded that the transaction did constitute a sale of securities. The court also had to consider whether the transaction met one of the statutory or common law exceptions to the statute of frauds. The only relevant statutory exception was that of partial performance. The court held that performance of services could not qualify as a partial payment for the stock under the statutory language and, since none of the money had been paid as part of the price of the stock, this exception did not apply. The court also held that the common law promissory estoppel exception to the statute of frauds was inapplicable because there was no promise by the defendant to sign an already prepared writing or to sign a document whose wording had been agreed upon. The court noted that a promise to prepare a written contract at some time in the future was not sufficient to invoke the promissory estoppel exception.

The statute of frauds requirement was also the subject of continuing litigation during the Survey period in Gannon v. Baker. In this latest chapter, the court of appeals held (1) that an alleged agreement to "level" the ownership of stock in a corporation was too indefinite to enforce; and (2) that the transfer of the stock was to be made in exchange for consideration in the form of the transfer of ownership in another company and was unenforceable, therefore, because there was no written agreement stating the quantity and price for the stock. A dissenting opinion disagreed on the issue of indefiniteness, but did not address the statute of frauds issue.

VII. SECURED TRANSACTIONS

A. CREATION AND PERFECTION OF SECURITY INTERESTS

A continuing problem under Article 9 is whether an agreement that purports to be a lease of personal property is a true lease or merely a disguised security interest. The Texas legislature partially addressed this issue in the 1989 legislative session by adopting the revision of the official text of Section 1-201(37) proposed by the American Law Institute and the National Conference of Commissioners on Uniform State Laws. This revision is much more definitive than the earlier text in describing the tests to be used in deciding if a transaction creates a lease or a security interest. At this writing, the legis-

181. 821 S.W.2d at 740.
182. Id. at 741.
183. Id.
184. Id.
185. 830 S.W.2d 706 (Tex. App.—Houston [1st Dist.] 1992, writ denied). The case has been the subject of a previous court of appeals decision reported at 807 S.W.2d 793 (Tex. App.—Houston [1st Dist.] 1991), aff'd in part and rev'd in part, 818 S.W.2d 754 (Tex. 1991).
186. 830 S.W.2d at 710.
187. Id.
188. Id. at 711.
lature has not yet adopted Article 2A of the Code governing the substantive
details of lease transactions, but the adoption of the revised Section 1-
201(37) helps to clarify the line of distinction between leases and security
interests.

One of the special problems with leases as contrasted to security interests
is that, if a lease is a true lease, there is no requirement that any public filing
be made to alert third parties to the existence of the lessor's interest in the
property. If the transaction is classified as a security interest, a financing
statement must generally be filed to perfect the security interest and gain
protection against third parties. Even under the revision of Section 1-
201(37), the classification of a lease as a true lease instead of a security inter-
est is not always entirely clear, and a lessor is well-advised to take advantage
of the permissive filing permitted by Section 9.408 of the Code.\textsuperscript{189}

In \textit{Pierson v. GFH Financial Services Corp.},\textsuperscript{190} the purchaser of a farm
removed and sold irrigation equipment that had been on the property at the
time of purchase. GFH Financial Services subsequently sued the purchaser
of the farm, alleging that GFH had leased the equipment to a previous
owner of the farm and, as the lessor, was entitled to recover the equipment
or its value on a theory of conversion. The defendant argued that he ob-
tained lawful possession of the equipment when he purchased the farm be-
cause the lease was actually a secured transaction and GFH had not
perfected its security interest by properly filing a financing statement. The
court held that the lease was a true lease and, as such, did not require a filing
to protect the lease interest against the defendant as a purchaser of the
farm.\textsuperscript{191} Since no perfection was required to perfect the lease interest, the
court affirmed a judgment in favor of the lessor for the value of the equip-
ment. Curiously, the court noted that GFH had filed a fixture filing, appar-
tently in the belief that the irrigation equipment was installed as a fixture, but
the court did not seem to regard this filing as a proper permissive filing
under Section 9.408 of the Code.

In \textit{Austin Area Teachers Federal Credit Union v. First City Bank},\textsuperscript{192} a de-
positor assigned her rights to a certificate of deposit issued by a credit union
to a bank as security for a loan made to her son. The credit union acknowl-
edged the assignment by written notation and returned the assignment form
to the bank. After the son defaulted, the credit union permitted the depositor
to withdraw the funds from the certificate of deposit account. The bank then
sued the credit union for the funds that had been represented by the certifi-
cate of deposit. The court held that the assignment document, despite some
missing terms and some defects in form, was adequate when considered as a
whole, to create a valid assignment of the certificate of deposit in favor of the
bank to secure the son's indebtedness.\textsuperscript{193} The court also held that the secur-

\textsuperscript{189} TEX. BUS. & COM. CODE ANN. § 9.408 (Tex. UCC) (Vernon 1991).
\textsuperscript{190} 829 S.W.2d 311 (Tex. App.–Austin 1992, n.w.h.).
\textsuperscript{191} Id. at 316.
\textsuperscript{192} 825 S.W.2d 795 (Tex. App. –Austin 1992, writ denied).
\textsuperscript{193} Id.
ity interest did not require perfection to be enforceable against the debtor and against the credit union when neither party was a competing creditor for the funds. The acknowledgment of the assignment by an employee of the credit union who had at least apparent, if not actual, authority to make the acknowledgment was sufficient to bind the credit union by contract to hold the funds for the bank instead of releasing them to the depositor. The bank also attempted to use the assignment as the basis for a claim against additional funds held by the depositor in other accounts at the credit union. On this issue the court held that the language of the assignment was limited to the funds represented by the certificate of deposit and allowed recovery only for those funds.

In Continental Credit Corp. v. Wolfe City National Bank, a secured creditor filed a series of financing statements covering a debtor's inventory and accounts receivable in the form “Judy Summers d/b/a Greenville Pawn Shop.” Continental Credit Corporation subsequently purchased all of the assets of the business, including the inventory and accounts receivable. In a conversion action by the secured creditor against the purchaser, the court held that the financing statements were ineffective to perfect the security interest where the actual name of the debtor was “Pawn Partners, Inc.” The court reasoned that a third party searching the record for “Pawn Partners, Inc.” would not have found a financing statement indexed under the name of “Summers.” The court held the financing statements were “seriously misleading” and the purchaser therefore took free of the unperfected security interest.

A similar dispute between a secured creditor and the purchaser of a business arose in Chase Manhattan Bank v. J & L General Contractors, Inc. In this case the secured creditor filed a financing statement under the correct name of the debtor, but described the collateral as “[a]ll fixed assets including all equipment and fixtures listed.” Unfortunately for the creditor, no list was attached to the financing statement. The court held that the Code placed the duty to properly describe collateral on the secured party and the attempted description by reference to a non-existent list made the financing statement insufficient to perfect a security interest in the equipment and fixes.

194. Id. Perfection of the security interest may have been difficult, if not impossible, in this case as it appears that no physical certificate had actually been issued by the credit union. If an actual certificate had been issued, perfection could have been accomplished by possession. See Tex. Bus. & Com. Code Ann. §§ 9.304 & .305 (Tex. UCC) (Vernon 1991). Without the existence of an actual certificate, Article 9 does not provide a means for perfection of a security interest in a deposit account. See Tex. Bus. & Com. Code Ann. §§ 9.104(12) & .105(a)(5) (Tex. UCC) (Vernon 1991).

195. Austin Area Teachers, 825 S.W.2d at 800.

196. Id.


198. Id. at 691.

199. Id.


201. 832 S.W.2d 204 (Tex. App.—Beaumont 1992, n.w.h.).

202. Id. at 208.
Judgment was rendered for the purchaser on the conversion claim.

B. PRIORITIES

During the Survey period priority disputes between a secured lender and state taxing authorities arose in Wichita Falls v. ITT Commercial Financial Corp. and County of Burleson v. General Electric Capital Corp. In Wichita Falls the court held that a statutory tax lien that attached to the automobile inventory of a car dealer for unpaid property taxes did not give the taxing authority a valid claim for conversion against a secured party who repossessed the inventory following default by the taxpayer/debtor. The court reasoned that, despite the priority granted to the tax lien by section 32.05 of the Texas Tax Code, the taxing authority could not maintain an action for conversion under Texas law unless it could prove ownership, possession, or a right to possession. Because the taxing authority had not pursued the tax warrant procedure or foreclosure of the tax lien before the repossession took place, the court held it had no standing to maintain a conversion action. The court also assessed costs of appeal against the taxing authority, but, on this point, it was reversed by the Texas Supreme Court.

In County of Burleson, the taxing authority seized and sold a mobile home in which a creditor had properly perfected a security interest, but a jury found that the authority had not properly followed the statutory procedure for conducting a summary tax sale by failing to adequately attempt to identify and locate persons other than the owner who might have an interest in the property. Based on this failure to strictly comply with the statutory procedure, the court held the taxing authority liable to the secured party in an action for conversion of the mobile home.

In Tropicana Energy Co., Inc. v. Texas Ethanol, Inc., the priority dispute was between the holder of a perfected purchase money security interest and a landlord in possession of the collateral following default and termination of the debtor's lease. The court held that under section 9.306 of the

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203. Id. at 211.
204. Id. The court also discussed the question of whether the purchaser of the business qualified for protection as a buyer not in the ordinary course of business under Tex. Bus. & Com. Code Ann. § 9.301(a)(3) (Tex. UCC) (Vernon 1991) because the purchaser was a prior owner who reacquired the business by purchase in a foreclosure sale. The court held the purchaser met all of the requirements necessary to qualify as a buyer not in the ordinary course of business.
205. 827 S.W.2d 6 (Tex. App.—Fort Worth), rev'd in part, 835 S.W.2d 65 (Tex. 1992).
206. 831 S.W.2d 54 (Tex. App.—Houston [14th Dist.] 1992, writ denied).
207. Tex. Tax Code Ann. § 32.05(b) (Vernon 1992) provides, "A tax lien provided by this chapter takes priority over the claim of any creditor of a person whose property is encumbered by the lien and over the claim of any holder of a lien on property encumbered by the tax lien, whether or not the debt or lien existed before attachment of the tax lien."
208. 827 S.W.2d at 10.
210. 831 S.W.2d at 61. The court found that the failure to locate other persons with an interest in the property amounted to a violation of state and federal unlawful taking and due process constitutional requirements.
211. 832 S.W.2d 711 (Tex. App.—Fort Worth 1992, n.w.h.).
Code, the perfected security interest continued in the collateral and that the landlord's claim was subject to the security interest.\textsuperscript{212} The court affirmed a judgment granting possession of the collateral to the secured party for the purpose of foreclosing its perfected security interest.\textsuperscript{213}

C. Default

In \textit{Hall v. RTC}\textsuperscript{214} a loan was secured by stock and promissory notes owned by the debtor. The security agreement allowed the secured party to require additional collateral if it determined that the original collateral became unsatisfactory or if it declined in value. The agreement also permitted the debtor to substitute debenture notes for the collateral notes originally furnished under the security agreement. The debtor eventually offered to substitute debenture notes for the original collateral notes and also requested return of the stock. At about the same time, the lender became concerned about the deteriorating financial condition of the makers of the collateral notes and about the declining value of the stock.\textsuperscript{215} Faced with what it viewed as a decrease in the value of the property securing repayment, the lender refused the proffered substitution and also asked for additional collateral. Following this communication from the lender, the debtor stopped making payments on the loan. The issue before the court was whether the secured party or the debtor had breached the loan agreement. Based on the terms of the security agreement, the court concluded that the secured party was not required to assent to the proposed substitution of the debenture note when the debtor made return of the stock part of the proposal.\textsuperscript{216} The court also held that the secured party acted properly under the terms of the security agreement when it requested additional collateral. Noting that the secured party acted in accordance with the terms of the security agreement, the court rejected an argument by the debtor that the secured party violated a duty of good faith and fair dealing by refusing the proposed substitution and by demanding additional collateral.\textsuperscript{217} The court also rejected an argument that the debtor had substantially complied with the collateral substitution clause, noting there was no authority for applying the doctrine of "substantial compliance" to loan agreements.\textsuperscript{218}

\textsuperscript{212} \textit{Id.} at 713. \textit{Tex. Bus. \\& Com. Code Ann.} § 9.306(b) (Tex. UCC)(Vernon 1991) provides that, unless otherwise provided by Chapter 9 itself or unless otherwise agreed, a security interest continues in collateral notwithstanding sale, exchange or other disposition. There was no provision in Chapter 9 of the Code and there was no agreement that would terminate the security interest upon termination of the lease.

\textsuperscript{213} \textit{Tropicana Energy, Inc.}, 832 S.W.2d at 712.

\textsuperscript{214} 958 F.2d 75 (5th Cir. 1992).

\textsuperscript{215} \textit{Id.} at 77.

\textsuperscript{216} \textit{Id.} at 78.

\textsuperscript{217} \textit{Id.} at 79. The court pointed out that under Texas law such a duty is imposed only if there is a "special relationship" between the parties and that Texas courts had explicitly refused to extend a duty of good faith and fair dealing to lender-borrower relationships.

\textsuperscript{218} \textit{Id.}
D. REPOSSESSION

In the very significant decision of \textit{Mbank-El Paso v. Sanchez},\textsuperscript{219} the Texas Supreme Court held that Section 9.503 of the Code imposes a nondelegable duty on a secured party to avoid a breach of the peace in the repossession of collateral. Because this duty was held to be nondelegable, the secured party could not avoid liability for a breach of the peace committed by an independent contractor during the course of a repossession. The court held the recovery against the secured party could include both actual and punitive damages. The case was remanded for determination of the amount of damages.\textsuperscript{220}

In \textit{Winkle Chevy-Olds-Pontiac, Inc. v. Condon},\textsuperscript{221} a lessor repossessed a leased van containing the lessee's construction tools even though the lessee was current in making all payments under the lease. Under the terms of the lease, the lessor was required to give notice of default before effecting repossession.\textsuperscript{222} The lessor alleged that notice was given by certified mail; the lessee testified that such notice was never received. Despite several attempts by the lessee to contact the lessor after the repossession, the lessor refused to talk to the lessee and, for several days, the lessee believed the van had been stolen. The construction tools in the van were eventually returned, but only after the lessee had lost two construction jobs because he did not have the tools to complete the work. In an action brought by the lessee for breach of contract, conversion, and deceptive trade practices, the jury found for the lessee on all issues, including a claim for lost profits and a claim for mental anguish.\textsuperscript{223} Except for an amount of seven hundred dollars that represented a double recovery for loss of use, the court upheld all of the damage claims, including punitive damages for conversion and treble damages under the DTPA.\textsuperscript{224}

E. DISPOSITION OF COLLATERAL

It is a basic tenet of Article 9 that, unless collateral is perishable or threatens to decline rapidly in value, a debtor must receive notice of a proposed sale of collateral and the sale must be conducted in a commercially reason-

\textsuperscript{219} 836 S.W.2d 151 (Tex. 1992).
\textsuperscript{220} The wrongful acts committed by the independent contractor in \textit{Mbank-El Paso v. Sanchez}, 836 S.W.2d 151 (Tex. 1992), were egregious. In \textit{Sanchez}, while the debtor was mowing her lawn, two repossession company employees hooked a tow truck to the car parked in her driveway. When asked to explain their actions, the employees ignored the debtor. Attempting to halt the repossession until the police or her husband arrived, the debtor locked herself in the car. After towing the car into the street, the men gave her notice of the repossession and asked her to leave the vehicle or spend the weekend in the repossession yard with a Doberman pinscher. When she refused, she was taken on a high speed ride to a fenced and locked storage yard patrolled by an unchained guard dog. She was rescued later by her husband and the police.
\textsuperscript{221} 830 S.W.2d 740 (Tex. App.—Corpus Christi 1992, writ dism'd).
\textsuperscript{222} Id. at 743.
\textsuperscript{223} Id. at 742.
\textsuperscript{224} Id. at 747. The Court held that the damages for loss of use was duplicative of the damages awarded for the loss of value of the leased property. Id. at 746.
able manner.\textsuperscript{225} If notice is not properly given or if the sale is not properly conducted, the secured party is barred from recovering a deficiency judgment.\textsuperscript{226} In \textit{FDIC v. Payne,}\textsuperscript{227} a guarantor had pledged a diamond ring to a bank as collateral to secure a loan made to the principal debtor. After default by the debtor, the bank sold the ring without giving notice of the sale to the guarantor. In an action to collect a deficiency, the FDIC (which succeeded to the rights of the bank after the bank failed) argued that the guarantor had waived the right to receive notice of the sale of collateral prior to default as part of the guaranty agreement. The court rejected this argument, citing numerous cases to the effect that Texas law has consistently held that guarantors may not waive the right to notice of sale prior to default.\textsuperscript{228} Because notice of the sale had not been given, the FDIC was barred from recovering a deficiency.\textsuperscript{229}

In \textit{Knights of Columbus Credit Union v. Stock,}\textsuperscript{230} a notice of sale was sent to the debtor, but the notice failed to specify whether the disposition of the collateral was to be by public or private sale and did not contain a statement of the time and place for a public sale or the time after which a private sale would occur. The court held the defective notice barred recovery of a deficiency judgment.\textsuperscript{231} A more difficult question, however, was the effect on the deficiency claim of a cross-collateralization clause which had the effect of using the same collateral to secure three different loans. The court reasoned that the rule barring recovery of a deficiency should operate to discourage a creditor from failing to dispose of collateral in a commercially reasonable manner, but should not operate as a windfall to a defaulting debtor by absolving the debtor from liability for all loans owed to the creditor.\textsuperscript{232} Because the notice evidenced an intent to foreclose on the collateral for only one of the three loans, the court concluded that barring recovery only on that loan would sufficiently penalize the creditor for improper disposition without giving the debtor an undeserved windfall.\textsuperscript{233} The court applied the same reasoning to calculate the penalty recovery permitted to a consumer

\begin{footnotes}\textsuperscript{225} \textit{TEX. BUS. & COM. CODE ANN. \S 9.504(c) (Tex. UCC) (Vernon 1991).}
\textsuperscript{226} See, e.g., \textit{ITT Comm. Fin. Corp. v. Riehn, 796 S.W.2d 248 (Tex. App.-Dallas 1990, no writ) (creditor who elects to sell collateral must both give notice and sell in commercially reasonable manner to recover deficiency; failure to meet either requirement makes sale an act of conversion); Chase Comm. Corp. v. Datapoint Corp., 774 S.W.2d 359 (Tex. App.--Dallas 1989, no writ) (failure to sell collateral in commercially reasonable manner bars deficiency); Carroll v. General Elec. Credit Corp., 734 S.W.2d 153 (Tex. App.--Houston [1st Dist.] 1987, no writ) (failure to give notice of sale of collateral bars deficiency).}
\textsuperscript{227} 973 F.2d 403 (5th Cir. 1992).
\textsuperscript{228} \textit{Id. at 409.}
\textsuperscript{229} \textit{Id. at 411. The court also held that the FDIC had failed to meet the burden of pleading that the sale had been conducted in a commercially reasonable manner in violation of the rules governing pleading and proof in deficiency actions as announced in \textit{Greathouse v. Charter Nat'l Bank}, 35 Tex. Sup. Ct. J. 1017 (July 1, 1992). The failure of the FDIC to meet this pleading requirement was noted as an independent ground for denying recovery of a deficiency. \textit{Greathouse} is discussed in this article at note 238, infra.}
\textsuperscript{230} 814 S.W.2d 427 (Tex. App.--Dallas 1991, writ denied).
\textsuperscript{231} \textit{Id. at 431.}
\textsuperscript{232} \textit{Id. at 432.}
\textsuperscript{233} \textit{Id.}\end{footnotes}
debtor under section 9.507 of the Code and allowed the penalty for only the single loan under which the improper disposition was made. The court allowed the creditor to retain its security interests on the other two loans.

In *Thomas v. Price*, the debtor received several notices regarding the sale of his interest in a partnership that had been pledged as collateral for a loan and advising him of his right to redeem his interest by payment of the balance of the indebtedness. The debtor did not redeem and the sale of the partnership interest eventually occurred. In an action for the wrongful disposition of the collateral, the debtor did not contest the validity of the notice or the commercial reasonableness of the sale, but argued that the purchaser of the partnership interest did not act in good faith because the purchaser was, in effect, an "insider" who wanted to divest the debtor of his interest in the partnership. The court held that so long as the sale was conducted properly under section 9.504 of the Code, the issue of whether the purchaser acted in good faith was irrelevant. According to the court, the only relevant inquiry was whether the purchaser paid value for the collateral and the debtor never contended that the purchaser failed to pay sufficient consideration for the collateral.

### F. Pleading and Proving Commercially Reasonable Disposition

After years of uncertainty about the proper allocation of the burden of pleading and proving commercial reasonableness, the Texas Supreme Court has resolved the issue in the important case of *Greathouse v. Charter Nat'l Bank-Southwest*. After candidly noting that the Uniform Commercial Code had become anything but "uniform" on the issue of pleading and proving commercial reasonableness, both among the Texas courts of appeals and among the several states, the court announced the following rules for application in deficiency suits: (1) the creditor in a deficiency suit has the burden of initially pleading that a disposition of collateral was commercially reasonable; (2) this pleading may be made either specifically or generally; (3) if the allegations are specific, the creditor automatically assumes the burden of proving the allegations; and (4) if the pleading is general, the creditor is required to prove the disposition was commercially reasonable only if the debtor specifically denies such disposition in the answer. In a footnote, the court stated that these rules were applicable only in deficiency actions and that it was expressing no opinion on the allocation of the burdens of

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235. 975 F.2d 231 (5th Cir. 1992).

236. *Id.* at 239.

237. *Id.* at 238.

238. 814 S.W.2d at 432-33.

239. 35 Tex. Sup. Ct. J. 1017 (July 1, 1992). The opinion collects the conflicting prior decisions by the courts of appeals as to the allocation of the burden of pleading and proving commercial reasonableness.

pleading and proof in an action by a debtor against a creditor for wrongful foreclosure.241 The decision in Greathouse was quickly cited and followed by the federal courts and by the lower Texas courts.242

241. Id.

242. Greathouse was decided on July 1, 1992. By November 1, 1992, it had already been applied in the following reported cases, Thomas v. Price, 975 S.2d 231 (5th Cir. 1992); FDIC v. Payne, 973 F.2d 403 (5th Cir. 1992) and Roquemore v. Nat'l Commerce Bank, 837 S.W.2d 212 (Tex. App.—Texarkana 1992, n.w.h.), as well as being applied in some additional cases not yet released for publication. (The unreported decisions can be found on Lexis and Westlaw.)