



**DELBERT HOSEMAN**  
*Secretary of State*

**2009 BUSINESS REFORM STUDY GROUPS MEETING  
OF THE UNIFORM COMMERCIAL CODE AND DEBTOR CREDITORS LAWS  
STUDY GROUP**

**First Meeting**

Thursday, June 25, 2009  
11:00 A.M.

**Secretary of State's Office  
700 North Street  
Jackson, Mississippi**

**AGENDA**

1. Welcome – Cheryn Baker
2. Introduction of Members and Attendees
3. Remarks by Chairman Jerome Hafter
4. UCC Issues to Cover (See Attachment)
5. Debtor Creditor Issues to Cover
6. Next Steps for Upcoming Meetings
7. Reminder of Upcoming Meetings: Dates and Future Programs
8. Other Business
9. Adjourn 1:00 P.M (or earlier)

**Upcoming Meeting Dates: August 5, August 19, September 9, and September 23**

**Materials for Today's Meeting**

Committee Roster  
Booklet of Materials  
Powerpoint Presentation

## UCC Issues to Consider

1. Whether to adopt New Article 1 Definitions and General Provisions (2001) and non-uniform provisions to retain/uniform provisions to not adopt
2. Whether to adopt Amendments to Articles 3 and 4 (2002) and if so, whether any non-uniform changes need to be made to them
3. Whether to adopt any non-uniform provisions that might give some safe-harbors for foreclosure under Article 9 for what is commercially reasonable, such as Mississippi's non-uniform ten-day period for giving notice for disposition of collateral in consumer transactions in Section 75-9-612(b)
4. Whether to repeal MS Article 2 provision which prohibits sellers from disclaiming implied warranties of merchantability and fitness for a particular purpose
5. Whether to make any revisions to Section 75-9-502(a)(1) requirement that a financing statement must provide the name of the debtor in light of *Peoples Bank v. Bryant Cattle Company*, 504 F. 3d 549 (5<sup>th</sup> Cir. 2007)
6. Whether to make any revisions to Section 75-2-107(3) in light of *Feliciano Bank & Trust v. Manuel & Sessions, L.L.C.*, 943 So. 2d 736 (Miss. Ct. App. 2006)
7. Determine if there is a policy basis for having different statutes of limitation for negotiable and non-negotiable notes. If not, consider recommending changes to eliminate this distinction. Article 3's six-year statute of limitations in Section 75-3-118(a) applies to negotiable notes, the general three-year statute of limitations applies to non-negotiable notes.
8. Begin discussions of adoption of Revised Articles 2 and 2A (2003)

## Debtor Creditor Issues to Consider

1. Whether to change law to permit subcontractors to place a lien on the property owner's real property if the contractor doesn't pay the subcontractor the amount owed/due. Or to provide some other kind of protection to subcontractors.
2. Adoption of statutes for insolvency workouts for small creditors outside the bankruptcy laws

## UCC AND DEBTOR-CREDITOR LAWS STUDY GROUP

Prefix	First	Last	Company	City/St/Zip
1 Mr.	Nick	Anderson	Trustmark National Bank	Jackson, MS 39205
2 Mr.	John	Ash	J Thomas Ash Attorney at Law	Jackson, MS 39236-3219
3 Mr.	Richard	Barnes	Ole Miss Law School	University, MS 38677
4 Mr.	Russell	Bennett	Mississippi Bankers Association	Jackson, MS 39205
5 Ms.	Betty	Benton	Trustmark National Bank	Jackson, MS 39205
6 Mr.	Phillip	Buffington	MacNeill & Buffington, P.A.	Jackson, Mississippi 39236
7 Mr.	Robert	Byrd	Byrd & Wiser	Biloxi, MS 39533-1939
8 Mr.	Paul	Carrubba	Adams and Reese	Jackson, MS 39225-3276
9 Mr.	Rod	Clement	Brunini Grantham Grower & Hewes	Jackson, MS 39205-0119
10 Mr.	Robert	Davidson	MS State Senate	Jackson, MS 39211-6531
11 Mr.	Jason	Dean	Mississippi Economic Council	Jackson, MS 39225-3276
12 Mr.	Kenneth	Downs	Staple Cotton Cooperative Assoc	Greenwood, MS 38935-0547
13 Mr.	Craig	Geno	Harris Jernigan & Geno	Ridgeland, MS 39158-3380
14 Mr.	Jerome	Haftter	Phelps Dunbar	Jackson, MS 39225-3066
15 Ms.	Gina	Jacobs	Watkins Ludlam Winter & Stennis	Jackson, MS 39205-0427
16 Mr.	Jerry	Johnson	Baker Donelson Bearman Caldwell & Berko	Jackson, MS 39236-4167
17 Mr.	Owen	Lalor	On2Locate Inc	Ridgeland, MS 39157-2600
18 Mr.	Edward	Lawler	McKay Lawler	Ridgeland, MS 39158
19 Mr.	John	Laws	Laws Construction Company	Jackson, MS 39236
20 Mr.	William	Leech	Copeland Cook Taylor & Bush	Ridgeland, MS 39158-6020
21 Mr.	Matthew	McLaughlin	Balch & Bingham LLP	Jackson, Mississippi 39201
22 Mr.	Devere	McLennan	Ward Mechanical Equipment Inc.	Jackson, MS 39296
23 Rep.	Sam	Mims	MS House of Representatives	McComb, MS 39648
24 Mr.	Guy	Mitchell	Mitchell McNutt & Sams	Tupelo, MS 38802-7120
25 Mr.	William	Neely	MS State Senate	Jackson, MS 39215-1018
26 Mr.	Chuck	Nicholson	Community Bank	Brandon, MS
27 Mr.	Douglas	Noble	Phelps Dunbar	Jackson, MS 39225-3066
28 Rep.	Steve	Palazzo	MS House of Representatives	Biloxi, MS 39535
29 Mr.	Robert	Pooley	South Central Heating and Plumbing	Jackson, MS 39216
30 Mr.	Clarence "Jimbo"	Richardson	MS House of Representatives	Jackson, MS 39215-1018
31 Mr.	Tom	Riley	Mississippi Secretary of State	Jackson, MS 39205
32 Rep.	Margaret	Rogers	MS House of Representatives	New Albany, MS 38652
33 Mr.	Gordon	Sanford	BellSouth Telecommunications	Jackson, MS 39201-2135
34 Mr.	Curtis	Smith	Aultman Tyner Ruffin & Swetman Ltd	Hattiesburg, MS 39403-0750
35 Ms.	Adrian	Smith	Hancock Bank	Gulfport, MS 39501
36 Ms.	Aileen	Thomas	Watkins Ludlam Winter & Stennis	Jackson, MS 39205-0427
37 Mr.	John	Turner	Baskin McCarroll McCaskill & Campbell	Southaven, MS 38671-0190
38 Mr.	Terre	Vardaman	Attorney at Law	Brandon, MS 39043-1326
39 Sen.	Giles	Ward	MS Senate	Louisville, MS 39339
40 Mr.	Edward	Wilmesherr	Butler Snow O'Mara Stevens & Cannada	Jackson, MS 39225-2567
41 Mr.	Richard	Wise	H C Bailey Co	Ridgeland, MS 39157-1507
42 Mr.	Ralph	Young	Glover Young Walton & Simmons	Meridian, MS 39302-5514

**Co-Chairman - Jerome Haftter**

**Co-Chairman - Craig Geno**

**Co-Chairman - Ed Lawler**

**Co-Chairman - Rod Clement**



DELBERT HOSEMANN  
*Secretary of State*

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# Comparison of Revised Uniform Commercial Code Article 1 with Current Mississippi Statutes

Prepared by Mississippi Secretary of State, Policy & Research Division

June 2009

This table compares the most current version of Article 1 of the Uniform Commercial Code (UCC) with Mississippi’s current adoption of Article 1, which is based on a mix of different revisions of the UCC. The first column lists the most recent Article 1 code sections by section, while the middle column lists the corresponding section (if any) of Mississippi’s adoption of Article 1. The third column summarizes official comments made by the UCC’s drafters which explain the changes between the former and current versions.

<u>UCC – Part 1</u>	<u>MS – Part 1</u>	<u>Changes from prior version of Article 1</u>
<p>§ 75-1-101. Short Titles.</p> <p>(a) This [Act] may be cited as the Uniform Commercial Code.</p> <p>(b) This article may be cited as Uniform Commercial Code – General Provisions.</p>	<p>§ 75-1-101. Short Title.</p> <p>Chapters 1 through 10 of this title shall be known and may be cited as Uniform Commercial Code.</p>	<p>Subsection (b) is new, added in order to make the structure of Article 1 parallel with that of the other articles of the Uniform Commercial Code.</p>
<p>§ 75-1-102. Scope of Article.</p> <p>This article applies to a transaction to the extent that it is governed by another article of the Uniform Commercial Code.</p>	<p>No corresponding provision.</p>	<p><b>New section</b></p> <p>This section was revised to make it clearer that the provisions in Article 1 apply to any transaction governed by one of the other articles of the Uniform Commercial Code.</p>
<p>§ 75-1-103. Construction of Uniform Commercial Code to Promote its Purposes and Policies; Applicability of Supplemental Principles of Law.</p> <p>(a) The Uniform Commercial Code must be liberally construed and applied to promote its underlying purposes and policies, which are:</p> <p>(1) to simplify, clarify, and modernize the law governing commercial transactions;</p> <p>(2) to permit the continued expansion of commercial practices through custom, usage, and agreement of the parties; and</p> <p>(3) to make uniform the law among the various jurisdictions.</p> <p>(b) Unless displaced by the particular provisions of the Uniform Commercial Code, the principles of law and equity, including the law merchant and the law relative to capacity to contract, principal and agent, estoppel, fraud, misrepresentation, duress, coercion, mistake, bankruptcy, and other validating or invalidating cause supplement its provisions.</p>	<p>§ 75-1-102. Purposes; Rules of Construction; Variation by Agreement.</p> <p>(1) This code shall be liberally construed and applied to promote its underlying purposes and policies.</p> <p>(2) Underlying purposes and policies of this code are</p> <p>(a) to simplify, clarify and modernize the law governing commercial transactions;</p> <p>(b) to permit the continued expansion of commercial practices through custom, usage and agreement of the parties;</p> <p>(c) to make uniform the law among the various jurisdictions.</p> <p>§ 75-1-103. Supplementary General Principles of Law Applicable.</p> <p>Unless displaced by the particular provisions of this code, the principles of law and equity, including the law merchant and the law relative to capacity to contract, principal and agent, estoppel, fraud, misrepresentation, duress, coercion, mistake, bankruptcy, or other validating or invalidating cause shall supplement its provisions.</p>	<p>This section combines the previous Sections 1-102 and 1-103. Except for changing the form of reference to the Uniform Commercial Code and minor stylistic changes, the language is the same as in the previous sections. The provisions have been combined in this section to reflect the interrelationship between them.</p>
<p>§ 75-1-104. Construction Against Implied Repeal.</p> <p>The Uniform Commercial Code being a general act intended as a</p>	<p>§ 75-1-104. Construction Against Implicit Repeal.</p> <p>This code being a general act intended as a unified coverage of its subject</p>	<p>Except for changing the form of reference to the Uniform Commercial Code, this section is identical to former Section 1-104.</p>

unified coverage of its subject matter, no part of it shall be deemed to be impliedly repealed by subsequent legislation if such construction can reasonably be avoided.	matter, no part of it shall be deemed to be impliedly repealed by subsequent legislation if such construction can reasonably be avoided.	
<p>§ 75-1-105. Severability.</p> <p>If any provision or clause of the Uniform Commercial Code or its application to any person or circumstance is held invalid, the invalidity does not affect other provisions or applications of the Uniform Commercial Code which can be given effect without the invalid provision or application, and to this end the provisions of the Uniform Commercial Code are severable.</p>	<p>§ 75-1-108. Severability.</p> <p>If any provision or clause of this code or application thereof to any person or circumstances is held invalid, such invalidity shall not affect other provisions or applications of the code which can be given effect without the invalid provision or application, and to this end the provisions of this code are declared to be severable.</p>	Except for changing the form of reference to the Uniform Commercial Code, this section is identical to former Section 1-108.
<p>§ 75-1-106. Use of Singular and Plural; Gender.</p> <p>In the Uniform Commercial Code, unless the statutory context otherwise requires:</p> <p>(1) words in the singular number include the plural, and those in the plural include the singular; and</p> <p>(2) words of any gender also refer to any other gender.</p>	<p>§ 75-1-102. Purposes; Rules of Construction; Variation by Agreement.</p> <p>(5) In this code unless the context otherwise requires</p> <p>(a) words in the singular number include the plural, and in the plural include the singular;</p> <p>(b) words of the masculine gender include the feminine and the neuter, and when the sense so indicates words of the neuter gender may refer to any gender.</p>	Other than minor stylistic changes, this section is identical to former Section 1-102(5).
<p>§ 75-1-107. Section Captions.</p> <p>Section captions are part of the Uniform Commercial Code.</p>	<p>§ 75-1-109. Section Captions.</p> <p>Section captions are parts of this code.</p>	No change.
<p>§ 75-1-108. Relation to Electronic Signatures in Global and National Commerce Act.</p> <p>This article modifies, limits, and supersedes the federal Electronic Signatures in Global and National Commerce Act, 15 U.S.C. Section 7001 et seq., except that nothing in this article modifies, limits, or supersedes Section 7001(c) of that Act or authorizes electronic delivery of any of the notices described in Section 7003(b) of that Act.</p>	No corresponding provision.	<p><b>New section</b></p> <p>Section 102(a) of the federal Electronic Signatures in Global and National Commerce Act allows a state statute to modify, limit, or supersede the provisions of section 101 if certain criteria are met. Article 1 fulfills the first two of those three criteria; this Section fulfills the third criterion listed above.</p>

<u>UCC - Part 2</u>	<u>MS - Part 2</u>	
<p>§ 75-1-201. General Definitions.</p> <p>(a) Unless the context otherwise requires, words or phrases defined in this section, or in the additional definitions contained in other articles of the Uniform Commercial Code that apply to particular articles or parts thereof, have the meanings stated.</p> <p>(b) Subject to definitions contained in other articles of the Uniform Commercial Code that apply to particular articles or parts thereof:</p>	<p>§ 75-1-201. General Definitions.</p> <p>Subject to additional definitions contained in the subsequent chapters of the Uniform Commercial Code which are applicable to specific chapters or Parts thereof, and unless the context otherwise requires, in the Uniform Commercial Code:</p>	<p><b>See attached document discussing changes to individual definitions.</b></p> <p>In order to make it clear that all definitions in the Uniform Commercial Code do not apply if the context otherwise requires, a new subsection (a) to that effect has been added, and the definitions now appear in subsection (b). In other words, the definition applies whenever the defined term is used unless the context in which the defined term is used in the statute indicates that the term was not used in its defined sense.</p> <p>Consider, for example, Sections 3-103(a)(9) (defining “promise,” in relevant part, as “a written undertaking to pay money signed by the person undertaking to pay”) and 3-303(a)(1) (indicating that an instrument is issued or transferred for value if “the instrument is issued or transferred for a promise of performance, to the extent that the promise has been performed”). It is clear from the statutory context of the use of the word “promise” in Section 3-303(a)(1) that the term was not used in the sense of its definition in Section 3-103(a)(9). Thus, the Section 3-103(a)(9) definition should not be used to give meaning to the word “promise” in Section 3-303(a).</p>
<p>§ 75-1-202. Notice; Knowledge.</p> <p>(a) Subject to subsection (f), a person has “notice” of a fact if the person:</p> <p>(1) has actual knowledge of it;</p> <p>(2) has received a notice or notification of it; or</p> <p>(3) from all the facts and circumstances known to the person at the time in question, has reason to know that it exists.</p> <p>(b) “Knowledge” means actual knowledge. “Knows” has a corresponding meaning.</p> <p>(c) “Discover”, “learn”, or words of similar import refer to knowledge rather than to reason to know.</p> <p>(d) A person “notifies” or “gives” a notice or notification to another person by taking such steps as may be reasonably required to inform the other person in ordinary course, whether or not the other person actually comes to know of it.</p> <p>(e) Subject to subsection (f), a person “receives” a notice or notification when:</p> <p>(1) it comes to that person’s attention; or</p> <p>(2) it is duly delivered in a form reasonable under the circumstances at the place of business through which the contract was made or at another location held out by that person as the place for receipt of such communications.</p>	<p>§ 75-1-201. General Definitions.</p> <p>(25) Subject to subsection (27), a person has “notice” of a fact if the person:</p> <p>(A) Has actual knowledge of it;</p> <p>(B) Has received a notice or notification of it; or</p> <p>(C) From all the facts and circumstances known to the person at the time in question, has reason to know that it exists.</p> <p>A person “knows” or has “knowledge” of a fact when the person has actual knowledge of it. “Discover” or “learn” or a word or phrase of similar import refers to knowledge rather than to reason to know. The time and circumstances under which a notice or notification may cease to be effective are not determined by the Uniform Commercial Code.</p>	<p>These provisions are substantive rather than purely definitional. Accordingly, they have been relocated from former Section 1-201 to this section.</p>

<p>(f) Notice, knowledge, or a notice or notification received by an organization is effective for a particular transaction from the time it is brought to the attention of the individual conducting that transaction and, in any event, from the time it would have been brought to the individual's attention if the organization had exercised due diligence. An organization exercises due diligence if it maintains reasonable routines for communicating significant information to the person conducting the transaction and there is reasonable compliance with the routines. Due diligence does not require an individual acting for the organization to communicate information unless the communication is part of the individual's regular duties or the individual has reason to know of the transaction and that the transaction would be materially affected by the information.</p>		
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<p>§ 75-1-203. Lease Distinguished From Security Interest.</p> <p>(a) Whether a transaction in the form of a lease creates a lease or security interest is determined by the facts of each case.</p> <p>(b) A transaction in the form of a lease creates a security interest if the consideration that the lessee is to pay the lessor for the right to possession and use of the goods is an obligation for the term of the lease and is not subject to termination by the lessee, and:</p> <p>(1) the original term of the lease is equal to or greater than the remaining economic life of the goods;</p> <p>(2) the lessee is bound to renew the lease for the remaining economic life of the goods or is bound to become the owner of the goods;</p> <p>(3) the lessee has an option to renew the lease for the remaining economic life of the goods for no additional consideration or for nominal additional consideration upon compliance with the lease agreement; or</p> <p>(4) the lessee has an option to become the owner of the goods for no additional consideration or for nominal additional consideration upon compliance with the lease agreement.</p> <p>(c) A transaction in the form of a lease does not create a security interest merely because:</p> <p>(1) the present value of the consideration the lessee is obligated to pay the lessor for the right to possession and use of the goods is substantially equal to or is greater than the fair market value of the goods at the time the lease is entered into;</p> <p>(2) the lessee assumes risk of loss of the goods;</p> <p>(3) the lessee agrees to pay, with respect to the goods, taxes, insurance, filing, recording, or registration fees, or service or maintenance costs;</p> <p>(4) the lessee has an option to renew the lease or to become the owner of the goods;</p> <p>(5) the lessee has an option to renew the lease for a fixed rent that is equal to or greater than the reasonably predictable fair market rent for the use of the goods for the term of the renewal at the time the option is to be performed; or</p> <p>(6) the lessee has an option to become the owner of the goods for a fixed price that is equal to or greater than the reasonably predictable fair market value of the goods at the time the option is to be performed.</p> <p>(d) Additional consideration is nominal if it is less than the lessee's reasonably predictable cost of performing under the lease agreement if the option is not exercised. Additional consideration is not nominal if:</p> <p>(1) when the option to renew the lease is granted to the lessee, the rent</p>	<p>§ 75-1-201. General Definitions.</p> <p>(37) "Security interest" means an interest in personal property or fixtures which secures payment or performance of an obligation.</p> <p>(A) The term also includes any interest of a consignor and a buyer of accounts, chattel paper, a payment intangible, or a promissory note in a transaction that is subject to Article 9. The special property interest of a buyer of goods on identification of such goods to a contract for sale under Section 75-2-401 is not a "security interest," but a buyer may also acquire "security interest," by complying with Article 9. Except as otherwise provided in Section 75-2-505, the right of a seller or lessor of goods under Article 2 or 2A to retain or acquire possession of the goods is not a "security interest," but a seller or lessor may also acquire a "security interest" by complying with Article 9. The retention or reservation of title by a seller of goods notwithstanding shipment or delivery to the buyer (Section 75-2-401) is limited in effect to a reservation of a security interest.</p> <p>(B) Whether a transaction creates a lease or security interest is determined by the facts of each case; however, a transaction creates a security interest if the consideration the lessee is to pay the lessor for the right to possession and use of the goods is an obligation for the term of the lease not subject to termination by the lessee, and</p> <p>(i) The original term of the lease is equal to or greater than the remaining economic life of the goods,</p> <p>(ii) The lessee is bound to renew the lease for the remaining economic life of the goods or is bound to become the owner of the goods,</p> <p>(iii) The lessee has an option to renew the lease for the remaining economic life of the goods for no additional consideration or nominal additional consideration upon compliance with the lease agreement, or</p> <p>(iv) The lessee has an option to become the owner of the goods for no additional consideration or nominal additional consideration upon compliance with the lease agreement.</p> <p>(C) A transaction does not create a security interest merely because it provides that:</p> <p>(i) The present value of the consideration the lessee is obligated to pay the lessor for the right to possession and use of the goods is substantially equal to or is greater than the fair market value of the goods at the time the lease is entered into,</p> <p>(ii) The lessee assumes risk of loss of the goods, or agrees to pay taxes, insurance, filing, recording, or registration fees, or service or maintenance costs with respect to the goods,</p> <p>(iii) The lessee has an option to renew the lease or to become the owner of the goods,</p> <p>(iv) The lessee has an option to renew the lease for a fixed rent that is equal to or greater than the reasonably predictable fair market rent for the</p>	<p>This section is substantively identical to those portions of former Section 1-201(37) that distinguished "true" leases from security interests, except that the definition of "present value" formerly embedded in Section 1-201(37) has been placed in Section 1-201(28).</p>
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<p>is stated to be the fair market rent for the use of the goods for the term of the renewal determined at the time the option is to be performed; or</p> <p>(2) when the option to become the owner of the goods is granted to the lessee, the price is stated to be the fair market value of the goods determined at the time the option is to be performed.</p> <p>(e) The “remaining economic life of the goods” and “reasonably predictable” fair market rent, fair market value, or cost of performing under the lease agreement must be determined with reference to the facts and circumstances at the time the transaction is entered into.</p>	<p>use of the goods for the term of the renewal at the time the option is to be performed, or</p> <p>(v) The lessee has an option to become the owner of the goods for a fixed price that is equal to or greater than the reasonably predictable fair market value of the goods at the time the option is to be performed.</p> <p>(D) For purposes of this subsection (37):</p> <p>(i) Additional consideration is not nominal if:</p> <ol style="list-style-type: none"> <li>1. When the option to renew the lease is granted to the lessee the rent is stated to be the fair market rent for the use of the goods for the term of the renewal determined at the time the option is to be performed, or</li> <li>2. When the option to become the owner of the goods is granted to the lessee the price is stated to be the fair market value of the goods determined at the time the option is to be performed. Additional consideration is nominal if it is less than the lessee's reasonably predictable cost of performing under the lease agreement if the option is not exercised;</li> </ol> <p>(ii) “Reasonably predictable” and “remaining economic life of the goods” are to be determined with reference to the fact and circumstances at the time the transaction is entered into; and</p> <p>(iii) “Present value” means the amount as of a date certain of one or more sums payable in the future, discounted to the date certain. The discount is determined by the interest rate specified by the parties if the rate is not manifestly unreasonable at the time the transaction is entered into; otherwise, the discount is determined by a commercially reasonable rate that takes into account the facts and circumstances of each case at the time the transaction was entered into.</p>	
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<p>§ 75-1-204. Value.</p> <p>Except as otherwise provided in Articles 3, 4, [and] 5, [and] 6, a person gives value for rights if the person acquires them:</p> <p>(1) in return for a binding commitment to extend credit or for the extension of immediately available credit, whether or not drawn upon and whether or not a charge-back is provided for in the event of difficulties in collection;</p> <p>(2) as security for, or in total or partial satisfaction of, a preexisting claim;</p> <p>(3) by accepting delivery under a preexisting contract for purchase; or</p> <p>(4) in return for any consideration sufficient to support a simple contract.</p>	<p>§ 75-1-201. General Definitions.</p> <p>(44) "Value," except as otherwise provided with respect to negotiable instruments and bank collections (Sections 75-3-303, 75-4-208 and 75-4-209), a person gives "value" for rights if he acquires them:</p> <p>(A) In return for a binding commitment to extend credit or for the extension of immediately available credit whether or not drawn upon and whether or not a charge-back is provided for in the event of difficulties in collection; or</p> <p>(B) As security for or in total or partial satisfaction of a preexisting claim; or</p> <p>(C) By accepting delivery pursuant to a preexisting contract for purchase; or</p> <p>(D) Generally, in return for any consideration sufficient to support a simple contract.</p>	<p>Unchanged from former Section 1-201. These provisions are substantive rather than purely definitional, and accordingly, have been relocated from former Section 1-201 to this section.</p>
<p>§ 75-1-205. Reasonable Time; Seasonableness.</p> <p>(a) Whether a time for taking an action required by the Uniform Commercial Code is reasonable depends on the nature, purpose, and circumstances of the action.</p> <p>(b) An action is taken seasonably if it is taken at or within the time agreed or, if no time is agreed, at or within a reasonable time.</p>	<p>§ 75-1-204. Time; Reasonable Time; "Seasonably."</p> <p>(2) What is a reasonable time for taking any action depends on the nature, purpose and circumstances of such action.</p> <p>(3) An action is taken "seasonably" when it is taken at or within the time agreed or if no time is agreed at or within a reasonable time.</p>	<p>This section is derived from subsections (2) and (3) of former Section 1-204. Subsection (1) of that section is now incorporated in Section 1-302(b).</p>
<p>§ 75-1-206. Presumptions.</p> <p>Whenever the Uniform Commercial Code creates a "presumption" with respect to a fact, or provides that a fact is "presumed," the trier of fact must find the existence of the fact unless and until evidence is introduced that supports a finding of its nonexistence.</p>	<p>§ 75-1-201. General Definitions.</p> <p>(31) "Presumption" or "presumed" means that the trier of fact must find the existence of the fact presumed unless and until evidence is introduced which would support a finding of its nonexistence.</p>	<p>Stylistic changes only.</p>
<p><b>UCC – Part 3</b></p>	<p><b>MS – Part 3</b></p>	
<p>§ 75-1-301. Territorial Applicability; Parties' Power to Choose Applicable Law.</p> <p>(a) Except as otherwise provided in this section, when a transaction bears a reasonable relation to this state and also to another state or nation the parties may agree that the law either of this state or of such other state or nation shall govern their rights and duties.</p> <p>(b) In the absence of an agreement effective under subsection (a), and except as provided in subsection (c), the Uniform Commercial Code applies to transactions bearing an appropriate relation to this state.</p> <p>(c) If one of the following provisions of the Uniform Commercial Code specifies the applicable law, that provision governs and a contrary agreement is effective only to the extent permitted by the law so specified:</p> <p>(1) Section 75-2-402;</p>	<p>§ 75-1-105. Territorial Application of the Code; Parties' Power to Choose Applicable Law.</p> <p>(1) Except as provided hereafter in this section, when a transaction bears a reasonable relation to this state and also to another state or nation the parties may agree that the law either of this state or of such other state or nation shall govern their rights and duties. Failing such agreement, this code applies to transactions bearing an appropriate relation to this state. Provided, however, the law of the State of Mississippi shall always govern the rights and duties of the parties in regard to disclaimers of implied warranties of merchantability or fitness, limitations of remedies for breaches of implied warranties of merchantability or fitness, or the necessity for privity of contract to maintain a civil action for breach of implied warranties of merchantability or fitness notwithstanding any agreement by the parties that the laws of some other state or nation shall govern the rights and duties of the parties.</p> <p>(2) Where one of the following provisions of this code specifies the</p>	<p>While the revised Section 1-301 is substantively identical to the former UCC Section 1-105, it differs greatly from Mississippi's current implementation of Section 1-105.</p> <p>At present, Section 1-105 of the Mississippi UCC prohibits the contractual choice of law of any state other than Mississippi to govern the rights and duties of the parties in regard to (a) disclaimers of implied warranties of merchantability or fitness, (b) limitations of remedies from breach of implied warranties of merchantability or fitness, and (c) the necessity for privity of contract to maintain a civil action for breach of implied warranties of merchantability or fitness. See the attached <i>Comment on Conflict of Laws Provision of Article 1 of the UCC</i> for more detail.</p>

<p>(2) Sections 75-2A-105 and 75-2A-106;</p> <p>(3) Section 75-4-102;</p> <p>(4) Section 75-4A-507;</p> <p>(5) Section 75-5-116;</p> <p>[(6) Section 6-103;] (Article 6 has been repealed in Mississippi)</p> <p>(7) Section 75-8-110;</p> <p>(8) Sections 75-9-301 through 75-9-307.</p>	<p>applicable law, that provision governs and a contrary agreement is effective only to the extent permitted by the law (including the conflict of laws rules) so specified:</p> <p>Rights of creditors against sold goods (Section 75-2-402).</p> <p>Applicability of the Article on Leases (Sections 75-2A-105 and 75-2A-106).</p> <p>Applicability of the Article on Bank Deposits and Collections (Section 75-4-102).</p> <p>Governing law in the Article on Funds Transfers (Section 75-4A-507).</p> <p>Letters of credit (Section 75-5-116).</p> <p>Applicability of the Article on Investment Securities (Section 75-8-110).</p> <p>Law governing perfection, the effect of perfection or nonperfection, and the priority of security interests and agricultural liens (Sections 75-9-301 through 75-9-307).</p>	<p>Since MS has repealed Article 6 on Bulk Sales, this bracketed reference to Section 6-103 should not be included in this section if adopted in MS.</p>
<p>§ 75-1-302. Variation by Agreement.</p> <p>(a) Except as otherwise provided in subsection (b) or elsewhere in the Uniform Commercial Code, the effect of provisions of the Uniform Commercial Code may be varied by agreement.</p> <p>(b) The obligations of good faith, diligence, reasonableness, and care prescribed by the Uniform Commercial Code may not be disclaimed by agreement. The parties, by agreement, may determine the standards by which the performance of those obligations is to be measured if those standards are not manifestly unreasonable. Whenever the Uniform Commercial Code requires an action to be taken within a reasonable time, a time that is not manifestly unreasonable may be fixed by agreement.</p> <p>(c) The presence in certain provisions of the Uniform Commercial Code of the phrase “unless otherwise agreed”, or words of similar import, does not imply that the effect of other provisions may not be varied by agreement under this section.</p>	<p>§ 75-1-102. Purposes; Rules of Construction; Variation by Agreement.</p> <p>(3) The effect of provisions of this code may be varied by agreement, except as otherwise provided in this code and except that the obligations of good faith, diligence, reasonableness and care prescribed by this code may not be disclaimed by agreement but the parties may by agreement determine the standards by which the performance of such obligations is to be measured if such standards are not manifestly unreasonable.</p> <p>(4) The presence in certain provisions of this code of the words “unless otherwise agreed” or words of similar import does not imply that the effect of other provisions may not be varied by agreement under subsection (3).</p>	<p>This section combines the rules from subsections (3) and (4) of former Section 1-102 and subsection (1) of former Section 1-204. No substantive changes are made.</p>
<p>§ 75-1-303. Course of Performance, Course of Dealing, and Usage of Trade.</p> <p>(a) A “course of performance” is a sequence of conduct between the parties to a particular transaction that exists if:</p> <p>(1) the agreement of the parties with respect to the transaction involves repeated occasions for performance by a party; and</p> <p>(2) the other party, with knowledge of the nature of the performance and opportunity for objection to it, accepts the performance or acquiesces in it without objection.</p>	<p>§ 75-1-205. Course of Dealing and Usage of Trade.</p> <p>(1) A course of dealing is a sequence of previous conduct between the parties to a particular transaction which is fairly to be regarded as establishing a common basis of understanding for interpreting their expressions and other conduct.</p> <p>(2) A usage of trade is any practice or method of dealing having such regularity of observance in a place, vocation or trade as to justify an expectation that it will be observed with respect to the transaction in question. The existence and scope of such a usage are to be proved as facts. If it is established that such a usage is embodied in a written trade code or similar writing the interpretation of the writing is for the court.</p>	<p>This section integrates the “course of performance” concept from Articles 2 and 2A into the principles of former Section 1-205, which deals with course of dealing and usage of trade. In so doing, the section slightly modifies the articulation of the course of performance rules to fit more comfortably with the approach and structure of former Section 1-205.</p> <p>There are also slight modifications to be more consistent with the definition of “agreement” in former Section 1-201(3). It should be noted that a course of performance that might otherwise establish a defense to the obligation of a party to a negotiable instrument is not available as a defense against a holder in due course who took the instrument without notice of that course of performance.</p>

<p>(b) A “course of dealing” is a sequence of conduct concerning previous transactions between the parties to a particular transaction that is fairly to be regarded as establishing a common basis of understanding for interpreting their expressions and other conduct.</p> <p>(c) A “usage of trade” is any practice or method of dealing having such regularity of observance in a place, vocation, or trade as to justify an expectation that it will be observed with respect to the transaction in question. The existence and scope of such a usage must be proved as facts. If it is established that such a usage is embodied in a trade code or similar record, the interpretation of the record is a question of law.</p> <p>(d) A course of performance or course of dealing between the parties or usage of trade in the vocation or trade in which they are engaged or of which they are or should be aware is relevant in ascertaining the meaning of the parties’ agreement, may give particular meaning to specific terms of the agreement, and may supplement or qualify the terms of the agreement. A usage of trade applicable in the place in which part of the performance under the agreement is to occur may be so utilized as to that part of the performance.</p> <p>(e) Except as otherwise provided in subsection (f), the express terms of an agreement and any applicable course of performance, course of dealing, or usage of trade must be construed whenever reasonable as consistent with each other. If such a construction is unreasonable:</p> <p>(1) express terms prevail over course of performance, course of dealing, and usage of trade;</p> <p>(2) course of performance prevails over course of dealing and usage of trade; and</p> <p>(3) course of dealing prevails over usage of trade.</p> <p>(f) Subject to Section 75-2-209, a course of performance is relevant to show a waiver or modification of any term inconsistent with the course of performance.</p> <p>(g) Evidence of a relevant usage of trade offered by one party is not admissible unless that party has given the other party notice that the court finds sufficient to prevent unfair surprise to the other party.</p>	<p>(3) A course of dealing between parties and any usage of trade in the vocation or trade in which they are engaged or of which they are or should be aware give particular meaning to and supplement or qualify terms of an agreement.</p> <p>(4) The express terms of an agreement and an applicable course of dealing or usage of trade shall be construed wherever reasonable as consistent with each other; but when such construction is unreasonable, express terms control both course of dealing and usage of trade and course of dealing controls usage of trade.</p> <p>(5) An applicable usage of trade in the place where any part of performance is to occur shall be used in interpreting the agreement as to that part of the performance.</p> <p>(6) Evidence of a relevant usage of trade offered by one party is not admissible unless and until he has given the other party such notice as the court finds sufficient to prevent unfair surprise to the latter.</p>	
<p>§ 75-1-304. Obligation of Good Faith.</p> <p>Every contract or duty within the Uniform Commercial Code imposes an obligation of good faith in its performance and enforcement.</p>	<p>§ 75-1-203. Obligation of Good Faith.</p> <p>Every contract or duty within this code imposes an obligation of good faith in its performance or enforcement.</p>	<p>Except for changing the form of reference to the Uniform Commercial Code, this section is identical to former Section 1-203.</p>
<p>§ 75-1-305. Remedies to Be Liberally Administered.</p> <p>(a) The remedies provided by the Uniform Commercial Code must be liberally administered to the end that the aggrieved party may be put in as good a position as if the other party had fully performed but neither consequential or special damages nor penal damages may be had except as specifically provided in the Uniform Commercial Code or by other rule of law.</p>	<p>§ 75-1-106. Remedies to Be Liberally Administered.</p> <p>(1) The remedies provided by this code shall be liberally administered to the end that the aggrieved party may be put in as good a position as if the other party had fully performed but neither consequential or special nor penal damages may be had except as specifically provided in this code or by other rule of law.</p>	<p>Other than changes in the form of reference to the Uniform Commercial Code, this section is identical to former Section 1-106.</p>

<p>(b) Any right or obligation declared by the Uniform Commercial Code is enforceable by action unless the provision declaring it specifies a different and limited effect.</p>	<p>(2) Any right or obligation declared by this code is enforceable by action unless the provision declaring it specifies a different and limited effect.</p>	
<p>§ 75-1-306. Waiver or Renunciation of Claim or Right After Breach.</p> <p>A claim or right arising out of an alleged breach may be discharged in whole or in part without consideration by agreement of the aggrieved party in an authenticated record.</p>	<p>§ 75-1-107. Waiver or Renunciation of Claim or Right After Breach.</p> <p>Any claim or right arising out of an alleged breach can be discharged in whole or in part without consideration by a written waiver or renunciation signed and delivered by the aggrieved party.</p>	<p>This section changes former law in two respects. First, former Section 1-107, requiring the “delivery” of a “written waiver or renunciation” merges the separate concepts of the aggrieved party’s agreement to forego rights and the manifestation of that agreement. This section separates those concepts, and explicitly requires <i>agreement</i> of the aggrieved party. Second, the revised section reflects developments in electronic commerce by providing for memorialization in an authenticated record. In this context, a party may “authenticate” a record by (i) signing a record that is a writing or (ii) attaching to or logically associating with a record that is not a writing an electronic sound, symbol or process with the present intent to adopt or accept the record. See Sections 1-201(b)(37) and 9-102(a)(7).</p>
<p>§ 75-1-307. Prima Facie Evidence By Third-Party Documents.</p> <p>A document in due form purporting to be a bill of lading, policy or certificate of insurance, official weigher’s or inspector’s certificate, consular invoice, or any other document authorized or required by the contract to be issued by a third party is prima facie evidence of its own authenticity and genuineness and of the facts stated in the document by the third party.</p>	<p>§ 75-1-202. Prima Facie Evidence by Third Party Documents.</p> <p>A document in due form purporting to be a bill of lading, policy or certificate of insurance, official weigher’s or inspector’s certificate, consular invoice, or any other document authorized or required by the contract to be issued by a third party shall be prima facie evidence of its own authenticity and genuineness and of the facts stated in the document by the third party.</p>	<p>Except for minor stylistic changes, this Section is identical to former Section 1-202.</p>
<p>§ 75-1-308. Performance or Acceptance Under Reservation of Rights.</p> <p>(a) A party that with explicit reservation of rights performs or promises performance or assents to performance in a manner demanded or offered by the other party does not thereby prejudice the rights reserved. Such words as “without prejudice,” “under protest,” or the like are sufficient.</p> <p>(b) Subsection (a) does not apply to an accord and satisfaction.</p>	<p>§ 75-1-207. Performance or Acceptance Under Reservation of Rights.</p> <p>(1) A party who, with explicit reservation of rights, performs or promises performance or assents to performance in a manner demanded or offered by the other party does not thereby prejudice the rights reserved. Such words as “without prejudice,” “under protest” or the like are sufficient.</p> <p>(2) Subsection (1) does not apply to an accord and satisfaction.</p>	<p>This section is identical to former Section 1-207.</p>
<p>§ 75-1-309. Option to Accelerate at Will.</p> <p>A term providing that one party or that party’s successor in interest may accelerate payment or performance or require collateral or additional collateral “at will” or when the party “deems itself insecure,” or words of similar import, means that the party has power to do so only if that party in good faith believes that the prospect of payment or performance is impaired. The burden of establishing lack of good faith is on the party against which the power has been exercised.</p>	<p>§ 75-1-208. Option to Accelerate at Will.</p> <p>A term providing that one party or his successor in interest may accelerate payment or performance or require collateral or additional collateral “at will” or “when he deems himself insecure” or in words of similar import shall be construed to mean that he shall have power to do so only if he in good faith believes that the prospect of payment or performance is impaired. The burden of establishing lack of good faith is on the party against whom the power has been exercised.</p>	<p>Except for minor stylistic changes, this section is identical to former Section 1-208.</p>
<p>§ 75-1-310. Subordinated Obligations.</p> <p>An obligation may be issued as subordinated to performance of another obligation of the person obligated, or a creditor may subordinate its right to performance of an obligation by agreement with either the person obligated or another creditor of the person obligated. Subordination does not create a security interest as against either the common debtor or a subordinated creditor.</p>	<p>No corresponding provision.</p>	<p>This section is substantively identical to former Section 1-209. The language in that section stating that it “shall be construed as declaring the law as it existed prior to the enactment of this section and not as modifying it” has been deleted.</p>



# Comparison of Revised Uniform Commercial Code Article 1 with Current Mississippi Statutes

Prepared by Mississippi Secretary of State, Policy & Research Division

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## Revised definitions, Uniform Commercial Code Section 1-201

Introduction. Of the following revised Article 1 definitions, most differ from prior versions only stylistically or in terms of their organization. However, some minor substantive changes have been adopted to particular definitions, most notably “bank,” “fault,” “organization,” “person” and “surety.” Adopting the revised Article 1 will also add definitions of “consumer,” “record” and “state,” none of which are currently contained in Mississippi’s implementation of the UCC. The most notable substantive change in this revision of Article 1 is contained in the revised definition of “good faith”: whereas the former definition defined good faith simply as honesty in fact, the revised definition adds the element of commercial reasonableness.

Some definitions in former Section 1-201 have been reformulated as substantive provisions and have been moved to other sections. See Sections 1-202 (explicating concepts of notice and knowledge formerly addressed in Sections 1-201(25)-(27)), 1-204 (determining when a person gives value for rights, replacing the definition of “value” in former Section 1-201(44)), and 1-206 (addressing the meaning of presumptions, replacing the definitions of “presumption” and “presumed” in former Section 1-201(31)). Similarly, the portion of the definition of “security interest” in former Section 1-201(37) which explained the difference between a security interest and a lease has been relocated to Section 1-203.

Two definitions in former Section 1-201 have been deleted. The definition of “honor” in former Section 1-201(21) has been moved to Section 2-103(1)(b), inasmuch as the definition only applies to the use of the word in Article 2. The definition of “telegram” in former Section 1-201(41) has been deleted because that word no longer appears in the definition of “conspicuous.”

Revised UCC	Current MS statute	Changes from prior version of Article 1
(1) “Action”, in the sense of a judicial proceeding, includes recoupment, counterclaim, set-off, suit in equity, and any other proceeding in which rights are determined.	(1) “Action” in the sense of a judicial proceeding includes recoupment, counterclaim, set-off, suit in equity and any other proceedings in which rights are determined.  (Definition up to date)	Unchanged from the prior version.

<p>(2) “Aggrieved party” means a party entitled to pursue a remedy.</p>	<p>(2) “Aggrieved party” means a party entitled to resort to a remedy.</p> <p>(Definition up to date)</p>	<p>Unchanged from the prior version.</p>
<p>(3) “Agreement”, as distinguished from “contract”, means the bargain of the parties in fact, as found in their language or inferred from other circumstances, including course of performance, course of dealing, or usage of trade as provided in Section § 75-1-303.</p>	<p>(3) “Agreement” means the bargain of the parties in fact as found in their language or by implication from other circumstances including course of dealing or usage of trade or course of performance as provided in this code (Sections 75-1-205 and 75-2-208). Whether an agreement has legal consequences is determined by the provisions of this code, if applicable; otherwise by the law of contracts (Section 75-1-103). (Compare “Contract.”)</p>	<p>Revised definition derived from former Section 1-201. The revised definition does not appear to differ much in substance from Mississippi’s current definition.</p>
<p>(4) “Bank” means a person engaged in the business of banking and includes a savings bank, savings and loan association, credit union, and trust company.</p>	<p>(4) “Bank” means any person engaged in the business of banking.</p>	<p>Revised definition derived from Section 4A-104. The new definition explicitly recognizes savings banks, savings and loan associations, credit unions and trust companies as banks.</p>
<p>(5) “Bearer” means a person in possession of a negotiable instrument, document of title, or certificated security that is payable to bearer or indorsed in blank.</p>	<p>(5) “Bearer” means a person in control of a negotiable electronic document of title or a person in possession of an instrument, negotiable tangible document of title, or certificated security payable to bearer or indorsed in blank.</p>	<p>Unchanged from the prior version, which was derived from § 191 of the Uniform Negotiable Instruments Law.</p>
<p>(6) “Bill of lading” means a document evidencing the receipt of goods for shipment issued by a person engaged in the business of transporting or forwarding goods.</p>	<p>(6) “Bill of lading” means a document of title evidencing the receipt of goods for shipment issued by a person engaged in the business of directly or indirectly transporting or forwarding goods. The term does not include a warehouse</p>	<p>Revised definition derived from former Section 1-201. The revised definition does not appear to differ much in substance from Mississippi’s current definition.</p>

	receipt.	
(7) “Branch” includes a separately incorporated foreign branch of a bank.	(7) “Branch” includes a separately incorporated foreign branch of a bank.  (Definition up to date)	Unchanged from the prior version.
(8) “Burden of establishing” a fact means the burden of persuading the trier of fact that the existence of the fact is more probable than its nonexistence.	(8) “Burden of establishing” a fact means the burden of persuading the triers of fact that the existence of the fact is more probable than its nonexistence.  (Definition up to date)	Unchanged from the prior version.
(9) “Buyer in ordinary course of business” means a person that buys goods in good faith, without knowledge that the sale violates the rights of another person in the goods, and in the ordinary course from a person, other than a pawnbroker, in the business of selling goods of that kind. A person buys goods in the ordinary course if the sale to the person comports with the usual or customary practices in the kind of business in which the seller is engaged or with the seller’s own usual or customary practices. A person that sells oil, gas, or other minerals at the wellhead or minehead is a person in the business of selling goods of that kind. A buyer in ordinary course of business may buy for cash, by exchange of other property, or on secured or unsecured credit, and may acquire goods or documents of title under a preexisting contract for sale. Only a buyer that takes possession of the goods or has a right to recover the goods from the	(9) “Buyer in ordinary course of business” means a person that buys goods in good faith, without knowledge that the sale violates the rights of another person in the goods, and in the ordinary course from a person, other than a pawnbroker, in the business of selling goods of that kind. A person buys goods in the ordinary course if the sale to the person comports with the usual or customary practices in the kind of business in which the seller is engaged or with the seller's own usual or customary practices. A person that sells oil, gas, or other minerals at the wellhead or minehead is a person in the business of selling goods of that kind. A buyer in the ordinary course of business may buy for cash, by exchange of other property, or on secured or unsecured credit, and may acquire goods or documents of title under a preexisting contract for sale. Only a buyer that takes possession of	Except for minor stylistic changes, identical to former Section 1-201.

<p>seller under Article 2 may be a buyer in ordinary course of business. “Buyer in ordinary course of business” does not include a person that acquires goods in a transfer in bulk or as security for or in total or partial satisfaction of a money debt.</p>	<p>the goods or has a right to recover the goods from the seller under Title 75, Chapter 2, may be a buyer in ordinary course of business. A person that acquires goods in a transfer in bulk or as security for or in total or partial satisfaction of a money debt is not a buyer in ordinary course of business.</p>	
<p>(10) “Conspicuous”, with reference to a term, means so written, displayed, or presented that a reasonable person against which it is to operate ought to have noticed it. Whether a term is “conspicuous” or not is a decision for the court. Conspicuous terms include the following:</p> <p>(A) a heading in capitals equal to or greater in size than the surrounding text, or in contrasting type, font, or color to the surrounding text of the same or lesser size; and</p> <p>(B) language in the body of a record or display in larger type than the surrounding text, or in contrasting type, font, or color to the surrounding text of the same size, or set off from surrounding text of the same size by symbols or other marks that call attention to the language.</p>	<p>(10) “Conspicuous,” with reference to a term, means so written, displayed, or presented that a reasonable person against which it is to operate ought to have noticed it. Whether a term is “conspicuous” or not is a decision for the court. Conspicuous terms include the following:</p> <p>(A) A heading in capitals equal to or greater in size than the surrounding text, or in contrasting type, font, or color to the surrounding text of the same or lesser size; and</p> <p>(B) Language in the body of a record or display in larger type than the surrounding text, or in contrasting type, font, or color to the surrounding text of the same size, or set off from surrounding text of the same size by symbols or other marks that call attention to the language.</p> <p>(Definition up to date)</p>	<p>Unchanged from the prior version.</p>

<p>(11) “Consumer” means an individual who enters into a transaction primarily for personal, family, or household purposes.</p>	<p>Currently no corresponding definition in Mississippi’s implementation of the UCC.</p>	<p>Derived from Section 9-102(a)(25).</p>
<p>(12) “Contract”, as distinguished from “agreement”, means the total legal obligation that results from the parties’ agreement as determined by the Uniform Commercial Code as supplemented by any other applicable laws.</p>	<p>(11) “Contract” means the total legal obligation which results from the parties' agreement as affected by this code and any other applicable rules of law. (Compare “Agreement.”)</p>	<p>Except for minor stylistic changes, identical to former Section 1-201.</p>
<p>(13) “Creditor” includes a general creditor, a secured creditor, a lien creditor, and any representative of creditors, including an assignee for the benefit of creditors, a trustee in bankruptcy, a receiver in equity, and an executor or administrator of an insolvent debtor’s or assignor’s estate.</p>	<p>(12) “Creditor” includes a general creditor, a secured creditor, a lien creditor and any representative of creditors, including an assignee for the benefit of creditors, a trustee in bankruptcy, a receiver in equity and an executor or administrator of an insolvent debtor's or assignor's estate.</p> <p>(Definition up to date)</p>	<p>Unchanged from former Section 1-201.</p>
<p>(14) “Defendant” includes a person in the position of defendant in a counterclaim, cross-claim, or third-party claim.</p>	<p>(13) “Defendant” includes a person in the position of defendant in a cross-action or counterclaim.</p>	<p>Except for minor stylistic changes, identical to former Section 1-201.</p>
<p>(15) “Delivery”, with respect to an instrument, document of title, or chattel paper, means voluntary transfer of possession.</p>	<p>(14) “Delivery” with respect to an electronic document of title means voluntary transfer of control and with respect to instruments, tangible documents of title, chattel paper, or certificated securities means voluntary transfer of possession.</p>	<p>Derived from former Section 1-201. The reference to certificated securities has been deleted in light of the more specific treatment of the matter in Section 8-301.</p>
<p>(16) “Document of title” includes bill of lading, dock warrant, dock receipt, warehouse receipt or</p>	<p>(15) “Document of title” means a record (i) that in the regular course of business or financing is</p>	<p>Unchanged from former Section 1-201.</p>

<p>order for the delivery of goods, and also any other document which in the regular course of business or financing is treated as adequately evidencing that the person in possession of it is entitled to receive, hold, and dispose of the document and the goods it covers. To be a document of title, a document must purport to be issued by or addressed to a bailee and purport to cover goods in the bailee’s possession which are either identified or are fungible portions of an identified mass.</p>	<p>treated as adequately evidencing that the person in possession or control of the record is entitled to receive, control, hold, and dispose of the record and the goods the record covers and (ii) that purports to be issued by or addressed to a bailee and to cover goods in the bailee's possession which are either identified or are fungible portions of an identified mass. The term includes a bill of lading, transport document, dock warrant, dock receipt, warehouse receipt, and order for delivery of goods. An electronic document of title is evidenced by a record consisting of information stored in an electronic medium. A tangible document of title is evidenced by a record consisting of information that is inscribed on a tangible medium.</p>	
<p>(17) “Fault” means a default, breach, or wrongful act or omission.</p>	<p>(16) “Fault” means wrongful act, omission or breach.</p>	<p>Derived from former Section 1-201. “Default” has been added to the list of events constituting fault.</p>
<p>(18) “Fungible goods” means:</p> <p>(A) goods of which any unit, by nature or usage of trade, is the equivalent of any other like unit; or</p> <p>(B) goods that by agreement are treated as equivalent.</p>	<p>(17) “Fungible” with respect to goods or securities means goods or securities of which any unit is, by nature or usage of trade, the equivalent of any other like unit. Goods which are not fungible shall be deemed fungible for the purposes of this code to the extent that under a particular agreement or document unlike units are treated as equivalents.</p>	<p>Derived from former Section 1-201. References to securities have been deleted because Article 8 no longer uses the term “fungible” to describe securities. Accordingly, this provision now defines the concept only in the context of goods.</p>
<p>(19) “Genuine” means free of forgery or</p>	<p>(18) “Genuine” means free of forgery or</p>	<p>Unchanged from former Section 1-201.</p>

counterfeiting.	counterfeiting.  (Definition up to date)	
(20) “Good faith,” except as otherwise provided in Article 5, means honesty in fact and the observance of reasonable commercial standards of fair dealing.	(19) “Good faith” means honesty in fact in the conduct or transaction concerned.	<p>The former version of Section 1-201(19) defined “good faith” simply as honesty in fact; the definition contained no element of commercial reasonableness. Over time, however, amendments to other articles of the UCC touching upon good faith began to incorporate the element of objective commercial reasonableness.</p> <p>Thus, the definition of “good faith” in this section merely confirms what has been the case for a number of years as articles of the UCC have been amended or revised – the obligation of “good faith,” applicable in each article, is to be interpreted in the context of all articles except for Article 5 as including both the subjective element of honesty in fact and the objective element of the observance of reasonable commercial standards of fair dealing.</p> <p>Of course, as noted in the statutory text, the definition of “good faith” in this section does not apply when the narrower definition of “good faith” in revised Article 5 is applicable.</p> <p>As noted above, the definition of “good faith” in this section requires not only honesty in fact but also “observance of</p>

		reasonable commercial standards of fair dealing.” Although “fair dealing” is a broad term that must be defined in context, it is clear that it is concerned with the fairness of conduct rather than the care with which an act is performed. This is an entirely different concept than whether a party exercised ordinary care in conducting a transaction. Both concepts are to be determined in the light of reasonable commercial standards, but those standards in each case are directed to different aspects of commercial conduct.
<p>(21) “Holder” means:</p> <p>(A) the person in possession of a negotiable instrument that is payable either to bearer or to an identified person that is the person in possession; or</p> <p>(B) the person in possession of a document of title if the goods are deliverable either to bearer or to the order of the person in possession.</p>	<p>(20) “Holder” means:</p> <p>(A) The person in possession of a negotiable instrument that is payable either to bearer or to an identified person that is the person in possession;</p> <p>(B) The person in possession of a negotiable tangible document of title if the goods are deliverable either to bearer or to the order of the person in possession; or</p> <p>(C) A person in control of a negotiable electronic document of title.</p>	Derived from former Section 1-201. The definition has been reorganized for clarity.
<p>(22) “Insolvency proceeding” includes an assignment for the benefit of creditors or other proceeding intended to liquidate or rehabilitate the estate of the person involved.</p>	<p>(22) “Insolvency proceedings” includes any assignment for the benefit of creditors or other proceedings intended to liquidate or rehabilitate the estate of the person involved.</p>	Unchanged from the prior version.

	(Definition up to date)	
N/A	(21) To “honor” is to pay or to accept and pay, or where a credit so engages to purchase or discount a draft complying with the terms of the credit.	This provision, based on former Article 1 provision was deleted from current version of Article 1. See “Introduction.”
(23) “Insolvent” means:  (A) having generally ceased to pay debts in the ordinary course of business other than as a result of bona fide dispute;  (B) being unable to pay debts as they become due; or  (C) being insolvent within the meaning of federal bankruptcy law.	(23) A person is “insolvent” who either has ceased to pay his debts in the ordinary course of business or cannot pay his debts as they become due or is insolvent within the meaning of the federal bankruptcy law.	Derived from former Section 1-201 and reorganized.
(24) “Money” means a medium of exchange currently authorized or adopted by a domestic or foreign government. The term includes a monetary unit of account established by an intergovernmental organization or by agreement between two or more countries.	(24) “Money” means a medium of exchange authorized or adopted by a domestic or foreign government and includes a monetary unit of account established by an intergovernmental organization or by agreement between two (2) or more nations.	Substantively identical to former Section 1-201.
(25) “Organization” means a person other than an individual.	(28) “Organization” includes a corporation, government or governmental subdivision or agency, business trust, estate, trust, partnership or association, two (2) or more persons having a joint or common interest, or any other legal or	The former definition of this word has been replaced with the standard definition used in acts prepared by the National Conference of Commissioners on Uniform State Laws.

	commercial entity.	
(26) “Party”, as distinguished from “third party”, means a person that has engaged in a transaction or made an agreement subject to the Uniform Commercial Code.	(29) “Party,” as distinct from “third party,” means a person who has engaged in a transaction or made an agreement within this code.	Substantively identical to former Section 1-201.
(27) “Person” means an individual, corporation, business trust, estate, trust, partnership, limited liability company, association, joint venture, government, governmental subdivision, agency, or instrumentality, public corporation, or any other legal or commercial entity.	(30) “Person” includes an individual or an organization (see Section 75-1-102).	The former definition of this word has been replaced with the standard definition used in acts prepared by the National Conference of Commissioners on Uniform State Laws.
(28) “Present value” means the amount as of a date certain of one or more sums payable in the future, discounted to the date certain by use of either an interest rate specified by the parties if that rate is not manifestly unreasonable at the time the transaction is entered into or, if an interest rate is not so specified, a commercially reasonable rate that takes into account the facts and circumstances at the time the transaction is entered into.	(37)(D)(iii) “Present value” means the amount as of a date certain of one or more sums payable in the future, discounted to the date certain. The discount is determined by the interest rate specified by the parties if the rate is not manifestly unreasonable at the time the transaction is entered into; otherwise, the discount is determined by a commercially reasonable rate that takes into account the facts and circumstances of each case at the time the transaction was entered into.	This definition was formerly contained within the definition of “security interest” in former Section 1-201(37).
(29) “Purchase” means taking by sale, lease, discount, negotiation, mortgage, pledge, lien, security interest, issue or reissue, gift, or any other voluntary transaction creating an interest in property.	(32) “Purchase” includes taking by sale, discount, negotiation, mortgage, pledge, lien, security interest, issue or reissue, gift, or any other voluntary transaction creating an interest in property.	Derived from former Section 1-201. The form of definition has been changed from “includes” to “means.”

N/A	(31) “Presumption” or “presumed” means that the trier of fact must find the existence of the fact presumed unless and until evidence is introduced which would support a finding of its nonexistence.	Previous definition moved to Section 1-206 (see other UCC chart, first column).
(30) “Purchaser” means a person that takes by purchase.	(33) “Purchaser” means a person who takes by purchase.  (Definition up to date)	Unchanged from the prior version.
(31) “Record” means information that is inscribed on a tangible medium or that is stored in an electronic or other medium and is retrievable in perceivable form.	Currently no corresponding definition in Mississippi’s implementation of the UCC.	Derived from Section 9-102(a)(69).
(32) “Remedy” means any remedial right to which an aggrieved party is entitled with or without resort to a tribunal.	(34) “Remedy” means any remedial right to which an aggrieved party is entitled with or without resort to a tribunal.  (Definition up to date)	Unchanged from the prior version.
(33) “Representative” means a person empowered to act for another, including an agent, an officer of a corporation or association, and a trustee, executor, or administrator of an estate.	(35) “Representative” includes an agent, an officer of a corporation or association, and a trustee, executor or administrator of an estate, or any other person empowered to act for another.	Derived from former Section 1-201. Reorganized, and form changed from “includes” to “means.”
(34) “Right” includes remedy.	(36) “Rights” includes remedies.	Except for minor stylistic changes, identical to former Section 1-201.
(35) “Security interest” means an interest in personal property or fixtures which secures payment or performance of an obligation. “Security interest” includes any interest of a	(37) “Security interest” means an interest in personal property or fixtures which secures payment or performance of an obligation.	The definition is the first paragraph of the definition of “security interest” in former Section 1-201, with minor stylistic changes. The remaining portion of that definition has been

<p>consignor and a buyer of accounts, chattel paper, a payment intangible, or a promissory note in a transaction that is subject to Article 9. “Security interest” does not include the special property interest of a buyer of goods on identification of those goods to a contract for sale under Section 75-2-401, but a buyer may also acquire a “security interest” by complying with Article 9. Except as otherwise provided in Section 75-2-505, the right of a seller or lessor of goods under Article 2 or 2A to retain or acquire possession of the goods is not a “security interest”, but a seller or lessor may also acquire a “security interest” by complying with Article 9. The retention or reservation of title by a seller of goods notwithstanding shipment or delivery to the buyer under Section 75-2-401 is limited in effect to a reservation of a “security interest.” Whether a transaction in the form of a lease creates a “security interest” is determined pursuant to Section 75-1-203.</p>	<p>(A) The term also includes any interest of a consignor and a buyer of accounts, chattel paper, a payment intangible, or a promissory note in a transaction that is subject to Article 9. The special property interest of a buyer of goods on identification of such goods to a contract for sale under Section 75-2-401 is not a “security interest,” but a buyer may also acquire “security interest,” by complying with Article 9. Except as otherwise provided in Section 75-2-505, the right of a seller or lessor of goods under Article 2 or 2A to retain or acquire possession of the goods is not a “security interest,” but a seller or lessor may also acquire a “security interest” by complying with Article 9. The retention or reservation of title by a seller of goods notwithstanding shipment or delivery to the buyer (Section 75-2-401) is limited in effect to a reservation of a security interest.</p> <p>(B) Whether a transaction creates a lease or security interest is determined by the facts of each case; however, a transaction creates a security interest if the consideration the lessee is to pay the lessor for the right to possession and use of the goods is an obligation for the term of the lease not subject to termination by the lessee, and</p> <p>(i) The original term of the lease is equal to or greater than the remaining economic life of the goods,</p>	<p>moved to Section 1-203.</p>
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	<p>(ii) The lessee is bound to renew the lease for the remaining economic life of the goods or is bound to become the owner of the goods,</p> <p>(iii) The lessee has an option to renew the lease for the remaining economic life of the goods for no additional consideration or nominal additional consideration upon compliance with the lease agreement, or</p> <p>(iv) The lessee has an option to become the owner of the goods for no additional consideration or nominal additional consideration upon compliance with the lease agreement.</p> <p>(C) A transaction does not create a security interest merely because it provides that:</p> <p>(i) The present value of the consideration the lessee is obligated to pay the lessor for the right to possession and use of the goods is substantially equal to or is greater than the fair market value of the goods at the time the lease is entered into,</p> <p>(ii) The lessee assumes risk of loss of the goods, or agrees to pay taxes, insurance, filing, recording, or registration fees, or service or maintenance costs with respect to the goods,</p> <p>(iii) The lessee has an option to renew the lease or to become the owner of the goods,</p>	
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	<p>(iv) The lessee has an option to renew the lease for a fixed rent that is equal to or greater than the reasonably predictable fair market rent for the use of the goods for the term of the renewal at the time the option is to be performed, or</p> <p>(v) The lessee has an option to become the owner of the goods for a fixed price that is equal to or greater than the reasonably predictable fair market value of the goods at the time the option is to be performed.</p> <p>(D) For purposes of this subsection (37):</p> <p>(i) Additional consideration is not nominal if:</p> <ol style="list-style-type: none"> <li>1. When the option to renew the lease is granted to the lessee the rent is stated to be the fair market rent for the use of the goods for the term of the renewal determined at the time the option is to be performed, or</li> <li>2. When the option to become the owner of the goods is granted to the lessee the price is stated to be the fair market value of the goods determined at the time the option is to be performed. Additional consideration is nominal if it is less than the lessee's reasonably predictable cost of performing under the lease agreement if the option is not exercised;</li> </ol> <p>(ii) “Reasonably predictable” and “remaining economic life of the goods” are to be determined</p>	
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	<p>with reference to the fact and circumstances at the time the transaction is entered into; and</p> <p>(iii) “Present value” means the amount as of a date certain of one or more sums payable in the future, discounted to the date certain. The discount is determined by the interest rate specified by the parties if the rate is not manifestly unreasonable at the time the transaction is entered into; otherwise, the discount is determined by a commercially reasonable rate that takes into account the facts and circumstances of each case at the time the transaction was entered into.</p>	
<p>(36) “Send” in connection with a writing, record, or notice means:</p> <p>(A) to deposit in the mail or deliver for transmission by any other usual means of communication with postage or cost of transmission provided for and properly addressed and, in the case of an instrument, to an address specified thereon or otherwise agreed, or if there be none to any address reasonable under the circumstances; or</p> <p>(B) in any other way to cause to be received any record or notice within the time it would have arrived if properly sent.</p>	<p>(38) “Send” in connection with a writing, record, or notice means:</p> <p>(A) To deposit in the mail or deliver for transmission by any other usual means of communication with postage or cost of transmission provided for and properly addressed and, in the case of an instrument, to an address specified thereon or otherwise agreed, or if there be none to any address reasonable under the circumstances; or</p> <p>(B) In any other way to cause to be received any record or notice within the time it would have arrived if properly sent.</p> <p>(Definition up to date)</p>	<p>Derived from former Section 1-201. Compare with “notifies.”</p>

(37) “Signed” includes using any symbol executed or adopted with present intention to adopt or accept a writing.	(39) “Signed” includes any symbol executed or adopted by a party with present intention to authenticate a writing.	Derived from former Section 1-201. Former Section 1-201 referred to “intention to authenticate”; because other articles now use the term “authenticate,” the language has been changed to “intention to adopt or accept.”
(38) “State” means a State of the United States, the District of Columbia, Puerto Rico, the United States Virgin Islands, or any territory or insular possession subject to the jurisdiction of the United States.	Currently no corresponding definition in Mississippi’s implementation of the UCC.	This is the standard definition of the term used in acts prepared by the National Conference of Commissioners on Uniform State Laws.
(39) “Surety” includes a guarantor or other secondary obligor.	(40) “Surety” includes guarantor.	This definition makes it clear that “surety” includes all secondary obligors, not just those whose obligation refers to the person obligated as a surety.
(40) “Term” means a portion of an agreement that relates to a particular matter.	(42) “Term” means that portion of an agreement which relates to a particular matter.	Unchanged from the prior version.
N/A	(41) “Telegram” includes a message transmitted by radio, teletype, cable, any mechanical method of transmission, or the like.	This provision, based on former Article 1 provision was deleted from current version of Article 1. See “Introduction.”
(41) “Unauthorized signature” means a signature made without actual, implied, or apparent authority. The term includes a forgery.	(43) “Unauthorized” signature means one made without actual, implied or apparent authority and includes a forgery.	Unchanged from the prior version.
(42) “Warehouse receipt” means a receipt issued by a person engaged in the business of storing goods for hire.	(45) “Warehouse receipt” means a document of title issued by a person engaged in the business of storing goods for hire.	Unchanged from the prior version.
(43) “Writing” includes printing, typewriting, or any other intentional reduction to tangible form.	(46) “Written” or “writing” includes printing, typewriting, or any other intentional reduction to	Unchanged from the prior version.

<p>“Written” has a corresponding meaning.</p>	<p>tangible form.</p>	
<p>N/A</p>	<p>(44) “Value,” except as otherwise provided with respect to negotiable instruments and bank collections (Sections 75-3-303, 75-4-208 and 75-4-209), a person gives “value” for rights if he acquires them:</p> <p>(A) In return for a binding commitment to extend credit or for the extension of immediately available credit whether or not drawn upon and whether or not a charge-back is provided for in the event of difficulties in collection; or</p> <p>(B) As security for or in total or partial satisfaction of a preexisting claim; or</p> <p>(C) By accepting delivery pursuant to a preexisting contract for purchase; or</p> <p>(D) Generally, in return for any consideration sufficient to support a simple contract.</p>	<p>This provision was moved to Section 1-204. (see other UCC chart, first column).</p>

## **Comment on Conflict of Laws Provision of Article 1 of the UCC**

### **Section 75-1-105 of the existing Mississippi UCC**

#### **Section 1-301 of proposed revised Article 1**

Section 75-1-105(1) of the existing Mississippi UCC dealing with choice of law contains unique non-uniform provisions that prohibit the contractual choice of the law of any state other than Mississippi to govern the rights and duties of the parties in regard to disclaimers of implied warranties of merchantability or fitness, limitations of remedies from breach of implied warranties of merchantability or fitness or the necessary for privity of contract to maintain a civil action for breach of implied warranties of merchantability or fitness, notwithstanding the agreement of the parties that the laws of some other state or nation shall govern such duties.

The provisions of Section 75-1-105(1) were incorporated into the Mississippi UCC by the Mississippi Legislature in 1977 (Chapter 452 of the General Laws of 1997) as part of the special provisions of Article 2 and related code provisions that prohibit enforcement of disclaimers of implied warranties of merchantability and fitness for a particular purpose. The unique Mississippi law on disclaimers of implied warranties and prohibitions of contractual exclusion of remedies for breach of implied warranties in Article 2 of the UCC and procedural mandates to the courts not to enforce choice of non-Mississippi law in Section 11-7-18 are discussed my separate email memo dated June 17, 2009.

Mississippi's unique choice of law provisions have been the subject of several reported decisions. In *Price v. International T&T Corp*, 651 F. Supp. 706 (S.D. Miss. 1986), Judge Tom Lee held that this statute can only be applied to force choice of Mississippi substantive law on disclaimers of implied warranties and exclusion of remedies if the transaction bears some reasonable and appropriate relationship to Mississippi. Judge Lee stated that in the absence of such relationship of the contract to Mississippi, mandatory application of Mississippi substantive law violates constitutional due process. In contrast, in *IHP Industries Inc. v PerMAlert*, 947 F.Supp. 257 (S.D. Miss 1996), the District Court held that in a contract between an Illinois seller and a Missouri buyer, where the product was shipped to Mississippi and was serviced in Mississippi, there was adequate contact with Mississippi to enforce the provisions of Section 75-1-105(1) and to apply Mississippi law on disclaimer of warranties notwithstanding a contrary contractual choice of law provision. A discussion of the constitutional due process issues with Section 75-1-105 is found in McMurray, "A Constitutional Analysis of the Mississippi Commercial Code's Conflict of Laws Provision," 53 Miss. L.J. 619 (1983).

The *Comparison of Revised Uniform Commercial Code Article 1 with Current Mississippi Statutes* prepared by the Mississippi Secretary of State, Policy and Research Division points out that Section 75-1-105 is replaced in revised Article 1 by proposed Section 75-1-301. The Secretary of State's memo includes the Comment to the Official Text which states that new Section 1-301 is "substantially identical to former Section 105." This is accurate if a state had adopted the Official Text of original Article 1, Section 1-301, but of course Mississippi has adopted a unique form of Section 1-105 with provisions to mandate Mississippi law to govern of

disclaimers of implied warranties and limitations of remedies. So this comment is not accurate as to Mississippi.

The special provisions of Section 75-1-105(1) reflect an issue with the public policy of Mississippi on implied warranties. Therefore the drafting of new Section 75-1-301 should take into consideration the disposition of the provisions of Article 2 of the UCC on implied warranties and Section 11-7-18.<sup>1</sup>

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<sup>1</sup> Note that the Official Text of Section 1-301 quoted in the Secretary of State's memo includes a bracketed reference to Section 6-103. Mississippi has repealed entirely Article 6 on Bulk Sales . Therefore this reference should not be included in Section 1-305 if adopted in Mississippi.

To: The Secretary of State Uniform Commercial Code Laws Business Reform Study Group

From: Division of Policy and Research

Date: June 25, 2009

Re: 2002 Amendments to Articles 3 and 4 of the Uniform Commercial Code – Negotiable Instruments and Bank Deposits and Collections

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The 2002 Amendments to Articles 3 and 4 of the Uniform Commercial Code (the “UCC”) (the “2002 Amendments”) bring the Articles up to date with respect to electronically signed instruments and make some other minor revisions that generally give holders of certain instruments more enforcement power. Article 3 has been substantively revised to provide more liberal rules for consumer protection, enforcement of lost or stolen instruments, and enforcement of instruments against accommodation parties.<sup>1</sup> Other revisions to Article 3 provide some balance, such as the revisions to section 3-605 which protect accommodation parties in the event of a discharge of the principal obligor. Article 4 has been revised to add transfer and presentment warranties for remotely-created consumer items in sections 4-207 and 4-208, respectively, as well as minor revisions such as the substitution of “record” or “writing.”

New Defined Terms. New definitions have been added to the definitions section of Article 3, including “consumer account,” “consumer transaction,” “principal obligor,” “record,” “remotely-created consumer item,” and “secondary obligor,” all of which are used in the 2002 Amendments. The text of these definitions, along with the text of all of the other substantive 2002 Amendments, can be found in Exhibit B attached to this document.

Removal of Possession Requirement for Non-holders. The 2002 Amendments generally seem to create a more “holder-friendly” Article 3. For example, revised section 3-309 omits the language that required a non-holder with the rights of a holder to have been in possession of the instrument at the time it was lost or stolen in order to enforce the obligation represented by the instrument. In addition, the revised section 3-309 includes a provision which permits enforcement of an instrument by a non-holder who has “directly or indirectly acquired ownership of the instrument from a person who was entitled to enforce the instrument when loss of possession occurred.”<sup>2</sup> Mississippi’s section 75-3-309 requires that a non-holder must have been in possession of the instrument at the time it was lost or stolen in order to enforce the obligation. This revision was made in order to reject a decision reached in the Federal District Court for the District of Columbia where the plaintiff was denied recovery in a suit to enforce a note which was purchased from a party who was entitled to enforce, but who did not have possession as a result of the F.D.I.C. losing the original note.<sup>3</sup> Additionally, the omission of the requirement

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<sup>1</sup> An accommodation party is “a person who, without recompense or other benefit, signs a negotiable instrument for the purpose of being a surety for another party (called the *accommodated party*) to the instrument. The accommodation party can sign in any capacity (i.e., as maker, drawer, acceptor, or indorser). An accommodation party is liable to all parties except the accommodated party, who impliedly agrees to pay the note or draft and to indemnify the accommodation party for all losses incurred in having to pay it.” BLACK’S LAW DICTIONARY (8<sup>th</sup> Ed. 2004).

<sup>2</sup> UCC § 3-209(a)(2) (2002).

<sup>3</sup> UCC § 3-309 cmt. 2 (*citing* Dennis Joslin Co., LLC v. Robinson Broadcasting Corp., 977 F. Supp 491 (D.D.C. 1997)).

that a party be in possession at the time loss of possession occurred allows parties to enforce instruments that were lost in transit, as well as secured parties who may not be in possession of the instrument but have a valid security interest therein.<sup>4</sup>

Added Warranties for Remotely-created Consumer Items. The 2002 Amendments also provide increased protection to consumers. Sections 3-416 and 3-417 have been revised to include transfer and presentment warranties for remotely-created consumer items.<sup>5</sup> These warranties were added to eliminate a certain form of check fraud, and allow payor banks to absolve themselves of liability for checks that were either not authorized by the consumer, or that were authorized but not for the amount shown.<sup>6</sup> The rationale behind the revision is that depository banks are in a better position than payor banks to monitor, and thus control, this type of fraud.<sup>7</sup>

Changes to Accommodation Party Liability. Section 3-419 has been revised to make it more favorable for holders. A new subsection has been added which provides that if an accommodation party guarantees payment, or fails to unambiguously indicate a guaranty of collection only, then the accommodation party will be primarily liable on the instrument without the enforcing party first having to seek recourse with the principal maker or drawer. This section merely incorporates into Article 3 surety and guaranty law principles that are currently followed in Mississippi.<sup>8</sup> Moreover, this revision gives accommodation parties a strong incentive to clarify the capacity in which they are signing, which serves to put subsequent holders on notice of parties against whom they may enforce. Besides the addition of the new subsection (e), the 2002 Amendments also added new language which provides that, in certain circumstances, an accommodation party may obtain relief that requires the accommodated party to perform its obligation on the instrument. The exact circumstances, presumably, are left to the courts to determine.

Changes to Encourage Prompt Disclosure of Transfers. Finally, the 2002 Amendments substantially overhauled section 3-602 by re-numbering existing subsections and adding new ones. The new subsection (b) provides that where an instrument is transferred without the obligor being notified, payments made by the obligor to the transferor will discharge his or her obligation on the instrument. This addition brings section 3-602 in line with UCC section 9-406(a),<sup>9</sup> the Restatement of Mortgages § 5.5,<sup>10</sup> and the Restatement of Contracts § 338,<sup>11</sup> which

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<sup>4</sup> UCC § 3-309 cmts. 2 and 3.

<sup>5</sup> Under the 2002 Amendments, a remotely-created consumer item means “an item drawn on a consumer account, which is not created by the payor bank and does not bear a handwritten signature purporting to be the signature of the drawer.” UCC § 3-103(16).

<sup>6</sup> UCC § 3-416 cmt. 8.

<sup>7</sup> *Id.*

<sup>8</sup> See *Brent v. Nat'l Bank of Commerce of Columbus*, 258 So. 2d 430, 434 (1972).

<sup>9</sup> UCC § 9-406(a) (“debtor . . . may discharge its obligation by paying the assignor until, but not after, the account debtor receives a notification, authenticated by the assignor or the assignee, that the amount due or to become due has been assigned and that payment is to be made to the assignee. After receipt of the notification, the account debtor may discharge its obligation by paying the assignee and may not discharge the obligation by paying the assignor”).

<sup>10</sup> “Except as otherwise provided by the Uniform Commercial Code, after transfer of an obligation secured by a mortgage, performance of the obligation to the transferor is effective against the transferee if rendered before the obligor receives notice of the transfer” Rest. 3d Prop. (Mortgages) § 5.5.

all provide that an obligor's performance to the transferor or assignor is effective as against the transferee or assignee if such performance is rendered prior to the obligor receiving notice of the transfer or assignment.<sup>12</sup> The new subsection (d) provides that a transferee is deemed to have knowledge of a payment under the new subsection (b) if the payment is made after a transfer, but before the payor has been notified. This subsection is one of the few that is unfavorable toward holders of instruments, but it encourages full and prompt disclosures of any transfers or assignments, and protects obligors from having to pay twice. In addition, new subsection (f) defines the word "signed" as used in section 3-602 with respect to a record that is not a writing to include electronic symbols, sounds, or processes used with the present intent to adopt or accept such record.

Changes to Provisions of Article 3 that are not in the MS Article 3. UCC sections 3-604 and 3-605, were also revised; however Mississippi has not adopted these sections of the UCC. Section 3-604 was merely updated with the addition of a provision including electronic symbols, sounds, and processes in the term "signed" as used in that section with respect to a record. Section 3-605 was substantially re-written to parallel modern interpretations of the laws of suretyship and guaranty – essentially applying the same rules to situations where the secondary obligor is party to the instrument, rather than a surety or guarantor of the principal obligor's obligation.<sup>13</sup>

As the comments to revised section 3-605 point out, though, there are several situations in which a party becomes a secondary obligor, and therefore comes under the purview of this section. An indorser incurs liability by signing the instrument for the purpose of transfer, and a drawer incurs liability with respect to a draft that is accepted by a party other than a bank.<sup>14</sup> Moreover, co-makers would qualify as secondary obligors due to the respective rights of contribution of each.<sup>15</sup> Subsections (a), (b), and (c) of revised section 3-605 deal with the discharge of a secondary obligor's obligation on the instrument in situations where the principal obligor is released (through payment or otherwise), extends the time for payment, or otherwise modifies his obligation. These subsections are based on the Restatement (Third) of Suretyship and Guaranty sections 39 through 41.<sup>16</sup> Subsection (a) alters the rule from the old version in providing that a secondary obligor may be released upon release of the principal obligor, provided the secondary obligor is a party to the instrument and has not consented to the challenged conduct. Under the old subsection (b) a secondary obligor's obligation was not discharged provided he had a right of recourse against the principal obligor.

Section 3-605 includes two new rules set out in subsections (g) and (h). Subsection (g) provides that the secondary obligor's right of recourse against the principal obligor is preserved in the event of release or extension if the terms of the release or extension provide either that the person entitled to enforce retains the right to enforce against the secondary obligor, or that the

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<sup>11</sup> "Except as stated in this Section, notwithstanding an assignment, the assignor retains his power to discharge or modify the duty of the obligor to the extent that the obligor performs or otherwise gives value until but not after the obligor receives notification that the right has been assigned and that performance is to be rendered to the assignee." Rest. 2d Contracts § 338(1).

<sup>12</sup> See UCC § 3-602 cmt. 2.

<sup>13</sup> UCC § 3-605 cmt. 1.

<sup>14</sup> UCC § 3-605 cmt. 3.

<sup>15</sup> *Id.*

<sup>16</sup> See UCC § 3-605 cmts. 4 through 6.

recourse of the secondary obligor continues as if the release or extension had not been granted. Subsection (h) outlines the secondary obligor's burden of proof with respect to the challenged conduct and the alleged loss or prejudice such conduct caused. However, the amendments also provide an exception to the secondary obligor's burden. If the secondary obligor demonstrates loss through impairment of its right of recourse, and the amount of loss is not reasonably calculable, a presumption arises that the loss is equal to the secondary obligor's liability on the instrument, and the burden then shifts to the person entitled to enforce to prove that the loss is actually less.<sup>17</sup> Overall section 3-605, as amended, gives accommodation parties greater rights with respect to discharge and modification, providing some balance with respect to the revised section 3-419 which favors holders over accommodation parties.

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<sup>17</sup> UCC § 3-605(i).

**Exhibit A – Table of 2002 Amendments to  
Articles 3 and 4 of the Uniform Commercial Code**

Current Mississippi Code Section	Revised UCC Code Section	Revision	Type of Revision
75-3-103(a). Definitions	3-103(a)	New definitions added: (2) “Consumer account” (3) “Consumer transaction” (11) “Principal obligor” (14) “Record” (16) “Remotely-created consumer item” (17) “Secondary obligor”	Substantive
75-3-106(a), (b). Unconditional Promise or Order	3-106	Changed “writing” to “record”	Substantive (see definition of “record” in Exhibit B)
75-3-116(b). Joint and Several Liability, Contribution	3-116(b)	Changed “except as provided in section 3-419(e)” to “except as provided in 3-419(f)”	Non-substantive
75-3-119. Notice of Right to Defend Action	3-119	Changed “written notice of the litigation” to “notice of the litigation in a record”	Stylistic
75-3-204. Indorsement	3-204	Does not include last part of Miss. subsection (a) which provides that indorsement on student loan instruments may be made by signed blanket indorsement, rather than by the manner otherwise prescribed by 3-204.	Substantive (however, this subsection is non-uniform)
75-3-305(a). Defenses and Claims in Recoupment	3-305(a)	Changed “except as stated in subsection (b)” to “except as otherwise provided in this section”	Stylistic
75-3-305. Defenses and Claims in Recoupment	3-305(e)	Added subsection (e) providing that a statement required by other law to the effect that rights of a holder or transferee are subject to claims and defenses asserted against original payee will be deemed included, if in fact such statement is not included. (see text in Exhibit B)	Substantive
	3-305(f)	Added subsection (f) providing that 3-305 is subject to other law. (see text in Exhibit B)	Substantive

75-3-309(a). Enforcement of Lost, Destroyed or Stolen Instrument	3-309(a)	Changed the form and substance, omitting requirement that person be in possession at time instrument was lost or stolen; Added provision that person who directly or indirectly acquired ownership from person entitled to enforce at time instrument was lost or stolen may enforce the instrument. (see text in Exhibit B)	Substantive & Stylistic
75-3-312(a)(3). Lost, Destroyed, or Stolen Cashier's Check, Teller's Check, or Certified Check	3-312(a)(3)	Changed "written statement" to "statement, made in a record"	Stylistic
75-3-415(a). Obligation of Indorser	3-415(a)	Changed "subsections (b), (c), and (d)" to "subsections (b), (c), (d), (e)"	Non-substantive
75-3-416(a). Transfer Warranties	3-416(a)(6)	Added subsection (6) creating additional transfer warranty for remotely-created consumer items. (see text in Exhibit B)	Substantive
75-3-417(a). Presentment Warranties	3-417(a)(4)	Added subsection (4) creating additional presentment warranty for remotely-created consumer items. (see text in Exhibit B)	Substantive
75-3-419(e). Instruments Signed for Accommodation	3-419(e)	Changed old subsection (e) to subsection (f), and re-wrote subsection (e) to provide that accommodation parties that guarantee payment, or fail to unambiguously guarantee collection only, are primarily liable on the instrument. (see text in Exhibit B)	Substantive
75-3-419(e). Instruments Signed for Accommodation	3-419(f)	Amended subsection (f) [old subsection (e)] to include provision that, in proper circumstances, the accommodated party may have to perform its obligation on the instrument to give relief to the accommodation party. (see text in Exhibit B)	Substantive
75-3-419(e). Instruments Signed for Accommodation	3-419(f)	Changed "accommodated party who" to "accommodated party that"	Stylistic

75-3-602(a). Payment	3-602(a)	Changed “subject to subsection (b)” to “subject to subsection (e); also removed “(i)” and “(ii)” which enumerated the two requirements for payment, but the requirements are unaltered.	Stylistic
75-3-602(b). Payment	3-602(e)	Moved old subsection (b) to subsection (e)	Non-substantive
	3-602(b)	New subsection (b) provides that an obligation may be discharged if payment is made to a person previously entitled to enforce if payor does not have adequate notification that instrument was transferred; revised (b) sets out requirements for adequate notification. (see text in Exhibit B)	Substantive
75-3-602. Payment	3-602(c)	Added subsection (c) which incorporates that part of old subsection (a) which provides that an obligation is discharged even though payment is made with knowledge of a claim on the instrument. (see text in Exhibit B)	Substantive
N/A	3-602(d)	Added subsection (d) providing that transferee is deemed to have knowledge of payment under [new] subsection (b) if payment is made after the transfer, but before payor has been notified. (see text in Exhibit B)	Substantive
N/A	3-602(e)	Old subsection (b)	Non-substantive
N/A	3-602(f)	Added subsection (f) providing that the word “signed” as used in this section with respect to a record that is not in writing includes electronic symbols, sounds, or processes with present intent to adopt or accept. (see text in Exhibit B)	Substantive
75-3-602(b). Payment	3-602(e)	Changed “not discharged under subsection (a)” to “not discharged under subsections (a) through (d)”	Non-substantive

N/A (Not adopted in Miss.)	3-604. Discharge by Cancellation or Renunciation	Added subsection (c) providing the word “signed” includes electronic symbols, sounds, or processes with the present intent to adopt or accept. (see text in Exhibit B)	Substantive
N/A (Not adopted in Miss.)	3-605. Discharge of Secondary Obligors	Substantially re-written from the previous version to provide secondary obligors more protection. (see text in Exhibit B)	Substantive
75-4-104(c). Definitions and Index of Definitions	4-104(c)	“Control” does not appear in list of definitions from other Articles that apply to this Article	Non-substantive
75-4-104(c)	4-104(c)	“Record” and “remotely-created consumer item” added to list of definitions in other Articles that apply to this Article	Substantive (see definitions of “record” and “remotely-created consumer item” in Exhibit B)
75-4-207(a). Transfer Warranties	4-207(a)(6)	Added subsection (6) providing transfer warranty for remotely-created consumer items	Substantive
75-4-208(a). Presentment Warranties	4-208(a)(4)	Added subsection (4) providing presentment warranty for remotely-created consumer items	Substantive
75-4-210(c). Security Interest of Collecting Bank in Items, Accompanying Documents, and Proceeds	4-210(c)	“possession or control” does not appear before the term “accompanying documents” in either the revised or pre-revision Art. 4	Non-substantive
75-4-212(a). Presentment by Notice of Item Not Payable By, Through, or at Bank; Liability of Drawer or Indorser	4-212(a)	“written notice” changed to “record providing notice”	Substantive (see definition of “record” in Exhibit B)
75-4-301(a)(3). Deferred Posting; Recovery of Payments by Return of Items; Time of Dishonor; Return of Items by Payor Bank	4-301(a)(3)	“Sends written notice” changed to “sends a record providing notice”	Substantive (see definition of “record” in Exhibit B)
75-4-401(a). When Bank May Charge Customer’s Account.	4-401(a)	“from that account” changed to “from the account”	Stylistic
75-4-403(b). Customer’s Right to Stop Payment; Burden of Proof of Loss	4-403(b)	“writing” changed to “record”	Substantive (see definition of “record” in Exhibit B)
75-4-404. Bank Not Obligated to Pay Check More Than Six Months Old	4-404	“Obligated” in title changed to “Obliged”	Stylistic

**Exhibit B – Text of Substantive Revisions in  
2002 Amendments to Articles 3 of the Uniform Commercial Code**

**Article 3 Revised Text:**

3-103. Definitions.

(2) <<+ "Consumer account" means an account established by an individual primarily for personal, family, or household purposes.+>>

<<+(3) "Consumer transaction" means a transaction in which an individual incurs an obligation primarily for personal, family, or household purposes.+>>

<<+(11) "Principal obligor," with respect to an instrument, means the accommodated party or any other party to the instrument against whom a secondary obligor has recourse under this article.+>>

<<+(14) ["Record" means information that is inscribed on a tangible medium or that is stored in an electronic or other medium and is retrievable in perceivable form.]>>

<<+(16) "Remotely-created consumer item" means an item drawn on a consumer account, which is not created by the payor bank and does not bear a handwritten signature purporting to be the signature of the drawer.+>>

<<+(17) "Secondary obligor," with respect to an instrument, means (a) an indorser or an accommodation party, (b) a drawer having the obligation described in [Section 3-414\(d\)](#), or (c) any other party to the instrument that has recourse against another party to the instrument pursuant to [Section 3-116\(b\)](#).+>>

3-305. Defenses and Claims in Recoupment; Claims in Consumer Transactions

<Text of subsec. (e) added by 2002 amendment>

<<+(e) In a consumer transaction, if law other than this article requires that an instrument include a statement to the effect that the rights of a holder or transferee are subject to a claim or defense that the issuer could assert against the original payee, and the instrument does not include such a statement:+>>

<<+(1) the instrument has the same effect as if the instrument included such a statement;+>>

<<+(2) the issuer may assert against the holder or transferee all claims and defenses that would have been available if the instrument included such a statement; and+>>

<<+(3) the extent to which claims may be asserted against the holder or transferee is determined as if the instrument included such a statement.+>>

<Text of subsec. (f) added by 2002 amendment>

<<+(f) This section is subject to law other than this article that establishes a different rule for consumer transactions.+>>

### 3-309. Enforcement of Lost, Destroyed or Stolen Instrument.

a) A person not in possession of an instrument is entitled to enforce the instrument if:

(1) the person seeking to enforce the instrument:

(A) was entitled to enforce the instrument when loss of possession occurred; or

(B) has directly or indirectly acquired ownership of the instrument from a person who was entitled to enforce the instrument when loss of possession occurred;

(2) the loss of possession was not the result of a transfer by the person or a lawful seizure; and

(3) the person cannot reasonably obtain possession of the instrument because the instrument was destroyed, its whereabouts cannot be determined, or it is in the wrongful possession of an unknown person or a person that cannot be found or is not amenable to service of process.

### 3-416. Transfer Warranties.

(a)<<+(6) with respect to a remotely-created consumer item, that the person on whose account the item is drawn authorized the issuance of the item in the amount for which the item is drawn.+>>

### 3-417. Presentment Warranties.

(a)<<+(4) with respect to any remotely-created consumer item, that the person on whose account the item is drawn authorized the issuance of the item in the amount for which the item is drawn.+>>

### 3-419. Instruments Signed for Accommodation.

<<+(e) If the signature of a party to an instrument is accompanied by words indicating that the party guarantees payment or the signer signs the instrument as an accommodation party in some other manner that does not unambiguously indicate an intention to guarantee collection rather than payment, the signer is obliged to pay the amount due on the instrument to a person entitled to enforce the instrument in the same circumstances as the accommodated party would be obliged, without prior resort to the accommodated party by the person entitled to enforce the instrument.+>>

<<-(e)->><<+(f)+>> An accommodation party who pays the instrument is entitled to reimbursement from the accommodated party and is entitled to enforce the instrument against the accommodated party. <<+ In proper circumstances, an accommodation party may obtain relief that requires the accommodated party to perform its obligations on the instrument.+>> An accommodated party <<-who->> <<+that+>> pays the instrument has no right of recourse against, and is not entitled to contribution from, an accommodation party.

### 3-602. Payment.

<<+(b) Subject to subsection (e), a note is paid to the extent payment is made by or on behalf of a party obliged to pay the note to a person that formerly was entitled to enforce the note only if at the time of the payment the party obliged to pay has not received adequate notification that the note has been transferred and that payment is to be made to the transferee. A notification is adequate only if it is signed by the transferor or the transferee; reasonably identifies the transferred note; and provides an address at which payments subsequently are to be made. Upon request, a transferee shall seasonably furnish reasonable proof that the note has been transferred. Unless the transferee complies with the request, a payment to the person that formerly was entitled to enforce the note is effective for purposes of subsection (c) even if the party obliged to pay the note has received a notification under this paragraph.+>>

<<+(c) Subject to subsection (e), to+>> the extent of <<-the payment->> <<+a payment under subsections (a) and (b)+>>, the obligation of the party obliged to pay the instrument is discharged even though payment is made with knowledge of a claim to the instrument under Section 3-306 by another person.

<<+(d) Subject to subsection (e), a transferee, or any party that has acquired rights in the instrument directly or indirectly from a transferee, including any such party that has rights as a holder in due course, is deemed to have notice of any payment that is made under subsection (b) after the date that the note is transferred to the transferee but before the party obliged to pay the note receives adequate notification of the transfer.+>>

<<+(f) As used in this section, "signed," with respect to a record that is not a writing, includes the attachment to or logical association with the record of an electronic symbol, sound, or process with the present intent to adopt or accept the record.+>>

### 3-604. Discharge by Cancellation or Renunciation.

(a) A person entitled to enforce an instrument, with or without consideration, may discharge the obligation of a party to pay the instrument (i) by an intentional voluntary act, such as surrender of the instrument to the party, destruction, mutilation, or cancellation of the instrument, cancellation or striking out of the party's signature, or the addition of words to the instrument

indicating discharge, or (ii) by agreeing not to sue or otherwise renouncing rights against the party by a signed <<-writing->> <<+ record+>>.

(b) Cancellation or striking out of an indorsement pursuant to subsection (a) does not affect the status and rights of a party derived from the indorsement.

<<+(c) In this section, "signed," with respect to a record that is not a writing, includes the attachment to or logical association with the record of an electronic symbol, sound, or process with the present intent to adopt or accept the record.+>>

### 3-605. Discharge of Secondary Obligors.

<The following is the text of section 3-605 as amended in 2002>

<For text of section 3-605 existing prior to amendment in 2002, see section 3-605.>

<<+(a) If a person entitled to enforce an instrument releases the obligation of a principal obligor in whole or in part, and another party to the instrument is a secondary obligor with respect to the obligation of that principal obligor, the following rules apply:+>>

<<+(1) Any obligations of the principal obligor to the secondary obligor with respect to any previous payment by the secondary obligor are not affected. Unless the terms of the release preserve the secondary obligor's recourse, the principal obligor is discharged, to the extent of the release, from any other duties to the secondary obligor under this article.+>>

<<+(2) Unless the terms of the release provide that the person entitled to enforce the instrument retains the right to enforce the instrument against the secondary obligor, the secondary obligor is discharged to the same extent as the principal obligor from any unperformed portion of its obligation on the instrument. If the instrument is a check and the obligation of the secondary obligor is based on an indorsement of the check, the secondary obligor is discharged without regard to the language or circumstances of the discharge or other release.+>>

<<+(3) If the secondary obligor is not discharged under paragraph (2), the secondary obligor is discharged to the extent of the value of the consideration for the release, and to the extent that the release would otherwise cause the secondary obligor a loss.+>>

<<+(b) If a person entitled to enforce an instrument grants a principal obligor an extension of the time at which one or more payments are due on the instrument and another party to the instrument is a secondary obligor with respect to the obligation of that principal obligor, the following rules apply:+>>

<<+(1) Any obligations of the principal obligor to the secondary obligor with respect to any previous payment by the secondary obligor are not affected. Unless the terms of the extension preserve the secondary obligor's recourse, the extension correspondingly extends the time for performance of any other duties owed to the secondary obligor by the principal obligor under

this article.+>>

<<+(2) The secondary obligor is discharged to the extent that the extension would otherwise cause the secondary obligor a loss.+>>

<<+(3) To the extent that the secondary obligor is not discharged under paragraph (2), the secondary obligor may perform its obligations to a person entitled to enforce the instrument as if the time for payment had not been extended or, unless the terms of the extension provide that the person entitled to enforce the instrument retains the right to enforce the instrument against the secondary obligor as if the time for payment had not been extended, treat the time for performance of its obligations as having been extended correspondingly.+>>

<<+(c) If a person entitled to enforce an instrument agrees, with or without consideration, to a modification of the obligation of a principal obligor other than a complete or partial release or an extension of the due date and another party to the instrument is a secondary obligor with respect to the obligation of that principal obligor, the following rules apply:+>>

<<+(1) Any obligations of the principal obligor to the secondary obligor with respect to any previous payment by the secondary obligor are not affected. The modification correspondingly modifies any other duties owed to the secondary obligor by the principal obligor under this article.+>>

<<+(2) The secondary obligor is discharged from any unperformed portion of its obligation to the extent that the modification would otherwise cause the secondary obligor a loss.+>>

<<+(3) To the extent that the secondary obligor is not discharged under paragraph (2), the secondary obligor may satisfy its obligation on the instrument as if the modification had not occurred, or treat its obligation on the instrument as having been modified correspondingly.+>>

<<+(d) If the obligation of a principal obligor is secured by an interest in collateral, another party to the instrument is a secondary obligor with respect to that obligation, and a person entitled to enforce the instrument impairs the value of the interest in collateral, the obligation of the secondary obligor is discharged to the extent of the impairment. The value of an interest in collateral is impaired to the extent the value of the interest is reduced to an amount less than the amount of the recourse of the secondary obligor, or the reduction in value of the interest causes an increase in the amount by which the amount of the recourse exceeds the value of the interest. For purposes of this subsection, impairing the value of an interest in collateral includes failure to obtain or maintain perfection or recordation of the interest in collateral, release of collateral without substitution of collateral of equal value or equivalent reduction of the underlying obligation, failure to perform a duty to preserve the value of collateral owed, under Article 9 or other law, to a debtor or other person secondarily liable, and failure to comply with applicable law in disposing of or otherwise enforcing the interest in collateral.+>>

<<+(e) A secondary obligor is not discharged under subsections (a)(3), (b), (c), or (d) unless the person entitled to enforce the instrument knows that the person is a secondary obligor or has

notice under Section 3-419(c) that the instrument was signed for accommodation.+>>

<<+(f) A secondary obligor is not discharged under this section if the secondary obligor consents to the event or conduct that is the basis of the discharge, or the instrument or a separate agreement of the party provides for waiver of discharge under this section specifically or by general language indicating that parties waive defenses based on suretyship or impairment of collateral. Unless the circumstances indicate otherwise, consent by the principal obligor to an act that would lead to a discharge under this section constitutes consent to that act by the secondary obligor if the secondary obligor controls the principal obligor or deals with the person entitled to enforce the instrument on behalf of the principal obligor.+>>

<<+(g) A release or extension preserves a secondary obligor's recourse if the terms of the release or extension provide that:+>>

<<+(1) the person entitled to enforce the instrument retains the right to enforce the instrument against the secondary obligor; and+>>

<<+(2) the recourse of the secondary obligor continues as if the release or extension had not been granted.+>>

<<+(h) Except as otherwise provided in subsection (i), a secondary obligor asserting discharge under this section has the burden of persuasion both with respect to the occurrence of the acts alleged to harm the secondary obligor and loss or prejudice caused by those acts.+>>

<<+(i) If the secondary obligor demonstrates prejudice caused by an impairment of its recourse, and the circumstances of the case indicate that the amount of loss is not reasonably susceptible of calculation or requires proof of facts that are not ascertainable, it is presumed that the act impairing recourse caused a loss or impairment equal to the liability of the secondary obligor on the instrument. In that event, the burden of persuasion as to any lesser amount of the loss is on the person entitled to enforce the instrument.+>>

**Article 4 Revised Text**

4-104. Definitions

- (c) The following definitions in other Articles apply to this Article
  - "Record" .....Section 3-103.
  - "Remotely-Created consumer item" .....Section 3-103.

4-207. Transfer Warranties

(a)(6) with respect to any remotely-created consumer item, that the person on whose account the item is drawn authorized the issuance of the item in the amount for which the item is drawn.

4-208. Presentment Warranties

(a)(4) with respect to any remotely-created consumer item, that the person on whose account the item is drawn authorized the issuance of the item in the amount for which the item is drawn.

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## UCC Articles 3 and 4

### Summary

Updates provisions of the UCC dealing with payment by checks and other paper instruments to provide essential rules for the new technologies and practices in payment systems.

### Final Act

Final Act Information

### Legislative Information Kit

- UCC 4 Summary
- UCC 3 Summary
- Legislative Fact Sheet
- [Link to Archive Information and Drafts](#)

### Bill Tracking

**Indiana** : Introduced as SB 501 in 2008-09 - ENACTED  
**New Mexico** : Introduced as SB 74 in 2008-09 - ENACTED  
**Oklahoma** : Introduced as SB 991 in 2008-09 - ENACTED  
**Massachusetts** : Introduced as HB 90 in 2008-09 - Filed

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## A Few Facts About The...

### Amendments to Articles 3 and 4 of the UCC

#### PURPOSE:

Updates provisions of the UCC dealing with payment by checks and other paper instruments to provide essential rules for the new technologies and practices in payment systems. UCC3/4 was amended in 2002 to keep pace with developments of legal rules in this area.

#### ORIGIN:

Completed by the Uniform Law Commissioners, in conjunction with the American Law Institute, in 2002.

#### APPROVED BY:

American Bar Association

#### STATE ADOPTIONS:

Arkansas  
 Kentucky  
 Minnesota  
 New Mexico  
 Nevada  
**South Carolina**  
**Texas**

#### 2009 INTRODUCTIONS:

Indiana  
 Massachusetts  
 Oklahoma

For any further information regarding Amendments to UCC Articles 3 and 4, please contact

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## SUMMARY

### Uniform Commercial Code

#### Revised Article 3

In 1896, four years after the Uniform Law Commissioners (ULC) first organized, they promulgated the Negotiable Instruments Law (NIL). It was adopted in every state in the United States, and was the first successful Uniform Act. When the Uniform Commercial Code (UCC) was promulgated initially in 1951, the old, venerable NIL was polished up a bit and offered as Article 3 of the new UCC. The old NIL in either its independent form or as part of the UCC has governed negotiable instruments in the United States for about 80 years, as its first major revisions are prepared for promulgation by the ULC in the year 1989. Another 80 or so years of service is expected for the revisions.

Negotiable instruments make the economy go around. That is why the law on negotiable instruments is important and why the work of the Uniform Law Commissioners has been lasting and uniformly adopted on this subject. What is a negotiable instrument? It is either a "draft," of which the most common subcategory is the "check," or a "note." A "draft" is merely an order from one person to another to pay money to a third person. A check, as a species of draft, illustrates. A person writes checks on a bank account which the bank maintains on that person's behalf. A check, as a kind of draft, is an order from the person/depositor as "drawer" to the bank/drawee for payment of money to a third person named on the check as "payee."

A "note" is evidence of a debt between the "maker," who promises to pay, and another person. A traditional promissory note is an example. One person borrows money from another person. The borrower signs a piece of paper that obligates him to pay the money back at a certain time. That piece of paper, which evidences the debt, is a "note."

Both notes and drafts can be negotiable or nonnegotiable, but negotiability is the issue that makes Article 3 essential. Drafts and notes represent money and have value, based upon that representation. It has long been accepted that drafts and notes can be passed from person to person, well beyond the persons who are parties to the initial transactions represented, almost as easily as money itself is passed from hand to hand. The ability to transfer drafts and notes from person to person, from hand to hand, to "negotiate" them is important to overall economic activity.

That becomes readily apparent when we think about that most common draft, the "check." A "check" is but a draft drawn on a bank. Checks are used to pay for everything, because of their convenience and security. A check has to be negotiable or it simply could not be used for the purposes of paying for nearly everything.

Also, "notes" are bought and sold daily in large quantities on the commercial paper markets in the United States. A person may buy a car or refrigerator on time and sign a note. The dealer will generally negotiate that note to another person in the market for commercial paper, thereby realizing his or her profit and obtaining funds to purchase more inventory to sell. The ability to negotiate these notes, again, is the key to making the market for commercial paper work. The economy needs negotiable instruments, specifically "drafts" and "notes" under Article 3 of the UCC.

"Drafts" and "notes" are "instruments" under Article 3. Besides being orders or promises to pay, they have to have three other characteristics to be instruments subject to Article 3. They must be unconditional order or promises to pay money on demand or at a time certain. They must be payable to "bearer" or to "order." A bearer instrument simply states that it is payable to bearer—no specific payee. Order instruments state the specific person or entity to which payment is to be made. Last, they must promise or order the payment of a fixed amount of money, although this characteristic changes between original and revised Article 3, and that change is described a little later on in this summary.

A negotiable instrument (note or draft) is simply one that a person, called a "holder in due course," who is not one of the persons who created the instrument originally, may negotiate or transfer to another person without difficulty, and who has the power, also, to enforce the instrument according to its terms. If the instrument is a draft, the holder in due course can present it for payment and expect to be paid. If the instrument is a note, a holder in due course can expect to receive payment when the debt is due. The holder

in due course can do these things even when the relationship between the original parties to the instrument would preclude their enforcement of the instrument for payment. The holder in due course is the essence of negotiable instruments. Free alienability of these instruments is their important characteristic, and holders in due course are the agents of free alienability.

How does a person become a holder in due course? He or she does so by taking the instrument in good faith from a prior holder for value without knowledge of any defects in the instrument, of any claims against the instrument, or of any defenses that may be asserted against its payment. The holder in due course, therefore, honestly receives the instrument, has paid for it, and can claim innocence with respect to any transactions which may have involved the instrument prior to its coming into his or her possession. The characteristic of innocence is, perhaps, primary.

Negotiation involves a specific sequence of acts that make up the transfer to a holder, and from one holder to another. There are two elements, depending upon the kind of instrument involved. If the instrument is a bearer instrument, delivery of the instrument from one person to another constitutes negotiation. If the instrument is an order instrument, it is negotiated by indorsement of the instrument by the current payee and physical delivery to another person, who becomes a holder.

Some kinds of drafts are bearer instruments, and they are passed from holder to holder just as money is passed. The common check, although it can be made out to bearer, is usually made out to a specific person. That check is an order instrument, and to negotiate it, the payee must indorse it and pass it on to the next holder. If the indorsement is to bearer, the check can be negotiated further simply by delivery to another person who becomes the next holder. If the indorsement is to a specific person, it remains an order instrument, and negotiation requires a further indorsement and physical delivery to another holder. Most of us are familiar with checks and how the rules of negotiable instruments apply to them, so they make good examples for illustrating these rules. It should be recognized that there are other instruments used in varieties of business transactions that are subject to the same general rules.

If negotiable instruments are used handily under current Article 3, why revise it? The basic reason for a revision is the accumulation of decisions based upon current Article 3, some of which have identified problems. It is possible after these many years to respond to these cases in statutory language, correcting the problems that some of the cases reflect. Also, the transactional environment has changed for negotiable instruments. Institutions such as banks, which are heavily engaged in transactions involving negotiable instruments, operate a little differently than they did when the UCC was first promulgated. Technology is a primary factor, along with an imperative need to use it. Check processing is an example of the need to modernize the law of negotiable instruments. Banks need to process checks faster in volume numbers that have grown astronomically. They need to be able to use electronic communications, computers, and visual scanners to process checks. The law of negotiable instruments, and bank deposits must accommodate these kinds of changes.

It is not possible in the context of a short summary to cover every aspect of the revision of Article 3. Remembering that the viability of negotiable instruments was and remains the reason for Article 3, a few of the improvements can be described as examples of the overall revision.

The scope of Article 3 narrows to a degree in the revision. It answers the question of what is a negotiable instrument by admitting, in theory, fewer instruments. Original Article 3 states that it applies to instruments that have certain characteristics of negotiable instruments, except that they are not made out "to order or bearer." Such instruments fall under original Article 3, but no holder of such instruments can be a "holder in due course."

This provision has been viewed as injecting considerable ambiguity into Article 3. Some contracts may have characteristics that make it a question as to whether Article 3 would apply. There may be unanticipated outcomes for parties to such contracts if Article 3 does apply. In revised Article 3, the ambiguity is removed. The only instrument to which Article 3 would apply that is not a bearer or order instrument is a check—an instrument payable at a bank. Checks, whether made out to order to bearer, ought to be treated as negotiable instruments. Holders of such instruments can be holders in due course, also.

Original Article 3 requires that a negotiable instrument state a "sum certain." The requirement of a sum certain is completely eliminated in revised Article 3. Rather than a sum certain, an instrument must show a "readily ascertainable amount of money, with or without interest or other charges described in the promise or order . . ." Rates of interest may be stated as "fixed or variable."

There is a very specific reason for eliminating the old "sum certain" requirement. Variable rates of interest, pegged to some sort of fluctuating standard rate of interest, are common as they were not in the time Article 3 was originally promulgated. Instruments with variable rates of interest cannot be negotiable instruments with the sum certain requirement, and such instruments should be negotiable instruments. Revised Article 3 assures that variable rate instruments will be negotiable.

Another example of improvements in Article 3 in the new revision is the statement of contribution rules for multiple parties to a draft or notes. If more than one person signs an instrument in the same capacity, Article 3 has always provided that they are jointly and severally liable in that capacity. But revised Article 3 provides further that a party who satisfies an instrument has a right of contribution from co-parties signing the instrument in the same capacity. Further, it deals with contribution when a co-party is insolvent. Contribution is divided between parties who are solvent.

An example for the above rule could involve three persons who co-sign a promissory note as makers. If one of them satisfies the note when it is due, revised Article 3 would permit that person to collect one-third of the payment from each of the co-makers. If one of them is found to be insolvent, the other solvent co-maker would be liable for one-half. The issue of contribution is not addressed in original Article 3.

Original Article 3 provides rules for determining when a cause of action arises or accrues under Article 3. Revised Article 3 adds a statute of limitations. It simply states the time periods within which any action under Article 3 must be brought, as an ordinary statute of limitations provision does.

When an instrument is an order instrument, it requires an indorsement for negotiation. An indorsement is exactly what might be expected, the person to whom payment is ordered signs his or her name on the instrument in the expected place. An indorsed check is a kind of order draft familiar to most people and is an appropriate example.

But endorsements may come with more than the signature. Endorsements that condition negotiation or payment are called restrictive endorsements in original Article 3, because they are intended to restrict the right to negotiate the instrument or to obtain payment. Article 3 has always erred on the side of negotiation. For that reason, an indorsement that purports to prohibit further transfer or negotiation has been always treated as ineffective.

Certain restrictive endorsements were given effect under original Article 3, however. "The first taker under an indorsement . . . had to apply any value . . . consistently with the indorsement . . .," for example. Revised Article 3 goes much further in limiting the effect of restrictive endorsements on the right to receive payment. Conditional language does not make an indorsement "restrictive" in revised Article 3. An indorsement conditioning the right to receive payment "does not affect the right of the indorsee to enforce the instrument." A person paying the instrument or taking it for value or collection may disregard the condition and the rights and liabilities of that person are not affected by whether the conditions have been fulfilled. Revised Article 3 errs even further on the side of effective negotiation.

Revised Article 3 follows original Article 3 by honoring certain restrictive endorsements such as "for deposit," "for collection," "pay any bank," and the like. These are restrictive endorsements applicable to instruments that are collected within the banking system. They are endorsements that must be honored, except in the case of intermediary banks or the non-depositary payor bank. While all others who wrongfully pay over such a restrictive indorsement are held for conversion of the instrument, intermediary banks and the non-depositary payor bank are not. Their role as mere conduits to the depositary bank would be impaired if there was liability. Revised Article 3, however, explicitly makes a non-depositary payor bank exempt from liability with intermediary banks, clarifying the position of the non-depositary payor bank as original Article 3 does not.

Revised Article 3 adds indicia of a regularly executed instrument to the other requirements for a holder in due course in original Article 3. If there is "apparent evidence of forgery or alteration" a holder cannot become a holder in due course. To this extent, the notion of holder in due course is a little more limited than in original Article 3, and the notion of innocence is given a little more specificity. However, if an instrument is clearly forged or altered, it is proper to charge the holder with knowledge of that obvious defect, and revised Article 3 does so.

These are examples of the kinds of improvements of Article 3 made in Revised Article 3. Revised Article 3 covers a great many other topics, including liability of parties to instruments, what happens when a negotiable instrument is dishonored, and discharge of instruments. Some of the older mechanical rules pertaining to such matters as presentment of an instrument as a condition to payment are relaxed. But the basic negotiable instrument remains as it was under original Article 3, and under the NIL. The changes in Revised Article 3 are adjustments to the existing act that make it a better one. Revised Article 3 will guarantee the effectiveness of negotiable instruments for the next century.

\*\*\*

Founded in 1892, the National Conference of Commissioners on Uniform State Laws is a confederation of state commissioners on uniform laws. Its membership comprises more than 300 attorneys, judges, and law professors, who are appointed by each of the 50 states, the District of Columbia, Puerto Rico, and the U.S. Virgin Islands, to draft uniform and model state laws and work toward their enactment.



## SUMMARY

### Uniform Commercial Code

#### Article 4

In the Uniform Commercial Code, Articles 3 and 4 are companion Articles. Article 3 provides for all negotiable instruments, including checks and certificates of deposit. Article 4 is entitled "Bank Deposits and Collections." Most checks are drawn upon bank accounts, and certificates of deposit are banking instruments. Banks, also, conduct transactions in other types of negotiable instruments, as well, and are the central institutions for conducting business in instruments. The close relationship between Articles 3 and 4 is, therefore, quite clear.

In 1990, as a revised Article 3 is complete, amendments to Article 4, also, are offered. A full revision of Article 4 is not offered. Representatives of the Federal Reserve Board announced in 1990 that it was contemplating the assumption of regulatory control over forward collection of checks, and may extend other regulatory control over bank deposits and collections. The Uniform Law Commissioners and the American Law Institute, therefore, have refrained from major revisions of Article 4, preferring to wait until the scope of the Federal Reserve Board's regulations are determined. The wait may be several years.

However, amendments to Article 4 are offered in conjunction with revised Article 3. These amendments take care of the immediate problems that have developed over the time that Article 4 has been in effect, and update the law pertaining to certain banking practices. It is in the amendments to Article 4 that banks are given the opportunity to utilize the best technology in processing checks, for example.

Article 4 establishes the basic rules by which banks handle checks and other "items" in the process of obtaining payment when presented for that purpose by any holder entitled to such payment. The operative term is "item," a term which covers checks or any instrument handled by a bank for collection or payment. A bank is defined, generally, in Article 1 of the UCC as "any person engaged in the business of banking." One of the amendments to Article 4 sharpens the definition by including "a savings bank, savings and loan association, credit union, or trust company." The broad range of institutions that have customers with accounts and checking privileges clearly become included.

Much of Article 4 concerns the obligations of banks in their varying roles in handling "items." Banks act as "depository" banks, "payor" banks, "intermediary" banks, "collecting" banks, and "presenting" banks. Much of the transactional environment involves banks dealing with each other in obtaining collection and payment of an "item," and Article 4 reflects this fact.

A "depository" bank is the bank in which an "item" first appears in the process of obtaining collection and payment. When any person deposits a check, for example, in an account, that person's bank is a "depository" bank. It is also a "collecting" bank, because its role is to send the "item" on its way to the "payor" bank for payment. It is collecting the value of the check deposited in its customer's account. The last "collecting" bank becomes a "presenting" bank, because it is the bank that delivers the instrument (or its representation) to the "payor" bank for payment. The "payor" bank is the bank in which the person who wrote the check has an account, and against whose account payment will be debited. Any bank in any given situation may perform one or more of these prescribed roles.

The fundamental task is, always, to get the "item" presented by somebody's customer to the right bank in a timely manner, so that it can be paid and all participants' books appropriately debited and credited in the process. Article 4, also, deals with the situation in which an "item" is entered into this payment system, and is dishonored. Who carries the loss in such a situation? Who warrants what in the process of transferring an "item" from one person or institution to another person or institution? These are the matters that Article 4 addresses. It has provided satisfactory governance for twenty plus years in all states in the United States.

The large share of amendments are for clarification and do not amount to any substantive change in existing sections of Article 4. There are some key amendments to note. Amended Article 4A permits "truncation" agreements, a concept never contemplated in original Article 4. A truncation agreement between a bank and a customer, allows a bank to present an "item" for payment by "transmission of an image of an item or

information describing the item ('presentment notice') rather than delivery of the item itself." Rather than deliver the check itself, an image of the check or encoded information of some sort is transmitted. The technology is available to permit such truncation of actual delivery of an instrument. The use of the technology saves time and money. Amended Article 4 allows agreement to use "truncation."

Amended Article 4 has a statute of limitations upon actions to enforce an obligation, duty or right arising under Article 4. The statute of limitations is three years after the cause of action accrues. Original Article 4 has no express statute of limitations, and this surprising omission is corrected in the amended version.

Original Article 4 provides for warranties of customers and collecting banks to a payor of an item. The warranties include good title, lack of knowledge of an unauthorized signature, and no material alteration of the instrument. There are some exceptions if the customer or collecting bank become a holder in due course.

Further, there are warranties from a customer or collecting bank to a subsequent transferee or collecting bank. In addition to the warranties mentioned above, the subsequent transferee or collecting bank has the advantage of warranted signatures on the instrument, lack of a defense against payment, and lack of knowledge of insolvency of the maker, acceptor, or drawer of an instrument. These warranties constitute the major obligations of persons and banks under Article 4. Each person or bank has certain responsibilities to the person who takes the instrument offered for the validity of that instrument.

Warranties change to a degree under amended Article 4. Transfer warranties to a subsequent transferee or collecting bank remain much the same. Presentment warranties apply with no exception for holder in due course status. Damages are more specific, as well. The major addition, however, comes with "encoding" and "retention" warranties. These are warranties from one who encodes information with respect to an item that the information is correctly encoded. Retention warranties refer to those who present items pursuant to a truncation agreement and retain the original instrument while transmitting an image of it as presentation for payment. This new warranty notion follows from the concept of truncation agreement in amended Article 4.

Another important amendment to Article 4 takes into account the practice of providing customers an itemized statement of items credited and debited against the customer's account in lieu of providing the actual item to the customer with the statement. Original Article 4 keyed the customer's responsibility to report on altered and/or forged items upon the receipt of the items with the customer's statement. Amended Article 4 permits a sufficiently detailed statement to be notification of altered and/or forged items, and keys the customer's responsibility to report such items upon the receipt of the statement, itself.

However, the bank providing such a statement must keep the items or legible copies for at least seven years, and must supply at least legible copies at the customer's request.

These are examples of the amendments to Article 4 that accompany the revised Article 3. These amendments will assure the utility of the banking system for the long foreseeable future. Perhaps at a future date, depending upon federal action, a fully revised Article 4 will be attempted. But that should not occur for many years. In the meantime the banking system needs these amendments.

\* \* \*

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D R A F T

FOR APPROVAL

**AMENDMENTS TO  
UNIFORM COMMERCIAL CODE ARTICLES 3 AND 4**

NATIONAL CONFERENCE OF COMMISSIONERS  
ON UNIFORM STATE LAWS

MEETING IN ITS ONE-HUNDRED-AND-ELEVENTH YEAR  
TUCSON, ARIZONA

JULY 26 - AUGUST 2, 2002

**AMENDMENTS TO  
UNIFORM COMMERCIAL CODE ARTICLES 3 AND 4**

*WITH PREFATORY NOTE AND PROPOSED COMMENTS*

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By

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and

NATIONAL CONFERENCE OF COMMISSIONERS  
ON UNIFORM STATE LAWS

*The ideas and conclusions set forth in this draft, including the proposed statutory language and any comments or reporter's notes, have not been passed upon by the National Conference of Commissioners on Uniform State Laws, the American Law Institute, or the Drafting Committee. They do not necessarily reflect the views of the Conference and its Commissioners, the Institute and its Members, and the Drafting Committee and its Members and Reporters. Proposed statutory language may not be used to ascertain the intent or meaning of any promulgated final statutory proposal.*

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AMENDMENTS TO UNIFORM COMMERCIAL CODE ARTICLES 3 AND 4

TABLE OF CONTENTS

SECTION 3-102. SUBJECT MATTER. 3
SECTION 3-103. DEFINITIONS. 3
SECTION 3-104. NEGOTIABLE INSTRUMENT. 7
SECTION 3-106. UNCONDITIONAL PROMISE OR ORDER. 7
SECTION 3-116. JOINT AND SEVERAL LIABILITY; CONTRIBUTION. 8
SECTION 3-118. STATUTE OF LIMITATIONS. 9
SECTION 3-119. NOTICE OF RIGHT TO DEFEND ACTION. 9
SECTION 3-203. TRANSFER OF INSTRUMENT; RIGHTS ACQUIRED BY TRANSFER. 10
SECTION 3-205. SPECIAL INDORSEMENT; BLANK INDORSEMENT; ANOMALOUS INDORSEMENT. 10
SECTION 3-301. PERSON ENTITLED TO ENFORCE INSTRUMENT. 10
SECTION 3-302. HOLDER IN DUE COURSE. 11
SECTION 3-303. VALUE AND CONSIDERATION. 11
SECTION 3-305. DEFENSES AND CLAIMS IN RECOUPMENT; CLAIMS IN CONSUMER TRANSACTIONS. 11
SECTION 3-306. CLAIMS TO AN INSTRUMENT. 14
SECTION 3-309. ENFORCEMENT OF LOST, DESTROYED, OR STOLEN INSTRUMENT. 14
SECTION 3-310. EFFECT OF INSTRUMENT ON OBLIGATION FOR WHICH TAKEN. 16
SECTION 3-312. LOST, DESTROYED, OR STOLEN CASHIER'S CHECK, TELLER'S CHECK, OR CERTIFIED CHECK. 16
SECTION 3-412. OBLIGATION OF ISSUER OF NOTE OR CASHIER'S CHECK. 18
SECTION 3-413. OBLIGATION OF ACCEPTOR. 18
SECTION 3-414. OBLIGATION OF DRAWER. 18
SECTION 3-415. OBLIGATION OF INDORSER. 19
SECTION 3-416. TRANSFER WARRANTIES. 19
SECTION 3-417. PRESENTMENT WARRANTIES. 20
SECTION 3-419. INSTRUMENTS SIGNED FOR ACCOMMODATION. 23
SECTION 3-502. DISHONOR. 24
SECTION 3-602. PAYMENT. 25
SECTION 3-604. DISCHARGE BY CANCELLATION OR RENUNCIATION. 27
SECTION 3-605. DISCHARGE OF SECONDARY OBLIGORS. 28
SECTION 4-103. VARIATION BY AGREEMENT; MEASURE OF DAMAGES; ACTION CONSTITUTING ORDINARY CARE. 43
SECTION 4-104. DEFINITIONS AND INDEX OF DEFINITIONS. 43
SECTION 4-207. TRANSFER WARRANTIES. 46
SECTION 4-208. PRESENTMENT WARRANTIES. 47
SECTION 4-212. PRESENTMENT BY NOTICE OF ITEM NOT PAYABLE BY, THROUGH, OR AT BANK; LIABILITY OF DRAWER OR INDORSER. 49
SECTION 4-301. POSTING; RECOVERY OF PAYMENT BY RETURN OF ITEMS; TIME OF DISHONOR; RETURN OF ITEMS BY PAYOR BANK. 50
SECTION 4-403. CUSTOMER'S RIGHT TO STOP PAYMENT; BURDEN OF PROOF OF LOSS. 51
SECTION 4-406. CUSTOMER'S DUTY TO DISCOVER AND REPORT UNAUTHORIZED SIGNATURE OR ALTERATION. 52

AMENDMENTS TO UNIFORM COMMERCIAL CODE ARTICLES 3 AND 4

Prefatory Note

This project arose from a request sent from the Federal Reserve Board of New York to the Conference, related to provisions of Regulation CC (12 C.F.R. Part 229) that govern a variety of matters related to check collection. Based on that request, the ALI and NCCUSL initiated a project that was to have been brought before the ALI membership in May 2001 and before NCCUSL in the summer of 2001. As it turned out, there was not adequate support for the Regulation CC part of the project on the part of either the Federal Reserve or the banking industry. At the summer 2001 meeting, NCCUSL's Executive Committee approved a sharply truncated agenda for this project, designed to limit it to items where the need for reform is plain and the opportunity for justifiable controversy small.

The draft that is submitted includes only the items approved as part of that agenda. The amendments are limited to Articles 3 and 4 of the Uniform Commercial Code and include the following items:

- 1. Transferring Lost Instruments.—At least one case has held that the receiver of a failed bank cannot enforce an instrument transferred to it in the portfolio of a failed bank if the instrument was lost before the transfer. The result in that case poses a serious problem for the FDIC. A revision to UCC § 3-309 will call for a contrary result, making it clear that the party seeking to enforce a lost instrument need not have been in possession of the instrument at the time that it was lost.
2. Payment and Discharge.—Amendments to UCC §§ 3-602 conform that provision to the rules for payment that appear in the Restatement of Mortgages and in the Restatement of Contracts.
3. Telephonically Generated Checks.—Several States have adopted non-uniform amendments dealing with the responsibility for unauthorized telephone-generated checks. The draft includes warranties that generally place the responsibility for such checks on depositary banks rather than payor banks. The proposed items are limited to items that are drawn on a consumer account and do not bear a manual signature. The Drafting Committee considered extending those provisions to items drawn on a commercial account, but concluded that there was not sufficient consensus in the banking community about how such provisions should apply.
4. Suretyship.—Amendments to UCC §§ 3-419 and 3-605 generally conform those

provisions to the rules in the Restatement of Suretyship and Guaranty. There is some controversy about the revisions that appear in Section 3-605(a), which differ from the existing version of Section 3-605 by raising the possibility that a lender will discharge a guarantor if it grants a complete release to a borrower. The Drafting Committee concluded that the altered provisions are appropriate, however, because (as the Comments below explain) the rule of law in the Restatement is superior in that it is fairer to the guarantor. Moreover (again, as the Comments explain), the Drafting Committee does not believe that the alterations will apply to a broad range of transactions.

5. Electronic Communications.—Amendments to various provisions of Articles 3 and 4 implement the policy of the Uniform Electronic Transactions Act to remove unnecessary obstacles to electronic communications.

6. Consumer Notes.—A provision analogous to UCC § 9-404(d) indicates that a note for which the Federal Trade Commission requires a notice to be included will be treated as if the notice had been included. There is some opposition to that provision, but the Drafting Committee concluded that the provisions provide an appropriate implementation of the applicable federal regulations.

7. United Nations Convention on International Bills of Exchange and International Promissory Notes.—The draft includes several comments indicating similarities and differences between Article 3 and the United Nations Convention, designed to facilitate implementation of the Convention if the United States ratifies that convention in the coming years.

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**AMENDMENTS TO  
UNIFORM COMMERCIAL CODE ARTICLES 3 AND 4**

**SECTION 3-102. SUBJECT MATTER.**

**Proposed Comments<sup>1</sup>**

Add the following to the end of Comment 5:

That Convention applies only to bills and notes that indicate on their face that they involve cross-border transactions. It does not apply at all to checks. Convention Articles 1(3), 2(1), 2(2). Moreover, because it applies only if the bill or note specifically calls for application of the Convention, Convention Article 1, there is little chance that the Convention will apply accidentally to a transaction that the parties intended to be governed by this Article.

**SECTION 3-103. DEFINITIONS.**

(a) In this Article:

(1) "Acceptor" means a drawee who has accepted a draft.

(2) "Consumer account" means an account established by an individual primarily for personal, family, or household purposes.

(3) "Consumer transaction" means a transaction in which an individual incurs an obligation primarily for personal, family, or household purposes.

(4) "Drawee" means a person ordered in a draft to make payment.

~~(5)~~ "Drawer" means a person who signs or is identified in a draft as a person ordering payment.

---

<sup>1</sup>Proposed Comments for unamended sections require Permanent Editorial Board approval, and are shown here only for informational purposes in this draft. No action is required in this meeting.

1           ~~(4)~~ “Good faith” means honesty in fact and the observance of reasonable commercial  
2 standards of fair dealing. ~~(6)~~ [Reserved]

3           ~~(5)~~ (7) “Maker” means a person who signs or is identified in a note as a person  
4 undertaking to pay.

5           ~~(6)~~ (8) “Order” means a written instruction to pay money signed by the person giving  
6 the instruction. The instruction may be addressed to any person, including the person giving the  
7 instruction, or to one or more persons jointly or in the alternative but not in succession. An  
8 authorization to pay is not an order unless the person authorized to pay is also instructed to pay.

9           ~~(7)~~ (9) “Ordinary care” in the case of a person engaged in business means observance  
10 of reasonable commercial standards, prevailing in the area in which the person is located, with  
11 respect to the business in which the person is engaged. In the case of a bank that takes an  
12 instrument for processing for collection or payment by automated means, reasonable commercial  
13 standards do not require the bank to examine the instrument if the failure to examine does not  
14 violate the bank’s prescribed procedures and the bank’s procedures do not vary unreasonably  
15 from general banking usage not disapproved by this Article or Article 4.

16           ~~(8)~~ (10) “Party” means a party to an instrument.

17           (11) “Principal obligor,” with respect to an instrument, means the accommodated  
18 party or any other party to the instrument against whom a secondary obligor has recourse under  
19 this article.

20           ~~(9)~~ (12) “Promise” means a written undertaking to pay money signed by the person  
21 undertaking to pay. An acknowledgment of an obligation by the obligor is not a promise unless

1 the obligor also undertakes to pay the obligation.

2           ~~(10)~~ (13) “Prove” with respect to a fact means to meet the burden of establishing the  
3 fact (Section 1-201(8)).

4           (14) [Reserved]

5           ~~(11)~~ (15) “Remitter” means a person who purchases an instrument from its issuer if  
6 the instrument is payable to an identified person other than the purchaser.

7           (16) “Remotely-created consumer item” means an item drawn on a consumer account  
8 which is not created by the payor bank and does not bear a handwritten signature purporting to be  
9 the signature of the drawer.

10           (17) “Secondary obligor,” with respect to an instrument, means (a) an indorser or an  
11 accommodation party, (b) a drawer having the obligation described in Section 3-414(d), or (c)  
12 any other party to the instrument that has recourse against another party to the instrument  
13 pursuant to Section 3-116(b).

14 (b) Other definitions applying to this Article and the sections in which they appear are:

15	“Acceptance”	Section 3-409
16	“Accommodated party”	Section 3-419
17	“Accommodation party”	Section 3-419
18	“Account”	Section 4-104
19	“Alteration”	Section 3-407
20	“Anomalous indorsement”	Section 3-205
21	“Blank indorsement”	Section 3-205
22	“Cashier’s check”	Section 3-104
23	“Certificate of deposit”	Section 3-104
24	“Certified check”	Section 3-409
25	“Check”	Section 3-104
26	“Consideration”	Section 3-303
27	“Draft”	Section 3-104
28	“Holder in due course”	Section 3-302

1	“Incomplete instrument”	Section 3-115
2	“Indorsement”	Section 3-204
3	“Indorser”	Section 3-204
4	“Instrument”	Section 3-104
5	“Issue”	Section 3-105
6	“Issuer”	Section 3-105
7	“Negotiable instrument”	Section 3-104
8	“Negotiation”	Section 3-201
9	“Note”	Section 3-104
10	“Payable at a definite time”	Section 3-108
11	“Payable on demand”	Section 3-108
12	“Payable to bearer”	Section 3-109
13	“Payable to order”	Section 3-109
14	“Payment”	Section 3-602
15	“Person entitled to enforce”	Section 3-301
16	“Presentment”	Section 3-501
17	“Reacquisition”	Section 3-207
18	“Special indorsement”	Section 3-205
19	“Teller’s check”	Section 3-104
20	“Transfer of instrument”	Section 3-203
21	“Traveler’s check”	Section 3-104
22	“Value”	Section 3-303

23 (c) The following definitions in other Articles apply to this Article:

24	“Bank”	Section 4-105
25	“Banking day”	Section 4-104
26	“Clearing house”	Section 4-104
27	“Collecting bank”	Section 4-105
28	“Depositary bank”	Section 4-105
29	“Documentary draft”	Section 4-104
30	“Intermediary bank”	Section 4-105
31	“Item”	Section 4-104
32	“Payor bank”	Section 4-105
33	“Suspends payments”	Section 4-104

34 (d) In addition, Article 1 contains general definitions and principles of construction and  
35 interpretation applicable throughout this Article.

**Proposed Comments**

2 Legislative Note. A jurisdiction that enacts this statute that has not yet enacted the revised  
3 version of UCC Article 1 should add to Section 3-103 the definition of “good faith” that appears  
4 in the official version of Section 1-201(b)(20) and the definition of “record” that appears in the  
5 official version of Section 1-201(b)(33a). Sections 3-103(a)(6) and (14) are reserved for that  
6 purpose.

7 Comment 4 should be revised by replacing the first two sentences with the following: This  
8 Article now uses the standard definition of good faith in revised Article 1.

9 Comment 6 should be replaced with the following: The definition of consumer account includes  
10 a joint account established by more than one individual. See Section 1-106(1).

11

**SECTION 3-104. NEGOTIABLE INSTRUMENT.**

**Proposed Comments**

14 5. There are some differences between the requirements of Article 3 and the requirements  
15 included in Article 3 of the Convention on International Bills of Exchange and International  
16 Promissory Notes. Most obviously, the Convention does not include the limitation on extraneous  
17 undertakings set forth in paragraph 3-104(a)(3), and does not permit documents payable to bearer  
18 that would be permissible under paragraph 3-104(a)(1) and Section 3-109. See Convention  
19 Article 3. In most respects, however, the requirements of Section 3-104 and Article 3 of the  
20 Convention are quite similar.

21

**SECTION 3-106. UNCONDITIONAL PROMISE OR ORDER.**

22

23 (a) Except as provided in this section, for the purposes of Section 3-104(a), a promise or  
24 order is unconditional unless it states (i) an express condition to payment, (ii) that the promise or  
25 order is subject to or governed by another ~~writing~~, record, or (iii) that rights or obligations with  
26 respect to the promise or order are stated in another ~~writing~~, record. A reference to another  
27 ~~writing~~ record does not of itself make the promise or order conditional.

28 (b) A promise or order is not made conditional (i) by a reference to another ~~writing~~ record

1 for a statement of rights with respect to collateral, prepayment, or acceleration, or (ii) because  
2 payment is limited to resort to a particular fund or source.

3 (c) If a promise or order requires, as a condition to payment, a countersignature by a  
4 person whose specimen signature appears on the promise or order, the condition does not make  
5 the promise or order conditional for the purposes of Section 3-104(a). If the person whose  
6 specimen signature appears on an instrument fails to countersign the instrument, the failure to  
7 countersign is a defense to the obligation of the issuer, but the failure does not prevent a  
8 transferee of the instrument from becoming a holder of the instrument.

9 (d) If a promise or order at the time it is issued or first comes into possession of a holder  
10 contains a statement, required by applicable statutory or administrative law, to the effect that the  
11 rights of a holder or transferee are subject to claims or defenses that the issuer could assert  
12 against the original payee, the promise or order is not thereby made conditional for the purposes  
13 of Section 3-104(a); but if the promise or order is an instrument, there cannot be a holder in due  
14 course of the instrument.

15  
16 **SECTION 3-116. JOINT AND SEVERAL LIABILITY; CONTRIBUTION.**

17 (a) Except as otherwise provided in the instrument, two or more persons who have the  
18 same liability on an instrument as makers, drawers, acceptors, indorsers who indorse as joint  
19 payees, or anomalous indorsers are jointly and severally liable in the capacity in which they sign.

20 (b) Except as provided in Section 3-419(e) or by agreement of the affected parties, a

1 party having joint and several liability who pays the instrument is entitled to receive from any  
2 party having the same joint and several liability contribution in accordance with applicable law.

3 ~~(c) Discharge of one party having joint and several liability by a person entitled to enforce~~  
4 ~~the instrument does not affect the right under subsection (b) of a party having the same joint and~~  
5 ~~several liability to receive contribution from the party discharged.~~

6 **Proposed Comments**

7 The last two sentences of comment 1 should be replaced by the following: Because one of the  
8 joint and several obligors may have recourse against the other joint and several obligor under  
9 subsection (b), each party that is jointly and severally liable under subsection (a) is a secondary  
10 obligor in part and a principal obligor in part, as those terms are defined in Section 3-103(a).  
11 Accordingly, Section 3-605 determines the effect of a release, an extension of time, or a  
12 modification of the obligation of one of the joint and several obligors, as well as the effect of an  
13 impairment of collateral provided by one of those obligors.

14  
15  
16 **SECTION 3-118. STATUTE OF LIMITATIONS.**

17 **Proposed Comments**

18 7. One of the most significant differences between this Article and the Convention on  
19 International Bills of Exchange and International Promissory Notes is that the statute of  
20 limitation under the Convention generally is only four years, rather than the six years provided by  
21 this section. See Convention Article 84.

22  
23 **SECTION 3-119. NOTICE OF RIGHT TO DEFEND ACTION.**

24 In an action for breach of an obligation for which a third person is answerable over pursuant  
25 to this Article or Article 4, the defendant may give the third person ~~written~~ notice of the litigation  
26 in a record, and the person notified may then give similar notice to any other person who is  
27 answerable over. If the notice states (i) that the person notified may come in and defend and (ii)

1 that failure to do so will bind the person notified in an action later brought by the person giving  
2 the notice as to any determination of fact common to the two litigations, the person notified is so  
3 bound unless after reasonable receipt of the notice the person notified does come in and defend.

4  
5 **SECTION 3-203. TRANSFER OF INSTRUMENT; RIGHTS ACQUIRED BY**  
6 **TRANSFER.**

7 **Proposed Comments**

8 6. The rules for transferring instruments set out in this section are similar to the rules in  
9 Article 13 of the Convention on International Bills of Exchange and International Promissory  
10 Notes.

11  
12 **SECTION 3-205. SPECIAL INDORSEMENT; BLANK INDORSEMENT;**  
13 **ANOMALOUS INDORSEMENT.**

14 **Proposed Comments**

15 4. Articles 14 and 16 of the Convention on International Bills of Exchange and International  
16 Promissory Notes includes similar rules for blank and special indorsements.

17  
18 **SECTION 3-301. PERSON ENTITLED TO ENFORCE INSTRUMENT.**

19 **Proposed Comments**

20 The following should be added before the last sentence: For example, it should include a  
21 remitter that has received an instrument from the issuer but has not yet transferred or negotiated  
22 the instrument to another person.

23  
24 **SECTION 3-302. HOLDER IN DUE COURSE.**

25 **Proposed Comments**

26 8. The status of holder in due course resembles the status of protected holder under Article

1 29 of the Convention on International Bills of Exchange and International Promissory Notes.  
2 The requirements for being a protected holder under Article 29 generally track those of Section  
3 3-302.

4  
5 **SECTION 3-303. VALUE AND CONSIDERATION.**

6 **Proposed Comments**

7 6. The term “promise” in paragraph (a)(1) is used in its normal meaning, not in the  
8 specialized meaning given that term in Section 3-103(a)(12). See Section 1-201 (“Changes from  
9 Former Law”). No inference should be drawn from the decision to retain the word “promise”  
10 here despite its specialized definition in Section 3-103. Indeed, that is true even though  
11 “undertaking” is used instead of “promise” in clause (i) of paragraph 3-104(a)(3). See Section 3-  
12 104 comment 1 (explaining the use of the term “undertaking” in Section 3-104 to avoid use of  
13 the defined term “promise”).

14  
15 **SECTION 3-305. DEFENSES AND CLAIMS IN RECOUPMENT; CLAIMS IN**  
16 **CONSUMER TRANSACTIONS.**

17 (a) Except as ~~stated in subsection (b); otherwise provided in this section~~, the right to  
18 enforce the obligation of a party to pay an instrument is subject to the following:

19 (1) a defense of the obligor based on (i) infancy of the obligor to the extent it is a  
20 defense to a simple contract, (ii) duress, lack of legal capacity, or illegality of the transaction  
21 which, under other law, nullifies the obligation of the obligor, (iii) fraud that induced the obligor  
22 to sign the instrument with neither knowledge nor reasonable opportunity to learn of its character  
23 or its essential terms, or (iv) discharge of the obligor in insolvency proceedings;

24 (2) a defense of the obligor stated in another section of this Article or a defense of the  
25 obligor that would be available if the person entitled to enforce the instrument were enforcing a

1 right to payment under a simple contract; and

2 (3) a claim in recoupment of the obligor against the original payee of the instrument if

3 the claim arose from the transaction that gave rise to the instrument; but the claim of the obligor

4 may be asserted against a transferee of the instrument only to reduce the amount owing on the

5 instrument at the time the action is brought.

6 (b) The right of a holder in due course to enforce the obligation of a party to pay the

7 instrument is subject to defenses of the obligor stated in subsection (a)(1), but is not subject to

8 defenses of the obligor stated in subsection (a)(2) or claims in recoupment stated in subsection

9 (a)(3) against a person other than the holder.

10 (c) Except as stated in subsection (d), in an action to enforce the obligation of a party to

11 pay the instrument, the obligor may not assert against the person entitled to enforce the

12 instrument a defense, claim in recoupment, or claim to the instrument (Section 3-306) of another

13 person, but the other person's claim to the instrument may be asserted by the obligor if the other

14 person is joined in the action and personally asserts the claim against the person entitled to

15 enforce the instrument. An obligor is not obliged to pay the instrument if the person seeking

16 enforcement of the instrument does not have rights of a holder in due course and the obligor

17 proves that the instrument is a lost or stolen instrument.

18 (d) In an action to enforce the obligation of an accommodation party to pay an instrument,

19 the accommodation party may assert against the person entitled to enforce the instrument any

20 defense or claim in recoupment under subsection (a) that the accommodated party could assert

1 against the person entitled to enforce the instrument, except the defenses of discharge in

2 insolvency proceedings, infancy, and lack of legal capacity.

3 (e) In a consumer transaction, if law other than this article requires that an instrument

4 include a statement to the effect that the rights of a holder or transferee are subject to a claim or

5 defense that the issuer could assert against the original payee, and the instrument does not include

6 such a statement:

7 (1) the instrument has the same effect as if the instrument included such a statement;

8 (2) the issuer may assert against the holder or transferee all claims and defenses that

9 would have been available if the instrument included such a statement; and

10 (3) the extent to which claims may be asserted against the holder or transferee is

11 determined as if the instrument included such a statement.

12 (f) This section is subject to law other than this article that establishes a different rule for

13 consumer transactions.

14 **Proposed Comments**

15 6. Subsection (e) is added to clarify the treatment of an instrument that omits the notice

16 currently required by the Federal Trade Commission Rule related to consumer credit sales (16

17 C.F.R. Part 433). It reflects the reasoning of cases such as Associates Home Equity Services,

18 Inc. v. Troup, 778 A.2d 529, 540-43 (N.J. Super. Ct. 2001); and Gonzalez v. Old Kent Mortgage

19 Co., 2000 WL 1469313, at \*5 (E.D. Pa. 2000). It is based on the language describing that rule in

20 Section 3-106(d) and the analogous provision in Section 9-404(d).

21 7. Subsection (f) is modeled on Sections 9-403(e) and 9-404(c). It ensures that Section 3-

22 305 is interpreted to accommodate relevant consumer-protection laws.

23 8. Articles 28 and 30 of the Convention on International Bills of Exchange and International

24 Promissory Notes includes a similar dichotomy, with a narrower group of defenses available

1 against a protected holder under Articles 28(1) and 30 than are available under Article 28(2)  
2 against a holder that is not a protected holder.

3  
4 **SECTION 3-306. CLAIMS TO AN INSTRUMENT.**

5 **Proposed Comments**

6 Add the following sentence at the end: The rule of this section is similar to the rule of Article  
7 30(2) of the Convention on International Bills of Exchange and International Promissory Notes.

8  
9 **SECTION 3-309. ENFORCEMENT OF LOST, DESTROYED, OR STOLEN**  
10 **INSTRUMENT.**

11 (a) A person not in possession of an instrument is entitled to enforce the instrument if

12 (1) the person seeking to enforce the instrument

13 ~~(i) the person was in possession of the instrument and (A) was~~ entitled to enforce  
14 ~~it the instrument~~ when loss of possession occurred, or

15 (B) has directly or indirectly acquired ownership of the instrument from a person  
16 who was entitled to enforce the instrument when loss of possession occurred;

17 ~~(ii) (2) the loss of possession was not the result of a transfer by the person or a~~  
18 ~~lawful seizure; and~~

19 ~~seizure, and (iii) (3) the person cannot reasonably obtain possession of the instrument~~  
20 ~~because the instrument was destroyed, its whereabouts cannot be determined, or it is in the~~  
21 ~~wrongful possession of an unknown person or a person that cannot be found or is not amenable~~

1 to service of process.

2 (b) A person seeking enforcement of an instrument under subsection (a) must prove the  
3 terms of the instrument and the person's right to enforce the instrument. If that proof is made,  
4 Section 3-308 applies to the case as if the person seeking enforcement had produced the  
5 instrument. The court may not enter judgment in favor of the person seeking enforcement unless  
6 it finds that the person required to pay the instrument is adequately protected against loss that  
7 might occur by reason of a claim by another person to enforce the instrument. Adequate  
8 protection may be provided by any reasonable means.

9 **Proposed Comments**

10 [Change existing comment to comment 1.]

11 2. Subsection (a) is intended to reject the result in Dennis Joslin Co. v. Robinson  
12 Broadcasting Corp., 977 F. Supp. 491 (D.D.C. 1997). A transferee of a lost instrument need  
13 prove only that its transferor was entitled to enforce, not that the transferee was in possession at  
14 the time the instrument was lost. The protections of subsection (a) should also be available when  
15 instruments are lost during transit, because whatever the precise status of ownership at the point  
16 of loss, either the sender or the receiver ordinarily would have been entitled to enforce the  
17 instrument during the course of transit. The revisions to subsection (a) are not intended to alter  
18 in any way the rules that apply to the destruction of checks in connection with truncation or any  
19 other expedited method of check collection or processing. See Section 3-604(a).

20 3. A security interest may attach to the right of a person not in possession of an instrument to  
21 enforce the instrument. Although the secured party may not be the owner of the instrument, the  
22 secured party may nevertheless be entitled to exercise its debtor's right to enforce the instrument  
23 by resorting to its collection rights under the circumstances described in Section 9-607. This  
24 section does not address whether the person required to pay the instrument owes any duty to a  
25 secured party that is not itself the owner of the instrument.  
26  
27



1 (c) If the obligated bank pays the amount of a check to a claimant under subsection (b)(4)  
2 and the check is presented for payment by a person having rights of a holder in due course, the  
3 claimant is obliged to (i) refund the payment to the obligated bank if the check is paid, or (ii) pay  
4 the amount of the check to the person having rights of a holder in due course if the check is  
5 dishonored.

6 (d) If a claimant has the right to assert a claim under subsection (b) and is also a person  
7 entitled to enforce a cashier's check, teller's check, or certified check which is lost, destroyed, or  
8 stolen, the claimant may assert rights with respect to the check either under this section or  
9 Section 3-309.

10 **SECTION 3-412. OBLIGATION OF ISSUER OF NOTE OR CASHIER'S CHECK.**

11 **Proposed Comments**

12 4. The rule of this section is similar to the rule of Article 39 of the Convention on  
13 International Bills of Exchange and International Promissory Notes.

14 **SECTION 3-413. OBLIGATION OF ACCEPTOR.**

15 **Proposed Comments**

16 Add the following sentence at the end of the comment: The rule of this section is similar to  
17 the rule of Articles 41 of the Convention on International Bills of Exchange and International  
18 Promissory Notes. Articles 42 and 43 of the Convention include more detailed rules that in many  
19 respects do not have parallels in this Article.

20 **SECTION 3-414. OBLIGATION OF DRAWER.**

21 **Proposed Comments**

22 7. The obligation of the drawer under this section is similar to the obligation of the drawer  
23 under Article 38 of the Convention on International Bills of Exchange and International

1 Promissory Notes.

2  
3  
4 **SECTION 3-415. OBLIGATION OF INDORSER.**

5  
6 **Proposed Comments**

7 6. The rule of this section is similar to the rule of Article 44 of the Convention on  
8 International Bills of Exchange and International Promissory Notes.

9  
10  
11 **SECTION 3-416. TRANSFER WARRANTIES.**

12 (a) A person who transfers an instrument for consideration warrants to the transferee and,  
13 if the transfer is by indorsement, to any subsequent transferee that:

14 (1) the warrantor is a person entitled to enforce the instrument;

15 (2) all signatures on the instrument are authentic and authorized;

16 (3) the instrument has not been altered;

17 (4) the instrument is not subject to a defense or claim in recoupment of any party

18 which can be asserted against the warrantor; ~~and~~

19 (5) the warrantor has no knowledge of any insolvency proceeding commenced with  
20 respect to the maker or acceptor or, in the case of an unaccepted draft, the ~~drawer;~~ drawer; and

21 (6) with respect to a remotely-created consumer item, that the person on whose  
22 account the item is drawn authorized the issuance of the item in the amount for which the item is  
23 drawn.

24 (b) A person to whom the warranties under subsection (a) are made and who took the  
25 instrument in good faith may recover from the warrantor as damages for breach of warranty an  
26 amount equal to the loss suffered as a result of the breach, but not more than the amount of the  
27

1 instrument plus expenses and loss of interest incurred as a result of the breach.  
2 (c) The warranties stated in subsection (a) cannot be disclaimed with respect to checks.  
3 Unless notice of a claim for breach of warranty is given to the warrantor within 30 days after the  
4 claimant has reason to know of the breach and the identity of the warrantor, the liability of the  
5 warrantor under subsection (b) is discharged to the extent of any loss caused by the delay in  
6 giving notice of the claim.  
7 (d) A [cause of action] for breach of warranty under this section accrues when the  
8 claimant has reason to know of the breach.

9 **Proposed Comments**

10 8. Subsection (a)(6) is based on a number of nonuniform amendments designed to address  
11 concerns about certain kinds of check fraud. The provision implements a limited rejection of  
12 Price v. Neal, 97 Eng. Rep. 871 (K.B. 1762), so that in certain circumstances (those involving  
13 remotely-created consumer checks) the payor bank can use a warranty claim to absolve itself of  
14 responsibility for honoring an unauthorized item. The provision rests on the premise that  
15 monitoring by depository banks can control this type of fraud more effectively than any practices  
16 readily available to payor banks. The provision expressly includes both the case in which the  
17 consumer does not authorize the item at all and also the case in which the consumer authorizes  
18 the item but in an amount different from the amount in which the item is drawn. Similar  
19 provisions appear in Sections 3-417, 4-207, and 4-208.

20 The provision supplements applicable federal law, which requires telemarketers who submit  
21 instruments for payment to obtain the customer's "express verifiable authorization," which may  
22 be either in writing or tape recorded and must be made available upon request to the customer's  
23 bank. Federal Trade Commission's Telemarketing Sales Rule, 16 C.F.R. § 310.3(a)(3),  
24 implementing the Telemarketing and Consumer Fraud and Abuse Prevention Act, 15 U.S.C. §§  
25 6101-6108. Some states also have consumer-protection laws governing authorization of  
26 instruments in telemarketing transactions. *See, e.g.*, 9 Vt. Stat. Ann. § 2464.

27  
28 9. Article 45 of the Convention on International Bills of Exchange and International  
29 Promissory Notes includes similar warranties.

30  
31 **SECTION 3-417. PRESENTMENT WARRANTIES.**  
32

33 (a) If an unaccepted draft is presented to the drawee for payment or acceptance and the

1 drawee pays or accepts the draft, (i) the person obtaining payment or acceptance, at the time of  
2 presentment, and (ii) a previous transferor of the draft, at the time of transfer, warrant to the  
3 drawee making payment or accepting the draft in good faith that:  
4 (1) the warrantor is, or was, at the time the warrantor transferred the draft, a person  
5 entitled to enforce the draft or authorized to obtain payment or acceptance of the draft on behalf  
6 of a person entitled to enforce the draft;  
7 (2) the draft has not been altered; ~~and~~  
8 (3) the warrantor has no knowledge that the signature of the drawer of the draft is  
9 ~~unauthorized; unauthorized; and~~  
10 (4) with respect to any remotely-created consumer item, that the person on whose  
11 account the item is drawn authorized the issuance of the item in the amount for which the item is  
12 drawn.  
13 (b) A drawee making payment may recover from any warrantor damages for breach of  
14 warranty equal to the amount paid by the drawee less the amount the drawee received or is  
15 entitled to receive from the drawer because of the payment. In addition, the drawee is entitled to  
16 compensation for expenses and loss of interest resulting from the breach. The right of the drawee  
17 to recover damages under this subsection is not affected by any failure of the drawee to exercise  
18 ordinary care in making payment. If the drawee accepts the draft, breach of warranty is a defense  
19 to the obligation of the acceptor. If the acceptor makes payment with respect to the draft, the  
20 acceptor is entitled to recover from any warrantor for breach of warranty the amounts stated in  
21 this subsection.  
22 (c) If a drawee asserts a claim for breach of warranty under subsection (a) based on an

1 unauthorized indorsement of the draft or an alteration of the draft, the warrantor may defend by  
2 proving that the indorsement is effective under Section 3-404 or 3-405 or the drawer is  
3 precluded under Section 3-406 or 4-406 from asserting against the drawee the unauthorized  
4 indorsement or alteration.

5 (d) If (i) a dishonored draft is presented for payment to the drawer or an indorser or (ii)  
6 any other instrument is presented for payment to a party obliged to pay the instrument, and (iii)  
7 payment is received, the following rules apply:

8 (1) The person obtaining payment and a prior transferor of the instrument warrant to  
9 the person making payment in good faith that the warrantor is, or was, at the time the warrantor  
10 transferred the instrument, a person entitled to enforce the instrument or authorized to obtain  
11 payment on behalf of a person entitled to enforce the instrument.

12 (2) The person making payment may recover from any warrantor for breach of  
13 warranty an amount equal to the amount paid plus expenses and loss of interest resulting from  
14 the breach.

15 (e) The warranties stated in subsections (a) and (d) cannot be disclaimed with respect to  
16 checks. Unless notice of a claim for breach of warranty is given to the warrantor within 30 days  
17 after the claimant has reason to know of the breach and the identity of the warrantor, the liability  
18 of the warrantor under subsection (b) or (d) is discharged to the extent of any loss caused by the  
19 delay in giving notice of the claim.

20 (f) A [cause of action] for breach of warranty under this section accrues when the  
21 claimant has reason to know of the breach.

22 **Proposed Comments**

1 9. For discussion of subsection (a)(4), see Comment 8 to Section 3-416.  
2  
3

4 **SECTION 3-419. INSTRUMENTS SIGNED FOR ACCOMMODATION.**

5 (a) If an instrument is issued for value given for the benefit of a party to the instrument  
6 (“accommodated party”) and another party to the instrument (“accommodation party”) signs the  
7 instrument for the purpose of incurring liability on the instrument without being a direct  
8 beneficiary of the value given for the instrument, the instrument is signed by the accommodation  
9 party “for accommodation.”

10 (b) An accommodation party may sign the instrument as maker, drawer, acceptor, or  
11 indorser and, subject to subsection (d), is obliged to pay the instrument in the capacity in which  
12 the accommodation party signs. The obligation of an accommodation party may be enforced  
13 notwithstanding any statute of frauds and whether or not the accommodation party receives  
14 consideration for the accommodation.

15 (c) A person signing an instrument is presumed to be an accommodation party and there  
16 is notice that the instrument is signed for accommodation if the signature is an anomalous  
17 indorsement or is accompanied by words indicating that the signer is acting as surety or guarantor  
18 with respect to the obligation of another party to the instrument. Except as provided in Section  
19 3-605, the obligation of an accommodation party to pay the instrument is not affected by the fact  
20 that the person enforcing the obligation had notice when the instrument was taken by that person  
21 that the accommodation party signed the instrument for accommodation.

22 (d) If the signature of a party to an instrument is accompanied by words indicating  
23 unambiguously that the party is guaranteeing collection rather than payment of the obligation of

1 another party to the instrument, the signer is obliged to pay the amount due on the instrument to a  
2 person entitled to enforce the instrument only if (i) execution of judgment against the other party  
3 has been returned unsatisfied, (ii) the other party is insolvent or in an insolvency proceeding, (iii)  
4 the other party cannot be served with process, or (iv) it is otherwise apparent that payment cannot  
5 be obtained from the other party.

6 (e) If the signature of a party to an instrument is accompanied by words indicating that the  
7 party guarantees payment or the signer signs the instrument as an accommodation party in some  
8 other manner that does not unambiguously indicate an intention to guarantee collection rather  
9 than payment, the signer is obliged to pay the amount due on the instrument to a person entitled  
10 to enforce the instrument in the same circumstances as the accommodated party would be  
11 obliged, without prior resort to the accommodated party by the person entitled to enforce the  
12 instrument.

13 (f) An accommodation party who pays the instrument is entitled to reimbursement from  
14 the accommodated party and is entitled to enforce the instrument against the accommodated  
15 party. In proper circumstances, an accommodation party may obtain relief that requires the  
16 accommodated party to perform its obligations on the instrument. An accommodated party who  
17 that pays the instrument has no right of recourse against, and is not entitled to contribution from,  
18 an accommodation party.

19  
20 **SECTION 3-502. DISHONOR.**

21 **Proposed Comments**

22  
23 The following should replace the first paragraph of comment 4:  
24

1 Subsection (b) applies to unaccepted drafts other than documentary drafts. Subsection (b)(1)  
2 applies to checks. Except for checks presented for immediate payment over the counter, which  
3 are covered by subsection (b)(2), dishonor occurs according to rules stated in Article 4. Those  
4 rules contemplate four separate situations that warrant discussion. The first two situations arise  
5 in the normal course of affairs, in which the drawee bank makes settlement for the amount of the  
6 check to the presenting bank. In the first situation, the drawee bank under Section 4-301 recovers  
7 this settlement if it returns the check by its midnight deadline (Section 4-104). In that case the  
8 check is not paid and dishonor occurs under Section 3-502(b)(1). The second situation arises if  
9 the drawee bank has made such a settlement and does not return the check or give notice of  
10 dishonor or nonpayment within the midnight deadline. In that case, the settlement becomes final  
11 payment of the check under Section 4-215. Thus, no dishonor occurs regardless of whether the  
12 drawee bank retains the check indefinitely or for some reason returns the check after its midnight  
13 deadline.

14  
15 The third and fourth situations arise less commonly, in cases in which the drawee bank does  
16 not settle for the check when it is received. Under Section 4-302 if the drawee bank is not also  
17 the depository bank and retains the check without settling for it beyond midnight of the day it is  
18 presented for payment, the bank at that point becomes "accountable" for the amount of the check,  
19 i.e., it is obliged to pay the amount of the check. If the drawee bank is also the depository bank,  
20 the bank becomes accountable for the amount of the check if the bank does not pay the check or  
21 return it or send notice of dishonor by its midnight deadline. Hence, if the drawee bank is also  
22 the depository bank and does not either settle for the check when it is received (a settlement that  
23 would ripen into final payment if the drawee bank failed to take action to recover the settlement  
24 by its midnight deadline) or return the check or an appropriate notice by its midnight deadline,  
25 the drawee bank will become accountable for the amount of the check under Section 4-302.  
26 Thus, in all cases in which the drawee bank becomes accountable under Section 4-302, the check  
27 has not been paid (either by a settlement that became unrecoverable or otherwise) and thus, under  
28 Section 3-502(b)(1), the check is dishonored.  
29

30 The fact that a bank that is accountable for the amount of the check under Section 4-302 is  
31 obliged to pay the check under Section 3-502(b) does not mean that the check has been paid.  
32 Indeed, because each of the paragraphs of Section 4-302(b) is limited by its terms to situations in  
33 which a bank has not paid the item, a drawee bank will be accountable under Section 4-302 only  
34 in situations in which it has not previously paid the check. Section 3-502(b)(1) reflects the view  
35 that a person presenting a check is entitled to payment, not just the ability to hold the drawee  
36 accountable under Section 4-302. If that payment is not made in a timely manner, the check is  
37 dishonored.  
38

39 **SECTION 3-602. PAYMENT.**

40  
41 (a) Subject to subsection ~~(b)~~; (e), an instrument is paid to the extent payment is made~~(f)~~

1 by or on behalf of a party obliged to pay the instrument, and~~(ii)~~ to a person entitled to enforce the  
2 instrument.

3 (b) Subject to subsection (e) a note is paid to the extent payment is made by or on behalf  
4 of a party obliged to pay the note to a person that formerly was entitled to enforce the note only if  
5 at the time of the payment the party obliged to pay has not received adequate notification that the  
6 note has been transferred and that payment is to be made to the transferee. A notification is  
7 adequate only if it is signed by the transferor or the transferee, reasonably identifies the  
8 transferred note; and provides an address at which payments subsequently can be made. Upon  
9 request, a transferee shall seasonably furnish reasonable proof that the note has been transferred.  
10 Unless the transferee complies with the request, a payment to the person that formerly was  
11 entitled to enforce the note is effective for purposes of subsection (c) even if the party obliged to  
12 pay the note has received a notification under this paragraph.

13 (c) Subject to subsection (e), to the extent of the payment, a payment under subsections  
14 (a) and (b), the obligation of the party obliged to pay the instrument is discharged even though  
15 payment is made with knowledge of a claim to the instrument under Section 3-306 by another  
16 person.

17 (d) Subject to subsection (e), a transferee, or any party that has acquired rights in the  
18 instrument directly or indirectly from a transferee, including any such party that has rights as a  
19 holder in due course, is deemed to have notice of any payment that is made under subsection (b)  
20 after the date that the note is transferred to the transferee but before the party obliged to pay the  
21 note receives adequate notification of the transfer.

22 ~~(b)~~ (e) The obligation of a party to pay the instrument is not discharged under ~~subsection~~

1 ~~(a)~~ subsections (a) through (d) if:

2 (1) a claim to the instrument under Section 3-306 is enforceable against the party  
3 receiving payment and (i) payment is made with knowledge by the payor that payment is  
4 prohibited by injunction or similar process of a court of competent jurisdiction, or (ii) in the case  
5 of an instrument other than a cashier's check, teller's check, or certified check, the party making  
6 payment accepted, from the person having a claim to the instrument, indemnity against loss  
7 resulting from refusal to pay the person entitled to enforce the instrument; or

8 (2) the person making payment knows that the instrument is a stolen instrument and  
9 pays a person it knows is in wrongful possession of the instrument.

10 (f) As used in this section, "signed," with respect to a record that is not a writing, includes  
11 the attachment to or logical association with the record of an electronic symbol, sound, or process  
12 to or with the record with the present intent to adopt or accept the record.

#### Proposed Comments

13 [Change existing comment to comment 1.]  
14  
15  
16

17 2. Subsection (a) covers payments made in a traditional manner, to the person entitled to  
18 enforce the instrument. Subsection (b) deals with the situation in which a person entitled to  
19 enforce the instrument transfers the instrument without giving notice to parties obligated to pay  
20 the instrument. If that happens and one of those parties subsequently makes a payment to the  
21 transferor, the payment is effective even though it is not made to the person entitled to enforce  
22 the instrument. Unlike the earlier version of Section 3-602, this rule is consistent with Section 9-  
23 406(a), Restatement of Mortgages § 5.5, and Restatement of Contracts § 338(1).  
24

25 3. In determining the party to whom a payment is made for purposes of this section, courts  
26 should look to traditional rules of agency. Thus, if the original payee of a note transfers  
27 ownership of the note to a third party but continues to service the obligation, the law of agency  
28 might treat payments made to the original payee as payments made to the third party.  
29  
30

1           **SECTION 3-604. DISCHARGE BY CANCELLATION OR RENUNCIATION.**

2           (a) A person entitled to enforce an instrument, with or without consideration, may  
3 discharge the obligation of a party to pay the instrument (i) by an intentional voluntary act, such  
4 as surrender of the instrument to the party, destruction, mutilation, or cancellation of the  
5 instrument, cancellation or striking out of the party's signature, or the addition of words to the  
6 instrument indicating discharge, or (ii) by agreeing not to sue or otherwise renouncing rights  
7 against the party by a signed ~~writing~~ record.

8           (b) Cancellation or striking out of an indorsement pursuant to subsection (a) does not  
9 affect the status and rights of a party derived from the indorsement.

10           (c) As used in this section, "signed," with respect to a record that is not a writing,  
11 includes the attachment to or logical association with the record of an electronic symbol, sound,  
12 or process to or with the record with the present intent to adopt or accept the record.

13  
14  
15           **SECTION 3-605. DISCHARGE OF SECONDARY OBLIGORS, ~~DISCHARGE OF~~**  
16 **~~INDORSERS AND ACCOMMODATION PARTIES.~~**

17           (a) If a person entitled to enforce an instrument releases the obligation of a principal  
18 obligor in whole or in part, and another party to the instrument is a secondary obligor with  
19 respect to the obligation of that principal obligor, the following rules apply:

20           (1) Any obligations of the principal obligor to the secondary obligor with respect to  
21 any previous payment by the secondary obligor are not affected. Unless the terms of the release  
22 preserve the secondary obligor's recourse, the principal obligor is discharged, to the extent of the  
23 release, from any other duties to the secondary obligor under this article.

1           (2) Unless the terms of the release provide that the person entitled to enforce the  
2 instrument retains the right to enforce the instrument against the secondary obligor, the secondary  
3 obligor is discharged to the same extent as the principal obligor from any unperformed portion of  
4 its obligation on the instrument. If the instrument is a check and the obligation of the secondary  
5 obligor is based on an indorsement of the check, the secondary obligor is discharged without  
6 regard to the language or circumstances of the discharge or other release.

7           (3) If the secondary obligor is not discharged under paragraph (2), the secondary  
8 obligor is discharged to the extent of the value of the consideration for the release, and to the  
9 extent that the release would otherwise cause the secondary obligor a loss.

10           (b) If a person entitled to enforce an instrument grants a principal obligor an extension of  
11 the time at which one or more payments are due on the instrument and another party to the  
12 instrument is a secondary obligor with respect to the obligation of that principal obligor, the  
13 following rules apply:

14           (1) Any obligations of the principal obligor to the secondary obligor with respect to  
15 any previous payment by the secondary obligor are not affected. Unless the terms of the  
16 extension preserve the secondary obligor's recourse, the extension correspondingly extends the  
17 time for performance of any other duties owed to the secondary obligor by the principal obligor  
18 under this article.

19           (2) The secondary obligor is discharged to the extent that the extension would  
20 otherwise cause the secondary obligor a loss.

21           (3) To the extent that the secondary obligor is not discharged under paragraph (2), the  
22 secondary obligor may perform its obligations to a person entitled to enforce the instrument as if

1 the time for payment had not been extended or, unless the terms of the extension provide that the  
2 person entitled to enforce the instrument retains the right to enforce the instrument against the  
3 secondary obligor as if the time for payment had not been extended, treat the time for  
4 performance of its obligations as having been extended correspondingly.

5 (c) If a person entitled to enforce an instrument agrees, with or without consideration, to a  
6 modification of the obligation of a principal obligor other than a complete or partial release or an  
7 extension of the due date and another party to the instrument is a secondary obligor with respect  
8 to the obligation of that principal obligor, the following rules apply:

9 (1) Any obligations of the principal obligor to the secondary obligor with respect to  
10 any previous payment by the secondary obligor are not affected. The modification  
11 correspondingly modifies any other duties owed to the secondary obligor by the principal obligor  
12 under this article.

13 (2) The secondary obligor is discharged from any unperformed portion of its  
14 obligation to the extent that the modification would otherwise cause the secondary obligor a loss.

15 (3) To the extent that the secondary obligor is not discharged under paragraph (2), the  
16 secondary obligor may satisfy its obligation on the instrument as if the modification had not  
17 occurred, or treat its obligation on the instrument as having been modified correspondingly.

18 (d) If the obligation of a principal obligor is secured by an interest in collateral, another  
19 party to the instrument is a secondary obligor with respect to that obligation, and a person  
20 entitled to enforce the instrument impairs the value of the interest in collateral, the obligation of  
21 the secondary obligor is discharged to the extent of the impairment. The value of an interest in  
22 collateral is impaired to the extent the value of the interest is reduced to an amount less than the

1 amount of the recourse of the secondary obligor, or the reduction in value of the interest causes  
2 an increase in the amount by which the amount of the recourse exceeds the value of the interest.  
3 For purposes of this subsection, impairing the value of an interest in collateral includes failure to  
4 obtain or maintain perfection or recordation of the interest in collateral, release of collateral  
5 without substitution of collateral of equal value or equivalent reduction of the underlying  
6 obligation, failure to perform a duty to preserve the value of collateral owed, under Article 9 or  
7 other law, to a debtor or other person secondarily liable, and failure to comply with applicable  
8 law in disposing of or otherwise enforcing the interest in collateral.

9 (e) A secondary obligor is not discharged under subsection (a)(3), (b), (c), or (d) unless  
10 the person entitled to enforce the instrument knows that the person is a secondary obligor or has  
11 notice under Section 3-419(c) that the instrument was signed for accommodation.

12 (f) A secondary obligor is not discharged under this section if the secondary obligor  
13 consents to the event or conduct that is the basis of the discharge, or the instrument or a separate  
14 agreement of the party provides for waiver of discharge under this section specifically or by  
15 general language indicating that parties waive defenses based on suretyship or impairment of  
16 collateral. Unless the circumstances indicate otherwise, consent by the principal obligor to an act  
17 that would lead to a discharge under this section constitutes consent to that act by the secondary  
18 obligor if the secondary obligor controls the principal obligor or deals with the person entitled to  
19 enforce the instrument on behalf of the principal obligor.

20 (g) A release or extension preserves a secondary obligor's recourse if the terms of the  
21 release or extension provide that the person entitled to enforce the instrument retains the right to  
22 enforce the instrument against the secondary obligor; and the recourse of the secondary obligor

1 ~~continues as though the release or extension had not been granted.~~

2 ~~(h) Except as otherwise provided in subsection (i), a secondary obligor asserting~~  
3 ~~discharge under this section has the burden of persuasion both with respect to the occurrence of~~  
4 ~~the acts alleged to harm the secondary obligor and loss or prejudice caused by those acts.~~

5 ~~(i) If the secondary obligor demonstrates prejudice caused by an impairment of its~~  
6 ~~recourse, and the circumstances of the case indicate that the amount of loss is not reasonably~~  
7 ~~susceptible of calculation or requires proof of facts that are not ascertainable, it is presumed that~~  
8 ~~the act impairing recourse caused a loss or impairment equal to the liability of the secondary~~  
9 ~~obligor on the instrument. In that event, the burden of persuasion as to any lesser amount of the~~  
10 ~~loss is on the person entitled to enforce the instrument.~~

11 ~~(a) In this section, the term "indorser" includes a drawer having the obligation described~~  
12 ~~in Section 3-414(d);~~

13 ~~(b) Discharge, under Section 3-604, of the obligation of a party to pay an instrument does~~  
14 ~~not discharge the obligation of an indorser or accommodation party having a right of recourse~~  
15 ~~against the discharged party;~~

16 ~~(c) If a person entitled to enforce an instrument agrees, with or without consideration, to~~  
17 ~~an extension of the due date of the obligation of a party to pay the instrument, the extension~~  
18 ~~discharges an indorser or accommodation party having a right of recourse against the party whose~~  
19 ~~obligation is extended to the extent the indorser or accommodation party proves that the~~  
20 ~~extension caused loss to the indorser or accommodation party with respect to the right of~~  
21 ~~recourse;~~

22 ~~(d) If a person entitled to enforce an instrument agrees, with or without consideration, to a~~

1 ~~material modification of the obligation of a party other than an extension of the due date, the~~  
2 ~~modification discharges the obligation of an indorser or accommodation party having a right of~~  
3 ~~recourse against the person whose obligation is modified to the extent the modification causes~~  
4 ~~loss to the indorser or accommodation party with respect to the right of recourse. The loss~~  
5 ~~suffered by the indorser or accommodation party as a result of the modification is equal to the~~  
6 ~~amount of the right of recourse unless the person enforcing the instrument proves that no loss~~  
7 ~~was caused by the modification or that the loss caused by the modification was an amount less~~  
8 ~~than the amount of the right of recourse.~~

9 ~~(e) If the obligation of a party to pay an instrument is secured by an interest in collateral~~  
10 ~~and a person entitled to enforce the instrument impairs the value of the interest in collateral, the~~  
11 ~~obligation of an indorser or accommodation party having a right of recourse against the obligor is~~  
12 ~~discharged to the extent of the impairment. The value of an interest in collateral is impaired to~~  
13 ~~the extent (i) the value of the interest is reduced to an amount less than the amount of the right of~~  
14 ~~recourse of the party asserting discharge, or (ii) the reduction in value of the interest causes an~~  
15 ~~increase in the amount by which the amount of the right of recourse exceeds the value of the~~  
16 ~~interest. The burden of proving impairment is on the party asserting discharge;~~

17 ~~(f) If the obligation of a party is secured by an interest in collateral not provided by an~~  
18 ~~accommodation party and a person entitled to enforce the instrument impairs the value of the~~  
19 ~~interest in collateral, the obligation of any party who is jointly and severally liable with respect to~~  
20 ~~the secured obligation is discharged to the extent the impairment causes the party asserting~~  
21 ~~discharge to pay more than that party would have been obliged to pay, taking into account rights~~  
22 ~~of contribution, if impairment had not occurred. If the party asserting discharge is an~~

1 accommodation party not entitled to discharge under subsection (c), the party is deemed to have a  
2 right to contribution based on joint and several liability rather than a right to reimbursement. The  
3 burden of proving impairment is on the party asserting discharge.

4 ~~(g) Under subsection (c) or (f), impairing value of an interest in collateral includes (i)~~  
5 ~~failure to obtain or maintain perfection or recordation of the interest in collateral, (ii) release of~~  
6 ~~collateral without substitution of collateral of equal value, (iii) failure to perform a duty to~~  
7 ~~preserve the value of collateral owed, under Article 9 or other law, to a debtor or surety or other~~  
8 ~~person secondarily liable, or (iv) failure to comply with applicable law in disposing of collateral.~~

9 (h) An accommodation party is not discharged under subsection (c), (d), or (e) unless the  
10 person entitled to enforce the instrument knows of the accommodation or has notice under  
11 Section 3-419(c) that the instrument was signed for accommodation.

12 (i) ~~A party is not discharged under this section if (i) the party asserting discharge consents~~  
13 ~~to the event or conduct that is the basis of the discharge, or (ii) the instrument or a separate~~  
14 ~~agreement of the party provides for waiver of discharge under this section either specifically or~~  
15 ~~by general language indicating that parties waive defenses based on suretyship or impairment of~~  
16 ~~collateral.~~

#### 17 Proposed Comments

18 The following should be substituted for the existing comments.

19 1. This section contains rules that are applicable when a secondary obligor (as defined in  
20 Section 3-103(a)(17)) is a party to an instrument. These rules essentially parallel modern  
21 interpretations of the law of suretyship and guaranty that apply when a secondary obligor is not a  
22 party to an instrument. See generally *Restatement of the Law, Third, Suretyship and Guaranty*  
23 (1996).

24 2. Like the law of suretyship and guaranty, Section 3-605 provides secondary obligors with  
25  
26  
27

1 defenses that are not available to other parties to instruments. The general operation of Section  
2 3-605, and its relationship to the law of suretyship and guaranty, can be illustrated by an  
3 example. Bank agrees to lend \$10,000 to Borrower, but only if Backer also is liable for  
4 repayment of the loan. The parties could consummate that transaction in three different ways.  
5 First, if Borrower and Backer incurred those obligations with contracts not governed by this  
6 Article, the general law of suretyship and guaranty would be applicable. Under modern  
7 nomenclature, Bank is the “obligee,” Borrower is the “principal obligor,” and Backer is the  
8 “secondary obligor.” See *Restatement of Suretyship and Guaranty* §1. Then assume that Bank  
9 and Borrower agree to a modification of their rights and obligations after the note is signed. For  
10 example, they might agree that Borrower may repay the loan at some date after the due date, or  
11 that Borrower may discharge its repayment obligation by paying Bank \$3,000 rather than  
12 \$10,000. Alternatively, suppose that Bank releases collateral that Borrower has given to secure  
13 the loan. Under the law of suretyship and guaranty, the secondary obligor may be discharged  
14 under certain circumstances if these modifications of the obligations between Bank (the obligee)  
15 and Borrower (the principal obligor) are made without the consent of Backer (the secondary  
16 obligor). The rights that the secondary obligor has to a discharge of its liability in such cases  
17 commonly are referred to as suretyship defenses. The extent of the discharge depends upon the  
18 particular circumstances. See *Restatement of Suretyship and Guaranty* §§ 37, 39-44.

19  
20 A second possibility is that the parties might decide to use a negotiable instrument to  
21 effectuate the loan. In that scenario, Borrower signs a note under which Borrower is obliged to  
22 pay \$10,000 to the order of Bank on a due date stated in the note. Backer becomes liable for the  
23 repayment obligation by signing the note as a co-maker or indorser. In either case the note is  
24 signed for accommodation, Backer is an accommodation party, and Borrower is the  
25 accommodated party. See Section 3-419 (describing the obligations of accommodation parties).  
26 For purposes of Section 3-605, Backer is also a “secondary obligor” and Borrower is a “principal  
27 obligor,” as those terms are defined in Section 3-103. Because Backer is a party to the  
28 instrument, its rights to a discharge based on any modification of obligations between Bank and  
29 Borrower are governed by Section 3-605 rather than by the general law of suretyship and  
30 guaranty. Within Section 3-605, subsection (a) describes the consequences of a release of  
31 Borrower, subsection (b) describes the consequences of an extension of time, and subsection (c)  
32 describes the consequences of other modifications.

33  
34 The third possibility is that Borrower would use an instrument governed by this Article to  
35 evidence its repayment obligation, but Backer’s obligation would be created in some way other  
36 than by becoming party to that instrument. In that case, Backer’s rights are determined by  
37 suretyship and guaranty law rather than by this Article. See Comment 3 to Section 3-419.

38  
39 Secondary liability also often arises in connection with a note in a transaction that does not  
40 involve a secondary obligor at the time that the principal obligation is created, where there is  
41 subsequently a transfer of the collateral that is given to secure the obligation of the principal  
42 obligor to repay the note. That occurs under the rule that a transferee of real or personal property  
43 that assumes the obligation of the transferor as maker of a note secured by the property becomes

1 by operation of law a principal obligor, with the transferor becoming a secondary obligor.  
2 *Restatement of Suretyship and Guaranty* § 2(e); *Restatement of Mortgages* § 5.1. Article 3 does  
3 not determine the effect of the release of the transferee in that case because the assuming  
4 transferee is not a “party” to the instrument as defined in Section 3-103(a)(10). Section 3-605(a)  
5 does not apply then because the holder has not discharged the obligation of a “principal obligor,”  
6 a term defined in Section 3-103(a)(11). Thus, the resolution of that question is governed by the  
7 law of suretyship. See *Restatement of Suretyship and Guaranty* § 39.

8  
9 3. Section 3-605 is not however, limited to the conventional situation of the accommodation  
10 party discussed in Comment 2. It also applies in four other situations. First, it applies to  
11 indorsers of notes who are not accommodation parties. Unless an indorser signs without  
12 recourse, the indorser’s liability under Section 3-415(a) is functionally similar to that of a  
13 guarantor of payment. For example, if Bank in the hypothetical discussed in Comment 2  
14 indorsed the note and transferred it to Second Bank, Bank is liable to Second Bank in the event  
15 of dishonor of the note by Borrower. Section 3-415(a). Because of that secondary liability as  
16 indorser, Bank qualifies as a “secondary obligor” under Section 3-103(a)(17) and has the same  
17 rights under Section 3-605 as an accommodation party.

18  
19 Second, a similar analysis applies to the drawer of a draft that is accepted by a party that is  
20 not a bank. Under Section 3-414(d), that drawer has liability on the same terms as an indorser  
21 under Section 3-415(a). Thus, the drawer in that case is a “secondary obligor” under Section 3-  
22 103(a)(17) and has rights under Section 3-605 to that extent.

23  
24 Third, a similar principle justifies application of Section 3-605 to persons who indorse a  
25 check. Assume that Drawer draws a check to the order of Payee. Payee then indorses the check  
26 and transfers it to Transferee. If Transferee presents the check and it is dishonored, Transferee  
27 may recover from Drawer under Section 3-414 or Payee under Section 3-415. Because of that  
28 secondary liability as an indorser, Payee is a secondary obligor under Section 3-103(a)(17).  
29 Drawer is a “principal obligor” under Section 3-103(a)(11). As noted in Comment 4, below,  
30 however, Section 3-605(a)(3) will discharge indorsers of checks in some cases in which other  
31 secondary obligors will not be discharged by this section.

32  
33 Fourth, this section also deals with the rights of co-makers of instruments, even when those  
34 co-makers do not qualify as accommodation parties. The co-makers’ rights of contribution under  
35 Section 3-116 make each co-maker a secondary obligor to the extent of that right of contribution.

36  
37 4. Subsection (a) is based on *Restatement of Suretyship and Guaranty* § 39. It addresses the  
38 effects of a release of the principal obligor by the person entitled to enforce the instrument.  
39 Paragraph (a)(1) governs the effect of that release on the principal obligor’s duties to the  
40 secondary obligor; paragraphs (a)(2) and (a)(3) govern the effect of that release on the secondary  
41 obligor’s duties to the person entitled to enforce the instrument.

42  
43 With respect to the duties of the principal obligor, the release of course cannot affect

1 obligations of the principal obligor with respect to payments that the secondary obligor already  
2 has made. But with respect to future payments by the secondary obligor, paragraph (a)(1) (based  
3 on *Restatement of Suretyship and Guaranty* § 39(a)) provides that the principal obligor is  
4 discharged, to the extent of the release, from any other duties to the secondary obligor. That rule  
5 is appropriate because otherwise the discharge granted to the principal obligor would be illusory:  
6 it would have obtained a release from a person entitled to enforce that instrument, but it would be  
7 directly liable for the same sum to the secondary obligor if the secondary obligor later complied  
8 with its secondary obligation to pay the instrument. This discharge does not occur, though, if the  
9 terms of the release effect a “preservation of recourse” as described in subsection (g). See  
10 Comment 10, below.

11  
12 The discharge under paragraph (a)(1) of the principal obligor’s duties to the secondary  
13 obligor is broad, applying to all duties under this article. This includes not only the principal  
14 obligor’s liability as a party to an instrument (as a maker, drawer or indorser under Sections 3-  
15 412 through 3-415) but also obligations under Sections 3-116 and 3-419.

16  
17 Paragraph (a)(2) is based closely on *Restatement of Suretyship and Guaranty* § 39(b). It  
18 articulates a default rule that the release of a principal obligor also discharges the secondary  
19 obligor, to the extent of the release granted to the principal obligor, from any unperformed  
20 portion of its obligation on the instrument. The discharge of the secondary obligor under  
21 paragraph (a)(2) is phrased more narrowly than the discharge of the principal obligor is phrased  
22 under paragraph (a)(1) because, unlike principal obligors, the only obligations of secondary  
23 obligors in Article 3 are “on the instrument” as makers or indorsers.

24  
25 The parties can opt out of that rule by including a contrary statement in the terms of the  
26 release. The provision does not contemplate that any “magic words” are necessary. Thus,  
27 discharge of the secondary obligor under paragraph (a)(2) is avoided not only if the terms of the  
28 release track the statutory language (e.g., the person entitled to enforce the instrument “retains the  
29 right to enforce the instrument” against the secondary obligor), or if the terms of the release  
30 effect a preservation of recourse under subsection (g), but also if the terms of the release include  
31 a simple statement that the parties intend to “release the principal obligor but not the secondary  
32 obligor” or that the person entitled to enforce the instrument “reserves its rights” against the  
33 secondary obligor. At the same time, because paragraph (a)(2) refers to the “terms of the  
34 release,” extrinsic circumstances cannot be used to establish that the parties intended the  
35 secondary obligor to remain obligated. If a release of the principal obligor includes such a  
36 provision, the secondary obligor is, nonetheless, discharged to the extent of the consideration that  
37 is paid for the release; that consideration is treated as a payment in partial satisfaction of the  
38 instrument.

39  
40 Notwithstanding language in the release that prevents discharge of the secondary obligor  
41 under paragraph (a)(2), paragraph (a)(3) discharges the secondary obligor from its obligation to a  
42 person entitled to enforce the instrument to the extent that the release otherwise would cause the  
43 secondary obligor a loss. The rationale for that provision is that a release of the principal obligor

1 changes the economic risk for which the secondary obligor contracted. This risk may be  
2 increased in two ways. First, by releasing the principal obligor, the person entitled to enforce the  
3 instrument has eliminated the likelihood of future payments by the principal obligor that would  
4 lessen the obligation of the secondary obligor. Second, unless the release effects a preservation  
5 of the secondary obligor's recourse, the release eliminates the secondary obligor's claims against  
6 the principal obligor with respect to any future payment by the secondary obligor. The discharge  
7 provided by this paragraph prevents that increased risk from causing the secondary obligor a loss.  
8 Moreover, permitting releases to be negotiated between the principal obligor and the person  
9 entitled to enforce the instrument without regard to the consequences to the secondary obligor  
10 would create an undue risk of opportunistic behavior by the obligee and principal obligor. That  
11 concern is lessened, and the discharge is not provided by paragraph (a)(3), if the secondary  
12 obligor has consented to the release or is deemed to have consented to it under subsection (f)  
13 (which presumes consent by a secondary obligor to actions taken by a principal obligor if the  
14 secondary obligor controls the principal obligor or deals with the person entitled to enforce the  
15 instrument on behalf of the principal obligor). See Comment 9, below.

16 Subsection (a) (and Restatement Section 39(b), the concepts of which it follows quite  
17 closely) is designed to facilitate negotiated workouts between a creditor and a principal obligor,  
18 so long as they are not at the expense of a secondary obligor who has not consented to the  
19 arrangement (either specifically or by waiving its rights to discharge under this section). Thus,  
20 for example, the provision facilitates an arrangement in which the principal obligor pays some  
21 portion of a guaranteed obligation, the person entitled to enforce the instrument grants a release  
22 to the principal obligor in exchange for that payment, and the person entitled to enforce the  
23 instrument pursues the secondary obligor for the remainder of the obligation. Under paragraph  
24 (a)(2), the person entitled to enforce the instrument may pursue the secondary obligor despite the  
25 release of the principal obligor so long as the terms of the release provide for this result. Under  
26 paragraph (a)(3), though, the secondary obligor will be protected against any loss it might suffer  
27 by reason of that release (if the secondary obligor has not waived discharge under subsection (f)).  
28 It should be noted that the obligee may be able to minimize the risk of such loss (and, thus, of  
29 the secondary obligor's discharge) by giving the secondary obligor prompt notice of the release  
30 even though such notice is not required.

31 The foregoing principles are illustrated by the following cases:  
32

33 *Case 1.* D borrows \$1000 from C. The repayment obligation is evidenced by a note issued  
34 by D, payable to the order of C. S is an accommodation indorser of the note. As the due date  
35 of the note approaches, it becomes obvious that D cannot pay the full amount of the note and  
36 may soon be facing bankruptcy. C, in order to collect as much as possible from D and lessen  
37 the need to seek recovery from S, agrees to release D from its obligation under the note in  
38 exchange for \$100 in cash. The agreement to release D is silent as to the effect of the release  
39 on S. Pursuant to Section 3-605(a)(2), the release of D discharges S from its obligations to C  
40 on the note.  
41  
42  
43

1 *Case 2.* Same facts as Case 1, except that the terms of the release provide that C retains its  
2 rights to enforce the instrument against S. D is discharged from its obligations to S pursuant  
3 to Section 3-605(a)(1), but S is not discharged from its obligations to C pursuant to Section  
4 3-605(a)(2). However, if S could have recovered from D any sum it paid to C (had D not  
5 been discharged from its obligation to S), S has been harmed by the release and is discharged  
6 pursuant to Section 3-605(a)(3) to the extent of that harm.  
7

8 *Case 3.* Same facts as Case 1, except that the terms of the release provide that C retains its  
9 rights to enforce the instrument against S and that S retains its recourse against D. Under  
10 subsection (g), the release effects a preservation of recourse. Thus, S is not discharged from  
11 its obligations to C pursuant to Section 3-605(a)(2) and D is not discharged from its  
12 obligations to S pursuant to Section 3-605(a)(1). Because S's claims against D are preserved,  
13 S will not suffer the kind of loss described in Case 2. If no other loss is suffered by S as a  
14 result of the release, S is not discharged pursuant to this section.  
15

16 *Case 4.* Same facts as Case 3, except that D had made arrangements to work at a second job  
17 in order to earn the money to fulfill its obligations on the note. When C released D, however,  
18 D canceled the plans for the second job. While S still retains its recourse against D, S may be  
19 discharged from its obligation under the instrument to the extent that D's decision to forgo  
20 the second job causes S a loss because forgoing the job renders D unable to fulfill its  
21 obligations to S under Section 3-419.  
22

23 Subsection (a) reflects a change from former Section 3-605(b), which provided categorically  
24 that the release of a principal obligor by the person entitled to enforce the instrument did not  
25 discharge a secondary obligor's obligation on the instrument and assumed that the release also  
26 did not discharge the principal obligor's obligations to the secondary obligor under Section 3-  
27 419. The rule under subsection (a) is much closer to the policy of the *Restatement of Suretyship*  
28 *and Guaranty* than was former Section 3-605(b). The change, however, is likely to affect only a  
29 narrow category of cases. First, as discussed above, Section 3-605 applies only to transactions in  
30 which the payment obligation is represented by a negotiable instrument, and, within that set of  
31 transactions, only to those transactions in which the secondary obligation is incurred by  
32 indorsement or cosigning, not to transactions that involve a separate document of guaranty. See  
33 Comment 2, above. Second, as provided in subsection (f), secondary obligors cannot obtain a  
34 discharge under subsection (a) in any transaction in which they have consented to the challenged  
35 conduct. Thus, subsection (a) will not apply to any transaction that includes a provision waiving  
36 suretyship defenses (a provision that is almost universally included in commercial loan  
37 documentation) or to any transaction in which the creditor obtains the consent of the secondary  
38 obligor at the time of the release.  
39

40 The principal way in which subsection (a) goes beyond the policy of *Restatement* § 39 is with  
41 respect to the liability of indorsers of checks. Specifically, the last sentence of paragraph (a)(2)  
42 provides that a release of a principal obligor grants a complete discharge to the indorser of a  
43 check, without requiring the indorser to prove harm. In that particular context, it seems likely

1 that continuing responsibility for the indorser often would be so inconsistent with the  
2 expectations of the parties as to create a windfall for the creditor and an unfair surprise for the  
3 indorser. Thus, the statute implements a simple rule that grants a complete discharge. The  
4 creditor, of course, can avoid that rule by contracting with the secondary obligor for a different  
5 result at the time that the creditor grants the release to the principal obligor.  
6

7 5. Subsection (b) is based on *Restatement of Suretyship and Guaranty* § 40 and relates to  
8 extensions of the due date of the instrument. An extension of time to pay a note is often  
9 beneficial to the secondary obligor because the additional time may enable the principal obligor  
10 to obtain the funds to pay the instrument. In some cases, however, the extension may cause loss  
11 to the secondary obligor, particularly if deterioration of the financial condition of the principal  
12 obligor reduces the amount that the secondary obligor is able to recover on its right of recourse  
13 when default occurs. For example, suppose that the instrument is an installment note and the  
14 principal debtor is temporarily short of funds to pay a monthly installment. The payee agrees to  
15 extend the due date of the installment for a month or two to allow the debtor to pay when funds  
16 are available. Paragraph (b)(2) provides that an extension of time results in a discharge of the  
17 secondary obligor, but only to the extent that the secondary obligor proves that the extension  
18 caused loss. See subsection (h) (discussing the burden of proof under Section 3-605). Thus, if  
19 the extension is for a long period, the secondary obligor might be able to prove that during the  
20 period of extension the principal obligor became insolvent, reducing the value of the right of  
21 recourse of the secondary obligor. In such a case, paragraph (b)(2) discharges the secondary  
22 obligor to the extent of that harm. Although not required to notify the secondary obligor of the  
23 extension, the payee can minimize the risk of loss by the secondary obligor by giving the  
24 secondary obligor prompt notice of the extension; prompt notice can enhance the likelihood that  
25 the secondary obligor's right of recourse can remain valuable, and thus can limit the likelihood  
26 that the secondary obligor will suffer a loss because of the extension. See *Restatement of*  
27 *Suretyship and Guaranty* Section 38 comment b.  
28

29 If the secondary obligor is not discharged under paragraph (b)(2) (either because it would not  
30 suffer a loss by reason of the extension or because it has waived its right to discharge pursuant to  
31 subsection (f)), it is important to understand the effect of the extension on the rights and  
32 obligations of the secondary obligor. Consider the following cases:  
33

34 *Case # 5.* A borrows money from Lender and issues a note payable to the order of Lender  
35 that is due on April 1, 2002. B signs the note for accommodation at the request of Lender. B  
36 signed the note either as co-maker or as an anomalous indorser. In either case Lender  
37 subsequently makes an agreement with A extending the due date of A's obligation to pay the  
38 note to July 1, 2002. In either case B did not agree to the extension, and the extension did not  
39 address Lender's rights against B. Under paragraph (b)(1), A's obligations to B under this  
40 article are also extended to July 1, 2002. Under paragraph (b)(3), if B is not discharged, B  
41 may treat its obligations to Lender as also extended, or may pay the instrument on the original  
42 due date.  
43

1 *Case # 6.* Same facts as Case # 5, except that the extension agreement includes a statement  
2 that the Lender retains its right to enforce the note against B on its original terms. Under  
3 paragraph (b)(3), B is liable on the original due date, but under paragraph (b)(1) A's  
4 obligations to B under Section 3-419 are not due until July 1, 2002.  
5

6 *Case #7.* Same facts as Case #5, except that the extension agreement includes a statement  
7 that the Lender retains its right to enforce the note against B on its original terms and B  
8 retains its recourse against A as though no extension had been granted. Under paragraph  
9 (b)(3), B is liable on the original due date. Under paragraph (b)(1), A's obligations to B  
10 under Section 3-419 are not extended.  
11

12 Under section 3-605(b), the results in Case #5 and Case #7 are identical to the results that  
13 follow from the law of suretyship and guaranty. See *Restatement of Suretyship and Guaranty* §  
14 40. The situation in Case #6 is not specifically addressed in the Restatement, but the resolution  
15 in this Section is consistent with the concepts of suretyship and guaranty law as reflected in the  
16 Restatement.  
17

18 As a practical matter, an extension of the due date will normally occur only when the  
19 principal obligor is unable to pay on the due date. The interest of the secondary obligor normally  
20 is to acquiesce in the willingness of the person entitled to enforce the instrument to wait for  
21 payment from the principal obligor rather than to pay right away and rely on an action against the  
22 principal obligor that may have little or no value. But in unusual cases the secondary obligor  
23 may prefer to pay the holder on the original due date so as to avoid continuing accrual of interest.  
24 In such cases, the secondary obligor may do so. See paragraph (b)(3). If the terms of the  
25 extension provide that the person entitled to enforce the instrument retains its right to enforce the  
26 instrument against the secondary obligor on the original due date, though, those terms are  
27 effective and the secondary obligor may not delay payment until the extended due date. Unless  
28 the extension agreement effects a preservation of recourse, however, the secondary obligor may  
29 not proceed against the principal obligor under Section 3-419 until the extended due date. See  
30 paragraph (b)(1). To the extent that delay causes loss to the secondary obligor it is discharged  
31 under paragraph (b)(2).  
32

33 Even in those cases in which a secondary obligor does not have a duty to pay the instrument  
34 on the original due date, it always has the right to pay the instrument on that date, and perhaps  
35 minimize its loss by doing so. The secondary obligor is not precluded, however, from asserting  
36 its rights to discharge under Section 3-605(b)(2) if it does not exercise that option. The critical  
37 issue is whether the extension caused the secondary obligor a loss by increasing the difference  
38 between its cost of performing its obligation on the instrument and the amount recoverable from  
39 the principal obligor under this Article. The decision by the secondary obligor not to exercise its  
40 option to pay on the original due date may, under the circumstances, be a factor to be considered  
41 in the determination of that issue, especially if the secondary obligor has been given prompt  
42 notice of the extension (as discussed above).  
43

1 6. Subsection (c) is based on *Restatement of Suretyship and Guaranty* § 41. It is a residual  
2 provision, which applies to modifications of the obligation of the principal obligor that are not  
3 covered by subsections (a) and (b). Under subsection (c), a modification of the obligation of the  
4 principal obligor (other than a release covered by subsection (a) or an extension of the due date  
5 covered by subsection (b)), will result in discharge of the secondary obligor to the extent the  
6 modification causes loss to the secondary obligor.

7  
8 The following is an illustration of the kind of case to which subsection (c) applies:  
9

10 *Case # 8.* Corporation borrows money from Lender and issues a note payable to Lender. X  
11 signs the note as an accommodation party for Corporation. The note refers to a loan  
12 agreement under which the note was issued, which states various events of default that allow  
13 Lender to accelerate the due date of the note. Among the events of default are breach of  
14 covenants not to incur debt beyond specified limits and not to engage in any line of business  
15 substantially different from that currently carried on by Corporation. Without consent of X,  
16 Lender agrees to modify the covenants to allow Corporation to enter into a new line of  
17 business that X considers to be risky, and to incur debt beyond the limits specified in the loan  
18 agreement to finance the new venture. This modification discharges X to the extent that the  
19 modification otherwise would cause X a loss.  
20

21 7. Subsection (d) is based on *Restatement of Suretyship and Guaranty* § 42 and deals with  
22 the discharge of secondary obligors by impairment of collateral. The last sentence of subsection  
23 (d) states four common examples of what is meant by impairment. Because it uses the term  
24 “includes,” the provision allows a court to find impairment in other cases as well. There is  
25 extensive case law on impairment of collateral. The secondary obligor is discharged to the extent  
26 that the secondary obligor proves that impairment was caused by a person entitled to enforce the  
27 instrument. For example, assume that the payee of a secured note fails to perfect the security  
28 interest. The collateral is owned by the principal obligor who subsequently files in bankruptcy.  
29 As a result of the failure to perfect, the security interest is not enforceable in bankruptcy. If the  
30 payee were to obtain payment from the secondary obligor, the secondary obligor would be  
31 subrogated to the payee’s security interest in the collateral under Section 3-419 and general  
32 principles of suretyship law. See *Restatement of Suretyship and Guaranty* § 28(1)(c). In this  
33 situation, though, the value of the security interest is impaired completely because the security  
34 interest is unenforceable. Thus, the secondary obligor is discharged from its obligation on the  
35 note to the extent of that impairment. If the value of the collateral impaired is as much or more  
36 than the amount of the note, and if there will be no recovery on the note as an unsecured claim,  
37 there is a complete discharge. Subsection (d) applies whether the collateral is personalty or  
38 realty, whenever the obligation in question is in the form of a negotiable instrument.  
39

40 8. Subsection (e) is based on the former Section 3-605(h). The requirement of knowledge in  
41 the first clause is consistent with Section 9-628. The requirement of notice in the second clause  
42 is consistent with Section 3-419(c).  
43

1 9. The importance of the suretyship defenses provided in Section 3-605 is greatly diminished  
2 by the fact that the right to discharge can be waived as provided in subsection (f). The waiver  
3 can be effectuated by a provision in the instrument or in a separate agreement. It is standard  
4 practice to include such a waiver of suretyship defenses in notes prepared by financial institutions  
5 or other commercial creditors. Thus, Section 3–605 will result in the discharge of an  
6 accommodation party on a note only in the occasional case in which the note does not include  
7 such a waiver clause and the person entitled to enforce the note nevertheless takes actions that  
8 would give rise to a discharge under this section without obtaining the consent of the secondary  
9 obligor.

10 Because subsection (f) by its terms applies only to a discharge “under this section,”  
11 subsection (f) does not operate to waive a defense created by other law (such as the law  
12 governing enforcement of security interests under Article 9) that cannot be waived under that  
13 law. See, e.g., Section 9-602.  
14

15 The last sentence of subsection (f) creates an inference of consent on the part of the  
16 secondary obligor whenever the secondary obligor controls the principal obligor or deals with the  
17 creditor on behalf of the principal obligor. That sentence is based on *Restatement of Suretyship*  
18 *and Guaranty* § 48(2).  
19

20 10. Subsection (g) explains the criteria for determining whether the terms of a release or  
21 extension preserve the secondary obligor’s recourse, a concept of importance in the application  
22 of subsections (a) and (b). First, the terms of the release or extension must provide that the  
23 person entitled to enforce the instrument retains the right to enforce the instrument against the  
24 secondary obligor. Second, the terms of the release or extension must provide that the recourse  
25 of the secondary obligor against the principal obligor continues as though the release or extension  
26 had not been granted. Those requirements are drawn from *Restatement of Suretyship and*  
27 *Guaranty* § 38.  
28

29 11. Subsections (h) and (i) articulate rules for the burden of persuasion under Section 3-605.  
30 Those rules are based on *Restatement of Suretyship and Guaranty* § 49.  
31

32 **SECTION 4-103. VARIATION BY AGREEMENT; MEASURE OF DAMAGES;**  
33 **ACTION CONSTITUTING ORDINARY CARE.**  
34

35 **Proposed Comments**

36 [In comment 4, the reference to 3-103(a)(4) should be to 1-201(b)(20).]  
37  
38  
39  
40

1           **SECTION 4-104. DEFINITIONS AND INDEX OF DEFINITIONS.**

2           (a) In this Article, unless the context otherwise requires:

3           (1) "Account" means any deposit or credit account with a bank, including a demand,  
4 time, savings, passbook, share draft, or like account, other than an account evidenced by a  
5 certificate of deposit;

6           (2) "Afternoon" means the period of a day between noon and midnight;

7           (3) "Banking day" means the part of a day on which a bank is open to the public for  
8 carrying on substantially all of its banking functions;

9           (4) "Clearing house" means an association of banks or other payors regularly clearing  
10 items;

11           (5) "Customer" means a person having an account with a bank or for whom a bank  
12 has agreed to collect items, including a bank that maintains an account at another bank;

13           (6) "Documentary draft" means a draft to be presented for acceptance or payment if  
14 specified documents, certificated securities (Section 8-102) or instructions for uncertificated  
15 securities (Section 8-102), or other certificates, statements, or the like are to be received by the  
16 drawee or other payor before acceptance or payment of the draft;

17           (7) "Draft" means a draft as defined in Section 3-104 or an item, other than an  
18 instrument, that is an order;

19           (8) "Drawee" means a person ordered in a draft to make payment;

20           (9) "Item" means an instrument or a promise or order to pay money handled by a bank  
21 for collection or payment. The term does not include a payment order governed by Article 4A or  
22 a credit or debit card slip;

1           (10) "Midnight deadline" with respect to a bank is midnight on its next banking day  
2 following the banking day on which it receives the relevant item or notice or from which the time  
3 for taking action commences to run, whichever is later;

4           (11) "Settle" means to pay in cash, by clearing-house settlement, in a charge or credit  
5 or by remittance, or otherwise as agreed. A settlement may be either provisional or final;

6           (12) "Suspends payments" with respect to a bank means that it has been closed by  
7 order of the supervisory authorities, that a public officer has been appointed to take it over, or  
8 that it ceases or refuses to make payments in the ordinary course of business.

9           (b) Other definitions applying to this Article and the sections in which they appear are:

10	"Agreement for electronic presentment" . . . . .	Section 4-110.
11	"Bank" . . . . .	<del>Section 4-105.</del>
12	"Collecting bank" . . . . .	Section 4-105.
13	"Depository bank" . . . . .	Section 4-105.
14	"Intermediary bank" . . . . .	Section 4-105.
15	"Payor bank" . . . . .	Section 4-105.
16	"Presenting bank" . . . . .	Section 4-105.
17	"Presentment notice" . . . . .	Section 4-110.
18		

19           (c) The following definitions in other Articles apply to this Article:

20	"Acceptance" . . . . .	Section 3-409.
21	"Alteration" . . . . .	Section 3-407.
22	"Cashier's check" . . . . .	Section 3-104.
23	"Certificate of deposit" . . . . .	Section 3-104.
24	"Certified check" . . . . .	Section 3-409.
25	"Check" . . . . .	Section 3-104.
26	"Good faith" . . . . .	Section 3-103.
27	"Holder in due course" . . . . .	Section 3-302.
28	"Instrument" . . . . .	Section 3-104.
29	"Notice of dishonor" . . . . .	Section 3-503.
30	"Order" . . . . .	Section 3-103.
31	"Ordinary care" . . . . .	Section 3-103.
32	"Person entitled to enforce" . . . . .	Section 3-301.
33	"Presentment" . . . . .	Section 3-501.
34	"Promise" . . . . .	Section 3-103.

1	“Prove”	Section 3-103.
2	“Record”	Section 3-103.
3	“Remotely-Created consumer item”	Section 3-103.
4	“Teller’s check”	Section 3-104.
5	“Unauthorized signature”	Section 3-403.

6 (d) In addition, Article 1 contains general definitions and principles of construction and  
7 interpretation applicable throughout this Article.

8 **SECTION 4-207. TRANSFER WARRANTIES.**

9 (a) A customer or collecting bank that transfers an item and receives a settlement or other  
10 consideration warrants to the transferee and to any subsequent collecting bank that:

- 11 (1) the warrantor is a person entitled to enforce the item;
- 12 (2) all signatures on the item are authentic and authorized;
- 13 (3) the item has not been altered;
- 14 (4) the item is not subject to a defense or claim in recoupment (Section 3–305(a)) of  
15 any party that can be asserted against the warrantor; ~~and~~
- 16 (5) the warrantor has no knowledge of any insolvency proceeding commenced with  
17 respect to the maker or acceptor or, in the case of an unaccepted draft, the ~~drawer~~ drawer; and

18 (6) with respect to any remotely-created consumer item, that the person on whose  
19 account the item is drawn authorized the issuance of the item in the amount for which the item is  
20 drawn.

21 (b) If an item is dishonored, a customer or collecting bank transferring the item and  
22 receiving settlement or other consideration is obliged to pay the amount due on the item (i)  
23 according to the terms of the item at the time it was transferred, or (ii) if the transfer was of an  
24

1 incomplete item, according to its terms when completed as stated in Sections 3–115 and 3–407.  
2 The obligation of a transferor is owed to the transferee and to any subsequent collecting bank that  
3 takes the item in good faith. A transferor cannot disclaim its obligation under this subsection by  
4 an indorsement stating that it is made “without recourse” or otherwise disclaiming liability.

5 (c) A person to whom the warranties under subsection (a) are made and who took the  
6 item in good faith may recover from the warrantor as damages for breach of warranty an amount  
7 equal to the loss suffered as a result of the breach, but not more than the amount of the item plus  
8 expenses and loss of interest incurred as a result of the breach.

9 (d) The warranties stated in subsection (a) cannot be disclaimed with respect to checks.  
10 Unless notice of a claim for breach of warranty is given to the warrantor within 30 days after the  
11 claimant has reason to know of the breach and the identity of the warrantor, the warrantor is  
12 discharged to the extent of any loss caused by the delay in giving notice of the claim.

13 (e) A cause of action for breach of warranty under this section accrues when the claimant  
14 has reason to know of the breach.

15 **Proposed Comments**

- 16 [Change existing comment to comment 1.]
- 17
- 18
- 19 2. For an explanation of subsection (a)(6), see comment 8 to Section 3-416.
- 20
- 21
- 22

23 **SECTION 4-208. PRESENTMENT WARRANTIES.**

24 (a) If an unaccepted draft is presented to the drawee for payment or acceptance and the  
25 drawee pays or accepts the draft, (i) the person obtaining payment or acceptance, at the time of  
presentment, and (ii) a previous transferor of the draft, at the time of transfer, warrant to the

1 drawee that pays or accepts the draft in good faith that:

2 (1) the warrantor is, or was, at the time the warrantor transferred the draft, a person  
3 entitled to enforce the draft or authorized to obtain payment or acceptance of the draft on behalf  
4 of a person entitled to enforce the draft;

5 (2) the draft has not been altered; and

6 (3) the warrantor has no knowledge that the signature of the purported drawer of the  
7 draft is ~~unauthorized; unauthorized; and~~

8 (4) with respect to any remotely-created consumer item, that the person on whose  
9 account the item is drawn authorized the issuance of the item in the amount for which the item is  
10 drawn.

11 (b) A drawee making payment may recover from a warrantor damages for breach of  
12 warranty equal to the amount paid by the drawee less the amount the drawee received or is  
13 entitled to receive from the drawer because of the payment. In addition, the drawee is entitled to  
14 compensation for expenses and loss of interest resulting from the breach. The right of the drawee  
15 to recover damages under this subsection is not affected by any failure of the drawee to exercise  
16 ordinary care in making payment. If the drawee accepts the draft (i) breach of warranty is a  
17 defense to the obligation of the acceptor, and (ii) if the acceptor makes payment with respect to  
18 the draft, the acceptor is entitled to recover from a warrantor for breach of warranty the amounts  
19 stated in this subsection.

20 (c) If a drawee asserts a claim for breach of warranty under subsection (a) based on an  
21 unauthorized indorsement of the draft or an alteration of the draft, the warrantor may defend by  
22 proving that the indorsement is effective under Section 3-404 or 3-405 or the drawer is

1 precluded under Section 3-406 or 4-406 from asserting against the drawee the unauthorized  
2 indorsement or alteration.

3 (d) If (i) a dishonored draft is presented for payment to the drawer or an indorser or (ii)  
4 any other item is presented for payment to a party obliged to pay the item, and the item is paid,  
5 the person obtaining payment and a prior transferor of the item warrant to the person making  
6 payment in good faith that the warrantor is, or was, at the time the warrantor transferred the item,  
7 a person entitled to enforce the item or authorized to obtain payment on behalf of a person  
8 entitled to enforce the item. The person making payment may recover from any warrantor for  
9 breach of warranty an amount equal to the amount paid plus expenses and loss of interest  
10 resulting from the breach.

11 (e) The warranties stated in subsections (a) and (d) cannot be disclaimed with respect to  
12 checks. Unless notice of a claim for breach of warranty is given to the warrantor within 30 days  
13 after the claimant has reason to know of the breach and the identity of the warrantor, the  
14 warrantor is discharged to the extent of any loss caused by the delay in giving notice of the claim.

15 (f) A cause of action for breach of warranty under this section accrues when the claimant  
16 has reason to know of the breach.

17 **Proposed Comments**

18 [Change existing comment to comment 1.]

19 2. For an explanation of subsection (a)(4), see comment 8 to Section 3-416.  
20  
21  
22  
23



1 that problem, but it is not clear that agreements by banks with their customers can resolve all  
2 such issues. In any event, paragraph (a)(2) should eliminate the need for such agreements.

3  
4 Nothing in paragraph (a)(2) authorizes the payor bank to destroy the check. If the check is  
5 destroyed intentionally, the party obligated to pay the instrument may be discharged under  
6 Section 3-604(a). If the instrument is destroyed inadvertently, any party trying to enforce the  
7 check would be left to its rights under Section 3-309.

8  
9 **SECTION 4-403. CUSTOMER'S RIGHT TO STOP PAYMENT; BURDEN OF**

10  
11 **PROOF OF LOSS.**

12 (a) A customer or any person authorized to draw on the account if there is more than one  
13 person may stop payment of any item drawn on the customer's account or close the account by an  
14 order to the bank describing the item or account with reasonable certainty received at a time and  
15 in a manner that affords the bank a reasonable opportunity to act on it before any action by the  
16 bank with respect to the item described in Section 4-303. If the signature of more than one  
17 person is required to draw on an account, any of these persons may stop payment or close the  
18 account.

19 (b) A stop-payment order is effective for six months, but it lapses after 14 calendar days if  
20 the original order was oral and was not confirmed in writing a record within that period. A stop-  
21 payment order may be renewed for additional six-month periods by a writing record given to the  
22 bank within a period during which the stop-payment order is effective.

23 (c) The burden of establishing the fact and amount of loss resulting from the payment of  
24 an item contrary to a stop-payment order or order to close an account is on the customer. The  
25 loss from payment of an item contrary to a stop-payment order may include damages for dishonor  
26 of subsequent items under Section 4-402.

1  
2 **SECTION 4-406. CUSTOMER'S DUTY TO DISCOVER AND REPORT**

3  
4 **UNAUTHORIZED SIGNATURE OR ALTERATION.**

5 **Proposed Comments**

6 [In comment 4, the reference to 3-103(a)(4) should be to 1-201(b)(20).]

**§ 75-4-101. Short Title**

This chapter may be cited as Uniform Commercial Code--Bank Deposits and Collections.

**§ 75-4-102. Applicability**

(a) To the extent that items within this chapter are also within Chapters 3 and 8, they are subject to those chapters. If there is conflict, this chapter governs Chapter 3, but Chapter 8 governs this chapter.

(b) The liability of a bank for action or non-action with respect to an item handled by it for purposes of presentment, payment, or collection is governed by the law of the place where the bank is located. In the case of action or non-action by or at a branch or separate office of a bank, its liability is governed by the law of the place where the branch or separate office is located.

**§ 75-4-103. Variation by Agreement; Measure of Damages; Action Constituting Ordinary Care**

(a) The effect of the provisions of this chapter may be varied by agreement, but the parties to the agreement cannot disclaim a bank's responsibility for its lack of good faith or failure to exercise ordinary care or limit the measure of damages for the lack or failure. However, the parties may determine by agreement the standards by which the bank's responsibility is to be measured if those standards are not manifestly unreasonable.

(b) Federal Reserve regulations and operating circulars, clearinghouse rules, and the like have the effect of agreements under subsection (a), whether or not specifically assented to by all parties interested in items handled.

(c) Action or non-action approved by this chapter or pursuant to Federal Reserve regulations or operating circulars is the exercise of ordinary care and, in the absence of special instructions, action or non-action consistent with clearinghouse rules and the like or with a general banking usage not disapproved by this chapter, is prima facie the exercise of ordinary care.

(d) The specification or approval of certain procedures by this chapter is not disapproval of other procedures that may be reasonable under the circumstances.

(e) The measure of damages for failure to exercise ordinary care in handling an item is the amount of the item reduced by an amount that could not have been realized by the exercise of ordinary care. If there is also bad faith it includes any other damages the party suffered as a proximate consequence.

**§ 75-4-104. Definitions and Index of Definitions**

(a) In this chapter, unless the context otherwise requires:

(1) "Account" means any deposit or credit account with a bank, including a demand, time, savings, passbook, share draft, or like account, other than an account evidenced by a certificate of deposit;

(2) "Afternoon" means the period of a day between noon and midnight;

(3) "Banking day" means the part of a day on which a bank is open to the public for carrying on substantially all of its banking functions;

(4) "Clearinghouse" means an association of banks or other payors regularly clearing items;

(5) "Customer" means a person having an account with a bank or for whom a bank has agreed to collect items, including a bank that maintains an account at another bank;

(6) "Documentary draft" means a draft to be presented for acceptance or payment if specified documents, certificated securities ([Section 75-8-102](#)) or instructions for uncertificated securities ([Section 75-8-102](#)), or other certificates, statements, or the like are to be received by the drawee or other payor before acceptance or payment of the draft;

(7) "Draft" means a draft as defined in [Section 75-3-104](#) or an item, other than an instrument, that is an order;

(8) "Drawee" means a person ordered in a draft to make payment;

(9) "Item" means an instrument or a promise or order to pay money handled by a bank for collection or payment. The term does not include a payment order governed by Chapter 4A or a credit or debit card slip;

(10) "Midnight deadline" with respect to a bank is midnight on its next banking day following the banking day on which it receives the relevant item or notice or from which the time for taking action commences to run, whichever is later;

(11) "Settle" means to pay in cash, by clearinghouse settlement, in a charge or credit or by remittance, or otherwise as agreed. A settlement may be either provisional or final;

(12) "Suspends payments" with respect to a bank means that it has been closed by order of the supervisory authorities, that a public officer has been appointed to take it over, or that it ceases or refuses to make payments in the ordinary course of business.

(b) Other definitions applying to this chapter and the sections in which they appear are:

"Agreement for electronic presentment"	Section 75-4-110
"Bank"	Section 75-4-105
"Collecting bank"	Section 75-4-105
"Depository bank"	Section 75-4-105
"Intermediary bank"	Section 75-4-105
"Payor bank"	Section 75-4-105
"Presenting bank"	Section 75-4-105
"Presentment notice"	Section 75-4-110

(c) The following definitions in other chapters apply to this chapter:

"Acceptance"	Section 75-3-409
"Alteration"	Section 75-3-407
"Cashier's check"	Section 75-3-104
"Certificate of deposit"	Section 75-3-104
"Certified check"	Section 75-3-409
"Check"	Section 75-3-104
"Control"	Section 75-7-106
"Good faith"	Section 75-3-103
"Holder in due course"	Section 75-3-302
"Instrument"	Section 75-3-104
"Notice of dishonor"	Section 75-3-503
"Order"	Section 75-3-103
"Ordinary care"	Section 75-3-103
"Person entitled to enforce"	Section 75-3-301
"Presentment"	Section 75-3-501

“Promise”	Section 75-3-103
“Prove”	Section 75-3-103
“Teller’s check”	Section 75-3-104
“Unauthorized signature”	Section 75-3-403

(d) In addition, Chapter 1 contains general definitions and principles of construction and interpretation applicable throughout this chapter.

**§ 75-4-105. “Bank”; “Depository Bank”; “Payor Bank”; “Intermediary Bank”; “Collecting Bank”; “Presenting Bank”**

In this chapter:

- (1) “Bank” means a person engaged in the business of banking, including a savings bank, savings and loan association, credit union, or trust company;
- (2) “Depository bank” means the first bank to take an item even though it is also the payor bank, unless the item is presented for immediate payment over the counter;
- (3) “Payor bank” means a bank that is the drawee of a draft;
- (4) “Intermediary bank” means a bank to which an item is transferred in course of collection except the depository or payor bank;
- (5) “Collecting bank” means a bank handling an item for collection except the payor bank;
- (6) “Presenting bank” means a bank presenting an item except a payor bank.

**§ 75-4-106. “Payable Through” or “Payable at” Bank; Collecting Bank**

- (a) If an item states that it is “payable through” a bank identified in the item, (i) the item designates the bank as a collecting bank and does not by itself authorize the bank to pay the item, and (ii) the item may be presented for payment only by or through the bank.
- (b) If an item states that it is “payable at” a bank identified in the item, (i) the item designates the bank as a collecting bank and does not by itself authorize the bank to pay the item, and (ii) the item may be presented for payment only by or through the bank.
- (c) If a draft names a nonbank drawee and it is unclear whether a bank named in the draft is a co-drawee or a collecting bank, the bank is a collecting bank.

**§ 75-4-107. Separate Office of Bank**

A branch or separate office of a bank is a separate bank for the purpose of computing the time within which and determining the place at or to which action may be taken or notices or orders must be given under this chapter and under Chapter 3.

**§ 75-4-108. Time of Receipt of Items**

- (a) For the purpose of allowing time to process items, prove balances, and make the necessary entries on its books to determine its position for the day, a bank may fix an afternoon hour of 2 P.M. or later as a cutoff hour for the handling of money and items and the making of entries on its books.
- (b) An item or deposit of money received on any day after a cutoff hour so fixed or after the close of the banking day may be treated as being received at the opening of the next banking day.

**§ 75-4-109. Delays**

(a) Unless otherwise instructed, a collecting bank in a good faith effort to secure payment of a specific item drawn on a payor other than a bank, and with or without the approval of any person involved, may waive, modify, or extend time limits imposed or permitted by this code for a period not exceeding two (2) additional banking days without discharge of drawers or indorsers or liability to its transferor or a prior party.

(b) Delay by a collecting bank or payor bank beyond time limits prescribed or permitted by this code or by instructions is excused if (i) the delay is caused by interruption of communication or computer facilities, suspension of payments by another bank, war, emergency conditions, failure of equipment, or other circumstances beyond the control of the bank, and (ii) the bank exercises such diligence as the circumstances require.

**§ 75-4-110. Electronic Presentation**

(a) “Agreement for electronic presentation” means an agreement, clearinghouse rule, or Federal Reserve regulation or operating circular, providing that presentation of an item may be made by transmission of an image of an item or information describing the item (“presentation notice”) rather than delivery of the item itself. The agreement may provide for procedures governing retention, presentment, payment, dishonor, and other matters concerning items subject to the agreement.

(b) Presentment of an item pursuant to an agreement for presentment is made when the presentment notice is received.

(c) If presentment is made by presentment notice, a reference to “item” or “check” in this chapter means the presentment notice unless the context otherwise indicates.

**§ 75-4-111. Statute of Limitations**

An action to enforce an obligation, duty, or right arising under this chapter must be commenced within three (3) years after the cause of action accrues.

**Part 2. Collection of Items: Depository and Collecting Banks**

**§ 75-4-201. Status of Collecting Bank as Agent and Provisional Status of Credits; Applicability of Chapter; Item Indorsed “Pay Any Bank”**

(a) Unless a contrary intent clearly appears and before the time that a settlement given by a collecting bank for an item is or becomes final, the bank, with respect to the item, is an agent or sub-agent of the owner of the item and any settlement given for the item is provisional. This provision applies regardless of the form of indorsement or lack of indorsement and even though credit given for the item is subject to immediate withdrawal as of right or is in fact withdrawn; but the continuance of ownership of an item by its owner and any rights of the owner to proceeds of the item are subject to rights of a collecting bank, such as those resulting from outstanding advances on the item and rights of recoupment or setoff. If an item is handled by banks for purposes of presentment, payment, collection, or return, the relevant provisions of this chapter apply even though action of the parties clearly establishes that a particular bank has purchased the item and is the owner of it.

(b) After an item has been indorsed with the words “pay any bank” or the like, only a bank may acquire the rights of a holder until the item has been:

- (1) Returned to the customer initiating collection; or
- (2) Specially indorsed by a bank to a person who is not a bank.

**§ 75-4-202. Responsibility for Collection or Return: When Action Timely**

(a) A collecting bank must exercise ordinary care in:

- (1) Presenting an item or sending it for presentment;
- (2) Sending notice of dishonor or nonpayment or returning an item other than a documentary draft to the bank’s transferor after

learning that the item has not been paid or accepted, as the case may be;

(3) Settling for an item when the bank receives final settlement; and

(4) Notifying its transferor of any loss or delay in transit within a reasonable time after discovery thereof.

(b) A collecting bank exercises ordinary care under subsection (a) by taking proper action before its midnight deadline following receipt of an item, notice, or settlement. Taking proper action within a reasonably longer time may constitute the exercise of ordinary care, but the bank has the burden of establishing timeliness.

(c) Subject to subsection (a)(1), a bank is not liable for the insolvency, neglect, misconduct, mistake, or default of another bank or person or for loss or destruction of an item in the possession of others or in transit.

#### § 75-4-203. Effect of Instructions

Subject to Chapter 3 concerning conversion of instruments ([Section 75-3-420](#)) and restrictive indorsements ([Section 75-3-206](#)), only a collecting bank's transferor can give instructions that affect the bank or constitute notice to it, and a collecting bank is not liable to prior parties for any action taken pursuant to the instructions or in accordance with an agreement with its transferor.

#### § 75-4-204. Methods of Sending and Presenting; Sending Directly to Payor Bank

(a) A collecting bank shall send items by a reasonably prompt method, taking into consideration relevant instructions, the nature of the item, the number of those items on hand, the cost of collection involved, and the method generally used by it or others to present those items.

(b) A collecting bank may send:

(1) An item directly to the payor bank;

(2) An item to a nonbank payor if authorized by its transferor; and

(3) An item other than documentary drafts to a nonbank payor, if authorized by Federal Reserve regulation or operating circular, clearinghouse rule, or the like.

(c) Presentment may be made by a presenting bank at a place where the payor bank or other payor has requested that presentment be made.

#### § 75-4-205. Depository Bank Holder of Unindorsed Item

If a customer delivers an item to a depository bank for collection:

(1) The depository bank becomes a holder of the item at the time it receives the item for collection if the customer at the time of delivery was a holder of the item, whether or not the customer indorses the item, and, if the bank satisfies the other requirements of [Section 75-3-302](#), it is a holder in due course; and

(2) The depository bank warrants to collecting banks, the payor bank or other payor, and the drawer that the amount of the item was paid to the customer or deposited to the customer's account.

#### § 75-4-206. Transfer Between Banks

Any agreed method that identifies the transferor bank is sufficient for the item's further transfer to another bank.

#### § 75-4-207. Transfer Warranties

(a) A customer or collecting bank that transfers an item and receives a settlement or other consideration warrants to the transferee and to any subsequent collecting bank that:

(1) The warrantor is a person entitled to enforce the item;

(2) All signatures on the item are authentic and authorized;

(3) The item has not been altered;

(4) The item is not subject to a defense or claim in recoupment ([Section 75-3-305\(a\)](#)) of any party that can be asserted against the warrantor; and

(5) The warrantor has no knowledge of any insolvency proceeding commenced with respect to the maker or acceptor or, in the case of an unaccepted draft, the drawer.

(b) If an item is dishonored, a customer or collecting bank transferring the item and receiving settlement or other consideration is obliged to pay the amount due on the item (i) according to the terms of the item at the time it was transferred, or (ii) if the transfer was of an incomplete item, according to its terms when completed as stated in [Sections 75-3-115](#) and [75-3-407](#). The obligation of a transferor is owed to the transferee and to any subsequent collecting bank that takes the item in good faith. A transferor cannot disclaim its obligation under this subsection by an indorsement stating that it is made "without recourse" or otherwise disclaiming liability.

(c) A person to whom the warranties under subsection (a) are made and who took the item in good faith may recover from the warrantor as damages for breach of warranty an amount equal to the loss suffered as a result of the breach, but not more than the amount of the item plus expenses and loss of interest incurred as a result of the breach.

(d) The warranties stated in subsection (a) cannot be disclaimed with respect to checks. Unless notice of a claim for breach of warranty is given to the warrantor within thirty (30) days after the claimant has reason to know of the breach and the identity of the warrantor, the warrantor is discharged to the extent of any loss caused by the delay in giving notice of the claim.

(e) A cause of action for breach of warranty under this section accrues when the claimant has reason to know of the breach.

#### § 75-4-208. Presentment Warranties

(a) If an unaccepted draft is presented to the drawee for payment or acceptance and the drawee pays or accepts the draft, (i) the person obtaining payment or acceptance, at the time of presentment, and (ii) a previous transferor of the draft, at the time of transfer, warrant to the drawee that pays or accepts the draft in good faith that:

(1) The warrantor is, or was, at the time the warrantor transferred the draft, a person entitled to enforce the draft or authorized to obtain payment or acceptance of the draft on behalf of a person entitled to enforce the draft;

(2) The draft has not been altered; and

(3) The warrantor has no knowledge that the signature of the purported drawer of the draft is unauthorized.

(b) A drawee making payment may recover from a warrantor damages for breach of warranty equal to the amount paid by the drawee less the amount the drawee received or is entitled to receive from the drawer because of the payment. In addition, the drawee is entitled to compensation for expenses and loss of interest resulting from the breach. The right of the drawee to recover damages under this subsection is not affected by any failure of the drawee to exercise ordinary care in making payment. If the drawee accepts the draft (i) breach of warranty is a defense to the obligation of the acceptor, and (ii) if the acceptor makes payment with respect to the draft, the acceptor is entitled to recover from a warrantor for breach of warranty the amounts stated in this subsection.

(c) If a drawee asserts a claim for breach of warranty under subsection (a) based on an unauthorized indorsement of the draft or an alteration of the draft, the warrantor may defend by proving that the indorsement is effective under [Section 75-3-404](#) or [75-3-405](#) or the drawer is precluded under [Section 75-3-406](#) or [75-4-406](#) from asserting against the drawee the unauthorized indorsement or alteration.

(d) If (i) a dishonored draft is presented for payment to the drawer or an indorser or (ii) any other item is presented for payment

to a party obliged to pay the item, and the item is paid, the person obtaining payment and a prior transferor of the item warrant to the person making payment in good faith that the warrantor is, or was, at the time the warrantor transferred the item, a person entitled to enforce the item or authorized to obtain payment on behalf of a person entitled to enforce the item. The person making payment may recover from any warrantor for breach of warranty an amount equal to the amount paid plus expenses and loss of interest resulting from the breach.

(e) The warranties stated in subsections (a) and (d) cannot be disclaimed with respect to checks. Unless notice of a claim for breach of warranty is given to the warrantor within thirty (30) days after the claimant has reason to know of the breach and the identity of the warrantor, the warrantor is discharged to the extent of any loss caused by the delay in giving notice of the claim.

(f) A cause of action for breach of warranty under this section accrues when the claimant has reason to know of the breach.

#### **§ 75-4-209. Encoding and Retention Warranties**

(a) A person who encodes information on or with respect to an item after issue warrants to any subsequent collecting bank and to the payor bank or other payor that the information is correctly encoded. If the customer of a depository bank encodes, that bank also makes the warranty.

(b) A person who undertakes to retain an item pursuant to an agreement for electronic presentment warrants to any subsequent collecting bank and to the payor bank or other payor that retention and presentment of the item comply with the agreement. If a customer of a depository bank undertakes to retain an item, that bank also makes this warranty.

(c) A person to whom warranties are made under this section and who took the item in good faith may recover from the warrantor as damages for breach of warranty an amount equal to the loss suffered as a result of the breach, plus expenses and loss of interest incurred as a result of the breach.

#### **§ 75-4-210. Security Interest of Collecting Bank in Items, Accompanying Documents and Proceeds**

(a) A collecting bank has a security interest in an item and any accompanying documents or the proceeds of either:

- (1) In case of an item deposited in an account, to the extent to which credit given for the item has been withdrawn or applied;
- (2) In case of an item for which it has given credit available for withdrawal as of right, to the extent of the credit given, whether or not the credit is drawn upon or there is a right of charge-back; or
- (3) If it makes an advance on or against the item.

(b) If credit given for several items received at one time or pursuant to a single agreement is withdrawn or applied in part, the security interest remains upon all the items, any accompanying documents or the proceeds of either. For the purpose of this section, credits first given are first withdrawn.

(c) Receipt by a collecting bank of a final settlement for an item is a realization on its security interest in the item, accompanying documents, and proceeds. So long as the bank does not receive final settlement for the item or give up possession of the item or possession or control of the accompanying documents for purposes other than collection, the security interest continues to that extent and is subject to Title 75, Chapter 9, but:

- (1) No security agreement is necessary to make the security interest enforceable ([Section 75-9-203\(b\)\(3\)\(A\)](#));
- (2) No filing is required to perfect the security interest; and
- (3) The security interest has priority over conflicting perfected security interests in the item, accompanying documents, or proceeds.

#### **§ 75-4-211. When Bank Gives Value for Purposes of Holder in Due Course**

For purposes of determining its status as a holder in due course, a bank has given value to the extent it has a security interest in

an item, if the bank otherwise complies with the requirements of [Section 75-3-302](#) on what constitutes a holder in due course.

#### **§ 75-4-212. Presentment by Notice of Item Not Payable by, Through, or at Bank; Liability of Drawer or Indorser**

(a) Unless otherwise instructed, a collecting bank may present an item not payable by, through, or at a bank by sending to the party to accept or pay a written notice that the bank holds the item for acceptance or payment. The notice must be sent in time to be received on or before the day when presentment is due and the bank must meet any requirement of the party to accept or pay under [Section 75-3-501](#) by the close of the bank's next banking day after it knows of the requirement.

(b) If presentment is made by notice and payment, acceptance, or request for compliance with a requirement under [Section 75-3-501](#) is not received by the close of business on the day after maturity or, in the case of demand items, by the close of business on the third banking day after notice was sent, the presenting bank may treat the item as dishonored and charge any drawer or indorser by sending it notice of the facts.

#### **§ 75-4-213. Medium and Time of Settlement by Bank**

(a) With respect to settlement by a bank, the medium and time of settlement may be prescribed by Federal Reserve regulations or circulars, clearinghouse rules, and the like, or agreement. In the absence of such prescription:

- (1) The medium of settlement is cash or credit to an account in a Federal Reserve bank of or specified by the person to receive settlement; and
  - (2) The time of settlement is:
    - (i) With respect to tender of settlement by cash, a cashier's check, or teller's check, when the cash or check is sent or delivered;
    - (ii) With respect to tender of settlement by credit in an account in a Federal Reserve bank, when the credit is made;
    - (iii) With respect to tender of settlement by a credit or debit to an account in a bank, when the credit or debit is made or, in the case of tender of settlement by authority to charge an account, when the authority is sent or delivered; or
    - (iv) With respect to tender of settlement by a funds transfer, when payment is made pursuant to [Section 75-4A-406\(a\)](#) to the person receiving settlement.
- (b) If the tender of settlement is not by a medium authorized by subsection (a) or the time of settlement is not fixed by subsection (a), no settlement occurs until the tender of settlement is accepted by the person receiving settlement.
- (c) If settlement for an item is made by cashier's check or teller's check and the person receiving settlement, before its midnight deadline:
- (1) Presents or forwards the check for collection, settlement is final when the check is finally paid; or
  - (2) Fails to present or forward the check for collection, settlement is final at the midnight deadline of the person receiving settlement.
- (d) If settlement for an item is made by giving authority to charge the account of the bank giving settlement in the bank receiving settlement, settlement is final when the charge is made by the bank receiving settlement if there are funds available in the account for the amount of the item.

#### **§ 75-4-214. Right of Charge-Back or Refund; Liability of Collecting Bank; Return of Item**

(a) If a collecting bank has made provisional settlement with its customer for an item and fails by reason of dishonor, suspension of payments by a bank, or otherwise to receive a settlement for the item which is or becomes final, the bank may revoke the settlement given by it, charge back the amount of any credit given for the item to its customer's account, or obtain refund from its customer, whether or not it is able to return the item, if by its midnight deadline or within a longer reasonable time after it learns the facts it returns the item or sends notification of the facts. If the return or notice is delayed beyond the bank's midnight deadline or a longer reasonable time after it learns the facts, the bank may revoke the settlement, charge back the credit, or

obtain refund from its customer, but it is liable for any loss resulting from the delay. These rights to revoke, charge back, and obtain refund terminate if and when a settlement for the item received by the bank is or becomes final.

- (b) A collecting bank returns an item when it is sent or delivered to the bank's customer or transferor or pursuant to its instructions.
- (c) A depository bank that is also the payor may charge back the amount of an item to its customer's account or obtain refund in accordance with the section governing return of an item received by a payor bank for credit on its books ([Section 75-4-301](#)).
- (d) The right to charge back is not affected by:
  - (1) Previous use of a credit given for the item; or
  - (2) Failure by any bank to exercise ordinary care with respect to the item, but a bank so failing remains liable.
- (e) A failure to charge back or claim refund does not affect other rights of the bank against the customer or any other party.
- (f) If credit is given in dollars as the equivalent of the value of an item payable in foreign money, the dollar amount of any charge-back or refund must be calculated on the basis of the bank-offered spot rate for the foreign money prevailing on the day when the person entitled to the charge-back or refund learns that it will not receive payment in ordinary course.

**[§ 75-4-215. Final Payment of Item by Payor Bank; when Provisional Debits and Credits Become Final; when Certain Credits Become Available for Withdrawal](#)**

- (a) An item is finally paid by a payor bank when the bank has first done any of the following:
  - (1) Paid the item in cash;
  - (2) Settled for the item without having a right to revoke the settlement under statute, clearinghouse rule, or agreement; or
  - (3) Made a provisional settlement for the item and failed to revoke the settlement in the time and manner permitted by statute, clearinghouse rule, or agreement.
- (b) If provisional settlement for an item does not become final, the item is not finally paid.
- (c) If provisional settlement for an item between the presenting and payor banks is made through a clearinghouse or by debits or credits in an account between them, then to the extent that provisional debits or credits for the item are entered in accounts between the presenting and payor banks or between the presenting and successive prior collecting banks seriatim, they become final upon final payment of the item by the payor bank.
- (d) If a collecting bank receives a settlement for an item which is or becomes final, the bank is accountable to its customer for the amount of the item and any provisional credit given for the item in an account with its customer becomes final.
- (e) Subject to (i) applicable law stating a time for availability of funds and (ii) any right of the bank to apply the credit to an obligation of the customer, credit given by a bank for an item in a customer's account becomes available for withdrawal as of right:
  - (1) If the bank has received a provisional settlement for the item, when the settlement becomes final and the bank has had a reasonable time to receive return of the item and the item has not been received within that time;
  - (2) If the bank is both the depository bank and the payor bank, and the item is finally paid, at the opening of the bank's second banking day following receipt of the item.
- (f) Subject to applicable law stating a time for availability of funds and any right of a bank to apply a deposit to an obligation of the depositor, a deposit of money becomes available for withdrawal as of right at the opening of the bank's next banking day after receipt of the deposit.

**[§ 75-4-216. Insolvency and Preference](#)**

- (a) If an item is in or comes into the possession of a payor or collecting bank that suspends payment and the item has not been finally paid, the item must be returned by the receiver, trustee, or agent in charge of the closed bank to the presenting bank or the closed bank's customer.
- (b) If a payor bank finally pays an item and suspends payments without making a settlement for the item with its customer or the presenting bank which settlement is or becomes final, the owner of the item has a preferred claim against the payor bank.
- (c) If a payor bank gives or a collecting bank gives or receives a provisional settlement for an item and thereafter suspends payments, the suspension does not prevent or interfere with the settlement's becoming final if the finality occurs automatically upon the lapse of certain time or the happening of certain events.
- (d) If a collecting bank receives from subsequent parties settlement for an item, which settlement is or becomes final and the bank suspends payments without making a settlement for the item with its customer which settlement is or becomes final, the owner of the item has a preferred claim against the collecting bank.

**Part 3. Collection of Items: Payor Banks**

**[§ 75-4-301. Deferred Posting; Recovery of Payment by Return of Items; Time of Dishonor; Return of Items by Payor Bank](#)**

- (a) If a payor bank settles for a demand item other than a documentary draft presented otherwise than for immediate payment over the counter before midnight of the banking day of receipt, the payor bank may revoke the settlement and recover the settlement if, before it has made final payment and before its midnight deadline, it:
  - (1) Returns the item; or
  - (2) Sends written notice of dishonor or nonpayment if the item is unavailable for return.
- (b) If a demand item is received by a payor bank for credit on its books, it may return the item or send notice of dishonor and may revoke any credit given or recover the amount thereof withdrawn by its customer, if it acts within the time limit and in the manner specified in subsection (a).
- (c) Unless previous notice of dishonor has been sent, an item is dishonored at the time when for purposes of dishonor it is returned or notice sent in accordance with this section.
- (d) An item is returned:
  - (1) As to an item presented through a clearinghouse, when it is delivered to the presenting or last collecting bank or to the clearinghouse or is sent or delivered in accordance with clearinghouse rules; or
  - (2) In all other cases, when it is sent or delivered to the bank's customer or transferor or pursuant to instructions.

**[§ 75-4-302. Payor Bank's Responsibility for Late Return of Item](#)**

- (a) If an item is presented to and received by a payor bank, the bank is accountable for the amount of:
  - (1) A demand item, other than a documentary draft, whether properly payable or not, if the bank, in any case in which it is not also the depository bank, retains the item beyond midnight of the banking day of receipt without settling for it or, whether or not it is also the depository bank, does not pay or return the item or send notice of dishonor until after its midnight deadline; or
  - (2) Any other properly payable item unless, within the time allowed for acceptance or payment of that item, the bank either accepts or pays the item or returns it and accompanying documents.

(b) The liability of a payor bank to pay an item pursuant to subsection (a) is subject to defenses based on breach of a presentment warranty ([Section 75-4-208](#)) or proof that the person seeking enforcement of the liability presented or transferred the item for the purpose of defrauding the payor bank.

**§ 75-4-303. When Items Subject to Notice, Stop Payment Order, Legal Process or Setoff; Order in Which Items May Be Charged or Certified**

(a) Any knowledge, notice, or stop-payment order received by, legal process served upon, or setoff exercised by a payor bank, comes too late to terminate, suspend, or modify the bank's right or duty to pay an item or to charge its customer's account for the item if the knowledge, notice, stop-payment order, or legal process is received or served and a reasonable time for the bank to act thereon expires or the setoff is exercised after the earliest of the following:

- (1) The bank accepts or certifies the item;
- (2) The bank pays the item in cash;
- (3) The bank settles for the item without having a right to revoke the settlement under statute, clearinghouse rule, or agreement;
- (4) The bank becomes accountable for the amount of the item under [Section 75-4-302](#) dealing with the payor bank's responsibility for late return of items; or
- (5) With respect to checks, a cutoff hour no earlier than one (1) hour after the opening of the next banking day after the banking day on which the bank received the check and no later than the close of that next banking day or, if no cutoff hour is fixed, the close of the next banking day after the banking day on which the bank received the check.

(b) Subject to subsection (a), items may be accepted, paid, certified, or charged to the indicated account of its customer in any order.

**Part 4. Relationship Between Payor Bank and Its Customer**

**§ 75-4-401. When Bank May Charge Customer's Account**

(a) A bank may charge against the account of a customer an item that is properly payable from that account even though the charge creates an overdraft. An item is properly payable if it is authorized by the customer and is in accordance with any agreement between the customer and bank.

(b) A customer is not liable for the amount of an overdraft if the customer neither signed the item nor benefited from the proceeds of the item.

(c) A bank may charge against the account of a customer a check that is otherwise properly payable from the account, even though payment was made before the date of the check, unless the customer has given notice to the bank of the postdating describing the check with reasonable certainty. The notice is effective for the period stated in [Section 75-4-403\(b\)](#) for stop-payment orders, and must be received at such time and in such manner as to afford the bank a reasonable opportunity to act on it before the bank takes any action with respect to the check described in [Section 75-4-303](#). If a bank charges against the account of a customer a check before the date stated in the notice of postdating, the bank is liable for damages for the loss resulting from its act. The loss may include damages for dishonor of subsequent items under [Section 75-4-402](#).

(d) A bank that in good faith makes payment to a holder may charge the indicated account of its customer according to:

- (1) The original terms of the altered item; or
- (2) The terms of the completed item, even though the bank knows the item has been completed unless the bank has notice that the completion was improper.

**§ 75-4-402. Bank's Liability to Customer for Wrongful Dishonor; Time of Determining Insufficiency of Account**

(a) Except as otherwise provided in this chapter, a payor bank wrongfully dishonors an item if it dishonors an item that is properly payable, but a bank may dishonor an item that would create an overdraft unless it has agreed to pay the overdraft.

(b) A payor bank is liable to its customer for damages proximately caused by the wrongful dishonor of an item. Liability is limited to actual damages proved and may include damages for an arrest or prosecution of the customer or other consequential damages. Whether any consequential damages are proximately caused by the wrongful dishonor is a question of fact to be determined in each case.

(c) A payor bank's determination of the customer's account balance on which a decision to dishonor for insufficiency of available funds is based may be made at any time between the time the item is received by the payor bank and the time that the payor bank returns the item or gives notice in lieu of return, and no more than one determination need be made. If, at the election of the payor bank, a subsequent balance determination is made for the purpose of reevaluating the bank's decision to dishonor the item, the account balance at that time is determinative of whether a dishonor for insufficiency of available funds is wrongful.

**§ 75-4-403. Customer's Right to Stop Payment; Burden of Proof of Loss**

(a) A customer or any person authorized to draw on the account if there is more than one person may stop payment of any item drawn on the customer's account or close the account by an order to the bank describing the item or account with reasonable certainty received at a time and in a manner that affords the bank a reasonable opportunity to act on it before any action by the bank with respect to the item described in [Section 75-4-303](#). If the signature of more than one person is required to draw on an account, any of these persons may stop payment or close the account.

(b) A stop-payment order is effective for six (6) months, but it lapses after fourteen (14) calendar days if the original order was oral and was not confirmed in writing within that period. A stop-payment order may be renewed for additional six-month periods by a writing given to the bank within a period during which the stop-payment order is effective.

(c) The burden of establishing the fact and amount of loss resulting from the payment of an item contrary to a stop-payment order or order to close an account is on the customer. The loss from payment of an item contrary to a stop-payment order may include damages for dishonor of subsequent items under [Section 75-4-402](#).

**§ 75-4-404. Bank Not Obligated to Pay Check More Than Six Months Old**

A bank is under no obligation to a customer having a checking account to pay a check, other than a certified check, which is presented more than six (6) months after its date, but it may charge its customer's account for payment made thereafter in good faith.

**§ 75-4-405. Death or Incompetence of Customer**

(a) A payor or collecting bank's authority to accept, pay, or collect an item or to account for proceeds of its collection, if otherwise effective, is not rendered ineffective by incompetence of a customer of either bank existing at the time the item is issued or its collection is undertaken if the bank does not know of an adjudication of incompetence. Neither death nor incompetence of a customer revokes the authority to accept, pay, collect, or account until the bank knows of the fact of death or of an adjudication of incompetence and has reasonable opportunity to act on it.

(b) Even with knowledge, a bank may for ten (10) days after the date of death pay or certify checks drawn on or before that date unless ordered to stop payment by a person claiming an interest in the account.

**§ 75-4-406. Customer's Duty to Discover and Report Unauthorized Signature or Alteration**

(a) A bank that sends or makes available to a customer a statement of account showing payment of items for the account shall either return or make available to the customer the items paid or provide information in the statement of account sufficient to allow the customer reasonably to identify the items paid. The statement of account provides sufficient information if the item is described by item number, amount, and date of payment.

(b) If the items are not returned to the customer, the person retaining the items shall either retain the items or, if the items are destroyed, maintain the capacity to furnish legible copies of the items until the expiration of seven (7) years after receipt of the items. A customer may request an item from the bank that paid the item, and that bank must provide in a reasonable time either the item or, if the item has been destroyed or is not otherwise obtainable, a legible copy of the item.

(c) If a bank sends or makes available a statement of account or items pursuant to subsection (a), the customer must exercise reasonable promptness in examining the statement or the items to determine whether any payment was not authorized because of an alteration of an item or because of a purported signature by or on behalf of the customer was not authorized. If, based on the statement or items provided, the customer should reasonably have discovered the unauthorized payment, the customer must promptly notify the bank of the relevant facts.

(d) If the bank proves that the customer failed, with respect to an item, to comply with the duties imposed on the customer by subsection (c), the customer is precluded from asserting against the bank:

(1) The customer's unauthorized signature or any alteration on the item, if the bank also proves that it suffered a loss by reason of the failure; and

(2) The customer's unauthorized signature or alteration by the same wrongdoer on any other item paid in good faith by the bank if the payment was made before the bank received notice from the customer of the unauthorized signature or alteration and after the customer had been afforded a reasonable period of time, not exceeding thirty (30) days, in which to examine the item or statement of account and notify the bank.

(e) If subsection (d) applies and the customer proves that the bank failed to exercise ordinary care in paying the item and that the failure substantially contributed to loss, the loss is allocated between the customer precluded and the bank asserting the preclusion according to the extent to which the failure of the customer to comply with subsection (c) and the failure of the bank to exercise ordinary care contributed to the loss. If the customer proves that the bank did not pay the item in good faith, the preclusion under subsection (d) does not apply.

(f) Without regard to care or lack of care of either the customer or the bank, a customer who does not within one (1) year after the statement or items are made available to the customer (subsection (a)) discover and report the customer's unauthorized signature on or any alteration on the item is precluded from asserting against the bank the unauthorized signature or alteration. If there is a preclusion under this subsection, the payor bank may not recover for breach of warranty under [Section 75-4-208](#) with respect to the unauthorized signature or alteration to which the preclusion applies.

#### § 75-4-407. Payer Bank's Right to Subrogation on Improper Payment

If a payor bank has paid an item over the order of the drawer or maker to stop payment, or after an account has been closed, or otherwise under circumstances giving a basis for objection by the drawer or maker, to prevent unjust enrichment and only to the extent necessary to prevent loss to the bank by reason of its payment of the item, the payor bank is subrogated to the rights:

(1) Of any holder in due course on the item against the drawer or maker;

(2) Of the payee or any other holder of the item against the drawer or maker either on the item or under the transaction out of which the item arose; and

(3) Of the drawer or maker against the payee or any other holder of the item with respect to the transaction out of which the item arose.

### **Part 5. Collection of Documentary Drafts**

#### § 75-4-501. Handling of Documentary Drafts; Duty to Send for Presentment and to Notify Customer of Dishonor

A bank that takes a documentary draft for collection shall present or send the draft and accompanying documents for presentment and, upon learning that the draft has not been paid or accepted in due course, shall seasonably notify its customer of the fact even though it may have discounted or bought the draft or extended credit available for withdrawal as of right.

#### § 75-4-502. Presentment of "On Arrival" Drafts

If a draft or the relevant instructions require presentment "on arrival," "when goods arrive" or the like, the collecting bank need not present until in its judgment a reasonable time for arrival of the goods has expired. Refusal to pay or accept because the goods have not arrived is not dishonor; the bank must notify its transferor of the refusal but need not present the draft again until it is instructed to do so or learns of the arrival of the goods.

#### § 75-4-503. Responsibility of Presenting Bank for Documents and Goods; Report of Reasons for Dishonor; Referee in Case of Need

Unless otherwise instructed and except as provided in Chapter 5, a bank presenting a documentary draft:

(1) Must deliver the documents to the drawee on acceptance of the draft if it is payable more than three (3) days after presentment; otherwise, only on payment; and

(2) Upon dishonor, either in the case of presentment for acceptance or presentment for payment, may seek and follow instructions from any referee in case of need designated in the draft or, if the presenting bank does not choose to utilize the referee's services, it must use diligence and good faith to ascertain the reason for dishonor, must notify its transferor of the dishonor and of the results of its effort to ascertain the reasons therefor, and must request instructions. However, the presenting bank is under no obligation with respect to goods represented by the documents except to follow any reasonable instructions seasonably received; it has a right to reimbursement for any expense incurred in following instructions and to prepayment of or indemnity for those expenses.

#### § 75-4-504. Privilege of Presenting Bank to Deal with Goods; Security Interest for Expenses

(a) A presenting bank that, following the dishonor of a documentary draft, has seasonably requested instructions but does not receive them within a reasonable time may store, sell, or otherwise deal with the goods in any reasonable manner.

(b) For its reasonable expenses incurred by action under subsection (a), the presenting bank has a lien upon the goods or their proceeds, which may be foreclosed in the same manner as an unpaid seller's lien.

West's Annotated Mississippi Code [Currentness](#)

Title 75. Regulation of Trade, Commerce and Investments ([Refs & Annos](#))

[Chapter 3](#). Uniform Commercial Code--Negotiable Instruments ([Refs & Annos](#))

[Part 1](#). General Provisions and Definitions

→ [§ 75-3-101. Short Title](#)

This chapter may be cited as Uniform Commercial Code -- Negotiable Instruments.

#### [§ 75-3-102. Subject Matter](#)

- (a) This chapter applies to negotiable instruments. It does not apply to money, to payment orders governed by Chapter 4A, or to securities governed by Chapter 8.
- (b) If there is conflict between this chapter and Chapter 4 or 9, Chapters 4 and 9 govern.
- (c) Regulations of the Board of Governors of the Federal Reserve System and operating circulars of the Federal Reserve Banks supersede any inconsistent provision of this chapter to the extent of the inconsistency.

#### [§ 75-3-103. Definitions](#)

- (a) In this chapter:
- (1) "Acceptor" means a drawee who has accepted a draft.
- (2) "Drawee" means a person ordered in a draft to make payment.
- (3) "Drawer" means a person who signs or is identified in a draft as a person ordering payment.
- (4) "Good faith" means honesty in fact and the observance of reasonable commercial standards of fair dealing.
- (5) "Maker" means a person who signs or is identified in a note as a person undertaking to pay.
- (6) "Order" means a written instruction to pay money signed by the person giving the instruction. The instruction may be addressed to any person, including the person giving the instruction, or to one or more persons jointly or in the alternative but not in succession. An authorization to pay is not an order unless the person authorized to pay is also instructed to pay.
- (7) "Ordinary care" in the case of a person engaged in business means observance of reasonable commercial standards, prevailing in the area in which the person is located, with respect to the business in which the person is engaged. In the case of a bank that takes an instrument for processing for collection or payment by automated means, reasonable commercial standards do not require the bank to examine the instrument if the failure to examine does not violate the bank's prescribed procedures and the bank's procedures do not vary unreasonably from general banking usage not disapproved by this chapter or Chapter 4.
- (8) "Party" means a party to an instrument.

(9) "Promise" means a written undertaking to pay money signed by the person undertaking to pay. An acknowledgment of an obligation by the obligor is not a promise unless the obligor also undertakes to pay the obligation.

(10) "Prove" with respect to a fact means to meet the burden of establishing the fact ([Section 75-1-201\(8\), Mississippi Code of 1972](#)).

(11) "Remitter" means a person who purchases an instrument from its issuer if the instrument is payable to an identified person other than the purchaser.

(b) Other definitions applying to this chapter and the sections in which they appear are:

"Acceptance"	Section 75-3-409
"Accommodated party"	Section 75-3-419
"Accommodation party"	Section 75-3-419
"Alteration"	Section 75-3-407
"Anomalous indorsement"	Section 75-3-205
"Blank indorsement"	Section 75-3-205
"Cashier's check"	Section 75-3-104
"Certificate of deposit"	Section 75-3-104
"Certified check"	Section 75-3-409
"Check"	Section 75-3-104
"Consideration"	Section 75-3-303
"Draft"	Section 75-3-104
"Holder in due course"	Section 75-3-302
"Incomplete instrument"	Section 75-3-115
"Indorsement"	Section 75-3-204
"Indorser"	Section 75-3-204
"Instrument"	Section 75-3-104

“Issue”	Section 75-3-105
“Issuer”	Section 75-3-105
“Negotiable instrument”	Section 75-3-104
“Negotiation”	Section 75-3-201
“Note”	Section 75-3-104
“Payable at a definite time”	Section 75-3-108
“Payable on demand”	Section 75-3-108
“Payable to bearer”	Section 75-3-109
“Payable to order”	Section 75-3-109
“Payment”	Section 75-3-602
“Person entitled to enforce”	Section 75-3-301
“Presentment”	Section 75-3-501
“Reacquisition”	Section 75-3-207
“Special indorsement”	Section 75-3-205
“Teller’s check”	Section 75-3-104
“Transfer of instrument”	Section 75-3-203
“Traveler’s check”	Section 75-3-104
“Value”	Section 75-3-303
(c) The following definitions in other chapters apply to this chapter:	
“Bank”	Section 75-4-105
“Banking day”	Section 75-4-104
“Clearinghouse”	Section 75-4-104
“Collecting bank”	Section 75-4-105

“Depository bank”	Section 75-4-105
“Documentary draft”	Section 75-4-104
“Intermediary bank”	Section 75-4-105
“Item”	Section 75-4-104
“Payor bank”	Section 75-4-105
“Suspends payments”	Section 75-4-104

(d) In addition, Chapter 1 contains general definitions and principles of construction and interpretation applicable throughout this chapter.

**§ 75-3-104. Negotiable Instrument**

(a) Except as provided in subsections (c) and (d), “negotiable instrument” means an unconditional promise or order to pay a fixed amount of money, with or without interest or other charges described in the promise or order, if it:

(1) Is payable to bearer or to order at the time it is issued or first comes into possession of a holder;

(2) Is payable on demand or at a definite time; and

(3) Does not state any other undertaking or instruction by the person promising or ordering payment to do any act in addition to the payment of money, but the promise or order may contain (i) an undertaking or power to give, maintain, or protect collateral to secure payment, (ii) an authorization or power to the holder to confess judgment or realize on or dispose of collateral, or (iii) a waiver of the benefit of any law intended for the advantage or protection of an obligor.

(b) “Instrument” means a negotiable instrument.

(c) An order that meets all of the requirements of subsection (a), except paragraph (1), and otherwise falls within the definition of “check” in subsection (f) is a negotiable instrument and a check.

(d) A promise or order other than a check is not an instrument if, at the time it is issued or first comes into possession of a holder, it contains a conspicuous statement, however expressed, to the effect that the promise or order is not negotiable or is not an instrument governed by this chapter.

(e) An instrument is a “note” if it is a promise and is a “draft” if it is an order. If an instrument falls within the definition of both “note” and “draft,” a person entitled to enforce the instrument may treat it as either.

(f) “Check” means (i) a draft, other than a documentary draft, payable on demand and drawn on a bank or (ii) a cashier’s check or teller’s check. An instrument may be a check even though it is described on its face by another term, such as “money order.”

(g) “Cashier’s check” means a draft with respect to which the drawer and drawee are the same bank or branches of the same bank.

(h) "Teller's check" means a draft drawn by a bank (i) on another bank, or (ii) payable at or through a bank.

(i) "Traveler's check" means an instrument that (i) is payable on demand, (ii) is drawn on or payable at or through a bank, (iii) is designated by the term "traveler's check" or by a substantially similar term, and (iv) requires, as a condition to payment, a countersignature by a person whose specimen signature appears on the instrument.

(j) "Certificate of deposit" means an instrument containing an acknowledgment by a bank that a sum of money has been received by the bank and a promise by the bank to repay the sum of money. A certificate of deposit is a note of the bank.

#### § 75-3-105. Issue of Instrument

(a) "Issue" means the first delivery of an instrument by the maker or drawer, whether to a holder or nonholder, for the purpose of giving rights on the instrument to any person.

(b) An unissued instrument, or an unissued incomplete instrument that is completed, is binding on the maker or drawer, but nonissuance is a defense. An instrument that is conditionally issued or is issued for a special purpose is binding on the maker or drawer, but failure of the condition or special purpose to be fulfilled is a defense.

(c) "Issuer" applies to issued and unissued instruments and means a maker or drawer of an instrument.

#### § 75-3-106. Unconditional Promise or Order

(a) Except as provided in this section, for the purposes of [Section 75-3-104\(a\)](#), a promise or order is unconditional unless it states (i) an express condition to payment, (ii) that the promise or order is subject to or governed by another writing, or (iii) that rights or obligations with respect to the promise or order are stated in another writing. A reference to another writing does not of itself make the promise or order conditional.

(b) A promise or order is not made conditional (i) by a reference to another writing for a statement of rights with respect to collateral, prepayment, or acceleration, or (ii) because payment is limited to resort to a particular fund or source.

(c) If a promise or order requires, as a condition to payment, a countersignature by a person whose specimen signature appears on the promise or order, the condition does not make the promise or order conditional for the purposes of [Section 75-3-104\(a\)](#). If the person whose specimen signature appears on an instrument fails to countersign the instrument, the failure to countersign is a defense to the obligation of the issuer, but the failure does not prevent a transferee of the instrument from becoming a holder of the instrument.

(d) If a promise or order at the time it is issued or first comes into possession of a holder contains a statement, required by applicable statutory or administrative law, to the effect that the rights of a holder or transferee are subject to claims or defenses that the issuer could assert against the original payee, the promise or order is not thereby made conditional for the purposes of [Section 75-3-104\(a\)](#); but if the promise or order is an instrument, there cannot be a holder in due course of the instrument.

#### § 75-3-107. Instrument Payable in Foreign Money

Unless the instrument otherwise provides, an instrument that states the amount payable in foreign money may be paid in the foreign money or in an equivalent amount in dollars calculated by using the current bank-offered spot rate at the place of payment for the purchase of dollars on the day on which the instrument is paid.

#### § 75-3-108. Payable on Demand or at Definite Time

(a) A promise or order is "payable on demand" if it (i) states that it is payable on demand or at sight, or otherwise indicates that it is payable at the will of the holder, or (ii) does not state any time of payment.

(b) A promise or order is "payable at a definite time" if it is payable on elapse of a definite period of time after sight or acceptance or at a fixed date or dates or at a time or times readily ascertainable at the time the promise or order is issued, subject to rights of (i) prepayment, (ii) acceleration, (iii) extension at the option of the holder, or (iv) extension to a further definite time at the option of the maker or acceptor or automatically upon or after a specified act or event.

(c) If an instrument, payable at a fixed date, is also payable upon demand made before the fixed date, the instrument is payable on demand until the fixed date and, if demand for payment is not made before that date, becomes payable at a definite time on the fixed date.

#### § 75-3-109. Payable to Bearer or to Order

(a) A promise or order is payable to bearer if it:

(1) States that it is payable to bearer or to the order of bearer or otherwise indicates that the person in possession of the promise or order is entitled to payment;

(2) Does not state a payee; or

(3) States that it is payable to or to the order of cash or otherwise indicates that it is not payable to an identified person.

(b) A promise or order that is not payable to bearer is payable to order if it is payable (i) to the order of an identified person or (ii) to an identified person or order. A promise or order that is payable to order is payable to the identified person.

(c) An instrument payable to bearer may become payable to an identified person if it is specially indorsed pursuant to [Section 75-3-205\(a\)](#). An instrument payable to an identified person may become payable to bearer if it is indorsed in blank pursuant to [Section 75-3-205\(b\)](#).

#### § 75-3-110. Identification of Person to Whom Instrument is Payable

(a) The person to whom an instrument is initially payable is determined by the intent of the person, whether or not authorized, signing as, or in the name or behalf of, the issuer of the instrument. The instrument is payable to the person intended by the signer even if that person is identified in the instrument by a name or other identification that is not that of the intended person. If more than one (1) person signs in the name or behalf of the issuer of an instrument and all the signers do not intend the same person as payee, the instrument is payable to any person intended by one or more of the signers.

(b) If the signature of the issuer of an instrument is made by automated means, such as a check-writing machine, the payee of the instrument is determined by the intent of the person who supplied the name or identification of the payee, whether or not authorized to do so.

(c) A person to whom an instrument is payable may be identified in any way, including by name, identifying number, office, or account number. For the purpose of determining the holder of an instrument, the following rules apply:

(1) If an instrument is payable to an account and the account is identified only by number, the instrument is payable to the person to whom the account is payable. If an instrument is payable to an account identified by number and by the name of a person, the instrument is payable to the named person, whether or not that person is the owner of the account identified by

number.

(2) If an instrument is payable to:

- (i) A trust, an estate, or a person described as trustee or representative of a trust or estate, the instrument is payable to the trustee, the representative, or a successor of either, whether or not the beneficiary or estate is also named;
  - (ii) A person described as agent or similar representative of a named or identified person, the instrument is payable to the represented person, the representative, or a successor of the representative;
  - (iii) A fund or organization that is not a legal entity, the instrument is payable to a representative of the members of the fund or organization; or
  - (iv) An office or to a person described as holding an office, the instrument is payable to the named person, the incumbent of the office, or a successor to the incumbent.
- (d) If an instrument is payable to two (2) or more persons alternatively, it is payable to any of them and may be negotiated, discharged, or enforced by any or all of them in possession of the instrument. If an instrument is payable to two (2) or more persons not alternatively, it is payable to all of them and may be negotiated, discharged, or enforced only by all of them. If an instrument payable to two (2) or more persons is ambiguous as to whether it is payable to the persons alternatively, the instrument is payable to the persons alternatively.

#### § 75-3-111. Place of Payment

Except as otherwise provided for items in Chapter 4, an instrument is payable at the place of payment stated in the instrument. If no place of payment is stated, an instrument is payable at the address of the drawee or maker stated in the instrument. If no address is stated, the place of payment is the place of business of the drawee or maker. If a drawee or maker has more than one (1) place of business, the place of payment is any place of business of the drawee or maker chosen by the person entitled to enforce the instrument. If the drawee or maker has no place of business, the place of payment is the residence of the drawee or maker.

#### § 75-3-112. Interest

- (a) Unless otherwise provided in the instrument, (i) an instrument is not payable with interest, and (ii) interest on an interest-bearing instrument is payable from the date of the instrument.
- (b) Interest may be stated in an instrument as a fixed or variable amount of money or it may be expressed as a fixed or variable rate or rates. The amount or rate of interest may be stated or described in the instrument in any manner and may require reference to information not contained in the instrument. If an instrument provides for interest, but the amount of interest payable cannot be ascertained from the description, interest is payable at the judgment rate in effect at the place of payment of the instrument and at the time interest first accrues.

#### § 75-3-113. Date of Instrument

- (a) An instrument may be antedated or postdated. The date stated determines the time of payment if the instrument is payable at a fixed period after date. Except as provided in [Section 75-4-401\(c\)](#), an instrument payable on demand is not payable before the date of the instrument.
- (b) If an instrument is undated, its date is the date of its issue or, in the case of an unissued instrument, the date it first comes

into possession of a holder.

#### § 75-3-114. Contradictory Terms of Instrument

If an instrument contains contradictory terms, typewritten terms prevail over printed terms, handwritten terms prevail over both, and words prevail over numbers.

#### § 75-3-115. Incomplete Instrument

- (a) "Incomplete instrument" means a signed writing, whether or not issued by the signer, the contents of which show at the time of signing that it is incomplete but that the signer intended it to be completed by the addition of words or numbers.
- (b) Subject to subsection (c), if an incomplete instrument is an instrument under [Section 75-3-104](#), it may be enforced according to its terms if it is not completed, or according to its terms as augmented by completion. If an incomplete instrument is not an instrument under [Section 75-3-104](#), but, after completion, the requirements of [Section 75-3-104](#) are met, the instrument may be enforced according to its terms as augmented by completion.
- (c) If words or numbers are added to an incomplete instrument without authority of the signer, there is an alteration of the incomplete instrument under [Section 75-3-407](#).
- (d) The burden of establishing that words or numbers were added to an incomplete instrument without authority of the signer is on the person asserting the lack of authority.

#### § 75-3-116. Joint and Several Liability, Contribution

- (a) Except as otherwise provided in the instrument, two (2) or more persons who have the same liability on an instrument as makers, drawers, acceptors, indorsers who indorse as joint payees, or anomalous indorsers are jointly and severally liable in the capacity in which they sign.
- (b) Except as provided in [Section 75-3-419\(e\)](#) or by agreement of the affected parties, a party having joint and several liability who pays the instrument is entitled to receive from any party having the same joint and several liability contribution in accordance with applicable law.
- (c) Discharge of one (1) party having joint and several liability by a person entitled to enforce the instrument does not affect the right under subsection (b) of a party having the same joint and several liability to receive contribution from the party discharged.

#### § 75-3-117. Other Agreements Affecting Instrument

Subject to applicable law regarding exclusion of proof of contemporaneous or previous agreements, the obligation of a party to an instrument to pay the instrument may be modified, supplemented, or nullified by a separate agreement of the obligor and a person entitled to enforce the instrument, if the instrument is issued or the obligation is incurred in reliance on the agreement or as part of the same transaction giving rise to the agreement. To the extent an obligation is modified, supplemented, or nullified by an agreement under this section, the agreement is a defense to the obligation.

#### § 75-3-118. Statute of Limitations

- (a) Except as provided in subsection (e), an action to enforce the obligation of a party to pay a note payable at a definite time must be commenced within six (6) years after the due date or dates stated in the note or, if a due date is accelerated, within six

(6) years after the accelerated due date.

(b) Except as provided in subsection (d) or (e), if demand for payment is made to the maker of a note payable on demand, an action to enforce the obligation of a party to pay the note must be commenced within six (6) years after the demand. If no demand for payment is made to the maker, an action to enforce the note is barred if neither principal nor interest on the note has been paid for a continuous period of ten (10) years.

(c) Except as provided in subsection (d), an action to enforce the obligation of a party to an unaccepted draft to pay the draft must be commenced within three (3) years after dishonor of the draft or ten (10) years after the date of the draft, whichever period expires first.

(d) An action to enforce the obligation of the acceptor of a certified check or the issuer of a teller's check, cashier's check, or traveler's check must be commenced within three (3) years after demand for payment is made to the acceptor or issuer, as the case may be.

(e) An action to enforce the obligation of a party to a certificate of deposit to pay the instrument must be commenced within six (6) years after demand for payment is made to the maker, but if the instrument states a due date and the maker is not required to pay before that date, the six-year period begins when a demand for payment is in effect and the due date has passed.

(f) An action to enforce the obligation of a party to pay an accepted draft, other than a certified check, must be commenced (i) within six (6) years after the due date or dates stated in the draft or acceptance if the obligation of the acceptor is payable at a definite time, or (ii) within six (6) years after the date of the acceptance if the obligation of the acceptor is payable on demand.

(g) Unless governed by other law regarding claims for indemnity or contribution, an action (i) for conversion of an instrument, for money had and received, or like action based on conversion, (ii) for breach of warranty, or (iii) to enforce an obligation, duty, or right arising under this chapter and not governed by this section must be commenced within three (3) years after the cause of action accrues.

#### § 75-3-119. Notice of Right to Defend Action

In an action for breach of an obligation for which a third person is answerable over pursuant to this chapter or Chapter 4, the defendant may give the third person written notice of the litigation, and the person notified may then give similar notice to any other person who is answerable over. If the notice states (i) that the person notified may come in and defend and (ii) that failure to do so will bind the person notified in an action later brought by the person giving the notice as to any determination of fact common to the two (2) litigations, the person notified is so bound unless after reasonable receipt of the notice the person notified does come in and defend.

#### §§ 75-3-120 to 75-3-122. Repealed by Laws 1992, Ch. 420, § 112, eff. January 1, 1993

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#### § 75-3-201. Negotiation

(a) "Negotiation" means a transfer of possession, whether voluntary or involuntary, of an instrument by a person other than the issuer to a person who thereby becomes its holder.

(b) Except for negotiation by a remitter, if an instrument is payable to an identified person, negotiation requires transfer of possession of the instrument and its indorsement by the holder. If an instrument is payable to bearer, it may be negotiated by transfer of possession alone.

#### § 75-3-202. Negotiation Subject to Rescission

(a) Negotiation is effective even if obtained (i) from an infant, a corporation exceeding its powers, or a person without capacity, (ii) by fraud, duress, or mistake, or (iii) in breach of duty or as part of an illegal transaction.

(b) To the extent permitted by other law, negotiation may be rescinded or may be subject to other remedies, but those remedies may not be asserted against a subsequent holder in due course or a person paying the instrument in good faith and without knowledge of facts that are a basis for rescission or other remedy.

#### § 75-3-203. Transfer of Instrument; Rights Acquired by Transfer

(a) An instrument is transferred when it is delivered by a person other than its issuer for the purpose of giving to the person receiving delivery the right to enforce the instrument.

(b) Transfer of an instrument, whether or not the transfer is a negotiation, vests in the transferee any right of the transferor to enforce the instrument, including any right as a holder in due course, but the transferee cannot acquire rights of a holder in due course by a transfer, directly or indirectly, from a holder in due course if the transferee engaged in fraud or illegality affecting the instrument.

(c) Unless otherwise agreed, if an instrument is transferred for value and the transferee does not become a holder because of lack of indorsement by the transferor, the transferee has a specifically enforceable right to the unqualified indorsement of the transferor, but negotiation of the instrument does not occur until the indorsement is made.

(d) If a transferor purports to transfer less than the entire instrument, negotiation of the instrument does not occur. The transferee obtains no rights under this chapter and has only the rights of a partial assignee.

#### § 75-3-204. Indorsement

(a) "Indorsement" means a signature, other than that of a signer as maker, drawer, or acceptor, that alone or accompanied by other words is made on an instrument for the purpose of (i) negotiating the instrument, (ii) restricting payment of the instrument, or (iii) incurring indorser's liability on the instrument, but regardless of the intent of the signer, a signature and its accompanying words is an indorsement unless the accompanying words, terms of the instrument, place of the signature, or other circumstances unambiguously indicate that the signature was made for a purpose other than indorsement. For the purpose of determining whether a signature is made on an instrument, a paper affixed to the instrument is a part of the instrument; provided, however, that an indorsement of instruments representing student loans, including loans that are insured by the United States Secretary of Education under [20 U.S.C.A. 1071, et seq.](#), as amended, or by a state or nonprofit private institution or organization with which the United States Secretary of Education has an agreement under [20 U.S.C.A. 1078\(b\)](#) as amended, may be made by signed blanket indorsement, rather than in the manner otherwise provided in this subsection, if a notation to that effect is made in the name of the transferee on the instrument representing the student loan.

(b) "Indorser" means a person who makes an indorsement.

(c) For the purpose of determining whether the transferee of an instrument is a holder, an indorsement that transfers a security interest in the instrument is effective as an unqualified indorsement of the instrument.

(d) If an instrument is payable to a holder under a name that is not the name of the holder, indorsement may be made by the holder in the name stated in the instrument or in the holder's name or both, but signature in both names may be required by a person paying or taking the instrument for value or collection.

**§ 75-3-205. Special Indorsement; Blank Indorsement; Anomalous Indorsement**

(a) If an indorsement is made by the holder of an instrument, whether payable to an identified person or payable to bearer, and the indorsement identifies a person to whom it makes the instrument payable, it is a "special indorsement." When specially indorsed, an instrument becomes payable to the identified person and may be negotiated only by the indorser of that person. The principles stated in [Section 75-3-110](#) apply to special indorsements.

(b) If an indorsement is made by the holder of an instrument and it is not a special indorsement, it is a "blank indorsement." When indorsed in blank, an instrument becomes payable to bearer and may be negotiated by transfer of possession alone until specially indorsed.

(c) The holder may convert a blank indorsement that consists only of a signature into a special indorsement by writing, above the signature of the indorser, words identifying the person to whom the instrument is made payable.

(d) "Anomalous indorsement" means an indorsement made by a person who is not the holder of the instrument. An anomalous indorsement does not affect the manner in which the instrument may be negotiated.

**§ 75-3-206. Restrictive Indorsement**

(a) An indorsement limiting payment to a particular person or otherwise prohibiting further transfer or negotiation of the instrument is not effective to prevent further transfer or negotiation of the instrument.

(b) An indorsement stating a condition to the right of the indorsee to receive payment does not affect the right of the indorsee to enforce the instrument. A person paying the instrument or taking it for value or collection may disregard the condition, and the rights and liabilities of that person are not affected by whether the condition has been fulfilled.

(c) If an instrument bears an indorsement (i) described in [Section 75-4-201\(b\)](#), or (ii) in blank or to a particular bank using the words "for deposit," "for collection," or other words indicating a purpose of having the instrument collected by a bank for the indorser or for a particular account, the following rules apply:

(1) A person, other than a bank, who purchases the instrument when so indorsed converts the instrument unless the amount paid for the instrument is received by the indorser or applied consistently with the indorsement.

(2) A depository bank that purchases the instrument or takes it for collection when so indorsed converts the instrument unless the amount paid by the bank with respect to the instrument is received by the indorser or applied consistently with the indorsement.

(3) A payor bank that is also the depository bank or that takes the instrument for immediate payment over the counter from a person other than a collecting bank converts the instrument unless the proceeds of the instrument are received by the indorser or applied consistently with the indorsement.

(4) Except as otherwise provided in paragraph (3), a payor bank or intermediary bank may disregard the indorsement and is not liable if the proceeds of the instrument are not received by the indorser or applied consistently with the indorsement.

(d) Except for an indorsement covered by subsection (c), if an instrument bears an indorsement using words to the effect that

payment is to be made to the indorsee as agent, trustee, or other fiduciary for the benefit of the indorser or another person, the following rules apply:

(1) Unless there is notice of breach of fiduciary duty as provided in [Section 75-3-307](#), a person who purchases the instrument from the indorsee or takes the instrument from the indorsee for collection or payment may pay the proceeds of payment or the value given for the instrument to the indorsee without regard to whether the indorsee violates a fiduciary duty to the indorser.

(2) A subsequent transferee of the instrument or person who pays the instrument is neither given notice nor otherwise affected by the restriction in the indorsement unless the transferee or payor knows that the fiduciary dealt with the instrument or its proceeds in breach of fiduciary duty.

(e) The presence on an instrument of an indorsement to which this section applies does not prevent a purchaser of the instrument from becoming a holder in due course of the instrument unless the purchaser is a converter under subsection (c) or has notice or knowledge of breach of fiduciary duty as stated in subsection (d).

(f) In an action to enforce the obligation of a party to pay the instrument, the obligor has a defense if payment would violate an indorsement to which this section applies and the payment is not permitted by this section.

**§ 75-3-207. Reacquisition**

Reacquisition of an instrument occurs if it is transferred to a former holder, by negotiation or otherwise. A former holder who reacquires the instrument may cancel indorsements made after the reacquirer first became a holder of the instrument. If the cancellation causes the instrument to be payable to the reacquirer or to bearer, the reacquirer may negotiate the instrument. An indorser whose indorsement is canceled is discharged, and the discharge is effective against any subsequent holder.

**§ 75-3-208. Repealed by Laws 1992, Ch. 420, § 112, eff. January 1, 1993**

**§ 75-3-301. Person Entitled to Enforce Instrument**

"Person entitled to enforce" an instrument means (i) the holder of the instrument, (ii) a nonholder in possession of the instrument who has the rights of a holder, or (iii) a person not in possession of the instrument who is entitled to enforce the instrument pursuant to [Section 75-3-309](#) or [75-3-418\(d\)](#). A person may be a person entitled to enforce the instrument even though the person is not the owner of the instrument or is in wrongful possession of the instrument.

**§ 75-3-302. Holder in Due Course**

(a) Subject to subsection (c) and [Section 75-3-106\(d\)](#), "holder in due course" means the holder of an instrument if:

(1) The instrument when issued or negotiated to the holder does not bear such apparent evidence of forgery or alteration or is not otherwise so irregular or incomplete as to call into question its authenticity; and

(2) The holder took the instrument (i) for value, (ii) in good faith, (iii) without notice that the instrument is overdue or has been dishonored or that there is an uncured default with respect to payment of another instrument issued as part of the same series, (iv) without notice that the instrument contains an unauthorized signature or has been altered, (v) without notice of any claim to the instrument described in [Section 75-3-306](#), and (vi) without notice that any party has a defense or claim in recoupment described in [Section 75-3-305\(a\)](#).

(b) Notice of discharge of a party, other than discharge in an insolvency proceeding, is not notice of a defense under subsection (a), but discharge is effective against a person who became a holder in due course with notice of the discharge. Public

filing or recording of a document does not of itself constitute notice of a defense, claim in recoupment, or claim to the instrument.

(c) Except to the extent a transferor or predecessor in interest has rights as a holder in due course, a person does not acquire rights of a holder in due course of an instrument taken (i) by legal process or by purchase in an execution, bankruptcy, or creditor's sale or similar proceeding, (ii) by purchase as part of a bulk transaction not in ordinary course of business of the transferor, or (iii) as the successor in interest to an estate or other organization.

(d) If, under [Section 75-3-303\(a\)\(1\)](#), the promise of performance that is the consideration for an instrument has been partially performed, the holder may assert rights as a holder in due course of the instrument only to the fraction of the amount payable under the instrument equal to the value of the partial performance divided by the value of the promised performance.

(e) If (i) the person entitled to enforce an instrument has only a security interest in the instrument and (ii) the person obliged to pay the instrument has a defense, claim in recoupment, or claim to the instrument that may be asserted against the person who granted the security interest, the person entitled to enforce the instrument may assert rights as a holder in due course only to an amount payable under the instrument which, at the time of enforcement of the instrument, does not exceed the amount of the unpaid obligation secured.

(f) To be effective, notice must be received at a time and in a manner that gives a reasonable opportunity to act on it.

(g) This section is subject to any law limiting status as a holder in due course in particular classes of transactions.

#### [§ 75-3-303. Value and Consideration](#)

(a) An instrument is issued or transferred for value if:

- (1) The instrument is issued or transferred for a promise of performance, to the extent the promise has been performed;
- (2) The transferee acquires a security interest or other lien in the instrument other than a lien obtained by judicial proceeding;
- (3) The instrument is issued or transferred as payment of, or as security for, an antecedent claim against any person, whether or not the claim is due;
- (4) The instrument is issued or transferred in exchange for a negotiable instrument; or
- (5) The instrument is issued or transferred in exchange for the incurring of an irrevocable obligation to a third party by the person taking the instrument.

(b) "Consideration" means any consideration sufficient to support a simple contract. The drawer or maker of an instrument has a defense if the instrument is issued without consideration. If an instrument is issued for a promise of performance, the issuer has a defense to the extent performance of the promise is due and the promise has not been performed. If an instrument is issued for value as stated in subsection (a), the instrument is also issued for consideration.

#### [§ 75-3-304. Overdue Instrument](#)

(a) An instrument payable on demand becomes overdue at the earliest of the following times:

- (1) On the day after the day demand for payment is duly made;

(2) If the instrument is a check, ninety (90) days after its date; or

(3) If the instrument is not a check, when the instrument has been outstanding for a period of time after its date which is unreasonably long under the circumstances of the particular case in light of the nature of the instrument and usage of the trade.

(b) With respect to an instrument payable at a definite time the following rules apply:

(1) If the principal is payable in installments and a due date has not been accelerated, the instrument becomes overdue upon default under the instrument for nonpayment of an installment, and the instrument remains overdue until the default is cured.

(2) If the principal is not payable in installments and the due date has not been accelerated, the instrument becomes overdue on the day after the due date.

(3) If a due date with respect to principal has been accelerated, the instrument becomes overdue on the day after the accelerated due date.

(c) Unless the due date of principal has been accelerated, an instrument does not become overdue if there is default in payment of interest but no default in payment of principal.

#### [§ 75-3-305. Defenses and Claims in Recoupment](#)

(a) Except as stated in subsection (b), the right to enforce the obligation of a party to pay an instrument is subject to the following:

(1) A defense of the obligor based on (i) infancy of the obligor to the extent it is a defense to a simple contract, (ii) duress, lack of legal capacity, or illegality of the transaction which, under other law, nullifies the obligation of the obligor, (iii) fraud that induced the obligor to sign the instrument with neither knowledge nor reasonable opportunity to learn of its character or its essential terms, or (iv) discharge of the obligor in insolvency proceedings;

(2) A defense of the obligor stated in another section of this chapter or a defense of the obligor that would be available if the person entitled to enforce the instrument were enforcing a right to payment under a simple contract; and

(3) A claim in recoupment of the obligor against the original payee of the instrument if the claim arose from the transaction that gave rise to the instrument; but the claim of the obligor may be asserted against a transferee of the instrument only to reduce the amount owing on the instrument at the time the action is brought.

(b) The right of a holder in due course to enforce the obligation of a party to pay the instrument is subject to defenses of the obligor stated in subsection (a)(1), but is not subject to defenses of the obligor stated in subsection (a)(2) or claims in recoupment stated in subsection (a)(3) against a person other than the holder.

(c) Except as stated in subsection (d), in an action to enforce the obligation of a party to pay the instrument, the obligor may not assert against the person entitled to enforce the instrument a defense, claim in recoupment, or claim to the instrument ([Section 75-3-306](#)) of another person, but the other person's claim to the instrument may be asserted by the obligor if the other person is joined in the action and personally asserts the claim against the person entitled to enforce the instrument. An obligor is not obliged to pay the instrument if the person seeking enforcement of the instrument does not have rights of a holder in due course and the obligor proves that the instrument is a lost or stolen instrument.

(d) In an action to enforce the obligation of an accommodation party to pay an instrument, the accommodation party may assert against the person entitled to enforce the instrument any defense or claim in recoupment under subsection (a) that the accommodated party could assert against the person entitled to enforce the instrument, except the defenses of discharge in insolvency proceedings, infancy, and lack of legal capacity.

#### § 75-3-306. Claims to an Instrument

A person taking an instrument, other than a person having rights of a holder in due course, is subject to a claim of a property or possessory right in the instrument or its proceeds, including a claim to rescind a negotiation and to recover the instrument or its proceeds. A person having rights of a holder in due course takes free of the claim to the instrument.

#### § 75-3-307. Notice of Breach of Fiduciary Duty

(a) In this section:

(1) "Fiduciary" means an agent, trustee, partner, corporate officer or director, or other representative owing a fiduciary duty with respect to an instrument.

(2) "Represented person" means the principal, beneficiary, partnership, corporation, or other person to whom the duty stated in paragraph (1) is owed.

(b) If (i) an instrument is taken from a fiduciary for payment or collection or for value, (ii) the taker has knowledge of the fiduciary status of the fiduciary, and (iii) the represented person makes a claim to the instrument or its proceeds on the basis that the transaction of the fiduciary is a breach of fiduciary duty, the following rules apply:

(1) Notice of breach of fiduciary duty by the fiduciary is notice of the claim of the represented person.

(2) In the case of an instrument payable to the represented person or the fiduciary as such, the taker has notice of the breach of fiduciary duty if the instrument is (i) taken in payment of or as security for a debt known by the taker to be the personal debt of the fiduciary, (ii) taken in a transaction known by the taker to be for the personal benefit of the fiduciary, or (iii) deposited to an account other than an account of the fiduciary, as such, or an account of the represented person.

(3) If an instrument is issued by the represented person or the fiduciary as such, and made payable to the fiduciary personally, the taker does not have notice of the breach of fiduciary duty unless the taker knows of the breach of fiduciary duty.

(4) If an instrument is issued by the represented person or the fiduciary as such, to the taker as payee, the taker has notice of the breach of fiduciary duty if the instrument is (i) taken in payment of or as security for a debt known by the taker to be the personal debt of the fiduciary, (ii) taken in a transaction known by the taker to be for the personal benefit of the fiduciary, or (iii) deposited to an account other than an account of the fiduciary, as such, or an account of the represented person.

#### § 75-3-308. Proof of Signatures and Status as Holder in Due Course

(a) In an action with respect to an instrument, the authenticity of, and authority to make, each signature on the instrument is admitted unless specifically denied in the pleadings. If the validity of a signature is denied in the pleadings, the burden of establishing validity is on the person claiming validity, but the signature is presumed to be authentic and authorized unless the action is to enforce the liability of the purported signer and the signer is dead or incompetent at the time of trial of the issue of validity of the signature. If an action to enforce the instrument is brought against a person as the undisclosed principal of a person who signed the instrument as a party to the instrument, the plaintiff has the burden of establishing that the defendant is liable on the instrument as a represented person under [Section 75-3-402\(a\)](#).

(b) If the validity of signatures is admitted or proved and there is compliance with subsection (a), a plaintiff producing the instrument is entitled to payment if the plaintiff proves entitlement to enforce the instrument under [Section 75-3-301](#), unless the defendant proves a defense or claim in recoupment. If a defense or claim in recoupment is proved, the right to payment of the plaintiff is subject to the defense or claim, except to the extent the plaintiff proves that the plaintiff has rights of a holder in due course which are not subject to the defense or claim.

#### § 75-3-309. Enforcement of Lost, Destroyed, or Stolen Instrument

(a) A person not in possession of an instrument is entitled to enforce the instrument if (i) the person was in possession of the instrument and entitled to enforce it when loss of possession occurred, (ii) the loss of possession was not the result of a transfer by the person or a lawful seizure, and (iii) the person cannot reasonably obtain possession of the instrument because the instrument was destroyed, its whereabouts cannot be determined, or it is in the wrongful possession of an unknown person or a person that cannot be found or is not amenable to service of process.

(b) A person seeking enforcement of an instrument under subsection (a) must prove the terms of the instrument and the person's right to enforce the instrument. If that proof is made, [Section 75-3-308](#) applies to the case as if the person seeking enforcement had produced the instrument. The court may not enter judgment in favor of the person seeking enforcement unless it finds that the person required to pay the instrument is adequately protected against loss that might occur by reason of a claim by another person to enforce the instrument. Adequate protection may be provided by any reasonable means.

#### § 75-3-310. Effect of Instrument on Obligation for Which Taken

(a) Unless otherwise agreed, if a certified check, cashier's check, or teller's check is taken for an obligation, the obligation is discharged to the same extent discharge would result if an amount of money equal to the amount of the instrument were taken in payment of the obligation. Discharge of the obligation does not affect any liability that the obligor may have as an indorser of the instrument.

(b) Unless otherwise agreed and except as provided in subsection (a), if a note or an uncertified check is taken for an obligation, the obligation is suspended to the same extent the obligation would be discharged if an amount of money equal to the amount of the instrument were taken, and the following rules apply:

(1) In the case of an uncertified check, suspension of the obligation continues until dishonor of the check or until it is paid or certified. Payment or certification of the check results in discharge of the obligation to the extent of the amount of the check.

(2) In the case of a note, suspension of the obligation continues until dishonor of the note or until it is paid. Payment of the note results in discharge of the obligation to the extent of the payment.

(3) Except as provided in paragraph (4), if the check or note is dishonored and the obligee of the obligation for which the instrument was taken is the person entitled to enforce the instrument, the obligee may enforce either the instrument or the obligation. In the case of an instrument of a third person which is negotiated to the obligee by the obligor, discharge of the obligor on the instrument also discharges the obligation.

(4) If the person entitled to enforce the instrument taken for an obligation is a person other than the obligee, the obligee may not enforce the obligation to the extent the obligation is suspended. If the obligee is the person entitled to enforce the instrument but no longer has possession of it because it was lost, stolen, or destroyed, the obligation may not be enforced to the extent of the amount payable on the instrument, and to that extent the obligee's rights against the obligor are limited to enforcement of the instrument.

(c) If an instrument other than one described in subsection (a) or (b) is taken for an obligation, the effect is (i) that stated in subsection (a) if the instrument is one on which a bank is liable as maker or acceptor, or (ii) that stated in subsection (b) in any other case.

#### § 75-3-311. Accord and Satisfaction by Use of Instrument

(a) If a person against whom a claim is asserted proves that (i) that person in good faith tendered an instrument to the claimant as full satisfaction of the claim, (ii) the amount of the claim was unliquidated or subject to a bona fide dispute, and (iii) the claimant obtained payment of the instrument, the following subsections apply.

(b) Unless subsection (c) applies, the claim is discharged if the person against whom the claim is asserted proves that the instrument or an accompanying written communication contained a conspicuous statement to the effect that the instrument was tendered as full satisfaction of the claim.

(c) Subject to subsection (d), a claim is not discharged under subsection (b) if either of the following applies:

(1) The claimant, if an organization, proves that (i) within a reasonable time before the tender, the claimant sent a conspicuous statement to the person against whom the claim is asserted that communications concerning disputed debts, including an instrument tendered as full satisfaction of a debt, are to be sent to a designated person, office, or place, and (ii) the instrument or accompanying communication was not received by that designated person, office, or place.

(2) The claimant, whether or not an organization, proves that within ninety (90) days after payment of the instrument, the claimant tendered repayment of the amount of the instrument to the person against whom the claim is asserted. This paragraph does not apply if the claimant is an organization that sent a statement complying with paragraph (1)(i).

(d) A claim is discharged if the person against whom the claim is asserted proves that within a reasonable time before collection of the instrument was initiated, the claimant, or an agent of the claimant having direct responsibility with respect to the disputed obligation, knew that the instrument was tendered in full satisfaction of the claim.

#### § 75-3-312. Lost, Destroyed, or Stolen Cashier's Check, Teller's Check, or Certified Check

(a) In this section:

(1) "Check" means a cashier's check, teller's check, or certified check.

(2) "Claimant" means a person who claims the right to receive the amount of a cashier's check, teller's check, or certified check that was lost, destroyed, or stolen.

(3) "Declaration of loss" means a written statement, made under penalty of perjury, to the effect that (i) the declarer lost possession of a check, (ii) the declarer is the drawer or payee of the check, in the case of a certified check, or the remitter or payee of the check, in the case of a cashier's check or teller's check, (iii) the loss of possession was not the result of a transfer by the declarer or a lawful seizure, and (iv) the declarer cannot reasonably obtain possession of the check because the check was destroyed, its whereabouts cannot be determined, or it is in the wrongful possession of an unknown person or a person that cannot be found or is not amenable to service of process.

(4) "Obligated bank" means the issuer of a cashier's check or teller's check or the acceptor of a certified check.

(b) A claimant may assert a claim to the amount of a check by a communication to the obligated bank describing the check with reasonable certainty and requesting payment of the amount of the check, if (i) the claimant is the drawer or payee of a

certified check or the remitter or payee of a cashier's check or teller's check, (ii) the communication contains or is accompanied by a declaration of loss of the claimant with respect to the check, (iii) the communication is received at a time and in a manner affording the bank a reasonable time to act on it before the check is paid, and (iv) the claimant provides reasonable identification if requested by the obligated bank. Delivery of a declaration of loss is a warranty of the truth of the statements made in the declaration. If a claim is asserted in compliance with this subsection, the following rules apply:

(1) The claim becomes enforceable at the later of (i) the time the claim is asserted, or (ii) the ninetieth day following the date of the check, in the case of a cashier's check or teller's check, or the ninetieth day following the date of acceptance, in the case of a certified check.

(2) Until the claim becomes enforceable, it has no legal effect and the obligated bank may pay the check or, in the case of a teller's check, may permit the drawee to pay the check. Payment to a person entitled to enforce the check discharges all liability of the obligated bank with respect to the check.

(3) If the claim becomes enforceable before the check is presented for payment, the obligated bank is not obliged to pay the check.

(4) When the claim becomes enforceable, the obligated bank becomes obliged to pay the amount of the check to the claimant if payment of the check has not been made to a person entitled to enforce the check. Subject to [Section 75-4-302\(a\)\(1\)](#), payment to the claimant discharges all liability of the obligated bank with respect to the check.

(c) If the obligated bank pays the amount of a check to a claimant under subsection (b)(4) and the check is presented for payment by a person having rights of a holder in due course, the claimant is obliged to (i) refund the payment to the obligated bank if the check is paid, or (ii) pay the amount of the check to the person having rights of a holder in due course if the check is dishonored.

(d) If a claimant has the right to assert a claim under subsection (b) and is also a person entitled to enforce a cashier's check, teller's check, or certified check which is lost, destroyed, or stolen, the claimant may assert rights with respect to the check either under this section or [Section 75-3-309](#).

#### § 75-3-401. Signature

(a) A person is not liable on an instrument unless (i) the person signed the instrument, or (ii) the person is represented by an agent or representative who signed the instrument and the signature is binding on the represented person under [Section 75-3-402](#).

(b) A signature may be made (i) manually or by means of a device or machine, and (ii) by the use of any name, including a trade or assumed name, or by a word, mark, or symbol executed or adopted by a person with present intention to authenticate a writing.

#### § 75-3-402. Signature by Representative

(a) If a person acting, or purporting to act, as a representative signs an instrument by signing either the name of the represented person or the name of the signer, the represented person is bound by the signature to the same extent the represented person would be bound if the signature were on a simple contract. If the represented person is bound, the signature of the representative is the "authorized signature of the represented person" and the represented person is liable on the instrument, whether or not identified in the instrument.

(b) If a representative signs the name of the representative to an instrument and the signature is an authorized signature of the

represented person, the following rules apply:

- (1) If the form of the signature shows unambiguously that the signature is made on behalf of the represented person who is identified in the instrument, the representative is not liable on the instrument.
- (2) Subject to subsection (c), if (i) the form of the signature does not show unambiguously that the signature is made in a representative capacity or (ii) the represented person is not identified in the instrument, the representative is liable on the instrument to a holder in due course that took the instrument without notice that the representative was not intended to be liable on the instrument. With respect to any other person, the representative is liable on the instrument unless the representative proves that the original parties did not intend the representative to be liable on the instrument.
- (c) If a representative signs the name of the representative as drawer of a check without indication of the representative status and the check is payable from an account of the represented person who is identified on the check, the signer is not liable on the check if the signature is an authorized signature of the represented person.

#### § 75-3-403. Unauthorized Signature

- (a) Unless otherwise provided in this chapter or Chapter 4, an unauthorized signature is ineffective except as the signature of the unauthorized signer in favor of a person who in good faith pays the instrument or takes it for value. An unauthorized signature may be ratified for all purposes of this chapter.
- (b) If the signature of more than one (1) person is required to constitute the authorized signature of an organization, the signature of the organization is unauthorized if one of the required signatures is lacking.
- (c) The civil or criminal liability of a person who makes an unauthorized signature is not affected by any provision of this chapter which makes the unauthorized signature effective for the purposes of this chapter.

#### § 75-3-404. Impostors; Fictitious Payees

- (a) If an impostor, by use of the mails or otherwise, induces the issuer of an instrument to issue the instrument to the impostor, or to a person acting in concert with the impostor, by impersonating the payee of the instrument or a person authorized to act for the payee, an indorsement of the instrument by any person in the name of the payee is effective as the indorsement of the payee in favor of a person who, in good faith, pays the instrument or takes it for value or for collection.
- (b) If (i) a person whose intent determines to whom an instrument is payable ([Section 75-3-110\(a\)](#) or [\(b\)](#)) does not intend the person identified as payee to have any interest in the instrument, or (ii) the person identified as payee of an instrument is a fictitious person, the following rules apply until the instrument is negotiated by special indorsement:
  - (1) Any person in possession of the instrument is its holder.
  - (2) An indorsement by any person in the name of the payee stated in the instrument is effective as the indorsement of the payee in favor of a person who, in good faith, pays the instrument or takes it for value or for collection.
- (c) Under subsection (a) or (b), an indorsement is made in the name of a payee if (i) it is made in a name substantially similar to that of the payee or (ii) the instrument, whether or not indorsed, is deposited in a depository bank to an account in a name substantially similar to that of the payee.
- (d) With respect to an instrument to which subsection (a) or (b) applies, if a person paying the instrument or taking it for value or for collection fails to exercise ordinary care in paying or taking the instrument and that failure substantially contributes to

loss resulting from payment of the instrument, the person bearing the loss may recover from the person failing to exercise ordinary care to the extent the failure to exercise ordinary care contributed to the loss.

#### § 75-3-405. Employer's Responsibility for Fraudulent Indorsement by Employee

- (a) In this section:
  - (1) "Employee" includes an independent contractor and employee of an independent contractor retained by the employer.
  - (2) "Fraudulent indorsement" means (i) in the case of an instrument payable to the employer, a forged indorsement purporting to be that of the employer, or (ii) in the case of an instrument with respect to which the employer is the issuer, a forged indorsement purporting to be that of the person identified as payee.
  - (3) "Responsibility" with respect to instruments means authority (i) to sign or indorse instruments on behalf of the employer, (ii) to process instruments received by the employer for bookkeeping purposes, for deposit to an account, or for other disposition, (iii) to prepare or process instruments for issue in the name of the employer, (iv) to supply information determining the names or addresses of payees of instruments to be issued in the name of the employer, (v) to control the disposition of instruments to be issued in the name of the employer, or (vi) to act otherwise with respect to instruments in a responsible capacity. "Responsibility" does not include authority that merely allows an employee to have access to instruments or blank or incomplete instrument forms that are being stored or transported or are part of incoming or outgoing mail, or similar access.
- (b) For the purpose of determining the rights and liabilities of a person who, in good faith, pays an instrument or takes it for value or for collection, if an employer entrusted an employee with responsibility with respect to the instrument and the employee or a person acting in concert with the employee makes a fraudulent indorsement of the instrument, the indorsement is effective as the indorsement of the person to whom the instrument is payable if it is made in the name of that person. If the person paying the instrument or taking it for value or for collection fails to exercise ordinary care in paying or taking the instrument and that failure substantially contributes to loss resulting from the fraud, the person bearing the loss may recover from the person failing to exercise ordinary care to the extent the failure to exercise ordinary care contributed to the loss.
- (c) Under subsection (b), an indorsement is made in the name of the person to whom an instrument is payable if (i) it is made in a name substantially similar to the name of that person or (ii) the instrument, whether or not indorsed, is deposited in a depository bank to an account in a name substantially similar to the name of that person.

#### § 75-3-406. Negligence Contributing to Forged Signature or Alteration of Instrument

- (a) A person whose failure to exercise ordinary care substantially contributes to an alteration of an instrument or to the making of a forged signature on an instrument is precluded from asserting the alteration or the forgery against a person who, in good faith, pays the instrument or takes it for value or for collection.
- (b) Under subsection (a), if the person asserting the preclusion fails to exercise ordinary care in paying or taking the instrument and that failure substantially contributes to loss, the loss is allocated between the person precluded and the person asserting the preclusion according to the extent to which the failure of each to exercise ordinary care contributed to the loss.
- (c) Under subsection (a), the burden of proving failure to exercise ordinary care is on the person asserting the preclusion. Under subsection (b), the burden of proving failure to exercise ordinary care is on the person precluded.

#### § 75-3-407. Alteration

(a) "Alteration" means (i) an unauthorized change in an instrument that purports to modify in any respect the obligation of a party, or (ii) an unauthorized addition of words or numbers or other change to an incomplete instrument relating to the obligation of a party.

(b) Except as provided in subsection (c), an alteration fraudulently made discharges a party whose obligation is affected by the alteration unless that party assents or is precluded from asserting the alteration. No other alteration discharges a party, and the instrument may be enforced according to its original terms.

(c) A payor bank or drawee paying a fraudulently altered instrument or a person taking it for value, in good faith and without notice of the alteration, may enforce rights with respect to the instrument (i) according to its original terms, or (ii) in the case of an incomplete instrument altered by unauthorized completion, according to its terms as completed.

#### **§ 75-3-408. Drawee Not Liable on Unaccepted Draft**

A check or other draft does not of itself operate as an assignment of funds in the hands of the drawee available for its payment, and the drawee is not liable on the instrument until the drawee accepts it.

#### **§ 75-3-409. Acceptance of Draft: Certified Check**

(a) "Acceptance" means the drawee's signed agreement to pay a draft as presented. It must be written on the draft and may consist of the drawee's signature alone. Acceptance may be made at any time and becomes effective when notification pursuant to instructions is given or the accepted draft is delivered for the purpose of giving rights on the acceptance to any person.

(b) A draft may be accepted although it has not been signed by the drawer, is otherwise incomplete, is overdue, or has been dishonored.

(c) If a draft is payable at a fixed period after sight and the acceptor fails to date the acceptance, the holder may complete the acceptance by supplying a date in good faith.

(d) "Certified check" means a check accepted by the bank on which it is drawn. Acceptance may be made as stated in subsection (a) or by a writing on the check which indicates that the check is certified. The drawee of a check has no obligation to certify the check, and refusal to certify is not dishonor of the check.

#### **§ 75-3-410. Acceptance Varying Draft**

(a) If the terms of a drawee's acceptance vary from the terms of the draft as presented, the holder may refuse the acceptance and treat the draft as dishonored. In that case, the drawee may cancel the acceptance.

(b) The terms of a draft are not varied by an acceptance to pay at a particular bank or place in the United States, unless the acceptance states that the draft is to be paid only at that bank or place.

(c) If the holder assents to an acceptance varying the terms of a draft, the obligation of each drawer and indorser that does not expressly assent to the acceptance is discharged.

#### **§ 75-3-411. Refusal to Pay Cashier's Checks, Teller's Checks, and Certified Checks**

(a) In this section, "obligated bank" means the acceptor of a certified check or the issuer of a cashier's check or teller's check bought from the issuer.

(b) If the obligated bank wrongfully (i) refuses to pay a cashier's check or certified check, (ii) stops payment of a teller's check, or (iii) refuses to pay a dishonored teller's check, the person asserting the right to enforce the check is entitled to compensation for expenses and loss of interest resulting from the nonpayment and may recover consequential damages if the obligated bank refuses to pay after receiving notice of particular circumstances giving rise to the damages.

(c) Expenses or consequential damages under subsection (b) are not recoverable if the refusal of the obligated bank to pay occurs because (i) the bank suspends payments, (ii) the obligated bank asserts a claim or defense of the bank that it has reasonable grounds to believe is available against the person entitled to enforce the instrument, (iii) the obligated bank has a reasonable doubt whether the person demanding payment is the person entitled to enforce the instrument, or (iv) payment is prohibited by law.

#### **§ 75-3-412. Obligation of Issuer of Note or Cashier's Check**

The issuer of a note or cashier's check or other draft drawn on the drawer is obliged to pay the instrument (i) according to its terms at the time it was issued or, if not issued, at the time it first came into possession of a holder, or (ii) if the issuer signed an incomplete instrument, according to its terms when completed, to the extent stated in [Sections 75-3-115](#) and [75-3-407](#). The obligation is owed to a person entitled to enforce the instrument or to an indorser who paid the instrument under [Section 75-3-415](#).

#### **§ 75-3-413. Obligation of Acceptor**

(a) The acceptor of a draft is obliged to pay the draft (i) according to its terms at the time it was accepted, even though the acceptance states that the draft is payable "as originally drawn" or equivalent terms, (ii) if the acceptance varies the terms of the draft, according to the terms of the draft as varied, or (iii) if the acceptance is of a draft that is an incomplete instrument, according to its terms when completed, to the extent stated in [Sections 75-3-115](#) and [75-3-407](#). The obligation is owed to a person entitled to enforce the draft or to the drawer or an indorser who paid the draft under [Section 75-3-414](#) or [75-3-415](#).

(b) If the certification of a check or other acceptance of a draft states the amount certified or accepted, the obligation of the acceptor is that amount. If (i) the certification or acceptance does not state an amount, (ii) the amount of the instrument is subsequently raised, and (iii) the instrument is then negotiated to a holder in due course, the obligation of the acceptor is the amount of the instrument at the time it was taken by the holder in due course.

#### **§ 75-3-414. Obligation of Drawer**

(a) This section does not apply to cashier's checks or other drafts drawn on the drawer.

(b) If an unaccepted draft is dishonored, the drawer is obliged to pay the draft (i) according to its terms at the time it was issued or, if not issued, at the time it first came into possession of a holder, or (ii) if the drawer signed an incomplete instrument, according to its terms when completed, to the extent stated in [Sections 75-3-115](#) and [75-3-407](#). The obligation is owed to a person entitled to enforce the draft or to an indorser who paid the draft under [Section 75-3-415](#).

(c) If a draft is accepted by a bank, the drawer is discharged, regardless of when or by whom acceptance was obtained.

(d) If a draft is accepted and the acceptor is not a bank, the obligation of the drawer to pay the draft if the draft is dishonored by the acceptor is the same as the obligation of an indorser under [Section 75-3-415\(a\)](#) and [\(c\)](#).

(e) If a draft states that it is drawn "without recourse" or otherwise disclaims liability of the drawer to pay the draft, the drawer is not liable under subsection (b) to pay the draft if the draft is not a check. A disclaimer of the liability stated in

subsection (b) is not effective if the draft is a check.

(f) If (i) a check is not presented for payment or given to a depository bank for collection within thirty (30) days after its date, (ii) the drawee suspends payments after expiration of the 30-day period without paying the check, and (iii) because of the suspension of payments, the drawer is deprived of funds maintained with the drawee to cover payment of the check, the drawer to the extent deprived of funds may discharge its obligation to pay the check by assigning to the person entitled to enforce the check the rights of the drawer against the drawee with respect to the funds.

#### § 75-3-415. Obligation of Indorser

(a) Subject to subsections (b), (c), and (d) and to [Section 75-3-419\(d\)](#), if an instrument is dishonored, an indorser is obliged to pay the amount due on the instrument (i) according to the terms of the instrument at the time it was indorsed, or (ii) if the indorser indorsed an incomplete instrument, according to its terms when completed, to the extent stated in [Sections 75-3-115](#) and [75-3-407](#). The obligation of the indorser is owed to a person entitled to enforce the instrument or to a subsequent indorser who paid the instrument under this section.

(b) If an indorsement states that it is made “without recourse” or otherwise disclaims liability of the indorser, the indorser is not liable under subsection (a) to pay the instrument.

(c) If notice of dishonor of an instrument is required by [Section 75-3-503](#) and notice of dishonor complying with that section is not given to an indorser, the liability of the indorser under subsection (a) is discharged.

(d) If a draft is accepted by a bank after an indorsement is made, the liability of the indorser under subsection (a) is discharged.

(e) If an indorser of a check is liable under subsection (a) and the check is not presented for payment, or given to a depository bank for collection, within thirty (30) days after the day the indorsement was made, the liability of the indorser under subsection (a) is discharged.

#### § 75-3-416. Transfer Warranties

(a) A person who transfers an instrument for consideration warrants to the transferee and, if the transfer is by indorsement, to any subsequent transferee that:

- (1) The warrantor is a person entitled to enforce the instrument;
- (2) All signatures on the instrument are authentic and authorized;
- (3) The instrument has not been altered;
- (4) The instrument is not subject to a defense or claim in recoupment of any party which can be asserted against the warrantor; and
- (5) The warrantor has no knowledge of any insolvency proceeding commenced with respect to the maker or acceptor or, in the case of an unaccepted draft, the drawer.

(b) A person to whom the warranties under subsection (a) are made and who took the instrument in good faith may recover from the warrantor as damages for breach of warranty an amount equal to the loss suffered as a result of the breach, but not more than the amount of the instrument plus expenses and loss of interest incurred as a result of the breach.

(c) The warranties stated in subsection (a) cannot be disclaimed with respect to checks. Unless notice of a claim for breach of warranty is given to the warrantor within thirty (30) days after the claimant has reason to know of the breach and the identity of the warrantor, the liability of the warrantor under subsection (b) is discharged to the extent of any loss caused by the delay in giving notice of the claim.

(d) A cause of action for breach of warranty under this section accrues when the claimant has reason to know of the breach.

#### § 75-3-417. Presentment Warranties

(a) If an unaccepted draft is presented to the drawee for payment or acceptance and the drawee pays or accepts the draft, (i) the person obtaining payment or acceptance, at the time of presentment, and (ii) a previous transferor of the draft, at the time of transfer, warrant to the drawee making payment or accepting the draft in good faith that:

- (1) The warrantor is, or was, at the time the warrantor transferred the draft, a person entitled to enforce the draft or authorized to obtain payment or acceptance of the draft on behalf of a person entitled to enforce the draft;
- (2) The draft has not been altered; and
- (3) The warrantor has no knowledge that the signature of the drawer of the draft is unauthorized.

(b) A drawee making payment may recover from any warrantor damages for breach of warranty equal to the amount paid by the drawee less the amount the drawee received or is entitled to receive from the drawer because of the payment. In addition, the drawee is entitled to compensation for expenses and loss of interest resulting from the breach. The right of the drawee to recover damages under this subsection is not affected by any failure of the drawee to exercise ordinary care in making payment. If the drawee accepts the draft, breach of warranty is a defense to the obligation of the acceptor. If the acceptor makes payment with respect to the draft, the acceptor is entitled to recover from any warrantor for breach of warranty the amounts stated in this subsection.

(c) If a drawee asserts a claim for breach of warranty under subsection (a) based on an unauthorized indorsement of the draft or an alteration of the draft, the warrantor may defend by proving that the indorsement is effective under [Section 75-3-404](#) or [75-3-405](#) or the drawer is precluded under [Section 75-3-406](#) or [75-4-406](#) from asserting against the drawee the unauthorized indorsement or alteration.

(d) If (i) a dishonored draft is presented for payment to the drawer or an indorser or (ii) any other instrument is presented for payment to a party obliged to pay the instrument, and (iii) payment is received, the following rules apply:

- (1) The person obtaining payment and a prior transferor of the instrument warrant to the person making payment in good faith that the warrantor is, or was, at the time the warrantor transferred the instrument, a person entitled to enforce the instrument or authorized to obtain payment on behalf of a person entitled to enforce the instrument.
- (2) The person making payment may recover from any warrantor for breach of warranty an amount equal to the amount paid plus expenses and loss of interest resulting from the breach.

(e) The warranties stated in subsections (a) and (d) cannot be disclaimed with respect to checks. Unless notice of a claim for breach of warranty is given to the warrantor within thirty (30) days after the claimant has reason to know of the breach and the identity of the warrantor, the liability of the warrantor under subsection (b) or (d) is discharged to the extent of any loss caused by the delay in giving notice of the claim.

(f) A cause of action for breach of warranty under this section accrues when the claimant has reason to know of the breach.

#### § 75-3-418. Payment or Acceptance by Mistake

(a) Except as provided in subsection (c), if the drawee of a draft pays or accepts the draft and the drawee acted on the mistaken belief that (i) payment of the draft had not been stopped pursuant to [Section 75-4-403](#) or (ii) the signature of the drawer of the draft was authorized, the drawee may recover the amount of the draft from the person to whom or for whose benefit payment was made or, in the case of acceptance, may revoke the acceptance. Rights of the drawee under this subsection are not affected by failure of the drawee to exercise ordinary care in paying or accepting the draft.

(b) Except as provided in subsection (c), if an instrument has been paid or accepted by mistake and the case is not covered by subsection (a), the person paying or accepting may, to the extent permitted by the law governing mistake and restitution, (i) recover the payment from the person to whom or for whose benefit payment was made or (ii) in the case of acceptance, may revoke the acceptance.

(c) The remedies provided by subsection (a) or (b) may not be asserted against a person who took the instrument in good faith and for value or who in good faith changed position in reliance on the payment or acceptance. This subsection does not limit remedies provided by [Section 75-3-417](#) or [75-4-407](#).

(d) Notwithstanding [Section 75-4-215](#), if an instrument is paid or accepted by mistake and the payor or acceptor recovers payment or revokes acceptance under subsection (a) or (b), the instrument is deemed not to have been paid or accepted and is treated as dishonored, and the person from whom payment is recovered has rights as a person entitled to enforce the dishonored instrument.

#### § 75-3-419. Instruments Signed for Accommodation

(a) If an instrument is issued for value given for the benefit of a party to the instrument ("accommodated party") and another party to the instrument ("accommodation party") signs the instrument for the purpose of incurring liability on the instrument without being a direct beneficiary of the value given for the instrument, the instrument is signed by the accommodation party "for accommodation."

(b) An accommodation party may sign the instrument as maker, drawer, acceptor, or indorser and, subject to subsection (d), is obliged to pay the instrument in the capacity in which the accommodation party signs. The obligation of an accommodation party may be enforced notwithstanding any statute of frauds and whether or not the accommodation party receives consideration for the accommodation.

(c) A person signing an instrument is presumed to be an accommodation party and there is notice that the instrument is signed for accommodation if the signature is an anomalous indorsement or is accompanied by words indicating that the signer is acting as surety or guarantor with respect to the obligation of another party to the instrument. Except as provided in [Section 75-3-605](#), the obligation of an accommodation party to pay the instrument is not affected by the fact that the person enforcing the obligation had notice when the instrument was taken by that person that the accommodation party signed the instrument for accommodation.

(d) If the signature of a party to an instrument is accompanied by words indicating unambiguously that the party is guaranteeing collection rather than payment of the obligation of another party to the instrument, the signer is obliged to pay the amount due on the instrument to a person entitled to enforce the instrument only if (i) execution of judgment against the other party has been returned unsatisfied, (ii) the other party is insolvent or in an insolvency proceeding, (iii) the other party cannot be served with process, or (iv) it is otherwise apparent that payment cannot be obtained from the other party.

(e) An accommodation party who pays the instrument is entitled to reimbursement from the accommodated party and is

entitled to enforce the instrument against the accommodated party. An accommodated party who pays the instrument has no right of recourse against, and is not entitled to contribution from, an accommodation party.

#### § 75-3-420. Conversion of Instrument

(a) The law applicable to conversion of personal property applies to instruments. An instrument is also converted if it is taken by transfer, other than a negotiation, from a person not entitled to enforce the instrument or a bank makes or obtains payment with respect to the instrument for a person not entitled to enforce the instrument or receive payment. An action for conversion of an instrument may not be brought by (i) the issuer or acceptor of the instrument or (ii) a payee or indorsee who did not receive delivery of the instrument either directly or through delivery to an agent or a co-payee.

(b) In an action under subsection (a), the measure of liability is presumed to be the amount payable on the instrument, but recovery may not exceed the amount of the plaintiff's interest in the instrument.

(c) A representative, other than a depository bank, who has in good faith dealt with an instrument or its proceeds on behalf of one who was not the person entitled to enforce the instrument is not liable in conversion to that person beyond the amount of any proceeds that it has not paid out.

#### § 75-3-501. Presentment

(a) "Presentment" means a demand made by or on behalf of a person entitled to enforce an instrument (i) to pay the instrument made to the drawee or a party obliged to pay the instrument or, in the case of a note or accepted draft payable at a bank, to the bank, or (ii) to accept a draft made to the drawee.

(b) The following rules are subject to Chapter 4, agreement of the parties, and clearinghouse rules and the like:

(1) Presentment may be made at the place of payment of the instrument and must be made at the place of payment if the instrument is payable at a bank in the United States; may be made by any commercially reasonable means, including an oral, written, or electronic communication; is effective when the demand for payment or acceptance is received by the person to whom presentment is made; and is effective if made to any one (1) of two (2) or more makers, acceptors, drawees, or other payors.

(2) Upon demand of the person to whom presentment is made, the person making presentment must (i) exhibit the instrument, (ii) give reasonable identification and, if presentment is made on behalf of another person, reasonable evidence of authority to do so, and (iii) sign a receipt on the instrument for any payment made or surrender the instrument if full payment is made.

(3) Without dishonoring the instrument, the party to whom presentment is made may (i) return the instrument for lack of a necessary indorsement, or (ii) refuse payment or acceptance for failure of the presentment to comply with the terms of the instrument, an agreement of the parties, or other applicable law or rule.

(4) The party to whom presentment is made may treat presentment as occurring on the next business day after the day of presentment if the party to whom presentment is made has established a cut-off hour not earlier than 2 p.m. for the receipt and processing of instruments presented for payment or acceptance and presentment is made after the cut-off hour.

#### § 75-3-502. Dishonor

(a) Dishonor of a note is governed by the following rules:

(1) If the note is payable on demand, the note is dishonored if presentment is duly made to the maker and the note is not paid on the day of presentment.

(2) If the note is not payable on demand and is payable at or through a bank or the terms of the note require presentment, the note is dishonored if presentment is duly made and the note is not paid on the day it becomes payable or the day of presentment, whichever is later.

(3) If the note is not payable on demand and paragraph (2) does not apply, the note is dishonored if it is not paid on the day it becomes payable.

(b) Dishonor of an unaccepted draft other than a documentary draft is governed by the following rules:

(1) If a check is duly presented for payment to the payor bank otherwise than for immediate payment over the counter, the check is dishonored if the payor bank makes timely return of the check or sends timely notice of dishonor or nonpayment under [Section 75-4-301](#) or [75-4-302](#), or becomes accountable for the amount of the check under [Section 75-4-302](#).

(2) If a draft is payable on demand and paragraph (1) does not apply, the draft is dishonored if presentment for payment is duly made to the drawee and the draft is not paid on the day of presentment.

(3) If a draft is payable on a date stated in the draft, the draft is dishonored if (i) presentment for payment is duly made to the drawee and payment is not made on the day the draft becomes payable or the day of presentment, whichever is later, or (ii) presentment for acceptance is duly made before the day the draft becomes payable and the draft is not accepted on the day of presentment.

(4) If a draft is payable on elapse of a period of time after sight or acceptance, the draft is dishonored if presentment for acceptance is duly made and the draft is not accepted on the day of presentment.

(c) Dishonor of an unaccepted documentary draft occurs according to the rules stated in subsections (b)(2), (3), and (4), except that payment or acceptance may be delayed without dishonor until no later than the close of the third business day of the drawee following the day on which payment or acceptance is required by those paragraphs.

(d) Dishonor of an accepted draft is governed by the following rules:

(1) If the draft is payable on demand, the draft is dishonored if presentment for payment is duly made to the acceptor and the draft is not paid on the day of presentment.

(2) If the draft is not payable on demand, the draft is dishonored if presentment for payment is duly made to the acceptor and payment is not made on the day it becomes payable or the day of presentment, whichever is later.

(e) In any case in which presentment is otherwise required for dishonor under this section and presentment is excused under [Section 75-3-504](#), dishonor occurs without presentment if the instrument is not duly accepted or paid.

(f) If a draft is dishonored because timely acceptance of the draft was not made and the person entitled to demand acceptance consents to a late acceptance, from the time of acceptance the draft is treated as never having been dishonored.

#### [§ 75-3-503. Notice of Dishonor](#)

(a) The obligation of an indorser stated in [Section 75-3-415\(a\)](#) and the obligation of a drawer stated in [Section 75-3-414\(d\)](#) may not be enforced unless (i) the indorser or drawer is given notice of dishonor of the instrument complying with this sec-

tion or (ii) notice of dishonor is excused under [Section 75-3-504\(b\)](#).

(b) Notice of dishonor may be given by any person; may be given by any commercially reasonable means, including an oral, written, or electronic communication; and is sufficient if it reasonably identifies the instrument and indicates that the instrument has been dishonored or has not been paid or accepted. Return of an instrument given to a bank for collection is sufficient notice of dishonor.

(c) Subject to [Section 75-3-504\(c\)](#), with respect to an instrument taken for collection by a collecting bank, notice of dishonor must be given (i) by the bank before midnight of the next banking day following the banking day on which the bank receives notice of dishonor of the instrument, or (ii) by any other person within thirty (30) days following the day on which the person receives notice of dishonor. With respect to any other instrument, notice of dishonor must be given within thirty (30) days following the day on which dishonor occurs.

#### [§ 75-3-504. Excused Presentment and Notice of Dishonor](#)

(a) Presentment for payment or acceptance of an instrument is excused if (i) the person entitled to present the instrument cannot with reasonable diligence make presentment, (ii) the maker or acceptor has repudiated an obligation to pay the instrument or is dead or in insolvency proceedings, (iii) by the terms of the instrument presentment is not necessary to enforce the obligation of indorsers or the drawer, (iv) the drawer or indorser whose obligation is being enforced has waived presentment or otherwise has no reason to expect or right to require that the instrument be paid or accepted, or (v) the drawer instructed the drawee not to pay or accept the draft or the drawee was not obligated to the drawer to pay the draft.

(b) Notice of dishonor is excused if (i) by the terms of the instrument notice of dishonor is not necessary to enforce the obligation of a party to pay the instrument, or (ii) the party whose obligation is being enforced waived notice of dishonor. A waiver of presentment is also a waiver of notice of dishonor.

(c) Delay in giving notice of dishonor is excused if the delay was caused by circumstances beyond the control of the person giving the notice and the person giving the notice exercised reasonable diligence after the cause of the delay ceased to operate.

#### [§ 75-3-505. Evidence of Dishonor](#)

(a) The following are admissible as evidence and create a presumption of dishonor and of any notice of dishonor stated:

(1) A document regular in form as provided in subsection (b) which purports to be a protest;

(2) A purported stamp or writing of the drawee, payor bank, or presenting bank on or accompanying the instrument stating that acceptance or payment has been refused unless reasons for the refusal are stated and the reasons are not consistent with dishonor;

(3) A book or record of the drawee, payor bank, or collecting bank, kept in the usual course of business which shows dishonor, even if there is no evidence of who made the entry.

(b) A protest is a certificate of dishonor made by a United States consul or vice-consul, or a notary public or other person authorized to administer oaths by the law of the place where dishonor occurs. It may be made upon information satisfactory to that person. The protest must identify the instrument and certify either that presentment has been made or, if not made, the reason why it was not made, and that the instrument has been dishonored by nonacceptance or nonpayment. The protest may also certify that notice of dishonor has been given to some or all parties.

[§§ 75-3-506 to 75-3-511. Repealed by Laws 1992, Ch. 420, § 112, eff. January 1, 1993](#)

[§§ 75-3-506 to 75-3-511. Repealed by Laws 1992, Ch. 420, § 112, eff. January 1, 1993](#)

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[§§ 75-3-506 to 75-3-511. Repealed by Laws 1992, Ch. 420, § 112, eff. January 1, 1993](#)

[§ 75-3-601. Discharge and Effect of Discharge](#)

(a) The obligation of a party to pay the instrument is discharged as stated in this chapter or by an act or agreement with the party which would discharge an obligation to pay money under a simple contract.

(b) Discharge of the obligation of a party is not effective against a person acquiring rights of a holder in due course of the instrument without notice of the discharge.

[§ 75-3-602. Payment](#)

(a) Subject to subsection (b), an instrument is paid to the extent payment is made (i) by or on behalf of a party obliged to pay the instrument, and (ii) to a person entitled to enforce the instrument. To the extent of the payment, the obligation of the party obliged to pay the instrument is discharged even though payment is made with knowledge of a claim to the instrument under [Section 75-3-306](#) by another person.

(b) The obligation of a party to pay the instrument is not discharged under subsection (a) if:

(1) A claim to the instrument under [Section 75-3-306](#) is enforceable against the party receiving payment and (i) payment is made with knowledge by the payor that payment is prohibited by injunction or similar process of a court of competent jurisdiction, or (ii) in the case of an instrument other than a cashier's check, teller's check, or certified check, the party making payment accepted, from the person having a claim to the instrument, indemnity against loss resulting from refusal to pay the person entitled to enforce the instrument; or

(2) The person making payment knows that the instrument is a stolen instrument and pays a person it knows is in wrongful possession of the instrument.

[§ 75-3-603. Tender of Payment](#)

(a) If tender of payment of an obligation to pay an instrument is made to a person entitled to enforce the instrument, the effect of tender is governed by principles of law applicable to tender of payment under a simple contract.

(b) If tender of payment of an obligation to pay an instrument is made to a person entitled to enforce the instrument and the tender is refused, there is discharge, to the extent of the amount of the tender, of the obligation of an indorser or accommodation party having a right of recourse with respect to the obligation to which the tender relates.

(c) If tender of payment of an amount due on an instrument is made to a person entitled to enforce the instrument, the obli-

gation of the obligor to pay interest after the due date on the amount tendered is discharged. If presentment is required with respect to an instrument and the obligor is able and ready to pay on the due date at every place of payment stated in the instrument, the obligor is deemed to have made tender of payment on the due date to the person entitled to enforce the instrument.

## IMPLIED WARRANTIES UNDER MISSISSIPPI ARTICLE 2 ISSUES

**From:** Owen P. Lalor **Sent:** Tuesday, June 16, 2009

**To:** Jerome C. Hafter

**Subject:** Business Reform - UCC and Debtor Creditors Laws Study Group

One of my primary areas of interest is to have Mississippi adopt the majority position (approximately 38 states) with respect to implied warranties under Article 2 and Article 2A of the UCC. The prohibition against waiver, disclaimer or modification of the implied warranties of merchantability and fitness for a particular purpose and contractual modification or limitation of remedies in consumer transactions is a serious factor limiting employment opportunities in Mississippi. Consumer products manufacturers are hard pressed to justify exposing their nationwide business to implied warranties when headquartered in Mississippi.

The following excerpts contrast a few of the pertinent UCC statutes of Mississippi with their counterparts in Florida. The risks to a manufacturer when Mississippi UCC provisions govern a consumer transaction are significantly greater than under Florida law. If we can change this, more consumer products business can have their principal place of business and sales operations in Mississippi.

### MISSISSIPPI UCC

#### **75-2-315.1. Limitation of exclusion or modification of warranties to consumers.**

(1) Any oral or written language used by a seller of consumer goods and services, which attempts to exclude or modify any implied warranties of merchantability and fitness for a particular purpose or to exclude or modify the consumer's remedies for breach of those warranties, is unenforceable. However, the seller may recover from the manufacturer any damages resulting from breach of the implied warranty of merchantability or fitness for a particular purpose.

(2) Any oral or written language used by a manufacturer of consumer goods, which attempts to limit or modify a consumer's remedies for breach of the manufacturer's express warranties, is unenforceable.

#### **75-2-719. Contractual modification or limitation of remedy.**

(1) Subject to the provisions of subsections (2), (3), and (4) of this section and of Section 75-2-718 on liquidation and limitation of damages,

(a) The agreement may provide for remedies in addition to or in substitution for those provided in this chapter and may limit or alter the measure of damages recoverable under this chapter, as by limiting the buyer's remedies to return of the goods and repayment of the price or to repair and replacement of nonconforming goods or parts; and

(b) Resort to a remedy as provided is optional unless the remedy is expressly agreed to be exclusive, in which case it is the sole remedy.

(2) Where circumstances cause an exclusive or limited remedy to fail of its essential purpose, remedy may be had as provided in this Code.

(3) **Consequential damages may be limited or excluded unless the limitation or exclusion is unconscionable. Limitation of consequential damages for injury to the person in the case of consumer goods is prima facie unconscionable** but limitation of damages where the loss is commercial is not.

(4) **Any limitation of remedies which would deprive the buyer of a remedy to which he may be entitled for breach of an implied warranty of merchantability or fitness for a particular purpose shall be prohibited.** The provisions of this subsection do not apply to computer hardware, computer software, and services performed on computer hardware and computer software, which are sold between merchants.

## **CONTRAST with FLORIDA STATUTES:**

### **672.316**

#### **Title XXXIX [39] COMMERCIAL RELATIONS**

#### **Chapter 672 UNIFORM COMMERCIAL CODE: SALES**

### **672.316 Exclusion or modification of warranties.**

(1) Words or conduct relevant to the creation of an express warranty **and** words or conduct tending to negate or limit warranty shall be construed wherever reasonable as consistent with each other; but, subject to the provisions of this chapter on parol or extrinsic evidence (s. 672.202), negation or limitation is inoperative to the extent that such construction is unreasonable.

(2) Subject to subsection (3), to exclude or modify the **implied** warranty of merchantability or any part of it, the language must mention merchantability **and** in case of a writing must be conspicuous; **and**, to exclude or modify any **implied** warranty of fitness, the exclusion must be by a writing **and** conspicuous. Language to exclude all **implied** warranties of fitness is sufficient if it states, for example, that "There are no warranties which extend beyond the description on the face hereof."

(3) Notwithstanding subsection (2):

(a) Unless the circumstances indicate otherwise, all **implied** warranties are excluded by expressions like "as is" or "with all faults" or other language which in common understanding calls the buyer's attention to the exclusion of warranties **and** makes plain that there is no **implied** warranty; **and**

(b) When the buyer before entering into the contract has examined the goods or the sample or model as fully as he or she desired or has refused to examine the goods, there is no **implied** warranty with regard to defects which an examination ought in the circumstances to have revealed to him or her; **and**

(c) An **implied** warranty can also be excluded or modified by a course of dealing or course of performance or usage of trade.

(d) In a transaction involving the sale of cattle or hogs, there is no **implied** warranty that the cattle or hogs are free from sickness or disease. However, no

exemption applies in cases where the seller knowingly sells cattle or hogs that are diseased.

(4) Remedies for breach of warranty can be limited in accordance with the provisions of this chapter on liquidation or limitation of damages and on contractual modification of remedy (ss. 672.718 and 672.719).

(5) The procurement, processing, storage, distribution, or use of whole blood, plasma, blood products, and blood derivatives for the purpose of injecting or transfusing the same, or any of them, into the human body for any purpose whatsoever is declared to be the rendering of a service by any person participating therein and does not constitute a sale, whether or not any consideration is given therefor; and the implied warranties of merchantability and fitness for a particular purpose are not applicable.

(6) The procurement, processing, testing, storing, or providing of human tissue and organs for human transplant, by an institution qualified for such purposes, is the rendering of a service; and such service does not constitute the sale of goods or products to which implied warranties of merchantability or fitness for a particular purpose are applicable. No implied warranties exist as to defects which cannot be detected, removed, or prevented by reasonable use of available scientific procedures or techniques.

#### **672.718 Liquidation or limitation of damages; deposits.**

(1) Damages for breach by either party may be liquidated in the agreement but only at an amount which is reasonable in the light of the anticipated or actual harm caused by the breach, the difficulties of proof of loss, and the inconvenience or nonfeasibility of otherwise obtaining an adequate remedy. A term fixing unreasonably large liquidated damages is void as a penalty.

(2) Where the seller justifiably withholds delivery of goods because of the buyer's breach, the buyer is entitled to restitution of any amount by which the sum of his or her payments exceeds:

(a) The amount to which the seller is entitled by virtue of terms liquidating the seller's damages in accordance with subsection (1), or

(b) In the absence of such terms, 20 percent of the value of the total performance for which the buyer is obligated under the contract or \$500, whichever is smaller.

(3) The buyer's right to restitution under subsection (2) is subject to offset to the extent that the seller establishes:

(a) A right to recover damages under the provisions of this chapter other than subsection (1), and

(b) The amount or value of any benefits received by the buyer directly or indirectly by reason of the contract.

(4) Where a seller has received payment in goods their reasonable value or the proceeds of their resale shall be treated as payments for the purposes of subsection (2); but if the seller has notice of the buyer's breach before reselling goods received in part

performance, his or her resale is subject to the conditions laid down in this chapter on resale by an aggrieved seller (s. 672.706).

**672.719 Contractual modification or limitation of remedy.**

(1) Subject to the provisions of subsections (2) and (3) of this section and of the preceding section on liquidation and limitation of damages:

(a) The agreement may provide for remedies in addition to or in substitution for those provided in this chapter and may limit or alter the measure of damages recoverable under this chapter, as by limiting the buyer's remedies to return of the goods and repayment of the price or to repair and replacement of nonconforming goods or parts; and

(b) Resort to a remedy as provided is optional unless the remedy is expressly agreed to be exclusive, in which case it is the sole remedy.

(2) Where circumstances cause an exclusive or limited remedy to fail of its essential purpose, remedy may be had as provided in this code.

(3) Consequential damages may be limited or excluded unless the limitation or exclusion is unconscionable. Limitation of consequential damages for injury to the person in the case of consumer goods is prima facie unconscionable but limitation of damages where the loss is commercial is not.

Owen:

I am glad to have your thoughts on Mississippi's non-uniform provisions of Article 2 prohibiting exclusions of implied warranties and limitations on remedies. There are of course other provisions which relate to these subjects including the non-uniform prohibition in Section 75-1-105 (the UCC choice of law provision) against choice of non-Mississippi law to govern on the subject matter of exclusion of implied warranties of merchantability and fitness for a particular purpose and limitation of remedies for breach of these implied warranties and Section 11-7-18 which holds inoperative disclaimers of implied warranties in the sale of goods.

Your message mentions that these provisions make it less attractive to manufacture and sell consumer goods in Mississippi and that the adoption of provision from the Official Version of the UCC on this subject or the enactments in other states would make sale of Mississippi manufactured consumer goods more viable. Actually amendments to Article 2 of the UCC enacted in other states in recent years have included provisions making unenforceable disclaimers of these implied warranties and limitations on remedies in regard to consumer goods and in regard to personal injuries and wrongful death. (In some states, the courts have achieved the same result by judicial interpretation of the unconscionability provisions of Article 2 or under the doctrine of good faith and fair dealing.) Therefore, as to consumer goods, the law in Mississippi is not much different from most other jurisdictions.

Where the real issue exists is in regard to sales of non-consumer goods, respect to which, under Mississippi law, implied warranties of merchantability and fitness for a particular purpose cannot be disclaimed or limited even among sophisticated buyers and sellers. See *J.L. Teel Co. Inc. v. Houston United Sales*, 491 So. 2d 851, 859 (Miss. 1986) (disclaimer of implied warranties not

enforceable as to office copying machine - not consumer goods); *C.F. Murry v. Blackwell*, 966 So. 2d 901 (Miss. App. 2007) (as general rule, implied warranties may not be waived or disclaimed under Mississippi law, except where disclaimer is expressly permitted as with certain used cars under Section 75-2-315.1(3)).

A major issue, as I see it, is that these non-uniform provisions of Mississippi's UCC and related statutes making disclosure of implied warranties unenforceable were adopted by the Mississippi Legislature after much effort by the plaintiff-oriented bar. Even in the tort reform era under Governors Musgrove and Barbour (when a number of other statutes were modified to put caps on tort and products liability damages and to establish more difficult burdens of proof in personal injury cases), there was tacit agreement not to modify the provisions of Article 2 and interrelated statutes concerning disclaimers of implied warranties in the sale of goods.

A lot of thought has been given to the implied warranty issue, particularly by the Business Law Advisory Group under previous Secretaries of State. My current assessment is that modification of these isolated non-uniform provisions of UCC Articles 2, 2A and 1 and Section 11-7-18 would be difficult to accomplish on a single issue basis. However, if the modification of existing Article 2 and Article 2A was done as part of a general adoption of the new Uniform Version of the Official Text of Articles 2 and 2A, then the repeal of the non-uniform provisions relating to disclaimers of implied warranties might be easier to enact both as to consumer goods and as to non-consumer goods.

This is definitely an issue that should be addressed and considered in the UCC Committee both as potential "stand-alone" legislation and as part of the enactment of the new Articles 2 and 2A.



## A Few Facts About The...

### Amendments to UCC Articles 2 and 2A

#### PURPOSE:

Article 2 of the Uniform Commercial Code has governed the sale of goods since its promulgation in 1951. UCC2 has been amended to accommodate electronic commerce and to reflect development of business practices, changes in other law, and interpretive difficulties of practical significance. UCC2A provides a legal framework for leases of personal property; it has been amended to update and modernize the Article, and to conform to the changes in Article 2.

#### ORIGIN:

Completed by the National Conference of Commissioners on Uniform State Laws and the American Law Institute in 2003.

#### APPROVED BY:

American Bar Association

#### STATE ADOPTIONS:

#### 2009 INTRODUCTIONS:

For any further information regarding Amendments to UCC Articles 2 and 2A, please contact Mike Kerr or Katie Robinson at 312-450-6600.

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## SUMMARY

### 2003 Amendments Uniform Commercial Code: Article 2 - Sales

Article 2 of the Uniform Commercial Code (UCC) was derived from the Uniform Sales Act, originally promulgated by the Uniform Law Commissioners in 1906. The Uniform Sales Act became Article 2 when the UCC was originally promulgated in 1951. Between 1951 and 2003, there were no extensive amendments proposed, only some amendments conforming Article 2 to revisions of other UCC articles. In 2003, a group of modernizing amendments have been promulgated by the American Law Institute and the National Conference of Commissioners on Uniform State Laws. The UCC is a joint enterprise of the ALI and the ULC.

Article 2 provides the fundamental rules of contract for the sale of goods. With key exceptions, such as good faith and reasonableness, the rules of Article 2 are default rules that may be waived or modified by agreement. The rules provide for each stage of a contractual relationship from formation to performance. Included are provisions governing implied and express warranties, risk of loss, statute of frauds and extrinsic evidence, interpretation, auction sales, "gap-filling" terms that apply when parties fail to reach agreement, breaches of contract and remedies for breaches of contract.

Goods are generally tangible, moveable objects that are not real estate, securities, or things in action. A sale is a transfer of title to goods from one person to another for a price. The rules of Article 2 do not govern gifts, leases or secured transactions, though there are provisions that interrelate with other articles of the UCC.

Bringing amendments for Article 2 to conclusion took a long time. The study effort began in the late 1980's. Initially, the integration of Article 2 into a larger article covering more than sales of goods was thoroughly explored. This proved not to be feasible. Then there were many hard issues to address against the fact of a basic statute that serves sales transactions very well. It was decided that a full-scale revision was not merited, but that discrete amendments to address some current issues could improve the functioning of Article 2. That process concluded in the Spring of 2003 with the final approval of amendments by the American Law Institute. The Uniform Law Commissioners had approved them in late-summer 2002.

It is not feasible to cover every amendment in a short summary such as this one. Of course, the basic Article 2 remains sacrosanct. The amendments update the article to accommodate electronic commerce, which is desirable to avoid questions of interrelation with federal law, and also to reflect the development of business practices, changes in other law, and to resolve some interpretive difficulties of practical significance. The following are examples of important amendments:

- 1. Electronic Transactions.** Technology has changed the face of transactions in goods and the law of sales must adapt to that reality. There are amendments that substitute newly defined terms, record and sign, for every requirement for a writing or manual signature in Article 2. The newly defined terms include electronically stored documents and electronic signatures. The 2003 amendments to Article 2 make electronic records and signatures the equivalent for enforcement purposes of paper documents and manual signatures. In addition, amendments provide that an electronic record or signature is attributable to a person if it is that person's electronic act or the act of that person's electronic agent. An amendment also provides that an electronic communication has legal effect even if no person is aware of its receipt, and that receipt of an electronic communication establishes that it was received, but not that the content received was the content sent. Contracts

may clearly be formed through electronic agents. These are fundamental rules for the conduct of electronic transactions, necessary to make them fully effective. An amendment, also, assures that the rules for electronic transactions will not be preempted by federal law.

**2. Conflicts with Other Applicable Law.** The range of law affecting sales is much broader and more complex than it was when Article 2 was originally promulgated. There are conflict problems that an amendment attempts to solve. For example, an amendment provides that a transaction under Article 2 is also subject to an applicable certificate of title statute, but not to the extent of affecting the rights of a buyer in the ordinary course of business arising before registration of title in the name of another buyer. Other laws that are recognized to apply are rules governing consumer transactions, and special statutes governing such things as agricultural products, transfer of human blood, and artists' products. When there is a conflict between Article 2 and a rule so recognized, the other law prevails.

**3. Statute of Frauds.** Statute of frauds requirements limit the extent to which an oral contract may be enforced. Original Article 2 permitted the enforcement of oral contracts that do not exceed \$500.00 in price. An amendment raises the amount to \$5000.00.

**4. Battle of Forms Rules Simplified.** When seller and buyer exchange records incorporating offer and acceptance of a contract, there can be confusion as to the resulting terms. Original Article 2 contained elaborate rules designed to resolve the issues that arise in a forms battle, but they have proved unsatisfactory in practice. The amendments separate the issues of contract formation and contract terms and create a framework for determining the terms of contracts formed in any manner, including by a battle of forms. The terms of a contract are the terms that appear in the records of both parties, terms that the parties agree to even if not in mutual records and terms supplied or incorporated under any provision in Article 2. In a classic forms battle, the rules give no preference to the terms of either party.

**5. Consumer Contracts.** The amendments create a new category of sales contracts – consumer contracts – and provide certain protections for consumers who enter into such contracts. For example, sellers in consumer contracts that want to disclaim implied warranties of quality must do so in language that plainly conveys to the consumer the nature of the risk being assumed. In some instances, additional flexibility has been added for non-consumer contracts, as by permitting a seller to cure following a buyer's revocation of acceptance, while retaining the original rule precluding cure in such cases for consumers.

**6. Warranties to Remote Purchasers.** Article 2 governs implied and express warranties of quality. The existing warranties run to the immediate buyer (or those in some relationship to the immediate buyer other than purchaser from that buyer) of the goods. Much case law has developed, however, relating to warranties to a "remote purchaser," someone who "buys or leases goods from an immediate buyer or other person in the normal chain of distribution." Amendments to Article 2 provide two new statutory obligations in the nature of express warranties to remote purchasers. The first establishes a warranty based on any record packaged with or accompanying goods that articulates a remedial promise or an affirmation of fact, promise or description that reasonably could be taken as an obligation. The other warranty is based upon affirmation of fact, promise or description of goods, or recitation of a remedial promise in an advertisement or similar communication to the public.

**7. Shipment Terms, F.O.B., F.A.S., C.I.F.** There are precise rules respecting certain kinds of shipment terms in Part 3 of Article 2. Obligations under these rules are amply covered as a matter of usage of trade. Because these rules are archaic and do not conform to current practices, they are repealed in the amendments to Article 2.

The 2003 Amendments to Article 2 of the Uniform Commercial Code represent a considerable improvement over existing law and prepare the law of sales for sales of goods in the electronic

marketplace.

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## SUMMARY

### 2003 Amendments Uniform Commercial Code: Article 2A - Leases

Uniform Commercial Code (UCC) Article 2A - Leases, governs true leases of goods. It was added to the Uniform Commercial Code in 1987, and amended in 1990. It was the first article added to the UCC after its original promulgation in 1951, and responded to the enormous increase in the use of leases that began in the 1970's. Leasing became used in that time as a method of financing transactions in goods. In finance leases, lessor and lessee became analogous to creditor and debtor in these kinds of transactions.

In a true lease, the lessor gives possession and right to use the goods to the lessee for a fixed period of time in return for rent. The title to the property and a meaningful residual interest remain with the lessor. A "finance lease" is a true lease in which the lessor is not the fundamental supplier of the goods leased, but leases goods to lessees as a means of financing their acquisition from the supplier. UCC Article 2A governs finance leases as true leases, but treats them differently in some respects from other true leases. For example, UCC 2A provides an implied warranty of quality, but since the lessor in a finance lease is not the source of the goods, the warranty does not run directly to the lessor. The lessor passes through warranties given by the supplier under other law (principally a sale warranty of fitness) to the lessor, to the lessee. UCC 2A provides for priority of lessor interests for finance leases, analogous to the concept of priority between creditors in secured transactions under UCC Article 9. Great care was taken to establish finance leases as a separate financing category from secured transactions so that no doubt as to the method of establishing priority for any transaction would arise.

UCC 2A was largely derived from UCC Article 2 - Sales, building upon the familiar law of sales contracts with provenance back to the original Uniform Sales Act of 1906 and continuing into Article 2, originally promulgated in 1951. UCC 2A, like Article 2, is essentially the rules of contract for the specific kind of transaction. Many of the rules for leases can be and are functionally the same as the rules for sales, but adapted to the lease transaction. Like Article 2, Article 2A is primarily a set of default rules that may be waived or varied in the contract, with important exceptions such as the requirement of "good faith." UCC Article 2A provides basic contract rules, including rules for offer and acceptance of a contract, statute of frauds, warranties, assignment of interests, risk of loss and remedies upon breach of contract.

In 2003, another set of amendments has been promulgated by the American Law Institute and the Uniform Law Commissioners, the two organizations responsible for the Uniform Commercial Code. Any statute, even one as relatively new as Article 2A is, needs to be updated, and 2003 is the occasion for a needed update. Electronic transactions are a major reason for providing amendments in 2003, as will be noted later on. Because amendments are individual and cover a large number of sections, it is not possible to cover every amendment in a short summary. Here are some of the most important ones, however:

**1. Electronic Transactions.** Technology has changed the face of transactions in goods and the law of leases must adapt to that reality. Amendments substitute newly defined terms, record and sign, for every requirement for a writing or manual signature in Article 2A. These newly defined terms include electronically stored documents and electronic signatures. The 2003 amendments to Article 2A make electronic records and signatures the equivalent for enforcement purposes to paper documents and manual signatures. In addition, amendments provide that an electronic record or signature is attributable to a person if it is that person's electronic act or the act of that person's electronic agent. An amendment also provides that an electronic communication has legal effect even if no person is

aware of its receipt, and that receipt of an electronic communication establishes that it was received, but not that the content received was the content sent. Contracts may clearly be formed through electronic agents. These are fundamental rules for the conduct of electronic transactions, necessary to make them fully effective. An amendment, also, assures that the rules for electronic transactions will not be preempted by federal law.

**2. Effect of Certificate of Title.** Goods, such as automobiles, which are often leased are also subject to state certificate of title statutes, and there is a conflict of law problem that Article 2A addresses. Prior Article 2A provides that goods registered under a certificate of title statute of a state remain subject to that law until either surrender of the certificate or when four months lapse once the goods have left the registering state. There is a gap potential therefore, if a new certificate of title is not applied for within the four month period. The amendments fills the gap. The law of the state where a certificate of title originally is registered applies until a new certificate of title in another state becomes effective, and compliance is governed by the law of the original state until the new law becomes effective for the purposes of determining compliance with a certificate of title statute.

**3. Warranties against Interference.** The lessee does not have title to goods leased. The interference warranties in Article 2A, however, run to the lessee in much the same way warranty of title runs to the buyer in a sale, but to warrant the enjoyment of the benefits of the lease, not title. The amendments articulate the warranty more specifically, but do not change their basic nature. The lessor continues to warrant that no claim against the lessor will interfere with the lessee's enjoyment. The major addition to the warranty against interference is a "colorable claim to or interest in the goods which will unreasonably expose the lessee to litigation."

**4. Liquidated Damages When Lessee Insolvent.** Any lease contract may state limitations on damages and/or liquidated damages for breach. If a lessor, currently, withholds or stops delivery of goods when a lessee defaults or is insolvent, the lessee is entitled to restitution for the amount lease payments exceed the liquidated amount or, if none, 20% of present value or \$500.00, whichever is the lesser amount. The amended rule merely allows restitution for the amount lessee's payments exceed the lessor's entitlement when lessor's damages are liquidated. This better reflects actual damages and conforms to current practices.

**5. Lessee's Damages upon Lessor's Breach of Contract.** The lessee's general remedies for breach of contract by the lessor are more particularly and expressly provided in the 2003 amendments than is the case under original Article 2A.

**6. Lessor's Remedies upon Lessee's Breach of Contract.** These remedies, like those of the lessee's, are more particularly and expressly provided for.

These amendments suggest modest updating and reflect revisions in Articles 1 and 9 of the UCC that have already occurred. Enacting these amendments should be undertaken as soon as possible to keep UCC Article 2A - Leases, as current as possible.

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D R A F T

FOR APPROVAL

**PROPOSED AMENDMENTS TO  
UNIFORM COMMERCIAL CODE ARTICLE 2 - SALES**

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NATIONAL CONFERENCE OF COMMISSIONERS

ON UNIFORM STATE LAWS

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MEETING IN ITS ONE-HUNDRED-AND-ELEVENTH YEAR

TUCSON, ARIZONA

JULY 26 - AUGUST 2, 2002

**PROPOSED AMENDMENTS TO  
UNIFORM COMMERCIAL CODE ARTICLE 2 - SALES**

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ON UNIFORM STATE LAWS

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**COMMITTEE TO PREPARE AMENDMENTS TO UNIFORM COMMERCIAL CODE  
ARTICLE 2 - SALES**

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#### **PROPOSED AMENDMENTS TO**

#### **UNIFORM COMMERCIAL CODE ARTICLE 2 - SALES**

#### **TABLE OF CONTENTS**

##### **PART 1**

##### **SHORT TITLE, GENERAL CONSTRUCTION AND SUBJECT MATTER**

SECTION 2-102. SCOPE; CERTAIN SECURITY AND OTHER TRANSACTIONS EXCLUDED FROM THIS  
ARTICLE. 1

SECTION 2-103. DEFINITIONS AND INDEX OF DEFINITIONS. 4

SECTION 2-104. DEFINITIONS: "MERCHANT"; "BETWEEN MERCHANTS"; "FINANCING AGENCY". 11

SECTION 2-105. DEFINITIONS: TRANSFERABILITY; ~~"GOODS"~~; "FUTURE" GOODS; "LOT"; "COMMERCIAL UNIT". 12

SECTION 2-108. TRANSACTIONS SUBJECT TO OTHER LAW. 13

#### PART 2

FORM, FORMATION, TERMS AND READJUSTMENT OF CONTRACT; ELECTRONIC CONTRACTING

SECTION 2-201. FORMAL REQUIREMENTS; STATUTE OF FRAUDS. 16

SECTION 2-202. FINAL ~~WRITTEN~~ EXPRESSION IN A RECORD: PAROL OR EXTRINSIC EVIDENCE. 20

SECTION 2-203. SEALS INOPERATIVE. 22

SECTION 2-204. FORMATION IN GENERAL. 22

SECTION 2-205. FIRM OFFERS. 24

SECTION 2-206. OFFER AND ACCEPTANCE IN FORMATION OF CONTRACT. 24

SECTION 2-207. ~~ADDITIONAL TERMS IN ACCEPTANCE OR TERMS OF CONTRACT~~; EFFECT OF CONFIRMATION. 25

SECTION 2-208. ~~COURSE OF PERFORMANCE ON PRACTICAL CONSTRUCTION RESERVED.~~ 29

SECTION 2-209. MODIFICATION; RESCISSION AND WAIVER. 29

SECTION 2-210. DELEGATION OF PERFORMANCE; ASSIGNMENT OF RIGHTS. 30

SECTION 2-211. LEGAL RECOGNITION OF ELECTRONIC CONTRACTS, RECORDS AND SIGNATURES. 35

SECTION 2-212. ATTRIBUTION. 36

SECTION 2-213 . ELECTRONIC COMMUNICATION. 38

#### PART 3

GENERAL OBLIGATION AND CONSTRUCTION OF CONTRACT

SECTION 2-302. UNCONSCIONABLE CONTRACT OR ~~CLAUSE-TERM.~~ 39

SECTION 2-304. PRICE PAYABLE IN MONEY, GOODS, REALTY, OR OTHERWISE. 40

SECTION 2-305. OPEN PRICE TERM. 41

SECTION 2-308. ABSENCE OF SPECIFIED PLACE FOR DELIVERY. 42

SECTION 2-309. ABSENCE OF SPECIFIC TIME PROVISIONS; NOTICE OF TERMINATION. 42

SECTION 2-310. OPEN TIME FOR PAYMENT OR RUNNING OF CREDIT AUTHORITY TO SHIP UNDER RESERVATION. 43

SECTION 2-311. OPTIONS AND COOPERATION RESPECTING PERFORMANCE. 44

SECTION 2-312. WARRANTY OF TITLE AND AGAINST INFRINGEMENT; BUYER'S OBLIGATION AGAINST INFRINGEMENT. 45

SECTION 2-313. EXPRESS WARRANTIES BY AFFIRMATION, PROMISE, DESCRIPTION, SAMPLE; REMEDIAL PROMISE. 48

SECTION 2-313A. OBLIGATION TO REMOTE PURCHASER CREATED BY RECORD PACKAGED WITH OR ACCOMPANYING GOODS. 52

SECTION 2-313B. OBLIGATION TO REMOTE PURCHASER CREATED BY COMMUNICATION TO THE PUBLIC. 57

SECTION 2-314. IMPLIED WARRANTY: MERCHANTABILITY; USAGE OF TRADE. 60

SECTION 2-316. EXCLUSION OR MODIFICATION OF WARRANTIES. 64

SECTION 2-318. THIRD PARTY BENEFICIARIES OF WARRANTIES EXPRESS OR IMPLIED. 69

SECTION 2-319. ~~F.O.B. AND F.A.S. TERMS RESERVED.~~ 71

SECTION 2-320. ~~C.I.F. AND C. & F. TERMS RESERVED.~~ 73

SECTION 2-321. ~~C.I.F. OR C. & F.; "NET LANDED WEIGHTS"; "PAYMENT ON ARRIVAL"; WARRANTY OF CONDITION ON ARRIVAL RESERVED.~~ 74

SECTION 2-322. ~~DELIVERY "EX-SHIP" RESERVED.~~ 75

~~SECTION 2-323. FORM OF BILL OF LADING REQUIRED IN OVERSEAS SHIPMENT; "OVERSEAS"~~

~~RESERVED.~~ 76

~~SECTION 2-324. "NO ARRIVAL, NO SALE" TERM RESERVED.~~ 77

~~SECTION 2-325. "LETTER OF CREDIT" TERM; "CONFIRMED CREDIT" FAILURE TO PAY BY AGREED LETTER OF CREDIT.~~ 78

~~SECTION 2-326. SALE ON APPROVAL AND SALE OR RETURN; CONSIGNMENT SALES AND RIGHTS OF CREDITORS.~~ 79

SECTION 2-328. SALE BY AUCTION. 80

PART 4  
TITLE, CREDITORS AND GOOD FAITH PURCHASERS

SECTION 2-401. PASSING OF TITLE; RESERVATION FOR SECURITY; LIMITED APPLICATION OF THIS SECTION. 82

SECTION 2-402. RIGHTS OF SELLER'S CREDITORS AGAINST SOLD GOODS. 83

SECTION 2-403. POWER TO TRANSFER; GOOD FAITH PURCHASE OF GOODS; "ENTRUSTING". 84

PART 5  
PERFORMANCE

SECTION 2-501. INSURABLE INTEREST IN GOODS; MANNER OF IDENTIFICATION OF GOODS. 86

SECTION 2-502. BUYER'S RIGHT TO GOODS ON SELLER'S INSOLVENCY. 87

SECTION 2-503. MANNER OF SELLER'S TENDER OF DELIVERY. 88

SECTION 2-504. SHIPMENT BY SELLER. 90

SECTION 2-505. SELLER'S SHIPMENT UNDER RESERVATION. 90

SECTION 2-506. RIGHTS OF FINANCING AGENCY. 91

SECTION 2-507. EFFECT OF SELLER'S TENDER; DELIVERY ON CONDITION. 92

SECTION 2-508. CURE BY SELLER OF IMPROPER TENDER OR DELIVERY; REPLACEMENT. 93

SECTION 2-509. RISK OF LOSS IN THE ABSENCE OF BREACH. 95

SECTION 2-510. EFFECT OF BREACH ON RISK OF LOSS. 97

SECTION 2-512. PAYMENT BY BUYER BEFORE INSPECTION. 97

SECTION 2-513. BUYER'S RIGHT TO INSPECTION OF GOODS. 98

SECTION 2-514. WHEN DOCUMENTS DELIVERABLE ON ACCEPTANCE; WHEN ON PAYMENT. 99

PART 6  
BREACH, REPUDIATION AND EXCUSE

SECTION 2-601. BUYER'S RIGHTS ON IMPROPER DELIVERY. 100

SECTION 2-602. MANNER AND EFFECT OF ~~RIGHTFUL~~ REJECTION. 100

SECTION 2-603. MERCHANT BUYER'S DUTIES AS TO ~~RIGHTFULLY~~ REJECTED GOODS. 101

SECTION 2-604. BUYER'S OPTIONS AS TO SALVAGE OF ~~RIGHTFULLY~~ REJECTED GOODS. 102

SECTION 2-605. WAIVER OF BUYER'S OBJECTIONS BY FAILURE TO PARTICULARIZE. 103

SECTION 2-606. WHAT CONSTITUTES ACCEPTANCE OF GOODS. 105

SECTION 2-607. EFFECT OF ACCEPTANCE; NOTICE OF BREACH; BURDEN OF ESTABLISHING BREACH AFTER ACCEPTANCE; NOTICE OF CLAIM OR LITIGATION TO PERSON ANSWERABLE OVER. 106

SECTION 2-608. REVOCATION OF ACCEPTANCE IN WHOLE OR IN PART. 108

SECTION 2-609. RIGHT TO ADEQUATE ASSURANCE OF PERFORMANCE. 110

SECTION 2-610. ANTICIPATORY REPUDIATION. 110

SECTION 2-611. RETRACTION OF ANTICIPATORY REPUDIATION. 111

SECTION 2-612. "INSTALLMENT CONTRACT"; BREACH. 112

SECTION 2-613. CASUALTY TO IDENTIFIED GOODS. 113

SECTION 2-615. EXCUSE BY FAILURE OF PRESUPPOSED CONDITIONS. 113

SECTION 2-616. PROCEDURE ON NOTICE CLAIMING EXCUSE. 114

PART 7  
REMEDIES

SECTION 2-702. SELLER'S REMEDIES ON DISCOVERY OF BUYER'S INSOLVENCY. 115

SECTION 2-703. SELLER'S REMEDIES IN GENERAL. 117

SECTION 2-704. SELLER'S RIGHT TO IDENTIFY GOODS TO THE CONTRACT NOTWITHSTANDING BREACH OR TO SALVAGE UNFINISHED GOODS. 119

SECTION 2-705. SELLER'S STOPPAGE OF DELIVERY IN TRANSIT OR OTHERWISE. 120

SECTION 2-706. SELLER'S RESALE INCLUDING CONTRACT FOR RESALE. 121

SECTION 2-707. "PERSON IN THE POSITION OF A SELLER". 126

SECTION 2-708. SELLER'S DAMAGES FOR NON-ACCEPTANCE OR REPUDIATION. 127

SECTION 2-709. ACTION FOR THE PRICE. 131

SECTION 2-710. SELLER'S INCIDENTAL AND CONSEQUENTIAL DAMAGES. 132

SECTION 2-711. BUYER'S REMEDIES IN GENERAL; BUYER'S SECURITY INTEREST IN REJECTED GOODS. 133

SECTION 2-712. "COVER"; BUYER'S PROCUREMENT OF SUBSTITUTE GOODS. 136

SECTION 2-713. BUYER'S DAMAGES FOR NON-DELIVERY OR REPUDIATION. 137

SECTION 2-714. BUYER'S DAMAGES FOR BREACH IN REGARD TO ACCEPTED GOODS. 140

SECTION 2-716. ~~BUYER'S RIGHT TO SPECIFIC PERFORMANCE OR;~~ BUYER'S RIGHT REPLEVIN. 140

SECTION 2-717. DEDUCTION OF DAMAGES FROM THE PRICE. 142

SECTION 2-718. LIQUIDATION OR LIMITATION OF DAMAGES; DEPOSITS. 142

SECTION 2-722. WHO CAN SUE THIRD PARTIES FOR INJURY TO GOODS. 145

SECTION 2-723. PROOF OF MARKET: TIME AND PLACE. 146

SECTION 2-724. ADMISSIBILITY OF MARKET QUOTATIONS. 147

SECTION 2-725. STATUTE OF LIMITATIONS IN CONTRACTS FOR SALE. 147

PART 8  
TRANSITION PROVISIONS

SECTION 2-801. EFFECTIVE DATE. 152

SECTION 2-802. AMENDMENT OF EXISTING ARTICLE 2. 152

SECTION 2-803. APPLICABILITY. 152

SECTION 2-804. SAVINGS CLAUSE. 153

**PROPOSED AMENDMENTS TO**  
**UNIFORM COMMERCIAL CODE ARTICLE 2 - SALES**

**PART 1**

**SHORT TITLE, GENERAL CONSTRUCTION AND SUBJECT MATTER**

**~~SECTION 2-102. SCOPE; CERTAIN SECURITY AND OTHER TRANSACTIONS EXCLUDED FROM THIS ARTICLE.~~**

~~Unless the context otherwise requires, this Article applies to transactions in goods; it does not apply to any transaction which although in the form of an unconditional contract to sell or present sale is intended to operate only as a security transaction nor does this Article impair or repeal any statute regulating sales to consumers, farmers or other specified classes of buyers.~~

(1) Unless the context otherwise requires, and subject to Section 2-108, this article applies to transactions in goods. This Article does not apply to any transaction which although in the form of an unconditional contract to sell or present sale is intended to operate only as a security transaction.

(2) Except as provided in subsection (4), in the case of a transaction involving both goods and non-goods, a court may resolve a dispute by the application of this article to the entire transaction, by the application of other law to the entire transaction, or by the application of this article to part of the transaction and other law to part of the transaction. In making the determination as to the law applicable to the transaction, the court shall take into consideration the nature of the transaction and of the dispute.

(3) This article does not apply to transactions that do not involve goods.

(4) A transaction in a product consisting of computer information and goods that are solely the medium containing the computer information is not a transaction in goods, but a court is not precluded from applying provisions in this article to a dispute concerning whether the goods conform to the contract.

(5) Nothing in this article alters, creates, or diminishes rights in intellectual property.

### **Proposed Comments**

1. This Article applies to transactions in goods. The term "goods" is defined in Section 2-103(1)(m).

2. A great many transactions involve both goods and non-goods. Some transactions involve goods and services. Others involve goods and property other than goods, such as realty, intellectual property, or other intangible personal property. As subsection (2) makes clear, there is no hard and fast rule that determines whether, and the extent to which, this Article applies to disputes arising out of such transactions. There is a large body of case law concerning transactions involving goods and services, and somewhat less precedent concerning other such transactions. The variety of combinations of goods and non-goods that may comprise a transaction, and the types of disputes that a court may be called upon to resolve, make it inadvisable to enact firm principles to determine the applicable body of law. Subsection (2) recognizes that principles that work well in some contexts may not work well in others. Accordingly, it directs courts, in determining whether this Article or other law governs a particular matter before it, to take into consideration the nature of the transaction and of the dispute. Courts should not apply this Article or other law without careful consideration of these matters. In a particular transaction, the non-goods aspect or the goods aspect may predominate. Even though one aspect predominates, however, the core of the dispute may relate to the aspect that does not predominate. Moreover, there may be times when the provisions in this Article, which are designed for goods, simply are not appropriate for application to other aspects of the transaction, and the same may at times be true regarding application of other law to the goods aspect. Finally, in a transaction that is not easily severable into goods and non-goods aspects, a court might decide that it is appropriate to apply one body of law to the entire transaction.

As the nature of transactions evolves over time, the character of those transactions is impossible to predict. Accordingly, this section neither endorses nor rejects any particular approach for determining the applicability of Article 2 to disputes arising from any particular transaction. *[At this point, the comment will provide seven examples (assuming that we can find them) of approaches that courts have used in some cases (with neither indorsement nor condemnation). The seven examples, taken as a whole, are completely neutral inasmuch as the first six consist of mirror-image pairs, while the seventh involves breaking the transaction into goods and non-goods components. The seven examples are: (i) Article 2 applied because goods predominate, (ii) other law applied because non-goods predominate, (iii) Article 2 applied because goods are gravamen, even though goods do not predominate (or without regard to whether they do), (iv) other law applied, because non-goods are gravamen, even though goods predominate (or without regard to whether they do), (v) Article 2 applied to an integrated product, even though it contains information, (vi) other law applied to an integrated product, even though it contains goods, (vii) transaction broken down into its elements, with Article 2 applying only to the goods.]*

3. Subsection (3) states explicitly what has always been true - this Article does not apply to transactions that do not involve goods. Thus, for example, this Article does not govern a contract solely for services or solely for information. When a dispute in such a transaction is before a court, unless a different statute controls, the court is left to do what common-law courts traditionally have done - determine the best rule for the situation before it.

4. Subsection (4) recognizes that transactions in which the only goods involved are a medium containing computer information are essentially information transactions and, thus, should not be categorized as transactions in goods. In such a case, however, there may be a dispute about whether the medium itself (the goods) is defective, and the court is not precluded from applying relevant provisions of this Article.

5. Subsection (5) makes it clear that application of this Article to the informational aspect of a transaction does not alter, create, or diminish rights in intellectual property. To the extent that such rights are governed by other state law, nothing in this Article changes that state law. To the extent that such rights are governed by federal law, under the Supremacy Clause of the Constitution of the United States, nothing in this Article can determine those rights. The fact that a court under subsection (2) applies this Article to a transaction in which goods containing copyrighted information are transferred does not mean that the information itself has been sold for purposes of state law (*see next paragraph*) and does not determine whether the transfer constitutes a "first sale" for purposes of federal copyright law.

In transactions that involve information, the agreement between the parties sometimes contains restrictions on certain uses or future transfers of the information. As is true with analogous restrictions with respect to goods, this Article does not address the enforceability of these restrictions. If the restrictions are effective under other law, this Article does not invalidate them; if they are ineffective under other law, nothing in this Article validates them. See Section 1-103.

## **SECTION 2-103. DEFINITIONS AND INDEX OF DEFINITIONS.**

(1) In this article unless the context otherwise requires

(a) "Buyer" means a person ~~who~~ that buys or contracts to buy goods.

(b) "Computer information" means information in electronic form which is obtained from or through the use of a computer or which is in a form capable of being processed by a computer.

### **Proposed Comment**

Information is not computer information unless it is in electronic form. Thus, information printed on paper is not computer information.

(c) "Conspicuous", with reference to a term, means so written, displayed, or presented that a reasonable person against which it is to operate ought to have noticed it. A term in an electronic record intended to evoke a response by an electronic agent is conspicuous if it is presented in a form that would enable a reasonably configured electronic agent to take it into account or react to it without review of the record by an individual. Whether a term is "conspicuous" or not is a decision for the court. Conspicuous terms include the following:

(i) for a person:

(A) a heading in capitals equal to or greater in size than the surrounding text, or in contrasting type, font, or color to the surrounding text of the same or lesser size;

(B) language in the body of a record or display in larger type than the surrounding text, or in contrasting type, font, or color to the surrounding text of the same size, or set off from surrounding text of the same size by symbols or other marks that call attention to the language; and

(ii) for a person or an electronic agent, a term that is so placed in a record or display that the person or electronic agent cannot proceed without taking action with respect to the particular term.

### **Proposed Comment**

The definition of "conspicuous" may be moved to revised Article 1. The first sentence is based on original Section 1-201(10) but the concept is expanded to include terms in electronic records. The general standard is, that to be conspicuous, a term ought to be noticed by a reasonable person. The second sentence states a special rule for situations where the sender of an electronic record intends to evoke a response from an electronic agent; the presentation of the term must be capable of evoking a response from a reasonably configured electronic agent. Whether a term is conspicuous is an issue for the court.

Paragraphs (i) and (ii) set out several methods for making a term conspicuous. The requirement that a term be conspicuous functions both as notice (the term ought to be noticed) and as a basis for planning (giving guidance to the party that relies on the term about how that result can be achieved).

Paragraph (i), which relates to the general standard for conspicuousness, is based on original Section 1-201(10) but is intended to give more guidance. Paragraph (ii) is new and relates to the special standard for electronic records intended to evoke a response from an electronic agent. Although these paragraphs indicate some of the methods for making a term attention-calling, the test is whether attention can reasonably be expected to be called to it. The statutory language should not be construed to permit a result that is inconsistent with that test.

(d) "Consumer" means an individual who buys or contracts to buy goods that, at the time of contracting, are intended by the individual to be used primarily for personal, family, or household purposes.

### **Proposed Comment**

The definition is significant in determining whether a contract qualifies as a consumer contract. A consumer is a natural person (*cf.* Section 1-201(30)) who enters into a transaction for a purpose typically

associated with consumers - i.e., a personal, family or household purpose. The requirement that the buyer intend that the goods be used "primarily" for personal, family or household purposes is generally consistent with the definition of consumer goods in revised Article 9. See Section 9-102(a)(23).

(e) "Consumer contract" means a contract between a merchant seller and a consumer.

**Proposed Comment**

This term is limited to a contract for sale between a seller that is a "merchant" and a buyer that is a "consumer". Thus, neither a sale by a consumer to a consumer nor a sale by a merchant to an individual who intends that the goods be used primarily in a home business qualify as a consumer contract.

(f) "Delivery" means the voluntary transfer of physical possession or control of goods.

**Proposed Comment**

The definition of "delivery" as it applies to goods may be moved to revised Article 1, which already contains a definition of the term as it applies to an instrument, document of title or chattel paper.

(g) "Electronic" means relating to technology having electrical, digital, magnetic, wireless, optical, electromagnetic, or similar capabilities.

**Proposed Comment**

The definition of "electronic" may be moved to revised Article 1. The electronic contracting provisions, including the definitions of "electronic," "electronic agent," "record," "electronic record," "information processing system," and certain the electronic aspects of "receive" are based on the provisions of the Uniform Electronic Transactions Act and are consistent with the federal Electronic Signatures in Global and National Commerce Act (15 U.S.C. SECTION 7001 *et seq.*).

(h) "Electronic agent" means a computer program or an electronic or other automated means used independently to initiate an action or respond to electronic records or performances in whole or in part, without review or action by an individual.

**Proposed Comment**

The definition of "electronic agent" may be moved to revised Article 1.

(i) "Electronic record" means a record created, generated, sent, communicated, received, or stored by electronic means.

**Proposed Comment**

The definition of "electronic record" may be moved to revised Article 1.

(j) "Foreign exchange transaction" means a transaction in which one party agrees to deliver a quantity of a specified money or unit of account in consideration of the other party's agreement to deliver another quantity of different money or unit of account either currently or at a future date, and in which delivery is to be through funds transfer, book entry accounting, or other form of payment order, or other agreed means to transfer a credit balance. The term includes a transaction of this type involving multiple moneys and spot, forward, option, or other products derived from underlying moneys and any combination of these transactions. The term does not include a transaction involving multiple moneys in which one or both of the parties is obligated to make physical delivery, at the time of contracting or in the future, of banknotes, coins, or other form of legal tender or specie.

**Proposed Comment**

This definition, which is new, is used in the definition of goods in Section 2-103(1)(l), which now excludes "the subject matter of foreign exchange transactions."

~~(b)~~ (k) "Good faith" ~~in the case of a merchant~~ means honesty in fact and the observance of reasonable commercial standards of fair dealing ~~in the trade~~.

*Legislative Note: This definition should not be adopted if the jurisdiction has enacted revised Article 1.*

(l) "Goods" means all things that are movable at the time of identification to a contract for sale. The term includes future goods, specially manufactured goods, the unborn young of animals, growing crops, and other identified things attached to realty as described in Section 2-107. The term does not include information, the money in which the price is to be paid, investment securities under Article 8, the subject matter of foreign exchange transactions, and choses in action.

### **Proposed Comment**

The definition of "goods" has been amended to exclude information. See Section 2-103(1)(m). It has also been amended to exclude the subject matter of "foreign exchange transactions." See Section 2-103(1)(j). Although a contract in which currency is the commodity exchanged is a sale of goods, an exchange in which delivery is "through funds transfer, book entry accounting, or other form of payment order, or other agreed means to transfer a credit balance" is not a sale of goods and is not governed by Article 2. In the latter case, Article 4A or other law applies. On the other hand, if the parties agree to a forward transaction where, after January 1, 2002, dollars are to be physically delivered in exchange for the delivery of Euros, the transaction is not within the "foreign exchange" exclusion and Article 2 applies.

(m) "Information" means data, text, images, sounds, mask works, computer programs, software, databases, or the like, including collections and compilations. The term includes computer information.

(e) (n) "Receipt of goods" means taking physical possession of them.

(o) "Record" means information that is inscribed on a tangible medium or that is stored in an electronic or other medium and is retrievable in perceivable form.

*Legislative Note: This definition should not be adopted if the jurisdiction has enacted revised Article 1.*

(p) "Remedial promise" means a promise by the seller to repair or replace the goods or to refund all or part of the price upon the happening of a specified event.

### **Proposed Comment**

A "remedial promise" is a promise by the seller to take remedial action upon the happening of a specified event. The types of remediation contemplated are specified in the definition - repair or replacement of the goods, or refund of all or part of the price. No other promise by a seller qualifies as a remedial promise. Further, the seller is entitled to specify precisely the event that will trigger its obligation. Typical examples include a commitment to repair any parts that prove to be defective, or a commitment to refund the purchase price if the goods fail to perform in a certain manner. A post-sale promise to fix a problem that the seller is not obligated to fix in order to placate a dissatisfied customer is not within the definition of remedial promise.

It is irrelevant whether the promised remedy is exclusive under Section 2-719(1) or merely additional to the buyer's normal Code remedies. Whether the promised remedy is exclusive, and if so whether it has failed its essential purpose, is determined under Section 2-719.

Use of the term resolves a statute-of-limitations problem. Under original Section 2-725, a right of action for breach of an express warranty accrued at the time of tender unless the warranty explicitly extended to the future performance of the goods, in which case a discovery rule applied. By contrast, a right of action for breach of an ordinary (non-warranty) promise accrued when the promise was breached. A number of courts held that commitments by sellers to take remedial action in the event the goods proved to be defective during a specified period of time constituted warranties and applied the time-of-tender rule; other courts used strained reasoning that allowed them to apply the discovery rule even though the promise at issue referred to the future performance of the seller, not the goods.

This Article takes the position that a promise by the seller to take remedial action is not a warranty at all and therefore is not subject to either the time-of-tender or discovery rule. Section 2-725(2)(c) separately addresses the accrual of a right of action for a remedial promise. For further explanation, see Proposed Comment 2 to Section 2-725.

(d) (q) "Seller" means a person who that sells or contracts to sell goods.

(r) "Sign" means, with present intent to authenticate or adopt a record,

(i) to execute or adopt a tangible symbol; or

(ii) to attach to or logically associate with the record an electronic sound, symbol, or process.

### **Proposed Comment**

The definition is broad enough to cover any record that is signed within the meaning of present Article 1 (Section 1-201(39)) or that contains an electronic signature within the meaning of the Uniform Electronic Transactions Act (Section 2(8)). It is consistent with the federal Electronic Signatures in Global and National Commerce Act (15 U.S.C. SECTION 7001 *et seq.*).

(2) Other definitions applying to this Article or to specified Parts thereof, and the sections in which they appear are:

"Acceptance". Section 2-606.

~~"Banker's credit". Section 2-325.~~

"Between merchants". Section 2-104.

"Cancellation". Section 2-106(4).

"Commercial unit". Section 2-105.

~~"Confirmed credit". Section 2-325.~~

"Conforming to contract". Section 2-106.

"Contract for sale". Section 2-106.

"Cover". Section 2-712.

"Entrusting". Section 2-403.

"Financing agency". Section 2-104.

"Future goods". Section 2-105.

~~"Goods". Section 2-105.~~

"Identification". Section 2-501.

"Installment contract". Section 2-612.

~~"Letter of Credit". Section 2-325.~~

"Lot". Section 2-105.

"Merchant". Section 2-104.

~~"Overseas". Section 2-323.~~

"Person in position of seller". Section 2-707.

"Present sale". Section 2-106.

"Sale". Section 2-106.

"Sale on approval". Section 2-326.

"Sale or return". Section 2-326.

"Termination". Section 2-106.

(3) The following definitions in other Articles apply to this Article:

"Check". Section 3-104(f).

~~"Consignee". Section 7-102.~~

~~"Consignor". Section 7-102.~~

~~"Consumer goods". Section 9-109.~~

"Dishonor". Section 3-502.

"Draft". Section 3-104(e).

"Injunction against honor". Section 5-109(b).

"Letter of credit". Section 5-102(a)(10).

(4) In addition Article 1 contains general definitions and principles of construction and interpretation applicable throughout this Article.

**SECTION 2-104. DEFINITIONS: "MERCHANT"; "BETWEEN MERCHANTS"; "FINANCING AGENCY".**

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

(2) "Financing agency" means a bank, finance company or other person ~~who that~~ in the ordinary course of business makes advances against goods or documents of title or ~~who that~~ by arrangement with either the seller or the buyer intervenes in ordinary course to make or collect payment due or claimed under the contract for sale, as by purchasing or paying the seller's draft or making advances against it or by merely taking it for collection whether or not documents of title accompany the draft. "Financing agency" includes also a bank or other person ~~who that~~ similarly intervenes between persons ~~who that~~ are in the position of seller and buyer in respect to the goods (Section 2-707).

(3) "Between merchants" means in any transaction with respect to which both parties are chargeable with the knowledge or skill of merchants.

**SECTION 2-105. DEFINITIONS: TRANSFERABILITY; "GOODS"; "FUTURE" GOODS; "LOT"; "COMMERCIAL UNIT".**

(1) "Goods" means ~~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 (Article 8) and things in action. "Goods" also includes the unborn young of animals and growing crops and other identified things attached to realty as described in the section on goods to be severed from realty (Section 2-107).~~

(2) (1) Goods must be both existing and identified before any interest in them can pass. Goods which are not both existing and identified are "future" goods. A purported present sale of future goods or of any interest therein operates as a contract to sell.

(3) (2) There may be a sale of a part interest in existing identified goods.

(4) (3) An undivided share in an identified bulk of fungible goods is sufficiently identified to be sold although the quantity of the bulk is not determined. Any agreed proportion of such a bulk or any quantity thereof agreed upon by number, weight or other measure may to the extent of the seller's interest in the bulk be sold to the buyer ~~who that~~ then becomes an owner in common.

(5) (4) "Lot" means a parcel or a single article which is the subject matter of a separate sale or delivery, whether or not it is sufficient to perform the contract.

(6) (5) "Commercial unit" means such a unit of goods as by commercial usage is a single whole for purposes of sale and division of which materially impairs its character or value on the market or in use. A commercial unit may be a single article (as a machine) or a set of articles (as a suite of furniture or an assortment of sizes) or a quantity (as a bale, gross, or carload) or any other unit treated in use or in the relevant market as a single whole.

**SECTION 2-108. TRANSACTIONS SUBJECT TO OTHER LAW.**

(1) A transaction subject to this article is also subject to any applicable:

(a) [list any certificate of title statutes of this State covering automobiles, trailers, mobile homes, boats, farm tractors, or the like], except with respect to the rights of a buyer in ordinary course of business under Section 2-403(2) which arise before a certificate of title covering the goods is effective in the name of any other buyer;

(b) rule of law that establishes a different rule for consumers; or

(c) statute of this State to which the transaction is subject, such as statutes dealing with:

(i) the sale or lease of agricultural products;

(ii) the transfer of blood, blood products, human tissues, or parts;

- (iii) the consignment or transfer by artists of works of art or fine prints;
  - (iv) distribution agreements, franchises, and other relationships through which goods are sold;
  - (v) the misbranding or adulteration of food products or drugs; and
  - (vi) dealers in particular products, such as automobiles, motorized wheelchairs, agricultural equipment, and hearing aids.
- (2) Except for the rights of a buyer in ordinary course of business under subsection (1)(a), in the event of a conflict between this article and a law referred to in subsection (1), that law governs.
- (3) For purposes of this article, failure to comply with a law referred to in subsection (1) has only the effect specified in that law.
- (4) This article modifies, limits, and supersedes the federal Electronic Signatures in Global and National Commerce Act, 15 U.S.C. Section 7001 et seq., except that nothing in this article modifies, limits, or supersedes Section 7001(c) of that Act or authorizes electronic delivery of any of the notices described in Section 7003(b) of that Act.

#### **Proposed Comment**

1. Section 2-108, which is new, follows the form of Section 2A-104(1).
2. In subsection (1), it is assumed that Article 2 is subject to any applicable federal law, such as the United Nations Convention on Contracts for the International Sale of Goods (CISG) or the Magnuson-Moss Warranty Act.
3. Subsection (1)(a) permits the states to list any applicable certificate-of-title statutes and provides that Article 2 is subject to their provisions on the transfer and effect of title except for the rights of a buyer in ordinary course of business in certain limited situations. In entrustment situations, subsection (1)(a) overrides those certificate-of-title statutes that provide that a person cannot qualify as an owner unless a certificate has been issued in the person's name. By contrast, in those cases where an owner in whose name a certificate has been issued entrusts a titled asset to a dealer that then sells it to a buyer in ordinary course of business, this section provides that the priority issue between the owner and the buyer is to be resolved in the first instance by reference to the certificate-of-title statute.

Illustration #1. Suppose that a used car is stolen from Owner by Thief and Thief, by fraud, is able to obtain a clean certificate of title from State X. Thief sells the car to Buyer, a good faith purchaser for value but not a buyer in ordinary course of business, and transfers the certificate of title to Buyer. The exception in subsection (1)(a) does not apply to protect Buyer. Further, under Section 2-403(1) Buyer does not get good title from Thief, regardless of the certificate. The same result follows if the applicable state certificate of title law makes the certificate prima facie evidence of ownership. Buyer will prevail, however, if the applicable law conflicts with the result obtained under this Article by making issuance of the certificate conclusive on title.

Illustration #2. Dealer sells a new car to Buyer #1 and signs a form permitting Buyer #1 to apply for a certificate of title. Buyer #1 leaves the car with Dealer so that Dealer can finish its preparation work on the car. While the car remains in Dealer's possession and before the state issues a certificate of title in Buyer #1's name, Buyer #2 makes Dealer a better offer on the car, which Dealer accepts. Buyer #1 entrusted the car to Dealer, and if Buyer #2 qualifies as a buyer in ordinary course of business its title to the car will be superior to that of Buyer #1.

Illustration #3. Owner in whose name a certificate of title has been issued leaves a car with Dealer for repair. Dealer sells the car to Buyer, who qualifies as a buyer in ordinary course of business. If the certificate-of-title law in the state resolves the priority contest between Owner and Buyer, that solution should be implemented. Otherwise, Buyer prevails under Section 2-403(2).

4. This section also deals with the effect of a conflict or failure to comply with any other state law that might apply to a transaction governed by this Article. Subsection (1) provides that a transaction subject to this Article is also subject to other applicable law, and subsection (2) provides that in the event of a conflict the other law governs (except for the rights of a buyer in ordinary course of business under subsection (1)(a)).

Subsection (1)(b) provides that this Article is also subject to any rule of law that establishes a different rule for consumers. "Rule of law" includes a statute, an administrative rule properly promulgated under the statute, and final court decision.

The relationship between Article 2 and federal and state consumer laws will vary from transaction to

transaction and from State to State. For example, the Magnuson-Moss Warranty Act, 15 U.S.C.A. SECTION 2301 et. seq., may or may not apply to the consumer dispute in question and the applicable state "lemon law" may provide more or less protection than Magnuson-Moss. To the extent of application, the other laws control. Otherwise, Article 2 controls.

Subsection (1)(c) provides an illustrative but not exhaustive list of other applicable state statutes that may preempt all or part of Article 2. For example, franchise contracts may be regulated by state franchise acts, the seller of unmerchantable blood or human tissue may be insulated from warranty liability and disclaimers of the implied warranty of merchantability may be invalidated by non-uniform amendments to Article 2. The existence, scope, and effect of these statutes must be assessed from State to State.

Assuming that there is a conflict, subsection (3) deals with the failure of parties to the contract to comply with the applicable law. The failure has the "effect specified" in the law. Thus, the failure to obtain a required license may make the contract illegal, and therefore unenforceable, while the nonnegligent supply of unmerchantable blood under a "blood shield" statute may mean only that the supplier is insulated from liability for injury to person or property.

5. Subsection (4) takes advantage of a provision of the federal Electronic Signatures in Global and National Commerce Act (E-Sign). E-Sign permits state law to modify, limit or supersede its provisions if the state law is consistent with Titles I and II of E-Sign, gives no special legal effect or validity to and does not require the implementation or application of specific technologies or technical specifications, and if enacted subsequent to E-Sign makes specific reference to E-Sign. Subsection (4) does not apply to section 101(c) of E-Sign, nor does it authorize electronic delivery of the notices described in section 103 (b) of E-Sign.

## PART 2

### FORM, FORMATION, TERMS AND READJUSTMENT OF CONTRACT; ELECTRONIC CONTRACTING

#### SECTION 2-201. FORMAL REQUIREMENTS; STATUTE OF FRAUDS.

(1) Except as otherwise provided in this section a A contract for the sale of goods for the price of \$500 \$5,000 or more is not enforceable by way of action or defense unless there is some writing record sufficient to indicate that a contract for sale has been made between the parties and signed by the party against whom which enforcement is sought or by his the party's authorized agent or broker. A writing record is not insufficient because it omits or incorrectly states a term agreed upon but the contract is not enforceable under this subsection beyond the quantity of goods shown in such the writing record.

(2) Between merchants if within a reasonable time a writing record 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 (1) against such party the recipient unless written notice of objection to its contents is given in a record within 10 days after it is received.

(3) A contract which does not satisfy the requirements of subsection (1) but which is valid in other respects is enforceable

(a) if the goods are to be specially manufactured for the buyer and are not suitable for sale to others in the ordinary course of the seller's business and the seller, before notice of repudiation is received and under circumstances which reasonably indicate that the goods are for the buyer, has made either a substantial beginning of their manufacture or commitments for their procurement; or

(b) if the party against whom which enforcement is sought admits in his the party's pleading, or in the party's testimony or otherwise in court under oath that a contract for sale was made, but the contract is not enforceable under this provision paragraph beyond the quantity of goods admitted; or

(c) with respect to goods for which payment has been made and accepted or which have been received and accepted (Sec. 2-606).

(4) A contract that is enforceable under this section is not rendered unenforceable merely because it is not capable of being performed within one year or any other applicable period after its making.

### Proposed Comment

1. The record required by subsection (1) need not contain all the material terms of the contract and the material terms that are stated need not be precise or accurate. All that is required is that the record afford a basis for believing that the offered oral evidence rests on a real transaction. The record may be written in lead pencil on a scratch pad or entered into a laptop computer. It need not indicate which party is the buyer and which party is the seller. The only term which must appear is the quantity term, which need not be accurately stated but recovery is limited to the amount stated. A term indicating that the quantity is based on the output of the seller or the requirements of the buyer is a quantity term for purposes of this section. The price, time and place of payment or delivery, the general quality of the goods, or any particular warranties may all be omitted.

Special emphasis must be placed on the permissibility of omitting the price term. In many valid contracts for sale the parties do not mention the price in express terms. The buyer is bound to pay and the seller to accept a reasonable price, which the trier of the fact will determine. Frequently the price is not mentioned since the parties have based their agreement on a price list or catalogue known to both of them, and the list or catalogue serves as an efficient safeguard against perjury. Finally, "market" prices and valuations that are current in the vicinity constitute a similar check. Of course, if the "price" consists of goods rather than money, the quantity of goods must be stated.

There are only three definite and invariable requirements as to the memorandum made by subsection (1). First, the memorandum must evidence a contract for the sale of goods; second, the memorandum must be signed; and third, the memorandum must have a quantity term.

2. The phrase "Except as otherwise provided in this section" has been deleted from subsection (1). This means that the statement in subsection (3) of three statutory exceptions to subsection (1) does not preclude the possibility that a promisor will be estopped to raise the statute-of-frauds defense in appropriate cases.

3. "Partial performance" as a substitute for the required record can validate the contract only for the goods which have been accepted or for which payment has been made and accepted.

Receipt and acceptance either of goods or of the price constitutes an unambiguous overt admission by both parties that a contract actually exists. If the court can make a just apportionment, therefore, the agreed price of any goods actually delivered can be recovered without a writing or, if the price has been paid, the seller can be forced to deliver an apportionable part of the goods. The overt actions of the parties make admissible evidence of the other terms of the contract necessary to a just apportionment. This is true even though the actions of the parties are not in themselves inconsistent with a different transaction such as a consignment for resale or a mere loan of money.

Part performance by the buyer requires that the buyer deliver something that is accepted by the seller as the performance. Thus, part payment may be made by money or check, accepted by the seller. If the agreed price consists of goods or services, then they must also have been delivered and accepted. When the seller accepts partial payment for a single item the statute is satisfied entirely.

4. Between merchants, failure to answer a confirmation of a contract in a record that satisfies the requirements of subsection (1) against the sender within ten days of receipt renders the record sufficient against the recipient. The only effect, however, is to take away from the party that fails to answer the defense of the Statute of Frauds; the burden of persuading the trier of fact that a contract was in fact made orally prior to the record confirmation is unaffected.

A merchant includes a person "that by occupation purports to have knowledge or skill peculiar to the practices or goods involved in the transaction." Section 2-104(1)(emphasis supplied). Thus, a professional or a farmer should be considered a merchant because the practice of objecting to an improper confirmation ought to be familiar to any person in business.

5. Failure to satisfy the requirements of this section does not render the contract void for all purposes, but merely prevents it from being judicially enforced in favor of a party to the contract. For example, a buyer that takes possession of goods as provided in an oral contract which the seller has not meanwhile repudiated is not a trespasser. Nor would the statute-of-frauds provisions of this section be a defense to a third person that wrongfully induces a party to refuse to perform an oral contract, even though the injured party cannot maintain an action for damages against the party so refusing to perform.

6. It is not necessary that the record be delivered to anybody, nor is this section intended to displace decisions that have given effect to lost records. It need not be signed by both parties, but except as stated in subsection (2) it is not sufficient against a party that has not signed it. Prior to a dispute, no one can determine which party's signature may be necessary, but from the time of contracting each party should be aware that it is the signature of the other which is important.

7. If the making of a contract is admitted in court, either in a written pleading, by stipulation or by oral statement before the court, or is admitted under oath but not in court, as by testimony in a deposition or an affidavit filed with a motion, no additional record is necessary. Subsection (3)(b) makes it impossible to admit the contract in these contexts and still use the Statute of Frauds as a defense. However, the contract is not thus conclusively established. The admission is evidential against the maker of the truth of the facts admitted and of nothing more; as against the other party, it is not evidential at all.

8. Subsection (4), which is new, repeals the "one year" provision of the Statute of Frauds for contracts

for the sale of goods. The phrase "any other applicable period" recognizes that some state statutes apply to periods longer than one year. The confused and contradictory interpretations under the so-called "one year" clause are illustrated in *C.R. Klewin, Inc. v. Flagship Properties, Inc.*, 600 A.2d 772 (Conn. 1991) (Peters, J.).

## **SECTION 2-202. FINAL WRITTEN EXPRESSION IN A RECORD: PAROL OR EXTRINSIC EVIDENCE.**

(1) Terms with respect to which the confirmatory ~~memoranda~~ records of the parties agree or which are otherwise set forth in a writing record intended by the parties as a final expression of their agreement with respect to such terms as are included therein may not be contradicted by evidence of any prior agreement or of a contemporaneous oral agreement but may be ~~explained or~~ supplemented by evidence of:

(a) ~~by course of dealing or usage of trade (Section 1-205) or by course of performance (Section 2-208)~~ course of performance, course of dealing or usage of trade (Section 1-303); and

(b) ~~by evidence of consistent additional terms unless the court finds the writing record to have been intended also as a complete and exclusive statement of the terms of the agreement.~~

(2) Terms in a record may be explained by evidence of course of performance, course of dealing, or usage of trade without a preliminary determination by the court that the language used is ambiguous.

### **Proposed Comment**

1. Subsection (1) codifies the parol evidence rule, the operation of which depends on the intention of both parties that the terms in a record are the "final expression of their agreement with respect to the included terms." Without this mutual intention to integrate the record, the parol evidence rule does not apply to exclude other terms allegedly agreed to prior to or contemporaneously with the record. Unless there is a final record, these alleged terms are provable as part of the agreement by relevant evidence from any credible source. When each party sends a confirmatory record, mutual intention to integrate is presumed for terms "with respect to which the confirmatory records of the parties agree."

2. Because a record is final for the included terms (an integration), this does not mean that the parties intended that the record contain all the terms of their agreement (a total integration). If a record is final

but not complete and exclusive, it cannot be contradicted by evidence of prior agreements reflected in a record or prior or contemporaneous oral agreements, but it can be supplemented by other evidence, drawn from any source, of consistent additional terms. Even if the record is final, complete and exclusive, it can be supplemented by evidence of noncontradictory terms drawn from an applicable course of performance, course of dealing, or usage of trade unless those sources are carefully negated by a term in the record. If the record is final, complete and exclusive it cannot be supplemented by evidence of terms drawn from other sources, even terms that are consistent with the record.

3. The cross-references in subsection (1)(a) have been changed to correspond with revised Article 1.

4. Whether a writing is final, and whether a final writing is also complete, are issues for the court. This section rejects any assumption that because a record has been worked out which is final on some matters, it is to be taken as including all the matters agreed upon. If the additional terms are those that, if agreed upon, they would certainly have been included in the document in the view of the court, then evidence of their alleged making must be kept from the trier of fact. This article takes no position on the evidentiary strength of a merger clause as evidence of a mutual intent that the record be final and complete since that depends upon the particular circumstances involved.

5. This section does not exclude evidence introduced to show that the contract is avoidable for misrepresentation, mistake, or duress, or that the contract or a term is unenforceable because of unconscionability. Similarly, this section does not operate to exclude evidence of a subsequent modification or evidence that, for the purpose of claiming excuse, both parties assumed that a certain event would not occur.

6. Issues of interpretation are generally left to the courts. In interpreting terms in a record, subsection (2) permits either party to introduce evidence drawn from a course of performance, a course of dealing, or a usage of trade without any preliminary determination by the court that the term at issue is ambiguous. The subsection deals with that circumstance and no other. This article takes no position on whether a preliminary determination of ambiguity is a condition to the admissibility of evidence drawn from any other source or on whether a contract clause can exclude an otherwise applicable implied-in-fact source.

Legislative Note: The cross-references in subsection (1)(a) should not be changed if the jurisdiction has not adopted revised Article 1.

**SECTION 2-203. SEALS INOPERATIVE.** The affixing of a seal to a writing record evidencing a contract for sale or an offer to buy or sell goods does not constitute the writing record a sealed instrument and the law with respect to sealed instruments does not apply to such a contract or offer.

#### **SECTION 2-204. FORMATION IN GENERAL.**

(1) A contract for sale of goods may be made in any manner sufficient to show agreement, including offer and acceptance, conduct by both parties which recognizes the existence of such a contract, the interaction of electronic agents, or the interaction of an electronic agent and an individual.

(2) An agreement sufficient to constitute a contract for sale may be found even though the moment of its making is undetermined.

(3) Even though one or more terms are left open a contract for sale does not fail for indefiniteness if the parties have intended to make a contract and there is a reasonably certain basis for giving an appropriate remedy.

(4) Except as otherwise provided in Sections 2-211 through 2-213, the following rules apply:

(a) A contract may be formed by the interaction of electronic agents of the parties, even if no individual was aware of or reviewed the electronic agents' actions or the resulting terms and agreements.

(b) A contract may be formed by the interaction of an electronic agent and an individual acting on the individual's own behalf or for another person. A contract is formed if the individual takes actions that the individual is free to refuse to take or makes a statement that the individual has reason to know will:

(i) cause the electronic agent to complete the transaction or performance; or

(ii) indicate acceptance of an offer, regardless of other expressions or actions by the individual to which the electronic agent cannot react.

#### **Proposed Comment**

1. Subsection (1) sets forth the basic policy of recognizing any manner of expression of agreement. In addition to traditional contract formation by oral or written agreement, or by performance, subsection (1) provides that an agreement may be made by electronic means. Regardless of how the agreement is formed under this section, the legal effect of the agreement is subject to the other provisions of this Article.

2. Under subsection (1), appropriate conduct by the parties may be sufficient to establish an agreement. Subsection (2) is directed primarily to the situation when the correspondence does not disclose the exact point at which the deal was closed, but the conduct of the parties indicate that a binding obligation has been undertaken.

3. Subsection (3) states the principle for "open terms" which underlies later sections of this Article. If the parties intend to enter into a binding agreement, this subsection recognizes the agreement as valid in law, despite missing terms, if there is any reasonably certain basis for granting a remedy based on commercial standards of indefiniteness. Neither certainty for what the parties were to do nor a finding of the exact amount of damages is required. Neither is the fact that one or more terms are left to be agreed upon enough by itself to defeat an otherwise adequate agreement. This Act makes provision elsewhere for missing terms needed for performance, open price, remedies and the like.

The more terms the parties leave open, the less likely it is that the parties have intended to conclude a binding agreement, but their actions may be conclusive on the matter despite the omissions.

4. Subsections (4)(a) and (b) are derived from Sections 14(a) and (b) of the Uniform Electronic Transactions Act (UETA). Subsection (4)(a) confirms that contracts may be formed by machines functioning as electronic agents parties to a transaction. This subsection is intended to negate any claim that lack of human intent, at the time of contract formation, prevents contract formation. When machines are involved, the requisite intention to contract flows from the programing and use of the machine. This provision, along with sections 2-211, 2-212, and 2-213, is intended to remove barriers to electronic contract formation.

5. Subsection (4)(b) validates contracts formed by an individual and an electronic agent. This subsection substantiates an anonymous click-through transaction. As with subsection (4)(a), the intent to contract by the electronic agent flows from the programing and use of the machine. The requisite intent to contract by the individual is found by the acts of the individual that the individual has reason to know

will be interpreted by the machine as allowing the machine to complete the transaction or performance, or that will be interpreted by the machine as signifying acceptance on the part of the individual. This intent is only found, though, when the individual is free to refuse to take the actions that the machine will interpret as acceptance or allowance to complete the transaction. For example, if A goes to a website that provides for purchasing goods over the Internet, and after choosing items to be purchased is confronted by a screen which advises her that the transaction will be completed if A clicks "I agree" then A will be bound by the click if A knew or had reason to know that the click would be interpreted as signifying acceptance and A was free to refuse the click.

6. Nothing in this section is intended to restrict equitable defenses, such as fraud or mistake, in electronic contract formation. However, because the law of electronic mistake is not well developed, and because factual issues may arise that are not easily resolved by legal standards developed for nonelectronic transactions, courts should not automatically apply standards developed in other contexts. Courts should also factor in the specific differences between electronic and nonelectronic transactions to resolve equitable claims in electronic contracts.

**SECTION 2-205. FIRM OFFERS.** An offer by a merchant to buy or sell goods in a signed record which by its terms gives assurance that it will be held open is not revocable, for lack of consideration, during the time stated or if no time is stated for a reasonable time, but in no event may such period of irrevocability exceed three months; but any such term of assurance ~~on a form~~ in a form record supplied by the offeree must be separately signed by the offeror.

#### **SECTION 2-206. OFFER AND ACCEPTANCE IN FORMATION OF CONTRACT.**

(1) Unless otherwise unambiguously indicated by the language or circumstances

(a) an offer to make a contract shall be construed as inviting acceptance in any manner and by any medium reasonable in the circumstances;

(b) an order or other offer to buy goods for prompt or current shipment shall be construed as inviting acceptance either by a prompt promise to ship or by the prompt or current shipment of conforming or non-conforming goods, but ~~such a~~ the shipment of non-conforming goods does not constitute an acceptance if the seller seasonably notifies the buyer that the shipment is offered only as an accommodation to the buyer.

(2) Where the beginning of a requested performance is a reasonable mode of acceptance an offeror who

that is not notified of acceptance within a reasonable time may treat the offer as having lapsed before acceptance.

(3) A definite and seasonable expression of acceptance in a record operates as an acceptance even if it contains terms additional to or different from the offer.

#### **Proposed Comment**

1. Subsection (1)(b) deals with the situation where a shipment which is made following an order contains defective goods. The nonconforming shipment is normally understood as intended to close the bargain even though it constitutes a breach. However, the seller by stating that the shipment is nonconforming and is offered only as an accommodation to the buyer keeps the shipment of from operating as an acceptance.

2. The mirror image rule is rejected in subsection (3), but any responsive record must still be fairly regarded as an "acceptance" and not as a proposal for a different transaction such that it should be construed to be a rejection of the offer.

#### **SECTION 2-207. ADDITIONAL TERMS IN ACCEPTANCE OR TERMS OF CONTRACT; EFFECT OF CONFIRMATION.**

~~(1) A definite and seasonable expression of acceptance or a written confirmation which is sent within a reasonable time operates as an acceptance even though it states terms additional to or different from those offered or agreed upon, unless acceptance is expressly made conditional on assent to the additional or different terms.~~

~~(2) The additional terms are to be construed as proposals for addition to the contract. Between merchants such terms become part of the contract unless:~~

~~(a) the offer expressly limits acceptance to the terms of the offer;~~

~~(b) they materially alter it; or~~

~~(c) notification of objection to them has already been given or is given within a reasonable time after notice of them is received.~~

~~(3) Conduct by both parties which recognizes the existence of a contract is sufficient to establish a contract for sale although the writings of the parties do not otherwise establish a contract. In such case the terms of the particular contract consist of those terms on which the writings of the parties agree, together with any supplementary terms incorporated under any other provisions of this Act.~~

If (i) conduct by both parties recognizes the existence of a contract although their records do not otherwise establish a contract, (ii) a contract is formed by an offer and acceptance, or (iii) a contract formed in any manner is confirmed by a record that contains terms additional to or different from those in the contract being confirmed, the terms of the contract, subject to Section 2-202, are:

(a) terms that appear in the records of both parties;

(b) terms, whether in a record or not, to which both parties agree; and

(c) terms supplied or incorporated under any provision of this Act.

#### **Proposed Comment**

1. This section applies to all contracts for the sale of goods, and it is not limited only to those contracts where there has been a "battle of the forms."

2. This section applies only when a contract has been formed under other provisions of Article 2. This section functions solely to define the terms of the contract. When forms are exchanged before or during performance, the result from the application of this section differs from the original Section 2-207 and the common law in that this section gives no preference to the first or the last form; it applies the same test to the terms in each. Terms in a record that insist on all of that record's terms and no others as a condition of contract formation have no effect on the operation of this section. When one party's record insists on its own terms as a condition to contract formation, if that party does not subsequently perform or otherwise acknowledge the existence of a contract, if the other party does not agree to those terms, the record's insistence on its own terms will keep a contract from being formed under Sections 2-204 or 2-206, and this section is not applicable. As with original Section 2-207, courts will have to distinguish between "confirmations" that are addressed in this section and "modifications" that are addressed in Section 2-209.

3. By inviting a court to determine whether a party "agrees" to the other party's terms, the text recognizes the enormous variety of circumstances that may be presented under this section, and the

section gives the court greater discretion to include or exclude certain terms than original Section 2-207 did. In many cases, performance alone should not be construed to be agreement to the terms in another's record by one that has sent or will send its own record with additional or different terms. Thus a party that sends a record (however labeled or characterized, including an offer, counteroffer, acceptance, acknowledgment, purchase order, confirmation or invoice) with additional or different terms should not be regarded as having agreed to any of the other party's additional or different terms by performance. In that case, the terms are determined under paragraph (a) (terms in both records) and paragraph (c) (supplied or incorporated by this Act). Concomitantly, performance after an original agreement between the parties (orally, electronically or otherwise) should not normally be construed to be agreement to terms in the other's record unless that record is part of the original agreement.

The result would be different where no agreement precedes the performance and only one party sends a record. If, for example, a buyer sends a purchase order and there is no oral or other agreement, and the seller delivers in response to the purchase order but the seller does not send the seller's own acknowledgment or acceptance, the seller should normally be treated as having agreed to the terms of the purchase order.

Of course, an offeree's unqualified response, such as "I accept," to an offer that contained many terms would show agreement to all of the offer's terms. In some cases an expression of acceptance accompanied by one or more additional terms also might demonstrate the offeree's agreement to the terms of the offer. For example, consider a buyer that sends a purchase order with technical specifications and a seller that responds with a record stating "Thank you for your order. We will fill it promptly. Note that we do not make deliveries after 3:00 p.m. on Fridays." Here a court could find that both parties agreed to the technical specifications.

In some cases a court might find nonverbal agreement to additional or different terms that appear in only one record. If, for example, both parties' forms called for the sale of 700,000 nuts and bolts but the purchase order or another record of the buyer conditioned the sale on a test of a sample to see if the nuts and bolts would perform properly, the seller's sending a small sample to the buyer might be construed to be an agreement to buyer's condition. A court could find that the contract called for arbitration where both forms provided for arbitration but each contained immaterially different arbitration provisions. It is possible that trade practice in a particular trade or course of dealing between contracting parties might treat the offeree's performance as acceptance of the offeror's terms even when the offeree sent its own record; conversely trade practice or course of dealing might bind the offeror to terms in the offeree's form when the expectation in the trade or in the course of dealing so directs.

In a rare case terms in the records of both parties might not become part of the contract; that might happen where the parties contemplated agreement to a single negotiated record, each exchanged similar proposals and commenced interim performance but never reached a negotiated agreement because of differences over crucial terms. There is a limitless variety of verbal and nonverbal behavior that may be claimed to be an agreement to another's record. The section leaves the interpretation of that behavior to the wise discretion of the courts.

4. An "agreement" may include terms derived from a course of performance, a course of dealing, and usage of trade. See Section 1-201. If the members of a trade or if the contracting parties expect to be bound by a term that appears in the record of only one contracting party, that term is part of the agreement. However, repeated use of a particular term or repeated failure to object to a term on another's record is not normally sufficient in itself to establish a course of performance, a course of dealing or a trade usage.

5. The section omits any specific treatment of terms on or in the container in which the goods are delivered. Amended Article 2 takes no position on the question whether a court should follow the reasoning in Hill v. Gateway 2000, 105 F.3d 1147 (7th Cir. 1997) (Section 2-207 does not apply to these cases; the "rolling contract" is not made until acceptance of the seller's terms after the goods and terms are delivered) or the contrary reasoning in Step-Saver Data Systems, Inc. v. Wyse Technology, 939 F.2d 91 (3d Cir.1991) (contract is made at time of oral or other bargain and "shrink wrap" terms or those in the container become part of the contract only if they comply with provisions like Section 2-207).

#### **SECTION 2-208. COURSE OF PERFORMANCE ON PRACTICAL CONSTRUCTION RESERVED.**

~~(1) Where the contract for sale involves repeated occasions for performance by either party with knowledge of the nature of the performance and opportunity for objection to it by the other, any course of performance accepted or acquiesced in without objection shall be relevant to determine the meaning of the agreement.~~

~~(2) The express terms of the agreement and any such course of performance, as well as any course of dealing and usage of trade, shall be construed whenever reasonable as consistent with each other; but when such construction is unreasonable, express terms shall control course of performance and course of performance shall control both course of dealing and usage of trade (Section 1-205).~~

~~(3) Subject to the provisions of the next section on modification and waiver, such course of performance~~

~~shall be relevant to show a waiver or modification of any term inconsistent with such course of performance.~~

#### **Proposed Comment**

This section has been moved to revised Article 1 (Section 1-303).

Legislative Note: This section should not be repealed if the jurisdiction has not adopted revised Article 1.

#### **SECTION 2-209. MODIFICATION; RESCISSION AND WAIVER.**

(1) An agreement modifying a contract within this Article needs no consideration to be binding.

~~(2) A signed agreement~~ An agreement in a signed record which excludes modification or rescission except by a signed ~~writing record~~ cannot be otherwise modified or rescinded, but except as between merchants such a requirement on a form in a form record supplied by the merchant must be separately signed by the other party.

(3) The requirements of the statute of frauds section of this Article (Section 2-201) must be satisfied if the contract as modified is within its provisions.

(4) Although an attempt at modification or rescission does not satisfy the requirements of subsection (2) or (3) it can operate as a waiver.

(5) A party ~~who~~ that has made a waiver affecting an executory portion of the contract may retract the waiver by reasonable notification received by the other party that strict performance will be required of any term waived, unless the retraction would be unjust in view of a material change of position in reliance on the waiver.

#### **SECTION 2-210. DELEGATION OF PERFORMANCE; ASSIGNMENT OF RIGHTS.**

~~(1) A party may perform his duty through a delegate unless otherwise agreed or unless the other party has a substantial interest in having his original promisor perform or control the acts required by the contract. No delegation of performance relieves the party delegating of any duty to perform or any liability for breach.~~

~~(2) Unless otherwise agreed all rights of either seller or buyer can be assigned except where the~~

assignment would materially change the duty of the other party, or increase materially the burden or risk imposed on him by his contract, or impair materially his chance of obtaining return performance. A right to damages for breach of the whole contract or a right arising out of the assignor's due performance of his entire obligation can be assigned despite agreement otherwise.

(3) Unless the circumstances indicate the contrary a prohibition of assignment of "the contract" is to be construed as barring only the delegation to the assignee of the assignor's performance.

(4) An assignment of "the contract" or of "all my rights under the contract" or an assignment in similar general terms is an assignment of rights and unless the language or the circumstances (as in an assignment for security) indicate the contrary, it is a delegation of performance of the duties of the assignor and its acceptance by the assignee constitutes a promise by him to perform those duties. This promise is enforceable by either the assignor or the other party to the original contract.

(5) The other party may treat any assignment which delegates performance as creating reasonable grounds for insecurity and may without prejudice to his rights against the assignor demand assurances from the assignee (Section 2-609).

(1) If the seller or buyer assigns rights under a contract, the following rules apply:

(a) Subject to paragraph (b) and except as otherwise provided in Section 9-406 or as otherwise agreed, all rights of either seller or buyer may be assigned unless the assignment would materially change the duty of the other party, increase materially the burden or risk imposed on that party by the contract, or impair materially that party's chance of obtaining return performance. A right to damages for breach of the whole contract or a right arising out of the assignor's due performance of its entire obligation can be assigned despite an agreement otherwise.

(b) The creation, attachment, perfection, or enforcement of a security interest in the seller's interest under a contract is not an assignment that materially changes the duty of or materially increases the burden or risk imposed on the buyer or materially impairs the buyer's chance of obtaining return performance within paragraph (a) unless, and then only to the extent that, enforcement of the security interest results in a delegation of a material performance of the seller. Even in that event, the creation, attachment, perfection, and enforcement of the security interest remain effective. However, the seller is liable to the buyer for damages caused by the delegation to the extent that the damages could not reasonably be prevented by the buyer, and a court having jurisdiction may grant other appropriate relief, including cancellation of the contract or an injunction against enforcement of the security interest or consummation of the enforcement.

(2) If the seller or buyer delegates performance of its duties under a contract, the following rules apply:

(a) A party may perform its duties through a delegate unless otherwise agreed or unless the other party has a substantial interest in having the original promisor perform or control the acts required by the

contract. No delegation of performance relieves the party delegating of any duty to perform or any liability for breach.

(b) Acceptance of a delegation of duties by the assignee constitutes a promise to perform those duties. This promise is enforceable by either the assignor or the other party to the original contract.

(c) The other party may treat any delegation of duties as creating reasonable grounds for insecurity and may without prejudice to its rights against the assignor demand assurances from the assignee under Section 2-609.

(d) A contractual term prohibiting the delegation of duties otherwise delegable under paragraph (a) is enforceable, and an attempted delegation is not effective.

(3) An assignment of "the contract" or of "all my rights under the contract" or an assignment in similar general terms is an assignment of rights and unless the language or the circumstances, as in an assignment for security, indicate the contrary, it is also a delegation of performance of the duties of the assignor.

(4) Unless the circumstances indicate the contrary a prohibition of assignment of "the contract" is to be construed as barring only the delegation to the assignee of the assignor's performance.

#### **Proposed Comment**

1. This section is consistent with original Section 2-210 but follows a different organizational approach. Subsection (1) deals with the assignment of rights, subsection (2) deals with the delegation of duties, and subsections (3) and (4) are interpretive rules of general applicability. The section has also been changed to conform with revised Article 9.

2. Generally, this section recognizes both the assignment of rights and the delegation of duties as normal and permissible incidents of a contract for the sale of goods.

3. Subsection (1)(a) treats the effect of an assignment by either the seller or the buyer of the rights but not the duties arising under the contract for sale. These rights may be effectively assigned to a third person unless the assignment materially increases the duty, burden or risk, or materially impairs expected performance to the other party, or, subject to subsection (1)(b) and Section 9-406 (discussed below), otherwise agreed. Even then a right to damages for breach of the whole contract or a right arising out of the assignor's due performance of its entire obligation can be assigned despite contrary agreement.

An assignment, however, is not effective if it would "materially change the duty of the other party, increase materially the burden or risk imposed on that party by the contract, or increase materially that party's likelihood of obtaining return performance." Subsection (1)(a). The cases where these limitations apply are rare. For example, a seller that has fully performed the contract should always be able to assign the right to payment. This is the basis for most accounts receivable financing. If, however, the contract is still executory, the assignment of the right to payment to a third person might decrease the seller's incentive to perform and, thus, increase the buyer's risk. Similarly, the buyer's assignment of the right to receive a fixed quantity of goods should not usually be objectionable but if the parties have a "requirements" contract, the assignment could increase materially the seller's risk.

Subsection (1)(a) is subject to Section 9-406 of revised Article 9. That provision makes rights to payment for goods sold ("accounts"), whether or not earned, freely alienable by invalidating anti-assignment terms in agreements between account debtors and seller-assignors, and also by invalidating terms that render these assignments a breach.

4. Subsection (1)(a) is subject to subsection (1)(b), which conforms with revised Article 9. If an assignment of rights creates a security interest in the seller's interest under the contract, including a right to future payments, subsection (1)(b) states that there is no material impairment under subsection (1)(a) unless the creation, attachment, perfection and enforcement "results in a delegation of material performance of the seller." This is not likely in most assignments, and the buyer's basic protection is to demand adequate assurance of due performance from the seller if the assignment creates reasonable grounds for insecurity.

5. Occasionally a seller or buyer will delegate duties under the contract without also assigning rights. For example, a dealer might delegate its duty to procure and deliver a fixed quantity of goods to the buyer to a third party. In these cases, subsection (2) states the limitations on that power. A contract term prohibiting the delegation of duties renders an attempted delegation ineffective. Subsection (2)(d).

Second, if the third person accepts the delegation, an enforceable promise is made to both the delegator and the person entitled under the contract to perform those duties. Subsection (2)(b). In short, as to the person entitled under the contract a third party beneficiary contract is created. However, the delegator's duty to perform under the contract is not discharged unless the person entitled to performance agrees to substitute the delegatee for the delegator (a novation). See subsection (2)(a), last sentence.

Third, the person entitled under the contract may treat any delegation of duties as reasonable grounds for insecurity and may demand adequate assurance of due performance for the assignee-delegatee. Subsection (2)(c).

Finally, in any event, a delegation of duties is not effective if the person entitled under the contract has a "substantial interest in having the original promisor perform or control the performance required by the contract." Subsection (2)(a).

6. In the case of ambiguity, subsection (3) provides a rule of interpretation to determine when an assignment of rights should also be considered a delegation of duties. When there is ambiguity, the preference is to construe the language as both a delegation of duties as well as an assignment of rights.

7. This section is not intended as a complete statement of the law of delegation and assignment but is limited to clarifying a few points doubtful under the case law. Particularly, neither this section nor this Article touches directly on such questions as the need or effect of notice of the assignment, the rights of successive assignees, or any question of the form of an assignment, either as between the parties or as against any third parties. Some of these questions are dealt with in Article 9.

Legislative Note: The cross-reference to Section 9-406 in subsection (1)(a) will have to be deleted if the jurisdiction has not adopted revised Article 9.

## **SECTION 2-211. LEGAL RECOGNITION OF ELECTRONIC CONTRACTS, RECORDS AND SIGNATURES.**

(1) A record or signature may not be denied legal effect or enforceability solely because it is in electronic form.

(2) A contract may not be denied legal effect or enforceability solely because an electronic record was used in its formation.

(3) This article does not require a record or signature to be created, generated, sent, communicated, received, stored, or otherwise processed by electronic means or in electronic form.

(4) A contract formed by the interaction of an individual and an electronic agent under Section 2-204(4) (b) does not include terms provided by the individual if the individual had reason to know that the agent could not react to the terms as provided.

#### **Proposed Comment**

1. This section is new. Subsections (1) and (2) are derived from Section 7(a) and (b) of the Uniform Electronic Transactions Act (UETA), and subsection (3) is derived from Section 5(b) of UETA. Subsection (4) is based on Section 206(c) of the Uniform Computer Information Transactions Act (UCITA). Each subsection conforms to the federal Electronic Signatures in Global and National Commerce Act (15 U.S.C. SECTION 7001 *et seq.*).

2. This section sets forth the premise that the medium in which a record, signature, or contract is created, presented or retained does not affect its legal significance. Subsections (1) and (2) are designed to eliminate the single element of medium as a reason to deny effect or enforceability to a record, signature, or contract. The fact that the information is set forth in an electronic, as opposed to paper, medium is irrelevant.

3. A contract may have legal effect and yet be unenforceable. *See* Restatement 2d Contracts Section 8. To the extent that a contract in electronic form may have legal effect but be unenforceable, subsection (2) validates its legality. Likewise, to the extent that a record or signature in electronic form may have legal effect but be unenforceable, subsection (1) validates the legality of the record or signature.

For example, though a contract may be unenforceable, the parties' electronic records may have collateral effects, as in the case of a buyer that insures goods purchased under a contract that is unenforceable under Section 2-201. The insurance company may not deny a claim on the ground that the buyer is not the owner, though the buyer may have no direct remedy against the seller for failure to deliver. *See* Restatement 2d Contracts, Section 8, Illustration 4. Whether an electronic record or signature is valid under other law is not addressed by this Act.

4. While subsection (2) validates the legality of an electronic contract, it does not in any way diminish the requirements of Sections 2-204 and 2-206 regarding the formation of contracts, and the requirements of those sections, where applicable, must be met for contract formation.

**SECTION 2-212. ATTRIBUTION.** An electronic record or electronic signature is attributed to a person if the record was created by or the signature was the act of the person or the person's electronic agent or the person is otherwise bound by the act under the law.

#### **Proposed Comment**

1. This section is new. It is based on Section 9 of the Uniform Electronic Transactions Act (UETA).

2. As long as the electronic record was created by a person or the electronic signature resulted from a person's action it will be attributed to that person. The legal effect of the attribution is to be derived from other provisions of this Act or from other law. This section simply assures that these rules will be applied in the electronic environment. A person's actions include actions taken by a human agent of the person as well as actions taken by an electronic agent, *i.e.*, the tool, of the person. Although this section may appear to state the obvious, it assures that the record or signature is not ascribed to a machine, as opposed to the person operating or programming the machine.

3. In each of the following cases, both the electronic record and electronic signature would be attributable to a person under this section:

A. The person types his/her name as part of an e-mail purchase order;

B. The person's employee, pursuant to authority, types the person's name as part of an e-mail purchase order;

C. The person's computer, programmed to order goods upon receipt of inventory information within particular parameters, issues a purchase order which includes the person's name, or other identifying information, as part of the order.

In each of these cases, other law would ascribe both the signature and the action to the person if done in a paper medium. This section expressly provides that the same result will occur when an electronic medium is used.

4. Nothing in this section affects the use of an electronic signature as a means of attributing a record to a person. See Section 2-102(a)(1). Once an electronic signature is attributed to the person, the electronic record with which it is associated would also be attributed to the person unless the person established fraud, forgery, or other invalidating cause. However, an electronic signature is not the only method for attribution of a record.

5. In the context of attribution of records, normally the content of the record will provide the necessary information for a finding of attribution. It is also possible that an established course of dealing between parties may result in a finding of attribution. Just as with a paper record, evidence of forgery or counterfeiting may be introduced to rebut the evidence of attribution. The use of facsimile transmissions provides a number of examples of attribution using information other than a signature. A facsimile may be attributed to a person because of the information printed across the top of the page that indicates the machine from which it was sent. Similarly, the transmission may contain a letterhead which identifies the sender. Some cases have held that the letterhead actually constituted a signature because it was a symbol adopted by the sender with intent to sign the record. However, the signature determination resulted from the necessary finding of intention in that case. Other cases have found facsimile letterheads NOT to be signatures because the requisite intention was not present. The critical point is that with or without a signature, information within the electronic record may well suffice to provide the facts resulting in attribution of an electronic record to a particular party.

6. Certain information may be present in an electronic environment that does not appear to attribute but which clearly links a person to a particular record. Numerical codes, personal identification numbers, public and private key combinations, all serve to establish the party to which an electronic record should be attributed. Security procedures will be another piece of evidence available to establish attribution.

7. Once it is established that a record or signature is attributable to a particular person, the effect of the record or signature must be determined in light of the context and surrounding circumstances, including the parties' agreement, if any. This will primarily be governed by other sections of this article. See, e.g., sections 2-201, 2-202, 2-204, 2-206, 2-207, and 2-209.

## **SECTION 2-213 . ELECTRONIC COMMUNICATION.**

(1) If the receipt of an electronic communication has a legal effect, it has that effect even though no individual is aware of its receipt.

(2) Receipt of an electronic acknowledgment of an electronic communication establishes that the communication was received but, in itself, does not establish that the content sent corresponds to the content received.

### **Proposed Comment**

1. This section is new. Its provisions are adapted from Sections 15(e) and (f) of the Uniform Electronic Transactions Act (UETA).

2. This section deals with electronic communications generally and is not limited to electronic records, which must be retrievable in perceivable form. The section does not resolve the questions of when or where electronic communications are determined to be sent or received; nor does it indicate that a communication has any particular substantive legal effect. This Article determines the time of receipt of a notice that is an electronic record.

3. Subsection (1) makes clear that receipt is not dependent on a person having notice that the communication is in the person's electronic system. The paper analog is the recipient that never reads a mail notice.

4. Subsection (2) provides legal certainty regarding the effect of an electronic acknowledgment. It only addresses the fact of receipt, not the quality of the content, nor whether the electronic communication was read or "opened."

5. This section does not address the question of whether the exchange of electronic communications constitutes the formation of a contract. Questions of formation are addressed by Sections 2-204 and 2-206.

### PART 3

#### GENERAL OBLIGATION AND CONSTRUCTION OF CONTRACT

##### SECTION 2-302. UNCONSCIONABLE CONTRACT OR ~~CLAUSE TERM~~.

(1) If the court as a matter of law finds the contract or any ~~clause term~~ of the contract to have been unconscionable at the time it was made the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable ~~clause term~~, or it may so limit the application of any unconscionable ~~clause term~~ as to avoid any unconscionable result.

(2) When it is claimed or appears to the court that the contract or any ~~clause term~~ thereof may be unconscionable the parties shall be afforded a reasonable opportunity to present evidence as to its commercial setting, purpose and effect to aid the court in making the determination.

##### Proposed Comment

1. This section is intended to make it possible for the courts to police explicitly against the contracts or terms which they find to be unconscionable instead of by adverse construction of language, by manipulation of the rules of offer and acceptance or by determinations that the term is contrary to public policy or to the dominant purpose of the contract. The section is intended to allow a court to pass directly on the unconscionability of the contract or a particular term of the contract and to make a conclusion of law as to its unconscionability. Courts have been particularly vigilant when the contract at issue is set forth in a standard form. The principle is one of prevention of oppression and unfair surprise and not of disturbance of allocation of risks because of superior bargaining power. The basic test is whether, in the light of the general commercial background and the commercial needs of the particular trade or case, the term or contract involved is so one-sided as to be unconscionable under the circumstances existing at the time of the making of the contract.

2. Under this section the court, in its discretion, may refuse to enforce the contract as a whole if it is permeated by the unconscionability, or it may strike any single term or group of terms which are so tainted or which are contrary to the essential purpose of the agreement or to material terms to which the parties have expressly agreed, or it may simply limit unconscionable results.

3. The present section is addressed to the court, and the decision is to be made by it. The evidence

referred to in subsection (2) is for the court's consideration, not the jury's. Only the agreement which results from the court's action on these matters is to be submitted to the general trier of the facts.

##### SECTION 2-304. PRICE PAYABLE IN MONEY, GOODS, REALTY, OR OTHERWISE.

(1) The price can be made payable in money or otherwise. If it is payable in whole or in part in goods each party is a seller of the goods which ~~he~~ that party is to transfer.

(2) Even though all or part of the price is payable in an interest in realty the transfer of the goods and the seller's obligations with reference to them are subject to this Article, but not the transfer of the interest in realty or the transferor's obligations in connection therewith.

##### SECTION 2-305. OPEN PRICE TERM.

(1) The parties if they so intend can conclude a contract for sale even though the price is not settled. In such a case the price is a reasonable price at the time for delivery if

(a) nothing is said as to price; or

(b) the price is left to be agreed by the parties and they fail to agree; or

(c) the price is to be fixed in terms of some agreed market or other standard as set or recorded by a third person or agency and it is not so set or recorded.

(2) A price to be fixed by the seller or by the buyer means a price ~~for him to fix~~ to be fixed in good faith.

(3) When a price left to be fixed otherwise than by agreement of the parties fails to be fixed through fault of one party the other may at ~~his~~ the party's option treat the contract as canceled or ~~himself~~ the party may fix a reasonable price.

(4) Where, however, the parties intend not to be bound unless the price be fixed or agreed and it is not fixed or agreed there is no contract. In such a case the buyer must return any goods already received or if unable so to do must pay their reasonable value at the time of delivery and the seller must return any portion of the price paid on account.

### **SECTION 2-308. ABSENCE OF SPECIFIED PLACE FOR DELIVERY.**

Unless otherwise agreed

(a) the place for delivery of goods is the seller's place of business or if ~~he it~~ has none ~~his~~ the seller's residence; but

(b) in a contract for sale of identified goods which to the knowledge of the parties at the time of contracting are in some other place, that place is the place for their delivery; and

(c) documents of title may be delivered through customary banking channels.

### **SECTION 2-309. ABSENCE OF SPECIFIC TIME PROVISIONS; NOTICE OF TERMINATION.**

(1) The time for shipment or delivery or any other action under a contract if not provided in this Article or agreed upon shall be a reasonable time.

(2) Where the contract provides for successive performances but is indefinite in duration it is valid for a reasonable time but unless otherwise agreed may be terminated at any time by either party.

(3) Termination of a contract by one party except on the happening of an agreed event requires that reasonable notification be received by the other party and an agreement dispensing with notification is invalid if its operation would be unconscionable. However, a term specifying standards for the nature and timing of notice is enforceable if the standards are not manifestly unreasonable.

#### **Proposed Comment**

The last sentence of subsection (3) is new and is based on Section 1-102(3). It provides for greater party autonomy. In an appropriate circumstances the parties may agree that the standard for notice is no notice at all.

### **SECTION 2-310. OPEN TIME FOR PAYMENT OR RUNNING OF CREDIT AUTHORITY TO SHIP UNDER RESERVATION.**

Unless otherwise agreed

(a) payment is due at the time and place at which the buyer is to receive the goods even though the place

of shipment is the place of delivery; and

(b) if the seller is required or authorized to send the goods ~~he~~ the seller may ship them under reservation, and may tender the documents of title, but the buyer may inspect the goods after their arrival before payment is due unless such inspection is inconsistent with the terms of the contract (Section 2-513); and

(c) if tender of delivery is authorized and agreed to be made by way of documents of title otherwise than by subsection (b) then payment is due at the time and place at which the buyer is to receive the documents regardless of where the goods are to be received; and

(d) where the seller is required or authorized to ship the goods on credit the credit period runs from the time of shipment but post-dating the invoice or delaying its dispatch will correspondingly delay the starting of the credit period.

#### **Proposed Comment**

The word "required" has been added to paragraph (b) to make that provision consistent with other usages throughout Article 2 and with the common understanding of business practices. See, e.g., Sections 2-504 and 2-509(1). Paragraph (c) has been amended for clarity.

### **SECTION 2-311. OPTIONS AND COOPERATION RESPECTING PERFORMANCE.**

(1) An agreement for sale which is otherwise sufficiently definite (subsection (3) of Section 2-204) to be a contract is not made invalid by the fact that it leaves particulars of performance to be specified by one of the parties. Any such specification must be made in good faith and within limits set by commercial reasonableness.

(2) Unless otherwise agreed specifications relating to assortment of the goods are at the buyer's option and ~~except as otherwise provided in subsections (1)(e) and (3) of Section 2-319~~ specifications or arrangements relating to shipment are at the seller's option.

(3) Where such specification would materially affect the other party's performance but is not seasonably made or where one party's cooperation is necessary to the agreed performance of the other but is not seasonably forthcoming, the other party in addition to all other remedies

(a) is excused for any resulting delay in ~~his own~~ that party's performance; and

(b) may also either proceed to perform in any reasonable manner or after the time for a material part of

his ~~that party's own~~ performance treat the failure to specify or to cooperate as a breach by failure to deliver or accept the goods.

### Proposed Comment

The cross-reference in subsection (2) has been deleted because the referenced provisions no longer exist. The introductory phrase ("[u]nless otherwise agreed") is sufficient to make the point.

## **SECTION 2-312. WARRANTY OF TITLE AND AGAINST INFRINGEMENT; BUYER'S OBLIGATION AGAINST INFRINGEMENT.**

(1) Subject to subsection (2) there is in a contract for sale a warranty by the seller that

(a) ~~the title conveyed shall be good, good~~ and its transfer rightful and shall not, because of any colorable claim to or interest in the goods, unreasonably expose the buyer to litigation; and

(b) ~~the goods shall be delivered free from any security interest or other lien or encumbrance of which the buyer at the time of contracting has no knowledge.~~

~~(2) A warranty under subsection (1) will be excluded or modified only by specific language or by circumstances which give the buyer reason to know that the person selling does not claim title in himself or that it is purporting to sell only such right or title as it or a third person may have.~~

~~(3) Unless otherwise agreed a seller who is a merchant regularly dealing in goods of the kind warrants that the goods shall be delivered free of the rightful claim of any third person by way of infringement or the like but a buyer who furnishes specifications to the seller must hold the seller harmless against any such claim which arises out of compliance with the specifications.~~

(2) Unless otherwise agreed a seller that is a merchant regularly dealing in goods of the kind warrants that the goods shall be delivered free of the rightful claim of any third person by way of infringement or the like but a buyer that furnishes specifications to the seller must hold the seller harmless against any such claim that arises out of compliance with the specifications.

(3) A warranty under this section may be disclaimed or modified only by specific language or by circumstances that give the buyer reason to know that the seller does not claim title, that the seller is purporting to sell only the right or title as the seller or a third person may have, or that the seller is selling subject to any claims of infringement or the like.

### Proposed Comment

1. Subsection (1) makes provision for a buyer's basic needs for a title which the buyer in good faith expects to acquire by the purchase, namely, that the buyer receive a good, clean title transferred also in a rightful manner so that the buyer will not be exposed to a lawsuit in order to protect it. Under subsection (1), the seller warrants that (1) the title conveyed is good, (2) the transfer is rightful, and (3) the transfer does not unreasonably expose the buyer to litigation because a third person has or asserts a "colorable claim" to or interest in the goods.

In addition to sales in which there is an actual cloud on the title, a warranty that the "title conveyed is good and its transfer rightful" also covers cases where the title is good but the transfer is not rightful. For example, a wrongful transfer with good title occurs where a merchant bailee to which goods are entrusted for repair sells them without authority to a buyer in the ordinary course of business. See Section 2-403(2); Sumner v. Fel-Air, Inc., 680 P.2d 1109 (Alaska 1984).

The subsection now expressly states what the courts have long recognized; further protection for the buyer is needed when the title is burdened by colorable claims that affect the value of the goods. See Frank Arnold KRS, Inc. v. L.S. Meier Auction Co., Inc., 806 F.2d 462 (3d Cir. 1986) (two lawsuits contest title); Jeanneret v. Vichey, 693 F.2d 259 (2d Cir. 1982) (export restrictions in country from which painting was taken affect value); Colton v. Decker, 540 N.W.2d 172 (S.D. 1995) (conflicting vehicle identification numbers). Therefore, not only is the buyer entitled to a good title, but the buyer is also entitled to a marketable title, and until the colorable claim is resolved the market for the goods is impaired. See Wright v. Vickaryous, 611 P.2d 20 (Alaska 1980).

The justification for this rule is that the buyer of goods that are warranted as to title has a right to rely on the fact that there will be no need later to have to contest ownership. The mere casting of a substantial shadow over the buyer's title, regardless of the ultimate outcome, violates the warranty of good title. See American Container Corp. v. Hanley Trucking Corp., 111 N.J. Super. 322, 268 A.2d 313,318 (1970). It should be noted that not any assertion of a claim by a third party will constitute a breach of the warranty of title. The claim must be reasonable and colorable. See C.F. Sales, Inc. v. Amfert, 344 N.W.2d 543 (Iowa 1983).

The warranty of title extends to a buyer whether or not the seller was in possession of the goods at the time the sale or contract to sell was made.

Consistent with original Article 2, this section does not provide for a separate warranty of quiet possession in addition to the warranty of title. Disturbance of quiet possession, although not mentioned specifically, is one way, among many, in which the breach of the warranty of title might be established.

The "knowledge" referred to in subsection (1)(b) is actual knowledge as distinct from notice.

2. The provisions of this Article requiring notification to the seller within a reasonable time after the buyer's discovery of a breach (Section 2-607(3)(a)) apply to notice of a breach of the warranty of title when the seller's breach was innocent. However, if the seller's breach was in bad faith, the seller cannot claim prejudice by the delay in giving notice.

3. Subsection (2) provides the warranty against infringement. Unlike the warranty of title, for this warranty the seller must be a merchant that is "regularly dealing in goods of the kind" sold.

When the goods are part of the seller's normal stock and are sold in the normal course of business, it is the seller's duty to see that no claim of infringement of a patent or trademark by a third party will mar the buyer's title. A sale by a person other than a dealer, however, raises no implication in its circumstances of such a warranty. Nor is there such an implication when the buyer orders goods to be assembled, prepared or manufactured on the buyer's own specifications. If, in such a case, the resulting product infringes a patent or trademark, the liability will run from buyer to seller. There is, under these circumstances, a tacit representation on the part of the buyer that the seller will be safe in manufacturing according to the specifications, and the buyer is under an obligation in good faith to indemnify the seller for any loss suffered.

4. Subsection (3) deals with the disclaimer or modification of the warranties of title or against infringement. This is a self-contained provision governing the modification or disclaimer of warranties under this section; the warranties in this section are not designated as "implied" warranties, and hence are not subject to the modification and disclaimer provisions of Section 2-316(2) and (3). Unlike Section 2-316, subsection (3) of this section does not have any specific requirements that the disclaimer or modification be contained in a record or be conspicuous.

Subsection (3) recognizes that sales by sheriffs, executors, certain foreclosing lienors and persons

similarly situated may be so out of the ordinary commercial course that their peculiar character is immediately apparent to the buyer and therefore no personal obligation is imposed upon the seller that is purporting to sell only an unknown or limited right. This subsection does not touch upon and leaves open all questions of restitution arising in these cases, when a unique article so sold is reclaimed by a third party as the rightful owner.

Foreclosure sales under Article 9 are another matter. Section 9-610 of revised Article 9 provides that a disposition of collateral under that section includes warranties such as those imposed by this section on a voluntary disposition of property of the kind involved. Consequently, unless properly excluded under subsection (3) or under the special provisions for exclusion in Section 9-610, a disposition under that section of collateral consisting of goods includes the warranties imposed by subsection (1) and, if applicable, subsection (2).

6. The statute of limitations for a breach of warranty under this section is determined under the provisions set out in Section 2-725(1) and (3)(c).

#### **SECTION 2-313. EXPRESS WARRANTIES BY AFFIRMATION, PROMISE, DESCRIPTION, SAMPLE; REMEDIAL PROMISE.**

(1) In this section, "immediate buyer" means a buyer that enters into a contract with the seller.

(+) (2) Express warranties by the seller to the immediate buyer are created as follows:

(a) Any affirmation of fact or promise made by the seller to the buyer which relates to the goods and becomes part of the basis of the bargain creates an express warranty that the goods shall conform to the affirmation or promise.

(b) Any description of the goods which is made part of the basis of the bargain creates an express warranty that the goods shall conform to the description.

(c) Any sample or model which is made part of the basis of the bargain creates an express warranty that the whole of the goods shall conform to the sample or model.

(2) (3) It is not necessary to the creation of an express warranty that the seller use formal words such as "warrant" or "guarantee" or that he the seller have a specific intention to make a warranty, but an affirmation merely of the value of the goods or a statement purporting to be merely the seller's opinion or commendation of the goods does not create a warranty.

(4) Any remedial promise made by the seller to the immediate buyer creates an obligation that the promise will be performed upon the happening of the specified event.

### **Proposed Comment**

1. Subsections (2) and (3) are identical to original Article 2 except that the term "immediate buyer" is used to make clear that the section is limited to express warranties and remedial promises made by a seller to a buyer with which the seller has a contractual relationship. Sections 2-313A and 2-313B address obligations that run directly from a seller to a remote purchaser.

2. Subsection (4) introduces the term "remedial promise," which was not used in original Article 2. This section deals with remedial promises to immediate buyers; sections 2-313A and 2-313B deal with remedial promises running directly from a seller to a remote purchaser. Remedial promise is defined in Section 2-103(1)(m).

3. "Express" warranties rest on "dickered" aspects of the individual bargain, and go so clearly to the essence of that bargain that words of disclaimer in a form are repugnant to the basic dickered terms. "Implied" warranties rest so clearly on a common factual situation or set of conditions that no particular language or action is necessary to evidence them and they will arise in such a situation unless unmistakably negated. As with original Article 2, warranties of description and sample are designated "express" rather than "implied."

4. This section is limited in its scope and direct purpose to express warranties and remedial promises made by the seller to the immediate buyer as part of a contract for sale. It is not designed in any way to disturb those lines of case law growth which have recognized that warranties need not be confined to contracts within the scope of this Article.

Section 2-313B recognizes that a seller may incur an obligation to a remote purchaser through a medium for communication to the public, such as advertising. An express warranty to an immediate buyer may also arise through a medium for communication to the public if the elements of this section are satisfied.

The fact that a buyer has rights against an immediate seller under this section does not preclude the buyer from also asserting rights against a remote seller under Section 2-313A or 2-313B.

5. The present section deals with affirmations of fact or promises made by the seller, descriptions of the goods, or exhibitions of samples or models, exactly as any other part of a negotiation which ends in a contract is dealt with. No specific intention to make a warranty is necessary if any of these factors is made part of the basis of the bargain. In actual practice affirmations of fact and promises made by the seller about the goods during a bargain are regarded as part of the description of those goods; hence no particular reliance on these statements need be shown in order to weave them into the fabric of the agreement. Rather, any fact which is to take these affirmations or promises, once made, out of the agreement requires clear affirmative proof. The issue normally is one of fact.

6. In view of the principle that the whole purpose of the law of warranty is to determine what it is that the seller has in essence agreed to sell, the policy is adopted of those cases which refuse except in unusual circumstances to recognize a material deletion of the seller's obligation. Thus, a contract is normally a contract for a sale of something describable and described. A clause generally disclaiming "all warranties, express or implied" cannot reduce the seller's obligation for the description and therefore cannot be given literal effect under Section 2-316(1).

This is not intended to mean that the parties, if they consciously desire, cannot make their own bargain as they wish. But in determining what they have agreed upon good faith is a factor and consideration should be given to the fact that the probability is small that a real price is intended to be exchanged for a pseudo-obligation.

7. Subsection (2)(b) makes specific some of the principles set forth above when a description of the goods is given by the seller.

A description need not be by words. Technical specifications, blueprints and the like can afford more exact description than mere language and if made part of the basis of the bargain goods must conform with them. Past deliveries may set the description of quality, either expressly or impliedly by course of dealing. Of course, all descriptions by merchants must be read against the applicable trade usages with the general rules as to merchantability resolving any doubts.

8. The basic situation as to statements affecting the true essence of the bargain is no different when a sample or model is involved in the transaction. This section includes both a "sample" actually drawn

from the bulk of goods which is the subject matter of the sale, and a "model" which is offered for inspection when the subject matter is not at hand and which has not been drawn from the bulk of the goods.

Although the underlying principles are unchanged, the facts are often ambiguous when something is shown as illustrative, rather than as a straight sample. In general, the presumption is that any sample or model, just as any affirmation of fact, is intended to become a basis of the bargain. But there is no escape from the question of fact. When the seller exhibits a sample purporting to be drawn from an existing bulk, good faith of course requires that the sample be fairly drawn. But in mercantile experience the mere exhibition of a "sample" does not of itself show whether it is merely intended to "suggest" or to "be" the character of the subject-matter of the contract. The question is whether the seller has so acted with reference to the sample as to become responsible that the whole shall have at least the values shown by it. The circumstances aid in answering this question. If the sample has been drawn from an existing bulk, it must be regarded as describing values of the goods contracted for unless it is accompanied by an unmistakable denial of responsibility. If, on the other hand, a model of merchandise not on hand is offered, the mercantile presumption that it has become a literal description of the subject matter is not so strong, and particularly so if modification on the buyer's initiative impairs any feature of the model.

9. The precise time when words of description or affirmation are made or samples are shown is not material. The sole question is whether the language or samples or models are fairly to be regarded as part of the contract. If language that would otherwise create an obligation under this section is used after the closing of the deal (as when the buyer when taking delivery asks and receives an additional assurance), an obligation will arise if the requirements for a modification are satisfied. See Downie v. Abex Corp., 741 F.2d 1235 (10th Cir. 1984).

10. Concerning affirmations of value or a seller's opinion or commendation under subsection (3), the basic question remains the same: What statements of the seller have in the circumstances and in objective judgment become part of the basis of the bargain? As indicated above, all of the statements of the seller do so unless good reason is shown to the contrary. The provisions of subsection (3) are included, however, since common experience discloses that some statements or predictions cannot fairly be viewed as entering into the bargain. Even as to false statements of value, however, the possibility is left open that a remedy may be provided by the law relating to fraud or misrepresentation.

There are a number of factors relevant to determining whether an expression creates a warranty under this section or is merely puffing. For example, the relevant factors may include whether the seller's representations taken in context, (1) were general rather than specific, (2) related to the consequences of

buying rather than the goods themselves, (3) were "hedged" in some way, (4) were related to experimental rather than standard goods, (5) were concerned with some aspects of the goods but not a hidden or unexpected non-conformity, (6) were informal statements made in a formal contracting process, (7) were phrased in terms of opinion rather than fact, or (8) were not capable of objective measurement.

11. The use of the word "promise" in subsection (2)(a) is unusual in that it refers to statements about the quality or performance characteristics of the goods. For example, a seller might make an affirmation of fact to the buyer that the goods are of a certain quality, or may promise that the goods when delivered will be of a certain quality, or may promise that the goods will perform in a certain manner after delivery. In normal usage, "promise" refers to a what a person, not goods, will do; that is, a promise is a commitment to act, or refrain from acting, in a certain manner in the future. A promise about the quality or performance characteristics of the goods creates an express warranty if the other elements of a warranty are present whereas a promise by which the seller commits itself to take remedial action upon the happening of a specified event is a remedial promise. The distinction has meaning in the context of the statute of limitations. A right of action for breach of an express warranty accrues when the goods are tendered to the immediate buyer (Section 2-725(3)(a)) unless the warranty consists of a promise that explicitly extends to the future performance of the goods and discovery must await the time for performance, in which case accrual occurs when the immediate buyer discovers or should have discovered the breach (Section 2-725(3)(d)). Section 2-725(2)(c) separately addresses the accrual of a right of action for breach of a remedial promise.

Remedial promise is dealt with in a separate subsection to make clear that it is a concept separate and apart from express warranty and that the elements of an express warranty, such as basis of the bargain, are not applicable.

#### **SECTION 2-313A. OBLIGATION TO REMOTE PURCHASER CREATED BY RECORD PACKAGED WITH OR ACCOMPANYING GOODS.**

(1) This section applies only to new goods and goods sold or leased as new goods in a transaction of purchase in the normal chain of distribution. In this section:

(a) "Immediate buyer" means a buyer that enters into a contract with the seller.

(b) "Remote purchaser" means a person that buys or leases goods from an immediate buyer or other person in the normal chain of distribution.

(2) If a seller in a record packaged with or accompanying the goods makes an affirmation of fact or promise that relates to the goods, provides a description that relates to the goods, or makes a remedial promise, and the seller reasonably expects the record to be, and the record is, furnished to the remote purchaser, the seller has an obligation to the remote purchaser that:

(a) the goods will conform to the affirmation of fact, promise or description unless a reasonable person in the position of the remote purchaser would not believe that the affirmation of fact, promise or description created an obligation; and

(b) the seller will perform the remedial promise.

(3) It is not necessary to the creation of an obligation under this section that the seller use formal words such as "warrant" or "guarantee" or that the seller have a specific intention to undertake an obligation, but an affirmation merely of the value of the goods or a statement purporting to be merely the seller's opinion or commendation of the goods does not create an obligation.

(4) The following rules apply to the remedies for breach of an obligation created under this section:

(a) The seller may modify or limit the remedies available to the remote purchaser if the modification or limitation is furnished to the remote purchaser no later than the time of purchase or if the modification or limitation is contained in the record that contains the affirmation of fact, promise or description.

(b) Subject to a modification or limitation of remedy, a seller in breach is liable for incidental or consequential damages under Section 2-715, but the seller is not liable for lost profits.

(c) The remote purchaser may recover as damages for breach of a seller's obligation arising under subsection (2) the loss resulting in the ordinary course of events as determined in any manner that is reasonable.

(5) An obligation that is not a remedial promise is breached if the goods did not conform to the affirmation of fact, promise or description creating the obligation when the goods left the seller's control.

#### **Proposed Comment**

1. Sections 2-313A and 2-313B are new, and they follow case law and practice in extending a seller's obligations regarding new goods to remote purchasers. This section deals with what are commonly called "pass-through warranties". In the paradigm situation, a manufacturer will sell goods in a package to a retailer and include in the package a record that sets forth the obligations that the manufacturer is willing to undertake in favor of the ultimate party in the distributive chain, the person that buys or leases the goods from the retailer. If the manufacturer had sold the goods directly to the ultimate party the statements in the record might amount to an express warranty or remedial promise under Section 2-313.

No direct contract exists between the seller and the remote purchaser, and thus the seller's obligation under this section is not referred to as an "express warranty." Use of "obligation" rather than "express warranty" avoids any inference that the basis of the bargain test is applicable here. The test for whether an obligation other than a remedial promise arises is similar in some respects to the basis of the bargain test, but the test set forth in this section is exclusive. Because "remedial promise" in Section 2-313 is not subject to the basis of the bargain test, that term is used in this section.

2. The party to which an obligation runs under this section may either buy or lease the goods, and thus the term "remote purchaser" is used. The term is more limited than "purchaser" in Article 1, however, and does not include a donee or any voluntary transferee who is not a buyer or lessee. Moreover, the remote purchaser must be part of the normal chain of distribution for the particular product. That chain will by definition include at least three parties and may well include more - for example, the manufacturer might sell first to a wholesaler, that would then resell the goods to a retailer for sale or lease to the public. A buyer or lessee from the retailer would qualify as a remote purchaser and could invoke this section against either the manufacturer or the wholesaler (if the wholesaler provided a record to the retailer to be furnished to the ultimate party), but no subsequent transferee, such as a used-goods buyer or sublessee, could qualify. The law governing assignment and third-party beneficiary, including Section 2-318, must be consulted to determine whether a party other than the remote purchaser can enforce an obligation created under this section.

3. The application of this section is limited to new goods and goods sold or leased as new goods within the normal chain of distribution. It does not apply to goods that are sold outside the normal chain, such as "gray" goods or salvaged goods, nor does it apply if the goods are unused but sold as seconds. The concept is flexible, and determining whether goods have been sold or leased in the normal chain of distribution requires consideration of the seller's expectations with regard to the manner in which its goods will reach the remote purchaser. For example, a car manufacturer may be aware that certain of its dealers transfer cars among themselves, and under the particular circumstances of the case a court might find that a new car sold initially to one dealer but leased to the remote purchaser by another dealer was leased in the normal chain of distribution. The concept may also include such practices as door-to-door sales and distribution through a nonprofit organization (e.g., Girl Scout cookies).

The phrase "goods sold or leased as new goods" refers to goods that in the normal course of business would be considered new. There are many instances in which goods might be used for a limited purpose yet be sold or leased in the normal chain of distribution as new goods. For example, goods that have been returned to a dealer by a purchaser and placed back into the dealer's inventory might be sold or leased as new goods in the normal chain of distribution. Other examples might include goods that have

been used for the purpose of inspection (e.g., a car that has been test-driven) and goods that have been returned by a sale-or-return buyer (Section 2-326).

4. This section applies only to obligations set forth in a record that is packaged with the goods or otherwise accompanies them (subsection (2)). Examples include a label affixed to the outside of a container, a card inside a container, or a booklet handed to the remote purchaser at the time of purchase. In addition, the seller must be able to anticipate that the remote purchaser will acquire the record, and therefore this section is limited to records that the seller reasonably expects to be furnished, and that are in fact furnished, to the remote purchaser.

Neither this section nor Section 2-313B are intended to overrule cases that impose liability on facts outside the direct scope of one of the sections. For example, the sections are not intended to overrule a decision imposing liability on a seller that distributes a sample to a remote purchaser.

5. Obligations other than remedial promises created under this section are analogous to express warranties and are subject to a test that is akin to the basis of the bargain test of Section 2-313(2). The seller is entitled to shape the scope of the obligation, and the seller's language tending to create an obligation must be considered in context. If a reasonable person in the position of the remote purchaser, reading the seller's language in its entirety, would not believe that an affirmation of fact, promise or description created an obligation, there is no liability under this section.

6. There is no difference between remedial promise as used in this section (and Section 2-313B) and the same term as used in Section 2-313.

7. Subsection (4)(a) makes clear that the seller may employ the provisions of Section 2-719 to modify or limit the remedies available to the remote purchaser for breach of the seller's obligation hereunder. The modification or limitation may appear on the same record as the one which creates the obligation, or it may be provided to the remote purchaser separately, but in no event may it be furnished to the remote purchaser any later than the time of purchase.

The requirements and limitations set forth in Section 2-719, such as the requirement of an express statement of exclusivity and the tests for failure of essential purpose (Section 2-719(2)) and

unconscionability (Section 2-719(3)) are applicable to a modification or limitation of remedy under this section.

8. As with express warranties, no specific language or intention is necessary to create an obligation, and whether an obligation exists is normally an issue of fact. Subsection (3) is virtually identical to Section 2-313(3), and the tests developed under the common law and under that section to determine whether a statement creates an obligation or is mere puffing are directly applicable to this section.

Just as a seller can limit the extent to which its language creates an express warranty under Section 2-313 by placing that language in a broader context, so too can a seller under this section or Section 2-313B limit the extent of its liability to a remote purchaser (subsection(4)(a)). In other words, the seller, in undertaking an obligation under these sections, can spell out the scope and limits of that obligation.

9. As a rule, a remote purchaser may recover monetary damages measured in the same manner as in the case of an aggrieved buyer under Section 2-714, including incidental and consequential damages to the extent they would be available to an aggrieved buyer. Subsection (4)(c) parallels Section 2-714(1) in allowing the buyer to recover for loss resulting in the ordinary course of events as determined in any manner which is reasonable. In the case of an obligation that is not a remedial promise, the normal measure of damages would be the difference between the value of the goods if they had conformed to the seller's statements and their actual value, and the normal measure of damages for breach of a remedial promise would be the difference between the value of the promised remedial performance and the value of the actual performance received.

Subsection (4)(b) precludes a remote purchaser from recovering consequential damages that take the form of lost profits.

Legislative Note: To maintain their relative positions in this Act, Sections 2-313A and 2-313B may have to be renumbered according to the convention used by a particular state. For example, in some states they may be designated as 2-313.1 and 2-313.2.

#### **SECTION 2-313B. OBLIGATION TO REMOTE PURCHASER CREATED BY**

## **COMMUNICATION TO THE PUBLIC.**

(1) This section applies only to new goods and goods sold or leased as new goods in a transaction of purchase in the normal chain of distribution. In this section:

(a) "Immediate buyer" means a buyer that enters into a contract with the seller.

(b) "Remote purchaser" means a person that buys or leases goods from an immediate buyer or other person in the normal chain of distribution.

(2) If a seller in advertising or a similar communication to the public makes an affirmation of fact or promise that relates to the goods, provides a description that relates to the goods, or makes a remedial promise, and the remote purchaser enters into a transaction of purchase with knowledge of and with the expectation that the goods will conform to the affirmation of fact, promise, or description, or that the seller will perform the remedial promise, the seller has an obligation to the remote purchaser that:

(a) the goods will conform to the affirmation of fact, promise or description unless a reasonable person in the position of the remote purchaser would not believe that the affirmation of fact, promise or description created an obligation; and

(b) the seller will perform the remedial promise.

(3) It is not necessary to the creation of an obligation under this section that the seller use formal words such as "warrant" or "guarantee" or that the seller have a specific intention to undertake an obligation, but an affirmation merely of the value of the goods or a statement purporting to be merely the seller's opinion or commendation of the goods does not create an obligation.

(4) The following rules apply to the remedies for breach of an obligation created under this section:

(a) The seller may modify or limit the remedies available to the remote purchaser if the modification or limitation is furnished to the remote purchaser no later than the time of purchase. The modification or limitation may be furnished as part of the communication that contains the affirmation of fact, promise or description.

(b) Subject to a modification or limitation of remedy, a seller in breach is liable for incidental or consequential damages under Section 2-715, but the seller is not liable for lost profits.

(c) The remote purchaser may recover as damages for breach of a seller's obligation arising under subsection (2) the loss resulting in the ordinary course of events as determined in any manner that is reasonable.

(5) An obligation that is not a remedial promise is breached if the goods did not conform to the

affirmation of fact, promise or description creating the obligation when the goods left the seller's control.

## **Proposed Comment**

1. Sections 2-313B and 2-313A are new, and they follow case law and practice in extending a seller's obligations regarding new goods to remote purchasers. This section deals with obligations to a remote purchaser created by advertising or a similar communication to the public. In the paradigm situation, a manufacturer will engage in an advertising campaign directed towards all or part of the market for its product and will make statements that if made to an immediate buyer would amount to an express warranty or remedial promise under Section 2-313. The goods, however, are sold to someone other than the recipient of the advertising and are then resold or leased to the recipient. By imposing liability on the seller, this section adopts the approach of cases such as *Randy Knitwear, Inc. v. American Cyanamid Co.*, 11 N.Y.2d 5, 226 N.Y.S.2d 363, 181 N.E.2d 399 (Ct. App. 1962).

If the seller's advertisement is made to an immediate buyer, whether the seller incurs liability is determined by Section 2-313 and this section is inapplicable.

2. This section parallels Section 2-313A in most respects, and the Proposed Comments to that section should be consulted. In particular, the reasoning of Comment 1 (scope and terminology), Comment 2 (definition of remote purchaser), Comment 3 (new goods and goods sold as new goods in the normal chain of distribution), Comment 4 (reasonable person in the position of the remote purchaser), Comment 6 (modification or limitation of remedy), Comment 7 (puffing and limitations on extent of obligation) and Comment 8 (damages) is adopted here.

3. This section provides an additional test for enforceability not found in Section 2-313A. In order to be held liable, the remote purchaser must, at the time of purchase, have knowledge of the affirmation of fact, promise, description or remedial promise and must also have an expectation that the goods will conform or that the seller will comply. This test is entirely subjective, while the reasonable person test in subsection (2)(a) is objective in nature.

Put another way, the seller will incur no liability to the remote purchaser if: i) the purchaser did not have knowledge of the seller's statement at the time of purchase; ii) the remote purchaser knew of the seller's statement at the time of purchase but did not expect the goods to conform or the seller to comply; iii) a reasonable person in the position of the remote purchaser would not believe that the seller's statement created an obligation (this test does not apply to remedial promises), or iv) the seller's statement is puffing.

In determining whether the tests set forth in this section are satisfied, a court should consider the temporal relationship between the communication and the purchase. For example, the remote purchaser may acquire the goods years after the seller's advertising campaign. In this circumstance, it would be highly unusual for the advertisement to have created the level of expectation in the remote purchaser or belief in the reasonable person in the position of the remote person necessary for the creation of an obligation under this section.

5. In determining whether an obligation arises under this Section, all information known to the remote purchaser at the time of contracting must be considered. For example, a news release by a manufacturer limiting the statements made in its advertising and known by the remote purchaser, or a communication to the remote purchaser by the immediate seller limiting the statements made in the manufacturer's advertising must be considered in determining whether the expectation test applicable to the remote purchaser and the belief test applicable to the reasonable person in the position of the remote purchaser are satisfied.

6. The remedies for breach of an obligation arising under this section may be modified or limited as set forth in Section 2-719. The modification or limitation may be contained in the advertisement that creates the obligation, or it may be separately furnished to the remote purchaser no later than the time of purchase.

7. Section 2-318 deals with the extension of obligations to certain third-party beneficiaries. Of course, no extension is necessary if the goods are purchased by an agent. In this case, the knowledge and expectation of the principal, not the agent, are relevant in determining whether an obligation arises under this section. Nothing in this Act precludes a court from determining that a household operates as a buying unit under the law of agency.

*Legislative Note: In order to maintain their relative positions in this Act, Sections 2-313A and 2-313B may have to be renumbered according to the convention used by a particular state. For example, in some states they may be designated as 2-313.1 and 2-313.2.*

## **SECTION 2-314. IMPLIED WARRANTY: MERCHANTABILITY; USAGE OF TRADE.**

(1) Unless excluded or modified (Section 2-316), a warranty that the goods shall be merchantable is implied in a contract for their sale if the seller is a merchant with respect to goods of that kind. Under this section the serving for value of food or drink to be consumed either on the premises or elsewhere is a sale.

(2) Goods to be merchantable must be at least such as

(a) pass without objection in the trade under the contract description; and

(b) in the case of fungible goods, are of fair average quality within the description; and

(c) are fit for the ordinary purposes for which such goods of that description are used; and

(d) run, within the variations permitted by the agreement, of even kind, quality and quantity within each unit and among all units involved; and

(e) are adequately contained, packaged, and labeled as the agreement may require; and

(f) conform to the promise or affirmations of fact made on the container or label if any.

(3) Unless excluded or modified (Section 2-316) other implied warranties may arise from course of dealing or usage of trade.

### **Proposed Comment**

1. The phrase "goods of that description" rather than "for which such goods are used" is used in subsection (2)(c). This emphasizes the importance of the agreed description in determining fitness for ordinary purposes.

2. The seller's obligation applies to present sales as well as to contracts to sell subject to the effects of any examination of specific goods. See Section 2-316(5). Also, the warranty of merchantability applies to sales for use as well as to sales for resale.

3. The question when the warranty is imposed turns basically on the meaning of the terms of the agreement as recognized in the trade. Goods delivered under an agreement made by a merchant in a

given line of trade must be of a quality comparable to that generally acceptable in that line of trade under the description or other designation of the goods used in the agreement. The responsibility imposed rests on any merchant-seller.

4. A specific designation of goods by the buyer does not exclude the seller's obligation that they be fit for the general purposes appropriate to the goods. A contract for the sale of second-hand goods, however, involves only an obligation as is appropriate to the goods for that is their contract description. A person making an isolated sale of goods is not a "merchant" within the meaning of the full scope of this section and, thus, no warranty of merchantability would apply. The seller's knowledge of any defects not apparent on inspection would, however, without need for express agreement and in keeping with the underlying reason of the present section and the provisions on good faith, impose an obligation that known material but hidden defects be fully disclosed.

5. Although a seller may not be a "merchant" as to the goods in question, if the seller states generally that the goods are "guaranteed" the provisions of this section may furnish a guide to the content of the resulting express warranty. This has particular significance in the case of second-hand sales, and has further significance in limiting the effect of fine-print disclaimer clauses where their effect would be inconsistent with large-print assertions of "guaranteee."

6. The second sentence of subsection (1) covers the warranty with respect to food and drink. The serving for value of food or drink for consumption on the premises or elsewhere is treated as a sale. Thus, both the patron in a restaurant and a buyer of "take out" food are protected by the implied warranty of merchantability.

7. Suppose that an unmerchantable lawn mower causes personal injury to the buyer, who is operating the mower. Without more, the buyer can sue the seller for breach of the implied warranty of merchantability and recover for injury to person "proximately resulting" from the breach. Section 2-715(2)(b).

This opportunity does not resolve the tension between warranty law and tort law where goods cause personal injury or property damage. The primary source of that tension arises from disagreement over whether the concept of defect in tort and the concept of merchantability in Article 2 are coextensive where personal injuries are involved, *i.e.*, if goods are merchantable under warranty law can they still be defective under tort law, and if goods are not defective under tort law can they be unmerchantable under warranty law? The answer to both questions should be no, and the tension between merchantability in

warranty and defect in tort where personal injury or property damage is involved should be resolved as follows:

When recovery is sought for injury to person or property, whether goods are merchantable is to be determined by applicable state products liability law. When, however, a claim for injury to person or property is based on an implied warranty of fitness under Section 2-315 or an express warranty under Section 2-313 or an obligation arising under Section 2-313A or 2-313B, this Article determines whether an implied warranty of fitness or an express warranty was made and breached, as well as what damages are recoverable under Section 2-715.

To illustrate, suppose that the seller makes a representation about the safety of a lawn mower that becomes part of the basis of the buyer's bargain. The buyer is injured when the gas tank cracks and a fire breaks out. If the lawnmower without the representation is not defective under applicable tort law, it is not unmerchantable under this section. On the other hand, if the lawnmower did not conform to the representation about safety, the seller made and breached an express warranty and the buyer may sue under Article 2.

8. Subsection (2) does not purport to exhaust the meaning of "merchantable" nor to negate any of its attributes not specifically mentioned in the text of the statute, but arising by usage of trade or through case law. The language used is "must be at least such as ...," and the intention is to leave open other possible attributes of merchantability.

9. Paragraphs (a) and (b) of subsection (2) are to be read together. Both refer, as indicated above, to the standards of that line of the trade which fits the transaction and the seller's business. "Fair average" is a term directly appropriate to agricultural bulk products and means goods centering around the middle belt of quality, not the least or the worst that can be understood in the particular trade by the designation, but such as can pass "without objection." Of course a fair percentage of the least is permissible but the goods are not "fair average" if they are all of the least or worst quality possible under the description. In cases of doubt as to what quality is intended, the price at which a merchant closes a contract is an excellent indication of the nature and scope of the merchant's obligation under the present section.

10. Fitness for the ordinary purposes for which goods of the type are used is a fundamental concept of the present section and is covered in paragraph (2)(c). As stated above, merchantability is also a part of the obligation owing to the buyer for use. Correspondingly, protection, under this aspect of the warranty,

of the person buying for resale to the ultimate consumer is equally necessary, and merchantable goods must therefore be "honestly" resalable in the normal course of business because they are what they purport to be.

11. Paragraph (2)(d) on evenness of kind, quality and quantity follows case law. But precautionary language has been added as a remainder of the frequent usages of trade which permit substantial variations both with and without an allowance or an obligation to replace the varying units.

12. Paragraph (2)(e) applies only where the nature of the goods and of the transaction require a certain type of container, package or label. Paragraph (2)(f) applies, on the other hand, wherever there is a label or container on which representations are made, even though the original contract, either by express terms or usage of trade, may not have required either the labeling or the representation. This follows from the general obligation of good faith which requires that a buyer should not be placed in the position of reselling or using goods delivered under false representations appearing on the package or container. No problem of extra consideration arises in this connection since, under this Article, an obligation is imposed by the original contract not to deliver mislabeled articles, and the obligation is imposed where mercantile good faith so requires and without reference to the doctrine of consideration.

13. Exclusion or modification of the warranty of merchantability, or of any part of it, is dealt with in Section 2-316. That section must be read with particular reference to its subsection (6) on limitation of remedies. The warranty of merchantability, wherever it is normal, is so commonly taken for granted that its exclusion from the contract is a matter threatening surprise and therefore requiring special precaution.

14. Subsection (3) is to make explicit that usage of trade and course of dealing can create warranties and that they are implied rather than express warranties and thus subject to exclusion or modification under Section 2-316. A typical instance would be the obligation to provide pedigree papers to evidence conformity of the animal to the contract in the case of a pedigreed dog or blooded bull.

15. In an action based on breach of warranty, it is of course necessary to show not only the existence of the warranty but the fact that the warranty was broken and that the breach of the warranty was the proximate cause of the loss sustained. In such an action an affirmative showing by the seller that the loss resulted from some action or event following the seller's delivery of the goods can operate as a defense. Equally, evidence indicating that the seller exercised care in the manufacture, processing or selection of the goods is relevant to the issue of whether the warranty was in fact broken. Action by the buyer

following an examination of the goods which ought to have indicated the defect complained of can be shown as matter bearing on whether the breach itself was the cause of the injury.

## **SECTION 2-316. EXCLUSION OR MODIFICATION OF WARRANTIES.**

(1) Words or conduct relevant to the creation of an express warranty and words or conduct tending to negate or limit warranty shall be construed wherever reasonable as consistent with each other; but subject to the provisions of this Article on parol or extrinsic evidence (Section 2-202) negation or limitation is inoperative to the extent that such construction is unreasonable.

(2) Subject to subsection (3), to exclude or modify the implied warranty of merchantability or any part of it in a consumer contract the language must be in a record, be conspicuous and state "The seller undertakes no responsibility for the quality of the goods except as otherwise provided in this contract," and in any other contract the language must mention merchantability and in case of a writing record must be conspicuous, and to Subject to subsection (3), to exclude or modify the implied warranty of fitness the exclusion must be by a writing in a record and be conspicuous. Language to exclude all implied warranties of fitness in a consumer contract must state "The seller assumes no responsibility that the goods will be fit for any particular purpose for which you may be buying these goods, except as otherwise provided in the contract," and in any other contract the language is sufficient if it states, for example, that "There are no warranties which extend beyond the description on the face hereof." Language that satisfies the requirements of this subsection for the exclusion and modification of a warranty in a consumer contract also satisfies the requirements for any other contract.

(3) Notwithstanding subsection (2):

(a) unless the circumstances indicate otherwise, all implied warranties are excluded by expressions like "as is", "with all faults" or other language which in common understanding calls the buyer's attention to the exclusion of warranties and, makes plain that there is no implied warranty, and in a consumer contract evidenced by a record is set forth conspicuously in the record; and

(b) when the buyer before entering into the contract has examined the goods or the sample or model as fully as he desired or has refused to examine the goods after a demand by the seller there is no implied warranty with regard to defects which an examination ought in the circumstances to have revealed to him the buyer; and

(c) an implied warranty can also be excluded or modified by course of dealing or course of performance or usage of trade.

(4) Remedies for breach of warranty can be limited in accordance with the provisions of this article on

liquidation or limitation of damages and on contractual modification of remedy (Sections 2-718 and 2-719).

### **Proposed Comment**

**1. Changes.** This section contains the following changes from original Section 2-718:

a) Subsection (2) sets forth new and more informative language for disclaimers of the implied warranty of merchantability and the implied warranty of fitness in consumer contracts. In both instances the language must be in a record and must be conspicuous. Use of this new language satisfies the requirements of this subsection for nonconsumer contracts.

b) If a consumer contract is set forth in a record, subsection (3) cannot be satisfied unless the language is in a record and is conspicuous.

c) Subsection (3)(b) now explicitly requires that there can be no refusal by a buyer unless there is a demand by the seller. Formerly, this requirement was found only in the comments.

2. Subsection (1) is designed principally to deal with those frequent clauses in sales contracts which seek to exclude "all warranties, express or implied." It seeks to protect a buyer from unexpected and unbargained language of disclaimer by denying effect to this language when inconsistent with language of express warranty and permitting the exclusion of implied warranties only by language or other circumstances which protect the buyer from surprise.

The seller is protected against false allegations of oral warranties by this Article's provisions on parol and extrinsic evidence and against unauthorized representations by the customary "lack of authority" clauses. This Article treats the limitation or avoidance of consequential damages as a matter of limiting remedies for breach, separate from the matter of creation of liability under a warranty. If no warranty exists, there is of course no problem of limiting remedies for breach of warranty. Under subsection (4), the question of limitation of remedy is governed by the sections referred to rather than by this section.

**3. The organizational structure of this section has not been changed. The general test for disclaimers of**

implied warranties remains in subsection (3)(a), and the more specific tests remain in subsection (2). A disclaimer that satisfies the requirements of subsection (3)(a) need not also satisfy any of the requirements of subsection (2).

4. Subsection (2) now distinguishes between commercial and consumer contracts. In a commercial contract, language within the contemplation of the subsection disclaiming the implied warranty of merchantability need not be in a record, but if it is in a record it must be conspicuous. Under this subsection, both record and conspicuousness are required to disclaim the implied warranty of merchantability in a consumer contract and to disclaim the implied warranty of fitness in any contract. Use of the language required by this subsection for consumer contracts satisfies the subsections language requirements for other contracts.

5. Subsection (3)(a) deals with general terms such as "as is," "as they stand," "with all faults," and the like. These terms in ordinary commercial usage are understood to mean that the buyer takes the entire risk as to the quality of the goods involved. The terms covered by the subsection are in fact merely a particularization of subsection (3)(c), which provides for exclusion or modification of implied warranties by usage of trade. Nothing in subsection (3)(a) prevents a term such as "there are no implied warranties" from being effective in appropriate circumstances, as when the term is a negotiated term between commercial parties.

Satisfaction of subsection (3)(a) does not require that the language be set forth in a record, but if there is a record the language must be conspicuous if the contract is a consumer contract.

6. Subsection (2) presupposes that the implied warranty in question exists unless excluded or modified. Whether or not language of disclaimer satisfies the requirements of this section, the language may be relevant under other sections to the question whether the warranty was ever in fact created. Thus, unless the provisions of this Article on parol and extrinsic evidence prevent, oral language of disclaimer may raise issues of fact as to whether reliance by the buyer occurred and whether the seller had "reason to know" under the section on implied warranty of fitness for a particular purpose.

7. The exceptions to the general rule set forth in subsections (3)(b) and (3)(c) are common factual situations in which the circumstances surrounding the transaction are in themselves sufficient to call the buyer's attention to the fact that no implied warranties are made or that a certain implied warranty is being excluded.

Under subsection (3)(b), warranties may be excluded or modified by the circumstances where the buyer examines the goods or a sample or model of them before entering into the contract. "Examination" as used in this paragraph is not synonymous with inspection before acceptance or at any other time after the contract has been made. It goes rather to the nature of the responsibility assumed by the seller at the time of the making of the contract. Of course if the buyer discovers the defect and uses the goods anyway, or if the buyer unreasonably fails to examine the goods before using them, resulting injuries may be found to result from the buyer's own action rather than proximately from a breach of warranty. See Sections 2-314 and 2-715.

To bring the transaction within the scope of "refused to examine" in subsection (3)(a), it is not sufficient that the goods are available for inspection. There must in addition be an actual examination by the buyer or a demand by the seller that the buyer examine the goods fully. The seller's demand must place the buyer on notice that the buyer is assuming the risk of defects which the examination ought to reveal.

Application of the doctrine of "caveat emptor" in all cases where the buyer examines the goods regardless of statements made by the seller is, however, rejected by this Article. Thus, if the offer of examination is accompanied by words as to their merchantability or specific attributes and the buyer indicates clearly a reliance on those words rather than on the buyer's examination, they give rise to an "express" warranty. In these cases the question is one of fact as to whether a warranty of merchantability has been expressly incorporated in the agreement.

The particular buyer's skill and the normal method of examining goods in the circumstances determine what defects are excluded by the examination. A failure to notice defects which are obvious cannot excuse the buyer. However, an examination under circumstances which do not permit chemical or other testing of the goods would not exclude defects which could be ascertained only by testing. Nor can latent defects be excluded by a simple examination. A professional buyer examining a product in the buyer's field will be held to have assumed the risk as to all defects which a professional in the field ought to observe, while a nonprofessional buyer will be held to have assumed the risk only for the defects as a layperson might be expected to observe.

8. The situation in which the buyer gives precise and complete specifications to the seller is not explicitly covered in this section, but this is a frequent circumstance by which the implied warranties may be excluded. The warranty of fitness for a particular purpose would not normally arise since in this situation there is usually no reliance on the seller by the buyer. The warranty of merchantability in a

transaction of this type, however, must be considered in connection with the next section on the cumulation and conflict of warranties. Under paragraph (c) of that section in case of an inconsistency the implied warranty of merchantability is displaced by the express warranty that the goods will comply with the specifications. Thus, where the buyer gives detailed specifications as to the goods, neither of the implied warranties as to quality will normally apply to the transaction unless consistent with the specifications.

### **SECTION 2-318. THIRD PARTY BENEFICIARIES OF WARRANTIES EXPRESS OR IMPLIED.**

(1) In this section:

(a) "Immediate buyer" means a buyer that enters into a contract with the seller.

(b) "Remote purchaser" means a person that buys or leases goods from an immediate buyer or other person in the normal chain of distribution.

#### **Alternative A to subsection (2)**

(2) A seller's warranty whether express or implied extends to any natural person who is in the family or household of his buyer or who is a guest in his home if it is reasonable to expect that such person may use, consume or be affected by the goods and who is injured in person by breach of the warranty. A seller's warranty whether express or implied to an immediate buyer, a seller's remedial promise to an immediate buyer, or a seller's obligation to a remote purchaser under Section 2-313A or 2-313B extends to any natural person who is in the family or household of the immediate buyer or the remote purchaser or who is a guest in the home of either if it is reasonable to expect that the person may use, consume or be affected by the goods and who is injured in person by breach of the warranty, remedial promise or obligation. A seller may not exclude or limit the operation of this section.

#### **Alternative B to subsection (2)**

(2) A seller's warranty whether express or implied extends to any natural person who may reasonably be expected to use, consume or be affected by the goods and who is injured in person by breach of the warranty. A seller's warranty whether express or implied to an immediate buyer, a seller's remedial promise to an immediate buyer, or a seller's obligation to a remote purchaser under Section 2-313A or 2-313B extends to any natural person who may reasonably be expected to use, consume or be affected by the goods and who is injured in person by breach of the warranty, remedial promise or obligation. A seller may not exclude or limit the operation of this section.

### **Alternative C to subsection (2)**

(2) A seller's warranty whether express or implied extends to any person who may reasonably be expected to use, consume or be affected by the goods and who is injured by breach of the warranty. A seller's warranty whether express or implied to an immediate buyer, a seller's remedial promise to an immediate buyer, or a seller's obligation to a remote purchaser under Section 2-313A or 2-313B extends to any person that may reasonably be expected to use, consume or be affected by the goods and that is injured by breach of the warranty, remedial promise or obligation. A seller may not exclude or limit the operation of this section with respect to injury to the person of an individual to whom the warranty, remedial promise or obligation extends.

### **Proposed Comment**

1. This section retains original Article 2's alternative approaches but expands each alternative to cover obligations arising under Sections 2-313A and 2-313B and remedial promises.

2. The last sentence of each alternative to subsection (2) is not meant to suggest that a seller is precluded from excluding or disclaiming a warranty which might otherwise arise in connection with the sale provided the exclusion or modification is permitted by Section 2-316. Nor is it intended to suggest that the seller is precluded from limiting the remedies of the immediate buyer or remote purchaser in any manner provided in Sections 2-718 or 2-719. See also Section 2-313A(4) and Section 2-313B(4). To the extent that the contract of sale contains provisions under which warranties are excluded or modified, or remedies for breach are limited, the provisions are equally operative against beneficiaries of warranties under this section. What this last sentence forbids is exclusion of liability by the seller to the persons to whom the warranties, obligations and remedial promises accruing to the immediate buyer or remote purchaser would extend under this section.

The last sentence of Alternative C permits a seller to reduce its obligations to third-party beneficiaries to a level commensurate with that imposed on the seller under Alternative B - that is, to eliminate liability to persons that are not individuals and to eliminate liability for damages other than personal injury.

3. As used in this section, the term "remote purchaser" refers to the party to whom an obligation initially runs under Section 2-313A or 2-313B. It does not refer to any subsequent purchaser of the goods.

4. As applied to warranties and remedial promises arising under Sections 2-313, 2-314 and 2-315, the

purpose of this section is to give certain beneficiaries the benefit of the warranties and remedial promises which the immediate buyer received in the contract of sale, thereby freeing any beneficiaries from any technical rules as to "privity." It seeks to accomplish this purpose without any derogation of any right or remedy arising under the law of torts. Implicit in the section is that any beneficiary of a warranty may bring a direct action for breach of warranty against the seller whose warranty extends to the beneficiary.

Obligations and remedial promises under Sections 2-313A and 2-313B arise initially in a non-privity context but are extended under this section to the same extent as warranties and remedial promises running to a buyer in privity.

### **SECTION 2-319. F.O.B. AND F.A.S. TERMS RESERVED.**

(1) Unless otherwise agreed the term F.O.B. (which means "free on board") at a named place, even though used only in connection with the stated price, is a delivery term under which

(a) when the term is F.O.B. the place of shipment, the seller must at that place ship the goods in the manner provided in this Article (Section 2-504) and bear the expense and risk of putting them into the possession of the carrier; or

(b) when the term is F.O.B. the place of destination, the seller must at his own expense and risk transport the goods to that place and there tender delivery of them in the manner provided in this Article (Section 2-503);

(c) when under either (a) or (b) the term is also F.O.B. vessel, car or other vehicle, the seller must in addition at his own expense and risk load the goods on board. If the term is F.O.B. vessel the buyer must name the vessel and in an appropriate case the seller must comply with the provisions of this Article on the form of bill of lading (Section 2-323).

(2) Unless otherwise agreed the term F.A.S. vessel (which means "free alongside") at a named port, even though used only in connection with the stated price, is a delivery term under which the seller must

(a) at his own expense and risk deliver the goods alongside the vessel in the manner usual in that port or on a dock designated and provided by the buyer; and

(b) obtain and tender a receipt for the goods in exchange for which the carrier is under a duty to issue a bill of lading.

~~(3) Unless otherwise agreed in any case falling within subsection (1)(a) or (c) or subsection (2) the buyer must seasonably give any needed instructions for making delivery, including when the term is F.A.S. or F.O.B. the loading berth of the vessel and in an appropriate case its name and sailing date. The seller may treat the failure of needed instructions as a failure of cooperation under this Article (Section 2-311). He may also at his option move the goods in any reasonable manner preparatory to delivery or shipment.~~

~~(4) Under the term F.O.B. vessel or F.A.S. unless otherwise agreed the buyer must make payment against tender of the required documents and the seller may not tender nor the buyer demand delivery of the goods in substitution for the documents.~~

#### **Proposed Comment**

Sections 2-319 through 2-324 have been eliminated because they are inconsistent with modern commercial practices.

#### **SECTION 2-320. C.I.F. AND C. & F. TERMS RESERVED.**

(1) The term C.I.F. means that the price includes in a lump sum the cost of the goods and the insurance and freight to the named destination. The term C. & F. or C.F. means that the price so includes cost and freight to the named destination.

(2) Unless otherwise agreed and even though used only in connection with the stated price and destination, the term C.I.F. destination or its equivalent requires the seller at his own expense and risk to

(a) put the goods into the possession of a carrier at the port for shipment and obtain a negotiable bill or bills of lading covering the entire transportation to the named destination; and

(b) load the goods and obtain a receipt from the carrier (which may be contained in the bill of lading) showing that the freight has been paid or provided for; and

(c) obtain a policy or certificate of insurance, including any war risk insurance, of a kind and on terms then current at the port of shipment in the usual amount, in the currency of the contract, shown to cover the same goods covered by the bill of lading and providing for payment of loss to the order of the buyer or for the account of whom it may concern; but the seller may add to the price the amount of the premium for any such war risk insurance; and

(d) prepare an invoice of the goods and procure any other documents required to effect shipment or to comply with the contract; and

~~(e) forward and tender with commercial promptness all the documents in due form and with any indorsement necessary to perfect the buyer's rights.~~

~~(3) Unless otherwise agreed the term C. & F. or its equivalent has the same effect and imposes upon the seller the same obligations and risks as a C.I.F. term except the obligation as to insurance.~~

~~(4) Under the term C.I.F. or C. & F. unless otherwise agreed the buyer must make payment against tender of the required documents and the seller may not tender nor the buyer demand delivery of the goods in substitution for the documents.~~

#### **Proposed Comment**

Sections 2-319 through 2-324 have been eliminated because they are inconsistent with modern commercial practices.

#### **SECTION 2-321. C.I.F. OR C. & F.: "NET LANDED WEIGHTS"; "PAYMENT ON ARRIVAL"; WARRANTY OF CONDITION ON ARRIVAL RESERVED.**

Under a contract containing a term C.I.F. or C. & F.

(1) Where the price is based on or is to be adjusted according to "net landed weights", "delivered weights", "out turn" quantity or quality or the like, unless otherwise agreed the seller must reasonably estimate the price. The payment due on tender of the documents called for by the contract is the amount so estimated, but after final adjustment of the price a settlement must be made with commercial promptness.

(2) An agreement described in subsection (1) or any warranty of quality or condition of the goods on arrival places upon the seller the risk of ordinary deterioration, shrinkage and the like in transportation but has no effect on the place or time of identification to the contract for sale or delivery or on the passing of the risk of loss.

(3) Unless otherwise agreed where the contract provides for payment on or after arrival of the goods the seller must before payment allow such preliminary inspection as is feasible; but if the goods are lost delivery of the documents and payment are due when the goods should have arrived.

#### **Proposed Comment**

Sections 2-319 through 2-324 have been eliminated because they are inconsistent with modern commercial practices.

**SECTION 2-322. ~~DELIVERY "EX-SHIP" RESERVED.~~**

~~(1) Unless otherwise agreed a term for delivery of goods "ex-ship" (which means from the carrying vessel) or in equivalent language is not restricted to a particular ship and requires delivery from a ship which has reached a place at the named port of destination where goods of the kind are usually discharged.~~

~~(2) Under such a term unless otherwise agreed~~

~~(a) the seller must discharge all liens arising out of the carriage and furnish the buyer with a direction which puts the carrier under a duty to deliver the goods; and~~

~~(b) the risk of loss does not pass to the buyer until the goods leave the ship's tackle or are otherwise properly unloaded.~~

**Proposed Comment**

Sections 2-319 through 2-324 have been eliminated because they are inconsistent with modern commercial practices

**SECTION 2-323. ~~FORM OF BILL OF LADING REQUIRED IN OVERSEAS SHIPMENT; "OVERSEAS" RESERVED.~~**

~~(1) Where the contract contemplates overseas shipment and contains a term C.I.F. or C. & F. or F.O.B. vessel, the seller unless otherwise agreed must obtain a negotiable bill of lading stating that the goods have been loaded in board or, in the case of a term C.I.F. or C. & F., received for shipment.~~

~~(2) Where in a case within subsection (1) a bill of lading has been issued in a set of parts, unless otherwise agreed if the documents are not to be sent from abroad the buyer may demand tender of the full set; otherwise only one part of the bill of lading need be tendered. Even if the agreement expressly requires a full set~~

~~(a) due tender of a single part is acceptable within the provisions of this Article on cure of improper delivery (subsection (1) of Section 2-508); and~~

~~(b) even though the full set is demanded, if the documents are sent from abroad the person tendering an incomplete set may nevertheless require payment upon furnishing an indemnity which the buyer in good faith deems adequate.~~

~~(3) A shipment by water or by air or a contract contemplating such shipment is "overseas" insofar as by usage of trade or agreement it is subject to the commercial, financing or shipping practices characteristic of international deep water commerce.~~

**Proposed Comment**

Sections 2-319 through 2-324 have been eliminated because they are inconsistent with modern commercial practices.

**SECTION 2-324. ~~"NO ARRIVAL, NO SALE" TERM RESERVED.~~**

~~Under a term "no arrival, no sale" or terms of like meaning, unless otherwise agreed,~~

~~(a) the seller must properly ship conforming goods and if they arrive by any means he must tender them on arrival but he assumes no obligation that the goods will arrive unless he has caused the non-arrival; and~~

~~(b) where without fault of the seller the goods are in part lost or have so deteriorated as no longer to conform to the contract or arrive after the contract time, the buyer may proceed as if there had been casualty to identified goods (Section 2-613).~~

**Proposed Comment**

Sections 2-319 through 2-324 have been eliminated because they are inconsistent with modern commercial practices.

**SECTION 2-325. ~~"LETTER OF CREDIT" TERM; "CONFIRMED CREDIT" FAILURE TO PAY BY AGREED LETTER OF CREDIT.~~**

(1) ~~Failure of the buyer seasonably to furnish an agreed letter of credit is a breach of the contract for sale.~~

(2) ~~The delivery to seller of a proper letter of credit suspends the buyer's obligation to pay. If the letter of credit is dishonored, the seller may on reasonable notification to the buyer require payment directly from him.~~

(3) ~~Unless otherwise agreed the term "letter of credit" or "banker's credit" in a contract for sale means an irrevocable credit issued by a financing agency of good repute and, where the shipment is overseas, of good international repute. The term "confirmed credit" means that the credit must also carry the direct obligation of such an agency which does business in the seller's financial market.~~

If the parties agree that the primary method of payment will be by letter of credit, the following rules apply:

(a) The buyer's obligation to pay is suspended by seasonable delivery to the seller of a letter of credit issued or confirmed by a financing agency of good repute in which the issuer and any confirmer undertake to pay against presentation of documents that evidence delivery of the goods.

(b) Failure of a party seasonably to furnish a letter of credit as agreed is a breach of the contract for sale.

(c) If the letter of credit is dishonored or repudiated, the seller on reasonable notification may require payment directly from the buyer.

#### **Proposed Comment**

This section has been amended to conform to revised Article 5.

#### **SECTION 2-326. SALE ON APPROVAL AND SALE OR RETURN; ~~CONSIGNMENT SALES AND RIGHTS OF CREDITORS.~~**

(1) Unless otherwise agreed, if delivered goods may be returned by the buyer even though they conform to the contract, the transaction is

(a) a "sale on approval" if the goods are delivered primarily for use, and

(b) a "sale or return" if the goods are delivered primarily for resale.

(2) ~~Except as provided in subsection (3),~~ goods Goods held on approval are not subject to the claims of the buyer's creditors until acceptance; goods held on sale or return are subject to such claims while in the

buyer's possession.

(3) ~~Where goods are delivered to a person for sale and such person maintains a place of business at which he deals in goods of the kind involved, under a name other than the name of the person making delivery, then with respect to claims of creditors of the person conducting the business the goods are deemed to be on sale or return. The provisions of this subsection are applicable even though an agreement purports to reserve title to the person making delivery until payment or resale or uses such words as "on consignment" or "on memorandum". However, this subsection is not applicable if the person making delivery~~

(a) ~~complies with an applicable law providing for a consignor's interest or the like to be evidenced by a sign, or~~

(b) ~~establishes that the person conducting the business is generally known by his creditors to be substantially engaged in selling the goods of others, or~~

(c) ~~complies with the filing provisions of the Article on Secured Transactions (Article 9).~~

(4) (3) Any "or return" term of a contract for sale is to be treated as a separate contract for sale within the statute of frauds section of this Article (Section 2-201) and as contradicting the sale aspect of the contract within the provisions of this Article on parol or extrinsic evidence (Section 2-202).

#### **Proposed Comment**

This section has been amended to conform to revised Article 9.

#### **SECTION 2-328. SALE BY AUCTION.**

(1) In a sale by auction if goods are put up in lots each lot is the subject of a separate sale.

(2) A sale by auction is complete when the auctioneer so announces by the fall of the hammer or in other customary manner. Where a bid is made ~~while the hammer is falling in acceptance of~~ during the process of completing the sale but before a prior bid is accepted the auctioneer ~~may in his~~ has discretion to reopen the bidding or to declare the goods sold under the prior bid ~~on which the hammer was falling.~~

(3) ~~Such a sale is with reserve unless the goods are in explicit terms put up without reserve. In an auction with reserve the auctioneer may withdraw the goods at any time until he announces completion of the sale. In an auction without reserve, after the auctioneer calls for bids on an article or lot, that article or~~

~~lot cannot be withdrawn unless no bid is made within a reasonable time. In either case a bidder may retract his bid until the auctioneer's announcement of completion of the sale, but a bidder's retraction does not revive any previous bid. A sale by auction is subject to the seller's right to withdraw the goods unless at the time the goods are put up or during the course of the auction it is announced in express terms that the right to withdraw the goods is not reserved. In an auction in which the right to withdraw the goods is reserved, the auctioneer may withdraw the goods at any time until completion of the sale is announced by the auctioneer. In an auction in which the right to withdraw the goods is not reserved, after the auctioneer calls for bids on an article or lot, the article or lot cannot be withdrawn unless no bid is made within a reasonable time. In either case a bidder may retract a bid until the auctioneer's announcement of completion of the sale, but a bidder's retraction does not revive any previous bid.~~

(4) If the auctioneer knowingly receives a bid on the seller's behalf or the seller makes or procures such a bid, and notice has not been given that liberty for such bidding is reserved, the buyer may at his the buyer's option avoid the sale or take the goods at the price of the last good faith bid prior to the completion of the sale. This subsection shall not apply to any bid at a ~~forced sale~~ an auction required by law.

#### **Proposed Comment**

This section has been amended to use language that is common among auctioneers. Specifically, "process of completing the sale" is used rather than "hammer falling" (subsection (2)); "right to withdraw the goods" is used rather than "with reserve" (subsection (3)).

### **PART 4**

#### **TITLE, CREDITORS AND GOOD FAITH PURCHASERS**

##### **SECTION 2-401. PASSING OF TITLE; RESERVATION FOR SECURITY; LIMITED APPLICATION OF THIS SECTION.**

Each provision of this Article with regard to the rights, obligations and remedies of the seller, the buyer, purchasers or other third parties applies irrespective of title to the goods except where the provision refers to such title. Insofar as situations are not covered by the other provisions of this Article and matters concerning title become material the following rules apply:

(1) Title to goods cannot pass under a contract for sale prior to their identification to the contract (Section 2-501), and unless otherwise explicitly agreed the buyer acquires by their identification a special property as limited by this Act. Any retention or reservation by the seller of the title (property) in goods shipped or delivered to the buyer is limited in effect to a reservation of a security interest. Subject

to these provisions and to the provisions of the Article on Secured Transactions (Article 9), title to goods passes from the seller to the buyer in any manner and on any conditions explicitly agreed on by the parties.

(2) Unless otherwise explicitly agreed title passes to the buyer at the time and place at which the seller completes his performance with reference to the physical delivery of the goods, despite any reservation of a security interest and even though a document of title is to be delivered at a different time or place; and in particular and despite any reservation of a security interest by the bill of lading

(a) if the contract requires or authorizes the seller to send the goods to the buyer but does not require ~~him~~ the seller to deliver them at destination, title passes to the buyer at the time and place of shipment; but

(b) if the contract requires delivery at destination, title passes on tender there.

(3) Unless otherwise explicitly agreed where delivery is to be made without moving the goods,

(a) if the seller is to deliver a document of title, title passes at the time when and the place where ~~he~~ the seller delivers such documents; or

(b) if the goods are at the time of contracting already identified and no documents are to be delivered, title passes at the time and place of contracting.

(4) A rejection or other refusal by the buyer to receive or retain the goods, whether or not justified, or a justified revocation of acceptance reverts title to the goods in the seller. Such reversion occurs by operation of law and is not a "sale".

#### **Proposed Comment**

The word "physical" been deleted in subsection (2) because the term "delivery" is now defined in section 2-103(1)(f) as "the voluntary transfer of physical possession or control of goods."

##### **SECTION 2-402. RIGHTS OF SELLER'S CREDITORS AGAINST SOLD GOODS.**

(1) Except as provided in subsections (2) and (3), rights of unsecured creditors of the seller with respect to goods which have been identified to a contract for sale are subject to the buyer's rights to recover the goods under this Article (Sections 2-502 and 2-716).

(2) A creditor of the seller may treat a sale or an identification of goods to a contract for sale as void if as

against ~~him~~ the creditor a retention of possession by the seller is fraudulent under any rule of law of the state where the goods are situated, except that retention of possession in good faith and current course of trade by a merchant-seller for a commercially reasonable time after a sale or identification is not fraudulent.

(3) ~~Nothing~~ Except as provided in Section 2-403(2), nothing in this Article shall be deemed to impair the rights of creditors of the seller

(a) under the provisions of the Article on Secured Transactions (Article 9); or

(b) where identification to the contract or delivery is made not in current course of trade but in satisfaction of or as security for a pre-existing claim for money, security or the like and is made under circumstances which under any rule of law of the state where the goods are situated would apart from this Article constitute the transaction a fraudulent transfer or voidable preference.

#### **Proposed Comment**

The introductory phrase in subsection (3) has been added because a change in Section 2-403(2) (required for conformity with revised Article 9) can cause impairment of the rights of a secured party.

### **SECTION 2-403. POWER TO TRANSFER; GOOD FAITH PURCHASE OF GOODS; "ENTRUSTING".**

(1) A purchaser of goods acquires all title which ~~his~~ the purchaser's transferor had or had power to transfer except that a purchaser of a limited interest acquires rights only to the extent of the interest purchased. A person with voidable title has power to transfer a good title to a good faith purchaser for value. When goods have been delivered under a transaction of purchase the purchaser has such power even though

(a) the transferor was deceived as to the identity of the purchaser, or

(b) the delivery was in exchange for a check which is later dishonored, or

(c) it was agreed that the transaction was to be a "cash sale", or

(d) the delivery was procured through criminal fraud ~~punishable as larcenous under the criminal law.~~

(2) Any entrusting ~~of possession~~ of goods to a merchant ~~who~~ that deals in goods of that kind gives ~~him~~

the merchant power to transfer all rights of the entruster all of the entruster's rights to the goods and to transfer the goods free of any interest of the entruster to a buyer in ordinary course of business.

(3) "Entrusting" includes any delivery and any acquiescence in retention of possession regardless of any condition expressed between the parties to the delivery or acquiescence and regardless of whether the procurement of the entrusting or the possessor's disposition of the goods have been such as to be ~~larcenous~~ punishable under the criminal law.

[*Legislative Note: If a state adopts the repealer of Article 6--Bulk Transfers (Alternative A), subsection (4) should read as follows:*]

(4) The rights of other purchasers of goods and of lien creditors are governed by the Articles on Secured Transactions (Article 9) and Documents of Title (Article 7).

[*Legislative Note: If a state adopts revised Article 6--Bulk Sales (Alternative B), subsection (4) should read as follows:*]

(4) The rights of other purchasers of goods and of lien creditors are governed by the Articles on Secured Transactions (Article 9), Bulk Sales (Article 6) and Documents of Title (Article 7).

#### **Proposed Comment**

1. References to "larceny" have been replaced in subsections (1) and (3) by more general language referring to "criminal fraud" (subsection (1)) and conduct "punishable under the criminal law" (subsection (3)).

2. Subsection (2) has been amended to conform with revised Article 9. See Section 9-315(a).

## **PART 5**

### **PERFORMANCE**

## **SECTION 2-501. INSURABLE INTEREST IN GOODS; MANNER OF IDENTIFICATION OF GOODS.**

(1) The buyer obtains a special property and an insurable interest in goods by identification of existing goods as goods to which the contract refers even though the goods so identified are non-conforming and he the buyer has an option to return or reject them. Such identification can be made at any time and in any manner explicitly agreed to by the parties. In the absence of explicit agreement identification occurs

(a) when the contract is made if it is for the sale of goods already existing and identified;

(b) if the contract is for the sale of future goods other than those described in paragraph (c), when goods are shipped, marked or otherwise designated by the seller as goods to which the contract refers;

(c) when the crops are planted or otherwise become growing crops or the young are conceived if the contract is for the sale of unborn young to be born within twelve months after contracting or for the sale of crops to be harvested within twelve months or the next normal harvest season after contracting whichever is longer.

(2) The seller retains an insurable interest in goods so long as title to or any security interest in the goods remains in ~~him~~ the seller and where the identification is by the seller alone ~~he~~ the seller may until default or insolvency or notification to the buyer that the identification is final substitute other goods for those identified.

(3) Nothing in this section impairs any insurable interest recognized under any other statute or rule of law.

## **SECTION 2-502. BUYER'S RIGHT TO GOODS ON SELLER'S INSOLVENCY.**

(1) Subject to ~~subsection (2)~~ subsections (2) and (3) and even though the goods have not been shipped a buyer ~~who~~ that has paid a part or all of the price of goods in which ~~he~~ the buyer has a special property under the provisions of the immediately preceding section may on making and keeping good a tender of any unpaid portion of their price recover them from the seller ~~if the seller becomes insolvent within ten days after receipt of the first installment on their price. if:~~

(a) in the case of goods bought by a consumer, the seller repudiates or fails to deliver as required by the contract; or

(b) in all cases, the seller becomes insolvent within ten days after receipt of the first installment on their price.

(2) The buyer's right to recover the goods under subsection (1) vests upon acquisition of a special property, even if the seller had not then repudiated or failed to deliver.

(2) (3) If the identification creating ~~his~~ the special property has been made by the buyer ~~he,~~ the buyer acquires the right to recover the goods only if they conform to the contract for sale.

### **Proposed Comment**

Subsection (1)(a) and subsection (2) are new. With one exception, the amendments are consistent with a conforming amendment approved as part of the revision of Article 9. The exception is that the conforming amendment limits the vesting rule in subsection (2) to cases governed by subsection (1)(a), whereas the vesting rule in this draft applies to all cases within subsection (1).

## **SECTION 2-503. MANNER OF SELLER'S TENDER OF DELIVERY.**

(1) Tender of delivery requires that the seller put and hold conforming goods at the buyer's disposition and give the buyer any notification reasonably necessary to enable ~~him~~ the buyer to take delivery. The manner, time and place for tender are determined by the agreement and this Article, and in particular

(a) tender must be at a reasonable hour, and if it is of goods they must be kept available for the period reasonably necessary to enable the buyer to take possession; but

(b) unless otherwise agreed the buyer must furnish facilities reasonably suited to the receipt of the goods.

(2) Where the case is within the next section respecting shipment tender requires that the seller comply with its provisions.

(3) Where the seller is required to deliver at a particular destination tender requires that ~~he~~ the seller comply with subsection (1) and also in any appropriate case tender documents as described in subsections (4) and (5) of this section.

(4) Where goods are in the possession of a bailee and are to be delivered without being moved

(a) tender requires that the seller either tender a negotiable document of title covering such goods or procure acknowledgment by the bailee to the buyer of the buyer's right to possession of the goods; but

(b) tender to the buyer of a non-negotiable document of title or of a ~~written direction to a record~~ directing the bailee to deliver is sufficient tender unless the buyer seasonably objects, and except as

otherwise provided in Article 9 receipt by the bailee of notification of the buyer's rights fixes those rights as against the bailee and all third persons; but risk of loss of the goods and of any failure by the bailee to honor the non-negotiable document of title or to obey the direction remains on the seller until the buyer has had a reasonable time to present the document or direction, and a refusal by the bailee to honor the document or to obey the direction defeats the tender.

(5) Where the contract requires the seller to deliver documents

(a) ~~he the seller~~ must tender all such documents in correct form, ~~except as provided in this Article with respect to bills of lading in a set (subsection (2) of Section 2-323); and~~

(b) tender through customary banking channels is sufficient and dishonor of a draft accompanying the documents constitutes non-acceptance or rejection.

#### **Proposed Comment**

1. Subsection (4)(a) clarifies that the bailee's acknowledgment must be made to the buyer. *See Jason's Foods, Inc. v. Peter Eckrick & Sons, Inc.*, 774 F.2d 214 (7th Cir. 1985). There is a similar amendment to Section 2-509(2)(b).

2. Under subsection (4)(b), receipt by the bailee of notification of a buyer's rights fixes those rights as against the bailee and third parties except as otherwise provided in Article 9. The exception for Article 9 conforms with revised Article 9.

3. The cross-reference in subsection (5)(a) has been deleted because Section 2-323 no longer exists. All documents, including bills in a set, must be in "correct form," meaning the form required by the contract.

#### **SECTION 2-504. SHIPMENT BY SELLER.**

Where the seller is required or authorized to send the goods to the buyer and the contract does not require ~~him~~ the seller to deliver them at a particular destination, then unless otherwise agreed ~~he~~ the seller must

(a) ~~put the conforming~~ goods in the possession of ~~such~~ a carrier and make ~~such~~ a proper contract for their transportation, ~~as may be reasonable~~ having regard to the nature of the goods and other

circumstances of the case; and

(b) obtain and promptly deliver or tender in due form any document necessary to enable the buyer to obtain possession of the goods or otherwise required by the agreement or by usage of trade; and

(c) promptly notify the buyer of the shipment.

Failure to notify the buyer under paragraph (c) or to make a proper contract under paragraph (a) is a ground for rejection only if material delay or loss ensues.

#### **Proposed Comment**

The addition of "conforming" in paragraph (a) clarifies the relationship between this section and Section 2-601.

#### **SECTION 2-505. SELLER'S SHIPMENT UNDER RESERVATION.**

(1) Where the seller has identified goods to the contract by or before shipment:

(a) ~~his~~ the seller's procurement of a negotiable bill of lading to ~~his~~ the seller's own order or otherwise reserves in ~~him~~ the seller a security interest in the goods. ~~His~~ The seller's procurement of the bill to the order of a financing agency or of the buyer indicates in addition only the seller's expectation of transferring that interest to the person named.

(b) a non-negotiable bill of lading to ~~himself~~ the seller or ~~his~~ the seller's nominee reserves possession of the goods as security but except in a case of ~~conditional delivery~~ when a seller has a right to reclaim the goods under (subsection (2) of Section 2-507) a non-negotiable bill of lading naming the buyer as consignee reserves no security interest even though the seller retains possession of the bill of lading.

(2) When shipment by the seller with reservation of a security interest is in violation of the contract for sale, it constitutes an improper contract for transportation within the preceding section but impairs neither the rights given to the buyer by shipment and identification of the goods to the contract nor the seller's powers as a holder of a negotiable document.

#### **Proposed Comment**

The change from "conditional delivery" to "right to reclaim the goods" in subsection (1)(b) conforms to amended Section 2-507, where the seller's right to recover the goods following dishonor of a check in a cash-sale transaction is now stated in terms of a right of reclamation.

## SECTION 2-506. RIGHTS OF FINANCING AGENCY.

(1) ~~A Except as otherwise provided in Article 5, a financing agency by paying or purchasing for value a draft which relates to a shipment of goods acquires to the extent of the payment or purchase and in addition to its own rights under the draft and any document of title securing it any rights of the shipper in the goods including the right to stop delivery and the shipper's right to have the draft honored by the buyer.~~

(2) The right to reimbursement of a financing agency which has in good faith honored or purchased the draft under commitment to or authority from the buyer is not impaired by subsequent discovery of defects with reference to any relevant document which was apparently regular on its face.

### Proposed Comment

Subsection (1) has been amended to provide that Article 5 governs in the event of a conflict.

## SECTION 2-507. EFFECT OF SELLER'S TENDER; DELIVERY ON CONDITION.

(1) Tender of delivery is a condition to the buyer's duty to accept the goods and, unless otherwise agreed, to his the buyer's duty to pay for them. Tender entitles the seller to acceptance of the goods and to payment according to the contract.

(2) Where payment is due and demanded on the delivery to the buyer of goods or documents of title, ~~his right as against the seller to retain or dispose of them is conditional upon his making the payment due the seller may reclaim the goods delivered upon a demand made within a reasonable time after the seller discovers or should have discovered that payment was not made.~~

(3) The seller's right to reclaim under subsection (2) is subject to the rights of a buyer in ordinary course or other good-faith purchaser for value under this Article (Section 2-403).

### Proposed Comment

Subsection (2) has been amended to state directly that the seller's right to recover the goods from the buyer in a cash-sale transaction is a right of reclamation. The phrase "due and demanded" refers to the situation where the seller takes a check that is later dishonored. See Section 2-511. This change, and the addition of subsection (3), make the seller's rights parallel in credit-sale and cash-sale transactions. See Section 2-702.

## SECTION 2-508. CURE BY SELLER OF IMPROPER TENDER OR DELIVERY; REPLACEMENT.

~~(1) Where any tender or delivery by the seller is rejected because non-conforming and the time for performance has not yet expired, the seller may seasonably notify the buyer of his intention to cure and may then within the contract time make a conforming delivery.~~

~~(2) Where the buyer rejects a non-conforming tender which the seller had reasonable grounds to believe would be acceptable with or without money allowance the seller may if he seasonably notifies the buyer have a further reasonable time to substitute a conforming tender.~~

(1) Where the buyer rejects goods or a tender of delivery under Section 2-601 or 2-612 or except in a consumer contract justifiably revokes acceptance under Section 2-608(1)(b) and the agreed time for performance has not expired, a seller that has performed in good faith, upon seasonable notice to the buyer and at the seller's own expense, may cure the breach of contract by making a conforming tender of delivery within the agreed time. The seller shall compensate the buyer for all of the buyer's reasonable expenses caused by the seller's breach of contract and subsequent cure.

(2) Where the buyer rejects goods or a tender of delivery under Section 2-601 or 2-612 or except in a consumer contract justifiably revokes acceptance under Section 2-608(1)(b) and the agreed time for performance has expired, a seller that has performed in good faith, upon seasonable notice to the buyer and at the seller's own expense, may cure the breach of contract, if the cure is appropriate and timely under the circumstances, by making a tender of conforming goods. The seller shall compensate the buyer for all of the buyer's reasonable expenses caused by the seller's breach of contract and subsequent cure.

### Proposed Comment

1. Subsection (1) permits a seller that has made a nonconforming tender in any case to make a conforming tender within the contract time upon seasonable notification to the buyer. It presumes that the buyer has rightfully rejected or justifiably revoked acceptance under Section 2-608(1)(b) through timely notification to the seller and has complied with any particularization requirements imposed by Section 2-605(1). The subsection applies even where the seller has taken back the nonconforming goods and refunded the purchase price. The seller may still make a good tender within the contract period. The closer, however, it is to the contract date, the greater is the necessity for extreme promptness on the seller's part in notifying of the intention to cure, if the notification is to be "seasonable" under this subsection.

The rule of this subsection, moreover, is qualified by its underlying reasons. Thus if, after contracting for June delivery, a buyer later makes known to the seller a need for shipment early in the month and the seller ships accordingly, the "contract time" has been cut down by the supervening modification and the time for cure of tender must be referred to this modified time term.

2. Cure after a justifiable revocation of acceptance is not available as a matter of right in a consumer contract. Further, even in a nonconsumer contract no cure is available if the revocation is predicated on Section 2-608(1)(a). If the buyer is revoking because of a known defect that the seller has not been willing or able to cure, there is no justification for giving the seller a second chance to cure.

3. Subsection (2) expands the seller's right to cure after the time for performance has expired. As under subsection (1), the buyer's rightful rejection or in a nonconsumer contract justifiable revocation of acceptance under Section 2-608(1)(b) trigger the seller's right to cure. Original Section 2-508(2) was directed toward preventing surprise rejections by requiring the seller to have "reasonable grounds to believe" the nonconforming tender was acceptable. Although this test has been abandoned, the requirement that the initial tender be made in good faith prevents a seller from deliberately tendering goods that it knows the buyer cannot use in order to save its contract and then, upon rejection, insisting on a second bite at the apple. The good faith standard applies under both subsection (1) and subsection (2).

4. The seller's cure under both subsection (1) and subsection (2) must be of conforming goods. Conforming goods includes not only conformity to the contracted-for quality but also as to quantity or assortment or other similar obligations under the contract. Since the time for performance has expired in a case governed by subsection (2), however, the seller's tender of conforming goods required to effect a cure under this section could not conform to the contracted time for performance. Thus, subsection (1) requires that cure be tendered "within the agreed time" while subsection (2) requires that the tender be "appropriate and timely under the circumstances."

The requirement that the cure be "appropriate and timely under the circumstances" provides important protection for the buyer. If the buyer is acquiring inventory on a just-in-time basis and needs to procure substitute goods from another supplier in order to keep the buyer's process moving, the cure would not be timely. If the seller knows from the circumstances that strict compliance with the contract obligations is expected, the seller's cure would not be appropriate. If the seller attempts to cure by repair, the cure would not be appropriate if it resulted in goods that did not conform in every respect to the requirements of the contract. The standard for quality on the second tender is still governed by Section 2-601. Whether a cure is appropriate and timely should be tested based upon the circumstances and needs of the

buyer. Seasonable notice to the buyer and timely cure incorporate the idea that the notice and offered cure would be untimely if the buyer has reasonably changed its position in good faith reliance on the nonconforming tender.

5. Cure is at the seller's expense, and the seller is obligated to compensate the buyer for all the buyer's reasonable expenses caused by the breach and the cure. The term "reasonable expenses" is not limited to expenses that would qualify as incidental damages.

#### **SECTION 2-509. RISK OF LOSS IN THE ABSENCE OF BREACH.**

(1) Where the contract requires or authorizes the seller to ship the goods by carrier

(a) if it does not require ~~him~~ the seller to deliver them at a particular destination, the risk of loss passes to the buyer when the goods are ~~duly~~ delivered to the carrier even though the shipment is under reservation (Section 2-505); but

(b) if it does require ~~him~~ the seller to deliver them at a particular destination and the goods are there ~~duly~~ tendered while in the possession of the carrier, the risk of loss passes to the buyer when the goods are there ~~duly~~ so tendered as to enable the buyer to take delivery.

(2) Where the goods are held by a bailee to be delivered without being moved, the risk of loss passes to the buyer

(a) on ~~his~~ the buyer's receipt of a negotiable document of title covering the goods; or

(b) on acknowledgment by the bailee to the buyer of the buyer's right to possession of the goods; or

(c) after ~~his~~ the buyer's receipt of a non-negotiable document of title or other ~~written~~ direction to deliver in a record, as provided in subsection (4)(b) of Section 2-503.

(3) In any case not within subsection (1) or (2), the risk of loss passes to the buyer on ~~his~~ the buyer's receipt of the goods ~~if the seller is a merchant; otherwise the risk passes to the buyer on tender of delivery.~~

(4) The provisions of this section are subject to contrary agreement of the parties and to the provisions of this Article on sale on approval (Section 2-327) and on effect of breach on risk of loss (Section 2-510).

### **Proposed Comment**

1. The word "duly" has been deleted in subsections (1)(a) and (1)(b) because it has caused confusion. In a shipment contract, the risk of loss shifts to the buyer when the goods are delivered to the carrier as required by Section 2-504; in a destination contract, the risk of loss shifts when the goods are tendered to the buyer as required by Section 2-503(3).

2. Subsection (3) has been simplified by eliminating the distinction between merchant and non-merchant sellers. In a case not governed by subsection (1) or subsection (2) and not subject to a contrary result under subsection (4), the risk of loss passes to the buyer upon the buyer's receipt of the goods.

### **SECTION 2-510. EFFECT OF BREACH ON RISK OF LOSS.**

(1) Where a tender or delivery of goods so fails to conform to the contract as to give a right of rejection the risk of their loss remains on the seller until cure or acceptance.

(2) Where the buyer rightfully revokes acceptance ~~he~~ the buyer may to the extent of any deficiency in ~~his~~ the buyer's effective insurance coverage treat the risk of loss as having rested on the seller from the beginning.

(3) Where the buyer as to conforming goods already identified to the contract for sale repudiates or is otherwise in breach before risk of their loss has passed to ~~him~~ the buyer, the seller may to the extent of any deficiency in ~~his~~ the seller's effective insurance coverage treat the risk of loss as resting on the buyer for a commercially reasonable time.

### **SECTION 2-512. PAYMENT BY BUYER BEFORE INSPECTION.**

(1) Where the contract requires payment before inspection non-conformity of the goods does not excuse the buyer from so making payment unless

(a) the non-conformity appears without inspection; or

(b) despite tender of the required documents the circumstances would justify injunction against honor under this Act (Section 5-109(b)).

(2) Payment pursuant to subsection (1) does not constitute an acceptance of goods or impair the buyer's right to inspect or any of ~~his~~ the buyer's remedies.

### **SECTION 2-513. BUYER'S RIGHT TO INSPECTION OF GOODS.**

(1) Unless otherwise agreed and subject to subsection (3), where goods are tendered or delivered or identified to the contract for sale, the buyer has a right before payment or acceptance to inspect them at any reasonable place and time and in any reasonable manner. When the seller is required or authorized to send the goods to the buyer, the inspection may be after their arrival.

(2) Expenses of inspection must be borne by the buyer but may be recovered from the seller if the goods do not conform and are rejected.

(3) Unless otherwise agreed ~~and subject to the provisions of this Article on C.I.F. contracts (subsection (3) of Section 2-321)~~, the buyer is not entitled to inspect the goods before payment of the price when the contract provides

(a) for delivery "C.O.D." ~~or on other like terms~~ on terms that under applicable course of performance, course of dealing, or usage of trade are interpreted to preclude inspection before payment; or

(b) for payment against documents of title, except where such payment is due only after the goods are to become available for inspection.

(4) A place ~~or method~~ , method or standard of inspection fixed by the parties is presumed to be exclusive but unless otherwise expressly agreed it does not postpone identification or shift the place for delivery or for passing the risk of loss. If compliance becomes impossible, inspection shall be as provided in this section unless the place ~~or method~~ , method or standard fixed was clearly intended as an indispensable condition failure of which avoids the contract.

### **Proposed Comment**

1. The cross-reference in subsection (3) has been deleted because Section 2-321 no longer exists. The reference to "C.O.D." in subsection (3)(a) has been deleted for the same reason that Sections 2-319 through 2-324 have been deleted - terms that amount to commercial shorthand will no longer be included in the text of Article 2.

2. Subsection (4) has been amended to provide that, in addition to the place and method of inspection, the parties may agree on the standard of inspection. The change responds to the large number of cases

where there is a dispute about the appropriate standard of inspection. The word "compliance" in the second sentence of subsection (4) includes compliance with an agreed standard of inspection.

#### **SECTION 2-514. WHEN DOCUMENTS DELIVERABLE ON ACCEPTANCE; WHEN ON PAYMENT.**

Unless otherwise agreed and except as otherwise provided in Article 5, documents against which a draft is drawn are to be delivered to the drawee on acceptance of the draft if it is payable more than three days after presentment; otherwise, only on payment.

##### **Proposed Comment**

The exception for contrary provisions in Article 5 is new and makes this section consistent with Section 4-503, which also states that it is subject to Article 5. The specific question is what constitutes a time draft as opposed to a sight draft. Under Article 5, because an issuer may have up to seven days to determine compliance of documents (Section 5-108), the delay beyond three days does not necessarily indicate that the draft should be treated as a time draft.

### **PART 6**

#### **BREACH, REPUDIATION AND EXCUSE**

##### **SECTION 2-601. BUYER'S RIGHTS ON IMPROPER DELIVERY.**

Subject to the provisions of this Article on breach in installment contracts (Section 2-612) and on shipment by seller (Section 2-504), and unless otherwise agreed under the sections on contractual limitations of remedy (Sections 2-718 and 2-719), if the goods or the tender of delivery fail in any respect to conform to the contract, the buyer may

- (a) reject the whole; or
- (b) accept the whole; or

- (c) accept any commercial unit or units and reject the rest.

##### **Proposed Comment**

The cross-reference to Section 2-504, pursuant to which a seller's failure properly to notify a buyer or to make a proper contract of carriage is a ground for rejection only if material delay or loss ensues, has been included for accuracy.

##### **SECTION 2-602. MANNER AND EFFECT OF RIGHTFUL REJECTION.**

- (1) Rejection of goods must be within a reasonable time after their delivery or tender. It is ineffective unless the buyer seasonably notifies the seller.
- (2) Subject to the provisions of the two following sections on rejected goods (Sections 2-603 and 2-604) and to Section 2-608(4),
  - (a) after rejection any exercise of ownership by the buyer with respect to any commercial unit is wrongful as against the seller; and
  - (b) if the buyer has before rejection taken physical possession of goods in which ~~he~~ the buyer does not have a security interest under the provisions of this Article (subsection (3) of Section 2-711), ~~he~~ the buyer is under a duty after rejection to hold them with reasonable care at the seller's disposition for a time sufficient to permit the seller to remove them; but
  - (c) the buyer has no further obligations with regard to goods rightfully rejected.
- (3) The seller's rights with respect to goods wrongfully rejected are governed by the provisions of this Article on Seller's remedies in general (Section 2-703).

##### **Proposed Comment**

1. Elimination of the word "rightful" in the title makes it clear that a buyer can effectively reject goods even though the rejection is wrongful and constitutes a breach. See Section 2-703(1). The word "rightful" has also been deleted from the titles to Section 2-603 and 2-604. See Proposed Comments to those sections.

2. Subsection (2) has been amended to make it subject to Section 2-608(4), which deals with the

problem of post-rejection or post-revocation use of the goods. See Proposed Comment to Section 2-608.

#### **SECTION 2-603. MERCHANT BUYER'S DUTIES AS TO RIGHTFULLY-REJECTED GOODS.**

(1) Subject to any security interest in the buyer (subsection (3) of Section 2-711), when the seller has no agent or place of business at the market of rejection a merchant buyer is under a duty after rejection of goods in ~~his~~ the buyer's possession or control to follow any reasonable instructions received from the seller with respect to the goods and in the absence of such instructions to make reasonable efforts to sell them for the seller's account if they are perishable or threaten to decline in value speedily. ~~Instructions~~ In the case of a rightful rejection instructions are not reasonable if on demand indemnity for expenses is not forthcoming.

(2) When the buyer sells goods under subsection (1) following a rightful rejection, ~~he~~ the buyer is entitled to reimbursement from the seller or out of the proceeds for reasonable expenses of caring for and selling them, and if the expenses include no selling commission then to such commission as is usual in the trade or if there is none to a reasonable sum not exceeding ten per cent on the gross proceeds.

(3) In complying with this section the buyer is held only to good faith and good faith conduct hereunder is neither acceptance nor conversion nor the basis of an action for damages.

#### **Proposed Comment**

Consistent with the approach taken in Section 2-602, the title to this section has been amended to delete the word "rightful." Accordingly, except as otherwise stated in this section its provisions apply to all effective rejections, including rejections that are wrongful. Thus, any merchant buyer whose rejection is effective is subject to the duties set forth in the first sentence of subsection (1), and a merchant buyer that complies with those duties is entitled to the protection provided by subsection (3). However, the right to indemnity for expenses on demand under the second sentence of subsection (1) and the right to reimbursement for expenses and a commission under subsection (2) are limited to buyers whose rejections are rightful.

#### **SECTION 2-604. BUYER'S OPTIONS AS TO SALVAGE OF RIGHTFULLY-REJECTED GOODS.**

~~Subject to the provisions of the immediately preceding section on perishables if the seller gives no~~

~~instructions within a reasonable time after notification of rejection section~~, the buyer may store the rejected goods for the seller's account or reship them to ~~him~~ the seller or resell them for the seller's account with reimbursement as provided in the preceding section. Such action is not acceptance or conversion.

#### **Proposed Comment**

Consistent with the approach taken in Section 2-602, the title to this section has been amended to delete the word "rightful." Accordingly, its provisions apply to any buyer whose rejection is effective. Note, however, that this section is subject to Section 2-603, and the provisions of that section differentiate between rightful and wrongful rejections.

The reference to "perishables" has been deleted as misleading - Section 2-603 applies to more than just goods that are perishable. The phrase "if the seller gives no instructions within a reasonable time after notification of rejection" has been deleted as superfluous.

#### **SECTION 2-605. WAIVER OF BUYER'S OBJECTIONS BY FAILURE TO PARTICULARIZE.**

(1) The buyer's failure to state in connection with rejection a particular defect ~~or in connection with revocation of acceptance a defect that justifies revocation~~ which is ascertainable by reasonable inspection precludes ~~him~~ the buyer from relying on the unstated defect to justify rejection or ~~to establish breach~~ revocation of acceptance if the defect is ascertainable by reasonable inspection

(a) where the seller had a right to cure the defect and could have cured it if stated seasonably; or

(b) between merchants when the seller has after rejection made a request in writing a record and for a full and final written statement in record form of all defects on which the buyer proposes to rely.

(2) ~~Payment~~ A buyer's against documents tendered to the buyer made without reservation of rights precludes recovery of the payment for defects apparent on the face of the documents.

#### **Proposed Comment**

1. This section rests upon a policy of permitting the buyer to give a quick and informal notice of defects in a tender without penalizing the buyer for omissions, while at the same time protecting a seller that is reasonably misled by the buyer's failure to state curable defects. Where the defect in a tender is one which could have been cured by the seller, a buyer that merely rejects the delivery without stating any

objections to the tender is probably acting in commercial bad faith and seeking to get out of a deal which has become unprofitable. Following the general policy of this Article to preserve the deal wherever possible, subsection (1)(a) requires that the seller's right to correct the tender in the circumstances be protected.

Subsection (1) as revised makes three substantive changes. First, failure to particularize affects only the buyer's right to reject or revoke acceptance, not the buyer's right to establish breach. Waiver of a right to damages for breach because of a failure properly to notify the seller is governed by Section 2-607(3).

Second, subsection (1) now requires the seller to have had a right to cure under Section 2-508 in addition to having the ability to cure. This point was perhaps implicit in the prior provision, but it is now expressly stated to avoid any question of whether this section creates a seller's right to cure independent of the right enumerated in section 2-508. Thus if the defect is one that could be cured under Section 2-508, the buyer will have waived that defect as a basis for rejecting the goods, or possibly revoking acceptance, if the buyer fails to state the defect with sufficient particularity to facilitate the seller's exercise of its right to cure as provided in Section 2-508.

Subsection (1) as revised has been extended to include not only rejection but also revocation of acceptance. This is necessitated by the expansion of the right to cure (Section 2-508) to cover revocation of acceptance in nonconsumer contracts. The application of the subsection to revocation cases is limited in the following ways: 1) because a revocation under Section 2-608(1)(a) does not trigger a right to cure under Section 2-508, the revocation does not trigger subsection (1); 2) because Section 2-608(1)(b) involves defects that are by definition difficult to discover, there is no waiver under subsection (1) unless the defect at issue justifies the revocation and the buyer has notice of it; and 3) because the right to cure following revocation of acceptance is restricted under Section 2-508 to nonconsumer contracts, this section cannot be asserted against a consumer who is seeking to revoke acceptance. The consequences of a consumer's failure to give proper notice are governed by Section 2-607(3).

2. When the time for cure is past, subsection (1)(b) makes plain that a merchant seller is entitled upon request to a final statement of objections by a merchant buyer upon which the seller can rely. What is needed is a clear statement to the buyer of exactly what is being sought. A formal demand will be sufficient in the case of a merchant-buyer.

3. Subsection (2) has been revised to make clear that the buyer that makes payment upon presentation of

the documents to the buyer may waive defects, but that a person that is not the buyer, such as the issuer of a letter of credit, that pays as against documents is not waiving the buyer's right to assert defects in the documents as against the seller.

Subsection (2) applies to documents the same principle contained in section 2-606(1)(a) for the acceptance of goods; that is, if the buyer accepts documents that have apparent defects, the buyer is presumed to have waived the defects as a basis for rejecting the documents. Subsection (2) is limited to defects which are apparent on the face of the documents. When payment is required against documents, the documents must be inspected before the payment, and the payment constitutes acceptance of the documents. When the documents are delivered without requiring a contemporary payment by the buyer, the acceptance of the documents by non-objection is postponed until after a reasonable time for the buyer to inspect the documents. In either situation, however, the buyer "waives" only what is apparent on the face of the documents. Moreover, in either case, the acceptance of the documents does not constitute an acceptance of the goods and does not impair any options or remedies of the buyer for improper delivery of the goods. See Section 2-512(2).

## **SECTION 2-606. WHAT CONSTITUTES ACCEPTANCE OF GOODS.**

(1) Acceptance of goods occurs when the buyer

(a) after a reasonable opportunity to inspect the goods signifies to the seller that the goods are conforming or that he the buyer will take or retain them in spite of their non-conformity; or

(b) fails to make an effective rejection (subsection (1) of Section 2-602), but such acceptance does not occur until the buyer has had a reasonable opportunity to inspect them; or

(c) except as otherwise provided in Section 2-608(4), does any act inconsistent with the seller's ownership; but if such the act is wrongful as against the seller it is an acceptance only if ratified by him ratified by the seller.

(2) Acceptance of a part of any commercial unit is acceptance of that entire unit.

### **Proposed Comment**

The only substantive change is the cross-reference in subsection (1)(c) to Section 2-608(4), which deals with the problem of post-rejection or post-revocation use of the goods. See Proposed Comment to

Section 2-608.

**SECTION 2-607. EFFECT OF ACCEPTANCE; NOTICE OF BREACH; BURDEN OF ESTABLISHING BREACH AFTER ACCEPTANCE; NOTICE OF CLAIM OR LITIGATION TO PERSON ANSWERABLE OVER.**

(1) The buyer must pay at the contract rate for any goods accepted.

(2) Acceptance of goods by the buyer precludes rejection of the goods accepted and if made with knowledge of a non-conformity cannot be revoked because of it unless the acceptance was on the reasonable assumption that the non-conformity would be seasonably cured but acceptance does not of itself impair any other remedy provided by this Article for non-conformity.

(3) Where a tender has been accepted

(a) the buyer must within a reasonable time after ~~he~~ the buyer discovers or should have discovered any breach notify the seller ~~of breach or be barred from any remedy; ; however, failure to give timely notice bars the buyer from a remedy only to the extent that the seller is prejudiced by the failure and~~

(b) if the claim is one for infringement or the like (subsection (3) of Section 2-312) and the buyer is sued as a result of such a breach ~~he~~ the buyer must so notify the seller within a reasonable time after ~~he~~ the buyer receives notice of the litigation or be barred from any remedy over for liability established by the litigation.

(4) The burden is on the buyer to establish any breach with respect to the goods accepted.

(5) Where the buyer is sued for indemnity, breach of a warranty or other obligation for which ~~his seller another party~~ is answerable over

(a) ~~he~~ the buyer may give ~~his seller the other party~~ written notice of the litigation in a record. If the notice states that the ~~seller other party~~ may come in and defend and that if the ~~seller other party~~ does not do so ~~he~~ the other party will be bound in any action against ~~him~~ the other party by ~~his~~ the buyer by any determination of fact common to the two litigations, then unless the ~~seller other party~~ after seasonable receipt of the notice does come in and defend ~~he~~ the other party is so bound.

(b) if the claim is one for infringement or the like (subsection (3) of Section 2-312) the original seller may demand in ~~writing a record~~ that his its buyer turn over to ~~him~~ it control of the litigation including settlement or else be barred from any remedy over and if ~~he~~ it also agrees to bear all expense and to

satisfy any adverse judgment, then unless the buyer after seasonable receipt of the demand does turn over control the buyer is so barred.

(6) The provisions of subsections (3), (4) and (5) apply to any obligation of a buyer to hold the seller harmless against infringement or the like (subsection (3) of Section 2-312).

**Proposed Comment**

1. Subsection (3)(a) provides that a failure to give notice to the seller bars the buyer from a remedy for breach of contract only if the seller suffers prejudice due to the failure to notify. See Restatement (Second) of Contracts SECTION 229, excusing a condition where the failure is not material and implementation would result in disproportionate forfeiture.

2. The vouching-in procedure in subsection (5) has been expanded to include indemnity actions, and it has been broadened to include any other party that is answerable over, not just the immediate seller. As under former Article 2, all the provisions of this section are subject to any explicit reservation of rights. Section 1-207.

Vouching in does not confer on the notified seller a right to intervene, does not confer jurisdiction of any kind on the court over the seller, and does not create a duty to defend on the part of the seller. Those matters continue to be governed by the applicable rules of civil procedure and substantive law outside this section. Vouching in is based upon the principle that the seller is liable for its contractual obligations regarding the quality or title to the goods which the buyer is being forced to defend.

**SECTION 2-608. REVOCATION OF ACCEPTANCE IN WHOLE OR IN PART.**

(1) The buyer may revoke ~~his~~ acceptance of a lot or commercial unit whose non-conformity substantially impairs its value to ~~him~~ the buyer if ~~he~~ the buyer has accepted it

(a) on the reasonable assumption that its non-conformity would be cured and it has not been seasonably cured; or

(b) without discovery of such non-conformity if ~~his~~ the buyer's acceptance was reasonably induced either by the difficulty of discovery before acceptance or by the seller's assurances.

(2) Revocation of acceptance must occur within a reasonable time after the buyer discovers or should have discovered the ground for it and before any substantial change in condition of the goods which is not caused by their own defects. ~~It~~ The revocation is not effective until the buyer notifies the seller of it.

(3) A buyer ~~who~~ that so revokes has the same rights and duties with regard to the goods involved as if ~~he~~ the buyer had rejected them.

(4) If a buyer uses the goods after a rightful rejection or justifiable revocation of acceptance, the following rules apply:

(a) Any use by the buyer that is unreasonable under the circumstances is wrongful as against the seller and is an acceptance only if ratified by the seller.

(b) Any use of the goods that is reasonable under the circumstances is not wrongful as against the seller and is not an acceptance, but in an appropriate case the buyer shall be obligated to the seller for the value of the use to the buyer.

#### **Proposed Comment**

Subsection (4), which is new, deals with the problem of post-rejection or revocation use of the goods. The courts have developed several alternative approaches. Under original Article 2, a buyer's post-rejection or revocation use of the goods could be treated as an acceptance, thus undoing the rejection or revocation, could be a violation of the buyer's obligation of reasonable care, or could be a reasonable use for which the buyer must compensate the seller. Subsection (4) adopts the third approach. If the buyer's use after an effective rejection or a justified revocation of acceptance is unreasonable under the circumstances, it is inconsistent with the rejection or revocation of acceptance and is wrongful as against the seller. This gives the seller the option of ratifying the use, thereby treating it as an acceptance, or pursuing a non-Code remedy for conversion.

If the buyer's use is reasonable under the circumstances, the buyer's actions cannot be treated as an acceptance. The buyer must compensate the seller for the value of the use of the goods to the buyer. Determining the appropriate level of compensation requires a consideration of the buyer's particular circumstances and should take into account the defective condition of the goods. There may be circumstances, such as where the use is solely for the purpose of protecting the buyer's security interest in the goods, where no compensation is due the seller. In other circumstances, the seller's right to compensation must be netted out against any right of the buyer to damages.

#### **SECTION 2-609. RIGHT TO ADEQUATE ASSURANCE OF PERFORMANCE.**

(1) A contract for sale imposes an obligation on each party that the other's expectation of receiving due performance will not be impaired. When reasonable grounds for insecurity arise with respect to the performance of either party the other may ~~in writing~~ demand ~~in a record~~ adequate assurance of due performance and until ~~he~~ the party receives the assurance may if commercially reasonable suspend any performance for which ~~he~~ it has not already received the agreed return.

(2) Between merchants the reasonableness of grounds for insecurity and the adequacy of any assurance offered shall be determined according to commercial standards.

(3) Acceptance of any improper delivery or payment does not prejudice the aggrieved party's right to demand adequate assurance of future performance.

(4) After receipt of a justified demand failure to provide within a reasonable time not exceeding thirty days such assurance of due performance as is adequate under the circumstances of the particular case is a repudiation of the contract.

#### **SECTION 2-610. ANTICIPATORY REPUDIATION.**

(1) When either party repudiates the contract with respect to a performance not yet due the loss of which will substantially impair the value of the contract to the other, the aggrieved party may

(a) for a commercially reasonable time await performance by the repudiating party; or

(b) resort to any remedy for breach (Section 2-703 or Section 2-711), even though ~~he~~ the aggrieved party has notified the repudiating party that ~~he~~ it would await the latter's performance and has urged retraction; and

(c) in either case suspend ~~his own~~ performance or proceed in accordance with the provisions of this Article on the seller's right to identify goods to the contract notwithstanding breach or to salvage unfinished goods (Section 2-704).

(2) Repudiation includes language that a reasonable party would interpret to mean that the other party will not or cannot make a performance still due under the contract or voluntary, affirmative conduct that would appear to a reasonable party to make a future performance by the other party impossible.

#### **Proposed Comment**

Subsection (2), which is new, provides guidance on when a party can be considered to have repudiated a performance obligation based upon the Restatement (Second) of Contracts SECTION 250 and does not purport to be an exclusive statement of when a repudiation has occurred. As under prior law, repudiation centers upon an overt communication of intention, actions which render performance impossible, or a demonstration of a clear determination not to perform. Repudiation does not require that performance be made utterly impossible, rather, actions which reasonably indicate rejection of the performance obligation suffice. Failure to provide adequate assurance of due performance under Section 2-609 also operates as a repudiation.

### **SECTION 2-611. RETRACTION OF ANTICIPATORY REPUDIATION.**

(1) Until the repudiating party's next performance is due ~~he~~ that party can retract ~~his~~ the repudiation unless the aggrieved party has since the repudiation canceled or materially changed ~~his~~ position or otherwise indicated that ~~he considers~~ the repudiation is final.

(2) Retraction may be by any method which clearly indicates to the aggrieved party that the repudiating party intends to perform, but must include any assurance justifiably demanded under the provisions of this Article (Section 2-609).

(3) Retraction reinstates the repudiating party's rights under the contract with due excuse and allowance to the aggrieved party for any delay occasioned by the repudiation.

### **SECTION 2-612. "INSTALLMENT CONTRACT"; BREACH.**

(1) An "installment contract" is one which requires or authorizes the delivery of goods in separate lots to be separately accepted, even though the contract contains a clause "each delivery is a separate contract" or its equivalent.

(2) The buyer may reject any installment which is non-conforming if the non-conformity substantially impairs the value of that installment ~~and cannot be cured to the buyer~~ or if the non-conformity is a defect in the required documents; but if the non-conformity does not fall within subsection (3) and the seller gives adequate assurance of its cure the buyer must accept that installment.

(3) Whenever non-conformity or default with respect to one or more installments substantially impairs the value of the whole contract there is a breach of the whole. But the aggrieved party reinstates the contract if ~~he~~ the party accepts a non-conforming installment without seasonably notifying of cancellation or if ~~he~~ the party brings an action with respect only to past installments or demands

performance as to future installments.

### **Proposed Comment**

Subsection (2) has been amended to make it clear that the buyer's right in the first instance to reject an installment depends upon whether there has been a substantial impairment of the value of the installment to the buyer and not on the seller's ability to cure the nonconformity. The seller can prevent a rightful rejection by giving adequate assurances of cure. Amending subsection (2) by adding the words "to the buyer" makes the standard for rejecting an installment consistent with the standard for revoking acceptance under Section 2-608.

### **SECTION 2-613. CASUALTY TO IDENTIFIED GOODS.**

Where the contract requires for its performance goods identified when the contract is made, and the goods suffer casualty without fault of either party before the risk of loss passes to the buyer, ~~or in a proper case under a "no arrival, no sale" term (Section 2-324)~~ then

(a) if the loss is total the contract is ~~avoided~~ terminated; and

(b) if the loss is partial or the goods have so deteriorated as no longer to conform to the contract the buyer may nevertheless demand inspection and at ~~his~~ its option either treat the contract as ~~avoided~~ terminated or accept the goods with due allowance from the contract price for the deterioration or the deficiency in quantity but without further right against the seller.

### **Proposed Comment**

1. The cross-reference to Section 2-324 has been deleted because the referenced section no longer exists.

2. The change in paragraph (a) from "avoided" to "terminated" preserves pre-termination breaches. See Section 2-106(3).

### **SECTION 2-615. EXCUSE BY FAILURE OF PRESUPPOSED CONDITIONS.**

Except so far as a seller may have assumed a greater obligation and subject to the preceding section on substituted performance:

(a) Delay in ~~delivery or non-delivery~~ performance or non-performance in whole or in part by a seller ~~who that~~ he complies with paragraphs (b) and (c) is not a breach of ~~his~~ the seller's duty under a contract for sale if performance as agreed has been made impracticable by the occurrence of a contingency the non-occurrence of which was a basic assumption on which the contract was made or by compliance in good faith with any applicable foreign or domestic governmental regulation or order whether or not it later proves to be invalid.

(b) Where the causes mentioned in paragraph (a) affect only a part of the seller's capacity to perform, ~~he~~ the seller must allocate production and deliveries among ~~his~~ its customers but may at ~~his~~ its option include regular customers not then under contract as well as ~~his~~ its own requirements for further manufacture. ~~He~~ The seller may so allocate in any manner which is fair and reasonable.

(c) The seller must notify the buyer seasonably that there will be delay or non-delivery and, when allocation is required under paragraph (b), of the estimated quota thus made available for the buyer.

#### **Proposed Comment**

"[D]elivery or non-delivery" in Paragraph (a) has been changed to "performance or non-performance" to take into consideration the broad range of obligations that a seller may have in addition to the obligation to deliver the goods.

#### **SECTION 2-616. PROCEDURE ON NOTICE CLAIMING EXCUSE.**

(1) Where the buyer receives notification of a material or indefinite delay or an allocation justified under the preceding section ~~he~~ it may by ~~written~~ written notification in a record to the seller as to any delivery concerned, and where the prospective deficiency substantially impairs the value of the whole contract under the provisions of this Article relating to breach of installment contracts (Section 2-612), then also as to the whole,

(a) terminate and thereby discharge any unexecuted portion of the contract; or

(b) modify the contract by agreeing to take ~~his~~ its available quota in substitution.

(2) If after receipt of ~~such~~ notification from the seller the buyer fails ~~so~~ to modify the contract within a reasonable time not exceeding thirty days the contract ~~lapses~~ is terminated with respect to any deliveries

performance affected.

(3) The provisions of this section may not be negated by agreement except in so far as the seller has assumed a greater obligation under the preceding section.

#### **Proposed Comment**

In subsection (2), the change from "lapses" to "is terminated" conforms with the amendment of Section 2-613(a) and the change from "deliveries" to "performance" conforms with the amendment to Section 2-615(a).

### **PART 7**

### **REMEDIES**

#### **SECTION 2-702. SELLER'S REMEDIES ON DISCOVERY OF BUYER'S INSOLVENCY.**

(1) Where the seller discovers the buyer to be insolvent ~~he~~ the seller may refuse delivery except for cash including payment for all goods theretofore delivered under the contract, and stop delivery under this Article (Section 2-705).

(2) Where the seller discovers that the buyer has received goods on credit while insolvent ~~he~~ the seller may reclaim the goods upon demand made within ~~ten days~~ a reasonable time after the buyer's receipt of the goods, ~~but if misrepresentation of solvency has been made to the particular seller in writing within three months before delivery the ten day limitation does not apply.~~ Except as provided in this subsection the seller may not base a right to reclaim goods on the buyer's fraudulent or innocent misrepresentation of solvency or of intent to pay.

(3) The seller's right to reclaim under subsection (2) is subject to the rights of a buyer in ordinary course or other good-faith purchaser for value under this Article (Section 2-403). Successful reclamation of goods excludes all other remedies with respect to them.

#### **Proposed Comment**

1. The seller's right to withhold the goods or to stop delivery except for cash when the seller discovers the buyer's insolvency is made explicit in subsection (1) regardless of the passage of title, and the concept of stoppage has been extended to include goods in the possession of any bailee that has not yet attorned to the buyer.

2. Subsection (2) takes as its base line the proposition that any receipt of goods on credit by an insolvent buyer amounts to a tacit business misrepresentation of solvency and therefore is fraudulent as against the particular seller. The amendments omit the 10-day limitation and the 3-month exception to the 10-day limitation. If the buyer is in bankruptcy at the time of reclamation, the seller will have to comply with Section 546(c) of the Bankruptcy Code of 1978, which includes a 10-day limitation.

3. Because the right of the seller to reclaim goods under this section constitutes preferential treatment as against the buyer's other creditors, subsection (3) provides that such reclamation bars all of the seller's other remedies as to the goods involved.

4. The rights of a seller to reclamation under section 2-702 from its buyer are subordinate to the rights of good faith purchasers from that buyer under Section 2-403. The amendments take no position on the seller's claims to proceeds of the goods. Courts have disagreed on the seller's rights to proceeds of goods that would have been subject to reclamation had they not been resold.

#### **SECTION 2-703. SELLER'S REMEDIES IN GENERAL.**

~~Where the buyer wrongfully rejects or revokes acceptance of goods or fails to make a payment due on or before delivery or repudiates with respect to a part or the whole, then with respect to any goods directly affected and, if the breach is of the whole contract (Section 2-612), then also with respect to the whole undelivered balance, the aggrieved seller may~~

- ~~(a) withhold delivery of such goods;~~
- ~~(b) stop delivery by any bailee as hereafter provided (Section 2-705);~~
- ~~(c) proceed under the next section respecting goods still unidentified to the contract;~~
- ~~(d) resell and recover damages as hereafter provided (Section 2-706);~~
- ~~(e) recover damages for non-acceptance (Section 2-708) or in a proper case the price (Section 2-709);~~
- ~~(f) cancel.~~

(1) A breach of contract by the buyer includes the buyer's wrongful rejection or wrongful attempt to revoke acceptance of goods, wrongful failure to perform a contractual obligation, failure to make a payment when due, or repudiation.

(2) If the buyer is in breach of contract the seller may to the extent provided for by this Act or other law:

- (a) withhold delivery of the goods;
- (b) stop delivery of the goods under Section 2-705;
- (c) proceed under Section 2-704 with respect to goods unidentified to the contract or unfinished;
- (d) reclaim the goods under Section 2-507(2) or 2-702(2);
- (e) require payment directly from the buyer under Section 2-325(c);
- (f) cancel;
- (g) resell and recover damages under Section 2-706;
- (h) recover damages for nonacceptance or repudiation under Section 2-708(1);
- (i) recover lost profits under Section 2-708(2);
- (j) recover the price under Section 2-709;
- (k) obtain specific performance under Section 2-716;
- (l) recover liquidated damages under Section 2-718;
- (m) in other cases, recover damages in any manner that is reasonable under the circumstances.

(3) If a buyer becomes insolvent, the seller may:

- (a) withhold delivery under Section 2-702(1);
- (b) stop delivery of the goods under Section 2-705;
- (c) reclaim the goods under Section 2-702(2).

### **Proposed Comment**

1. This section is a list of the remedies of the seller available under this Article to remedy any breach by the buyer. It also lists the seller's statutory remedies in the event of buyer insolvency. The subsection does not address the extent to which other law provides additional remedies or supplements the statutory remedies in Article 2 ( see Section 1-103).

In addition to the statutory remedies, it contemplates agreed upon remedies, see subsection (2)(l). It does not address remedies that become available upon demand for adequate assurance under Section 2-609.

This Article rejects any doctrine of election of remedy as a fundamental policy and thus the remedies are essentially cumulative in nature and include all of the available remedies for breach. Whether the pursuit of one remedy bars another depends entirely on the facts of the individual case.

2. The buyer's breach which occasions the use of the remedies under this section may involve only one lot or delivery of goods, or may involve all of the goods which are the subject matter of the particular contract. The right of the seller to pursue a remedy as to all the goods when the breach is as to only one or more lots is covered by the section on breach in installment contracts. The present section deals only with remedies available after the goods involved in the breach have been determined by that section.

3. In addition to the typical case of refusal to pay or default in payment, the language in subsection (1), "fails to make a payment due," is intended to cover the dishonor of a check on due presentment, or the non-acceptance of a draft, and the failure to furnish an agreed letter of credit.

4. It should also be noted that this Act requires its remedies to be liberally administered and provides that any right or obligation which it declares is enforceable by action unless a different effect is specifically prescribed (Section 1-106).

### **SECTION 2-704. SELLER'S RIGHT TO IDENTIFY GOODS TO THE CONTRACT NOTWITHSTANDING BREACH OR TO SALVAGE UNFINISHED GOODS.**

(1) An aggrieved seller under the preceding section may

(a) identify to the contract conforming goods not already identified if at the time he the seller learned of the breach they the goods are in his the seller's possession or control;

(b) treat as the subject of resale goods which have demonstrably been intended for the particular contract even though those goods are unfinished.

(2) Where the goods are unfinished an aggrieved seller may in the exercise of reasonable commercial judgment for the purposes of avoiding loss and of effective realization either complete the manufacture and wholly identify the goods to the contract or cease manufacture and resell for scrap or salvage value or proceed in any other reasonable manner.

### **SECTION 2-705. SELLER'S STOPPAGE OF DELIVERY IN TRANSIT OR OTHERWISE.**

(1) The seller may stop delivery of goods in the possession of a carrier or other bailee when he the seller discovers the buyer to be insolvent (Section 2-702) ~~and may stop delivery of earload, truckload, plane load or larger shipments of express or freight~~ or when the buyer repudiates or fails to make a payment due before delivery or if for any other reason the seller has a right to withhold or reclaim the goods.

(2) As against such buyer the seller may stop delivery until

(a) receipt of the goods by the buyer; or

(b) acknowledgment to the buyer by any bailee of the goods, except a carrier, that the bailee holds the goods for the buyer; or

(c) such acknowledgment to the buyer by a carrier by reshipment or as warehouseman; or

(d) negotiation to the buyer of any negotiable document of title covering the goods.

(3)(a) To stop delivery the seller must so notify as to enable the bailee by reasonable diligence to prevent delivery of the goods.

(b) After such notification the bailee must hold and deliver the goods according to the directions of the seller but the seller is liable to the bailee for any ensuing charges or damages.

(c) If a negotiable document of title has been issued for goods, the bailee is not obliged to obey a

notification to stop until surrender of the document.

(d) A carrier ~~who~~ that has issued a non-negotiable bill of lading is not obliged to obey a notification to stop received from a person other than the consignor.

#### **Proposed Comment**

Subsection (1) has been amended to omit the restriction that prohibited stoppage of less than "carload, truckload, planeload or larger shipments" in certain circumstances. The capacity of carriers to identify shipments as small as a single package makes it feasible to stop small shipments.

#### **SECTION 2-706. SELLER'S RESALE INCLUDING CONTRACT FOR RESALE.**

(1) ~~Under the conditions stated in Section 2-703 on seller's remedies~~ In an appropriate case involving breach by the buyer, the seller may resell the goods concerned or the undelivered balance thereof. Where the resale is made in good faith and in a commercially reasonable manner the seller may recover the difference between the ~~contract price and the resale price and the contract price~~ together with any incidental or consequential damages allowed under the provisions of this Article (Section 2-710), but less expenses saved in consequence of the buyer's breach.

(2) Except as otherwise provided in subsection (3) or unless otherwise agreed resale may be at public or private sale including sale by way of one or more contracts to sell or of identification to an existing contract of the seller. Sale may be as a unit or in parcels and at any time and place and on any terms but every aspect of the sale including the method, manner, time, place and terms must be commercially reasonable. The resale must be reasonably identified as referring to the broken contract, but it is not necessary that the goods be in existence or that any or all of them have been identified to the contract before the breach.

(3) Where the resale is at private sale the seller must give the buyer reasonable notification of ~~his~~ an intention to resell.

(4) Where the resale is at public sale

(a) only identified goods can be sold except where there is a recognized market for a public sale of futures in goods of the kind; and

(b) it must be made at a usual place or market for public sale if one is reasonably available and except in the case of goods which are perishable or threaten to decline in value speedily the seller must give the

buyer reasonable notice of the time and place of the resale; and

(c) if the goods are not to be within the view of those attending the sale the notification of sale must state the place where the goods are located and provide for their reasonable inspection by prospective bidders; and

(d) the seller may buy.

(5) A purchaser ~~who~~ that buys in good faith at a resale takes the goods free of any rights of the original buyer even though the seller fails to comply with one or more of the requirements of this section.

(6) The seller is not accountable to the buyer for any profit made on any resale. A person in the position of a seller (Section 2-707) or a buyer ~~who~~ that has rightfully rejected or justifiably revoked acceptance must account for any excess over the amount of ~~his~~ the buyer's security interest, as hereinafter defined (subsection (3) of Section 2-711).

(7) Failure of a seller to resell under this section does not bar the seller from any other remedy.

#### **Proposed Comment**

1. **Changes.** Consistent with the revision of Section 2-710, this section now provides for consequential as well as incidental damages. Subsection (7) is new, and parallels the provision for buyer cover in 2-713. Original Section 2-706(1) measures damages by the difference between the resale price and the contract price; amended subsection (1) reverses these terms ("difference between the contract price and the resale price") because the contract price must be the larger number for there to be direct damages.

2. The right of resale under this section arises when a seller reclaims goods under Section 2-507 or a buyer repudiates or makes a wrongful but effective rejection. In addition, there is a right of resale if the buyer unjustifiably attempts to revoke acceptance and the seller takes back the goods. However, the seller may choose to ignore the buyer's unjustifiable attempt to revoke acceptance, in which case the appropriate remedy is an action for the price under Section 2-709. Application of the right of resale to cases of buyer repudiation is supplemented by subsection (2), which authorizes a resale of goods which are not in existence or were not identified to the contract before the breach.

Subsection (1) allows the seller to resell the goods after a buyer's breach of contract if the seller has possession or control of the goods. The seller may have possession or control of the goods at the time of the breach or may have regained possession of the goods upon the buyer's wrongful rejection. If the seller has regained possession of the goods from the buyer pursuant to Article 9, that Article controls the seller's rights of resale.

3. Under this Article the seller resells by authority of law, on the seller's own behalf, for the seller's own benefit and for the purpose of setting the seller's damages. The theory of a seller's agency is thus rejected. The question of whether the title to the goods has or has not passed to the buyer is not relevant for the operation of this section.

4. To recover the damages prescribed in subsection (1) the seller must act "in good faith and in a commercially reasonable manner" in making the resale. If the seller complies with the prescribed standards in making the resale, the seller may recover from the buyer the damages provided for in subsection (1). Evidence of market or current prices at any particular time or place is relevant only for the question of whether the seller acted in a commercially reasonable manner in making the resale.

5. Subsection (2) enables the seller to resell in accordance with reasonable commercial practices so as to realize as high a price as possible in the circumstances. A seller may sell at a public sale or a private sale as long as the choice is commercially reasonable. A "public" sale is one to which members of the public are admitted. A public sale is usually a sale by auction, but all auctions are not public auctions. A private sale may be effected by an auction or by solicitation and negotiation conducted either directly or through a broker. In choosing between a public and private sale, the character of the goods must be considered and relevant trade practices and usages must be observed. A public sale has further requirements stated in subsection (4).

The purpose of subsection (2) is to enable the seller to dispose of the goods to the best advantage, and therefore the seller is permitted in making the resale to depart from the terms and conditions of the original contract for sale to any extent "commercially reasonable" in the circumstances.

As for the place for resale, the focus is on the commercial reasonableness of the seller's choice as to the place for an advantageous resale. This section rejects the theory that the seller should normally resell at the agreed place for delivery and that a resale elsewhere can be permitted only in exceptional cases.

The time for resale is a reasonable time after the buyer's breach. What is a reasonable time depends on the nature of the goods, the condition of the market and the other circumstances of the case; its length cannot be measured by any legal yardstick or divided into degrees. When a seller contemplating resale receives a demand from the buyer for inspection under Section 2-515, the time for resale may be appropriately lengthened.

6. The provision of subsection (2) that the goods need not be in existence to be resold applies when the buyer is guilty of anticipatory repudiation of a contract for future goods before the goods or some of the

goods have come into existence. In this case, the seller may exercise the right of resale and fix the damages by "one or more contracts to sell" the quantity of conforming future goods affected by the repudiation.

The companion provision of subsection (2), that resale may be made although the goods were not identified to the contract prior to the buyer's breach, likewise contemplates an anticipatory repudiation by the buyer, but one occurring after the goods are in existence. The seller may identify goods to the contract after the breach, but must identify the goods being sold as pertaining to the breached contract. If the identified goods conform to the contract, their resale will fix the seller's damages as satisfactorily as if the goods had been identified before the breach.

7. If the resale is to be by private sale, subsection (3) requires that reasonable notification of the seller's intention to resell must be given to the buyer. Notification of the time and place of a private resale is not required.

8. Subsection (4) states requirements for a public resale. The requirements of this subsection are in addition to the requirements of subsection (2), which pertain to all resales under this section.

Paragraph (a) of subsection (4) qualifies the last sentence of subsection (2) with respect to resales of unidentified and future goods at public sale. If conforming goods are in existence the seller may identify them to the contract after the buyer's breach and then resell them at public sale. If the goods have not been identified, however, the seller may resell them at public sale only as "future" goods and only if there is a recognized market for public sale of futures in goods of the kind.

Subsection (4)(b) requires that the seller give the buyer reasonable notice of the time and place of a public resale so that the buyer may have an opportunity to bid or to secure the attendance of other bidders. An exception is made in the case of goods "which are perishable or threaten to decline speedily in value."

Since there would be no reasonable prospect of competitive bidding elsewhere, subsection (4)(b) requires that a public resale "must be made at a usual place or market for public sale if one is reasonably available"; i.e., a place or market which prospective bidders may reasonably be expected to attend. The

market may still be "reasonably available" under this subsection, although at a considerable distance from the place where the goods are located. In this case, the expense of transporting the goods for resale is recoverable from the buyer as part of the seller's incidental damages under subsection (1). However, the question of availability is one of commercial reasonableness in the circumstances and if such "usual" place or market is not reasonably available, a duly advertised public resale may be held at another place if it is one which prospective bidders may reasonably be expected to attend, as distinguished from a place where there is no demand whatsoever for goods of the kind.

Subsection (4)(c) is designed to permit intelligent bidding. Subsection (4)(d), which permits the seller to bid and, of course, to become the purchaser, benefits the original buyer by tending to increase the resale price and thus decreasing the damages the buyer will have to pay.

9. Subsection (5) allows a purchaser to take the goods free of the rights of the buyer even if the seller has not complied with this section. The policy of resolving any doubts in favor of the resale purchaser operates to the benefit of the buyer by increasing the price the purchaser should be willing to pay.

10. Subsection (6) recognizes that when the seller is entitled to resell under this Article, the goods are the seller's goods and the purpose of resale under this section is to set the seller's damages as against the buyer. However, a person in the position of the seller under Section 2-707 or a buyer asserting a security interest in the goods under Section 2-711(3) has only a limited right in the goods and so must account to the seller for any excess over the limited amount necessary to satisfy that right.

11. Subsection (7) expresses the policy that resale is not a mandatory remedy for the seller. Except as otherwise provided in Section 2-710, the seller is always free to choose between resale and damages for repudiation or nonacceptance under Section 2-708.

Subsection (7) parallels the provision in the cover section, Section 2-712. A seller that fails to comply with the requirements of this section may recover damages under Section 2-708(1). In addition, a seller may recover both incidental and consequential damages under Section 2-710 assuming the seller's damages have not been liquidated under Section 2-718 or limited under Section 2-719.

## **SECTION 2-707. "PERSON IN THE POSITION OF A SELLER".**

(1) A "person in the position of a seller" includes as against a principal an agent ~~who~~ that has paid or become responsible for the price of goods on behalf of ~~his~~ the principal or anyone ~~who~~ that otherwise holds a security interest or other right in goods similar to that of a seller.

(2) A person in the position of a seller ~~may as provided in this Article withhold or stop delivery (Section 2-705) and resell (Section 2-706) and recover incidental damages (Section 2-710) has the same remedies as a seller under this Article.~~

### **Proposed Comment**

Subsection (2) has been amended to permit a "person in the position of a seller" to have the full range of remedies available to a seller.

## **SECTION 2-708. SELLER'S DAMAGES FOR NON-ACCEPTANCE OR REPUDIATION.**

(1) Subject to subsection (2) and to the provisions of this Article with respect to proof of market price (Section 2-723)

(a) the measure of damages for non-acceptance ~~or repudiation~~ by the buyer is the difference between the ~~contract price and the market price at the time and place for tender and the unpaid contract price~~ together with any incidental ~~or consequential~~ damages provided in this Article (Section 2-710), but less expenses saved in consequence of the buyer's ~~breach~~; breach; and

(b) the measure of damages for repudiation by the buyer is the difference between the ~~contract price and the market price at the place for tender at the expiration of a commercially reasonable time after the seller learned of the repudiation, but no later than the time stated in paragraph (a), together with any incidental or consequential damages provided in this Article (Section 2-710), but less expenses saved in consequence of the buyer's breach.~~

(2) If the measure of damages provided in subsection (1) ~~or in Section 2-706~~ is inadequate to put the seller in as good a position as performance would have done then the measure of damages is the profit (including reasonable overhead) which the seller would have made from full performance by the buyer, together with any incidental ~~or consequential~~ damages provided in this Article (Section 2-710), ~~due allowance for costs reasonably incurred and due credit for payments or proceeds of resale.~~

### **Proposed Comment**

1. **Changes.** This section contains the following changes from original Section 2-708:

a) Consistent with the revision of Section 2-710, this section now provides for consequential as well as incidental damages. Subsection (1) has been divided into two paragraphs. The new paragraph, clarifies the measure of damages in anticipatory repudiation. The same approach has been taken in Section 2-713 on buyer's market-based damage claims.

b) Original Section 2-708(1) sets the measure of damages as the difference between the market price and the unpaid contract price. The word "unpaid" has been deleted as superfluous and misleading. An aggrieved buyer that has already paid a portion of the price is entitled to recover it in restitution under Section 2-718.

c) Original Section 2-708(1) measures damages by the difference between the resale price and the contract price. Subsection (1) of this draft reverses the terms ("difference between the contract price and the resale price") because the contract price must be the larger number in order for there to be direct damages. Compare Sections 2-712 and 2-713 on buyer's remedies, where the contract price is listed after the cover or market price.

d) Subsection (2) now has the following emphasized language added: "provided in subsection (1) or Section 2-706 is inadequate . . ." Most courts have correctly assumed that original Section 2-708(2) was an alternative to Section 2-706 as well as Section 2-708(1) but still have had to ask the question. See, e.g., R.E. Davis Chemical Corp. v. Diasonics, Inc., 826 F.2d 678 (7th Cir. 1987). The change makes this result explicit.

e) In subsection (2), the phrases that appeared in original 2-708(2), "due allowance for costs reasonably incurred" and "due credit for payments or proceeds of resale" have been deleted. As has been noted repeatedly (see, e.g., Harris, A General Theory for Measuring Seller's Damages for Total Breach of Contract, 60 Mich. L. Rev. 577 (1962)); the "due credit" language makes no sense for a seller that has lost a sale not because it ceased manufacture on a buyer's breach but because it has resold a finished product (that was made for its breaching buyer) to one its existing buyers. When a seller ceases manufacture and resells component parts for scrap or salvage value under Section 2-704(2), a credit for the proceeds is due the buyer to offset the damages under this section. And when a seller incurs costs that are not recovered by scrap or salvage, it must be given an "allowance" for those costs to measure its loss accurately. See E. Farnsworth Contracts Section 12.9 (3rd ed. 1999)(general measure of damages =

loss in value + other loss - cost avoided - loss avoided).

2. The right to damages under this section arises when a seller reclaims goods under Section 2-507 or a buyer repudiates or makes a wrongful but effective rejection. In addition, there is a right to damages under this Section if the buyer unjustifiably attempts to revoke acceptance and the seller takes back the goods. However, if the seller refuses to take the goods back in the face of the buyer's unjustifiable attempt to revoke acceptance, the appropriate remedy is an action for the price under Section 2-709.

3. The current market price at the time and place for tender is the standard by which damages for nonacceptance are to be determined. The time and place of tender is determined by Section 2-503 on tender of delivery and by the use of common shipping terms. The provisions of Section 2-723 are relevant in determining the market price.

In the event that there is no evidence available of the current market price at the time and place of tender, proof of a substitute market may be made as provided in Section 2-723. Furthermore, the section on the admissibility of market quotations is intended to ease materially the problem of providing competent evidence.

4. Subsection (1)(b) addresses the question of when the market price should be measured in the case of an anticipatory repudiation by the buyer. This section provides that the market price should be measured in a repudiation case at the place of tender under the agreement at a commercially reasonable time after the seller learned of the repudiation, but no later than the time of tender under the agreement. This time approximates the market price at the time the seller would have resold the goods, even though the seller has not done so under Section 2-706. In determining whether the seller has learned of the repudiation, the court should be sensitive to the rights of the aggrieved party when tactical behavior by the buyer has made the determination difficult. See Louisiana Power and Light v. Allegheny Ludlow, 517 F. Supp. 1319 (D.C.La. 1981).

In a long term contract the calculation of damages for repudiation will be complex. The court must first determine not only the market but also the contract price at the time of breach. Since contract prices in long term contracts are commonly escalated, the court will have to determine the escalated price at the time the aggrieved party learned of the repudiation. Next the court must determine the quantities contracted for in each of the succeeding years of the contract, apply the single difference between the market price and the escalated contract price (both prices determined at the time the aggrieved party learned of the repudiation) to the contracted quantity for each of those years, and discount those damages for each of the future years to a present value. See generally 1 J. White & R. Summers,

Uniform Commercial Code, Practitioner Ed. 4th 347 (1995).

5. Subsection (2) is used in the cases of uncompleted goods, jobbers or middlemen, and other lost-volume sellers. This remedy is an alternative to the remedy under subsection (1) or Section 2-706 and is available when the damages based upon resale of the goods or market price of the goods does not achieve the goal of full compensation for harm caused by the buyer's breach. No effort has been made to state how lost profits should be calculated because of the variety of situations in which this measurement may be appropriate and the variety of ways in which courts have measured lost profits. This subsection permits the recovery of lost profits in all appropriate cases. Since this section deals with the plaintiff's lost profit on a particular sale, and not with cases where a plaintiff is suing for the "lost profits" from an enterprise as consequential damages, it is not necessary to show a history of earnings; all that is necessary is that the plaintiff shows a loss of the marginal benefit to be gained from performance of the broken contract.

To qualify as a "lost volume" seller, the seller needs to show only that it could have supplied both the breaching purchaser and the resale purchaser with the goods. Islamic Republic of Iran v. Boeing Co., 771 F.2d 1279 (9th Cir. 1985). Where an aggrieved seller has sold goods made for the breaching party to another, courts should consider whether the seller could and would have made a profit on an additional sale in addition to the breached sale. If the Seller could not or would not have profitably made another sale in the absence of breach, there is no lost volume and the buyer would normally be made whole by a recovery of the incidental costs associated with the substitute transaction.

6. Consequential damages are not recoverable under this section unless seller has made reasonable attempts to minimize its damages in good faith, either by resale under Section 2-706 or by other reasonable means.

7. Where an agreement contains provisions for payment of a liquidated sum of money as an alternative to performance, (such take-or-pay contracts), a court must determine whether the agreement is truly for alternative performances or whether the alternatives are performance or liquidated damages. Recovery under this section is available when a buyer breaches an alternative performance contract. When the "alternative" is truly liquidated damages and when that damage provision complies with Section 2-718 recovery, is under the liquidated damage clause. See Roye Realty & Developing, Inc. v. Arkla, Inc., 863 P.2d 1150, 1154, 22 UCC2d 183 (Okla. 1993); 5A Corbin, Corbin on Contracts SECTION 1082, at 463-64 (1964).

8. In some cases an aggrieved party's resale should prevent that party from recovering the contract market difference under this section. If for example a seller does not lose a sale because of the buyer's breach and resells at a price equal to or in excess of the contract price, the seller should recover no more than incidental and consequential damages. To award an additional amount because the seller could show the market price was higher than the contract price would overcompensate the seller. Of course, a defendant, that wished so to limit a plaintiff seller, would have to prove the resale and show that it had the economic effect of limiting the aggrieved party's actual loss to an amount less than the contract market difference.

Whether a breaching party should be able to deprive an aggrieved party from the use of the contract market formulas on a showing that the aggrieved party's actual damages were less than the difference between the contract and the market prices has been much disputed in the academic literature and has not received a consistent answer from the courts. Compare Nobs Chemical USA Inc., v. Koppers Co. Inc., 616 F.2d 212 (5th Cir. 1980), reh'g denied 618 F.2d 1389 (5th Cir. 1980)(yes) and Allied Cannery & Packers, Inc. v. Victor Packing Co., 162 Cal. App.3d 905, 209 Cal. Rptr. 60 (1984)(yes) with Tongish v. Thomas, 840 P.2d 471 (Kan. 1992)(no). Even under the rule of Nobs Chemical, an aggrieved party should not be foreclosed from recovery of the contract market difference simply because that party chooses not to proceed with its transaction after the other party breaches. Trans World Metals, Inc. v. Southwire Co., 769 F.2d 902 (2d Cir. 1985). In most cases it will be difficult for a defendant buyer to show that an aggrieved seller's resale should foreclose recovery of the contract market difference under 2-708(1) or lost profit under 2-708(2). Since most commercial sellers would have made at least one additional sale had there had been no breach (the sale to the breaching buyer and the sale to the third party), the resale does not make the seller whole. Sometimes it may even be appropriate for a court to allow an aggrieved party to use a contract market formula in lieu of proof of its actual loss to preserve its business secrets. See Ben-Shahar and Bernstein, The Secrecy Interest in Contract Law, 109 Yale L. J. 1885 (2000).

#### **SECTION 2-709. ACTION FOR THE PRICE.**

(1) When the buyer fails to pay the price as it becomes due the seller may recover, together with any incidental or consequential damages under the next section, the price

(a) of goods accepted or of conforming goods lost or damaged within a commercially reasonable time after risk of their loss has passed to the buyer; and

(b) of goods identified to the contract if the seller is unable after reasonable effort to resell them at a reasonable price or the circumstances reasonably indicate that such effort will be unavailing.

(2) Where the seller sues for the price he the seller must hold for the buyer any goods which have been identified to the contract and are still in his the seller's control except that if resale becomes possible he the seller may resell them at any time prior to the collection of the judgment. The net proceeds of any such resale must be credited to the buyer and payment of the judgment entitles him the buyer to any goods not resold.

(3) After the buyer has wrongfully rejected or revoked acceptance of the goods or has failed to make a payment due or has repudiated (Section 2-610), a seller who that is held not entitled to the price under this section shall nevertheless be awarded damages for non-acceptance under the preceding section.

#### **Proposed Comment**

Subsection (1) has been amended to permit recovery of consequential damages as provided in amended Section 2-710.

#### **SECTION 2-710. SELLER'S INCIDENTAL AND CONSEQUENTIAL DAMAGES.**

(1) Incidental damages to an aggrieved seller include any commercially reasonable charges, expenses or commissions incurred in stopping delivery, in the transportation, care and custody of goods after the buyer's breach, in connection with return or resale of the goods or otherwise resulting from the breach.

(2) Consequential damages resulting from the buyer's breach include any loss resulting from general or particular requirements and needs of which the buyer at the time of contracting had reason to know and which could not reasonably be prevented by resale or otherwise.

(3) In a consumer contract, a seller may not recover consequential damages from a consumer.

#### **Proposed Comment**

1. Subsection (2), which permits an aggrieved seller to recover consequential damages, is based on Section 2-715(2)(a); that is, the loss must result from general or particular requirements of the seller of which the buyer had reason to know at the time of contracting. As with Section 2-715, the "tacit agreement" test is rejected and the buyer is not liable for losses that could have been mitigated.

Sellers rarely suffer compensable consequential damages. A buyer's usual default is failure to pay. In normal circumstances the disappointed seller will be able to sell to another, borrow to replace the

breaching buyer's promised payment, or otherwise adjust its affairs to avoid consequential loss. cf. Afram Export Corp. v. Metallurgiki Halypis, S.A., 772 F.2d 1358, 1368 (7<sup>th</sup> Cir. 1985).

2. Subsection (3) precludes seller's from recovering consequential damages from consumers. This provision is nonwaivable.

#### **SECTION 2-711. BUYER'S REMEDIES IN GENERAL; BUYER'S SECURITY INTEREST IN REJECTED GOODS.**

~~(1) Where the seller fails to make delivery or repudiates or the buyer rightfully rejects or justifiably revokes acceptance then with respect to any goods involved, and with respect to the whole if the breach goes to the whole contract (Section 2-612), the buyer may cancel and whether or not he has done so may in addition to recovering so much of the price as has been paid~~

~~(a) "cover" and have damages under the next section as to all the goods affected whether or not they have been identified to the contract; or~~

~~(b) recover damages for non-delivery as provided in this Article (Section 2-713).~~

~~(2) Where the seller fails to deliver or repudiates the buyer may also~~

~~(a) if the goods have been identified recover them as provided in this Article (Section 2-502); or~~

~~(b) in a proper case obtain specific performance or replevy the goods as provided in this Article (Section 2-716).~~

(1) A breach of contract by the seller includes the seller's wrongful failure to deliver or to perform a contractual obligation, making of a nonconforming tender of delivery or performance, or repudiation.

(2) If the seller is in breach of contract under subsection (1) the buyer may to the extent provided for by this Act or other law:

(a) in the case of rightful cancellation, rightful rejection or justifiable revocation of acceptance recover so much of the price as has been paid;

(b) deduct damages from any part of the price still due under Section 2-717;

(c) cancel;

(d) cover and have damages under Section 2-712 as to all goods affected whether or not they have been identified to the contract;

(e) recover damages for non-delivery or repudiation under Section 2-713;

(f) recover damages for breach with regard to accepted goods or breach with regard to a remedial promise under Section 2-714;

(g) recover identified goods under Section 2-502;

(h) obtain specific performance or obtain the goods by replevin or the like under Section 2-716;

(i) recover liquidated damages under Section 2-718;

(j) in other cases, recover damages in any manner that is reasonable under the circumstances.

(3) On rightful rejection or justifiable revocation of acceptance a buyer has a security interest in goods in ~~his~~ the buyer's possession or control for any payments made on their price and any expenses reasonably incurred in their inspection, receipt, transportation, care and custody and may hold such goods and resell them in like manner as an aggrieved seller (Section 2-706).

#### **Proposed Comment**

1. Despite the seller's breach, proper tender of delivery under the section on cure of improper tender or replacement can effectively preclude the buyer's remedies under this section, except for any delay involved.

2. To make it clear in subsection (3) that the buyer may hold and resell rejected goods if the buyer has paid a part of the price or incurred expenses of the type specified. "Paid" as used here includes acceptance of a draft or other time negotiable instrument or the signing of a negotiable note. The buyer's freedom of resale is coextensive with that of a seller under this Article except that the buyer may not keep any profit resulting from the resale and is limited to retaining only the amount of the price paid and the costs involved in the inspection and handing of the goods. The buyer's security interest in the goods is intended to be limited to the items listed in subsection (c), and the buyer is not permitted to retain such funds as the buyer might believe adequate for his damages. The buyer's right to cover, or to have damages for non-delivery, is not impaired by the buyer's exercise of the right of resale.

3. It should also be noted that this Act requires its remedies to be liberally administered and provides that any right or obligation which it declares is enforceable by action unless a different effect is specifically prescribed (Section 1-106).

#### **SECTION 2-712. "COVER"; BUYER'S PROCUREMENT OF SUBSTITUTE GOODS.**

(1) ~~After a breach within the preceding section~~ If the seller wrongfully fails to deliver or repudiates or the buyer rightfully rejects or justifiably revokes acceptance, the buyer may "cover" by making in good faith and without unreasonable delay any reasonable purchase of or contract to purchase goods in substitution for those due from the seller.

(2) The buyer may recover from the seller as damages the difference between the cost of cover and the contract price together with any incidental or consequential damages as hereinafter defined (Section 2-715), but less expenses saved in consequence of the seller's breach.

(3) Failure of the buyer to effect cover within this section does not bar ~~him~~ the buyer from any other remedy.

#### **Proposed Comment**

1. **Changes.** Original Section 2-712(1) refers to a seller's "breach" as the basis for the remedy in this section. The language has been changed to make it clear that there is a right to cover "[i]f the seller wrongfully fails to deliver or repudiates or the buyer rightfully rejects or justifiably revokes acceptance."

2. The purpose of this section is to provide the buyer with a remedy to enable the buyer to obtain the goods the buyer is entitled to under the contract with the seller. This remedy is the buyer's equivalent of the seller's right to resell.

The buyer is entitled to this remedy if the seller wrongfully fails to deliver the goods or repudiates the contract or if the buyer rightfully rejects or justifiably revokes acceptance. Cover is not available under this section if the buyer accepts the goods and does not rightfully revoke the acceptance.

3. Subsection (2) allows a buyer that has appropriately covered to measure damages by the difference

between the cover price and the contract price. In addition, the buyer is entitled to incidental damages, and when appropriate, consequential damages under Section 2-715.

4. The definition of "cover" is necessarily flexible, and therefore cover includes a series of contracts or sales as well as a single contract or sale, goods not identical with those involved but commercially usable as reasonable substitutes under the circumstances, and contracts on credit or delivery terms differing from the contract in breach but reasonable under the circumstances. The test of proper cover is whether at the time and place of cover the buyer acted in good faith and in a reasonable manner. It is immaterial that hindsight may later prove that the method of cover used was not the cheapest or most effective.

5. The requirement in subsection (1) that the buyer must cover "without unreasonable delay" is not intended to limit the time necessary for the buyer to examine reasonable options and decide how best to effect cover.

6. Subsection (3) expresses the policy that cover is not a mandatory remedy for the buyer. The buyer is always free to choose between cover and damages for nondelivery under Section 2-713. However, this subsection must be read in conjunction with the section 2-715(2)(a), which limits the recovery of consequential damages to those damages that could not reasonably be prevented by cover. Moreover, the operation of Section 2-716(3) on replevin and the like must be considered because the inability to cover is made an express condition to the right of the buyer to replevy the goods.

#### **SECTION 2-713. BUYER'S DAMAGES FOR NON-DELIVERY OR REPUDIATION.**

(1) Subject to the provisions of this Article with respect to proof of market price (Section 2-723), if the seller wrongfully fails to deliver or repudiates or the buyer rightfully rejects or justifiably revokes acceptance

(a) the measure of damages for non-delivery or repudiation in the case of wrongful failure to deliver by the seller or rightful rejection or justifiable revocation of acceptance by the buyer is the difference between the market price at the time when the buyer learned of the breach for tender under the contract and the contract price together with any incidental and or consequential damages provided in this Article (Section 2-715), but less expenses saved in consequence of the seller's breach: breach; and

(b) the measure of damages for repudiation by the seller is the difference between the market price at the expiration of a commercially reasonable time after the buyer learned of the repudiation, but no later than the time stated in paragraph (a), and the contract price together with any incidental or consequential damages provided in this Article (Section 2-715), but less expenses saved in consequence of the seller's breach.

(2) Market price is to be determined as of the place for tender or, in cases of rejection after arrival or revocation of acceptance, as of the place of arrival.

#### **Proposed Comment**

1. **Changes.** This section now provides a rule for anticipatory repudiation cases. This is consistent with the new rule for sellers in Section 2-708(1)(b). In a case not involving repudiation, the buyer's damages will be based on the market price at the time for tender under the agreement. This changes the former rule where the time for measuring damages was at the time the buyer learned of the breach.

2. This section provides for a buyer's expectancy damages when the seller wrongfully fails to deliver the goods or repudiates the contract or the buyer rightfully rejects or justifiably revokes acceptance. This section provides an alternative measure of damages to the cover remedy provided for in Section 2-712.

3. Under subsection (1)(a), the measure of damages for a wrongful failure to deliver the goods by the seller or a rightful rejection or justifiable revocation of acceptance by the buyer is the difference between the market price at the time for tender under the agreement and the contract price.

4. Subsection (2)(b) addresses the question when the market price should be measured in the case of an anticipatory repudiation by the seller. The market price should be measured in a repudiation case at the place where the buyer would have covered at a commercially reasonable time after the buyer learned of the repudiation, but no later than the time of tender under the agreement. This time approximates the market price at the time the buyer would have covered even though the buyer has not done so under Section 2-712. This subsection is designed to put the buyer in the position the buyer would have been in if the seller had performed by approximating the harm the buyer has suffered without allowing the buyer an unreasonable time to speculate on the market at the seller's expense.

5. The market or current price to be used in comparison with the contract price under this section is the price for goods of the same kind and in the same branch of trade.

When the current market price under this section is difficult to prove, Section 2-723 on determination and proof of market price is available to permit a showing of a comparable market price. When no market price is available, evidence of spot sale prices may be used to determine damages under this section. When the unavailability of a market price is caused by a scarcity of goods of the type involved, a good case may be made for specific performance under Section 2-716. See the Proposed Comment to that Section. For a discussion of the issues associated with long term contracts see the comments to 2-708.

6. In addition to the damages provides in this section, the buyer is entitled to incidental and consequential damages under Section 2-715.

7. A buyer that has covered may not recover the contract market difference under this section. If for example a construction company that intended to buy only one bulldozer covered by buying a bulldozer from a third party at or below the contract price after a seller's breach, the buyer should recover no more than incidental and consequential damages. To award an additional amount because the buyer could show the market price was higher than the contract price would put the buyer in a better position than performance would have. Of course, the seller would bear the burden of proving that cover had the economic effect of limiting the buyer's actual loss to an amount less than the contract market difference.

An apparent cover, which does not in fact replace the goods contracted for, should not foreclose the use of the contract market measure of damages. If, for example, the buyer intended to buy an undetermined number of bulldozers, the purchase of a bulldozer from a third party after breach would not necessarily reduce the buyer's damages. If the breaching seller cannot prove that the new purchase is in fact a replacement for the one not delivered under the contract, the "cover" purchase should not foreclose the buyer's recovery under 2-713 of the market contract difference.

For a discussion of the question when an aggrieved party should be foreclosed from a contract market recover because of its cover or resale, see the Proposed Comments to 2-708.

#### **SECTION 2-714. BUYER'S DAMAGES FOR BREACH IN REGARD TO ACCEPTED GOODS.**

(1) Where the buyer has accepted goods and given notification (subsection (3) of Section 2-607) he the buyer may recover as damages for any non-conformity of tender the loss resulting in the ordinary course of events from the seller's breach as determined in any manner which is reasonable.

(2) The measure of damages for breach of warranty is the difference at the time and place of acceptance between the value of the goods accepted and the value they would have had if they had been as warranted, unless special circumstances show proximate damages of a different amount.

(3) In a proper case any incidental and consequential damages under the next section may also be recovered.

#### **SECTION 2-716. BUYER'S RIGHT TO SPECIFIC PERFORMANCE OR; BUYER'S RIGHT REPLEVIN.**

(1) Specific performance may be decreed where the goods are unique or in other proper circumstances. In a contract other than a consumer contract, specific performance may be decreed if the parties have agreed to that remedy. However, even if the parties agree to specific performance, specific performance may not be decreed if the breaching party's sole remaining contractual obligation is the payment of money.

(2) The decree for specific performance may include such terms and conditions as to payment of the price, damages, or other relief as the court may deem just.

(3) The buyer has a right of replevin or the like for goods identified to the contract if after reasonable effort he the buyer is unable to effect cover for such goods or the circumstances reasonably indicate that such effort will be unavailing or if the goods have been shipped under reservation and satisfaction of the security interest in them has been made or tendered.

(4) The buyer's right under subsection (3) vests upon acquisition of a special property, even if the seller had not then repudiated or failed to deliver.

#### **Proposed Comment**

1. Changes: This section contains the following changes from original Section 2-716:

a) The caption has been amended to make it clear that either party may entitled to specific performance.

b) The second sentence of subsection (1) explicitly permits parties to bind themselves to specific

performance even where it would not otherwise be available.

c) In subsection (3), the phrase "or the like" has been added after "replevin" to reflect the fact that under the governing state law the right may be called "detinue," "sequestration," "claim and delivery," or something else.

d) Subsection (4) is new and corresponds with Section 2-502(b), which in turn is derived from (but broader than) the conforming amendments to Article 9. It provides a vesting rule for cases in which there is a right of replevin.

2. Uniqueness should be determined in light of the total circumstances surrounding the contract and is not limited to goods identified when the contract is formed. The typical specific performance situation today involves an output or requirements contract rather than a contract for the sale of an heirloom or priceless work of art. A buyer's inability to cover is evidence of "other proper circumstances."

3. Subsection (1) provides that a court may decree specific performance if the parties have agreed to that remedy; the parties' agreement to specific performance can be enforced even if legal remedies are entirely adequate. Even in a commercial contract, the third sentence of subsection (1) prevents the aggrieved party from obtaining specific performance if the only obligation of the party in breach is the payment of money. Whether a buyer is obligated to pay the price is determined by Section 2-709, not by this section.

Nothing in this section constrains the court's exercise of its equitable discretion in deciding whether to enter a decree for specific performance or in determining the conditions or terms of such a decree. This section assumes that the decree for specific performance will be conditioned on a tender of full performance by the party that is seeking the remedy.

4. The legal remedy of replevin or the like is also available for cases in which cover is unavailable and the goods have been identified to the contract. This is in addition to the prepaying buyer's right to recover identified goods upon the seller's insolvency or, when the goods have been bought for a personal, family, or household purpose, upon the seller's repudiation or failure to deliver (Section 2-502). If a negotiable document of title is outstanding, the buyer's right of replevin relates to the

document and does not directly relate to the goods. See Article 7, especially Section 7-602.

5. Subsection (4) provides that a buyer's right to replevin or the like vests upon the buyer's acquisition of a special property in the goods (Section 2-501) even if the seller has not at that time repudiated or failed to make a required delivery. This vesting rule assumes application of a "first in time" priority rule. In other words, if the buyer's rights vest under this rule before a creditor acquires an *in rem* right to the goods, including an Article 9 security interest and a lien created by levy, the buyer should prevail.

#### **SECTION 2-717. DEDUCTION OF DAMAGES FROM THE PRICE.**

The buyer on notifying the seller of his an intention to do so may deduct all or any part of the damages resulting from any breach of the contract from any part of the price still due under the same contract.

#### **SECTION 2-718. LIQUIDATION OR LIMITATION OF DAMAGES; DEPOSITS.**

(1) Damages for breach by either party may be liquidated in the agreement but only at an amount which is reasonable in the light of the anticipated or actual harm caused by the breach and, in a consumer contract, the difficulties of proof of loss, loss and the inconvenience or nonfeasibility of otherwise obtaining an adequate remedy. A term fixing unreasonably large liquidated damages is void as a penalty. Section 2-719 determines the enforceability of a term that limits but does not liquidate damages.

(2) Where the seller justifiably withholds delivery of goods or stops performance because of the buyer's breach or insolvency, the buyer is entitled to restitution of any amount by which the sum of his the buyer's payments exceeds (a) the amount to which the seller is entitled by virtue of terms liquidating the seller's damages in accordance with subsection (1); or (b) in the absence of such terms, twenty per cent of the value of the total performance for which the buyer is obligated under the contract or \$500, whichever is smaller.

(3) The buyer's right to restitution under subsection (2) is subject to offset to the extent that the seller establishes

(a) a right to recover damages under the provisions of this Article other than subsection (1), and

(b) the amount or value of any benefits received by the buyer directly or indirectly by reason of the contract.

(4) Where a seller has received payment in goods their reasonable value or the proceeds of their resale shall be treated as payments for the purposes of subsection (2); but if the seller has notice of the buyer's breach before reselling goods received in part performance, ~~his~~ the resale is subject to the conditions laid down in this Article on resale by an aggrieved seller (Section 2-706).

### **Proposed Comment**

1. **Changes:** This section contains the following changes from original Section 2-718:

a) In subsection (a), the requirements that the party seeking to enforce a term liquidating damages demonstrate "difficulties of proof of loss" and "inconvenience or nonfeasibility of otherwise obtaining an adequate remedy" have been eliminated in commercial contracts.

b) In subsection (a), the sentence "[a] term fixing unreasonably large liquidated damages is void as a penalty" has been eliminated as unnecessary and capable of causing confusion.

c) The last sentence of subsection (a) has been added to clarify the relationship between this section and Section 2-719.

d) In subsection (b), the circumstances in which restitution is available have been expanded to cover any situation where the seller stops performance on account of the buyer's breach or insolvency.

e) In subsection (b), the buyer's right to restitution is not limited by a statutory liquidated damages provision.

2. A valid liquidated damages term may liquidate the amount of all damages, including consequential and incidental damages. As under former law, liquidated damages clauses should be enforced if the amount is reasonable in light of the factors provided in subsection (a). This section thus respects the parties' ability to contract for damages while providing some control by requiring reasonableness based upon the circumstances of the particular case.

Under original Section 2-718, a party seeking to enforce a liquidated damages term had to demonstrate the difficulty of proving the loss and the inconvenience or nonfeasibility of obtaining an adequate remedy. These tests have been eliminated in commercial contracts but retained in consumer contracts.

3. The sentence from original Section 2-718(1) stating that an unreasonably large liquidated damages term is void as a penalty has been eliminated as unnecessary and misleading. If the liquidated damages are reasonable in light of the test of subsection (a), the term should be enforced, rendering the penalty language of the former law redundant. The sentence is also misleading because of its emphasis on unreasonably large damages. A liquidated damages term providing for damages that are unreasonably small under the test of subsection (a) is likewise unenforceable.

4. If a liquidated damages term is unenforceable, the remedies of this Article become available to the aggrieved party.

5. Under subsection (b), only the buyer's payments that are more than the amount of an enforceable liquidated damages term need be returned to the buyer. If the buyer has made payment by virtue of a trade-in or other goods deposited with the seller, subsection (d) provides that the reasonable value of such goods or their resale price should be used to determine what the buyer has paid, not the value the seller allowed the buyer in the trade-in. To assure that the seller obtains a reasonable price for such goods, the seller must comply with the resale provisions of Section 2-706 if the seller knows of the buyer's breach before it has otherwise resold them.

Subsection (b) expands the situations in which restitution is available. Original Section 2-718(2) was limited to circumstances in which the seller justifiably withheld delivery because of the buyer's breach. Subsection (b) extends the right to situations where the seller stops performance because of the buyer's breach or insolvency.

6. Subsection (c) continues the rule from former law without change. If there is no enforceable liquidated damages term, the buyer is entitled to restitution under subsection (b) subject to a set off of the seller for any damages to which it is otherwise entitled to under this Article.

**SECTION 2-722. WHO CAN SUE THIRD PARTIES FOR INJURY TO GOODS.** Where a third party so deals with goods which have been identified to a contract for sale as to cause actionable injury to a party to that contract

(a) a right of action against the third party is in either party to the contract for sale ~~who that~~ has title to or a security interest or a special property or an insurable interest in the goods; and if the goods have been destroyed or converted a right of action is also in the party ~~who that~~ either bore the risk of loss under the contract for sale or has since the injury assumed that risk as against the other;

(b) if at the time of the injury the party plaintiff did not bear the risk of loss as against the other party to the contract for sale and there is no arrangement between them for disposition of the recovery, ~~his the~~ party plaintiff's suit or settlement is, subject to ~~his its~~ its own interest, as a fiduciary for the other party to the contract;

(c) either party may with the consent of the other sue for the benefit of ~~whom which~~ which it may concern.

**SECTION 2-723. PROOF OF MARKET: TIME AND PLACE.**

~~(1) If an action based on anticipatory repudiation comes to trial before the time for performance with respect to some or all of the goods, any damages based on market price (Section 2-708 or Section 2-713) shall be determined according to the price of such goods prevailing at the time when the aggrieved party learned of the repudiation.~~

~~(2)~~ (1) If evidence of a price prevailing at the times or places described in this Article is not readily available the price prevailing within any reasonable time before or after the time described or at any other place which in commercial judgment or under usage of trade would serve as a reasonable substitute for the one described may be used, making any proper allowance for the cost of transporting the goods to or from such other place.

~~(3)~~ (2) Evidence of a relevant price prevailing at a time or place other than the one described in this Article offered by one party is not admissible unless and until he has given the other party such notice as the court finds sufficient to prevent unfair surprise.

**Proposed Comment**

Subsection (1) has been deleted because Sections 2-708(1)(b) and 2-713(1)(b) now provide the rule for the proper measure of damages in cases of repudiation.

**SECTION 2-724. ADMISSIBILITY OF MARKET QUOTATIONS.** Whenever the prevailing price or value of any goods regularly bought and sold in any established commodity market is in issue, reports in official publications or trade journals or in newspapers ~~or periodicals~~ periodicals or other means of communication in of general circulation published as the reports of such market shall be admissible in evidence. The circumstances of the preparation of such a report may be shown to affect its weight but not its admissibility.

**Proposed Comment**

The addition of "other means of communication" reflects the common use of non-paper media.

**SECTION 2-725. STATUTE OF LIMITATIONS IN CONTRACTS FOR SALE.**

~~(1) An action for breach of any contract for sale must be commenced within four years after the cause of action has accrued. By the original agreement the parties may reduce the period of limitation to not less than one year but may not extend it.~~

~~(2) A cause of action accrues when the breach occurs, regardless of the aggrieved party's lack of knowledge of the breach. A breach of warranty occurs when tender of delivery is made, except that where a warranty explicitly extends to future performance of the goods and discovery of the breach must await the time of such performance the cause of action accrues when the breach is or should have been discovered.~~

(1) Except as otherwise provided in this section, an action for breach of any contract for sale must be commenced within the later of four years after the right of action has accrued under subsection (2) or (3) or one year after the breach was or should have been discovered, but no longer than five years after the right of action accrued. By the original agreement the parties may reduce the period of limitation to not less than one year but may not extend it; however, in a consumer contract, the period of limitation may not be reduced.

(2) Except as otherwise provided in subsection (3), the following rules apply:

(a) Except as otherwise provided in this subsection, a right of action for breach of a contract accrues when the breach occurs, even if the aggrieved party did not have knowledge of the breach.

(b) For breach of a contract by repudiation, a right of action accrues at the earlier of when the aggrieved party elects to treat the repudiation as a breach or when a commercially reasonable time for awaiting performance has expired.

(c) For breach of a remedial promise, a right of action accrues when the remedial promise is not performed when due.

(d) In an action by a buyer against a person that is answerable over to the buyer for a claim asserted against the buyer, the buyer's right of action against the person answerable over accrues at the time the claim was originally asserted against the buyer.

(3) If a breach of a warranty arising under Section 2-312, 2-313(2), 2-314, or 2-315, or a breach of an obligation other than a remedial promise arising under Section 2-313A or 2-313B, is claimed the following rules apply:

(a) Except as otherwise provided in paragraph (c), a right of action for breach of a warranty arising under Section 2-313(2), 2-314 or 2-315 accrues when the seller has tendered delivery to the immediate buyer, as defined in Section 2-313, and has completed performance of any agreed installation or assembly of the goods.

(b) Except as otherwise provided in paragraph (c), a right of action for breach of an obligation other than a remedial promise arising under Section 2-313A or 2-313B accrues when the remote purchaser, as defined in sections 2-313A and 2-313B, receives the goods.

(c) Where a warranty arising under Section 2-313(2) or an obligation other than a remedial promise arising under 2-313A or 2-313B explicitly extends to future performance of the goods and discovery of the breach must await the time for performance the right of action accrues when the immediate buyer as defined in Section 2-313 or the remote purchaser as defined in Sections 2-313A and 2-313B discovers or should have discovered the breach.

(d) A right of action for breach of warranty arising under Section 2-312 accrues when the aggrieved party discovers or should have discovered the breach. However, an action for breach of the warranty of non-infringement may not be commenced more than six years after tender of delivery of the goods to the aggrieved party.

(3) (4) Where an action commenced within the time limited by subsection (1) is so terminated as to leave available a remedy by another action for the same breach such other action may be commenced after the expiration of the time limited and within six months after the termination of the first action unless the termination resulted from voluntary discontinuance or from dismissal for failure or neglect to prosecute.

(4) (5) This section does not alter the law on tolling of the statute of limitations nor does it apply to causes of action which have accrued before this Act becomes effective.

### **Proposed Comment**

1. Original Section 2-725 has been changed as follows: 1) The basic four-year limitation period in subsection (1) has been supplemented by a discovery rule that permits a cause of action to be brought within one year after the breach was or should have been discovered, although no later than five years after the time the cause would otherwise have accrued; 2) The applicable limitation period cannot be reduced in a consumer contract (subsection (1)); 3) Subsection (2) contains specific rules for cases of repudiation, breach of a remedial promise, and actions where another person is answerable over; 4) Subsection (3)(a) provides that the limitation period for breach of warranty accrues when tender of delivery has occurred and the seller has completed any agreed installation or assembly of the goods; 5) Subsection (3) contains specific rules for breach of an obligation arising under Section 2-313A or 2-313B, for breach of a warranty arising under Section 2-312, and for breach of a warranty against infringement.

2. Subsection (1) continues the four-year limitation period of original Article 2 but provides for a possible one-year extension to accommodate a discovery of the breach late in the four year period after accrual. The four year period under this Article is shorter than many other statutes of limitation for breach of contract and provides a period which is appropriate given the nature of the contracts under this Article and modern business practices. As under original Article 2, the period of limitation can be reduced to one year by an agreement in a commercial contract, but no reduction is permitted in consumer contracts.

3. Subsections (2) and (3) provide rules for accrual of the various types of action that this Article allows. Certainty of commercial relationships is advanced when the rules are clearly set forth. Subsection (2) deals with accrual rules for actions other than for breach of a warranty, including actions based on repudiation or breach of a remedial promise and actions where another person is answerable over. Subsection (3) deals with the accrual rules for the various claims based on a warranty, including a warranty of title and a warranty against infringement, or on an obligation other than a remedial promise arising under Section 2-313A or 2-313B.

Subsection (2)(a) states the general rule from prior law that a right of action for breach of contract accrues when the breach occurs without regard to the aggrieved party's knowledge of the breach. This general rule is then subject to the three more explicit rules in subsection (2) and to the rules for breach of warranty stated in subsection (3).

Subsection (2)(b) provides an explicit rule about repudiation cases. In a repudiation, the aggrieved party may await performance for a commercially reasonable time or resort to any remedy for breach. Section 2-610. The accrual rule for breach of contract in a repudiation case is keyed to the earlier of those two

time periods.

Subsection (2)(c) provides that a cause of action for breach of a remedial promise accrues when the promise is not performed at the time performance is due.

Subsection (2)(d) addresses the problem that has arisen in the cases when an intermediary party is sued for a breach of obligation for which its seller or another person is answerable over, but the limitations period in the upstream lawsuit has already expired. This subsection allows a party four years, or if reduced in the agreement, not less than one year, from when the claim is originally asserted against the buyer for the buyer to sue the person that is answerable over. Whether a party is in fact answerable over to the buyer is not addressed in this section.

4. Subsection (3) addresses the accrual rules for breach of a warranty arising under Section 2-312, 2-313 (2), 2-314 or 2-315, or of an obligation other than a remedial promise arising under Section 2-313A or 2-313B. The subsection does not apply to remedial promises arising under Section 2-313(4); all remedial promises are governed by subsection 2(c). The accrual rules explicitly incorporate the definitions of "immediate buyer" and "remote purchaser" in Sections 2-313, 2-313A and 2-313B. Any cause of action brought by another person to which the warranty or obligation extends is derivative in nature. Thus, the time period applicable to the immediate buyer or remote purchaser governs even if the action is brought by a person to which the warranty or obligation extends under Section 2-318.

Subsection (3)(a) continues the general rule that an action for breach of warranty accrues in the case of an express or implied warranty to an immediate buyer upon completion of tender of delivery of nonconforming goods to the immediate buyer but makes explicit that accrual is deferred until the completion of any installation or assembly that the seller has agreed to undertake. This extension of the time of accrual in the case of installation or assembly applies only in the case of the seller promising to install or assemble and not in the case of a third party, independent of the seller, undertaking that action.

Subsection (3)(b) addresses the accrual of a cause of action for breach of an obligation other than a remedial promise arising under Section 2-313A or 2-313B. In these cases, the cause of action accrues when the remote purchaser (as defined in those sections) receives the goods. This accrual rule balances the rights of the remote buyer or remote lessee to be able to have a cause of action based upon the warranty obligation the seller has created against the rights of the seller to have some limit on the length of time the seller is liable.

Both of these accrual rules are subject to the exception in subsection (3)(c) for a warranty or obligation that explicitly extends to the future performance of the goods and discovery of the breach must await the time for performance. In this case, the cause of action does not accrue until the buyer or remote purchaser discovers or should have discovered the breach.

With regard to a warranty of title or a warranty of non-infringement under Section 2-312, subsection (3) (d) provides that a cause of action accrues when the aggrieved party discovers or should have discovered the breach. In a typical case, the aggrieved party will not discover the breach until it is sued by a party asserting title to the goods or an infringement, an event which could be many years after the buyer acquired the goods. The accrual rule allows the aggrieved party appropriate leeway to then bring a claim against the person that made the warranty. In recognition of a need to have a time of repose in an infringement case, a party may not bring an action based upon a warranty of non-infringement more than six years after tender of delivery.

5. Subsection (4) states the saving provision included in many state statutes and permits an additional short period for bringing new actions where suits begun within the four year period have been terminated so as to leave a remedy still available for the same breach.

6. Subsection (5) makes it clear that this Article does not purport to alter or modify in any respect the law on tolling of the Statute of Limitations as it now prevails in the various jurisdictions.

## **PART 8**

### **TRANSITION PROVISIONS**

#### **SECTION 2-801. EFFECTIVE DATE.**

This [Act] shall become effective on , 20 .

**SECTION 2-802. AMENDMENT OF EXISTING ARTICLE 2.**

This [Act] amends [insert citation to existing Article 2].

**SECTION 2-803. APPLICABILITY.**

This [Act] applies to a transaction within its scope that is entered into on or after the effective date of this [Act]. This [Act] does not apply to a transaction that is entered into before the effective date of this [Act] even if the transaction would be subject to this [Act] if it had been entered into after the effective date of this [Act]. This [Act] does not apply to a cause of action that has accrued before the effective date of this [Act]. Section 2-313B of this [Act] does not apply to an advertisement of similar communication made before the effective date of this [Act].

**SECTION 2-804. SAVINGS CLAUSE.**

A transaction entered into before the effective date of this [Act] and the rights, obligations, and interests flowing from that transaction are governed by any statute or other law amended or repealed by this [Act] as if amendment or repeal had not occurred and may be terminated, completed, consummated, or enforced under that statute or other law.

# UCC Laws Study Group

## REVISED ARTICLE 1 OF THE UCC

Mississippi Secretary of State  
Policy and Research Division  
June 2009



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DELBERT HOSEMANN  
*Secretary of State*

# Background: Uniform Law Commission

- The Uniform Law Commission (ULC) is a non-profit, unincorporated association organized in 1892 to promote uniformity in state laws.
- It is comprised of commissioners appointed by each state and territory. Each commissioner must be a member of the bar.
- Commissioners draft model statutes to encourage the uniformity of law amongst the states.



# Background: Uniform Commercial Code

- First published in 1952 and is considered the ULC's greatest contribution to American law
- Provides for uniformity in state laws governing commercial transactions
- All 50 states and D.C. have enacted a version of the code (Louisiana has not adopted UCC Article 2 governing sales)
- Since it was first promulgated, the entire Code has been revised and amended several times



# What is Article 1?

Article 1 of the Uniform Commercial Code (UCC) provides definitions and general provisions which, in the absence of conflicting provisions, apply as default rules covering transactions and matters otherwise covered under a different article of the UCC.



# Purpose of the Revision

Between 1985 and 2003, the other articles of the UCC have been revised in their entirety. Revised Article 1 is necessary to address these revisions and reflect the most recent developments in commercial law.



# State Adoptions

Thirty-six (36) states have adopted revised Article 1

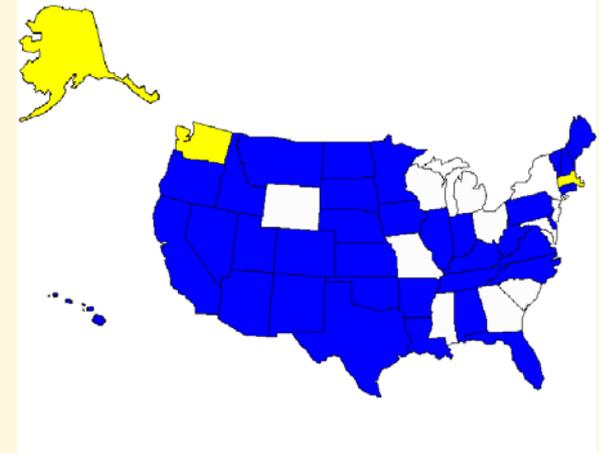
Alabama  
Arizona  
Arkansas  
California  
Colorado  
Connecticut  
Delaware  
Florida  
Hawaii  
Idaho  
Illinois  
Indiana  
Iowa  
Kansas  
Kentucky

Louisiana  
Maine  
Minnesota  
Montana  
Nebraska  
Nevada  
New Hampshire  
New Mexico  
North Carolina  
North Dakota  
Oklahoma  
Oregon  
Pennsylvania  
Rhode Island  
South Dakota

Tennessee  
Texas  
U.S. Virgin Islands  
Utah  
Vermont  
Virginia  
West Virginia

## INTRODUCED 2009

Alaska  
Massachusetts  
Washington



# Improvements in Revised Article 1

1. Modernization
2. Narrowed Scope
3. Clarification on when Non-UCC rules apply
4. Updated definition of Good Faith
5. Broader choice of law provision
6. Addition of Course of Performance
7. Deletion of certain provisions concerning the Statute of Frauds



# Substantive Changes

## Narrowed Scope

Section 1-102 now expressly states that the substantive rules of Article 1 apply only to transactions within the scope of the UCC. The Statute of Frauds provision aimed at transactions beyond the UCC has been deleted.



# Substantive Changes

## Application of Non-UCC Rules

Section 1-103 clarifies the application of supplemental principles of law, with clearer distinctions about where the UCC is preemptive.



# Substantive Changes

## Good Faith

In § 1-201, the definition of “good faith” is revised to say “honesty in fact and the observance of reasonable commercial standards of fair dealing”. This change conforms to the definition of good faith that applies in all of the recently revised UCC articles except Revised Article 5.



# Substantive Changes

## Course of Performance

Evidence of “course of performance,” currently only applicable to sales transactions under Article 2 and 2A, may now be used to interpret all contracts along with course of dealing and usage of trade.



# Substantive Changes

## Choice of Law Provision

Previously, parties could elect to use the law of any jurisdiction bearing a reasonable relation to the transaction. New § 1-301 permits parties to use the law of any state, or for international transactions, any country even if it does not bear a reasonable relation to the transaction.



# Variations in Existing Mississippi Law

## Mississippi Choice of Law Provision

Existing MS UCC §1-105 has unique non-uniform provisions which mandate that MS law always governs the rights and duties of parties in regard to:

1. Disclaimers of the implied warranty of merchantability
2. Limitations on remedies for breach of the implied warranty of merchantability
3. Requirements of privity in order to maintain a civil action for breach of the implied warranty of merchantability



# Why MS Should Adopt Revised Article 1

- Modernize existing commercial law
- Address substantive revisions to other Articles
- Clarify the application of Non-UCC rules to UCC transactions
- Update the definition of Good Faith and add Course of Performance
- Afford businesses and consumers a broader choice of law



# UCC Laws Study Group

- Conclusion
- Questions





# DELBERT HOSEMANN

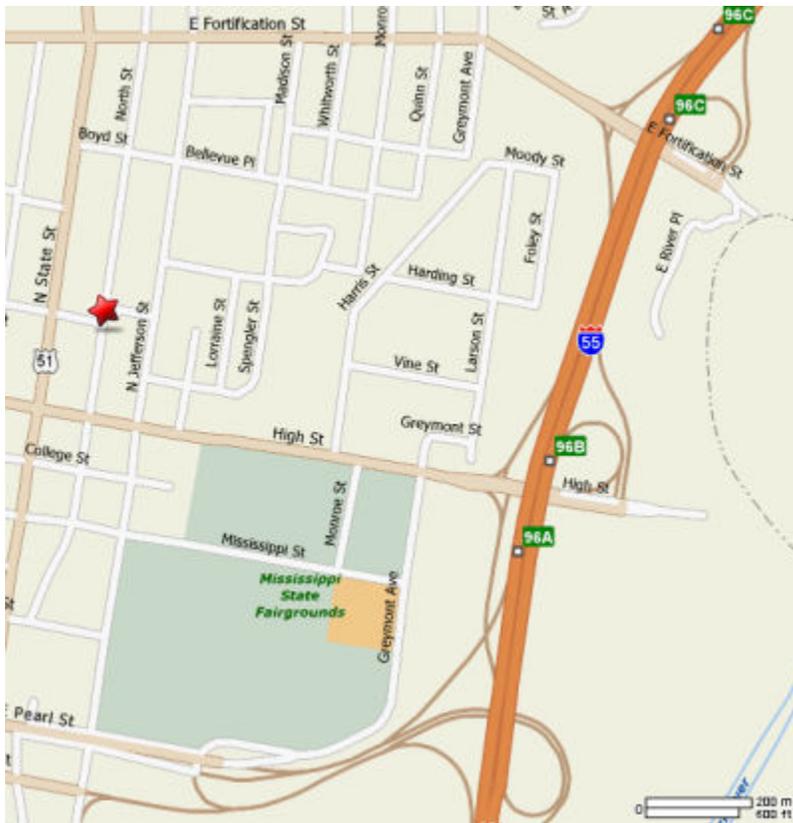
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## A NEW CHAPTER 2 FOR TEXAS: WELL-SUITED OR ILL-FITTING

*George E. Henderson\**

I.	A SHORT GUIDE TO THE DEVELOPMENT OF THE UCC AND THE ARTICLE 2 AMENDMENTS .....	239
	A. <i>The National Development</i> .....	239
	B. <i>Texas Developments</i> .....	241
	C. <i>Some Observations from History</i> .....	242
	D. <i>The Long Road to the 2003 Amendments</i> .....	243
II.	THE LEGISLATIVE RECORD .....	246
	A. <i>The Texas House Interim Hearing</i> .....	247
	B. <i>Summary of Objections and Amended Sections</i> .....	249
	1. <i>It Ain't Broke</i> .....	249
	2. <i>The Information/Goods Puzzle in § 2.103</i> .....	250
	3. <i>Freedom of Contract and § 2.207</i> .....	250
	4. <i>New Concepts of Liability</i> .....	251
	5. <i>Revisions of Merchantability and Fitness Implied     Warranty Disclaimer Rules</i> .....	252
	6. <i>Priorities Between Competing Purchasers of Entrusted     Goods (Motor Vehicles)</i> .....	252
	7. <i>Changes in the UCC Statute of Limitations</i> .....	253
	8. <i>National Provisions Not Included in the 2007 Bill</i> .....	253
	a. <i>Conforming Modifications</i> .....	254
	b. <i>Non-uniform Modifications and Changes in the 2007         Bill</i> .....	255
	c. <i>Modifications Affecting Remedies and Damages</i> .....	257
III.	ASSESSING THE CHANGES FOR TEXAS .....	259
	A. <i>The Information Exclusion</i> .....	260
	1. <i>The Information Issue in Interim National Drafts</i> .....	261
	2. <i>Information in the 2003 Amendments—The Definition</i> .....	264
	3. <i>Information and the 2007 Bill</i> .....	265
	4. <i>Continuing the Debate in the 2007 Bill</i> .....	268
	a. <i>The Sources of Scope Questions in Chapter 2</i> .....	269
	b. <i>Representative Tests and Cases for Code         Application</i> .....	271

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B.	<i>The Amended Battle of the Forms and Contract Formation Terms</i> .....	281
1.	<i>Current § 2-207 and the Text of Proposed Amendments:</i>	
	<i>The Contract Formation Terms of § 2-206</i> .....	283
2.	<i>Contract Terms Under Amended § 2-207</i> .....	287
	a. <i>Changes in the Introductory Clause</i> .....	288
	b. <i>Changes in the Operative Text of § 2-207</i> .....	289
	c. <i>Terms to Which Both Parties Agree</i> .....	289
3.	<i>Comparison of Current and Amended § 2-207 in Application</i> .....	292
4.	<i>Three Sample Transaction Patterns</i> .....	293
	a. <i>Battle of the Forms</i> .....	294
	b. <i>Confirmation Sent After an Agreement</i> .....	307
	c. <i>Gateway and Rolling Contract Cases</i> .....	310
C.	<i>The Remedial Promise Changes</i> .....	323
1.	<i>The Remedial Promise Issue</i> .....	324
2.	<i>The Remedial Promise and Limitations</i> .....	326
3.	<i>Some “Remedial Promise” Cases</i> .....	327
4.	<i>Case Law on Limitations for Remedial Promises</i> .....	330
5.	<i>The Remedial Promise Accrual Rule of § 2-725</i> .....	331
D.	<i>The Remote Purchaser Warranty and Remedial Promise</i> .....	332
1.	<i>The Privity Element in Express Warranties</i> .....	332
2.	<i>The Warranty or Remedial Promise to Remote Purchasers Under § 2-313A</i> .....	334
3.	<i>Some Aspects of § 2.313A of the 2007 Bill</i> .....	335
4.	<i>Approval of § 2-313A and Removal of § 2-313B</i> .....	337
E.	<i>Disclaimers of Implied Warranties</i> .....	338
1.	<i>Current Provisions</i> .....	339
2.	<i>Proposed Changes in § 2.316 Disclaimer Rules</i> .....	339
F.	<i>Consequential Damage Claims Against Buyers</i> .....	343
G.	<i>Priorities Between Competing Purchasers of Entrusted Goods</i> .....	345
H.	<i>Changes in Limitations Provisions of § 2.725</i> .....	348
1.	<i>The Basic Period of Limitation: § 2.725(a)</i> .....	348
2.	<i>The Accrual Rules: § 2.725(b)-(c)</i> .....	353
IV.	<i>A TAILORED AND WORTHWHILE PROPOSAL</i> .....	355
	APPENDIX I: BILL DRAFT .....	357
	APPENDIX II: DRAFT BILL ANALYSIS .....	445

A generous description, made almost ten years ago, of the preparation and search for approval of revisions to Article 2 of the Uniform Commercial Code (UCC) was that the project had been “long and arduous,” even at that point.<sup>1</sup> Not until 2003 did the National Conference of Commissioners on Uniform State Laws (NCCUSL) and the American Law Institute (ALI) approve consistent versions of amendments to Article 2.<sup>2</sup> Then in February 2004, the American Bar Association House of Delegates endorsed the Article 2 amendments at the ABA mid-year meeting in San Antonio, Texas.<sup>3</sup>

To date, no state has enacted the proposed 2003 Amendments to Article 2, and only three states—Kansas, Nevada, and Oklahoma—have introduced the proposed amendments.<sup>4</sup> Oklahoma has enacted, in a non-uniform version, one of the much-debated amendments proposed in the 2003 Amendments—the exclusion of “information” from “goods.”<sup>5</sup>

In Texas, a subcommittee of the Commercial Code Committee of the State Bar of Texas’s Business Law Section (the Texas Subcommittee) studied the 2003 Amendments and prepared a draft Bill with a related Bill Analysis in anticipation of the introduction of legislation during the Texas Legislature’s 2007 Session.<sup>6</sup> In late 2006, the Council of the Business Law Section of the

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1. Linda J. Rusch, *A History and Perspective of Revised Article 2: The Never Ending Saga of a Search for Balance*, 52 SMU L. REV. 1683, 1683 (1999).

2. NAT’L CONFERENCE OF COMM’RS ON UNIF. STATE LAWS, HANDBOOK OF THE NATIONAL CONFERENCE OF COMMISSIONERS ON UNIFORM STATE LAWS AND PROCEEDINGS OF THE ANNUAL CONFERENCE MEETING IN ITS 111TH YEAR 81 (2002). The NCCUSL approved the proposed Article 2 amendments at its meeting of July 26-August 2, 2002. *Id.* The ALI approved similar amendments at its 2003 Annual Meeting. AM. LAW INST., AMERICAN LAW INSTITUTE ANNUAL PROCEEDINGS: 80TH ANNUAL MEETING, 2003, at 195-96 (2004). For further discussion, see JAMES J. WHITE & ROBERT S. SUMMERS, UNIFORM COMMERCIAL CODE: REVISED ARTICLE 1 AND AMENDED ARTICLE 2—SUBSTANCE AND PROCESS SUPPLEMENT TO ACCOMPANY UNIFORM COMMERCIAL CODE 413-14 (2005) [hereinafter WHITE & SUMMERS, SUPPLEMENT]. The proposed amendments to Article 2 of the Uniform Commercial Code, as approved and promulgated by the NCCUSL and ALI, are called the “2003 Amendments.” This Article deals only with analysis of amendments proposed to Article 2—Sales, even though the promulgated amendments also cover Article 2A—Leases.

3. AM. BAR. ASS’N, 129TH ANNUAL REPORT OF THE AMERICAN BAR ASSOCIATION 14-17 (2004). The report also discusses the NCCUSL’s conclusions regarding the 2003 Amendments. *Id.* at 433.

4. E-mail from Michael R. Kerr, Legislative Director/Legal Counsel, NCCUSL, to author (Aug. 20, 2008, 11:46 CDT) (on file with author); E-mail from Michael R. Kerr, Legislative Director/Legal Counsel, NCCUSL, to author (Aug. 25, 2008, 16:39 CDT) (on file with author). The bills were S.B. 200, 73d Leg. Reg. Sess. (Nev. 2005), available at <http://www.leg.state.nv.us/73rd/bills/SB/SB200.pdf>; H.B. 2454, 2005 Leg., Reg. Sess. (Kan. 2005), available at <http://kslegislature.org/bills/2006/2454.pdf> (Article 2); H.B. 2455, 2005 Leg., Reg. Sess. (Kan. 2005), available at <http://kslegislature.org/bills/2006/2455.pdf> (Article 2A); H.B. 3129, 50th Leg., 2d Sess. (Okla. 2006), available at [http://webserver1.lsb.state.ok.us/2005-06bills/HB/HB3129\\_int.rtf](http://webserver1.lsb.state.ok.us/2005-06bills/HB/HB3129_int.rtf) (Article 2); H.B. 3084, 50th Leg., 2d Sess. (Okla. 2006), available at [http://webserver1.lsb.state.ok.us/2005-06bills/HB/HB3084\\_int.rtf](http://webserver1.lsb.state.ok.us/2005-06bills/HB/HB3084_int.rtf) (Article 2A).

5. OKLA. STAT. ANN. tit. 12A, §§ 2-105(1), 2-106(1) (West 2004). The Oklahoma Legislature amended the definition of “goods” in Article 2 to exclude “information” and the definition of “contract for sale” to exclude a “license of information.” *Id.*; see also OKLA. STAT. ANN. tit. 12A, § 2A-103(1)(h), (j) (West. Supp. 2008).

6. See Minutes of Council Meeting of the Business Law Section of the State Bar of Texas 4 (Dec. 2, 2006). The Texas Subcommittee began work in 2004. James Leeland of the Houston Bar is the subcommittee’s co-chairman. Professor Roy Ryden Anderson of the SMU Dedman School of Law is the

State Bar of Texas endorsed the work of the Texas Subcommittee.<sup>7</sup> The Council also authorized further consideration of the proposed Bill, recommended and supported by the Texas Business Law Foundation, for possible inclusion in legislation,<sup>8</sup> but the Council ultimately deferred final action pending review by a subcommittee of the Council of then-anticipated objections to the Bill.<sup>9</sup> The Texas Subcommittee prepared the proposed amendments to Chapters 2 and 2A of the Texas Business & Commerce Code in “Bill form” at that time.<sup>10</sup>

Consistent with the experience in other states and during the multi-year development of the 2003 Amendments, industry representatives and other interest groups raised objections to the Texas proposal.<sup>11</sup> As a result, the sponsoring groups did not proceed further with the filing of a bill, as the usual pressures of a legislative session timetable indicated little likelihood of a productive outcome.<sup>12</sup> At the conclusion of the 2007 session of the Texas Legislature, the Speaker of the Texas House of Representatives issued a charge to the House Committee on Business and Industry to conduct interim hearings on amendments to Chapters 2 and 2A of the Texas Business & Commerce Code in hopes of providing a better understanding of what was proposed and what was at issue.<sup>13</sup> The House Committee held an interim hearing on this legislation on May 15, 2008.<sup>14</sup>

This Article picks up where the 2007 legislative session ended—with the “Texas Amendments to Chapter 2” as then set out in a draft Bill and the accompanying Bill Analysis from the subcommittee of the Business Law Section.<sup>15</sup> This Article examines selected statutory revisions that concern recurring or problematic issues under the current Chapter 2 and its proposed amendments, tries them on for size in light of Texas (and national) developments, evaluates criticisms of the amendments, and assesses whether

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subcommittee’s co-chairman and reporter. The author joined the subcommittee in 2005. The author’s views should not be attributed to, and do not necessarily reflect, views of the Texas Subcommittee or any of its other members.

7. *See id.*

8. *See id.*

9. *Id.*

10. *See infra* app. I.

11. *See* Minutes of Council Meeting of the Business Law Section, *supra* note 6; *see, e.g.*, E-mail from Quentin Riegel, Vice-President, Nat’l Ass’n Mfrs., to Texas Subcommittee (Jan. 25, 2007, 15:04 CST) (on file with author).

12. *See* Minutes of Council Meeting of the Business Law Section, *supra* note 6.

13. Interim Study Charges, Texas House of Representatives, 80th Leg., Nov. 30, 2007, available at <http://www.house.state.tx.us/committees/charges/80interim/WholeInterimCharges.pdf>.

14. *Amendments to Chapter 2 & 2A of the Texas Business & Commerce Code, Interim Hearing Before the H. Comm. on Bus. & Indus.*, 80th Leg., Interim [hereinafter *Hearings*], available at <http://www.house.state.tx.us/committees/040.htm> (follow “Broadcast Archives” hyperlink; then follow “Interim Broadcasts, 05/15/08, 10:09 a.m. – 4:46 p.m.” hyperlink). For a discussion of the House Committee’s report, see *infra* notes 92-97 and accompanying text.

15. *See* discussion *infra* Part II.

the Texas Amendments to Chapter 2 fit the needs of a twenty-first century Texas.<sup>16</sup>

I. A SHORT GUIDE TO THE DEVELOPMENT OF THE UCC AND THE  
ARTICLE 2 AMENDMENTS<sup>17</sup>

A. *The National Development*

In 1940, William A. Schnader, president of the NCCUSL, proposed the preparation of a “uniform commercial code,” to encompass and revise existing NCCUSL Uniform State Laws and add coverage for other areas of commercial law.<sup>18</sup> After the NCCUSL and the ALI reached an agreement to develop a Uniform Commercial Code as a joint project of the two organizations in December 1944, the analysis and drafting of that Code began in 1945 under the direction of Karl N. Lewellyn of Columbia Law School as “Chief Reporter” and with an expected preparation time of a few years.<sup>19</sup> By 1951, the NCCUSL and ALI had approved a definitive text of the Uniform Commercial Code, and the American Bar Association House of Delegates had endorsed the Code.<sup>20</sup> The completion of edited text and comments of the UCC followed in 1952, about seven years after its start.<sup>21</sup>

The publication of the 1951 text of the Code, which included a series of last-minute modifications, brought a sense of completion.<sup>22</sup> But just as the

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16. See discussion *infra* Parts III-IV.

17. Texas’s version of the Uniform Commercial Code consists of Title 1, Chapters 1-11, of the Texas Business & Commerce Code. See TEX. BUS. & COM. CODE ANN. §§ 1.101-11.108 (Vernon 1994 & Supp. 2008). References to Texas UCC provisions are to its “Chapters” and “Sections,” as designated in the Texas Business & Commerce Code. See *id.* The official text of the UCC, promulgated by the NCCUSL and ALI, uses “Articles” rather than “Chapters,” so references to the official text version of the UCC are to its “Articles” and “Sections,” as designated in the published official text. The “Code” and “U.C.C.” refer to the Uniform Commercial Code generally. When a Texas provision is addressed specifically, the reference is to the Texas Business & Commerce Code.

18. See NAT’L CONFERENCE OF COMM’RS ON UNIF. STATE LAWS, HANDBOOK OF THE NATIONAL CONFERENCE OF COMMISSIONERS ON UNIFORM STATE LAWS AND PROCEEDINGS OF THE FIFTIETH ANNUAL CONFERENCE 58 (1940). The NCCUSL was organized in 1892, and its first major legislative project was the Uniform Negotiable Instruments Law, promulgated in 1896. See Frederick H. Miller, Patricia B. Fry & John P. Burton, *Introduction to the Uniform Commercial Code Annual Survey: The Centennial of the National Conference of Commissioners on Uniform State Laws*, 46 BUS. LAW. 1449, 1449-50 (1991). The Uniform Commercial Code replaced numerous uniform acts, including the Negotiable Instruments Law to the Uniform Trust Receipts Act. See Robert Braucher, *The Legislative History of the Uniform Commercial Code*, 58 COLUM. L. REV. 798, 799 (1958).

19. See William A. Schnader, *A Short History of the Preparation and Enactment of the Uniform Commercial Code*, 22 U. MIAMI L. REV. 1, 4-5 (1967).

20. See *id.* at 7; Braucher, *supra* note 18, at 800; NAT’L CONFERENCE OF COMM’RS ON UNIF. STATE LAWS, HANDBOOK OF THE NATIONAL CONFERENCE OF COMMISSIONERS ON UNIFORM STATE LAWS AND PROCEEDINGS OF THE SIXTIETH ANNUAL CONFERENCE MEETING 160-63 (1951); AM. BAR ASS’N, ANNUAL REPORT OF THE AMERICAN BAR ASSOCIATION 135 (1951).

21. See Braucher, *supra* note 18, at 800.

22. See Schnader, *supra* note 19, at 6-7 (reviewing conferences with interested parties and resulting late changes).

Code was to be introduced in numerous state legislatures in the fall of 1952, groups that had remained in the background during the years of the Code's initial preparation made additional objections.<sup>23</sup> Apart from Pennsylvania's 1953 enactment of the Code, the Code encountered strong headwinds<sup>24</sup> as existing academic debates spilled over into the legislatures.<sup>25</sup> In New York, the Governor referred the Code to the state's Law Revision Commission (LRC) for additional study and recommendation, and this study continued until the Commission published its February 1956 Report.<sup>26</sup> The New York revision process stopped all enactments of the Code; Pennsylvania remained the only state with an effective code by 1956.<sup>27</sup> Not only did the New York revision process halt enactment, the LRC Report itself raised obstacles to further enactment with its conclusion: "The Commission believes that it is clear, from the criticisms indicated in this Report, that the Uniform Commercial Code is not satisfactory in its present form and cannot be made satisfactory without comprehensive re-examination and revision in light of all critical comment obtainable."<sup>28</sup>

Facing opposition in New York, obviously a state of great influence in commercial law, the NCCUSL and ALI reassembled the Editorial Board for the project.<sup>29</sup> The Board reviewed the criticisms of the Code found in the LRC Report and in voluminous reports of hearings from 1953-56, produced a revised text in 1957 with changes from the 1952 version, and provided a complete revised text with comments in 1958.<sup>30</sup> The revisions in response to the LRC Report together with the efforts of the Code's supporters in Massachusetts led to a breakthrough in that state, which adopted the revised Code in 1957.<sup>31</sup> After Massachusetts's adoption came an annual increase in adopting states,

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23. See *id.*; Braucher, *supra* note 18, at 801-04.

24. See Schnader, *supra* note 19, at 8. Even though the Code was introduced in eight state legislatures in 1953, only Pennsylvania enacted it at that time. *Id.*; see also UNIF. COMMERCIAL CODE, 1 U.L.A. 1 (2004) (listing Pennsylvania as the first jurisdiction to adopt the Code in 1953).

25. Compare Arthur Linton Corbin, *The Uniform Commercial Code—Sales: Should It Be Enacted?*, 59 YALE L.J. 821, 836 (1950) ("The new Code should be enacted because it builds soundly on the existing Uniform Sales Act . . . [and] it provides within itself a method and principle of future growth."), with Samuel Williston, *The Law of Sales in the Proposed Uniform Commercial Code*, 63 HARV. L. REV. 561, 561 (1950) ("[I] feel compelled, contrary to my original expectation, to publish my reasons for opposition.")

26. See LAW REVISION COMM'N, STATE OF N.Y., REPORT OF THE LAW REVISION COMMISSION FOR 1956: REPORT RELATING TO THE UNIFORM COMMERCIAL CODE (1956) (Legislative Document (1956) No. 65(A)); Schnader, *supra* note 19, at 8.

27. See Schnader, *supra* note 19, at 9.

28. See LAW REVISION COMM'N, *supra* note 26, at 58.

29. See Schnader, *supra* note 19, at 9.

30. See Braucher, *supra* note 18, at 804.

31. See *id.* at 805-06; Schnader, *supra* note 19, at 9. The Code's proponents in Massachusetts included Walter D. Malcolm, former chairman of the ABA Committee on the Commercial Code, and Peter F. Coogan. See *id.*; Grant Gilmore, *Secured Transactions Under the Uniform Commercial Code*, 73 YALE L.J. 1303, 1305 (1964) (reviewing PETER F. COOGAN ET AL., SECURED TRANSACTIONS UNDER THE UNIFORM COMMERCIAL CODE (1963)). "That [the N.Y. Law Revision Commission Report] was not the end was entirely due to the devoted labors of a group of Massachusetts lawyers, among whom Mr. Coogan was a leading figure." *Id.*

with Texas's adoption of the UCC being effective July 1, 1966, and with enactment in all states except Louisiana by 1968.<sup>32</sup>

### B. Texas Developments

Texas had early exploratory contact with the UCC. In 1951, the Texas Legislature adopted a concurrent resolution for study of the Code, as it then stood, by the recently created Texas Legislative Council.<sup>33</sup> Although the council did issue a report, no legislative action followed for virtually a decade.<sup>34</sup> In 1962, in connection with the work of a subcommittee appointed by the Committee on Uniform State Laws of the State Bar of Texas, a report and recommendation of that subcommittee led to the preparation of a Bill introduced in the 1963 regular session of the Texas Legislature.<sup>35</sup> The House Judiciary Committee approved the Bill, but no Senate committee took any action in 1963, consistent with a reported commitment by the house sponsor that he would not make a strong effort to move the Bill on the floor of the House of Representatives.<sup>36</sup> This limited legislative support for the Code in 1963 suggests that some affected constituencies were not wholly in favor of the Code at that time.<sup>37</sup>

Prior to the 1965 legislative session, the State Bar of Texas again proposed enactment of the Code, as the national movement was gaining force.<sup>38</sup> At the time of the Bar's re-endorsement, twenty-nine states—including Arkansas, Oklahoma, and New Mexico—had enacted the Code, and most remaining states were ready to act.<sup>39</sup> This time, some actual opposition to the Code provisions, specifically § 2-318 regarding third-party beneficiaries of warranties and privity considerations, surfaced. The Board of Directors of the State Bar recommended that § 2-318, as promulgated, not be included as “such opposition to this section appeared to have developed so as to imperil the chances of adoption of the Code.”<sup>40</sup> Instead of proposing one of the standard § 2-318 options, the Texas UCC Bill included a non-uniform § 2.318 so as to

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32. See Schnader, *supra* note 19, at 11.

33. Tex. S. Con. Res. 46, 52d Leg., R.S., 1951 Tex. Gen. Laws 1524 (Uniform Commercial Code); see also Millard H. Ruud, *The Texas Legislative History of the Uniform Commercial Code*, 44 TEX. L. REV. 597 (1966) (recounting the events over several years leading to enactment of the Code in Texas and the role of the new Texas Legislative Council).

34. See discussion *infra* note 35.

35. See Rudd, *supra* note 33, at 598-99. The 1962 bar report covered the Code in a chapter by chapter summary. See *id.* at 598. Hubert D. Johnson of the Dallas Bar worked on the drafting of the Bill, which was introduced in the 1963 Texas Legislature as S.B. 309 and H.B. 553. Comm. on Unif. State Laws, State Bar of Tex., *Uniform State Laws*, 27 TEX. B.J. 505-06 (1964); Rudd, *supra* note 33, at 598-99.

36. See Rudd, *supra* note 33, at 509 n.13.

37. See discussion *supra* note 36.

38. See Ruud, *supra* note 33, at 599.

39. See Millard H. Ruud, *The Uniform Commercial Code—What its Enactment Would Mean to Texas*, 27 TEX. B.J. 943, 943 (1964).

40. See Rudd, *supra* note 39, at 1006 n.3; Rudd, *supra* note 33, at 601-02 (detailing concerns over § 2-318).

“[make] it abundantly clear that the Texas Code marks out for common-law development the question of what participants in the marketing chain are liable to what persons injured through the use of the marketed product.”<sup>41</sup>

With this skirmish over, enactment of the Code could proceed.<sup>42</sup> Each house of the legislature approved a conference committee report on May 19, 1965.<sup>43</sup> After enrollment, the Governor signed Senate Bill 141, completing the passage and enactment of the Code in Texas.<sup>44</sup> In 1967, the legislature adopted the Texas Business & Commerce Code, re-enacting the UCC as part of the larger Business & Commerce Code.<sup>45</sup>

### C. *Some Observations from History*

At this point, and in anticipation of some of the objections that observers have voiced regarding the birth and life (to date) of the 2003 Amendments, a few observations about the UCC as we now know it are relevant. First, the Code did not have fair winds and following seas on its initial voyage.<sup>46</sup> As Professor Grant Gilmore noted, “There was a period in the mid-1950’s when it appeared that the Code was dead.”<sup>47</sup> As described, four years of criticism and revision came between Pennsylvania’s 1953 enactment of the then-final text of the Code and Massachusetts’s 1957 adoption of a revised version.<sup>48</sup> This history of the Code’s promulgation, criticism, revision, and enactment (or amendment) should demonstrate that the Code, even as it presently stands, is not a finished work to be preserved intact for the ages but a work-in-progress. To quote Professor Gilmore again, “My own experience in teaching the Articles on Sales, Commercial Paper, and Bank Collections leaves me somewhat skeptical of the pervasiveness of divine inspiration in any part of the Code . . . .”<sup>49</sup>

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41. See Rudd, *supra* note 33, at 602. This non-uniform provision is carried forward in the proposed Amended Chapter 2. See discussion *infra* Parts II-IV.

42. See discussion *infra* notes 43-45.

43. See Rudd, *supra* note 33, at 600.

44. See Uniform Commercial Code, 59th Leg., R.S., ch. 721, 1965 Tex. Gen. Laws 1 (current version at TEX. BUS. & COM. CODE ANN. §§ 1.101-11.108 (Vernon 1994 & Supp. 2008)).

45. See Business & Commerce Code, 60th Leg., R.S., ch. 785, 1967 Tex. Gen. Laws 2343-2782 (current version at TEX. BUS. & COM. CODE ANN. §§ 1.101-11.108 (Vernon 1994 & Supp. 2008)).

46. See Gilmore, *supra* note 31, at 1305 (commenting that no state followed Pennsylvania in promptly enacting the Code after the final version was promulgated in 1952).

47. *Id.*; see also Lorin Brennan, *Why Article 2 Cannot Apply to Software Transactions*, 38 DUQ. L. REV. 459, 462 n.10 (2000) (“[I]t took almost twenty years for the entrenched legal establishment to accept [the UCC].”). Brennan quotes Max Planck to explain that “[a] new scientific truth does not triumph by converting its opponents and making them see the light, but rather because its opponents eventually die.” *Id.* at 462 n.11 (quoting MORRIS KLINE, *MATHEMATICS-THE LOSS OF CERTAINTY* 88 (1980)).

48. See Gilmore, *supra* note 31, at 1305.

49. *Id.* at 1307.

The present state of the Uniform Commercial Code also reflects an early concern of its supporters about actually achieving “uniformity.”<sup>50</sup> Texas concurs in the assessment that the Code is not uniform: “While this case involves a Uniform Commercial Code breach of express warranty claim, it seems that ‘the Uniform Commercial Code is not uniform.’”<sup>51</sup> In *Compaq Computer Corp. v. Lapray*, the Texas Supreme Court spent six pages cataloging non-uniform rules among the states on notice of breach to remote manufacturers under § 2-607 of the UCC (as a requirement for warranty recovery), reliance as an element of the “basis of the bargain” for an express warranty, and availability of express warranty relief for unmanifested defects.<sup>52</sup> Nonetheless, the Code is sufficiently “uniform” to be a functioning part of American law.

These reference points take away some of the power in frequently heard objections that oppose *any* action on the 2003 Amendments, seek to preclude any state-specific modifications of the 2003 Amendments, or warn of the uniformly adverse consequences of non-uniformity.<sup>53</sup> In the presence of (and even the proliferation of) non-uniform changes in the existing statute and with the extensive inter-jurisdictional disagreements about what the current Code means, such as those catalogued by the Texas Supreme Court in *Lapray*, one should not be afraid to look at changes that might alter a non-divinely inspired Code or that might be non-uniform.

#### D. *The Long Road to the 2003 Amendments*

The “long and arduous” road to the 2003 Amendments began in the 1980s.<sup>54</sup> An influential law review article cataloging problems in existing Article 2, both as to its drafting and its interpretation (and its conflicting interpretations), provided an early push.<sup>55</sup> The ALI-NCCUSL Permanent Editorial Board for the Uniform Commercial Code (the Permanent Editorial Board or PEB) requested in 1986, and received in 1987, a memorandum on the

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50. See, e.g., Schnader, *supra* note 19, at 10 (“[V]arious legislative bodies have seen fit to make a total of approximately 775 non-uniform amendments.”).

51. *Compaq Computer Corp. v. Lapray*, 135 S.W.3d 657, 673 (Tex. 2004) (quoting *Walsh v. Ford Motor Co.*, 807 F.2d 1000, 1016 (D.C. Cir. 1986)).

52. *Id.* at 674-80.

53. See *infra* Part II.B (summarizing common objections to the 2003 Amendments).

54. Rusch, *supra* note 1, at 1683. This Article’s summary of some fifteen years of work by and among the ALI, NCCUSL, and ABA is relatively brief compared to the massive academic literature on the project, its problems, and its results. For a more thorough sampling of academic literature on the UCC, see Symposium, *Symposium on Revised Article 1 and Proposed Revised Article 2 of the Uniform Commercial Code*, 54 SMU L. REV. 469 (2001).

55. See Fairfax Leary, Jr. & David Frisch, *Is Revision Due for Article 2?*, 31 VILL. L. REV. 399 (1986). Leary and Frisch’s article is credited with stimulating the Article 2 revision project. See Richard E. Speidel, *Introduction to Symposium on Proposed Revised Article 2*, 54 SMU L. REV. 787, 789 n.7 (2001).

revision of Article 2, leading to the appointment of a Study Group in 1988.<sup>56</sup> At the outset, the process for preparing a revised Article 2 rather resembled the process seen in the development of the original Code in the 1940s and early 1950s. The Study Group prepared its *Preliminary Report of the Uniform Commercial Code Article 2* and circulated it for comment in 1990;<sup>57</sup> in August 1991, it published a *Uniform Commercial Code, Article 2 Executive Summary*, recommending that a drafting committee undertake revisions to Article 2.<sup>58</sup> In due course, the NCCUSL appointed an Article 2 drafting committee for the revision project.<sup>59</sup> As the *Executive Summary* had identified some topics of concern in preparing revisions to Article 2 that were based on ancillary areas of the law, particularly issues relating to information licensing, the NCCUSL merged its Special Committee on Software Contracts with the Article 2 Drafting Committee in 1992; this led, for a time, to work on the development of a “hub and spoke” scheme for a revised Article 2.<sup>60</sup>

The Article 2 Drafting Committee grew to thirteen members by 1996 and also attracted the attention of industry groups at the drafting stage, much earlier than in the 1950s.<sup>61</sup> Attorneys for the involved industry groups consistently offered criticism of drafts, and at least in the view of the then-reporter for the Drafting Committee, “commercial interests opposed to Article 2’s revisions did not hesitate to venture outside the normal drafting process” to press their

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56. See Speidel, *supra* note 55, at 789 n.7. Speidel also provides a summary of the nine members of the initial study group. *Id.* at 799 n.9.

57. See *id.* at 789. For a reprint of the Preliminary Report, see PERMANENT EDITORIAL BD. FOR THE UNIF. COMMERCIAL CODE, PEB STUDY GROUP UNIFORM COMMERCIAL CODE ARTICLE 2 PRELIMINARY REPORT (1990) [hereinafter PEB STUDY GROUP, PRELIMINARY REPORT], reprinted in Task Force of the ABA Subcomm. on Gen. Provisions, Sales, Bulk Transfers, and Documents of Title, Comm. on the Unif. Commercial Code, *An Appraisal of the March 1, 1990, Preliminary Report of the Uniform Commercial Code Article 2 Study Group*, 16 DEL. J. CORP. L. 981 (1992) [hereinafter ABA Task Force, *Appraisal*]. The ABA Task Force *Appraisal* article contains a section by section reprinting of the Study Group’s report followed by the ABA Task Force’s appraisal of that report. See *id.* at 981 n.\*. For convenience of reference, discussions of the *Preliminary Report* will refer to its reprinting in the ABA Task Force *Appraisal* article.

58. See PEB Study Group, *PEB Study Group: Uniform Commercial Code, Article 2 Executive Summary*, 46 BUS. LAW. 1869 (1991). The ABA Subcommittee Task Force agreed that revisions should be made to Article 2. See ABA Task Force, *Appraisal*, *supra* note 57, at 985. Professor Anderson, Reporter for the Texas Subcommittee, was a member of the ABA Task Force in 1991. *Id.* at 981 n.\*.

59. Speidel, *supra* note 55, at 789 n.12 (summarizing the arrangements between the Permanent Editorial Board, NCCUSL, and ALI on drafting committees and review and approval of proposals).

60. See WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 406-08. The hub-and-spoke statutory structure is seen in the Texas Business Organizations Code. See Daryl B. Robertson, Robert Hamilton & George W. Coleman, *Introduction to Texas Business Organizations Code*, 38 TEX. J. BUS. L. 57, 62 (2002). The magnitude of the structural changes involved with a hub-and-spoke plan for Article 2 caused the NCCUSL to abandon the combined project in 1995, and the Article 2 drafting committee returned to traditional Article 2 issues. WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, app. IV, at 406-08. The software project ultimately became the Uniform Computer Information Transactions Act (UCITA), approved by NCCUSL in July 2000, but not a part of the UCC. See *id.* app. IV, at 408 n.7; Speidel, *supra* note 55, at 789-90.

61. WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 49-50; Speidel, *supra* note 55, at 790 n.14.

concerns.<sup>62</sup> Although the ALI had approved a final draft in May 1999, at the July 1999 meeting of the NCCUSL, “[a]fter two half-days of debate on the floor and after the [NCCUSL] membership rejected a proposal to remove some of the most contentious language concerning unconscionability, the leaders of NCCUSL pulled the draft from further consideration,” asserting insufficient time remained to complete the debate.<sup>63</sup>

Both reporters on the Drafting Committee promptly resigned.<sup>64</sup> The NCCUSL then appointed new reporters for the Article 2 Drafting Committee and reconstituted the committee.<sup>65</sup> From that reconstituted committee came the 2003 Amendments, although not without further battles.<sup>66</sup> Because the selection process for NCCUSL committees seeks “as much expertise and as many viewpoints as possible,”<sup>67</sup> it should not be surprising that the drafting of the Article 2 amendments, a statute which applies “across the board” in commercial and consumer contexts, remained contentious, especially after the 1999 meeting.<sup>68</sup>

After the reconstitution of the committee, the new committee decided to attempt amendments to Article 2, not a wholesale “revision,” which had been very ambitious.<sup>69</sup> Out of that work came the 2003 Amendments.<sup>70</sup> The comments of the then-President of the NCCUSL upon endorsement of the Article 2 Amendments by the ABA House of Delegates were fair, but optimistic: “We believe that these amendments are fair and balanced, and an improvement over existing law. The decades-long project to revise and update the Uniform Commercial Code is now complete.”<sup>71</sup> Of course, as to Article 2

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62. WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 50-51 (describing the extent of business objections and noting that White, a member of the drafting committee, thought some parts of the drafts were unwise); Speidel, *supra* note 55, at 791-92. In addition, White & Summers describe consumer and software licensor objections, based in part on the near parallel development of UCITA. WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 53.

63. WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 51-52; Rusch, *supra* note 1, at 1684-86.

64. WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 51; Rusch, *supra* note 1, at 1683 n.2.

65. See WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 51-52; Rusch, *supra* note 1, at 1686.

66. See WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, app. IV, at 405-18. Appendix IV of the *Supplement* sets out a history of the 2003 Amendments. See *id.* Professor White was a member of the Drafting Committee, both as originally organized and as reconstituted. *Id.* app. IV, at 405 n.2, 412 n.14.

67. Fred H. Miller, *Introduction to the Idaho Law Review Symposium on Uniform Commercial Code Article 2: In Celebration of the One Hundredth Birthday of the National Conference of Commissioners on Uniform State Laws*, 27 IDAHO L. REV. 409, 415 (1990).

68. One can assess the degree to which the committee was split from a brief comment by Professor White. See James J. White, *Default Rules in Sales and the Myth of Contracting Out*, 48 LOY. L. REV. 53, 84-85 (2002). Professor White acknowledges ghostwriting a paper delivered to the Article 2 drafting committee on behalf of General Electric Corp. *Id.* at 84. Even with the support of Professor White, the paper “barely got its head above water.” *Id.* at 84-85.

69. See WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, app. IV, at 412.

70. See *id.* at 412-14.

71. *Id.* at 414 (quoting Fred H. Miller, President, NCCUSL, ABA Approves Six NCCUSL Acts (Feb. 9, 2004)).

Amendments, the project could hardly be said to be complete. The amendments have not been enacted substantially as proposed in any state.<sup>72</sup>

## II. THE LEGISLATIVE RECORD

What is a legislator—or lawyer—to do to make sense of this? The NCCUSL-ALI partnership has produced a comprehensive set of amendments to Article 2, and the ABA has endorsed them.<sup>73</sup> The amendments have critics on almost every side of any issue.<sup>74</sup> As the initial Drafting Committee's Associate Reporter observed, even after the committee had reached the point of delivering its final 1999 draft, "letters . . . continued to pour in protesting various items in the revision," indicating the level of opposition that led to the withdrawal of that draft at the NCCUSL annual meeting.<sup>75</sup> And the efficacy of opposition to the 2003 Amendments can be inferred from the lack of national legislative progress on enacting the 2003 Amendments.<sup>76</sup>

To mark a small path through this minefield, this Article reviews, with emphasis on effects or issues in Texas law, the 2003 Amendments as modified by the Texas Subcommittee.<sup>77</sup> Such an effort requires access to proposed statutory texts, something that is not always a simple task. To provide the reader with the basic tools for the task, this Article includes (1) as Appendix I, the Texas Subcommittee's draft 2007 Bill to amend Chapters 2 and 2A of the Texas Business & Commerce Code, as prepared for delivery to the Texas Legislative Council, and (2) as Appendix II, the Texas Subcommittee's Draft Bill Analysis as of January 8, 2007 with respect to the proposed Chapter 2 and Chapter 2A amendments.<sup>78</sup> Of course, the official text of the 2003 Amendments of Article 2 appears in numerous publications, and need not be reproduced here.<sup>79</sup>

To those reference points, the Article also adds a short review of objections to the 2003 Amendments from witnesses appearing at the May 15, 2008 interim hearing before the Committee on Business and Industry of the Texas House of Representatives and a summary of comments or objections the Texas Subcommittee received from other interested groups.<sup>80</sup>

With those tools, and an open mind, an assessment of the effects to be anticipated for Chapter 2 under the 2007 Bill is in order and should help

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72. See *supra* note 4 and accompanying text.

73. See WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, app. IV, at 413-14.

74. See Rusch, *supra* note 1, at 1687 n.13.

75. *Id.* at 1689.

76. See *supra* note 4 and accompanying text.

77. See *infra* Part II.B.

78. References to provisions in the draft Bill amending Chapters 2 and 2A are identified by Texas Business & Commerce Code section number or by reference to sections of the "2007 Bill." The Texas Subcommittee's Draft Bill Analysis is hereinafter the "2007 Analysis."

79. See U.C.C. Art. 2 (amended 2003), 1 U.L.A. 360-593 (2004).

80. See *Hearings*, *supra* note 14.

legislators, lawyers, and judges in dealing with the 2003 Amendments and their aftermath in Texas.<sup>81</sup> As Professors White and Summers observe, even if the 2003 Amendments are not adopted, the analysis of these proposed amendments “casts much light by way of interpretation of the current law.”<sup>82</sup>

To assess every change proposed for Chapter 2 in the 2007 Bill would require more time—and thought—than suitable for any single law review article. Indeed, the approach here will be to focus on selected key issues, either as raised during the work of the Texas Subcommittee or as asserted by observers or opponents of the legislation, and to assess what changes result in Texas under the 2003 Amendment and the 2007 Bill. The quality and benefits of those changes will be left to the reader.

#### A. *The Texas House Interim Hearing*

The Committee on Business and Industry of the Texas House of Representatives held an interim hearing on May 15, 2008, regarding amendments to Chapters 2 and 2A of the Texas Business & Commerce Code.<sup>83</sup> A video record of that hearing is available at the Committee’s website.<sup>84</sup> The Committee’s witness list for the hearing was as follows:

- Roy Ryden Anderson
- Jean Braucher (Americans for Fair Electronic Commerce Transactions)
- Randy Burton
- Charles R. Keeton (General Electric Company)
- James H. Leeland
- Patricia A. Tauchert (Square D Company/Schneider Electric)
- Anne Peters (Texas Legislative Council—not testifying)
- Mark Bohannon (Software & Information Industry Association).<sup>85</sup>

Messrs. Anderson, Burton, and Leeland spoke in support of the proposed Texas amendments. Mr. Leeland is the Co-Chairman of the Texas Subcommittee, and Professor Anderson is the Co-Chairman and Reporter of that Texas Subcommittee.<sup>86</sup> Mr. Burton is a member of the Houston Bar and the Texas Subcommittee.<sup>87</sup> Ms. Braucher, Mr. Keeton, and Ms. Tauchert spoke

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81. See WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at iii.

82. See *id.*

83. See *Hearings*, *supra* note 14.

84. *Id.*

85. *Id.*

86. *Id.*

87. *Id.*

in opposition and have extensive prior involvement in the 2003 Amendments.<sup>88</sup> Mr. Bohannon commented on the Texas amendments and particularly opposed any change to the “information” exclusion.<sup>89</sup> The documents received by the Committee included three documents from the Texas Subcommittee: *Executive Summary of Proposed Legislation, Selected Aspects of Proposed Legislation, and Criticisms and Responses*.<sup>90</sup> A letter dated January 25, 2007, in opposition to the legislation as then proposed by the Texas Subcommittee, from the National Association of Manufacturers, the National Electrical Manufacturers Association, and the Marine Retailers Association to Mr. J. Scott Sheehan with the Texas Business Law Foundation was also provided to the Committee.<sup>91</sup>

In December 2008, the House Committee on Business and Industry released its *Interim Report* covering, among other study charges, its consideration of the amendments to Chapters 2 and 2A of the Texas Business & Commerce Code as proposed by the 2007 Bill.<sup>92</sup> The report identifies the primary concern of opponents of the 2007 Bill as the “lack of uniformity between states” should Texas enact the 2007 Bill or comparable legislation, with the consequence of anticipated, but undocumented, transition and compliance costs.<sup>93</sup> The report acknowledges testimony that the 2007 Bill does alleviate some concerns regarding the 2003 Amendments but concludes that “the costs of non-uniformity are too high” for Texas to enact the amendments.<sup>94</sup>

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88. See, e.g., WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 50; Memorandum from Jean Braucher to Members of the American Law Institute (May 1, 2003), available at [http://www.ali.org/ali\\_old/050503BraucherMotion.htm](http://www.ali.org/ali_old/050503BraucherMotion.htm).

89. *Hearings*, *supra* note 14, at 4:52 (testimony of Mark Bohannon); see *infra* Part II.B.2 (summarizing the concerns regarding “information” being excluded from the definition of “goods”); *infra* Part III.A (fully discussing the concerns regarding “information” being excluded from the definition of “goods”).

90. See *Executive Summary of Proposed Legislation: Interim Hearing on Proposed Amendments to the Texas Business and Commerce Code Chapters 2 (Sales) and 2A (Leases) Before the H. Comm. on Bus. and Indus.* (2008) (report of the Article 2 Subcomm., State Bar of Tex. Bus. Law Section) (on file with author); *Selected Aspects of Proposed Legislation: Interim Hearing on Proposed Amendments to the Texas Business and Commerce Code Chapters 2 (Sales) and 2A (Leases) Before the H. Comm. on Bus. and Indus.* (2008) (report of the Article 2 Subcomm., State Bar of Tex. Bus. Law Section) (on file with author); *Criticism & Responses: Interim Hearing on Proposed Amendments to the Texas Business and Commerce Code Chapters 2 (Sales) and 2A (Leases) Before the H. Comm. on Bus. and Indus.* (2008) (report of the Article 2 Subcomm., State Bar of Tex. Bus. Law Section) (on file with author).

91. Letter from Quentin Riegel, Vice President, Litigation & Deputy Gen. Counsel, Nat’l Assoc. of Mfrs., Clark R. Silcox, Counsel, Nat’l Elec. Mfrs. Assoc., Phil Keeter, President, Marine Retailers Assoc. of Am., to J. Scott Sheehan, Bus. Law Found., 1 (Jan 25, 2007), available at [http://www.nam.org/~media/Files/s\\_nam/docs/238200/238180.pdf.ashx](http://www.nam.org/~media/Files/s_nam/docs/238200/238180.pdf.ashx). Professor Braucher also handed up a summary of her testimony at the conclusion of her presentation. See *Hearings*, *supra* note 14, at 4:24 (testimony of Jean Braucher). That document was not included in copies obtained later from the committee clerk.

92. H. COMM. ON BUS. & INDUS., TEX. H. OF REP., INTERIM REPORT DECEMBER 2008: A REPORT TO THE HOUSE OF REPRESENTATIVES, 81ST TEXAS LEGISLATURE 19-23 (2008), available at <http://www.house.state.tx.us/committees/reports/80interim/CommitteeonBusineandIndustry.pdf>.

93. *Id.* at 22-23. The House Committee did not attempt to quantify or evaluate any costs that would actually be incurred, and the report does not refer to documentation or testimony that quantified or evaluates such costs.

94. *Id.* at 23.

The “non-uniformity argument” is an aspect of the “It Ain’t Broke” argument, discussed below.<sup>95</sup> While accepting the costs of the non-uniformity argument, the report does acknowledge that the contrary view has support as well: the amendments can clarify ambiguities and reduce litigation, with a consequent reduction in litigation and its costs.<sup>96</sup> But when assessing the non-uniformity argument as made by business or commercial interests (namely that non-uniformity increases costs of compliance due to state variations affecting a large enterprise), one should remember that Article 2 *already* has a significant number of state-specific, non-uniform amendments that concern, for example, consumer implied warranty disclaimers, and sellers have been able to cope with them thus far.<sup>97</sup>

On the basis of such existing non-uniformities, the effects of non-uniform variations as identified in the House *Interim Report*, although deserving attention, should not preclude serious consideration of the 2007 Bill on its merits. Thus, at the end of December 2008, the 2007 Bill remains a product of substantive work by the Texas Subcommittee, supported by the Council of the Business Law Section of the State Bar of Texas and ready for introduction before the legislative session commenced in January 2009.

### B. Summary of Objections and Amended Sections

Before turning to a more detailed consideration of objections to the 2003 Amendments in this Article, the most commonly identified complaints about the 2003 Amendments are summarized below (excluding some that would not apply to the Texas Subcommittee draft 2007 Bill).

#### 1. It Ain’t Broke

Most opponents of the 2003 Amendments assert some variation on the theme, “Article 2 ain’t broke, so don’t fix it,” or its companion, “There is no industry or commercial support for the amendments.”<sup>98</sup> And beyond the assertion that Article 2 “ain’t broke,” there is the political fact of consistent and organized opposition to the amendments.<sup>99</sup> Balanced against this view are, for example, testimony from the House Committee Interim Hearing as to the

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95. See *infra* Part II.B.1.

96. H. COMM. ON BUS. & INDUS., *supra* note 92, at 22.

97. See, e.g., sources cited *infra* note 784.

98. See *Hearings*, *supra* note 14, at 4:01 (testimony of Jean Braucher); Memorandum from Jeff Dodd, Member, ABA UCC Comm., to Stephanie Heller, Chair, ABA UCC Comm., 1-2 (Sept. 19, 2003) (on file with author). Professor Braucher also described the Amendments as a “solution in search of a problem.” See *Hearings*, *supra* note 14 (testimony of Jean Braucher); see also Letter from Quentin Riegel to J. Scott Sheehan, *supra* note 91 (describing a lack of industry support of the amendments).

99. See *Hearings*, *supra* note 14, at 4:27 (testimony of Patricia Tauchert) (referring to opposition of industry associations); Letter from Quentin Riegel to J. Scott Sheehan, *supra* note 91, at 1 (“[W]e are not aware of any industry group that supports revising Article 2 . . . .”); Memorandum from Holly K. Towle, UCC Comm. Member, to Stephanie Heller, Chair, ABA UCC Comm., 2-4 (Sept. 15, 2003).

dysfunctional nature of current § 2.207 and the fifteen-year record of work by the NCCUSL and ALI on revisions, an effort that would hardly be undertaken if no problems were present.<sup>100</sup> It is fair to say that, even if Article 2 “ain’t broke,” there are enough worn parts that an overhaul is in order to “improve” operations. And even *before* the actual work on revisions began, the authors of one article cautioned, “The ‘If it ain’t broke, don’t fix it’ syndrome must be avoided.”<sup>101</sup> A corollary of this first objection is the uniformity rule: The amendments have been proposed, but not enacted elsewhere, or “your state would not be uniform” with, as applicable, those who have *not* adopted the amendments or those who *have* adopted the amendments.<sup>102</sup> As Oklahoma has adopted its own non-uniform versions of the “information exclusion” without reported crisis, and as the state of the Uniform Commercial Code is not a uniform one, this objection is not the end of discussion.<sup>103</sup> The uniformity concern is, however, one that will be noted in connection with specific proposals in the 2007 Bill and deserves evaluation.

### 2. *The Information/Goods Puzzle in § 2.103*

Chapter 2 of the Business & Commerce Code “applies to transactions in goods.”<sup>104</sup> Do software “information” licenses come within the ambit of such a statute? Should Chapter 2 apply directly, by analogy, or not at all to “transactions in information”? The 2003 Amendments exclude, but do not define, information from the defined term “goods.”<sup>105</sup> “‘Goods’ means all things that are movable at the time of identification to a contract for sale. . . . The term does not include information, the money in which the price is to be paid, investment securities under Article 8, the subject matter of foreign exchange transactions, or choses in action.”<sup>106</sup> The 2007 Bill proposed by the Texas Subcommittee does not follow the 2003 Amendments on this point.<sup>107</sup> The complexities of the “information exclusion” receive attention below.<sup>108</sup>

### 3. *Freedom of Contract and § 2.207*

By common consent and the number of critical articles, “[e]xisting Sec. 2-207, the ‘Battle of the Forms’, is one of the most litigated sections of Article 2

100. See *Hearings*, *supra* note 14, at 3:26 (testimony of Randy Burton); *id.* at 3:26 (testimony of Roy Anderson).

101. See Leary & Frisch, *supra* note 55, at 468.

102. See *Hearings*, *supra* note 14, at 4:20 (testimony of Jean Braucher); *id.* at 4:45 (testimony of Charles Keeton).

103. See OKLA. STAT. ANN. tit. 12A, §§ 2-105(1), 2-106(1) (West Supp. 2008); *Compaq Computer Corp. v. Lapray*, 135 S.W.3d, 657, 673-74 (Tex. 2004).

104. TEX. BUS. & COM. CODE ANN. § 2.102 (Vernon 1994).

105. See U.C.C. Art. 2 (amended 2003), 1 U.L.A. 360-593 (2004).

106. U.C.C. § 2-103(1)(k) (amended 2003), 1 U.L.A. 373 (2004).

107. See *infra* app. I, § 2.103(a)(11); app. II, § 2.103(a)(11).

108. See *infra* Part III.A.

and its clarification was an area ripe for reform by the revision process.”<sup>109</sup> The 2003 Amendments revise § 2-207 and cognate provisions in § 2-206, and those changes, with some modifications, appear in the Texas Subcommittee 2007 Bill.<sup>110</sup> The criticisms of amended § 2-207 come under three banners:

First, the amendments undercut “freedom of contract” and alter commercial practice and allocation of risk.<sup>111</sup>

Second, the amendments do not endorse, or conversely do not preclude, the “rolling contract” or “pay now, terms later” contract, often called the “Gateway” problem.<sup>112</sup>

Third, the amendments will result in litigation over new issues on contract formation and contract terms, while sacrificing years of legal effort (by both judges and lawyers) and current business practice under current § 2-207.<sup>113</sup>

#### 4. New Concepts of Liability

In some areas, critics of the 2003 Amendments assert that the statute would create, impose, or inject new sources of liability.<sup>114</sup> Some of the “usual suspects” in this category of new liabilities that appear in the 2007 Bill are summarized below.

The Remedial Promise. In response to developing confusion in case law over the “repair warranty,” the 2003 Amendments and the Texas Subcommittee’s 2007 Bill define, and provide rules regarding, a “remedial promise.” That term is defined as follows: “[A] promise by a seller to repair or replace goods or to refund all or part of the price upon the happening of a specified event.”<sup>115</sup>

109. Memorandum from Patricia Tauchert, Member, ABA UCC Comm., to Stephanie Heller, Chair, and Members, ABA UCC Comm. and Article 2 Subcomm., 2 (Sept. 30, 2003) (on file with author). The 1991 *Executive Summary* by the PEB Study Group targeted § 2-207 as a provision for revision: “[§ 2-207] has generated confusion in the courts, excessive litigation, and continuing criticism from the commentators.” PEB Study Group, *supra* note 58, at 1874.

110. Compare *infra* app. I, §§ 2.206-207, with U.C.C. §§ 2-206 to -207 (amended 2003), 1 U.L.A. 395-97 (2004).

111. See NCCUSL, AMENDMENTS TO UNIFORM COMMERCIAL CODE ARTICLES 2 AND 2A: SYNOPSIS 1, 3 (on file with author) (“A few, however, have objected, claiming that [amended 2-207] somehow removes from parties the right to define the terms of their bargain . . . .”); Memorandum from Jeff Dodd to Stephanie Heller, *supra* note 98, at 2 (“In short, [current § 2-207] allows the parties to control the basis upon which they will enter into a contract. The revisions proposed to § 2-207 do not. They eschew terms set by the parties and favor those to be fixed in a courthouse or by the drafters of Article 2.”); Letter from Charles R. Keeton to Stephanie Heller, Chair, ABA UCC Comm., 3 (Sept. 19, 2003) (on file with author); Letter from Quentin Riegel to Scott Sheehan, *supra* note 91, at 1 (“[The amendments] disfavor terms offered by contracting parties in favor of default rules not of their choosing.”).

112. *Hearings*, *supra* note 14, at 4:09 (testimony of Jean Braucher); Letter from Charles R. Keeton to Stephanie Heller, *supra* note 111, at 2; Memorandum from Holly K. Towle to Stephanie Heller, *supra* note 99, at 2.

113. Letter from Charles R. Keeton to Stephanie Heller, *supra* note 111, at 3.

114. See *infra* note 117 and accompanying text.

115. U.C.C. § 2-103(1)(n) (amended 2003), 1 U.L.A. 373 (2004); see *infra* app. I, § 2.103(a)(14).

The Remote Purchaser Warranty. New § 2-313A (in the 2007 Bill, § 2.313A) gives explicit recognition to a warranty or remedial promise set out in a record that is packaged with or accompanies new goods, that the seller reasonably expects to reach a remote purchaser, and that is, in fact, furnished to that purchaser.<sup>116</sup> Although one should evaluate whether the remedial promise and remote purchaser warranty provisions actually inject “new concepts” into the Code, those provisions have certainly drawn criticism as sources of “new liability” and of “uncertainty” in interpretation of a new statute.<sup>117</sup>

Consequential Damage Claims Against Buyers. On the other side, the 2003 Amendments and the 2007 Bill *do* allow for consequential damage recovery against *buyers*, a new provision, but one with a history of academic analysis.<sup>118</sup>

#### 5. *Revisions of Merchantability and Fitness Implied Warranty Disclaimer Rules*

The 2003 Amendments and the 2007 Bill as proposed by the Texas Subcommittee set out new required disclaimer provisions in the case of consumer contracts regarding implied warranties of fitness for a particular purpose and of merchantability.<sup>119</sup> These changes attracted criticism from industry and commentators, most often for requiring changes to existing form contracts, but in some instances as being an inaccurate statement of what actually occurs in light of other laws, e.g., the Magnuson-Moss Warranty Act.<sup>120</sup> In conjunction with these amendments of § 2-316, there are related amendments in the definition of “conspicuous.”<sup>121</sup>

#### 6. *Priorities Between Competing Purchasers of Entrusted Goods (Motor Vehicles)*

Section 2-403 of the Code (§ 2.403 of the Texas Business & Commerce Code) sets out a rule to determine the relative priorities of those who purchase

116. U.C.C. § 2-313A (amended 2003), 1 U.L.A. 430-31 (2004); *see infra* app. I, § 2.313A. The Texas Subcommittee deleted a companion change—the addition of § 2-313B on warranties and remedial promises to remote purchasers as a result of advertisements to the public. *Cf.* U.C.C. § 2-313B (amended 2003), 1 U.L.A. 433-34 (2004).

117. *See* Letter from Charles R. Keeton to Stephanie Heller, *supra* note 111, at 3-4.

118. *See* U.C.C. §§ 2-708 to -710(2) (amended 2003), 1 U.L.A. 533, 536-37 (2004); Roy Ryden Anderson, *In Support of Consequential Damages for Sellers*, 11 J.L. & COM. 123, 128-33 (1992) (discussing the concept of such liability); *infra* app. I, §§ 2.708-.710(b).

119. *See* U.C.C. § 2-316 (amended 2003), 1 U.L.A. 441-42 (2004); *infra* app. I, § 2.316.

120. *See* Memorandum from Holly K. Towle to Stephanie Heller, *supra* note 99, at 3 (discussing issues of statutory text inaccuracy and the necessity for revision of standard documents); *see also infra* Part III.C.1-3 (discussing the inter-connection of the Code with the Magnuson-Moss Act).

121. *See* U.C.C. §§ 2-103(1)(b), 2-316 (amended 2003), 1 U.L.A. 372, 441-42 (2004); *infra* app. I, § 2.103(a)(2).

goods entrusted to a merchant by the rightful owner.<sup>122</sup> But that provision operates unpredictably in conjunction with § 2-108 (§ 2.108 of the Texas Business & Commerce Code) which makes a statutory cross-reference to the Certificate of Title Act.<sup>123</sup> Existing case law in Texas diverges on the correct interpretation of the two laws<sup>124</sup> and proposed §§ 2.108 and 2.403 provide a statement of the better, and expected, result.

### 7. Changes in the UCC Statute of Limitations

The initial study of UCC revisions by the PEB Study Group and the review of its *Preliminary Report* by the ABA Task Force both included questions about the operation of § 2-725 of the Code.<sup>125</sup> In addition to questions about the application of the Code's limitations rules to claims under existing provisions, the inclusion of remedial promise and remote purchaser obligations in the 2003 Amendments required the drafters to account for those new obligations in the overall statute of limitations. The revisions also needed to address the then-perceived need to provide some discovery rule relief, which led to other changes.<sup>126</sup>

Changes that alter or extend limitations periods attract opposition. The inclusion of an expanded period for discovery in the limitations revisions also provoked comment simply on the basis of uncertainty of outcome.<sup>127</sup> The result of the revisions is an amended § 2-725 that is longer and more complex than the present provision. The principles and pattern of current § 2-725 remain visible in amended § 2-725.

### 8. National Provisions Not Included in the 2007 Bill

As a result of the Texas Subcommittee's extended examination of the 2003 Amendments, the proposed 2007 Bill rejects several changes proposed in the Article 2 amendments as approved by the ALI and NCCUSL and adds or retains other provisions to preserve sound results reached under the existing statute.<sup>128</sup> The road map to these "non-standard" proposals is the Texas

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122. U.C.C. § 2-403 (amended 2003), 1 U.L.A. 460-61 (2004); *see also* TEX. BUS. & COM. CODE ANN. § 2.403 (Vernon 1994).

123. *See* TEX. TRANSP. CODE ANN. §§ 501.001-.151 (Vernon 2007); U.C.C. § 2-108 (amended 2003), 1 U.L.A. 383 (2004) (referring to § 2-403); *infra* app. I, § 2.108 (referring to § 2.403 and the Certificate of Title Act).

124. *See* Jonathon C. Clark, *Dude, Where's My Car? How the Proposed Uniform Certificate of Title Act Addresses Conflicts Between the Texas Certificate of Title Act and the Uniform Commercial Code*, 62 CONSUMER FIN. L.Q. REP. (2009) (forthcoming).

125. ABA Task Force, *Appraisal*, *supra* note 57, at 1246-50.

126. "The root cause of the different results in the cases is the perceived injustice caused by the [original] drafters' decision to choose tender of delivery as the time when a breach of warranty occurs and a cause of action accrues . . ." ABA Task Force, *Appraisal*, *supra* note 57, at 1248.

127. *See* Letter from Charles R. Keeton to Stephanie Heller, *supra* note 111, at 4.

128. *See infra* app. I.

Subcommittee's Bill Analysis, which is reproduced as Appendix II to this Article.<sup>129</sup> The non-standard provisions of the draft 2007 Bill are of two fundamental types: changes made (or not made) for conformity with other uniform laws enacted in Texas, and changes made (or not made) to state the better rule under the case law and legal principles of Chapter 2. They are summarized in that order below.<sup>130</sup>

*a. Conforming Modifications*

*i. Definitions*

Section 2.103 of the proposed 2007 Bill omits the definition of "consumer" proposed for Chapter 2 by the 2003 Amendments in addition to omitting definitions of "good faith" and "record," as recommended in the 2003 Amendments for jurisdictions that have enacted amendments of Chapter 1.<sup>131</sup> These three terms are currently defined in § 1.201(b)(11), (b)(20) and (b)(31) of Chapter 1 of the Texas Business & Commerce Code.<sup>132</sup>

Two definitional items in the 2003 Amendments that would make substantive change received specific attention in the preparation of drafts by the Texas Subcommittee. The Texas Subcommittee disagreed on substantive grounds with the portion of Official Comment 9 regarding proposed § 2.103 that suggested a seller's post-sale promise to correct a problem might not constitute a remedial promise, as newly defined in § 2.103.<sup>133</sup> Also on substantive grounds, the Texas Subcommittee disagreed with the proposed statutory exclusion of information from the scope-related definition of goods.<sup>134</sup> The remedial promise and goods-information issues receive fuller attention below.

*ii. Coordination of Statutory Provisions*

The Texas Subcommittee's draft 2007 Bill omits several operative provisions from Chapter 2 in deference to existing provisions of the Uniform Electronic Transactions Act (UETA).<sup>135</sup> Sections 2-211 through 2-313 of the

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129. See *infra* app. II.

130. See discussion *infra* Part II.B.8.a-c.

131. See *infra* app. I, § 2.103(a)(3), (10), (13); see also U.C.C. § 2-103(1)(c), (j), (m) (amended 2003), 1 U.L.A. 372 (2004).

132. TEX. BUS. & COM. CODE ANN. § 1.201(b)(11), (20), (31) (Vernon 1994 & Supp. 2008).

133. See *infra* app. II § 2.103; see also *infra* Part III.C (reviewing the subcommittee's disagreement on comments as to post-sale remedial promises).

134. See *infra* app. II, § 2.103; see also *infra* Part III.A.1-2 (reviewing the goods-information issue and the proposed statutory exclusion of information from the definition of goods).

135. TEX. BUS. & COM. CODE ANN. §§ 43.001-43.021 (Vernon 2002 & Supp. 2008) (codifying the UETA in Texas). Effective April 1, 2009, Chapter 43 will be repealed and Chapter 322 will become effective, reenacting UETA as part of a statutory revision, stated to be nonsubstantive, of miscellaneous commercial laws. See Act of May 15, 2008, 80th Leg., R.S., ch. 885, 2007 Tex. Gen. Laws 1905.

2003 Amendments replicate or slightly modify provisions currently found in §§ 43.007(a)-(b), 43.005(a), 43.009(a), and 43.015(e)-(f) within UETA.<sup>136</sup> Further, § 2-211(4) would adopt a provision from the much-discussed Uniform Computer Information Transactions Act.<sup>137</sup> Related to these electronic contracting provisions of the 2003 Amendments is proposed § 2-204(4) of the 2003 Amendments, which is partly taken from § 43.014(b) and (c) of UETA as enacted in Texas but also adds a new rule in proposed § 2-204(4)(b)(ii) that received strong criticism from consumer groups.<sup>138</sup> The Texas Subcommittee proposal recommends that the UETA provisions control. The parallel provisions and changes proposed as §§ 2-211 through 2-213 and the disputed change at § 2.204(d), corresponding to § 2-204(4) of the 2003 Amendments, are deleted from the 2007 Bill.<sup>139</sup>

*b. Non-uniform Modifications and Changes in the 2007 Bill*

*i. Section 2-313B*

Section § 2-313B of the 2003 Amendments would give statutory recognition to certain types of obligations to remote purchasers on the basis of “an advertisement or similar communication to the public” in defined circumstances.<sup>140</sup> In structure and terminology, it reads very much like proposed § 2-313A regarding obligations arising on the basis of a “record packaged with or accompanying the goods” and is discussed below.<sup>141</sup> The Texas Subcommittee included a revised § 2.313A in the draft 2007 Bill,<sup>142</sup> but it recommended against § 2-313B.<sup>143</sup>

*ii. Section 2.318*

As Texas presently has a unique § 2.318, which adopts none of the three standard options and leaves the question of third party beneficiaries of

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136. See TEX. BUS. & COM. CODE ANN. §§ 43.005, .007, .015; U.C.C. §§ 2-211 to -213 (amended 2003), 1 U.L.A. 405-406 (2004); *infra* app. II §§ 2.211-.213; see also UNIF. COMPUTER INFO. TRANSACTIONS ACT (amended 2002), 7.II U.L.A. 195 (2002 & Supp. 2008).

137. See U.C.C. § 2-211 cmt. 1 (amended 2003).

138. See *infra* app. II, § 2.204.

139. See *infra* app. II, §§ 2.204, 2.211-.213.

140. U.C.C. § 2-313B(3) (amended 2003), 1 U.L.A. 433-34 (2004).

141. See *infra* Part III.D; app. I, § 2.313A(c).

142. See *infra* app. I, § 2.313A. A Texas-specific, non-standard revision proposed in § 2.313A in the 2007 Bill is the inclusion of a new subsection (g) to tie directly with the proposed non-standard version of § 2.318 and carry forward the unique Texas provision for judicial determination of the availability of UCC causes of action to third persons not specifically within the statutory text. See *infra* app. I, § 2.313A(g).

143. See *infra* app. II, § 2.313A-B. “Although the two sections have almost the same words, their foundations in the cases and in the expectations of buyers and sellers are very different. Section 2-313A is wise and its foundation is strong; § 2-313B is of doubtful wisdom and its foundation is weak.” WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 103.

warranties to judicial resolution, the Texas Subcommittee recommends a similar, non-standard provision as § 2.318 in the 2007 Bill.<sup>144</sup> A coordinating addition to proposed § 2.313A is found in that section.<sup>145</sup>

*iii. Sections 2.206(c) and 2.207(a)*

As discussed below, the Texas Subcommittee draft recommends retaining the qualifying clause currently found in § 2.207(a)—“unless acceptance is expressly made conditional on assent to the additional or different terms”—as part of proposed § 2.206(c).<sup>146</sup> The 2007 Bill makes other clarifying changes to the standard introductory provision of § 2.207 to conform that introductory text with the contract formation provisions of amended Chapter 2.<sup>147</sup>

*iv. Sections 2.608 and 2.606*

Section 2-608 in the 2003 Amendments would add a new subsection (4) that deals with a buyer’s use of goods after rightful rejection or revocation of acceptance of the goods.<sup>148</sup> The Texas Subcommittee recognized that this amendment reflected existing case law when applied to a revocation of acceptance case but questioned extending the reasonable use doctrine to rightful rejection cases.<sup>149</sup> The 2007 Bill statutorily limits the reasonable continued use doctrine to the revocation of acceptance cases where it originated and does not statutorily extend it to rejection cases.<sup>150</sup>

To conform § 2.606 of the 2007 Bill with this limitation in § 2.608, the Texas Subcommittee revised § 2.606(a)(3) regarding acceptance to delete a cross reference to § 2.608.<sup>151</sup>

*v. Section 2.607*

Section 2.607(3)(a) of the 2003 Amendments would change the rules regarding a buyer’s notice to the seller of a defect in accepted goods.<sup>152</sup> The amendment as proposed would bar the buyer from its remedies regarding acceptance of defective goods “only to the extent that the seller is prejudiced by the failure” of the buyer to give notice.<sup>153</sup> In the Texas Subcommittee’s view,

144. *See infra* app. I, § 2.318; app. II, § 2.318.

145. *See infra* app. I, § 2.313A(g).

146. *Compare infra* app. I, § 2.206(c), with TEX. BUS. & COM. CODE ANN. § 2.207(a) (Vernon 1994). The relocation of the Chapter 2 provision on acceptance of an offer to § 2.206 in the 2007 Bill and the reasons for retaining the unless clause are discussed below. *See infra* Part III.B.

147. *See infra* app. I, § 2.207; *see also infra* app. II, § 2.207.

148. U.C.C. § 2-608(4) (amended 2003), 1 U.L.A. 502 (2004).

149. *See infra* app. II, § 2.608.

150. *See infra* app. I, § 2.608(d); app. II, § 2.608.

151. *See infra* app. I, § 2.606(a)(3); app. II, § 2.606.

152. *See* U.C.C. § 2-607(3)(a) (amended 2003), 1 U.L.A. 499 (2004).

153. *Id.*

the change proposed is both substantial and questionable.<sup>154</sup> The proposed 2007 Bill retains the text of current § 2.607(c)(1) on this point.<sup>155</sup>

*c. Modifications Affecting Remedies and Damages*

The Texas Subcommittee made several non-uniform changes to the remedies and damages provisions of the 2003 Amendments in the course of preparing the 2007 Bill. Particular modifications to §§ 2.701 through 2.718 are summarized below.

*i. Mitigation of Damages: §§ 2.703 and 2.711*

The Texas Subcommittee added parallel provisions in §§ 2.703 and 2.711, which outline the basic remedies of buyers and sellers under Chapter 2, to carry forward mitigation of damages principles recommended in the initial PEB Study Group *Preliminary Report* and by the ABA Task Force.<sup>156</sup> The 1999 draft of the then-proposed revision of Article 2, prepared for the NCCUSL annual meeting, expressly stated that an aggrieved party could not, unless an otherwise enforceable liquidated damages or limited remedy provision applied, recover damages “that could have been avoided by reasonable measures under the circumstances.”<sup>157</sup> The Texas Subcommittee added §§ 2.703(d) and 2.711(d) in the 2007 Bill to make explicit in the proposed Texas legislation the application of this mitigation principle to remedies available under Chapter 2.<sup>158</sup>

*ii. Seller’s Resale, Buyer’s Cover, and Mitigation: §§ 2.706 and 2.712*

In keeping with its modifications of §§ 2.703 and 2.711 to emphasize the mitigation principle and consistent with the just compensation standard of

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154. See *infra* app. II, § 2.607.

155. Compare *infra* app. I, § 2.607(c)(1), with TEX. BUS. & COM. CODE ANN. § 2.607(c)(1) (Vernon 1994).

156. ABA Task Force, *Appraisal*, *supra* note 58, at 1203-06.

157. NAT’L CONFERENCE OF COMM’RS ON UNIF. STATE LAWS, PROPOSED REVISIONS OF UNIFORM COMMERCIAL CODE ARTICLE 2—SALES § 2-803(b) (July 1999 Draft). The then-structure of the Article 2 revisions placed “Remedies” in a new Part 8, which applied to buyers, sellers, and other persons who were entitled to enforce obligations under Article 2. The mitigation of damages principle in § 2-803 had general application to remedies under that Part 8, and § 2-803 itself referred back to § 1-106, now § 1-305, of the UCC for the more general principle of just compensation: Article 2 remedies are to be liberally administered “to the end that the aggrieved party may be put in as good a position as if the other party had fully performed” but with special, consequential, and penal damages only available if “specifically provided by [the UCC] or other rule of law.” U.C.C. § 1-305, 1 U.L.A. 47 (2004); see TEX. BUS. & COM. CODE ANN. § 1.305 (Vernon Supp. 2008). Professor Anderson discusses the compensation and mitigation principles in the context of the development of the 2003 Amendments in Roy Ryden Anderson, *Of Hidden Agendas, Naked Emperors, and a Few Good Soldiers: The Conference’s Breach of Promise . . . Regarding Article 2 Damage Remedies*, 54 SMU L. Rev. 795, 799–802 (2001).

158. See *infra* app. I, §§ 2.703(d), 2.711(d); app. II, §§ 2.703, 2.711; see also Anderson, *supra* note 157, at 805, 822.

§ 1.305, the Texas Subcommittee also added specific non-uniform provisions in §§ 2.706 and 2.712. The particular revision in § 2.706 is the modification of subsection (g) by adding the clause shown in italics below:

(g) Failure of the seller to resell does not bar the seller from any other remedy, *but to the extent that the seller makes a proper resale under this section the seller may not recover greater damages based on a market price under Section 2.708.*<sup>159</sup>

As the Texas Subcommittee's Bill Analysis points out, this addition (1) applies to Chapter 2 seller's remedies the same standard as applies under the United Nations Convention on Contracts for the International Sale of Goods (CISG), (2) furthers the general principles noted above of allowing "full compensation to the aggrieved party subject to the aggrieved party's obligation to act reasonably to mitigate damages," and (3) produces consistency with the current and proposed treatment of buyers in regard to cover.<sup>160</sup>

For aggrieved buyers, the remedy matching resale by a seller is the cover remedy set out in § 2.712. To incorporate explicitly the just compensation principles in the buyer's cover remedy, the Texas Subcommittee proposed a non-uniform § 2.712(c), which corresponds to the addition made as § 2.706(g), as follows:

(c) Failure of the buyer to effect cover within this section does not bar the buyer from any other remedy, *but to the extent the buyer makes a proper cover under this section the buyer may not recover damages based on market price under the next section.*<sup>161</sup>

As the Bill Analysis observes, similar to its discussion regarding § 2.706(g), this non-uniform amendment to § 2.712(c) follows the CISG and reflects the consistent holdings of courts dealing with present § 2.712 and Official Comment 5 to § 2.713.<sup>162</sup> This modification also carries out the goal of making explicit the application of the general principles of just compensation and mitigation of damages.

### *iii. Liquidated Damages Modifications: § 2.718*

The 2003 Amendments proposed several substantial changes in the rules for liquidated damages provisions.<sup>163</sup> The Texas Subcommittee rejected all the proposed changes in § 2-718, save one, and recommended retention of the

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159. See *infra* app. I, § 2.706(g) (emphasis added).

160. See *infra* app. II, § 2.706; see also Anderson, *supra* note 157, at 806–11 (giving a thorough explication of the operation of the resale and market damage mechanisms under this provision).

161. See *infra* app. I, § 2.712(c) (emphasis added).

162. See *infra* app. II, § 2.712.

163. See U.C.C. § 2-718 (as amended 2003), 1 U.L.A. 549 (2004).

present day § 2.718 as the baseline provision on liquidated damages, with modifications.<sup>164</sup> The Bill Analysis provides an extended review of common law and Texas case law principles and of current UCC decisions as to liquidated damage provisions in support of the recommendation that the extensive revisions for liquidated damages be rejected and limited amendments be adopted.<sup>165</sup>

*iv. Amendment of § 2.713*

The amendments to § 2-713 in the 2003 Amendments affect the determination of a buyer's damages on repudiation or non-delivery. The Texas Subcommittee disagreed with a change in the "timing" of the measurement of damages as to non-delivery (and revocation) and recommended changes in the timing provisions of both affected subparts.<sup>166</sup> As revised in the 2007 Bill, the time at which damages are determined in a non-delivery or revocation of acceptance case would remain "when the buyer learned of the breach" and, in the case of a repudiation, would be the time when the buyer learned of the breach "but no later than the time for tender under the contract."<sup>167</sup> These are sensible modifications of the 2003 Amendments.

*v. Specific Performance Under § 2.716*

The 2003 Amendments expand the availability of specific performance in commercial contracts where the parties have agreed to the remedy, with some limitations, and the 2007 Bill includes those changes. The Texas Subcommittee proposed a drafting change, however, by inserting "also" into § 2.716(a), thereby endorsing the specific performance remedy where included in a commercial contract and indicating that the granting of such equitable relief remains in the court's discretion and is not purely a matter of contract. The agreement of the commercial parties to such relief is a factor to be considered, but that contractual term "cannot determine the court's discretion."<sup>168</sup>

### III. ASSESSING THE CHANGES FOR TEXAS

There is no easy portal for entry into an evaluation of the Article 2 amendments. The amendments are all interconnected, and there is more history than can be comprehended, both as to the "Original Code" of the 1950s and as

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164. See *infra* app. II, § 2.718; see also Anderson, *supra* note 157, at 838–40.

165. See *infra* app. II, § 2.718.

166. See *infra* app. II, § 2.713.

167. See *infra* app. I, § 2.713(a); app. II, § 2.713(a).

168. See *infra* app. II, § 2.716.

to the 2003 Amendments.<sup>169</sup> With that warning, we set off into the forest seeking to find a few clearings along the way.

### A. *The Information Exclusion*

In the early going, the definition of “goods” in existing § 2-105 was not highlighted for revision.<sup>170</sup> Neither the *Preliminary Report* of the Study Group appointed by the Permanent Editorial Board nor the ABA Task Force *Appraisal* identified § 2-105 for change.<sup>171</sup> Although the initial working groups did not immediately highlight the definitions of “goods” and “information” as critical issues,<sup>172</sup> the issue of whether “information”—principally computer software—was “in or out” of the Code had surfaced in the analysis of “scope” under § 2-102, often as an offshoot of the “goods-services” confusion:

A current example *of some interest* is a contract for the sale or license of computer systems, which involves hardware, software and various backup services. Are these “transactions in goods” to which Article 2 should apply? Is scope an either-or proposition or is there room for a selective application of relevant Article 2 sections to a part of the transaction?<sup>173</sup>

In the PEB Study Group’s *Executive Summary* of its *Preliminary Report*, the issue was not better focused.<sup>174</sup> Under the heading “Summary of Areas Where Revision Was Urged by Commentators But Where Study Group Disagreed,” the *Executive Summary* reported on three recurring “scope”

169. See, e.g., John D. Wladis, *U.C.C. Section 2-207: The Drafting History*, 49 BUS. LAW. 1029, 1029-30 n.3 (1994) (describing sources consulted on the drafting history of § 2-207). Professor Anderson cautioned against reliance on the drafting committee’s legislative history in seeking definitive answers on questions of interpretation: “Even those of us who have participated actively over the past several years in the Article 2 revision process, for example, would undoubtedly find either humorous or naive an attempt by any of us to argue an interpretation based on the ‘drafting history’ of this Article 2 revision process.” Anderson, *supra* note 157, at 800-01.

170. See U.C.C. § 2-105 (as amended 2003), 1 U.L.A. 379 (2004); see also TEX. BUS. & COM. CODE ANN. § 2.105(a) (Vernon 1994). Current § 2.105(a) of the Texas Business & Commerce Code provides:

(a) “Goods” means 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. “Goods” also includes the unborn young of animals and growing crops and other identified things attached to realty as described in . . . § 2.107.

171. ABA Task Force, *Appraisal*, *supra* note 57, at 1031. Although there were comments regarding scope under § 2-102 in the context of the lack of precision in the key phrase—particularly for “mixed” transactions—the scope standard of “transaction in goods” was ultimately unchanged. PEB STUDY GROUP, PRELIMINARY REPORT, *reprinted in* ABA Task Force, *Appraisal*, *supra* note 57, at 1024.

172. *Id.*; see also Leary & Frisch, *supra* note 55, at 462 (identifying “computer to computer ordering” as a revision issue under both the Statute of Frauds and Parol Evidence Rule, but not “information issues”).

173. PEB STUDY GROUP, PRELIMINARY REPORT, *reprinted in* ABA Task Force, *Appraisal*, *supra* note 57, at 1023 (emphasis added); see also Note, *Computer Programs as Goods Under the U.C.C.*, 77 MICH. L. REV. 1149, 1150 (1979) (arguing that “contracts for program copies are, in most contexts, transactions within the scope of Article 2”).

174. See *supra* note 173 and accompanying text.

questions that the Study Group had not found to be in need of revision but still deserved study.<sup>175</sup> Two were of a general character (“To what transactions involving goods should Article 2 apply” and “If Article 2 does not apply directly, when should a court extend it by analogy”), and none targeted the “goods-information” split.<sup>176</sup> In fact, the Study Group observed that the two questions quoted above, “although important, could be adequately answered by the courts under the current statute.”<sup>177</sup>

### 1. *The Information Issue in Interim National Drafts*

At the same time, however, the information-scope question was gaining visibility, including commentary by members of the Study Group.<sup>178</sup> Professor Boss, a member of the Study Group and an active participant in the ABA’s work on the Code, observed that changes not addressed in revision projects at that time included “the advent of computer technology and the transfer of rights of both a tangible and intangible variety [and] the increased use of licensing and other forms of transfers other than sales or leases,” which resulted in an increasing strain on the Uniform Commercial Code.<sup>179</sup>

However quiet its origins, the “goods-information” split quickly became a major issue in the Article 2 revision project.<sup>180</sup> In 1992, the NCCUSL merged its Special Committee on Software Contracts with the Drafting Committee on Article 2 and requested the combined committee to consider licenses of technology in the Article 2 project.<sup>181</sup> The merger and the evaluation of drafting structures led to the ultimate abandonment of the hub-and-spoke plan for a statute that would cover sales of goods; licenses; and contracts for intangibles, leases, and services.<sup>182</sup> In 1995, the NCCUSL stepped back from the hub-and-spoke structure, re-split the committees, and resumed the Article 2 project with its original focus.<sup>183</sup> The Computer and Technology Licensing Project Committee set out to draft a new Article 2B of the Code but subsequently realigned its work to produce a uniform statute—the Uniform Computer Information Transactions Act (UCITA)—that is separate from the

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175. PEB Study Group, *supra* note 58, at 1875.

176. *Id.* at 1875, 1878 (setting out the Study Group’s views after review of comments on its Preliminary Report).

177. *Id.* at 1875-76. Indeed, that position from 1991 is where the Texas Subcommittee proposed 2007 Bill came to rest on the “goods-information” issue. *See infra* Part III.A.4.

178. *See infra* note 179 and accompanying text.

179. Amelia H. Boss, *Developments on the Fringe: Article 2 Revisions, Computer Contracting, and Suretyship*, 46 BUS. LAW. 1803, 1807 (1991).

180. *See infra* notes 181-87 and accompanying text.

181. WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 406.

182. *Id.* at 407; *see also* Rusch, *supra* note 1, at 1686.

183. WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 408.

UCC.<sup>184</sup> In 1999, the NCCUSL completed and promulgated the UCITA,<sup>185</sup> which is under its own storm clouds. Only Virginia and Maryland have enacted the statute.<sup>186</sup> Some non-adopting states have taken the unusual step of enacting “bomb-shelter” laws to disable a contractual choice of law by making the law of a UCITA jurisdiction voidable in a computer-information transaction if enforcement is sought against a resident of the shelter state.<sup>187</sup>

After the removal of Article 2B—soon to be UCITA—from the Article 2 revision project, the Drafting Committee then had to address goods and information in Article 2 itself. One place where that debate occurred is in § 2-102 on scope, and another is in the definitions. The drafters found the following text in § 2-102: “Unless the context otherwise requires, this Article applies to transactions in goods; it does not apply to any transaction which although in the form of an unconditional contract to sell or present sale is intended to operate only as a security transaction . . . .”<sup>188</sup> As judges and lawyers will predict, and as the PEB Study Group *Preliminary Report* and the ABA Task Force *Appraisal* observed, the phrase “unless the context otherwise requires” does not promote clarity.<sup>189</sup> Similarly, “transactions in goods” offers opportunities for expanding the application of a statute with an otherwise limiting title of “Sales.”<sup>190</sup>

In the context of the “goods-information” argument, and with the example of other revisions then under way (for example, the revision of Article 9 of the Code that created extensive new definitions for secured transactions law), it is not surprising that the Article 2 Drafting Committee attempted a fairly specific statement about the place in, or outside of, Article 2 for transactions that involved computer information. In the July 2000 draft of amendments to Article 2, and reflecting efforts made in the 1999 draft, definitions of (1) “computer,” (2) “computer information,” and (3) “computer program” led to

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184. See *id.* (noting that UCITA is not part of the UCC but rather a NCCUSL Uniform Act); Rusch, *supra* note 1, at 1686; see also UNIF. COMPUTER INFO. TRANSACTIONS ACT (amended 2002), 7.II U.L.A. 195 (2002 & Supp. 2008).

185. NAT’L CONFERENCE OF COMM’RS ON UNIF. STATE LAWS, HANDBOOK OF THE NATIONAL CONFERENCE OF COMMISSIONERS ON UNIFORM STATE LAWS AND PROCEEDINGS OF THE ANNUAL CONFERENCE MEETING IN ITS 108TH YEAR 83-84 (1999) (Adoption of the Uniform Computer Information Transaction Act by the States); Christina Bohannon, *Copyright Preemption of Contracts*, 67 MD. L. REV. 616, 621-22 (2008). The NCCUSL subsequently amended this act in 2002. See UNIF. COMPUTER INFO. TRANSACTIONS ACT, 7.II U.L.A. 9 (Supp. 2008).

186. UNIF. COMPUTER INFO. TRANSACTIONS ACT (amended 2002), 7.II U.L.A. 195 (2002) (providing a table of jurisdictions wherein the act has been adopted); see Abby J. Hardwick, Note, *Amending the Uniform Commercial Code: How Will a Change in Scope Alter the Concept of Goods?*, 82 WASH. U. L.Q. 275, 286 n.93 (2004); Fred H. Miller, *Writing Your Own Rules: Contracting Out of (and into) the Uniform Commercial Code; Intrastate Choice of Law*, 40 LOY. L.A. L. REV. 217, 223 n.49 (2006).

187. See Harwick, *supra* note 186, at 286-87 (identifying Iowa, Vermont, West Virginia, and North Carolina as “bomb-shelter” states); Miller, *supra* note 186, at 225 n.60.

188. U.C.C. § 2-102 (amended 2003), 1 U.L.A. 371 (2004). Not to give away the story line, but the 2003 Amendments ultimately made no change in § 2-102. See *id.* § 2-102 note.

189. PEB STUDY GROUP, PRELIMINARY REPORT, reprinted in ABA Task Force, *Appraisal*, *supra* note 57, at 1023-25; ABA Task Force, *Appraisal*, *supra* note 57, at 1025-28.

190. *Id.* at 1024.

a detailed treatment of transactions that included both goods and computer information and that included a general rule that Article 2 “applies to the goods but not to the computer information or information rights in it.”<sup>191</sup> If a copy of a computer program were contained in and sold as part of goods, then Article 2 would apply to the copy and computer program *unless* (1) the goods sold were a computer or computer peripheral, or (2) giving the buyer use of or access to the program ordinarily would be a substantial purpose of transactions in goods of that type, in which case UCITA is the presumptively applicable law with respect to the copy and computer program that were included in the transaction.<sup>192</sup> And further, if a conflict were to arise between amended Article 2 and UCITA regarding the extent to which Article 2 applies to the copy of a computer program, UCITA would control.<sup>193</sup> It is fair to say that the “specific drafting” approach to scope in the July 2000 draft was not a model of clarity and that it dealt with a controversial issue. By the time of publication of the November 2000 Draft Revision of Uniform Commercial Code Article 2—Sales, these definitions were omitted and § 2-103 did not appear.<sup>194</sup> In February 2001, the reporters issued a revised § 2-103 with preliminary comments that modified the July 2000 text by, among other things, dropping the detailed § 2-103(b).<sup>195</sup>

On the attempted 1999-2000 revision of § 2-103 to deal with computer programs, one law review commentary noted that the Committee’s effort to deal with the “goods vs. information” conflict ran into problems after just one sentence: “The major difficulties in interpreting proposed Section 2-103(b) begin with the second sentence.”<sup>196</sup> Beyond difficulties in interpretation, however, the “goods vs. information” conflict rested on an intractable policy issue.<sup>197</sup> White and Summers capture it well:

[The split between NCCUSL and ALI over the disposition of UCITA] left many angry people on each side. . . .

This anger ensured that the bargaining over the scope provision in Amended Article 2 would be difficult. The consumers, licensees and some

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191. NAT’L CONFERENCE OF COMM’RS ON UNIF. STATE LAWS, REVISION OF UNIFORM COMMERCIAL CODE ARTICLE 2—SALES 24 (July 28-Aug. 4, 2000) [hereinafter NCCUSL, REVISION], available at <http://www.law.upenn.edu/bll/archives/ulc/ucc2/ucc20600.pdf> (discussing §§ 2-102 and 2-103). Drafting of the highly defined Article 9 revisions began in 1993 and led to NCCUSL and ALI approval of the proposed revisions in 1998. See U.C.C. § 9-101 cmt. 2, 3 U.L.A. 39 (2002).

192. NCCUSL, REVISION, *supra* note 191, at 23-29 (text and comments at UCC § 2-103 and particularly § 2-103(b), (c), (e), (f)).

193. *Id.*

194. NAT’L CONFERENCE OF COMM’RS ON UNIF. STATE LAWS, REVISION OF UNIFORM COMMERCIAL CODE ARTICLE 2—SALES 1-10 (Nov. 2000), available at <http://www.law.upenn.edu/bll/archives/ulc/ucc2/21100.pdf>.

195. NAT’L CONFERENCE OF COMM’RS ON UNIF. STATE LAWS, § 2-103. SCOPE (Feb. 2001), available at <http://www.law.upenn.edu/bll/archives/ulc/ucc2a/scope01.pdf>.

196. Ann Lousin, *Proposed UCC 2-103 of the 2000 Version of the Revision Article 2*, 54 SMU L. REV. 913, 918 (2001).

197. See *infra* note 198 and accompanying text.

others . . . wished to include every conceivable software/goods transaction in Article 2. In order to find their way to UCITA (or, more likely to the common law of contracts since UCITA has been adopted . . . only in Virginia and Maryland), the licensors wanted every possible transaction excluded from Article 2.

. . . .

In April 2001, the revision of Article 2 took a radical turn. The drafters, fearing software industry opposition, decided to remove the proposed software scope provision. Amended Article 2 reverts to the scope provision found in old 2-102.<sup>198</sup>

### 2. Information in the 2003 Amendments—The Definition

In the end, the national drafting committee changed the definition of “goods” by adding an “exclusion” for information, and they moved that definition out of current § 2-105, where it resided, to amended § 2-103.<sup>199</sup> The proposed new standard § 2-103(1)(k) reads:

“Goods” means all thing that are moveable at the time of identification to a contract for sale. The term includes future goods, specially manufactured goods, the unborn young of animals, growing crops, and other identified things attached to realty as described in Section 2-107. The term does not include information, the money in which the price is to be paid, investment securities under Article 8, the subject matter of foreign exchange transactions, or choses in action.<sup>200</sup>

The accompanying official comment then sets out a short essay on what an exclusion of undefined “information” means, suggests, and leaves open.<sup>201</sup> That comment includes an invitation to the courts to figure all this out: “When a transaction includes both the sale of goods and the transfer of rights in information, it is up to the courts to determine whether the transaction is entirely within or outside of this article, or whether or to what extent this article should be applied to a portion of the transaction.”<sup>202</sup>

The approach in § 2-103 and Comment 7 drew fire from all sides:

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198. WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 53.

199. See U.C.C. § 2-103 (amended 2003), 1 U.L.A. 373 (2004). The new definition is found in § 2-103(1)(k), and it also excludes, without controversy, “the subject matter of foreign exchange transactions.” *Id.*; see also *supra* note 170 (quoting TEX. BUS. & COM. CODE ANN. § 2.105(a) (Vernon 1994) (defining “goods”)).

200. U.C.C. § 2-103 (1)(k) (amended 2003), 1 U.L.A. 373 (2004).

201. U.C.C. § 2-103 cmt. 7 (amended 2003), 1 U.L.A. 375-76 (2004).

202. *Id.* Comment 7 does provide specific examples of what is “in” Article 2 (sales of “smart goods,” such as an automobile) and what is “out” (an electronic download of a computer program). *Id.* (citing *Specht v. Netscape*, 150 F. Supp. 2d 585 (S.D.N.Y. 2001), *aff’d* 306 F.3d 17 (2d Cir. 2002)).

- “[T]he new exclusion of ‘information’ from the definition of goods will destabilize the law of transactions in software and digital content.”<sup>203</sup>
- “I believe that this exclusion will, over time, eviscerate Article 2’s pre-eminent status as the basic law of the sale of goods.”<sup>204</sup>
- “Article 2 was originally written . . . only to cover goods. Appropriately and consequently, the proposed black-letter excludes information from the definition of goods. Yet the proposed comment . . . invites courts to apply Article 2 to all or part of any transaction involving both goods and information without standards, rationale or direction.”<sup>205</sup>
- “The final revisions excluded computer information from the definition of goods, a positive step, but abandoned the effort to deal with smart goods.”<sup>206</sup>
- “[T]he introduction of the undefined term ‘information’ conflates traditionally and rationally separate treatments of different types of information: Information intended for conceptual processing by the human mind—often referred to as ‘content’—ordinarily is not addressed by [Articles 2 and 2A]. Information that determines the function of a machine . . . ordinarily is addressed by [Articles 2 and 2A]: a wrong setting is as much a defect . . . as a structural fault.”<sup>207</sup>

### 3. Information and the 2007 Bill

The experience of the Texas Subcommittee was similar to that at the national level, with concerns about the exclusion, or inclusion, of “information” coming from industry and consumer interests.<sup>208</sup> As a consequence of the continuing inability of the affected interest groups and the national organizations to find a consensus position on a *new* statement of scope and the related definition of goods (or information) and to move past the unrelenting conflict over a statutory resolution of the goods-information issues, the Texas Subcommittee recommended that the 2007 Bill retain its present provisions in regard to “goods,” which is a non-uniform response, and that the 2007 Bill also

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203. Letter from Miriam Nisbet, President of Ams. for Fair Elec. Commerce Transactions, to Michael Traynor, President, ALL, 1 (April 21, 2003), *available at* <http://ucita.com/pdf/TraynorART2.pdf>.

204. Memorandum from Gail Hillebrand, Consumers Union, to ABA Bus. Law Section UCC Comm. Members, 1 (Sept. 4, 2003).

205. Memorandum from Holly K. Towle to Stephanie Heller, *supra* note 99, at 1-2.

206. Memorandum from Patricia Tauchert to Stephanie Heller, *supra* note 109, at 3.

207. Memorandum from Stephen Y. Chow to Stephen Sepinuck 2 (Sept. 19, 2003) (on file with author).

208. *See* Memorandum from James Leeland, Co-Chairman, Tex. Subcomm., to Tex. Subcomm. Members (discussing August 28, 2006 and September 6, 2006 telephone conferences of the Texas Subcommittee with Holly Towle and Jean Braucher) (on file with author). The multiple sources of criticism of the information exclusion are reviewed in Jean Braucher, *Contracting Out of Article 2 Using a “License” Label: A Strategy That Should Not Work for Software Products*, 40 LOY. L.A. L. REV. 261, 269 n.41 (2006).

keep the existing “scope” provisions, which is the uniform approach.<sup>209</sup> The Texas Subcommittee explained its position on the “information exclusion” as follows:

The proposed uniform amendment’s specific reference to “information” as an exclusion to the definition of goods, as well as the explanatory Comment 7, have drawn criticism from commercial and consumer groups alike. The Committee thus recommends that the reference to “information” be deleted. The proposed amendment’s exclusion of “information” from the definition of goods, as an abstract proposition, merely states a truism. The recommended deletion should result in no change in Texas law. The Committee also specifically rejects Comment 7 as ambiguous and, arguably, gratuitous. The Committee recommends that the issues referred to in Comment 7 be left entirely to the courts.<sup>210</sup>

This approach to the debate over coverage, or non-coverage, of transactions in “goods with information” leaves the issue where it now rests in Texas—before the courts.<sup>211</sup> It also deflects criticisms of the “information exclusion” proposed in the 2003 Amendments by preserving the current situation, without adding new ambiguity.<sup>212</sup>

[The] proposed amendments to Article 2 would exclude undefined “information” from the definition of goods. The uncertainty of what the exclusion means, if anything, is one of the key reasons the proposed amendments package has not been enacted by any jurisdiction. If information means intangible data, the exclusion adds nothing. No one thinks the sale of the recipe for Coca Cola would be a sale of goods.

The software customer coalition as well as software producers have all opposed the proposed exclusion of information because of its failure to clarify the law.<sup>213</sup>

The Texas Subcommittee recognized the ongoing conflict among interest groups and the variety of contexts in which the goods-information issue might arise and made a considered choice to leave the matter for resolution in the courts, a step similar to that taken in Texas in 1965 with respect to § 2.318 of the Code.<sup>214</sup> This approach to an intractable issue is one that the 2003 Amendments reflect in other ways. As expressed by a chairman of the Article 2 revisions PEB Drafting Committee at the 2002 Meeting of NCCUSL, “[A]

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209. See *infra* app. I, § 2.103(a)(11) (defining “goods”). The proposed 2007 Bill moves the definition of goods from § 2.105 to § 2.103; it also makes other uniform changes to exclude, e.g., “the subject matter of foreign exchange transactions.” See *infra* app. I, § 2.103(a)(11).

210. See *infra* app. II, § 2.103(a)(11).

211. See *infra* app. II, § 2.103(a)(11).

212. See *infra* app. II, § 2.103(a)(11).

213. Braucher, *supra* note 208, at 269; see also *supra* notes 210-12 and accompanying text.

214. See *infra* notes 215-17 and accompanying text; see *supra* notes 40-41, 144-45 (discussing § 2.318).

decision had been made in the amendments “to trust the courts” with reference to the exclusion of information from the definition of goods proposed in the 2003 Amendments.<sup>215</sup> The Texas Subcommittee’s 2007 Bill also places the matter in the courts but without commentary seeking to shape the result.<sup>216</sup> The 2003 Amendments and the 2007 Bill thus arrive at the same point: the courts will need to resolve the issue of whether, and to what extent, the UCC applies in these transactions.<sup>217</sup> As one former reporter for the PEB Drafting Committee wrote:

On the issue of scope of Article 2 and the exclusion of information. Without the [2003] amendments, the same state of the world exists [as with them]. The courts have to decide whether to apply article 2 to the mixed transaction of goods and information. With the [2003] amendments, the court has to decide whether to apply article 2 to the mixed transaction of goods and information.<sup>218</sup>

The continuation by the 2007 Bill of the existing treatment of “information” under present Code decisions does remove, except as to Oklahoma, the non-uniformity objection as to the treatment of information.<sup>219</sup> Texas will remain substantially aligned, statutorily, with the present statute in most other jurisdictions and based on the former reporter’s assessment quoted above, the adoption—or not—of the information exclusion does not alter the need for judicial resolution.<sup>220</sup>

The Texas Subcommittee’s disposition of the goods-information dispute—retaining the current language, with its existing need for construction, and reserving the issue for judicial resolution—also reflects an early, underlying aspect of Article 2. As mentioned in reviewing the drafting history of the 2003 Amendments, there are two basic approaches to legislative design, a highly defined and structured design, such as seen in present Article 9 of the Code, and a more open-ended, fact-dependent design.<sup>221</sup> That open-ended design is visible in current § 2.102 and § 2.103(a)(11),<sup>222</sup> a design which the Texas Subcommittee 2007 Bill does not alter.

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215. Jean Braucher, *Amended Article 2 and the Decision To Trust the Courts: The Case Against Enforcing Delayed Mass-Market Terms, Especially for Software*, 2004 WIS. L. REV. 753, 758-59.

216. *See supra* Part III.A.3.

217. *See supra* Part III.A.3.

218. Memorandum from Linda J. Rusch, Professor of Law, Hamline Univ. Sch. of Law, to ABA UCC Comm. Chair 1 (undated) (on file with author) (regarding endorsement of revisions to Articles 2 & 2A of the UCC).

219. *See supra* notes 4-5 and accompanying text.

220. Memorandum from Linda J. Rusch to ABA UCC Comm. Chair, *supra* note 218, at 1. Professor Rusch’s assessment substantially undercuts Mr. Bohannon’s claim at the House Committee Interim Hearing that the Texas Subcommittee is a radical change, at least in terms of result. *See supra* Part II.A. The 2007 Bill proposes no statutory change, but the result will be indistinguishable from the 2003 Amendments: the courts have to address “information” transactions.

221. *See supra* Part III.A.1.

222. *See* TEX. BUS. & COM. CODE ANN. §§ 2.102, 2.103(a)(11) (Vernon 1994).

The current style or fashion is to draft much more tightly, with a desperate attempt at internal logical inconsistency and the avoidance of all ambiguity by the definition of all possible terms. That style is, surely, going to make it more difficult to deal with the Code between [1968] and the year 2000, than it was to deal with the older acts up to 1960.

Article 2 is, however, less subject to that criticism than the rest of the Code. By comparison with Articles like 9, Article 2, when you study it, seems to have been drafted in a soft and mushy style . . . .

. . . .

The practitioners never managed to get Professor Llewellyn to reopen the Sales Article, which stayed soft and mushy. Everything in Article 2 turns on whether things are done, or not done, in good faith and in a commercially reasonable fashion, sometimes on whether they are done seasonably. . . . Out of that plastic material you can make pretty much whatever you're going to need to make in 1970 or 1990.<sup>223</sup>

The Texas Subcommittee proposal for §§ 2.102 and 2.103 on this issue both fits the “trust the courts” approach noted in connection with the 2003 Amendments and retains the plasticity of design that was inherent in Article 2 at the beginning.

#### 4. *Continuing the Debate in the 2007 Bill*

Should the 2007 Bill make a change, such as that suggested in the 2003 Amendments, and set out a statutory exclusion for the undefined term “information”? First, consider observations from the 1991 ABA Task Force *Appraisal* on the concerns set out in the initial PEB Study Group comments about the statement of scope in § 2-102 and possible modifications to (1) address “mixed” transactions (to suggest those transactions to which application by analogy was appropriate) or (2) set out more fully what is not affected by Article 2. The ABA Task Force did not support express scope changes:

Perhaps it is advisable to leave well enough alone and let the courts continue as they have been doing [as to scope and extension by analogy.]

. . . .

. . . The degree to which a court can and should appropriate Article 2 for non-sale transactions is not a statutory, but rather a judicial function.<sup>224</sup>

Thus, the Texas Subcommittee approach to § 2.103 and the information exclusion, while non-uniform with the 2003 Amendments, follows a policy

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223. Leary & Frisch, *supra* note 55, at 466 (quoting Prof. Grant Gilmore in P.F. COOGAN ET AL., ADVANCED ALI-ABA COURSE OF STUDY ON BANKING AND SECURED TRANSACTIONS UNDER THE UNIFORM COMMERCIAL CODE 108 (Feb. 1-4, 1968)).

224. ABA Task Force, *Appraisal*, *supra* note 57, at 1027-28.

approach consistent with the adaptable structure of Article 2 as originally drafted, with the views of the ABA Task Force at the outset of the Article 2 amendment project, and with the “trust the courts” position of the Drafting Committee. Likewise, the comments of Professor Rusch indicate that continuing the present scope and “goods” definition in the 2007 Bill will not alter the outcome when goods-information cases arise. With that in mind, does existing Texas case law on the goods and information issues dictate a different position? Should the 2007 Bill explicitly exclude (or include) information transactions under Chapter 2 to reflect Texas decisions?

*a. The Sources of Scope Questions in Chapter 2*

Questions of scope and coverage of information for Chapter 2 purposes may arise in a variety of ways. First is the “goods” question. Chapter 2 starts with the general statement that it “applies to transactions in goods,” but much of the operative text of Chapter 2 concerns “contracts for sale,” which in turn refers to sales of “goods.”<sup>225</sup> Thus, questions affecting application of the UCC to a transaction will include (1) whether “goods” are involved at all; (2) if goods are involved, do other property interests (e.g., realty or intellectual property) or other aspects of the transaction (e.g., provision of services) affect the determination of applicable law; and (3) if goods are involved, is the transaction a sale or something else?<sup>226</sup>

A question not consistently analyzed, but presently embedded in the definition of “goods,” is whether software transactions are excluded as transactions in “choses in action,” not in goods. Existing § 2.105(a) and proposed § 2.103(a)(11) exclude “things in action” or “choses in action,” respectively, from goods.<sup>227</sup> The owner of a copyright, under federal law, holds several exclusive rights that the owner alone may exercise or authorize others to exercise (i.e., license)—including rights to reproduce the work in copies, to prepare derivative works, and to distribute copies.<sup>228</sup> This “bundle of rights” is exclusive to the owner of the copyright; infringement occurs when one of the exclusive rights is violated.<sup>229</sup> The copyright holder may then bring an action

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225. TEX. BUS. & COM. CODE ANN. §§ 2.102, 2.106(a) (Vernon 1994) (stating that “contract” and “agreement” are limited to those relating to the present or future *sale of goods* and that “contract for sale” includes both a present *sale of goods* and a contract *to sell goods* in the future); *id.* § 2.201(a) (regarding “a contract for the sale of goods for the price of \$500 or more”); *id.* § 2.314(a) (“[A] warranty that the goods shall be merchantable is implied in a contract for their sale if the seller is a merchant (as to such goods)”).

226. See 1 JAMES L. WHITE & ROBERT S. SUMMERS, UNIFORM COMMERCIAL CODE 45-50 (5th ed. 2006) [hereinafter WHITE & SUMMERS, UNIFORM COMMERCIAL CODE].

227. TEX. BUS. & COM. CODE ANN. § 2.105(a) (Vernon 1994); *infra* app. I, § 2.103(a)(11).

228. 17 U.S.C. § 106(1)-(3) (2000). By way of example, *Black’s Law Dictionary* defines a “copyright” as “[a]n intangible, incorporeal right granted by statute to the author . . . for a specified period, with the sole and exclusive privilege of multiplying copies of the same and publishing and selling them.” BLACK’S LAW DICTIONARY 304 (5th ed. 1979).

229. 17 U.S.C. § 501(a) (2000) (“Anyone who violates any of the exclusive rights . . . is an infringer . . . .”); *Stewart v. Abend*, 495 U.S. 207, 220 (1990).

for infringement and obtain remedies set out in the Copyright Act.<sup>230</sup> The “rights” of a holder of the copyright in a software program are thus arguably excluded from “goods” by the “choses in action” exclusion of proposed § 2.103(a)(11) as well as by the existing “things in action” exclusion.<sup>231</sup> The Oklahoma Code Comment to title 12A § 2-105 of the Oklahoma UCC makes the same observation: “Since things in action are excluded from the term ‘goods,’ this Article does not govern generally intellectual property, nor assignment of contracts, or sale or assignment of accounts receivable.”<sup>232</sup>

This topic is seldom successfully explored in the software cases dealing with the application of Chapter 2.<sup>233</sup> In one well known case, *ProCD, Inc. v. Zeidenberg*, the Seventh Circuit noted, but was not deterred by, copyright issues and sale-license distinctions in deciding whether the UCC applied to a retail software and database transaction: “Whether there are legal differences between ‘contracts’ and ‘licenses’ (which may matter under the copyright doctrine of first sale) is a subject for another day.”<sup>234</sup>

In short, two related questions are present, if not fully recognized, in the usual dispute over application of the UCC to a computer software or other “information” related transaction. The first is that noted earlier: Is the subject matter of the transaction, especially in a “hybrid” transaction that may affect intellectual property interests, within or without the coverage of the UCC as a “goods” transaction? Second, is the transaction a sale or a license? Even an answer that the transaction is a sale does not always mean that the UCC applies to the issues before the court, as the goods-information issues in “hybrid” transactions may affect the first question. For “non-sale” transactions, White and Summers suggest an approach to the application of the UCC that considers “whether the particular facts of the transaction invite application” of Code principles by analogy.<sup>235</sup> And there are several tests available for evaluating whether the subject matter is within Article 2 as a transaction in goods.<sup>236</sup>

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230. See 17 U.S.C. §§ 501-513 (2000).

231. See *infra* app. I, § 2.103(a)(11); app. II, § 2.103(a)(11); see also *Monsanto Co. v. McFarling*, 363 F.3d 1336, 1342 (Fed. Cir. 2004) (noting that transaction for seeds was license of use, not of sale); *Rhone-Poulenc Agro, S.A. v. DeKalb Genetics*, 284 F.3d 1323, 1333 n.9 (Fed. Cir. 2002) (refusing to apply the UCC, citing the “general intangible” exclusion from “goods” in § 2A-103).

232. OKLA. STAT. ANN. tit. 12A, § 2-105 cmt. 1 (West Supp. 2008) (citations omitted). The Texas Subcommittee, in a similar way, observes that the exclusion of “information” states a truism. See *infra* app. II, § 2.105.

233. See Jeffrey B. Ritter, *Software Transactions and Uniformity: Accommodating Codes Under the Code*, 46 BUS. LAW. 1825, 1828-35 (1991).

234. *ProCD, Inc. v. Zeidenberg*, 86 F.3d 1447, 1450 (7th Cir. 1996).

235. WHITE & SUMMERS, UNIFORM COMMERCIAL CODE, *supra* note 226, at 48-49. White and Summers describe this as a “policy approach” different from other approaches in the case law. *Id.* A similar approach to determining the role of the UCC in non-sales transactions, especially software cases, is suggested by Professor Miller: “The key then to selecting the properly applicable law is the commercial setting” in which the benefits and consequences of applying the UCC can be assessed. Fred H. Miller, *Writing Your Own Rules*, 40 LOY. L.A. L. REV. 217, 224 n.54 (2007).

236. See *infra* Part III.A.4.b.

*b. Representative Tests and Cases for Code Application*

In the “hybrid” transactions, the prevailing test (developed in a goods-services context) is a “predominant purpose” test, with Article 2 applying to the entire transaction if its predominant purpose is sale of goods.<sup>237</sup> In some courts, the UCC applies only to the aspects of the transaction relevant to a sale of goods.<sup>238</sup> Factors that bear upon the sale/non-sale analysis of an information transaction include the mass-market or custom-design market involved, the extent to which professional services are required, the predominant purpose, and the payment terms (single payment, installments, or periodically calculated amounts).<sup>239</sup>

Cases considering whether a software transaction is a sale or license and those considering whether a transaction involves goods or services often draw upon decisions in the “other” line of analysis, with the easy option being for a court with a case in either category to refer to “cases that have applied Article 2 to software transactions,” and then move along to other points.<sup>240</sup> As one commentator observed, “It appears nearly impossible to reconcile these . . . ‘pure software’ cases [regarding the application of Article 2 to software transactions], particularly since each court included in its analysis citations to other software, turnkey, and ‘goods versus services’ decisions.”<sup>241</sup>

In *Advent Systems*, which applied the Article 2 Statute of Frauds to claims under a development agreement, the goods-services and sale-license lines of analysis crossed unobserved. The court was faced with disputes under two related, complex agreements that covered a “joint business collaboration” in which Advent would modify software and hardware interfaces for Unisys, provide “an experienced systems builder” to assist Unisys, provide sales and support training, and “sell hardware and license software” to Unisys.<sup>242</sup> There were additional fees for support services on a per customer basis.<sup>243</sup> Unisys was to purchase “certain of Advent hardware products and software licenses.”<sup>244</sup> The court in *Advent Systems* started with the observation that the UCC applies to “transactions in goods” pursuant to § 2-102, and then determined that

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237. WHITE & SUMMERS, UNIFORM COMMERCIAL CODE, *supra* note 226, at 48-49 (collecting cases). If the predominant purpose is not sale of goods, then the usual result is that the Code does not apply at all. *Id.*

238. *Id.*

239. *Id.* at 46-47.

240. *See infra* note 241 and accompanying text.

241. Ritter, *supra* note 233, at 1831; *see also* *Novamedix, Ltd. v. NDM Acq. Corp.* 166 F.3d 1177, 1181-82 (Fed. Cir. 1999) (illustrating the use of UCC “goods-services” predominant purpose decisions for other purposes, which exist to determine if a patent settlement agreement was a sale, with implied warranties, or another type of transaction). As *Novamedix* observes, “The world of commercial transactions is not limited to the binary world . . . in which an agreement that passes title to Article 2 goods must be either a contract for sale of goods or a contract for sale of services.” *Id.* at 1182.

242. *See Advent Sys. Ltd. v. Unisys Corp.*, 925 F.2d 670, 674 (3d Cir. 1991).

243. *See id.*

244. *Id.* The court did not comment on the extent of the products constituting “hardware” to be sold, which were included in a list of “products.” *See id.*

software (on a disk) was a good, akin to specially manufactured goods, in a “typical mixed goods and services arrangement” so that the UCC would apply.<sup>245</sup>

The court did not, however, explicitly analyze whether (“predominantly” or otherwise) the Advent-Unisys transaction was a sale or a license agreement, a question that the language of “sell hardware and license software” posed directly.<sup>246</sup> Classification of the transaction as a “sale” underpins application of the Code’s Statute of Frauds, which operates only for “a contract for sale.”<sup>247</sup> The Third Circuit looked at traditional goods-services considerations and concluded that Article 2 of the UCC applied because “the . . . main objective was to transfer ‘products’” and “the compensation structure of the agreement also focuses on ‘goods’” that, the court said, were items for sale, without an analysis of whether the “licenses” contemplated for “products” were “sales,” so as to bring the Statute of Frauds into play.<sup>248</sup>

In *Micro Data Base*, the court applied the goods-services analysis to a dispute regarding a custom software development and license project as “consistent with the weight of authority . . . for we can think of no reason why the UCC is not suitable” to govern the dispute.<sup>249</sup> The “goods” in *Micro Data Base* were a software program (SQL Access) that Dharma Systems agreed to adapt for Micro Data Base to use under a contract with the Internal Revenue Service for computer improvements.<sup>250</sup> Under the contract, Micro Data Base would pay Dharma a \$125,000 license fee plus an additional \$125,000 for programming to modify SQL Access into an “RDMS Emulation” form.<sup>251</sup> Although the court discussed the license fee and compensation terms in a goods-services analysis (finding the programs to be delivered are equivalent to specially manufactured goods), it did not attribute substance to Dharma’s continuing efforts to restrict distribution by license terms and Micro Data Base’s assurances (that were breached) as to restrictions on delivery to a third party. The court simply asserted that the transaction *was a sale* of goods; hence, the Code applied.<sup>252</sup>

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245. *Id.* at 676; *see also* Ritter, *supra* note 233, at 1829 (focusing on the “means of delivery” of software, for the “goods-services” issues leads to an odd result with downloaded software—if the test is the delivery of software on a disk, then downloaded software is not a good (by that standard), but the commercial relationship of the vendor and customer is otherwise comparable). *But cf.* U.C.C. § 2-103(k) (amended 2003), 1 U.L.A. 375 cmt. 7 (2004) (“The definition of ‘goods’ in this article has been amended to exclude information not associated with goods. Thus this article does not directly apply to an electronic transfer of information . . .”).

246. *Advent Sys. Ltd.*, 925 F.2d at 674.

247. TEX. BUS. & COM. CODE ANN. §§ 2.201(a), 2.725(a) (Vernon 1994); PA. CONS. STAT. ANN. tit. 13, § 2201(a) (Purdon 1984); *see also* Ritter, *supra* note 233, at 1828 n.14 (noting that the *Advent* court “leaves somewhat unclear whether the title to the software products was to be retained by Advent or was, in fact, transferred to Unisys”).

248. *Advent Sys. Ltd.*, 925 F.2d at 676.

249. *MicroDataBase Sys., Inc. v. Dharma Sys., Inc.*, 148 F.3d 649, 654-55 (7th Cir. 1998).

250. *Id.* at 651.

251. *Id.*

252. *See id.* at 654-55.

In contrast to the quick disposition of issues over proper characterization of a transaction in UCC cases, copyright cases have examined the sale-license question under an economic realities analysis. For example, *Softman Products Co. v. Adobe Systems, Inc.*, dealt with infringement claims of Adobe against a retail seller of unbundled products.<sup>253</sup> On the issue of whether Adobe had sold or licensed the products, the court looked at the terms under which Adobe distributed the product and found that (1) its distributors pay full price for the product and assume the risk of loss or of loss on subsequent sale, and (2) subsequent retail users obtain a single copy paying a one-time amount for an indefinite term of use.<sup>254</sup> Not surprisingly, the court held a sale to the distributor and then a resale to the retail customers was not copyright infringement by the distributor.<sup>255</sup>

*Novell, Inc. v. CPU Distributing, Inc.*, a recent Texas decision (applying Utah law), also dealt with the sale-license issue when considering claims for copyright and trademark infringement.<sup>256</sup> Novell brought these claims against a reseller of computer software that sold unbundled copies of Novell software.<sup>257</sup> The defendant (CPU) purchased these unbundled copies from the original equipment manufacturers (OEMs), who had themselves acquired the copies under distribution agreements with Novell.<sup>258</sup> The defendants relied on the “first sale” doctrine in opposition to Novell’s infringement claim.<sup>259</sup> Because Novell sold the software products to the OEMs, Novell could not prevent sales to CPU and their subsequent disposition of the product to others.<sup>260</sup> The court found that the OEMs’ agreements with Novell authorized the OEMs to sell or resell the products and transferred to the OEMs title and risk of loss.<sup>261</sup> Emphasizing these aspects of the OEM agreements, the court held Novell’s transactions with the OEMs were sales of the particular copies, not licenses, and Novell retained only its intellectual property rights in the copyrighted program itself.<sup>262</sup>

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253. *Softman Prods. Co. v. Adobe Sys., Inc.* 171 F. Supp. 2d 1075, 1080 (C.D. Cal. 2001).

254. *See id.* at 1085.

255. *See id.* at 1084-89.

256. *Novell, Inc. v. CPU Distrib., Inc.*, No. H-97-2326, 2000 U.S. Dist. LEXIS 9975, at \*3 (S.D. Tex. May 4, 2000).

257. *Id.*

258. *Id.*

259. *Id.* at \*7-10. The first sale doctrine can be found in 17 U.S.C. § 109(a) (2000). *Id.* at \*9. “[The] owner of a particular copy . . . lawfully made under this title . . . is entitled, without the authority of the copyright owner, to sell or otherwise dispose of the possession of that copy . . .” § 109(a). 17 U.S.C. § 109(b) (2000). Section 109(b) imposes restrictions on the subsequent rental, lease, or lending of such copy for the purpose of direct or indirect commercial advantage. *See id.*

260. *See Novell, Inc.*, 2000 U.S. Dist. LEXIS 9975, at \*10, \*19.

261. *Id.* at \*18.

262. *Id.* at \*18-\*19. *But cf. Monsanto Co. v. McFarling*, 488 F.3d 973, 976-77 (Fed. Cir. 2007), *cert. denied*, 128 S. Ct. 871, 871 (2008). Monsanto owned patents for herbicide-resistant soybean seeds and sued a farmer for saving seeds from the patented technology. *Id.* The court affirmed the district court’s holding that the defendant’s “seed saving” infringed on Monsanto’s patent. *Id.*

Other cases concentrating on the “sale” treatment of transactions between software developer-licensors and distributors when a product has been resold to persons making subsequent distribution reach differing results. These cases emphasize different contract provisions and economic terms but assert that courts seek to carry out the parties’ intent.<sup>263</sup> The software distribution cases recognize that an answer to the license-sale question requires an analysis of the parties’ expressed intent and the economic reality of the transactions; therefore, an all-purpose answer is not likely to emerge.<sup>264</sup>

When a sale-license issue arises under the UCC between the software developer and its immediate counter-party, the prevailing trend is for Article 2 to be applied—but with opposition from some courts and strong dissent from commentators.<sup>265</sup> *Grappo v. Alitalia Linee Aeree Italiane, S.p.A.* dealt with a contract for the purchase of a “non-exclusive license to use the Guest\*Star program,” under which the provider was to tailor the program for Alitalia.<sup>266</sup> The Second Circuit held the contract was one “for the sale of *personal property*” (as then defined in § 1-206 of the New York UCC) and thus subject to New York’s general UCC Statute of Frauds.<sup>267</sup> The Second Circuit then held this was *not* a sale of *goods*, to which § 2-201 would apply: “We reject this argument [that § 2-201 applies] for the same reason that we reject the proposition that the alleged contract was one for services: *the sale of a non-exclusive license* for copyrighted material was the core of the contract.”<sup>268</sup>

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263. *Compare* *Softman Prods. Co. v. Adobe Sys. Inc.*, 171 F. Supp. 2d 1075, 1080, 1085-90 (C.D. Cal. 2001) (holding, on copyright holder’s application for preliminary injunction against person distributing software copies purchased from licensed distributor, that transaction with single payment for perpetual transfer of possession is a sale and denying injunction as to copyright claims), *with* *Adobe Sys. Inc. v. Stargate Software Inc.*, 216 F. Supp. 2d 1051, 1052, 1054, 1060 (N.D. Cal. 2002) (holding, on copyright holder’s motion for summary judgment, that (1) a transaction between the developer and authorized reseller was a license, not a sale, and (2) the first sale doctrine does not protect subsequent purchasers).

264. *Adobe Sys. Inc.*, 216 F. Supp. 2d at 1052, 1054, 1060; *Softman Prods. Co.*, 171 F. Supp. at 1080, 1085-90; *see also* *Vernor v. Autodesk, Inc.*, 555 F. Supp. 2d 1164, 1169 (W.D. Wash. 2008) (“No bright-line rule distinguishes mere licenses from sales.”).

265. For examples of the prevailing trend, *see ProCD, Inc. v. Zeidenberg*, 86 F.3d 1447, 1450 (7th Cir. 1996) and *Advent Systems, Ltd. v. Unisys Corp.*, 925 F.2d 670, 674, 676 (3d Cir. 1991). *Advent Systems* referenced complex marketing and distribution agreements, including a provision from the parties’ Distribution Agreement that “Advent agrees to sell hardware and license software to Unisys,” to which the court applied a predominant purpose test: “Although determining the applicability of the U.C.C. to a contract by examining the predominance of goods or services has been criticized, we see no reason to depart from that practice here.” *Id.* (internal quotation marks omitted). For a strong critique of the application of Article 2, *see* generally Brennan, *supra* note 47.

266. *Grappo v. Alitalia Linee Aeree Italiane, S.p.A.*, 56 F.3d 427, 429-30 (2d Cir. 1995); *see also* Raymond T. Nimmer, *Through the Looking Glass: What Courts and UCITA Say About the Scope of Contract Law in the Information Age*, 38 DUQ. L. REV. 255, 299 (2000).

267. *Grappo*, 56 F.3d at 431. Texas repealed the general UCC Statute of Frauds and rewrote § 1.206 in 2003. *See* TEX. BUS. & COM. CODE ANN. § 1.206 (Vernon Supp. 2008).

268. *Grappo*, 56 F.3d at 432 (emphasis added). Nimmer asserts that *Grappo* mistakenly characterizes a license as a sale, even though the opinion takes Article 2 out of the case. Nimmer, *supra* note 266, at 299-300. As Nimmer expresses it, the UCC courts have a “goods-centric impulse” that results in the information aspect being subsumed into the goods being sold. *Id.*

In contrast to *Grappo*'s decision *not* to apply Article 2 standards, *ProCD, Inc. v. Zeidenberg* directly applied Article 2 in enforcing license restrictions against a retail purchaser of a database program who offered the information from the database to the public even though he had purchased a consumer version of the product.<sup>269</sup> To determine if the license terms were part of the retail purchase, the Seventh Circuit decided to use the UCC, casting aside concerns about whether the use of Article 2 was appropriate in a sale of copyrighted information:

Following the district court, we treat the licenses as ordinary contracts . . . and therefore as governed by the common law of contracts and the Uniform Commercial Code. Whether there are legal differences between “contracts” and “licenses” (which may matter under the copyright doctrine of first sale) is a subject for another day.<sup>270</sup>

Not surprisingly, non-copyright cases involving information product transactions look back to the tests developed in goods-services cases. Many of the initial software or programming cases involved turnkey computer/software systems or software customization projects for relatively unsophisticated computers that took substantial individualized services.<sup>271</sup> *W.R. Weaver Co. v. Burroughs Corp.* dealt with the problems under a hardware lease and contract for Burroughs “to provide and sell to Weaver” the necessary software, a contract that also provided for services of a district systems analyst.<sup>272</sup> *Chatlos Systems, Inc. v. National Cash Register Corp.* held a transaction for the lease of computer hardware that required an estimated three months of programming was a “sale of goods” notwithstanding the incidental service aspects and the lease arrangement.<sup>273</sup>

Texas cases have considered the applicability of the UCC to mixed “goods-services” contracts in several contexts but have only briefly touched on the computer software information area.<sup>274</sup> *Southwestern Bell Telephone Co. v. FDP Corp.*, held that Article 2 warranty provisions did not apply directly to

269. *ProCD*, 86 F.3d at 1450-53.

270. *Id.* at 1450-53. The *ProCD* court applied UCC § 2-204, not common law, to establish the contract. *Id.* at 1452. The district court noted, but had not analyzed, the terms of payment, lack of title retention, and the lack of a term for the license in finding a sale, not a license. *See id.* at 1450-54.

271. *See Brennan, supra* note 47, at 546-48.

272. *W.R. Weaver Co. v. Burroughs Corp.*, 580 S.W.2d 76, 78, 80 (Tex. Civ. App.—El Paso 1979, writ ref'd n.r.e.) (noting that the parties agreed the UCC applied to a sale of software).

273. *Chatlos Sys., Inc. v. Nat'l Cash Register Corp.*, 479 F. Supp. 738, 742 (D.N.J. 1979), *aff'd and remanded in part*, 635 F.2d 1081 (3d Cir. 1980).

274. *See Sw. Bell Tele. Co. v. FDP Corp.*, 811 S.W.2d 572, 575-76 (Tex. 1991); *W.R. Weaver Co.*, 580 S.W.2d at 78, 80. For non-Texas law cases where courts have applied the goods-services analysis in cases regarding software and scope, see, e.g., *Micro Data Base Sys., Inc. v. Dharma Sys., Inc.*, 148 F.3d 649, 655 (7th Cir. 1998) (applying goods-services analysis under the New Hampshire UCC), and *Advent Sys. Ltd. v. Unisys Corp.*, 925 F.2d 670, 676 (3d Cir. 1991) (“[W]e hold that software is a ‘good’ within the definition in the Code. . . . Although determining the applicability of the U.C.C. to a contract by examining the predominance of goods or services has been criticized, we see no reason to depart from that practice.”).

telephone directory advertising services because the sale of advertising is predominantly a service transaction.<sup>275</sup> Moving further along the spectrum toward covered “sales of goods,” but still finding the Code does not apply where services predominate, are cases dealing with construction of houses or design of real property improvements.<sup>276</sup> Closer to the line is *Geotech Energy*, which refused to apply the UCC to a project for the installation of a (used) telephone system that required programming to customize the telephone system for operation.<sup>277</sup> In a more recent case, however, a court concluded that a contract to design, supply, and install a power supply system in a hospital—a project the contract documents referred to as “a ‘product purchase’ for electrical distribution”—did come within the UCC (as to limitations) “because the sale of goods was the dominant factor or essence of the transaction between the parties.”<sup>278</sup>

The Fifth Circuit analyzed the goods-services issue under the Texas Business & Commerce Code in the context of a contract for a foundry, which used the proprietary information of the buyer, to produce and sell castings of propellers.<sup>279</sup> As the Fifth Circuit observed in *Propulsion Technologies*, the goods-services issue is not always the relevant question: “Under the Code manufacture-and-sale contracts are not even considered ‘hybrid’ contracts; rather, by the very definition in the statute, a transaction in ‘goods’ encompasses a seller’s manufacture and sale of products.”<sup>280</sup> As labor or service is an “input” into every good, the presence of design or service in a product sale contract should not distract a court from the sale of goods nature of the agreement, at least where the item sold is suitably classified as a “good.”<sup>281</sup>

In an alternative holding, however, the Fifth Circuit stated that if the dominant-factor or essence-of-the-transaction test were to be applied, the

275. *Sw. Bell Tele. Co.*, 811 S.W.2d at 574. The Texas court nonetheless gave an extended history of the law of warranty in sales of goods, considered “reference to the Code [to be] instructive,” and approved a jury instruction that quoted the Texas Business & Commerce Code. *Id.* at 575-76.

276. *See, e.g., G-W-L, Inc. v. Robichaux*, 643 S.W.2d 392, 394 (Tex. 1982) (stating that the test for application of the UCC to hybrid services and materials contract to design and construct a house is “whether the dominant factor or ‘essence’ of the transaction is the sale of the materials or the services” and holding in the alternative that the essence or dominant purpose in construction of a house is labor and work); *Palmer v. Espey Huston & Assoc., Inc.*, 84 S.W.3d 345, 355-56 (Tex. App.—Corpus Christi 2002, pet. denied) (referring to design of marina breakwater).

277. *Geotech Energy Corp. v. Gulf States Telecom & Info. Sys., Inc.*, 788 S.W.2d 386, 387, 389 (Tex. App.—Houston [14th Dist.] 1990, no writ) (stating that the dominant purpose or essence standard applies, but holding that plaintiff could not recover under the UCC because it was a lessee and failed to show assignment of warranty). *But see Ritter, supra* note 233, at 1834 (criticizing *Geotech*); *cf. Chatlos Sys., Inc.*, 479 F. Supp. at 742 (holding a transaction for the lease of computer hardware that required an estimated three months of programming was a “sale of goods’ notwithstanding the incidental service aspects and the lease arrangement”).

278. *Tarrant County Hosp. Dist. v. GE Automation Servs., Inc.*, 156 S.W.3d 885, 893 (Tex. App.—Fort Worth 2005, no pet.); *see also Westech Eng’g Inc. v. Clearwater Constructors, Inc.*, 835 S.W.2d 190, 197 (Tex. App.—Austin 1992, no writ).

279. *Propulsion Techs., Inc. v. Attwood Corp.*, 369 F.3d 896, 900-01 (5th Cir. 2004).

280. *Id.* at 900-01 (citing TEX. BUS. & COM. CODE ANN. 2.105(a) (Vernon 1994)).

281. *See id.* at 901.

contract in *Propulsion Technologies* was one for the sale of goods, even though “design” and “quality control” were required.<sup>282</sup> In its analysis, the court asserted, “Even where the production of goods is labor-intensive and the cost of goods is relatively inexpensive, such as . . . custom computer software, jurisprudence has considered the contracts . . . to be transactions predominately in ‘goods.’”<sup>283</sup>

This comment, made in the course of an alternative holding and directed at custom software, does reflect the general assessment of case law treatment of mass market software and other mass market technology products. But *Propulsion Technologies* has limited direct application to the evaluation of custom-designed or mass-market software transactions for purposes of either the sale-license or the goods-information issues.<sup>284</sup> First, and most obvious, the issues in *Propulsion Technologies* were not about the *seller’s* “information in the product.”<sup>285</sup> Second, the cases cited by the Fifth Circuit apply the laws of other jurisdictions (but they do find those other states’ UCCs to apply).<sup>286</sup> Third, the software programs in the cited cases were specifically developed or customized, not mass-market programs, and except for *Micro Data Base*, the opinions did not raise (or consider) one of the recurring issues in the goods-information conflict:<sup>287</sup> to what extent is copyright or trade secret law involved, and possibly controlling, both as to custom-designed and mass-market software?<sup>288</sup>

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282. *Id.*

283. *Id.* at 902.

284. *See id.* (briefly mentioning custom-designed software within a more general statement about the case at hand).

285. *See id.* at 903.

286. *Micro Data Base Sys., Inc. v. Dharma Sys., Inc.*, 148 F.3d 649, 651 (7th Cir. 1998) (applying the New Hampshire UCC to a contract for software company “to adapt its proprietary software program” and for payment of license fee and professional services costs as a transaction in which sale of goods predominates even if analyzed as a hybrid); *RRX Indus., Inc. v. Lab-Con, Inc.*, 772 F.2d 543, 546 (9th Cir. 1985) (applying the California UCC to contract “to timely install an operational software *system*, to repair malfunctions, and to train RRX employees”; classifying the contract as predominantly a *sales* transaction; and concluding that training, repair and upgrades were incidental to sale “and did not defeat characterization of the system as a good” (emphasis added)); *ePresence Inc. v. Evolve Software, Inc.*, 290 F. Supp. 2d 159, 161, 163 (D. Mass. 2002) (applying the California UCC to software license and services agreement for purchase of licensed program, customized by supplier, and for services, using predominant purpose test); *Colonial Life Co., Inc. of Am. v. Elec. Data Sys. Corp.*, 817 F. Supp. 235, 239 (D.N.H. 1993) (applying New Hampshire UCC and predominant factor standard to a contract “the principal object of which was to provide a license to use computer software.”). *But cf.* RESTATEMENT THIRD OF TORTS § 19 cmt. d (1998) (asserting that mass market software is treated as a good under the UCC and custom software as a service).

287. *See Micro Data Base*, 148 F.3d at 652. The plaintiff asserted a claim for misappropriation of trade secrets (the defendant having delivered copies of the customized software program to end users without executing a license agreement). *Id.* The court affirmed damages on that claim. *Id.* at 658.

288. It is not necessary, happily, in this Article to resolve the intricate issues of whether Article 2 or amended Article 2 applies to transactions denominated and documented as licenses of intellectual property (whether copyrighted or protected as a trade secret), as the 2007 Bill of the Texas Subcommittee specifically refers that issue to the courts. *Compare* Brennan, *supra* note 47, at 461 (discussing Article 2B’s provisions for determining the enforceability of mass market contracts and arguing that Article 2 is insufficient to govern information contracts), and Jeff C. Dodd, *Time and Assent in the Formation of Information Contracts: The*

Similar to *Propulsion Technologies* in its analysis (or perhaps in acknowledging that its analysis is limited) about the application of the Texas Business & Commerce Code to software transactions is *Recursion Software, Inc. v. Interactive Intelligence, Inc.*<sup>289</sup> This case involved claims by the owner of copyrighted software (Recursion) that a software developer (Interactive) had violated the terms of the license to the Voyager 2.0.1 program where Recursion asserted that Interactive could not have downloaded the program without agreeing to a license that prohibited a use Interactive had made of the program.<sup>290</sup> Interactive defended on the basis of being grandfathered as a user, and therefore, not subject to the use restriction.<sup>291</sup> The federal district court in *Recursion Software* identified the “contracts” at issue as the various *license agreements* that applied to several versions of the Voyager software.<sup>292</sup> But then, when addressing summary judgment relating to Interactive’s claims of breach of implied warranties as to Voyager 2.0.1 and holding that such were effectively disclaimed, the court turned to the Texas Code to resolve questions of warranty disclaimer.<sup>293</sup>

Although *Recursion Software* refers to the disclaimer provisions of § 2.316 of the Texas Code as the basis for its decision and discusses compliance with the conspicuousness requirement as to disclaimers of implied warranties of merchantability and fitness,<sup>294</sup> there is again little predictive value in its consideration of goods-information. The parties did not raise the question of whether the UCC applied to disclaimers of implied warranties, so “the Court assume[d] that it [did].”<sup>295</sup> The cases cited by the court are again less than comprehensive in considering the issue of inclusion or exclusion of software for purposes of the UCC.<sup>296</sup> Similarly, other courts have assumed that Article 2

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*Mischief of Applying Article 2 to Information Contracts*, 36 HOUS. L. REV. 195, 204-08 (1999), with Jean Braucher, *supra* note 208, at 262 (arguing that Article 2 works well when applied to software transactions). The (relatively) early cases applying the UCC to software transactions dealt with the extent of “services” in obtaining custom software because early computer hardware and software had idiosyncrasies or incompatibilities with computers from other makers and software from other developers. By contrast, for current mass market software, it is rather clear that the present role of services is much diminished in that segment of the market relative to the particular transaction and that the tendency is for courts to apply the UCC to mass market software transactions, even though the intellectual property law effects of applying the UCC may be problematic. See, e.g., Fred H. Miller, *supra* note 186, at 224 (2006). *But see*, ProCD, Inc. v. Zeidenberg, 86 F.3d 1447, 1452-53 (7th Cir. 1996).

289. See generally *Recursion Software, Inc. v. Interactive Intelligence, Inc.*, 425 F. Supp. 2d 756 (N.D. Tex. 2006).

290. *Id.* at 762. Interactive denied that it agreed to the license for the downloaded program. *Id.*

291. *Id.* at 763.

292. *Id.* at 765.

293. *Id.* at 786.

294. *Id.*

295. *Id.* at 786 n.17 (emphasis added). The court also observed that Interactive had failed to respond to the defense of warranty disclaimer. *Id.* at 786.

296. *Id.* at 786 n.17. Of the two Texas cases cited, the *Recursion* court notes that in one, the parties did not dispute application of the Texas Business & Commerce Code. Compare *Bray Int’l Inc. v. Computer Assocs. Int’l, Inc.*, 2005 WL 3371875, at \*3 (S.D. Tex. Dec. 12, 2005), with *Hou-Tex, Inc. v. Landmark Graphics, Inc.*, 26 S.W.3d 103, 108-11 (Tex. App.—Houston [14th Dist.] 2000, no pet.) (holding that the

governs software licensing. Anticipating, or perhaps hoping, for progress on the 2003 Amendments and UCITA, one court wrote: “Article 2 technically does not, and certainly will not in the future, govern software licenses, but for the time being, the Court will assume it does.”<sup>297</sup>

The few Texas “click-wrap” cases finding an agreement under § 2.207 are not UCC goods-information cases; rather, they involve online booking services, online domain name reservation services, or online computer purchases in which the enforceability or scope of arbitration provisions was at issue, not the source of applicable contract law.<sup>298</sup>

One last point to consider in assessing where Texas case law currently stands in cases in which goods are not the exclusive subject of the contract is the “gravamen of the action” standard.<sup>299</sup> The PEB Drafting Committee Reporter’s notes to the 2000 draft of the Article 2 Amendments comment that the gravamen of the action approach is “particularly appropriate” in transactions that present a goods-information divide.<sup>300</sup> In Texas, that analytic concept appears in medical services litigation tied to the medical liability amendments of the 1990s.

In *Sorokolit v. Rhodes*, the plaintiff asserted claims under the Deceptive Trade Practices Act (DTPA) on the grounds that a physician knowingly misrepresented the quality of his services and breached an express warranty as to the result of cosmetic surgery.<sup>301</sup> Tort reform legislation precluded DTPA actions “with respect to claims for damages for personal injury . . . alleged to have resulted, from negligence on the part of any physician.”<sup>302</sup> The question

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plaintiff could not recover on (1) implied warranties, because it was not in vertical privity, based on § 2.318 cases or (2) express warranties, because those warranties were effectively disclaimed). More importantly, the plaintiff in *Hou-Tex, Inc.* had abandoned on appeal its argument that the UCC did not apply to the transaction. *See id.* at 108 n.4. Thus, the court adopted the UCC without a debate on the point. *Id.*; *see also* *Novell, Inc. v. CPU Distributing, Inc.*, No. H-97-2326, 2000 U.S. Dist. LEXIS 9975 (S.D. Tex. May 4, 2000) (concluding that transaction between software developer with copyright in network software products and distributor of computer hardware and software pursuant to “Composite Signature Agreement for Novell Authorized OEMs” was a sale for “first sale” doctrine under copyright laws and that court does not refer to UCC as source of contract law). For an early computer transaction case in which the Texas Business & Commerce Code applied by agreement of the parties, or without discussion by the court, *see, e.g., W.R. Weaver Co. v. Burroughs Corp.*, 580 S.W.2d 76, 80 (Tex. Civ. App.—El Paso 1979, writ ref’d n.r.e.).

297. *i.Lan Sys., Inc. v. Netscout Serv. Level Corp.*, 183 F. Supp. 2d 328, 332 (D. Mass. 2002).

298. *See Provencher v. Dell, Inc.*, 409 F. Supp. 2d 1196, 1198-99 (C.D. Cal. 2006) (enforcing arbitration agreement); *DeFontes v. Dell Computers Corp.*, 2004 WL 253560, at \*1-3 (R.I. Jan. 29, 2004) (not enforcing arbitration agreement based on lack of customer assent); *Hotels.com, Inc. v. Canales*, 195 S.W.3d 147, 154-55 (Tex. App.—San Antonio 2006, no pet.) (online booking); *Dell, Inc. v. Muniz*, 163 S.W.3d 177, 179-80 (Tex. App.—San Antonio 2005, no pet.) (online computer purchase); *Barnett v. Network Solutions, Inc.*, 38 S.W.3d 200, 202 (Tex. App.—Eastland 2001, pet. denied) (domain name reservation).

299. *See Ritter, supra* note 233, at 1831 (discussing a software case applying the gravamen of the action test). *See generally* ROY R. ANDERSON, ROGER A. BARTLETT & W. DAVID EAST, *TEXAS UNIFORM COMMERCIAL CODE ANNOTATED* 68-72 (2007) (discussing the gravamen test).

300. *NCCUSL, REVISION, supra* note 191, at 26 (discussing § 2-103).

301. *Sorokolit v. Rhodes*, 889 S.W.2d 239, 240-41 (Tex. 1994).

302. *Id.* at 240 n.1 (quoting *TEX. REV. CIV. STAT. ANN.* art. 4590i, § 12.01(a) (Vernon Supp. 1994), *repealed by* Act of June 11, 2003, 78th Leg., R.S., ch. 204, § 10.09, 2003 Tex. Gen. Laws 884); *see also* *TEX.*

for the Texas Supreme Court in *Sorokolit* was whether the DTPA statute barred a claim based on an intentional breach of an express warranty of result.<sup>303</sup> The court concluded that “the *underlying nature* of the claim determines whether section 12.01(a) prevents suit for violation of the DTPA.”<sup>304</sup> Using that information, the court applied the gravamen of the action test to evaluate the source of the claim.<sup>305</sup> *Sorokolit* held that the DTPA statute did not bar claims for intentional breach of express warranty because such claims were not merely negligence claims recharacterized as warranty claims.<sup>306</sup>

Notwithstanding *Sorokolit*, application of the “underlying nature of the claim” standard in medical negligence-warranty claims has seldom resulted in the court finding a warranty claim.<sup>307</sup> For example, after *Sorokolit*, the Texas Supreme Court held that an implied warranty does not apply to goods when the goods in question are “provided as an inseparable part of the rendition of medical services.”<sup>308</sup> Because the Drafting Committee’s Reporter’s Note on the gravamen of the action analysis relates to an abandoned draft of § 2-103 and the Texas cases to date have not endorsed that approach in disputes cognate to the UCC, Texas courts are not likely to use the gravamen of the action or similar goods-services test to determine whether the UCC applies to a software transaction, if such were actually disputed by the parties.<sup>309</sup>

The most recent Texas decision on the law applicable to a software transaction is *Fieldtech Avionics & Instruments, Inc. v. Component Controls.Com, Inc.*<sup>310</sup> In *Fieldtech*, Component Control provided specified software, software modules, installation, training, and maintenance items.<sup>311</sup> The court applied Chapter 2 to the disputes between the software provider and

BUS. & COM. CODE ANN. §§ 17.46(b)(5), (7), (20), 17.50 (Vernon 2002 & Supp. 2008) (containing the relevant DTPA provisions).

303. See *Sorokolit*, 889 S.W.2d at 240-41.

304. *Id.* at 242 (emphasis added).

305. *Id.*

306. *Id.* at 242-43. Two justices dissented. See *id.* at 243 (Cornyn, J., dissenting).

307. Compare *Earle v. Ratliff*, 998 S.W.2d 882, 892-93 (Tex. 1999) (summarizing cases finding that claims were actually for negligent treatment), with *Sorokolit*, 889 S.W.2d at 242 (finding an express warranty claim).

308. *Walden v. Jeffrey*, 907 S.W.2d 446, 448 (Tex. 1995). *Walden* dealt with implied warranty claims under the DTPA relating to dentures prepared by the defendant dentist. *Id.* at 447. But whether the principle in *Walden* would exclude warranty claims relating to mass-market manufactured goods sold commercially by a merchant may remain open. See *Easterly v. HSP of Tex., Inc.*, 772 S.W.2d 211, 213-14 (Tex. App.—Dallas 1989, no writ) (finding that no breach of implied warranty exists when the sale of an epidural kit was so intimately related to the rendition of medical services and that hospital was not acting as a merchant); see also ANDERSON, BARTLETT & EAST, *supra* note 299, at 69 (discussing the application of Article 2 in hybrid transactions).

309. See Braucher, *supra* note 215, at 759 (arguing that the Code should apply to software related transactions and suggesting that “[i]ssues not covered in Article 2, such as use and transfer restrictions, should be dealt with by the common law until we get a fair statute to address them”). Braucher further indicates that the gravamen test should be used to determine whether the common law or the Code should apply to a transaction. *Id.*

310. See *Fieldtech Avionics & Instruments, Inc. v. Component Control.Com, Inc.*, 262 S.W.3d 813 (Tex. App.—Fort Worth 2008, no pet.).

311. *Id.* at 818.

customer without discussion: “Because Fieldtech’s rights . . . are governed by UCC article 2, we look to article 2 to guide our analysis.”<sup>312</sup> In short, no Texas decision contradicts the prevailing view under §§ 2.103 and 2.105 that Article 2 can be applied in disputes about software or other goods-information sales transactions where a UCC provision provides a reasonable and relevant rule for decision.<sup>313</sup>

The Texas Subcommittee encountered a fundamental economic and commercial dispute between multiple commercial, technological, and consumer interests.<sup>314</sup> As there is no foreseeable political resolution, the most productive approach may be to preserve the status quo on that intractable political issue and leave the matter for judicial resolution. The 2007 Bill accomplishes that current, if limited, goal.

### *B. The Amended Battle of the Forms and Contract Formation Terms*

The Article 2 revision project began and ended with a common understanding that the current § 2-207 is broken and merits repair, if not replacement. In 1990, the PEB Study Group commented, “Section 2-207 is controversial, complex and frequently litigated.”<sup>315</sup> Professor White identifies several ailments in current § 2-207, the principal ones being: (1) § 2-207(1) is a contract formation provision residing in a statutory provision about contract terms; (2) § 2-207 and the comments give “uncertain direction” regarding which terms in an offer survive an acceptance with variant terms; (3) “Section 2-207(1) refers to ‘additional or different’ terms” in an acceptance, but § 2-207(2) covers, explicitly at least, only additional terms, giving rise to long-running interpretive confusion; and (4) § 2-207 operates too restrictively and mechanically to allow courts to accommodate the varied and eccentric ways that contract issues arise.<sup>316</sup> In the final ALI discussions in 2003, before approving

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312. *Id.* at 825.

313. See Braucher, *supra* note 215, at 759 (“[T]he decided majority approach in the case law . . . is to apply Article 2 to disputes over mass-marketed software.”); see also *i.Lan Sys. Inc. v. Netscout Serv. Level Corp.*, 182 F. Supp 2d 328, 332 (D. Mass. 2002) (“[T]he Court will not overlook Article 2 simply because its provisions are imperfect in today’s world. Software licenses are entered into every day, and business persons reasonably expect that *some* law will govern them. For the time being, Article 2’s provisions . . . better fulfill those expectations than would the common law.”); ANDERSON, BARTLETT & EAST, *supra* note 299, at 69 (“Although the courts in most jurisdictions have held that Article 2 does apply to sales of computers and computer software, it is evident that Article 2 is ill equipped to deal with [issues from such transactions].”).

314. See *supra* Part II.B.

315. PEB STUDY GROUP, PRELIMINARY REPORT, reprinted in ABA Task Force, *Appraisal*, *supra* note 57, at 1054. The ABA Task Force concurred. See ABA Task Force, *Appraisal*, *supra* note 57, at 1057 (“Clearly some revision of section 2-207 is necessary as the existing text contains many interpretive difficulties.”).

316. See James J. White, *Contracting Under Amended 2-207*, 2004 WIS. L. REV. 723, 725-28; see also WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 180-83 (discussing problems with § 2-207).

the 2003 Amendments, Professor White observed, “Section 2-207 in its current form is incomprehensible and probably bad policy.”<sup>317</sup>

These criticisms are not new:

“[O]ne of the problems in this field, which has always been the delight of law professors . . . is the so-called battle of the forms where seller and buyer, each dedicated to his own brand of insanity, exchange forms which have nothing to do with each other and then ask counsel, “Well, where are we?” That was a problem that Professor Llewellyn dearly loved, and he put a long section in Article 2 which has been generally hailed . . . by members of the bar as probably the end of civilization as we know it.”<sup>318</sup>

“The truth is that it [§ 2-207] was a miserable, bungled, patched-up job—both text and comment—to which various hands . . . contributed at various points, each acting independently of the others (like the blind men and the elephant). It strikes me as ludicrous to pretend that the section can, or should, be construed as an integrated whole in light of what “the draftsman” “intended.” . . . The proper approach to § 2-207, which is arguably the greatest statutory mess of all time, is to take it light-heartedly (or, as Professor Corbin used to say, cheerfully).”<sup>319</sup>

Will the proposed amendments of “arguably the greatest statutory mess of all time” reduce “the ability of parties to rely on their contracts”<sup>320</sup> and operate to “eschew terms set by the parties and favor those to be fixed in a courthouse or by the drafters of Article 2” as critics of the changes assert?<sup>321</sup> One shorthand version of these criticisms is that the amendments to § 2-207 interfere with freedom of contract: “The amendments remove any real ability of contracting parties to define the terms of their bargain . . . .”<sup>322</sup> We consider these criticisms and the likely outcomes under amended § 2-207 of representative Texas cases below.

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317. *Discussion of the Uniform Commercial Code, Proposed Amendments to Article 2 (Sales) and 2A (Leases)*, 2003 A.L.I. PROC. 160, 186 (2004) (remarks of James J. White), available at 2003 ALI-PROCEED 160 (Westlaw).

318. Leary & Frisch, *supra* note 55, at 423 (first alteration in original) (quoting P.F. COOGAN ET AL., ADVANCED ALI-ABA COURSE OF STUDY ON BANKING AND SECURED TRANSACTIONS UNDER THE UNIFORM COMMERCIAL CODE 108 (1968)); see John E. Murray, *The Chaos of the “Battle of the Forms”*: Solutions, 39 VAND. L. REV. 1307, 1310 n.10 (1986) (citing P.F. COOGAN ET AL., *supra*, and attributing the statement to Professor Grant Gilmore).

319. White, *supra* note 316, at 724 (quoting Letter from Grant Gilmore, Professor, Vermont Law Sch., to Robert S. Summers, Professor, Cornell Univ. Law Sch. (Sept. 10, 1980)).

320. *Hearings*, *supra* note 14, at 4:43 (testimony of Charles R. Keeton).

321. Memorandum from Jeff Dodd to Stephanie Heller, *supra* note 98, at 2; Letter from Quentin Riegel to J. Scott Sheehan, *supra* note 91, at 1 (“[T]hey disfavor terms offered by contracting parties in favor of default rules not of their choosing . . .”).

322. NAT’L CONFERENCE OF COMM’RS ON UNIF. STATE LAWS, AMENDMENTS TO ARTICLE 2 AND 2A OF THE UNIFORM COMMERCIAL CODE: CRITICISMS AND RESPONSES 3 (2007) (on file with author).

1. *Current § 2-207 and the Text of Proposed Amendments: The Contract Formation Terms of § 2-206*

Sections 2.206 and 2.207 have a direct linkage. Section 2.206—Offer and Acceptance in Formation of Contract—describes baseline rules of offer and acceptance.<sup>323</sup> Current § 2.207—Additional Terms in Acceptance or Confirmation—begins with a well-known provision that is actually about *acceptance*:

(a) A definite and seasonable expression of acceptance or a written confirmation which is sent within a reasonable time operates as an acceptance even though it states terms additional to or different from those offered or agreed upon, unless acceptance is expressly made conditional on assent to the additional or different terms.<sup>324</sup>

The 2003 Amendments propose two changes affecting § 2-207(1): The amendments would relocate the subsection into § 2-206, regarding offer and acceptance, and the text of the new § 2-206(3) would be condensed. As proposed in the 2003 Amendments, new § 2-206(3) would read: “A definite and seasonable expression of acceptance in a record operates as an acceptance even if it contains terms additional to or different from the offer.”<sup>325</sup> Textually, proposed § 2-206(3) differs from present Texas § 2.207(c) by deleting two phrases: “which is sent within a reasonable time” and “unless acceptance is expressly made conditional on assent to the additional or different terms.”<sup>326</sup> The removal of “sent within a reasonable time” does not create a change in the law. Proposed § 2-206(3) retains the “seasonable expression” reference.<sup>327</sup> “Seasonable” already has a statutory definition of “within a reasonable time,” absent an agreed time period.<sup>328</sup> Consequently, the change in text does not affect timing for an acceptance or confirmation.

The deletion of the qualifying phrase “unless acceptance is expressly made conditional” sounds more substantial. In current § 2-207(1), this provides a relatively bright line between responses that operate as acceptances and responses that operate as rejections of the proposed deal.<sup>329</sup> Current § 2.207(a) and (proposed) § 2-206(3) provide that a “definite and seasonable expression of acceptance,” (suggesting a simple, common law acceptance) will operate as an acceptance “even if it contains terms additional to or different from” the

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323. TEX. BUS. & COM. CODE ANN. § 2.206 (Vernon 1994); *see also* U.C.C. § 2-206 (amended 2003), 1 U.L.A. 395-96 (2004).

324. TEX. BUS. & COM. CODE ANN. § 2.207(a) (Vernon 1994); *see also* U.C.C. § 2-207(1) (amended 2003), 1 U.L.A. 397 (2004).

325. U.C.C. § 2-206(3) (amended 2003), 1 U.L.A. 396 (2004).

326. *Compare id.*, with TEX. BUS. & COM. CODE ANN. § 2.207(a).

327. *See* U.C.C. § 2-206(3) (amended 2003), 1 U.L.A. 396 (2004).

328. TEX. BUS. & COM. CODE ANN. § 1.204 (Vernon Supp. 2008).

329. *See* WHITE & SUMMERS, UNIFORM COMMERCIAL CODE, *supra* note 226. *But cf.* Roto-Lith, Ltd. v. F.P. Bartlett & Co., Inc., 297 F.2d 497 (1st Cir. 1962).

offer.<sup>330</sup> The proper classification of a response that is an “acceptance plus other terms” presents obvious problems, however, in deciding if it is an acceptance or a non-acceptance. The original objective of bringing affirmative responses that included additional or differing terms into the category of “acceptances” was to undo the common law “mirror image” rule, under which any variance between the terms of the offer and the terms of the acceptance resulted in there being no effective acceptance, and hence no contract.<sup>331</sup> Targeting the case of *Poel v. Brunswick-Balke-Collender Co.*,<sup>332</sup> White and Summers assert that the “original drafter of 2-207 designed it mostly to keep the welscher in the contract” by a provision that “rejects the common law mirror image rule and converts many common law counteroffers into acceptances under 2-207(1).”<sup>333</sup>

Against this statutory conversion of some common law rejections into acceptances, current § 2.207(a) sets up a safety valve for the offeree who wants some (or all) of the terms in the “acceptance” to control over some (or all) of the terms in the offer: the “acceptance” may be made “expressly conditional on assent to the additional or different terms.”<sup>334</sup> That is a more explicit statement of the view of Professor Lewellyn, “that a document which said, ‘This is an acceptance only if the additional terms we state are taken by you’ is not a definite and reasonable expression of acceptance but is an expression of a counter-offer.”<sup>335</sup>

The result of such a “counter-offer” under the UCC is not what it used to be at common law, if the parties then perform.<sup>336</sup> In contrast to the common

330. TEX. BUS. & COM. CODE ANN. § 2.207(a); *see also* U.C.C. § 2-206(3) (amended 2003), 1 U.L.A. 396 (2004).

331. *See, e.g.*, 1 E. ALLAN FARNSWORTH, FARNSWORTH ON CONTRACTS § 3.13 (3d ed. 2004) (“Third, at least according to traditional contract doctrine, the commitment [in the offeree’s response] must be one on the terms proposed by the offer without the slightest variation.”).

332. *Poel et al. v. Brunswick-Balke-Collender Co.*, 110 N.E. 619 (N.Y. Ct. App. 1915) (discussing the inclusion of a provision in a purchaser order stating that “you must promptly acknowledge” added a condition preventing a contract absent the acknowledgement).

333. WHITE & SUMMERS, UNIFORM COMMERCIAL CODE, *supra* note 226, at 56-57. The text of current § 2.207(a) and proposed § 2.206(c)—following the national uniform texts—go beyond the original scope of Professor Lewellyn’s early drafts of this provision. Wladis, *supra* note 169, at 1031-35. Those earlier drafts dealt with *acceptances*, not confirmations, that attempted to include *additional*, not *different*, terms, so that “an acceptance coupled with a suggestion for the minor term to be added” would be interpreted as an acceptance, “not as a conditional acceptance (i.e., a counter-offer).” *Id.* at 1037; *see also* Murray, *supra* note 318, at 1319-22 (1986).

334. TEX. BUS. & COM. CODE ANN. § 2.207(a) (Vernon 1994). Note that it is an “acceptance” that may insist on assent to additional or different terms as a condition to a contract; confirmations, being tied to a “done deal,” are allowed to propose only “additional” terms. *See* TEX. BUS. & COM. CODE ANN. § 2.207 cmt. 2 (Vernon 1994). “This indicates that the proviso applies only to an acceptance and not to a confirmation.” Wladis, *supra* note 169, at 1039; *see also* WHITE & SUMMERS, UNIFORM COMMERCIAL CODE, *supra* note 226, at 59.

335. Murray, *supra* note 318, at 1323 (quoting 1 State of New York, 1954 New York Law Revision Commission Report, Hearings on the Uniform Commercial Code 117 (181)); *see also* Wladis, *supra* note 169, at 1037 (discussing the 1941 draft of Revised Uniform Sales Act).

336. *See* TEX. BUS. & COM. CODE ANN. § 2.207(c) cmt. 7; WHITE & SUMMERS, UNIFORM COMMERCIAL CODE, *supra* note 226, at 73; Murray, *supra* note 318, at 1322-32.

law cases that treated a seller's counter-offer in the form of a slightly varying sales order to have been accepted by the buyer if it then took the goods, under current § 2.207 in the case of an "expressly conditional" acceptance that has different terms of shipment and payment than the offer, "[m]ost courts under the Code hold that such an 'acceptance' [by the original offeror] merely by conduct does not constitute 'assent' [to the expressly conditional, different terms] . . . [but] the contract is formed . . . under 2-207(3)."<sup>337</sup> Thus, the safety valve of § 2-207(1) has a two-stage result: The offeree can choose to "not accept" by utilizing the "expressly conditional" proviso to § 2.207(a) and preclude initial formation of a contract, but performance thereafter leads to a contract on Code terms.<sup>338</sup>

This safety valve proviso does not appear in the 2003 Amendments.<sup>339</sup> The drafters assert that the deletion works no change in result.<sup>340</sup> The official version of the 2003 Amendments relies on Comment 3 to make the point: "A purported expression of acceptance containing additional or different terms would not be a 'definite' acceptance when the offeree's expression [of acceptance] clearly communicates to the offeror the offeree's unwillingness to do business unless the offeror assents to those additional or different terms."<sup>341</sup>

In contrast to the official proposed text of the 2003 Amendments, the Texas Subcommittee recommended that § 2.206(c) of the 2007 Bill *retain* the "expressly conditional" proviso from current § 2.207(a), so the amended section would read:

(c) A definite and seasonable expression of acceptance in a record operates as an acceptance even if it contains terms additional to or different from the offer, *unless acceptance is expressly made conditional on assent to the additional or different terms.*<sup>342</sup>

The Texas Subcommittee's Bill Analysis observed,

Although Official Comment 3 to the proposed amendment suggests, perhaps correctly, that the "unless" clause is superfluous and that no change in the law is intended by its deletion, the quoted language is reinserted in new subsection (c) in recognition of the fact that many acknowledgement forms in current use . . . adopt this language to make clear that the form does not

337. WHITE & SUMMERS, UNIFORM COMMERCIAL CODE, *supra* note 226, at 70.

338. TEX. BUS. & COM. CODE ANN. § 2-207(a), (c); *see* WHITE & SUMMERS, UNIFORM COMMERCIAL CODE, *supra* note 226, at 73. White & Summers caution that the wording of a document must clearly invoke the "conditional acceptance" provision, at risk of being classified as simple acceptance. *See id.* at 69-70 nn. 37-38.

339. *See supra* note 325 and accompanying text.

340. U.C.C. § 2-206 cmt. 3 (amended 2003), 1 U.L.A. 396 (2004).

341. *Id.*

342. *See infra* app. I, § 2.206(c) (emphasis added).

constitute an acceptance. Retaining this language will thus remove any uncertainty about the matter . . . .<sup>343</sup>

Given the history of § 2.207(a) with the proviso and the consequences to the parties when a response is an acceptance and when it operates as a “conditional acceptance,” this is a useful modification.<sup>344</sup> This retention of statutory text will clearly preserve the procedural status quo on what an offeree should do to “not accept” in its acknowledgment document, leaving for later what the effect of conflicting forms may be under amended § 2.207.<sup>345</sup>

This statutory statement also avoids a concern in interpreting the Code going back to its inception: What weight should be given to the Official Comments, or to bar committee comments, that precede (or in some cases follow) enactment?<sup>346</sup> The 1952 Official Text of the Code originally included a section on Official Comments, but the absence of any present statutory recognition results in the problem of whether comments can “lift themselves by their own bootstraps” into applicability.<sup>347</sup>

In Texas, “[a]lthough the Official UCC Comments following the code provisions are not law, they are persuasive authority concerning the interpretation of the statutory language.”<sup>348</sup> However, a discount may apply to comments of the Texas Subcommittee given courts’ recognition of the Official Comments and concern that bar committee comments (at least those not shown to be before the legislature) may be ex post comments and not fairly part of the legislative history.<sup>349</sup>

The Texas Subcommittee’s retention of the existing “expressly conditional acceptance” clause as part of the statute in proposed § 2.206(c) will continue the application of case analysis from current § 2.207(a) on questions of whether a response was an acceptance or a conditional acceptance, and will not resort to comments to explain that the statutory changes reflected no change in substance.<sup>350</sup> The limited changes that the Texas Subcommittee made in § 2.206(c), which incorporate the slightly edited text regarding “acceptance,”

343. See *infra* app. II, § 2.206.

344. Compare TEX. BUS. & COM. CODE ANN. § 2.207(a) (Vernon 1994), with *infra* app. I, § 2.206(c).

345. See *infra* app. I, § 2.206(c) (retaining the text of current § 2.207(a)).

346. See generally *infra* app. I, § 2.206(c) (avoiding the concern because the current statutory language is preserved).

347. Robert H. Skilton, *Some Comments on the Comments to the Uniform Commercial Code*, 1966 WIS. L. REV. 597, 599-601 (quoting HONNOLD, SALES AND SALES FINANCING 18 (2d ed. 1962) (discussing deletion of § 1-102(3)(f) of the 1952 Official Text of the Code)).

348. *Fetter v. Wells Fargo Bank Tex., N.A.*, 110 S.W.3d 683, 687 (Tex. App.—Houston [14th Dist.] 2003, no pet.) (citing *HRN, Inc. v. Shell Oil Co.*, 102 S.W.3d 205, 212 n.5 (Tex. App.—Houston [14th Dist.] 2003), *rev’d*, 144 S.W.3d 429 (Tex. 2004)).

349. *Id.* at 688-89 (“Because the State Bar Committee Comment was not before the legislature . . . we do not view it as persuasive in analyzing the issue in the present case.”).

350. See TEX. BUS. & COM. CODE ANN. § 2.207(a) (Vernon 1994); *infra* app. I, § 2.206(c). The Texas Subcommittee’s disposition of “information exclusion” would, however, entail some concern that the bar comments on that thorny problem might be of limited utility. See *supra* notes 221-23 and accompanying text.

retain the “conditional acceptance” proviso and will not work a change in the statute or Texas case law on that aspect of current § 2.207.

## 2. *Contract Terms Under Amended § 2-207*

In contrast to the continuity in the contract formation provisions of § 2-206 that now incorporate current § 2-207(1), the text and analysis of the remainder of proposed § 2-207 vary markedly from current § 2-207(b)-(c). To facilitate review of the amendments proposed for § 2.207(b)-(c) in the 2007 Bill, the text of the current statute and proposed amendment are listed below:

### **Current § 2.207(b)-(c). Additional Terms in Acceptance or Confirmation**

(b) The additional terms are to be construed as proposals for addition to the contract. Between merchants such terms become part of the contract unless:

- (1) the offer expressly limits acceptance to the terms of the offer;
- (2) they materially alter it; or
- (3) notification of objection to them has already been given or is given within a reasonable time after notice of them is received.

(c) Conduct by both parties which recognizes the existence of a contract is sufficient to establish a contract for sale although the writings of the parties do not otherwise establish a contract. In such case the terms of the particular contract consist of those terms on which the writings of the parties agree, together with any supplementary terms incorporated under any other provisions of this title.<sup>351</sup>

### **Proposed § 2.207. Terms of Contract; Effect of Confirmation**

Subject to Section 2.202, if a contract is [i] formed in any manner permitted by this chapter, or [ii] confirmed by a record that contains terms additional to or different from those in the contract being confirmed, the terms of the contract are:

- (1) terms that appear in the records of both parties;
- (2) terms, whether in a record or not, to which both parties agree; and
- (3) terms supplied or incorporated under any provision of this chapter.<sup>352</sup>

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351. TEX. BUS. & COM. CODE ANN. § 2.207(b)-(c) (Vernon 1994).

352. See *infra* app. I, § 2.207 (alteration in original)

*a. Changes in the Introductory Clause*

The 2003 Amendments and the 2007 Bill of the Texas Subcommittee make a threshold change that affects the application of amended § 2.207.<sup>353</sup> Under current § 2.207(b), additional terms proposed in an acceptance or confirmation may become part of a contract “between merchants” unless one of the three exclusionary clauses of § 2.207(b) intervenes.<sup>354</sup> There was not a parallel statutory route for inclusion of additional terms for a transaction that involved a *non-merchant*—especially consumers—in current § 2.207(b).<sup>355</sup> Amended § 2-207 applies, however, to *all* contracts within Article 2 (whether merchant or other) and not just to contracts involving a “battle of the forms.”<sup>356</sup>

The Texas Subcommittee 2007 Bill modifies the uniform introductory statement to § 2.207 in a way that also reflects application of amended § 2.207 to all contracts.<sup>357</sup> The 2007 Bill replaces the proposed uniform introductory clause with the following language: “Subject to Section 2.202 [on parol or extrinsic evidence], *if a contract is [i] formed in any manner permitted by this chapter, or [ii] confirmed by a record that contains terms additional to or different from those in the contract being confirmed, the terms of the contract are [as provided by the revised § 2.207].*”<sup>358</sup> This revised introductory provision makes two changes in the proposed uniform text.

First, the Texas Subcommittee Bill replaces the first two clauses of the introductory statement, “if (i) conduct by both parties recognizes the existences of a contract although their records do not otherwise establish a contract, (ii) a contract is formed by offer and acceptance,” with a comprehensive statement “if a contract is [i] formed in any manner permitted by this Chapter . . . .”<sup>359</sup> The Texas Subcommittee’s “formed in any manner” clause [i] confirms the principle stated in proposed Official Comment 1: “This section applies to all contracts for the sale of goods . . . .”<sup>360</sup> Within the Code, the Texas Subcommittee’s revision also directly links to amended § 2.204 regarding the formation of a contract: “A contract for sale of goods may be made in any manner sufficient to show agreement, including offer and acceptance, conduct by both parties which recognizes the existence of a contract, the interaction of electronic agents, and the interaction of an electronic agent and an

353. U.C.C. § 2-207 (amended 2003), 1 U.L.A. 397 (2004); *see infra* app. I, § 2.207.

354. TEX. BUS. & COM. CODE ANN. § 2.207(b).

355. *Id.*; *see also* WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 81 n.78 (collecting cases that deal with the non-merchant transaction).

356. U.C.C. § 2-207 (amended 2003), 1 U.L.A. 398 cmt. 1 (2004); *see also* Douglas G. Baird & Robert Weisberg, *Rules, Standards, and the Battle of the Forms: A Reassessment of § 2-207*, 68 VA. L. REV. 1217, 1217-20 (1982); Wladis, *supra* note 169, at 1035-36 (distinguishing conflicts in confirmations from the battle of forms with no antecedent agreement).

357. *See infra* app. I, § 2.207.

358. *See infra* app. I, § 2.207 (emphasis added).

359. *Compare* § 2-207 (amended 2003), 1 U.L.A. 397 (2004), *with infra* app. I, § 2.207.

360. U.C.C. § 2-207 (amended 2003), 1 U.L.A. 398 cmt. 1 (2004).

individual.”<sup>361</sup> The Texas Subcommittee’s revision of the introductory clause makes clear that § 2.207 is not limited in its application to “only” those contracts formed in the ways listed in the introductory clause.<sup>362</sup>

*b. Changes in the Operative Text of § 2-207*

After these introductory changes, amended § 2-207, both in its uniform text and in the 2007 Bill, makes a fundamental change in the methodology for determining the terms of some contracts. Instead of intricate issues about the “different-additional” inconsistencies and “built-in” notification of objection to variant proposed terms, amended § 2-207 sets out three sources for contract terms that apply in all transactions where a contract has been formed: “(a) terms that appear in the records of both parties; (b) terms, whether in a record or not, to which both parties agree; and (c) terms supplied or incorporated under any provision of this Act.”<sup>363</sup>

*c. Terms to Which Both Parties Agree*

As a precursor of evaluating the effect of these changes in more detail below, note the explicit inclusion of “terms . . . to which both parties agree.”<sup>364</sup> “Agreement” in the Texas Business & Commerce Code is the “bargain of the parties in fact, as found in their language or inferred from other circumstances, including course of performance, course of dealing, or usage of trade as provided in Section 1.303.”<sup>365</sup> Critics of amended § 2-207 who argue that it deprives persons of their freedom of contract have little to work with here.<sup>366</sup> Parties that actually agree on terms have nothing to fear from amended § 2-207; it will recognize those terms to which both parties agree and will consider several sources of agreement. Such a result, being an inquiry about the bargain in fact, does allow for disputes about the conduct or events showing what is the bargain in fact, as referenced in § 1.201(b)(3).<sup>367</sup> Disputes about agreement are the historic inquiry of contract law:

[C]ontractual liability is consensual. Since it is difficult . . . to take account of assent unless there has been an overt expression of it, courts have required

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361. U.C.C. § 2-204(1) (amended 2003), 1 U.L.A. 391 (2004); *see also infra* app. I, § 2.204 (containing identical language).

362. *See infra* app. II, § 2.207.

363. U.C.C. § 2-207 (amended 2003), 1 U.L.A. 397 (2004); *see also infra* app. I, § 2.207 (containing identical language).

364. U.C.C. § 2-207 (amended 2003), 1 U.L.A. 397 (2004).

365. TEX. BUS. & COM. CODE ANN. § 1.201(b)(3) (Vernon Supp. 2008).

366. *See infra* app. I, § 2.207(2).

367. *Hearings, supra* note 14, at 4:08 (testimony of Jean Braucher) (noting this new type of inquiry). The results will depend on “how courts respond to questions about agreement.” *Id.* Although she confirmed this factual question was a “new form of ambiguity,” Professor Braucher acknowledged it is a “better question.” *Id.*

that assent to the formation of a contract be manifested in some way, by words or other conduct, if it is to be effective.<sup>368</sup>

Promises become binding when there is a meeting of the minds and consideration is exchanged. So it was at King's Bench in common law England . . . and so it is today. Assent may be registered by a signature, a handshake, or a click of a computer mouse . . . across . . . the Internet.<sup>369</sup>

Questions of assent and agreement in contracting have always been factual at their base, as the UCC "contract" is the result of the "bargain of the parties in fact."<sup>370</sup> Because many § 2-207 cases are about whether a statutory "gap-filler" under Article 2 shall apply, part of the controversy over changes in amended § 2-207 is the product of different positions on how hard it should be to "include" a contractual term favored by one party and thereby "avoid" a statutory term that would apply if the agreement were silent or if the contractual term were knocked out by a conflict in terms.<sup>371</sup> A party's position on that issue, which is the focus of amended § 2-207, rests on whether, for that party or circumstance, the statutory terms that are in the background are good or bad.<sup>372</sup> One view is that the UCC standard terms favor buyers: "Sellers in commercial transactions consider the gap-filler terms to be too generous to buyers."<sup>373</sup> The contrary view is that UCC standard terms, being the product of work to capture commercial reality and of a rigorous examination of the statutory terms prior to their adoption, are the result of fairly made policy determinations as to what a buyer should expect to receive and a seller should expect to undertake and thus should presumptively apply.<sup>374</sup>

At a structural level, amended § 2-207 adopts the view that a contract term that differs from the "normal factual bargain" embedded in the Code should enter the contract only if the party seeking to include "its" term can meet the burden of providing "a clear demonstration that the other party should have reasonably understood the deviation from normative assumptions" was to be part of the contract.<sup>375</sup> In the framework of amended § 2-207, that means that the party who seeks to apply a term other than the default terms (the gap-fillers) of the UCC and those terms that appear in both forms will have to prove, under the proposed 2007 Bill, agreement by the other party to such term for purposes of § 2.207(ii) (which could be accomplished in some instances by its appearance in both forms) or that such term is within the terms supplied

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368. 1 FARNSWORTH, *supra* note 331, at 200-02.

369. *Specht v. Netscape Commc'ns Corp.*, 150 F. Supp. 2d 585, 587 (S.D.N.Y. 2001), *aff'd*, 306 F.3d 17 (2d Cir. 2002).

370. See TEX. BUS. & COM. CODE ANN. § 1.201(3), (12) (Vernon Supp. 2008).

371. See Mark E. Roszkowski & John D. Wladis, *Revised U.C.C. Section 2-207: Analysis and Recommendations*, 49 BUS. LAW. 1065, 1065-70 (1994).

372. TEX. BUS. & COM. CODE ANN. § 2.207 (Vernon 1994); see *infra* app. I, § 2.207.

373. See Roszkowski & Wladis, *supra* note 371, at 1069 (quoting Letter from Benjamin Wright to Article 2 Drafting Comm. (Feb. 7, 1993)).

374. See *id.* at 1069-70 (citing Murray, *supra* note 318, at 1373-74, 1377).

375. Murray, *supra* note 318, at 1378.

through § 2.207(iii), by course of dealing, usage of trade and the like. Such an issue of agreement can be litigated because it is factual.<sup>376</sup> Agreement and the expectations of parties have, however, long been fundamental to contract law: “Promises become binding when there is a meeting of the minds and consideration is exchanged. So it was at King’s Bench in common law England . . . .”<sup>377</sup> “Agreement” is a question the courts have answered for generations and can do so in the future.

Whether there was agreement in fact is also a better question than questions that are driven by which form came first in an exchange of forms or that try to apply “angular phraseology and . . . a subsection which was tacked on belatedly without the aid of the . . . principal draftsman.”<sup>378</sup> The “precise and fair identification of the parties’ factual bargain” is the goal of Article 2, so it makes sense to return to questions about agreement to reach that goal.<sup>379</sup> “Absent fraud or unconscionability, the law has always honored the contract that results from the offeree’s conscious acceptance of the offer, even in circumstances where the offeree had no power to modify the offer and when there was no prospect that the offeror would consider . . . a counteroffer.”<sup>380</sup>

Amended § 2-207 looks to the agreement of the parties for the terms of the contract, without the formalistic lens of the current section.<sup>381</sup> As a part of this process, amended § 2-207 initially looks to terms that appear in the records of *both* parties for all cases.<sup>382</sup> This provision carries forward part of current § 2.207(c) but applies the rule more broadly. Currently, where conduct establishes a contract although the writings of the parties do not, the “terms on which the writings of the parties agree” are part of the contract.<sup>383</sup> As amended

376. White, *supra* note 316, at 730 (“[2.207(2)] gives courts latitude to find agreement in the verbal and nonverbal behavior of the parties . . . . I predict this judicial interpretation of the parties’ conduct will be the battlefield under amended 2-207.”); *see Hearings, supra* note 14, at 4:14 (testimony of Jean Braucher).

377. *Specht v. Netscape Commc’ns Corp.*, 150 F. Supp. 2d 585, 587 (S.D.N.Y. 2001), *aff’d*, 306 F.3d 17 (2d Cir. 2002).

378. Murray, *supra* note 318, at 1309.

379. *Id.* at 1311; *see* WHITE & SUMMERS, UNIFORM COMMERCIAL CODE, *supra* note 226, at 57 (“[H]ow may [current] 2-207 be interpreted so as not to give an unearned and unfair advantage to the contracting party who by pure happenstance sends the first or in other cases second form? . . . [A]voiding favoritism because of timing is a difficult task under 2-207.”).

380. James J. White, *Autistic Contracts*, 45 WAYNE L. REV. 1693, 1699 (2000). *But see* Mark A. Lemley, *Terms of Use*, 91 MINN. L. REV. 459, 465 (2006) (“But in today’s electronic environment, the requirement of assent has withered away to the point where a majority of courts now reject any requirement that a party take any action at all demonstrating agreement to or even awareness of terms in order to be bound . . . .”).

381. *See* John D. Wladis, *Contract Formation Sections of the Proposed Revisions to U.C.C. Article 2*, 54 SMU L. REV. 997, 1030 (2001) (“The contract is formed on the jointly agreed upon terms, plus those terms incorporated by the U.C.C. The justification for applying the neutrality principle is to avoid any strategic advantage to sending the first or last record.”) The focus on agreement also affects the uses of § 2-207. White, *supra* note 316, at 731 (“[I]t is not quite fair to say that amended Section 2-207 is only about interpretation and not about the contract formation, because courts will also be answering formation questions when they decide whether the parties have *agreed* to a term.”).

382. *See infra* app. I, § 2.207(1); *see also* U.C.C. § 2-207(a) (amended 2003), 1 U.L.A. 397 (2004).

383. TEX. BUS. & COM. CODE ANN. § 2.207(c) (Vernon 1994).

§ 2.207 will apply to “all contracts,” terms appearing in both parties’ records will be used to determine the terms of contracts across a wider scope.<sup>384</sup> When both parties use the same terms in records or confirmations, amended § 2-207 honors the agreement of the parties.<sup>385</sup>

### 3. *Comparison of Current and Amended § 2-207 in Application*

Given the long and vigorous opposition to these changes in § 2-207, an assessment of what the amended section would do under some representative Texas and other well-known decisions will be useful. First, there is one practical point worth remembering about the battle of the forms.

In 1994, Thomas J. McCarthy, Corporate Counsel in the Legal Department of E.I. du Pont de Nemours and Company, and chairperson of the ABA Task Force on the Article 2 Revisions, commented on developments in electronic contracting and the absence of “terms and conditions” in that new transactional process:

Business’ refusal to include legal boilerplate in the free text of transaction sets should not be surprising because it is illustrative of a reality of which commercial lawyers have long been aware. Businesspersons do not consider the boilerplate printed on the reverse side of their forms to be part of the deal unless it coincidentally reflects some aspect of custom, usage, course of dealing, or practice that they understand as implicit in the resulting transactional relationship.<sup>386</sup>

Of more recent date, one commentator reporting on the battle of the forms observed the following:

What I found is that nearly half of the twenty-five companies that I interviewed were either never or virtually never in a position even to engage in a battle of the forms at all, due to the nature of their contract formation practices. . . .

. . . .

Even where companies enter into a battle of the forms, they rarely find themselves in a position where the differences in the nonimmediate terms matter. The most common reason suggested . . . is that in most cases the

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384. *See infra* app. I, § 2.207.

385. A court will need to use caution in evaluating terms that appear with slight differences in both forms. Are they the same terms with immaterial differences, or different terms? *Compare* Memorandum from Jeff Dodd to Stephanie Heller, *supra* note 98, at 2 (“When is the last time that you saw matching proposed terms?”), *with* *Peters Fabrics, Inc. v. Jantzen, Inc.*, 582 F. Supp. 1287, 1291 (S.D.N.Y. 1984) (finding contract formation despite a slight variance in arbitration terms), *and* *Baird & Weisberg*, *supra* note 356, at 1233-35 (reviewing commonlaw mirror image cases where minimal variances did not prevent agreement).

386. Thomas J. McCarthy, *An Introduction: The Commercial Irrelevancy of the “Battle of the Forms,”* 49 BUS. LAW. 1019, 1026 (1994).

value of the relationship to both parties will exceed whatever amount is in controversy.<sup>387</sup>

The lack of concern in some business quarters about terms of sale beyond item, price, quantity, and delivery date recorded by these writers, aligns with the observation that “[t]he parties’ behavior tells one that the transaction cost of negotiating each of these deals outweighs the cost of an occasional bad warranty or an ineffective disclaimer.”<sup>388</sup>

Thus, for some substantial part of business transactions that are conducted without “express agreement” through negotiation, “[t]o find a contract after a mindless exchange of printed forms and to construct it from fragments of printed forms and code parts, is probably consistent with the expectations of the parties in the transactions under section 2-207.”<sup>389</sup> Perhaps “freedom of contract” is not the exact concern of opponents of revised § 2-207. If “freedom of contract” means “the right to make an agreement,” revised § 2-207 particularly includes terms to which both parties agree and encourages the courts to look to agreement evidenced by conduct or grounded on trade usage and course of dealing.<sup>390</sup>

#### 4. Three Sample Transaction Patterns

What remains then is the concern that changes made by revised § 2-207 would “upset the commercial balance between buyers and sellers”<sup>391</sup> or change the allocation of risk presently and commonly understood.<sup>392</sup> We shall test that concern in three settings:

- (1) The commercially common case of a battle of offer and acceptance forms, including forms that are drafted as “exclusive terms” forms, exchanged with little or no direct discussion.
- (2) The commercially common case of a form or forms sent in confirmation “after” the transaction is agreed.
- (3) The consumer and commercial case of “payment now, terms later,” often called a “Gateway” or “rolling contract” case.<sup>393</sup>

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387. Daniel Keating, *Exploring the Battle of the Forms in Action*, 98 MICH. L. REV. 2678, 2696, 2698 (2000). The sample of companies consulted was twenty-five companies with offices in St. Louis, Missouri, with the majority having sales of \$1 billion or more annually. *Id.* at 2693.

388. White, *Autistic Contracts*, *supra* note 380, at 1705.

389. *Id.*

390. *See supra* notes 382-85 and accompanying text.

391. Letter from Quentin Riegel to J. Scott Sheehan, *supra* note 91, at 1.

392. *See supra* Part II.B.3. (discussing questions of baseline UCC terms as favoring one party or another).

393. *Compare* Hill v. Gateway 2000, Inc., 105 F.3d 1147, 1148, 1151 (7th Cir. 1997) (enforcing arbitration term included in terms contained in the box for a computer delivered following telephone transaction), *with* Klocek v. Gateway, Inc., 104 F. Supp. 2d 1332, 1337-42 (D. Kan. 2000) (refusing to enforce arbitration term included in “terms in a box” for computer purchase and assuming the purchase was either a telephone order followed by shipment or an in-person purchase).

*a. Battle of the Forms*

First, in a commercial transaction between merchants where, without prior negotiation that produces an agreement in fact, each party sends its form that states “the terms of my form shall be the exclusive terms of the transaction, and recipient’s assent to these terms is a condition of any agreement,” the parties will have precluded an agreement from the exchange of forms alone.<sup>394</sup> If the offer and the acceptance (or either) require assent to only their respective terms, and differing material terms are in the forms, then no contract is formed through the exchange of forms.<sup>395</sup> If parties who exchanged forms that do not (under current § 2.207(a)) result in a contract, then proceed to perform such that a contract arises through conduct (§ 2.204), its terms are those prescribed by current § 2.207(c)—the terms on which the writings agree, plus supplementary terms incorporated under other provisions of the Code.<sup>396</sup>

Case law under the current § 2-207 has considered which terms apply when the “acceptance” in a battle of the forms case is really an expressly conditional response under § 2-207(1) with terms that differ from the offer.<sup>397</sup> An early question, reflecting common law counter-offer cases, was whether the initial offeror who accepts and pays for the goods after receiving the conflicting response conditioned on acceptance of its terms has agreed to the different terms that were a condition of the acceptance.<sup>398</sup> The first answer to that question was the now-abandoned *Roto-Lith* decision: Yes, the initial offeror’s (buyer’s) acceptance of and payment for goods, with knowledge of the conditional acceptance but without giving explicit assent to the altered term, constituted agreement to the terms set out in the conditional acceptance, and the response was treated as a common law counter-offer.<sup>399</sup> *Roto-Lith* reinstated the common law “last shot” rule and received frequent criticism for failing to implement the precepts of the Code in § 2-207.<sup>400</sup>

394. See, e.g., WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 72.

395. See *id.* (“Where the restrictive language in the offer is construed to limit forms of acceptance to documents that neither add nor contradict, no contract exists at the conclusion of the exchange of forms since no 2-207(1) acceptance occurred.”); see also *Boise Cascade Corp. v. Etsco, Ltd.*, 39 U.C.C. Rep. Serv. (CBC) 410, 414 (D. Or. 1984) (“The effect of the fact that both offer and acceptance expressly state that any contract formed must contain their terms and no others is that no contract was formed by the writings of the parties.”).

396. TEX. BUS. & COM. CODE ANN. § 2.207(c) (Vernon 1994); see, e.g., *Ionics, Inc. v. Elmwood Sensors, Inc.*, 110 F.3d 184, 189 (1st Cir. 1997); WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 72-73 (“Assume no contract exists under 2-207(1) yet the parties perform . . . [The] drafters sent us to section 2-207(3). . . .”). Section 2.207 of the Texas Business & Commerce Code does not vary from § 2.207 of the UCC except in numbering. See U.C.C. § 2-207, 1A U.L.A. 208-09 (2004).

397. See, e.g., *Roto-Lith, Ltd. v. F.P. Bartlett & Co., Inc.*, 297 F.2d 497 (1st Cir. 1962).

398. See *id.* at 500.

399. *Id.* *Roto-Lith* construed the seller’s response as an “acceptance expressly conditional on assent” to its terms, and applied the common law counter-offer rule to find assent by the buyer. *Id.* It is possible to construe the *Roto-Lith* response as an acceptance so that the disclaimer is not effective. WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 64.

400. See *Murray*, *supra* note 318, at 1330-31.

By 1997, with *Ionics, Inc. v. Elmwood Sensors, Inc.*, in which the First Circuit overruled *Roto-Lith*, the rejection of the first answer was complete.<sup>401</sup> In *Ionics*, the First Circuit held that no contract resulted from the exchange of exclusive and conditional conflicting forms, so that the seller's acknowledgment (with its warranty disclaimers and limitations) did not bind the buyer, even though acceptance of the goods and payment followed the receipt of the seller's form of acknowledgment.<sup>402</sup> The gap-filler terms provided by Article 2 on the issue in dispute (warranty) applied to the contract formed by the conduct of the parties, to the benefit of the purchaser, as it now had Code-implied warranties; the seller was adversely affected because it did not have its disclaimer and limitations.<sup>403</sup> There are several variations on the theme of what contract terms apply in an exchange of conflicting forms where at least one form insists that it can be accepted only on its terms.<sup>404</sup>

For purposes of analysis, the *Ionics* pattern can be Pattern (1)(A): The writings of the parties do *not* form a contract because each insists on a conflicting term, but performance follows, resulting in a contract by conduct whose provisions are determined by § 2.207(c) of the Texas Business & Commerce Code. Those terms are the "terms on which the writings of the parties agree" plus the "supplementary terms" incorporated under the Code.<sup>405</sup> Another Pattern (1)(A) case is *C. Itoh & Co. (America) Inc. v. Jordan International Co.*, in which the "expressly conditional" acceptance contained an additional term for arbitration, a point not covered in the offer nor supplied by the UCC.<sup>406</sup> The parties proceeded to perform, resulting in a contract, the terms of which did not include arbitration under the rule of current § 2.207(c): "If the seller does intend to close a deal irrespective of whether or not the buyer assents to the additional terms [in the response], he can hardly complain when

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401. *Ionics, Inc. v. Elmwood Sensors, Inc.*, 110 F.3d 184, 189 (1st Cir. 1997).

402. *Id.* at 189.

403. *Id.* at 189-90. The court depicted the *Ionics* offer as requiring exclusive terms, the *Elmwood* response as conditional on assent to its terms, and terms of the two documents as directly contradictory. *Id.* at 186-87. The court then applied a "knock out" rule to the differing terms under § 2-207(3). *Id.* at 189. The opinion went to some lengths to characterize the response by *Elmwood* (the seller) as being less than a counter-offer and even suggesting the *Elmwood* form "appears to contemplate an order's confirmation rather than . . . rejection in the form of a counter-offer," recognizing perhaps the need to avoid the "counteroffer riddle" described by Murray. *Id.* at 186; see *C. Itoh & Co. (Am.), Inc. v. Jordan Int'l. Co.*, 552 F.2d 1228, 1236-37 (7th Cir. 1977); Murray, *supra* note 318, at 1322. Grant Gilmore thought *Roto-Lith* was correctly decided on its facts: "I think it would have been outrageous to have saddled the seller with warranties, which (as the buyer knew) he had expressly (and quite reasonably) disclaimed." White, *Contracting Under Amended 2-207*, *supra* note 316, at 725 (quoting Letter from Grant Gilmore to Robert S. Summers, *supra* note 319).

404. See, e.g., WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 56-81; Murray, *supra* note 318, at 1330-43.

405. TEX. BUS. & COM. CODE ANN. § 2.207(c) (Vernon 1994).

406. *C. Itoh*, 552 F.2d at 1230.

the contract formed . . . as a result of the parties' conduct is held not to include those terms."<sup>407</sup>

In a Pattern 1(A) case under the proposed § 2.207, the result will be the same as in *Ionic*s and *C. Itoh*. The contract formed by conduct will not include terms that conflict. Those conflicting terms at issue in a dispute clearly do not appear in both records, nor are they terms to which both parties agree. Failing the tests of amended § 2.207(1) and (2), the conflicting terms fall out, leaving the terms provided by amended § 2.207(3).<sup>408</sup> The operation of § 2.207 is no longer influenced by terms "that insist on all of that record's terms and no other terms as a condition of contract formation."<sup>409</sup>

The next patterns for case analysis under Pattern (1) are those in which an offer and acceptance are not respectively conditional on the exclusivity of their terms but in which the "acceptance" has additional terms (Pattern (1)(B)) or has different terms (Pattern (1)(C)). Pattern (1)(B), the additional terms variety, is explicitly addressed by current § 2.207(b): "The additional terms are to be construed as proposals for addition [and between merchants will] become part of the contract" unless excluded by the three subparts of that section.<sup>410</sup> Official Comments 4 and 5 address the usual dispute over "additional terms"—determining whether they are a material alteration excluded by § 2.207(b)(2).<sup>411</sup> Additional terms that are material alterations under the Official Comments include the following: a warranty disclaimer in transactions when the warranties normally apply, a shortened period for notices of defects, and terms that are characterized as producing surprise or hardship unless expressly addressed.<sup>412</sup> Examples of additional terms that are *not* material alterations are set out in Official Comment 5.<sup>413</sup> Under the tests of § 2.207(b), "unread reasonable clauses (form and non-form) [are allowed] to enter the contract by silence," but assent by silence would not extend to unreasonable terms, as they would "materially alter[]" the deal.<sup>414</sup> If the question concerns an initial document (an offer by Party 1) as to which the responsive acceptance (from Party 2) is silent, or relies on an unstated UCC gap-filler to raise an additional term for inclusion, then the response of Party 2 does not present an additional term for analysis

407. *Id.* at 1238. "Since provision for arbitration is not . . . supplied by one of the Code's 'gap-filler' provisions . . . there is no arbitration term in the Section 2-207(3) contract . . ." *Id.* at 1237.

408. *See infra* app. I, § 2.207(1)-(3); *see also* U.C.C. § 2-207(a)-(c) (amended 2003), 1 U.L.A. 397 (2004); WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 185.

409. U.C.C. § 2-207 cmt. 2 (amended 2003), 1 U.L.A. 398 (2004).

410. TEX. BUS. & COM. CODE ANN. § 2.207(b).

411. *See id.* cmt. 4-5. Murray argues that current § 2.207(b)(2) on material alteration is the heart of the "additional" terms rules: "Subsection [(b)(2)] would excise terms that materially alter the offer *absent* any clause limiting acceptance . . . or anticipatorily objecting to variant terms." *See Murray, supra* note 318, at 1364-69. Murray argues that "additional" includes "different." *Id.*

412. TEX. BUS. & COM. CODE ANN. § 2.207 cmt. 4.

413. *See id.* cmt. 5.

414. Wladis, *supra* note 381, at 1014.

under § 2.207(2), and the offer is accepted as it stands.<sup>415</sup> In terms used by § 2.207, the response (be it acceptance or confirmation) that is silent on a term explicitly stated in the first document, or at most would rely on a gap-filler, does not propose an additional term that requires analysis under § 2.207 and its Comment 6.

Pattern (1)(C), with different terms in an effective acceptance (not conditional on assent to the terms), is the difficult case under current § 2.207. To begin, current § 2.207(b) speaks only to “additional” terms, even though § 2.207(a) refers to “additional or different” terms.<sup>416</sup> It is downhill from there in looking for an analysis of § 2.207 that, consistent with the statute and comments, can reconcile the treatment of “different” and “additional” when applied to acceptances.<sup>417</sup> However, a trend (in non-Texas decisions at least) is emerging. In a transaction in which the contract does arise from the exchange of forms, because the acceptance is not conditioned upon assent to its different term, but there is nonetheless a conflict between the terms proposed by Party 1 and Party 2, courts now tend to employ a “knock out” rule. The majority rule is expressed as follows: “[T]he discrepant terms fall out [on both sides] and are replaced by a suitable UCC gap filler.”<sup>418</sup>

*Northrop* observes that the Seventh Circuit’s preferred view would be that of the California courts, in which an offeree’s different term does not knock out both terms (including the offeror’s), but rather the offeror’s term remains and the different term from the offeree drops out.<sup>419</sup> This minority alternative uses the “additional terms” rules for a “different” term: because a different term will almost always be a material alteration in the terms offered (if it were additional), under the California reading of § 2.207(b)(2), the material alteration (and not the original term) drops out.<sup>420</sup>

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415. See WHITE & SUMMERS, UNIFORM COMMERCIAL CODE, *supra* note 226, at 63-64 n.22-23. *But see* Murray, *supra* note 318, at 1369 (observing that “it is absurd” to include implied UCC terms in an offer and to exclude them from the same form when looking for additional or different terms in a response or acceptance).

416. TEX. BUS. & COM. CODE ANN. § 2.207(a)-(b).

417. See generally Murray, *supra* note 318, at 1365 (canvassing the issues and concluding that “[i]f ‘different’ terms are included in subsection (2), they will be excised from the definite and seasonable expression of acceptance. This consequence is another evil that has been recognized in both case law and legal commentaries—the offeror always wins.”). White & Summers disagree on what should happen to different terms. See WHITE & SUMMERS, UNIFORM COMMERCIAL CODE, *supra* note 226, at 57-63.

418. *Northrop Corp. v. Litronic Ind.*, 29 F.3d 1173, 1178 (7th Cir. 1994) (predicting Illinois courts would adopt the majority view); see also *Daitom, Inc. v. Pennwalt Corp.*, 741 F.2d 1569, 1579 (10th Cir. 1984) (analyzing conflict between express term of offer and implied UCC term of non-conditional acceptance, and predicting Pennsylvania courts would adopt a “knock out” rule as to differing terms); *Reilly Foam Corp. v. Rubbermaid Corp.*, 206 F. Supp. 2d 643 (E.D. Pa. 2002); *Wladis*, *supra* note 381, at 1030 (noting that “[m]ost courts have applied the knockout rule” on conflicting terms, so that neither is in the contract). *But cf.* *Idaho Power Co. v. Westinghouse Elec. Corp.*, 596 F.2d 924 (9th Cir. 1979) (implied U.C.C. term does not create “different” term).

419. See *Northrop*, 29 F.3d at 1178.

420. See *id.* (citing *Steiner v. Mobil Corp.*, 569 P.2d 751, 759 n.5 (Cal. 1977)).

Texas cases have not squarely addressed the question of which terms apply when conflicting, exclusive terms are exchanged in a transaction with a contract arising solely out of performance (e.g., Pattern (1)(A) above). But a dispute in Texas under Pattern (1)(A) facts should have the same result under proposed § 2.207 as under present § 2.207.<sup>421</sup> Positing an expressly conditional response with “exclusive” terms that differ from those proposed in the offer, such that no contract was formed by the writings, proposed § 2.206(c)—which parallels current § 2.207(a)—precludes the conditional response itself from producing a contract from the exchange of documents alone.<sup>422</sup> In this pattern, proposed § 2.204(a)(2) brings the transaction under proposed § 2.207 as the “conduct” of the parties has recognized the existence of a contract although the exchange of records of the parties did not.<sup>423</sup> Proposed § 2.207(1)-(3) will then operate, as does current § 2.207(c), to determine the terms of the contract from the terms in both records (terms on which the writings of the parties agree) plus terms supplied or incorporated under any provision of Chapter 2 (supplementary terms incorporated under other provisions of the Code).<sup>424</sup> The only difference in text is that proposed § 2.207(2) will expressly include terms on which both parties agree, a provision of limited impact in litigation and one that does not change the outcome.<sup>425</sup>

Texas cases have raised issues under Patterns (1)(B) and (1)(C) that may have different outcomes under proposed § 2.207. *Reynolds Metals Co. v. Westinghouse Electric Corp.* is almost a Pattern (1)(C) case of differing terms in a contract that is formed by offer and acceptance.<sup>426</sup> Westinghouse sent a “full proposal” to Reynolds for the sale of an electric transformer and an engineer to perform the installation work.<sup>427</sup> The Westinghouse proposal excluded consequential damages, provided a one-year warranty from date of shipment, and excluded other warranties.<sup>428</sup> Reynolds, as a buyer, then “accepted the Westinghouse proposal with a purchase order whose warranty terms *conflicted to some extent*” with the Westinghouse proposal but were otherwise “compatible.”<sup>429</sup> Westinghouse acknowledged the Reynolds order

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421. See discussion *supra* Part III.B.4.

422. See discussion *supra* Part III.B.4. For example, *Ionics, Inc. v. Elmwood Sensors, Inc.*, and *C. Itoh & Co. (Am.) Inc. v. Jordan Int'l Co.*, would have like outcomes under current and proposed § 2.207. See *Ionics, Inc. v. Elmwood Sensors, Inc.*, 110 F.3d 184 (1st Cir. 1997); *C. Itoh & Co. (Am.) Inc. v. Jordan Int'l Co.*, 552 F.2d 1228 (7th Cir. 1977).

423. See *infra* app. I, § 2.204(a)(2); see also U.C.C. § 2-204(1) (amended 2003), 1 U.L.A. 386, 392 (2004).

424. See *infra* app. I, § 2.207; see also U.C.C. § 2-207 (amended 2003), 1 U.L.A. 397 (2004).

425. See TEX. BUS. & COM. CODE ANN. §§ 2.206-.207 (Vernon 1994); *infra* app. I, §§ 2.206-.207.

426. See generally *Reynolds Metals Co. v. Westinghouse Elec. Corp.* 758 F.2d 1073 (5th Cir. 1985).

427. *Id.* at 1074.

428. *Id.*

429. *Id.* (emphasis added). Note that acceptance by Reynolds meant that the determination of contract terms under current § 2.207 is under the rules applicable to “agreed” contracts of § 2.207(a). See *id.* Wladis makes the point that “[t]he drafters of Current 2-207 probably intended the terms of the offer to control” but that there is not a statutory statement that a contract formed by a definite expression of acceptance means that the offeree is bound by the terms of the offer. Wladis, *supra* note 381, at 1030 n.204.

and began to manufacture the transformer.<sup>430</sup> Thereafter at the request of Reynolds, Westinghouse extended the warranty term for a year in exchange for a payment by Reynolds.<sup>431</sup> Of course, the transformer failed, due to (according to Reynolds) improper design and improper installation.<sup>432</sup> Westinghouse defended on the grounds that its warranty, even as extended, had expired and that its liability was limited under its liability exclusion to the purchase price of the transformer, the proposal having excluded consequential and incidental damages, and Reynolds having failed to object to those terms in its response.<sup>433</sup>

The district court had applied a knock out rule under § 2.207(b) on the basis of conflicting terms between the offer (Westinghouse's warranty disclaimer) and the acceptance (Reynolds's acceptance "whose warranty terms conflicted to some extent" with the offer) to eliminate the warranty terms of each to the extent of conflict, but nonetheless found that limitations on warranty clauses had expired.<sup>434</sup> The Fifth Circuit merely noted a split of authority on whether a conflicting term in an acceptance (i.e., not an "additional" term in a confirmation) would be the only term to drop out, or would cause both the offeror's original limited warranty term and the conflicting term in the acceptance to knock each other out, thus reverting to UCC implied terms.<sup>435</sup> The Fifth Circuit held in *Reynolds* that the absence of an explicit term in the Reynolds acceptance that differed from the Westinghouse limitation of liability provision meant that the Westinghouse liability limitation term was included in the contract as accepted by Reynolds.<sup>436</sup> Under current § 2.207, the liability disclaimer term of the Westinghouse office was accepted by a "non-conditional" acceptance from Reynolds, an acceptance that did not propose a conflicting term on the point.<sup>437</sup>

The result in *Reynolds* seems to have turned on: (1) neither form, or at least not the Reynolds acceptance document, being an exclusive terms form—requiring agreement to the terms stated and no others as a condition of the contract—so that the court classified this as a contract by agreement, at least as to a controlling term; and (2) the Reynolds acceptance not setting up a direct

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430. *Reynolds*, 758 F.2d at 1074. Note that neither document is said to be an "exclusive terms" form. *See id.* at 1074-75. The court's usage of "Reynolds accepted" indicates that the parties had reached a contract on the writings then, so that § 2.702(c) does not apply. *See id.* at 1074.

431. *Id.*

432. *Id.* at 1075.

433. *Id.* at 1075-76.

434. *Id.* at 1076 n.5. This knock out rule for differing terms in an acceptance constituted the district court's prediction of how a Texas court would rule. *Id.*

435. *Id.* The split cited by the Fifth Circuit is that captured in WHITE & SUMMERS, UNIFORM COMMERCIAL CODE, *supra* note 226, at 57-63.

436. *Id.* at 1078 ("The district court correctly found that Westinghouse's disclaimer of liability . . . was part of the parties' contract."). Interestingly, the Fifth Circuit used a § 2.207 analysis to include a liability limitation provision that it then applied to damage claims relating to installation services. *Id.*

437. *See id.* *Reynolds* thus suggests that an implied U.C.C. term will not be read into a responsive document so as to create differing terms. *See Idaho Power Co. v. Westinghouse Elec. Corp.*, 596 F.2d 924, 927 (9th Cir. 1979).

conflict, in stated terms, with the Westinghouse damage limitation clause.<sup>438</sup> At least for those cases in which an offer and a non-conditional acceptance can be construed to result in a contract, *Reynolds* shows that an offer and acceptance (with no more than an implicit UCC gap filling term to conflict with an offered term) means that the contract resulting from the writings of the parties (i.e., the offer and acceptance) includes the offeror's express term by agreement.<sup>439</sup> That is the view of White and Summers as well.<sup>440</sup>

Another "nearly" Pattern 1(C) case is *United States ex rel. Varco Pruden Buildings v. Reid & Gary Strickland Co.*, also a construction contract case with complex facts.<sup>441</sup> In *Varco Pruden*, not one but two sets of purchase orders were exchanged: "On June 4, 1993, Strickland signed and returned to Varco Pruden . . . a purchase order for metal building components. . . . [On August 2, 1993], Strickland submitted an order form to Varco Pruden . . . [and] Varco Pruden returned the form on March 15, 1994."<sup>442</sup> Of course, the two (apparently signed) order forms conflicted, this time on the applicable law. In discussing the argument (of Varco Pruden) that if the June 4th purchase order delivery was only an offer, then the second exchange presented a § 2.207 issue of what to do with differing terms on applicable law, the Fifth Circuit commented that under Texas law, "there is a split of authority as to whether the offeror's terms control or whether the conflicting terms drop out of the contract," citing *Reynolds* and *Brochstein's, Inc. v. Whittaker Corp.*<sup>443</sup> The Fifth Circuit did not tackle the "knock out" issue under Texas law as it concluded "the stronger view appears to be that the June 4 order was a binding contract under [both New Mexico and Texas enactments of § 2-207] and the August 2 order was a valid modification under Texas Business & Commerce Code § 2.209" and the New Mexico counterpart.<sup>444</sup> Thus, *Reynolds* and *Varco Pruden* find agreements that have consistent terms rather than agreements with differing terms, so as to require the court to determine which different term controlled.<sup>445</sup>

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438. See *Reynolds*, 758 F.2d at 1078-80. A conflict could arise indirectly by reference to §§ 2.714 and 2.715 of the Texas Business & Commerce Code, which permit recovery of consequential damages in a proper case. WHITE & SUMMERS, UNIFORM COMMERCIAL CODE, *supra* note 226, at 63-64 (discussing the indirect conflict case and referencing *Idaho Power*).

439. *Reynolds*, 758 F.2d at 1078. Note that performance of such contracts is often the reason a Statute of Frauds issue does not arise. Cf. TEX. BUS. & COM. CODE ANN. § 2.201 (Vernon 1994).

440. WHITE & SUMMERS, UNIFORM COMMERCIAL CODE, *supra* note 226, at 64 n.23.

441. *United States ex rel. Varco Pruden Bldgs. v. Reid & Gary Strickland Co.*, 161 F.3d 915, 917-18 (5th Cir. 1998).

442. *Id.* at 917.

443. *Id.* at 921. As to New Mexico law, the court observed that terms in the June 4 and August 2 orders that conflicted would not become part of the contract. *Id.* (citing *Gardner Zemke Co. v. Dunham Bush, Inc.*, 850 P.2d 319 (N.M. 1993)). The court concluded that it did not need to resolve the "knock out" question for Texas U.C.C. purposes because, even if the choice of Tennessee law remained (as a surviving term in an offer), Texas courts (as the forum pursuant to a venue selection clause stipulated to be valid) would not permit that choice to control as Tennessee had no substantial relationship to the parties or transaction. *Id.*

444. *Id.*

445. See discussion *supra* notes 426-44.

*Permian Petroleum Co. v. Petroleos Mexicanos* is a Texas case that addresses the rule under current § 2.207 for Pattern (1)(B) additional terms.<sup>446</sup> Pursuant to telex orders, Permian delivered liquefied petroleum gas shipments to Petroleos Mexicanos (Pemex) with invoices that included a provision for interest on unpaid balances.<sup>447</sup> Pemex disputed its liability for interest.<sup>448</sup> If Pemex's telex orders to Permian for deliveries were considered offers (rather than invitations for offers to be made to Pemex), "Permian's invoices were written confirmations of acceptance which operate as acceptances . . . and the interest provision in the Permian invoices was a proposal for an addition to the contract."<sup>449</sup> Based on its confirmation approach, the Fifth Circuit applied the standards of Comment 5 to § 2.207 on additional terms and held that Permian's interest term became part of the contract.<sup>450</sup>

The proposed amendments to §§ 2.206 and 2.207 would not alter the results in every case. *Ionics* involved Pattern (1)(A) conflicts between exchanged forms, which the First Circuit construed to be mutually exclusive: "In summary, Ionics' order included language stating that the contract would be governed exclusively by the terms included on the purchase order and that all remedies . . . would be available . . . Elmwood, in turn, sent Ionics an Acknowledgment stating that the contract was governed exclusively by the terms in the Acknowledgment, and Ionics was given ten days to reject this 'counteroffer.'"<sup>451</sup> As there was an expressly conditional acceptance, the First Circuit held that the contract was formed by performance (not by the exchange of forms alone), conflicting terms cancelled out, and the applicable terms were the common terms in each form plus terms supplied by the Code.<sup>452</sup> In *Ionics*,

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446. *Permian Petrol. Co. v. Petroleos Mexicanos*, 934 F.2d 635, 654-55 (5th Cir. 1991).

447. *Id.* at 654.

448. *Id.*

449. *Id.* The *Permian* reference to "invoices [that] were written confirmations of acceptance which operate as acceptances" is confusing on the facts of the case. *Id.* The *Permian* court stated that after receipt of a Pemex telex, "Permian delivered the LPG with invoices which were stamped by Pemex upon receipt." *Id.* Thus, the invoices were too late to be an *acceptance* proposing additional terms because the contract had been partially performed by the vendor—the party seeking to include interest terms. *Id.*; see *Enpro Sys., Ltd. v. Namasco Corp.*, 382 F. Supp. 2d 874, 882-83 (S.D. Tex. 2005). A confirmation that proposes, but does not attempt to require assent, to different or additional terms with reference to an existing oral agreement can operate as an acceptance by "not negating" that oral agreement and may also satisfy Statute of Frauds requirements. See *Echo, Inc. v. Whitson Co., Inc.*, 121 F.3d 1099, 1103-04 (7th Cir. 1997); *Mid-South Packers, Inc. v. Shoney's, Inc.*, 761 F.2d 1117, 1123 (5th Cir. 1985). However, proposed § 2.207[ii] makes clear that a "confirmation" as such, even with different or additional terms, refers to an already existing agreement that is being "confirmed" but with a proposal for other terms. See *infra*, app. I, § 2.207[ii]; see also *Dorton v. Collins & Aikman Corp.*, 453 F.2d 1161 (6th Cir. 1972) (discussing confirmation-acceptance differences).

450. TEX. BUS. & COM. CODE ANN. § 2.207 cmt. 5 (Vernon 1994); *Permian*, 934 F.2d at 654.

451. *Ionics, Inc. v. Elmwood Sensors, Inc.*, 110 F.3d 184, 186-87 (1st Cir. 1997). The warranty terms were "diametrically opposed." *Id.* (quoting *Ionics, Inc. v. Elmwood Sensors, Inc.*, 896 F. Supp. 66, 68 (D. Mass. 1995)).

452. *Ionics*, 110 F.3d at 189-90. *Ionics* passes over a couple of points in its enthusiasm to undo *Roto-Lith*. *Id.* at 187-89. First, the offer from Ionics did not limit the contract to its terms. *Id.* But cf. *Salt River Project Agric. Improvement & Power Dist. v. Westinghouse Elec. Corp.*, 694 P.2d 267, 274-75 (Ariz. Ct. App. 1983), *approved in part, vacated in part, remanded*, 694 P.2d 198, 215 (Ariz. 1984) (explaining that an

the purchaser/offeror's implicit (Code) warranty term was therefore reinstated by its inclusion as a Code supplementary term.<sup>453</sup>

The result for an *Ionics* case under amended § 2.207 will be the same as under current § 2.207. An expressly conditional acceptance will, absent other facts, block the formation of a contract by the exchange of forms with conflicting terms under amended § 2.206(c): an expression of acceptance operates as an acceptance “unless acceptance is expressly made conditional on assent.”<sup>454</sup> The source of the contract is then considered under § 2.204(a)(2), “conduct by both parties which recognizes the existence of a contract.”<sup>455</sup> When a contract can then be enforced post-performance, its terms are “terms that appear in the records of both parties” and “terms supplied or incorporated under any provision of this chapter” (e.g., implied warranties under §§ 2.314-.315, and damage remedies under §§ 2.714-.715).<sup>456</sup> In this Pattern (1)(A), both current § 2.207 and amended § 2.207 “enshrine the neutrality principle: neither party's form controls.”<sup>457</sup>

The *Reynolds* case is not quite a Pattern (1)(C) structure because the Fifth Circuit did not have to address what happens in Texas to the different (conflicting) terms in an acceptance that is not itself conditioned on assent.<sup>458</sup> The District Court had predicted that conflicting terms in an offer and acceptance would result in a knock out of both.<sup>459</sup> Similarly, it is not quite a Pattern (1)(B) case—there was not an additional term on damages expressly proposed in the acceptance but rather an acceptance of the damage limitation as set out in the offer.<sup>460</sup> *Reynolds*, however, illustrates the Pattern (1)(B) problem under amended § 2.207 concerning the disposition of a term in only one of two documents, where the contract is formed by the documents.<sup>461</sup> The offer in *Reynolds* came from Westinghouse, the seller, in the form of a proposal that incorporated disclaimers of implied warranties and incidental and consequential damages.<sup>462</sup> Reynolds then “accepted the Westinghouse proposal with a purchase order whose *warranty* terms conflicted to some extent” but was “in all other respects compatible” with the offer, and work commenced.<sup>463</sup> Although

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explicit term in an offer deeming any variance to be a counteroffer results in conditional acceptance being treated as a true counteroffer, accepted by conduct of offeror even absent express assent). Second, the conflict in terms was not between express terms, but between an implied term and an express term. *Ionics*, 110 F.3d at 187-89.

453. *Ionics*, 110 F.3d at 187-89.

454. See *infra* app. I, § 2.206(c).

455. See *infra* app. I, § 2.204(a)(2); see also *infra* app. I, § 2.201(c)(3) (explaining the performance exception to the Statute of Frauds).

456. See *infra* app. I, §§ 2.207(1), (3), 2.314-.315, 2.714-.715.

457. Wladis, *supra* note 381, at 1028-89 (analyzing 2001 text of amendments, which substantially conform to 2003 Amendments in § 2.207).

458. *Reynolds Metals Co. v. Westinghouse Elec. Corp.*, 758 F.2d 1073, 1076 n.5 (5th Cir. 1985).

459. *Id.*

460. *Id.* at 1074-76.

461. *Id.*; see *infra* app. I, § 2.207.

462. *Reynolds*, 758 F.2d at 1074.

463. *Id.* (emphasis added).

the Fifth Circuit noted a split on whether *conflicting* terms between an offer and an acceptance either cancel each other out or the second form's conflicting terms are simply not included under present § 2.207, it held that the liability disclaimer in the original offer (Westinghouse) was included as a contract term because the acceptance did not have a conflicting term and was silent on the point (implying UCC standard provisions only).<sup>464</sup> Consequently, because the express disclaimer was in the offer and was *not* objected to, the express term controlled as a term to which the offeree had agreed.<sup>465</sup>

*Permian* is also a Pattern (1)(B) case—the additional term was in the acceptance/confirmation of the seller.<sup>466</sup> The Fifth Circuit held that the additional term regarding interest, to which Pemex did not object until trial, was an included additional term as it was not a material alteration under § 2.207(b).<sup>467</sup>

Amended § 2.207 applies to contracts “formed in any manner.”<sup>468</sup> Thus, the liability disclaimer and remedy limitation seen in the *Reynolds* offer and the interest provision in *Permian* would *not* be automatically included as a contract term under either amended § 2.207(1)—it does not appear in both records—nor under § 2.207(3)—it is *not* supplied by Chapter 2, which provides otherwise.<sup>469</sup> Is a liability disclaimer and remedy limitation in an offer like that in *Reynolds* or an interest provision in an acceptance like the one in *Permian* completely excluded by amended § 2.207 if the other party is simply silent?<sup>470</sup> The bare-bones outcome of *Reynolds* and *Permian* under amended § 2.207 would likely be different from the outcome in each under current § 2.207.<sup>471</sup> As explained in Official Comment 2 to amended § 2-207, “When forms are *exchanged* before or during performance, the result from application of this [new] section differs from the prior Section 2-207 . . . and the common law in that this section gives no preference to either the first or the last form . . . .”<sup>472</sup> The extensive case and commentary on § 2-207 considered by the PEB Drafting Committee included cases in which a term in an offer was not expressly objected to in the acceptance, and thus became part of the contract terms. With that sort of background to the drafting of current § 2-207, the express recognition by the statute of only “terms that appear in the records of both parties” shows that automatic inclusion as a contract terms of offer terms not “objected to” in an

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464. *Id.* at 1076, 1078.

465. *Id.* at 1078-80.

466. *Permian Petrol. Co. v. Petroleos Mexicanos*, 934 F.2d 635, 653-55 (5th Cir. 1991).

467. *Id.*; see also text accompanying *supra* note 449 (discussing the confirmation aspect of *Permian*).

468. See *infra* app. I, § 2.207.

469. See *infra* app. I, § 2.207(1), (3).

470. See *infra* note 472 and accompanying text.

471. See *infra* note 472 and accompanying text.

472. U.C.C. § 2-207 cmt. 2 (amended 2003), 1 U.L.A. 398 (2004) (emphasis added). The commonlaw rule is sometimes called a “last-shot rule” and the Code rule a “first-shot rule,” although the text and interpretations of § 2-207 do not produce consistent results. See Baird & Weisberg, *supra* note 356, at 1246-47; Murray, *supra* note 318, at 1370 n. 229.

acceptance is unlikely, absent more.<sup>473</sup> As observed with respect to the July 2000 draft of § 2-207, which tracks proposed § 2-207 in relevant particulars, “Additional terms that appear in the offer or the acceptance are not part of the contract under the Revision [of § 2-207], unless the other party agrees to them.”<sup>474</sup>

As the preceding phrase suggests, the answer to how terms in a single form as in a *Reynolds* or *Permian* case will be treated by amended § 2.207 in Pattern (1)(B) does not stop at this point. Amended § 2.207(2) includes, as part of the terms of the contract, terms, whether in a record or not, to which both parties agree.<sup>475</sup> The easy case for applying the “both parties agree” rule to the terms only in an offer is “a straightforward acceptance of an offer” or even an “acceptance accompanied by one or more additional terms.”<sup>476</sup> In the straightforward acceptance case (i.e., the second form says only “I accept” and either refers to or restates quantity, price, product, and shipment date from the first form), it is fair to say all the offeror’s terms are included under “both parties agree.”<sup>477</sup> In the case in which some additional terms appear, the offeror has a more difficult road but may have a basis for inclusion of offeror’s terms that were not affected by the response as constituting “agreed” terms, under the umbrella of the Code’s definition of “agreement.”<sup>478</sup>

*Construction Aggregates Corp. v. Hewitt-Robins, Inc.* recognizes that conduct (or other evidence) can show a party’s agreement to a term that does not appear in both records.<sup>479</sup> As described by the court there, the contract for a major component of a construction project consisted of (1) the buyer’s purchase order, which the buyer requested the seller to confirm, (2) the seller’s response, that stated its acceptance of the order “was predicated on certain modifications,” which the court treated as a counteroffer because it was expressly conditional, including a limited warranty and remedy term and disclaimer of consequential damages, and (3) a telephone discussion about the buyer’s request for a “change only in the terms of payment” set out in the seller’s response, which the seller accepted in a letter.<sup>480</sup> When the component failed to perform, the buyer sued on warranty claims; the seller defended under the warranty and liability disclaimers of its response/acceptance.<sup>481</sup> The Seventh Circuit held that the contract terms were those of the seller’s conditional response, which the court treated as a counteroffer that the buyer

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473. See U.C.C. § 2-207; *infra* app. I, § 2.207.

474. Wladis, *supra* note 381, at 1030.

475. U.C.C. § 2-207 cmt. 3 (amended 2003), 1 U.L.A. 397-98 (2004).

476. *Id.*

477. See *id.*

478. See *id.* (providing an example of additional terms not causing a knock out result).

479. See *Constr. Aggregates Corp. v. Hewitt-Robins, Inc.*, 404 F.2d 505, 509 (7th Cir. 1968), *cert. denied*, 395 U.S. 921 (1969).

480. *Id.* at 508-09. The changes were confirmed in a letter from the seller to the buyer as to which the buyer made no objection. *Id.*

481. *Id.* at 508.

accepted in a telephone call, except only those payment terms as to which the buyer objected.<sup>482</sup> As the court observed, “CAC can be said to have accepted the terms of H-R’s counter-offer.”<sup>483</sup>

Even more clearly, in *Cosden Oil & Chemical Co. v. Karl O. Helm Aktiengesellschaft*, the seller’s signing of buyer’s purchase confirmations operated as an acceptance of those terms, precluding addition of terms from the seller’s subsequent shipping documents.<sup>484</sup> Under the facts of a case such as *Reynolds*, however, the objections of the offeree (Reynolds) addressed only to the warranty terms and occurring in only an exchange of forms—without actual discussion—may be less effective to show agreement to the damage and liability disclaimer of the offeror (Westinghouse) to make that part of the contract under proposed § 2.207(ii).<sup>485</sup> Conversely, in *Permian*, the addition of an interest term in an invoice would not be evidence of an agreement to the term that belatedly appears in one document.<sup>486</sup> But proof of a usage of trade or course of dealing could bring the term in pursuant to § 2.207(3).<sup>487</sup>

Amended § 2.207 would not work a change from current § 2.207 on the inclusion of terms appearing in a single document “when assent has been manifested by conduct indicating that a particular term is part of the contract.”<sup>488</sup> As White and Summers observe, “This subsection gives courts latitude to find agreement in the verbal and nonverbal behavior of the parties *even when* the term to which they have agreed is not included in the records that either has sent, and even when the term is contradicted by the other’s form. We predict that this will be the battlefield under amended 2.207.”<sup>489</sup> Thus, while Pattern 1(A) cases will, as illustrated above, have similar outcomes under current and proposed § 2.207, the other two patterns will have more focus on agreement to terms, both explicit and from usage of trade and similar sources.<sup>490</sup>

This sort of inquiry will be justified, and even encouraged, by the opening clause in the text of amended § 2.207, stating that the rules on contract terms are subject to § 2.202, the amended provision on parol evidence.<sup>491</sup> Amended § 2.202 includes a new provision: “Terms in a record may be explained by evidence of course of performance, course of dealing, or usage of trade without a preliminary determination by the court that the language used is

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482. *Id.* at 509-10.

483. *Id.* On the other side of this approach is *H&W Industries, Inc. v. Occidental Chemical Corp.*, which analyzed proffered evidence of trade usage and found that the evidence was properly excluded as not credible as to the initial agreement for the transaction in question. *See H&W Indus., Inc. v. Occidental Chem. Corp.*, 911 F.2d 1118, 1122 (5th Cir. 1990).

484. *Cosden Oil & Chem. Co. v. Karl O. Helm Aktiengesellschaft*, 736 F.2d 1064, 1075 (5th Cir. 1984).

485. *Reynolds Metal Co. v. Westinghouse Elec. Corp.*, 758 F.2d 1073, 1077-78 (5th Cir. 1985).

486. *Permian Petrol. Co. v. Petroleos Mexicanos*, 934 F.2d 635, 654 (5th Cir. 1991).

487. *See infra* app. I, § 2.207(3).

488. Wladis, *supra* note 381, at 1029.

489. WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 184-85 (emphasis added).

490. *See infra* app. I, § 2.207(2)-(3).

491. *See infra* app. I, § 2.207.

ambiguous.”<sup>492</sup> This is, of course, from the same cloth as the definition of “agreement,” which will clearly affect this analysis of terms to which both parties agree.<sup>493</sup>

Whether amended § 2.207 results, for example, in the “exit” of remedy limitation and the “entrance” of implied warranties where the forms of the two parties do not match on these points depends on the factual underpinnings of the case. If the case is like *Cosden* or *Construction Aggregates*, the answer is probably the same under current and proposed § 2.207: facts that show an agreement of the parties or perhaps an established usage of trade will bring clause (2) or (3) of amended § 2.207 into play, so that terms will be included even if in a single document.<sup>494</sup> If we assume forms that are not expressly conditional or assent to their respective terms but have varying terms between the first order and a subsequent acceptance with terms—additional or different—to which the offeror does *not* object but does not expressly agree to by words or conduct, and then the offeror accepts goods and makes payment, we would have a contract on the writings of the parties under current § 2.207 and proposed § 2.207.<sup>495</sup> In this Pattern 1(C) situation, we have several possible answers, with the prospect of a “knock out” rule, although that is not a unanimous result.<sup>496</sup> Current § 2.207 would then look to the three tests of § 2.207(b) to determine inclusion or exclusion: offer limited acceptance to its terms; notification of objection; or material alteration of the offered term (from which the knock out rule on different terms derives).<sup>497</sup> Amended § 2.207 would be more limiting and knock out all varying terms unless the variances were resolved by proof of agreement or by terms supplied or incorporated under other provisions of Chapter 2.<sup>498</sup>

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492. See *infra* app. I, § 2.202(b). A generous early approval of the use of “course of dealing and usage of trade” to explain and supplement explicit written terms appears in *Columbia Nitrogen Corp. v. Royster Co.*, which held testimony of industry expectations that stated contract annual volumes were understood as estimates only, to be adjusted in light of circumstances, could be admitted even though the contract documents had specific quantities. See *Columbia Nitrogen Corp. v. Royster Co.*, 451 F.2d 3, 10-11 (4th Cir. 1971).

493. See TEX. BUS. & COM. CODE ANN. § 1.201(b)(3) (Vernon Supp. 2008) (defining agreement).

494. Other Texas cases suggest similar results. One case held that a contract was formed on the seller’s quotation that included all material terms and the buyer’s telex of intent stating goods, quantities, price, and delivery terms, plus price escalation and a much-discussed “data books” term. *Axelson, Inc. v. McEvoy-Willis*, 7 F.3d 1230, 1233 (5th Cir. 1993). An order sent by the buyer three months later with more detailed terms never became part of the contract. *Id.* *Axelson* would be an example under amended § 2.207 of a “straightforward acceptance” of terms appearing in single record. Another case excluded terms proposed in the original offer where the offeror signed the buyer’s purchase order on different terms and only specified objections to limited terms, but not the terms at issue: “[The] letter and WesTech’s signing of the purchase agreement amounted to an acceptance of all of the terms of the purchase agreement except those items of difference specifically noted in Wright’s letter.” *WesTech Eng’r., Inc. v. Clearwater Constructors, Inc.*, 835 S.W.2d 190, 199 (Tex. App.—Austin 1992, no writ).

495. TEX. BUS. & COM. CODE ANN. § 2.207 (Vernon 1994); *infra* app. I, § 2.207.

496. See *supra* text accompanying notes 416-20.

497. *Id.*; see text accompanying *supra* notes 416-20.

498. See *infra* app. I, § 2.207; see also *infra* note 643 and accompanying text.

*b. Confirmation Sent After an Agreement*

The second transaction pattern to compare results under current § 2.207 against results under amended § 2.207 is the pattern of a confirmation sent following an oral agreement. This pattern has fairly clear consequences under current § 2.207(b), even where there are additional terms proposed in the confirmation. First, recall that a confirmation is textually different from an “acceptance” in current § 2.207(a): an “expression of acceptance *or* a written confirmation.”<sup>499</sup> However, the text of current § 2.207(a) indicates that a confirmation, as well as an acceptance, “operates as an acceptance even though it states terms additional to or different from those offered or agreed upon.”<sup>500</sup> Amended § 2.207[ii] is the proposed revision of this text in the 2007 Bill; as revised, it refers to “a contract . . . [ii] confirmed by a record that contains terms additional to or different from those in the contract being confirmed.”<sup>501</sup>

*Brochstein’s, Inc. v. Whittaker Corp.* is an example of a Pattern 2 case from Texas.<sup>502</sup> In a continuing series of transactions, Brochstein’s representative would place a telephone order with a Whittaker representative, who would agree on the telephone call to fill the order.<sup>503</sup> Neither representative expressed any condition to its offer or acceptance, or advised that additional terms would be required.<sup>504</sup> The two parties then exchanged purchase orders (Brochstein) and acknowledgements or invoices (Whittaker), which apparently differed on warranty terms between the orders and acknowledgements.<sup>505</sup> The contract was formed by the telephone exchange; thus, each confirming document proposed additions to the contract that differed from, and served as objections to, the corresponding terms of the other.<sup>506</sup> Based on the conflict between confirming forms and the deemed objection by each party to the other’s conflicting term for purposes of current § 2.207(b)(3), the *Brochstein’s* court struck the conflicting terms and held the contract terms

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499. TEX. BUS. & COM. CODE ANN. § 2.207(a) (emphasis added).

500. *Id.*; see also *Permian Petrol. Co. v. Petroleos Mexicanos*, 934 F.2d 635, 654-55 (5th Cir. 1991); *Dorton v. Collins & Aikman Corp.*, 453 F.2d 1161 (6th Cir. 1972) (discussing confirmation-acceptance differences); *Enpro Systems, Ltd. v. Namasco Corp.*, 325 F. Supp. 2d 874, 882-83 (S.D. Tex. 2005) (discussing the role of a confirmation following contract formation).

501. See *infra* app. I, § 2.207; see also U.C.C. § 2-207 (amended 2003), 1 U.L.A. 209 (2004). As amended § 2.207 would apply to all contracts, the same elements would be reviewed both for contracts created by an acceptance and those being confirmed, so there should not be a gap as the result of omitting acceptances in this phrase in § 2.207[ii]. See *infra* app. II, § 2.207. A reference to different or additional terms in an acceptance is “[c]onspicious by its absence.” See *infra* app. II, § 2.207.

502. See *Brochstein’s Inc. v. Whittaker Corp.*, 791 F. Supp. 660, 661-62 (S.D. Tex. 1992).

503. *Id.* at 661.

504. *Id.*

505. *Id.*

506. *Id.* Where clauses on confirming forms sent by both parties conflict, each party must be “assumed to object” to the term conflicting with its form. TEX. BUS. & COM. CODE ANN. § 2.207 cmt. 6 (Vernon 1994).

were the terms agreed by telephone, the matching terms in both forms, and the terms provided by the UCC.<sup>507</sup>

In a variation on the *Brochstein* court's version of Pattern 2 cases, *Enpro Systems, Ltd. v. Namasco Corp.* dealt with whether a seller's delivery ticket or invoice operated as a confirmation (or even an acceptance) that could add a warranty disclaimer under § 2.207(b).<sup>508</sup> The court in *Enpro* relied on (1) evidence showing that the delivery ticket or invoice was to the receiving department rather than the purchasing department, implying its non-confirmation character, (2) the existence of a contract and its performance by delivery certainly no later than, and likely prior to, the delivery of the ticket or invoice, and (3) the view that "the confirmation process must end," in concluding that the delivery ticket or invoice was not a confirmation that could propose additional terms.<sup>509</sup> As a final point, *Enpro* left open for trial the factual question of whether a warranty disclaimer and liability limitation could be brought in as contract terms through proof of a usage of trade.<sup>510</sup>

Another series of non-confirmation cases should be mentioned to see if amended § 2.207 would alter the outcomes. *Preston Farm & Ranch Supply, Inc. v. Bio-Zyme Enterprises* arose out of a usury counterclaim to a suit regarding an unpaid account for livestock feed.<sup>511</sup> Open account sales of feed began in 1975.<sup>512</sup> Bills sent monthly had a legend that interest would be charged on accounts unpaid after thirty days.<sup>513</sup> When Bio-Zyme sued on the account, the purchaser and his corporate successor asserted usury on the ground that there was no agreement to pay interest, and the amount charged exceeded the rate permitted for open accounts.<sup>514</sup> The trial court found an agreement to pay the contract rate.<sup>515</sup> "The question of whether an agreement was reached by the parties is generally a question of fact where the existence of the agreement is disputed."<sup>516</sup>

As the buyer and seller were both merchants, the court of appeals applied § 2.207 to find an agreement to pay interest and considered the interest notations to be within the range of non-material alterations in confirmations between merchants.<sup>517</sup> The Supreme Court disagreed: "[T]he process of acceptance and confirmation to which Section 2.207 is addressed stops short of

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507. *Brochstein's*, 791 F. Supp. at 661.

508. *Enpro Sys. Ltd. v. Namasco Corp.*, 382 F. Supp. 2d 874, 876 (S.D. Tex. 2005).

509. *Id.* at 883-84. The "cut-off" quality of *Enpro* and other cases bears upon the "rolling contract" issues below. See *infra* note 529 and accompanying text.

510. *Id.* at 887. This is an existing option that amended § 2-207 does not change. *Id.*

511. *Preston Farm & Ranch Supply, Inc. v. Bio-Zyme Enters.*, 625 S.W.2d 295, 296 (Tex. 1981).

512. *Id.*

513. *Id.*

514. *Id.* at 297.

515. *Id.*

516. *Id.* at 298.

517. *Preston Farm & Ranch Supply, Inc. v. Bio-Zyme Enters.*, 615 S.W.2d 258, 261 (Tex. Civ. App.—Dallas 1981), *aff'd*, 625 S.W.2d 295; see also TEX. BUS. & COM. CODE ANN. § 2.207 cmt. 5 (Vernon 1994) (regarding "a clause providing for interest on overdue invoices" as a reasonable addition).

a monthly statement sent after the goods have been shipped.”<sup>518</sup> But the conduct of the buyer in continuing to purchase and pay with knowledge of the terms supplied an agreement sufficient for usury law purposes even though the agreement was not in writing.<sup>519</sup>

Another usury case with similar facts, *Tubelite v. Risica & Sons, Inc.*, confirmed the *Preston Farm* view that an acknowledgement and monthly invoices were not confirmations for purposes of § 2.207 where the contract was earlier formed by the buyer’s acceptance of the vendor’s own proposal that did not include a term for interest on past due amounts.<sup>520</sup> Once a contract is formed, Texas courts are not amenable to adding terms by confirmations.<sup>521</sup>

How would Pattern 2 cases such as *Brochstein’s* fare under amended § 2.207? *Brochstein’s* itself should have the same result: where a contract is formed by offer and acceptance, even if oral, and then confirmed by one or more records with additional or different terms (as compared to the “actual” agreement), the terms of the contract will not include conflicting terms on the confirmations. As in *Brochstein’s*, the terms of the contract would be the terms on which the confirmation forms agree, the terms supplied by the Code, and the terms on which the parties agree.<sup>522</sup>

What about *Enpro* or *Cosden*, where post-contract the seller delivered a document that set out a warranty disclaimer (*Enpro*) or a *force majeure* term (*Cosden*)? Both cases disavow the application of current § 2.207 for modification of terms from documents coming after the contract has been performed by one party.<sup>523</sup> In *Cosden*, the seller, which sought to add its *force majeure* term, had delivered products under a buyer purchase order the seller had already signed and returned.<sup>524</sup> In *Enpro*, “contract formation occurred when Namasco accepted the offer by shipping the steel plate before Enpro had any opportunity to review the delivery ticket/invoice terms.”<sup>525</sup>

One could argue that in *Enpro*, a post-contract confirmation might create an opportunity for mischief on the theory that the belated confirmation with differing term presents a knock out problem because, on that point, the term will not appear in the records of both parties.<sup>526</sup> The fact that a prior agreement is being confirmed should preclude such an argument, as the court should look

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518. *Preston Farm & Ranch Supply*, 625 S.W.2d at 299-300.

519. *Id.*

520. *Tubelite v. Risica & Sons, Inc.*, 819 S.W.2d 801, 802 (Tex. 1991). *Risica* also considered and rejected modifications under § 2.209: “Acquiescence to the contract [modifications] by the party to be charged may be implied from his affirmative actions, such as when he continues to order and accept goods with the knowledge” of a service charge. *Id.* at 805 (noting that failure to object, without more, was not agreement).

521. *See id.*

522. *See* WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 187, *infra* app. I, § 2.207(1)-(3).

523. *See Cosden Oil & Chem. Co. v. Karl O. Helm Atkiengesellschaft*, 736 F.2d 1064, 1073 (5th Cir. 1984); *Enpro Sys., Ltd. v. Namasco Corp.*, 382 F. Supp. 2d 874, 876 (S.D. Tex. 2005).

524. *Cosden Oil & Chem. Co.*, 736 F.2d at 1073.

525. *Enpro Sys. Ltd.*, 382 F. Supp. 2d at 880.

526. *See* Corneill A. Stephens, *Escape from the Battle of the Forms: Keep It Simple, Stupid*, 11 LEWIS & CLARK L. REV. 233, 257 (2007).

to proposed § 2.207(1) to include the “terms, whether in a record or not, to which both parties agree” in the contract and sidestep a claim that *now* there is a term on which the forms do not match.<sup>527</sup> White and Summers would concur:

Assume an oral agreement followed by a mutual exchange of forms and performance. . . . What if a term in one of the forms contradicts a term in the prior oral agreement? Tough. By hypothesis the parties have an oral agreement to a particular term and a later contradiction of that term by one party would not itself . . . remove the term that both had agreed upon orally.<sup>528</sup>

Thus, under amended § 2.207, *Brochstein's*, *Enpro*, and *Cosden* should have results equivalent to those reached under current § 2.207.

### *c. Gateway and Rolling Contract Cases*

The third transaction pattern to examine under current and amended § 2.207 is the “*Gateway*” or “rolling contract” pattern—a contract whose terms are not set at a single time but arrive over time.<sup>529</sup> The issue can arise in a commercial as well as a consumer context. The concept of a “rolling contract” is an extension of the position taken in the UCC and the Texas Business & Commerce Code: “An agreement sufficient to constitute a contract may be found even though the moment of its making is undetermined.”<sup>530</sup>

Rolling or layered contracts are contracts in which terms follow or are developed over time and after performance begins. In such contracts, a buyer often orders and purchases goods before seeing all of the contract’s terms (which may, for example, be contained within the product packaging). The buyer is typically given the right to return the goods within a specified period if such terms are unacceptable to the buyer. A rolling or layered contract is not consummated at the time of purchase or order, but only after the return period has elapsed.<sup>531</sup>

As with the information exclusion, the treatment of rolling or layered contracts also produced several unsuccessful attempts at a definitive resolution

527. *Id.*

528. WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 187 (proposing the same result if the term in the oral, prior agreement was a Code-supplied term rather than an express term, contradicted by one of two later confirmations).

529. *See infra* note 531 and accompanying text.

530. *E.g.*, TEX. BUS. & COM. CODE ANN. § 2.204(b) (Vernon 1994); *see also* U.C.C. § 2-204(1) (amended 2003), 1 U.L.A. 391 (2004) (“A contract . . . may be made in any manner sufficient to show agreement . . .”).

531. Stephen E. Friedman, *Text and Circumstance: Warranty Disclaimers in a World of Rolling Contracts*, 46 ARIZ. L. REV. 677, 679-80 (2004); *see also* Robert A. Hillman, *Rolling Contracts*, 71 FORDHAM L. REV. 743, 752-56 (2002).

during the drafting and negotiation of the 2003 Amendments.<sup>532</sup> The result of the committee's work was Comment 5 to amended § 2-207:

The section omits any specific treatment of terms attached to the goods, or in or on the container in which the goods are delivered. This article takes no position on whether a court should following the reasoning in *Step-Saver Data Systems, Inc. v. Wyse Technology*, 939 F.2d 91 (3d Cir. 1991) and *Klocek v. Gateway, Inc.*, 104 F. Supp. 2d 1332 (D. Kan. 2002 (original 2-207 governs) or the contrary reasoning in *Hill v. Gateway 2000*, 105 F.3d 1147 (7th Cir. 1997) (original 2-207 inapplicable).<sup>533</sup>

As Texas does not have a “rolling contract” case in the software arena, we refer initially to some of the leading cases elsewhere as a sample to test for changes under amended § 2.207. A case that did not adopt the rolling contract concept is *Step-Saver Data Systems*, cited in Comment 5 quoted above.<sup>534</sup> *Step-Saver* applied Article 2 to a dispute over the inclusion, or exclusion, of warranty disclaimers and remedy limitations in a “boxtop license” of software that Step-Saver acquired from The SoftwareLink, Inc. (TSL).<sup>535</sup> The district court held the license terms on the software boxes were effective to disclaim liability and warranties.<sup>536</sup> The Third Circuit reversed and remanded the warranty claims.<sup>537</sup>

The purchases in *Step-Saver* occurred through telephone orders placed with TSL, which the TSL representative accepted on the telephone.<sup>538</sup> Step-Saver issued its purchase orders, and TSL shipped the packaged products with invoices.<sup>539</sup> The box-top license terms were not raised in the telephone discussions.<sup>540</sup> The dispute over the disclaimers revolved around the point at which contract terms were fixed: upon receipt and opening of the products, or upon the completion of the telephone purchase call.<sup>541</sup> TSL argued that the lack of complete terms in the telephone exchanges precluded forming a contract, or that TSL's acceptance was conditional on assent to the full terms, which included the license, and that Step-Saver accepted that license, particularly as it became aware of its terms over the course of repeated purchases.<sup>542</sup>

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532. See WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 194-95 (discussing an unadopted subsection proposed as part of § 2-207).

533. U.C.C. § 2-207 cmt. 5 (amended 2003), 1 U.L.A. 399 (2004). Even this “no position” comment has its critics. See Braucher, *supra* note 215, at 763 n.61 (“It is clear that Article 2 addresses the issue . . . . It is just that amended Article 2 fails to state clearly how it deals with the issue, leaving the courts to guess.”) Braucher also opposes even the terms “rolling” and “layered” contracts. *Id.* at 757.

534. See *Step-Saver Data Sys., Inc. v. Wyse Tech.*, 939 F.2d 91, 99 (3d Cir. 1991).

535. See *id.* at 98-99.

536. See *id.* at 95.

537. See *id.* at 108.

538. See *id.* at 95-96.

539. See *id.* at 96.

540. See *id.* at 95-96.

541. See *id.* at 96-97.

542. *Id.* at 97-98.

The Third Circuit rejected the conditional assent argument of TSL, on grounds that TSL failed to make its assent expressly conditional as required by § 2-207(1), and also rejected inclusion of the disclaimers by a course of dealing between the parties.<sup>543</sup> From there, it was a short step to exclude a warranty disclaimer, if considered as a proposed additional term, as it “would, as a matter of law, substantially alter the distribution of risk” under the agreement reached by the parties by telephone, an agreement that was itself sufficiently definite to enforce.<sup>544</sup>

*Klocek* is similar but dealt with arbitration terms rather than warranties in a non-merchant transaction.<sup>545</sup> The details of the purchase transaction were unclear.<sup>546</sup> The district court surveyed the cases on enforcement of terms delivered with the product, finding no Kansas or Missouri cases on point, and emphasized the importance for UCC purposes of whether “the parties formed their contract *before* or *after* the vendor communicated its terms” to the buyer.<sup>547</sup> Thus, the *Klocek* court cast the transaction as being fixed by a non-conditional acceptance by Gateway of the buyer’s offer to purchase at the point of sale.<sup>548</sup> As *Klocek* was not a merchant, the inclusion options of § 2-207(2) did not apply; it would take express agreement of *Klocek* to have the license-arbitration term apply.<sup>549</sup> *Klocek*’s retention of the computer did not suffice.<sup>550</sup>

On the opposite side of the rolling contract issues are *Hill v. Gateway 2000, Inc.*<sup>551</sup> and *M.A. Mortenson Co., Inc. v. Timberline Software Corp.*,<sup>552</sup> both of which follow the lead of *ProCD, Inc. v. Zeidenberg*.<sup>553</sup> *ProCD* dealt with enforcement of a shrinkwrap license, delivered in the product box with the data and program disks, which appeared in part on a startup screen when the program was used.<sup>554</sup> The Seventh Circuit skirted the question of including “different or additional” terms under § 2-207 by asserting that § 2-207 *only* applies where multiple forms conflict, and all relevant terms were found in a single form, the user guide-license: “Our case has only one form; UCC § 2-207 is irrelevant.”<sup>555</sup>

543. *Id.* at 101-104. *But cf.* *M.A. Mortenson v. Timberline Software Corp.*, 998 P.2d 305, 305 (Wash. 2000) (holding the contract was not fully integrated and the provision limiting consequential damages was not unconscionable).

544. *See Step-Saver Data Sys., Inc.*, 939 F.2d at 105.

545. *Klocek v. Gateway, Inc.*, 104 F. Supp. 1332, 1334 (D. Kan. 2000).

546. *See id.* at 1336-37.

547. *See id.* at 1338; U.C.C. § 2-206 (amended 2003), 1 U.L.A. 395-96 (2004).

548. *See Klocek*, 104 F. Supp. 2d at 1341.

549. *Id.*

550. *Id.* There was no evidence that Gateway informed *Klocek* of a “return-or-agree option,” or that additional terms were mentioned. *Id.*

551. *See Hill v. Gateway 2000, Inc.*, 105 F.3d 1147, 1151 (7th Cir. 1996).

552. *See M.A. Mortenson Co. v. Timberline Software Corp.*, 998 P.2d 305, 318-20 (Wash. 2000).

553. *See ProCD, Inc. v. Zeidenberg*, 86 F.3d 1447, 1455 (7th Cir. 1996).

554. *See id.* at 1449. This was not a “boxtop” license delivery as in *Step-Saver*, in which it was visible when delivered, but not enforced. *Id.* at 1450.

555. *See id.* at 1452. That statement is wrong. By its terms, § 2-207 can apply to a *single* document proposing additional (or different terms). Friedman, *supra* note 531, at 753; WHITE & SUMMERS,

The *ProCD* court then focused on § 2-204 and the proposition that the vendor, as offeror, can shape the transaction and provide that acceptance occurs when the buyer performs the acts the vendor specifies as acceptance, i.e., using the program after receipt (or notice) of the license, and further providing that the buyer may (or must) return the product to reject the terms.<sup>556</sup> The result was that Zeidenberg “accepted” all terms by use of the product, some time after he had obtained goods (if programs are goods) and paid the price.<sup>557</sup>

*Hill* applied the *ProCD* thesis to a consumer transaction and to a purchase of a computer system, not just the software, in a telephone order/payment transaction.<sup>558</sup> “Gateway shipped computers with the same sort of accept-or-return offer *ProCD* made to users of its software.”<sup>559</sup> The plaintiff in *Hill* asserted product defects so severe that the “shortcomings make Gateway a racketeer.”<sup>560</sup> Gateway sought to compel arbitration under the terms delivered with the product.<sup>561</sup> Under the *ProCD* principle that the offeror can set terms of the transaction and of acceptance, and as the plaintiff was relying on the “enclosed with the product” warranty terms as part of the racketeering claims, *Hill* holds the buyer bound by the terms delivered, as contract formation (and the end of setting its terms) does not occur at the time of purchase but at the point of retention after a return period.<sup>562</sup> Again, with this structure of the transaction, § 2-207 remained on the sidelines.

*Mortenson v. Timberline* expanded the *Hill* principle to a commercial purchase order transaction.<sup>563</sup> That is, *Hill* presented a single transaction, with the court permitting the seller to set (or reset) the terms of the offer; *Mortenson* presented a transaction with a commercial buyer’s purchase order, which the seller’s dealer may have accepted, and in which the seller’s terms arrived “with the product,” a point in time that *Permian* and *Cosden* say is too late for additional (let alone different) terms to be added.<sup>564</sup> Following *ProCD* down the line, *Mortenson* used § 2-204 to allow the seller to (belatedly) set the terms to be accepted, thus creating a commercial rolling contract.<sup>565</sup>

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SUPPLEMENT, *supra* note 2, at 192; *see also* TEX. BUS. & COM. CODE ANN. § 2.207 cmt. 1 (Vernon 1994) (“[F]ollowed by one or both parties sending formal memoranda . . .”).

556. *See ProCD*, 86 F.3d at 1452-53; *cf.* U.C.C. § 2-206(1)(b) (amended 2003), 1 U.L.A. 181 (2004) (describing an offer to purchase as inviting acceptance by shipment). *ProCD* highlights three issues: who is the offeror, who can influence “how” acceptance occurs, and when the was the contract made? *See ProCD*, 86 F.3d at 1452-53.

557. *ProCD*, 86 F.3d at 1450.

558. *See Hill v. Gateway 2000, Inc.*, 105 F.3d 1147, 1149 (7th Cir. 1997).

559. *See id.*

560. *Id.* at 1148.

561. *Id.*

562. *See id.* at 1149.

563. *M.A. Mortenson Co. v. Timberline Software Corp.*, 998 P.2d 305, 307 (Wash. 2000).

564. *See id.* at 309. Because of its approach to contract formation, *Mortenson* did not consider the modification issues under § 2-209. *Id.* at 320; *see also Hill*, 105 F.3d at 1150; *Permian Petrol. Co. v. Petroleos Mexicanos*, 934 F.2d 635, 647 (5th Cir. 1991); *Cosden Oil & Chem. Co. v. Karl O. Helm Aktiengesellschaft*, 736 F.2d 1064, 1067-68 (5th Cir. 1984).

565. *See M.A. Mortenson Co.*, 998 P.2d at 309-10.

*Mortenson* dealt with a commercial transaction (but not between merchants) in which the plaintiff (Mortenson) had issued a purchase order for eight copies of an improved construction cost estimating program from an existing supplier.<sup>566</sup> The supplier delivered the products, with license terms (particularly liability disclaimers) and an access device that was required for use of each copy of the program.<sup>567</sup> Although the facts about notice of license terms during installation were disputed, the Washington court held the license (and disclaimers) enforceable because licenses had been part of the parties' transactions over time and Mortenson's continued use of the product constituted assent to the license terms, which were not additional terms but original terms.<sup>568</sup> This result "fosters uncertainty" because there are two plausible results, one under § 2-207 and the other under § 2-204.<sup>569</sup>

Texas decisions on "rolling contract" issues have arisen in other contexts. *Preston Farm & Ranch Supply* sets the tone.<sup>570</sup> That case held that invoices sent periodically after purchases do not constitute "confirmations" because "the process of acceptance and confirmation to which Section 2.207 is addressed stops short of a monthly statement sent after the goods have been shipped."<sup>571</sup> In *Enpro*, in which warranty disclaimers were set out both on the delivery ticket accompanying the goods and on an invoice, the court refused to treat the disclaimers as proposed additional terms.<sup>572</sup> The contract had been formed, and its basic terms set, "[p]robably as early as the moment the steel left Namasco for shipment to Enpro and certainly by the time it arrived."<sup>573</sup> Furthermore, as to the disclaimers, "the court concludes as a matter of law that neither the Namasco delivery ticket nor the Namasco invoice is a written confirmation . . . under § 2.207."<sup>574</sup>

The recent case of *Fieldtech Avionics & Instruments, Inc. v. Component Control.Com, Inc.* extends the "closure" principle to a commercial "purchase order-license at installation" case.<sup>575</sup> The supplier of software prepared a proposal to Fieldtech for software, installation, training, and maintenance; the proposal was signed by a Fieldtech representative.<sup>576</sup> At installation, a "click-wrap" license appeared, which included a warranty disclaimer and remedy

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566. *See id.*

567. *See id.* at 307-08.

568. *Id.* at 309-10. The Washington court added that using trade evidence at trial was not contradicted, so that would support the inclusion of license terms as part of the "agreement" in fact. *Id.* at 314.

569. Wladis, *supra* note 169, at 1751-52.

570. *Preston Farm & Ranch Supply, Inc. v. Bio-Zyme Enters.*, 625 S.W.2d 295, 299-300 (Tex. 1981).

571. *Id.*

572. *See Enpro Sys., Ltd. v. Namasco Corp.*, 382 F. Supp. 2d 874, 882 (S.D. Tex. 2005).

573. *Id.* at 880.

574. *Id.* at 884; *see also Cosden Oil & Chem. Co. v. Karl O. Helm Aktiengesellschaft*, 736 F.2d 1064, 1076 (5th Cir. 1984) ("As a matter of law the invoice terms did not modify the contract under section 2.207.").

575. *Fieldtech Avionics & Instruments, Inc. v. Component Control.Com, Inc.*, 262 S.W.3d 813, 829 (Tex. App.—Fort Worth 2008, no pet.).

576. *See id.* at 818.

limitation.<sup>577</sup> Between delivery and installation, Fieldtech executed a certificate of acceptance to the lease financier of the products.<sup>578</sup> As to express warranties, the *Fieldtech* court held that a disclaimer of express warranties “must be communicated to the buyer before the sale is consummated” and that the click-wrap disclaimer was not effective when the purchaser accepted the seller’s proposal at least a month prior to delivery and installation.<sup>579</sup>

Related to *Fieldtech* and other time of contracting cases are several Texas click-wrap consumer cases.<sup>580</sup> In *Hotels.com, L.P. v. Canales*, the court faced a dispute over class certification where an internet website’s terms of use included an arbitration term and a Texas choice of law provision.<sup>581</sup> The plaintiff claimed that charges to users for “taxes” were misleading and exceeded actual taxes.<sup>582</sup> But the plaintiff had made a hotel reservation by telephone.<sup>583</sup> Because the majority of customer transactions by the defendant were done through the company’s website, the court had to consider whether Canales was an adequate representative of the class.<sup>584</sup> The terms of use appeared only on the website, which required the user to click “I Agree” before reserving a room.<sup>585</sup> The terms of use were not directly displayed on the webpage but were available through an adjacent hyperlink.<sup>586</sup> In its analysis, the court identified a variety of click-wrap and browse-wrap options, as well as cases recognizing certain procedures providing assent to some terms and other procedures that did not.<sup>587</sup> The trial court had not considered the applicability of terms of use in internet transactions, so the court of appeals did not rule on the effectiveness of the click-wrap agreement.<sup>588</sup> The court of appeals reversed the trial court’s class certification and remanded for “rigorous analysis” of the applicability of the terms of use to those reserving through the website as a prerequisite of class certification.<sup>589</sup> However, in *Barnett v. Network Solutions, Inc.*, the court of appeals enforced a forum selection clause in a dispute

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577. *See id.* at 829.

578. *See id.* at 821.

579. *Id.* at 829. *Fieldtech* relies on automobile warranty disclaimer cases under § 2.316 and does not discuss §§ 2.204 or 2.207. *See id.* at 828-29.

580. *See* Ronald J. Mann & Travis Siebeneicher, *Just One Click: The Reality of Internet Retail Contracting*, 108 COLUM. L. REV. 984, 988-93 (2008) (reviewing and assessing a variety of click-wrap and browse-wrap cases).

581. *See* *Hotels.com, L.P. v. Canales*, 195 S.W.3d 147, 149-50 (Tex. App.—San Antonio 2006, no pet.).

582. *See id.* at 150. In *Rogers v. Dell Computer Corp.*, the court of appeals required the trial court to re-examine the effectiveness of Dell’s arbitration provisions in a dispute over amounts charged as “taxes” where the terms were delivered with the products. *See* *Rogers v. Dell Computer Corp.*, 138 P.3d 826, 834 (Okla. 2005). The majority and dissenting opinions review and catalog cases on terms of use, click-wrap, and § 2.207. *See id.* at 832-33, 836-38.

583. *See* *Hotels.com*, 195 S.W.3d at 150.

584. *See id.* at 154.

585. *See id.*

586. *See id.* at 155.

587. *See id.* at 155-56.

588. *See id.* at 157.

589. *See id.*

concerning registration of internet domain names where the transaction, conducted online, required the user to scroll through and accept the terms of use, which included the forum selection clause.<sup>590</sup>

As Texas does not have a definitive “rolling contract” case analyzing § 2.207 issues in a software case, and as the leading national cases are split, what would change in Texas if the 2007 Bill were adopted?

If we posit *Klocek*, *Hill*, and *Mortenson* as test cases, having reached different results on the rolling contract issue under current § 2-207, what does amended § 2.207 do to the results in each case?<sup>591</sup> This experiment begins with the observation that amended § 2.207 changes the fundamental inquiry in these cases. Instead of asking *when* a contract arose (at the time of purchase or at the time the user retained the goods) to determine which terms were in the contract at that time, amended § 2.207 would apply the *same* tests to find the terms for all contracts—terms that appear in the records of both that are supplied by the UCC or that are agreed to by both parties.<sup>592</sup> It remains possible to have timing questions arise as to terms coming in later by way of a modification, as amended Chapter 2 retains § 2.209 with only editorial changes.<sup>593</sup>

In *Mortenson*, the “records” in the transaction were a buyer purchase order and the seller’s license terms that appeared in the shrinkwrap packages, manuals, and the introductory screens.<sup>594</sup> Are the liability limitations and disclaimers in the materials that were delivered with the goods and appeared on Startup screens included as contract terms under amended § 2.207? They do not appear in the records of both parties.<sup>595</sup> They are not supported, and indeed are contradicted by supplementary UCC provisions, so they do not become included terms by amended § 2.207(3).<sup>596</sup> Could the license and its liability limitations be terms “to which both parties agree” so as to apply under proposed § 2.207(2)?<sup>597</sup> The *Mortenson* court would say “yes,” even under the proposed amendments, in light of that court’s reliance on § 2-204 and its assessment of agreement under § 1-201.<sup>598</sup> Section 2-204 states that a contract “may be made

590. See *Barnett v. Network Solutions, Inc.*, 38 S.W.3d 200, 204 (Tex. App.—Eastland 2001, pet. denied).

591. See discussion *supra* notes 545-66 and accompanying text. Mann and Siebeneicher acknowledge the ascendance of the cases enforcing “delayed” terms: “Although reasonable minds could differ on whether these so-called ‘shrinkwrap’ contracts should be enforced, the law has coalesced around a general acceptance of their enforceability.” Mann & Siebeneicher, *supra* note 580, at 988.

592. See *infra* app. I, § 2.207. Amended § 2-207 clearly applies to the “single form” situation, removing one leg of Judge Easterbrook’s *ProCD* and *Hill* analysis: “Does amended 2-207 apply to cases like [Hill v.] Gateway? We think so. Judge Easterbrook was mistaken about cases with only one form, and his position would be even farther from the truth under amended 2-207 . . . .” WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 195; see also Friedman, *supra* note 531, at 711.

593. See TEX. BUS. & COM. CODE ANN. § 2.209 (Vernon 1994); *infra* app. I, § 2.209.

594. See *M.A. Mortenson Co. v. Timberline Software Corp.*, 998 P.2d 305, 307, 313 (Wash. 2000).

595. See *id.* at 310.

596. See *infra* app. I, § 2.207(3).

597. See *infra* app. I, § 2.207(2).

598. See *Mortenson*, 998 P.2d at 310-13; U.C.C. §§ 1-201(b)(3), 2-204(1) (amended 2003), 1 U.L.A. 16, 391 (2004).

in any manner sufficient to show agreement, including conduct by both parties” recognizing the existence of the contract, and § 1-201(b)(3) makes language and inferences from circumstances, including course of dealing and trade usage, part of “agreement.”<sup>599</sup> The Washington Supreme Court found an agreement in *Mortenson* when the supplier showed a usage of trade that was not disputed and a course of dealing under which the software had previously been purchased with license terms as there provided.<sup>600</sup>

Two statutory considerations argue against repeating the *Mortenson* result under amended § 2.207(2), which is the only route available to include the late-arriving license and limitation terms at issue short of a modification. First, § 2.206(1) continues to provide that an offer to buy goods for prompt shipment invites acceptance by that shipment.<sup>601</sup> This suggests that in some, if not many, instances, the shipment of products “forms” the contract well before the delayed terms arrive, which then makes finding “agreement” of both parties to the later terms harder than under the “contract upon use and retention” model.<sup>602</sup> Second, the *Mortenson* court’s emphasis on the buyer’s continued purchase and use of programs with notice of a license is balanced by the seller’s continued delivery of programs without explicitly insisting an agreement to its terms. White and Summers are not sure what happens with a second purchase after terms are delivered with the first purchase from the same seller, referring to the current rule that a buyer who orders (with a record) and then accepts and pays for goods is not agreeing to the seller’s last shot disclaimer.<sup>603</sup> This criticism of the *Mortenson* result is also supported by Comment 5 to amended § 2-207: “However, repeated use of a particular term or repeated failure to object to a term on another’s record is not normally sufficient in itself to establish a course of performance, a course of dealing or a trade usage.”<sup>604</sup>

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599. U.C.C. §§ 1-201(b)(3), 2-204(1) (amended 2003), 1 U.L.A. 16, 391 (2004); see *Mortenson*, 998 P.2d at 314.

600. See *Mortenson*, 998 P.2d at 314. *Mortenson* does not deal directly with an issue raised by the dissent and noted in an article by John D. Wladis. See *id.* at 316 (Sanders, J., dissenting); Wladis, *supra* note 169, at 1750-51. The supplier’s authorized dealer signed *Mortenson*’s purchase order and ordered the software for delivery to *Mortenson*. See *Mortenson*, 998 P.2d at 320 (Sanders, J., dissenting). Depending on the authority of the dealer—whose role is not clear—the contract may have been formed at the signing and was certainly formed upon shipment and delivery, and the contract and its terms set before the delivery of the license, leaving only § 2-209 modification available to add terms. See *id.* at 319-20.

601. See U.C.C. § 2-206(1) (amended 2003), 1 U.L.A. 295-96 (2004); *infra* app. I, § 2.206(a). Although not discussed in *Mortenson*, the buyer’s purchase order stated, “ADVISE PURCHASING PROMPTLY IF UNABLE TO SHIP AS REQUIRED.” *Mortenson*, 998 P.2d at 308. Certainly in consumer transactions, the normal expectation is prompt shipment.

602. See *Enpro Sys., Ltd. v. Namasco Corp.*, 382 F. Supp. 2d 874, 880, 884-85 (S.D. Tex. 2005). *Enpro* points out that failing to object to a late arriving term, without more, does not show agreement or course of dealing sufficient to ratify a term that is not performed such as by late payment of a interest charge. *Id.*; see *Preston Farm v. Bio-Zyme Enters.*, 625 S.W.2d 295, 298-300 (Tex. 1981).

603. WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 197; accord John D. Wladis et al., *Sales*, 56 BUS. LAW. 1747, 1751 (2001).

604. See U.C.C. § 2-207 cmt. 4 (amended 2003), 1 U.L.A. 398-99 (2004). The references in the comment to terms in a single record may be directed to cases in which forms are delivered by both parties as

*Mortenson* was not a merchant case; therefore, the current question of including proposed additional or different terms under the three merchant options of UCC § 2-207(2) did not arise.<sup>605</sup>

For merchant cases with additional, not different terms, amended § 2-207 would change the inquiry, as “terms . . . to which both parties agree” replaces “[not] materially alter” as the test for inclusion.<sup>606</sup> For non-merchant cases, current § 2-207 does not provide a way for additional proposed terms to come in, unless by express agreement (or perhaps as a modification).<sup>607</sup> Thus, as a *Mortenson* case would involve dual (and dueling) forms with a term that appears in one form, but not in both, the primary route for inclusion of, for example, a liability limitation from a late arriving warranty/remedy document as between the immediate parties under amended § 2-207 would be to find that both parties agreed, even if the “delayed formation” view is applied.<sup>608</sup> In working through the problems of determining an “agreement by both parties” under amended § 2-207(2), the decisions under current § 2-207(2)(b) on material alteration between merchants may be instructive:

Subsection [2-207(2), amended] is of particular interest . . . because it appears to cover situations in which additional terms are unilaterally added by one party. Subsection [2-207(2), amended] provides that such terms are included if the parties “agree” to the terms, but does not define “agree.” . . . [I]t is likely that courts will still struggle when terms are added, with no objection by the other party, and a contract is moved forward upon. . . . The same factors that are considered in determining surprise and hardship [under the material alteration provision of current § 2-207(2)(b)], i.e., course of conduct, sophistication of the parties, industry customs and the

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an earlier comment observes a seller that delivers without sending a record “should normally be treated” as having accepted. *Id.* cmt. 3.

605. See *Mortenson*, 998 P.2d at 312 n.9. Some merchant cases go to some length in failing to find assent to adverse later terms. See, e.g., *Dramond Fruit Growers, Inc. v. Krack Corp.*, 794 F.2d 1440 (9th Cir. 1986); *Transwestern Pipeline v. Monsanto Co.*, 53 Cal. Rptr. 2d 887 (Cal. Ct. App. 1996).

606. See *infra* app. I, § 2.207. Of course, “materially alter” and “different” describe most changes in terms that parties will litigate. For current purposes, the “offer . . . limit[ing] acceptance” and “objection to [terms]” may be set aside, as amended § 2.207 is not affected by such. See *infra* app. I, § 2.207.

607. See *Klocek v. Gateway, Inc.*, 104 F. Supp. 2d 1332, 1341 (D. Kan. 2000) (“Because plaintiff is not a merchant, additional or different terms . . . did not become part of the parties’ agreement unless plaintiff expressly agreed to them.” (citing KAN. U.C.C. ANN. § 2-207 cmt. 2 (West 1996))); see also TEX. BUS. & COM. CODE ANN. § 2.207 (Vernon 1994); Braucher, *supra* note 215, at 761.

608. Cf. *infra* app. I, § 2.313A; cf. also U.C.C. § 2-313A (amended 2003), 1 U.L.A. 430-31 (2004). In a “[r]emote purchaser” transaction, the seller that gives a warranty-like obligation to the remote purchase “in the box” may, in the same way, provide limitations on remedies and also has a statutory exception to lost profits liability. *Id.* Thus, the *Mortenson* result might be obtained by a different route, if the plaintiff were a remote (not immediate) purchaser. See *id.*

inconspicuousness of the term would all help a court in determining whether a term was agreed to.<sup>609</sup>

A court determined to find agreement from use after startup-display of a license/disclaimer or through course of dealing or usage of trade may be able to find the facts to support the *Mortenson* result, but that is not an inevitable conclusion under amended § 2-207. Further, the finding of agreement by application of a “use after notice of delayed terms analysis” resembles, uncomfortably, the *Roto-Lith* approach of validating the common-law “last shot,” which § 2.207 has long sought to avoid.<sup>610</sup> Last, the “notification” of a liability-limiting term may come so late in the process as to be coercive.<sup>611</sup>

*Klocek*, the consumer case without a purchase order or other form from the buyer but a set of seller’s terms “in the box” upon delivery, was an arbitration dispute with Gateway arising after *Hill* was decided, not a warranty or liability limitation dispute.<sup>612</sup> In assessing *Klocek*’s likely result under the 2007 Bill, recall that proposed § 2.207 applies to *all* contracts and presumptively excludes (unless agreement or supplemental terms are separately shown) additional or different terms (i.e., terms on which forms do not match or terms in an “only form”).<sup>613</sup> Although an “acceptance . . . expressly made conditional on assent to the additional or different terms” will block consensual contract formation in proposed § 2.206, that does not block the application of § 2.207 if the parties perform.<sup>614</sup>

In contrast to *Mortenson*, *Klocek* was a single transaction case with first access to license terms, at least in any substantive way, being when the customer opened the box.<sup>615</sup> There was no prior notice of an offer being conditional on “exclusive terms” of the seller: “Gateway provides no evidence that at the time of the sales transaction, it informed plaintiff that the transaction was conditioned on plaintiff’s acceptance of the Standard Terms. . . . Gateway states only that it enclosed the Standard Terms inside the computer box for plaintiff to read afterwards.”<sup>616</sup> This single transaction context removes one of

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609. Colin P. Marks, *The Limits of Limiting Liability in the Battle of the Forms: U.C.C. Section 2-207 and the “Material Alteration” Inquiry*, 33 PEPP. L. REV. 501, 532 (2006). Of course, “agreement” is defined in unchanged U.C.C. § 1-201(b)(3), 1 U.L.A. 16 (2004).

610. See TEX. BUS. & COM. CODE ANN. § 2.207; *Roto-Lith, Ltd. v. F.P. Bartlett & Co.*, 297 F.2d 497 (1st Cir. 1962).

611. WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 196-97 (observing that a vendor who relies on a click-through customer assent to a start-up screen disclaimer, not seen until the product is assembled and ready for use, is raising an objectionable means of securing assent).

612. See Friedman, *supra* note 531, at 712-17 (arguing that “delayed warranty disclaimers” should have different requirements for enforceability than other terms).

613. See *infra* app. I, § 2.207; see also U.C.C. § 2-207 (amended 2003), 1 U.L.A. 397 (2004).

614. See *infra* app. I, §§ 2.206(c), 2.207.

615. See *Klocek v. Gateway, Inc.*, 104 F. Supp. 2d 1332 (D. Kan. 2000) (“Whenever it sells a computer, Gateway includes a copy of the Standard Terms in the box which contains the computer battery and power cables and instruction manual.”).

616. *Id.* at 1341.

the “agreement” factors in *Mortenson*, that of prior similar transactions with similar license/disclaimer terms provided to the buyer.<sup>617</sup> Also, other factors identified in regard to the surprise or hardship cases under current § 2.207(b)(2) are not present in *Klocek*, such as equally sophisticated parties and known industry customs.<sup>618</sup> As the merchant rules of current § 2.207(b) did not apply in *Klocek*, the court stated that “the Standard Terms did not become part of the parties’ agreement unless plaintiff expressly agreed to them.”<sup>619</sup>

The *Klocek* court could easily reach the same result under amended § 2-207 as it did under current law: the arbitration clause would not get in under clause (1) because there is only one record, and Gateway could only satisfy clause (2) if there was an agreement by Klocek himself to bring the arbitration clause into force.<sup>620</sup> That “agreement” from both parties depends, as expressed in Comment 3, on “a variety of verbal and nonverbal behavior” that the court must assess.<sup>621</sup> Agreement by the buyer on the telephone call or e-mail to accept the terms (to come in the box), to accept a deferred effective date (after receipt), or to accept a notice on the box of “terms inside” (in a retail store purchase) would all be relevant but not necessarily conclusive.<sup>622</sup> A click-through agreement at the beginning of the installation at home following payment and delivery is suspect.<sup>623</sup> Conversely, in those consumer transactions (and some commercial transactions) where the only form is the seller’s, the “passive party’s inaction opens that party’s performance to an enlarged risk” of being found to agree by inaction in the right case.<sup>624</sup> However, *Klocek* and Texas decisions, such as *Preston Farm & Ranch Supply* and *Enpro*, that emphasize a cutoff on the addition of terms where a contract is formed prior to delivery of a monthly invoice or a delivery ticket are consistent with amended § 2-207 in recognizing that a “confirmation” follows an agreement and in testing the inclusion of any later terms against the existing agreement of the parties, an approach which does not encourage, but leaves the door open for, actual agreement to bring in further, later terms.<sup>625</sup>

Finally, what would happen to *Hill* under amended § 2-207? *Hill*, by the same judge who decided *ProCD*, followed *ProCD* and held the offeror

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617. See *M.A. Mortenson Co. v. Timberline Software Corp.*, 998 P.2d 305, 314 (Wash. 2000).

618. See Marks, *supra* note 609, at 532.

619. *Klocek*, 104 F. Supp. 2d at 1341. “Agreed” terms are, of course, the primary concern of amended § 2-207(b). See U.C.C. § 2-207(b) (amended 2003), 1 U.L.A. 397 (2004).

620. See WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 195-96. Recall that even if an expressly conditional acceptance prevents a contract from the records, amended § 2-207 will apply to contracts recognized by conduct. See U.C.C. § 2-207 (amended 2003), 1 U.L.A. 397 (2004). Supplemental or incorporated terms pursuant to amended § 2-207(c) might apply in some instances. *Id.*

621. See U.C.C. § 2-207 cmt. 3 (amended 2003), 1 U.L.A. 398 (2004).

622. See WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 196-98 (discussing these variations on establishing “agreement”); see also Braucher, *supra* note 215, at 762.

623. WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 196-98; see also Braucher, *supra* note 215, at 762.

624. See WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 188.

625. See generally *Enpro Sys., Ltd. v. Namasco Corp.*, 382 F. Supp. 2d 874 (S.D. Tex. 2005); *Preston Farm & Ranch Supply, Inc. v. Bio-Zyme Enters.*, 625 S.W.2d 295 (Tex. 1981).

(Gateway) could shape the offer and the contract, so that the contract arose upon retention past a thirty-day return period, not at the time of payment and delivery.<sup>626</sup> As a result, *Hill* applied the “in the box” arbitration term and instructed the district court to compel the plaintiff to arbitrate.<sup>627</sup>

In assessing the *Hill* result under amended § 2-207, it is clear that the court would have to apply, instead of maneuver around, § 2-207 to find the terms of the contract: “Does amended 2-207 apply to cases like [Hill v.] Gateway? We think so. Judge Easterbrook was mistaken about cases with only one form, and his position would be even farther from the truth under amended 2-207.”<sup>628</sup> Second, amended § 2-207 changes the standards for determining the “contents” of all Chapter 2 contracts, setting out the three sources for the terms of the contract. One option under amended § 2-207 (“terms that appear in the records of both parties”) simply is not available in the “only one form” transaction:

Since the arbitration clause appears only in Gateway’s record, it does not get into the contract under [amended § 2-207(1)]. If there is only one record, the clause does not meet [amended § 2-207(1)] for the want of a second record; if there are two records, it fails because the clause will not appear in the buyer’s record.<sup>629</sup>

As the UCC will not supply a default arbitration clause, and as it would be more than difficult to show a course of dealing or usage of trade with a single consumer that brought in arbitration through those sources, the remaining route available to bring an arbitration clause into the contract in a *Hill* case is to show it is a term “to which both parties agree” under amended § 2-207(2).

Here we reach the point where, as Official Comment 5 to amended § 2-207 says, “This article takes no position on whether a court should follow the reasoning” in *Klocek* or *Hill*.<sup>630</sup> Official Comment 3 to the amendment observes, “If, for example, a buyer sends a purchase order, there is no oral or other agreement, and the seller delivers the goods . . . but . . . does not send the seller’s own acknowledgement or acceptance[,] the seller should normally be treated as having agreed to the terms of the purchase order.”<sup>631</sup> This is one point for those supporting the *Gateway* position, as the vendor there *did* send a form. Official Comment 4, however, notes “repeated use of a particular term or repeated failure to object to a term on another’s record is not normally sufficient in itself to establish a course of performance, a course of dealing or a trade usage.”<sup>632</sup> Although written with likely reference to merchant or

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626. *Hill v. Gateway 2000, Inc.*, 105 F.3d 1147, 1150 (7th Cir. 1997).

627. *Id.* at 1151.

628. WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 195; see Friedman, *supra* note 531, at 711; cf. *Hill*, 105 F.3d at 1150 (“*ProCD* . . . concluded that, when there is only one form, ‘sec. 2-207 is irrelevant.’”).

629. WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 195-96.

630. U.C.C. § 2-207 cmt. 5 (amended 2003), 1 U.L.A. 398 (2004).

631. *Id.*

632. *Id.*

commercial transactions in which each party sends its own conflicting form but proceeds to perform, this comment does suggest that the uncritical consumer may have an argument in opposition to “agreement” by use or retention without explicit agreement or knowledge.<sup>633</sup> So give half a point to those opposing the *Gateway* position.

Would the customer’s retention of the goods in *Hill*, payment having been made before delivery, show agreement to an arbitration term or warranty disclaimer under Official Comment 3 to amended § 2-207? That comment refers to “a variety of verbal and nonverbal behavior that may suggest agreement to another’s record.”<sup>634</sup> The behavior that results in agreement, and hence contract, must demonstrate some degree of “assent” to the proposed terms of agreement.<sup>635</sup> As the event of assent in *Hill* comes after payment and delivery, the quality of that “action” as assent is attenuated. In contrast to its predecessor, *ProCD*, in which the purchaser had in hand a box with notice of enclosed terms at the time of purchase, *Hill* involved terms first seen after payment and delivery, although that did not affect the outcome in *Hill*.<sup>636</sup> Texas, as in other common law jurisdictions, follows an objective standard in determining the existence of a contract. For example,

The determination of a meeting of the minds, and thus offer and acceptance, is based on the objective standard of what the parties said and did and not on their subjective state of mind. . . .

. . . .

. . . Where the fact finder determines that one party reasonably drew the inference of a promise from the other party’s conduct, that promise will be given effect in law.<sup>637</sup>

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633. The determination of “agreement” by a party is a factual undertaking. The UCC “contract” refers to the legal obligations that result from the parties’ agreement, i.e., “bargain of the parties in fact.” TEX. BUS. & COM. CODE ANN. § 1.201(3), (12) (Vernon 1994 & Supp. 2008).

634. U.C.C. § 2-207 cmt. 3 (amended 2003), 1 U.L.A. 398 (2004).

635. See Christina L. Kunz, et al., *Browse-Wrap Agreements: Validity of Implied Assent in Electronic Form Agreements*, 59 BUS. LAW. 279, 281 (2003) (“[A] user validly and reliably assents to the terms of a browse-wrap agreement if the following four elements are satisfied: (i) The user is provided with adequate notice of the existence of the proposed terms. (ii) The user has a meaningful opportunity to review the terms. (iii) The user is provided with adequate notice that taking a specified action manifests assent to the terms. (iv) The user takes the action specified in the latter notice.”); cf. Mark A. Lemley, *Terms of Use*, 91 MINN. L. REV. 459, 465 (2006) (“But in today’s electronic environment [writing as to clickwrap, shrinkwrap and browsewrap licenses] the requirement of assent has withered away to the point where a majority of courts now reject any requirement that a party take any action at all demonstrating agreement or even awareness of terms in order to be bound by those terms.”).

636. Compare *ProCD, Inc. v. Zeidenberg*, 908 F. Supp. 640, 645 (W.D. Wis. 1996) (“[T]he Select Phone™ box mentions the agreement in one place in small print. The box does not detail the specific terms of the license.”), *rev’d*, 86 F.3d 1447 (7th Cir. 1996), with *Hill v. Gateway 2000, Inc.*, 105 F.3d 1147, 1150 (7th Cir. 1997) (“[T]he box containing Gateway’s computer did not [have a notice of enclosed terms].”). The *Hill* court rejected that argument against the effectiveness of the enclosed terms. *Hill*, 105 F.3d at 1150.

637. *Copeland v. Alsobrook*, 3 S.W.3d 598, 604-05 (Tex. App.—San Antonio 1999, no pet.); see, e.g., Juliet M. Moringiello, *Signals, Assent and Internet Contracting*, 57 RUTGERS L. REV. 1307, 1311-1317 (2005).

Thus, the court in *Hill* could use the option provided by amended § 2-207(2), the terms to which both parties agree, to reach the same result as before: “The performance of keeping the good past the return period in a typical consumer rolling contract could thus well be construed as acceptance of all terms in a seller’s record, since the buyer is unlikely to have sent a record.”<sup>638</sup> The counterargument rests on the theory that there must be an end to contracting, and it comes at payment and shipment, before these “in the box” terms arrive, and the test of amended § 2-207 applies to “that” contract—unless a *Gateway* seller obtains some advance consent that keeps the contracting process open until delivery. At the time the contract terms are determined under amended § 2-207, there are no terms in any delivered record to be agreed by the consumer in a telephone transaction, absent change in the way terms of sale are presented by the seller in that type of transaction.<sup>639</sup> This argument comports with the premise of *Preston Farm, Enpro Systems*, and *Fieldtech* in Texas and is also consistent with the text of amended § 2-207.<sup>640</sup>

As Official Comment 5 states, amended § 2-207 takes no position on the rolling contract, so any prediction of result is speculative.<sup>641</sup> Amended § 2-207 makes it dangerous to gamble with contracts by removing the “between the merchants” tests of § 2-207(2) and applying the three-part test of amended § 2-207 to all contracts.<sup>642</sup> If a provision is important to a party, it should actually negotiate to agreement with the counterparty. Otherwise, the more general knock out rule will produce more contracts on default terms.<sup>643</sup>

### C. The Remedial Promise Changes

The 2003 Amendments and the 2007 Bill bring into the Code a concept already seen in a variety of cases—the “remedial promise.”<sup>644</sup> “‘Remedial promise’ means a promise by the seller to repair or replace goods or to refund all or part of the price of goods upon the happening of a specified event.”<sup>645</sup>

Corresponding changes to § 2-725 bring the remedial promise under express rules of the Code’s statute of limitations as to the commencement of actions for breach of a remedial promise.<sup>646</sup> The Texas Subcommittee’s views

638. Friedman, *supra* note 531, at 711.

639. WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 196-97.

640. *Enpro Systems, Ltd. v. Namasco Corp.*, 382 F. Supp. 2d 874, 882-83 (S.D. Tex. 2005); *Preston Farm & Ranch Supply, Inc. v. Bio-Zyme Enters.*, 625 S.W.2d 295, 296 (Tex. 1981); *Fieldtech Avionics & Instruments, Inc. v. Component Control.com*, 262 S.W.3d 813 (Tex. App.—Fort Worth 2008, no pet.).

641. U.C.C. § 2-207 cmt. 5 (amended 2003), 1 U.L.A. 398 (2004).

642. Compare U.C.C. § 2-207 (amended 2003), 1 U.L.A. 397 (2004), with U.C.C. § 2-207(b), 1A U.L.A. 208-09 (2004) (prior Article 2).

643. See Wladis, *supra* note 381, at 1029 (criticizing amended § 2.207 for making it harder for “reasonable additional terms” to enter). But see WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 199 (“We are fans of amended 2-207, for we think it does old 2-207’s work better than the old section . . .”).

644. U.C.C. § 2-103(1)(n) (amended 2003), 1 U.L.A. 373 (2004); see *infra* app. I, § 2.103(a)(14).

645. U.C.C. § 2-103(1)(n); see *infra* app. I, § 2.103(a)(14).

646. See U.C.C. § 2-725 (amended 2003), 1 U.L.A. 556-57 (2004); *infra* app. I, § 2.725.

on these two related amendments are contained in Appendix II.<sup>647</sup> With one exception, the Texas Subcommittee endorsed these 2003 Amendments on remedial promise.<sup>648</sup>

### 1. *The Remedial Promise Issue*

The following comments handily depict “remedial promise” issues and need for revisions in Article 2:

I buy a new car, and not only do I have the warranties for the quality of the car, but the seller also promises to repair or replace any defective parts . . . . If the seller were not to do the work or repairs as promised, would that be a breach of warranty? And if it were a breach of warranty, then would it be governed by Article 2 and therefore subject to the statute of limitations from the time of delivery. The problem is that there really is not a breach . . . until the work is not done. . . .

On the other hand, many courts have treated these promises as part of the initial sale and have locked the buyer into the statute of limitations based on the time of delivery. . . . Under the Magnuson-Moss Act, the federal law mandates language in consumer contracts that refer to [repair terms as] “warranties” for what are “remedial promises” under the revisions of Article 2.<sup>649</sup>

As these remarks indicate, the “remedial promise” changes implicate UCC warranty and remedy provisions, the statute of limitations, and federal law.<sup>650</sup>

An example of the types of provisions from a retail sales agreement that can cause problems is as follows:

The ‘**Basic Warranty**’ covers the cost of all parts and labor needed to repair any item on your vehicle (except as noted below) that’s defective in material, workmanship, or factory preparation. . . .

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647. See *infra* app. II, § 2.725.

648. The Texas Subcommittee disagreed with the position on “post-sale promises” expressed in proposed Official Comment 9 to the 2003 Amendments. Official Comment 9 to proposed § 2-103 states in part: “A post-sale promise to correct a problem . . . that the seller is not [already] obligated to correct to placate a dissatisfied customer is not within the definition of remedial promise.” U.C.C. § 2-103(1) cmt. 9 (amended 2003), 1 U.L.A. 376 (2004). The Texas Subcommittee’s view is that both a modification analysis under § 2.209 and an analogy to an express warranty undertaking indicate a remedial promise could arise post-sale. See *infra* app. II, § 2.301.

649. John Kraemer & Henry Gabriel, *Article 1 and Article 2A: Changes in the Uniform Commercial Code Regarding General Provisions of Sales and Leases*, 2 DEPAUL BUS. & COM. L.J. 691, 697 (2004) (comments by Gabriel). *Contra* Memorandum from Jeff Dodd to Stephanie Heller, *supra* note 98, at 3 (“Though the avowed purpose of this new concept was to address a problem in the statute of limitations, application of the concept in proposed Revised Article 2 has been expanded: a remedial promise is now a new, separate agreement, with its own statute of limitations, rather than a contractual remedy.”).

650. See Magnuson-Moss Warranty—Federal Trade Commission Improvement Act, 15 U.S.C. §§ 2301-2512 (2000) (setting federal requirements for consumer warranties and providing its own specific definitions that vary from UCC definitions of comparable terms).

The ‘**Basic Warranty**’ covers every Chrysler supplied part of your vehicle, **EXCEPT** its tires and cellular telephone.

. . . .

The ‘**Basic Warranty**’ lasts for 36 months from the vehicle’s Warranty Start Date **OR** for 36,000 miles . . . whichever occurs first.<sup>651</sup>

This “Basic Warranty” would, for purposes of the Magnuson-Moss Act, be a warranty under the definition of “written warranty” provided by that Act, which covers

(A) any written affirmation of fact or written promise made in connection with the sale of a consumer product by a supplier to a buyer which relates to the nature of the material or workmanship and affirms or promises that such material or workmanship is defect free or will meet a specified level of performance over a specified period of time, or

(B) any undertaking in writing in connection with the sale by a supplier of a consumer product to refund, repair, replace, or take other remedial action . . . which written affirmation, promise, or undertaking becomes part of the basis of the bargain between a supplier and a buyer for purposes other than resale.<sup>652</sup>

This definition of “warranty” for purposes of the Magnuson-Moss Act is broader than that of “warranty” under current § 2.313, which provides for the creation of an “express warranty” under the Texas Code:

Express warranties by the seller are created as follows:

(1) Any affirmation of fact or promise *made by the seller to the buyer* which *relates to the goods* and becomes part of the *basis of the bargain* creates an express warranty that the *goods* shall conform to the affirmation or promise.

(2) Any *description of the goods* which is *made part of the basis of the bargain* creates an express warranty that the goods shall conform to the description.

(3) Any sample or model *which is made part of the basis of the bargain* creates an express warranty that the whole of the goods shall conform to the sample or model.<sup>653</sup>

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651. Mydlach v. DaimlerChrysler Corp., 875 N.E.2d 1047, 1051 (Ill. 2007) (first and second omissions in original) (quoting the defendant’s warranty terms).

652. 15 U.S.C. § 2301(6). Note that the affirmation or undertaking is not limited to one from the “seller” under the federal Act but rather includes any such undertaking or affirmation “in connection with a sale by a supplier” without a requirement that it come from the immediate seller. *Id.* The “supplier” is defined as “any person engaged in the business of making a consumer product directly or indirectly available to consumers.” 15 U.S.C. § 2301(4).

653. TEX. BUS. & COM. CODE ANN. § 2.313(a) (Vernon 1994) (emphasis added). As the Magnuson-Moss Act precludes a disclaimer of an implied warranty if a (federal) warranty is given, persons subject to the

For UCC purposes, the problem is whether a “repair warranty” such as that quoted above is an “affirmation of fact or promise . . . which relates to the goods” or a “description of the goods” so as to constitute a warranty at all under the Code.<sup>654</sup> The Magnuson-Moss Act removes that question for federal consumer warranty purposes because the “Basic Warranty” is within clause (B) above as an “undertaking in writing . . . to refund, repair, replace, or take other remedial action.”<sup>655</sup> But for both federal Magnuson-Moss Act and state UCC purposes, “a written warranty” or “express warranty” must be part of the “basis of the bargain.”<sup>656</sup>

## 2. *The Remedial Promise and Limitations*

Section 2.725 is the Texas Business & Commerce Code’s statute of limitations for Chapter 2.<sup>657</sup> For *warranties*, § 2.725(b) sets up a bright line for the accrual of warranty causes of action for purposes of limitations, as to both implied and express warranties, with separate treatment of explicit future performance warranties:

[(1)] A cause of action accrues when the breach occurs, regardless of the aggrieved party’s lack of knowledge of the breach.<sup>658</sup> [(2)] A breach of warranty occurs when tender of delivery is made, except that where a warranty explicitly extends to future performance of the goods and discovery of the breach must await the time of such performance the cause of action accrues when the breach is or should have been discovered.<sup>659</sup>

The basic period of limitations is four years under the 2007 Bill, but it may be reduced in the original agreement (except for consumer contracts) to not less than one year.<sup>660</sup> The limitation period applies to any breach of a contract

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federal rules seldom attempt to disclaim state implied warranties, although the “duration” of an implied warranty may be limited to “the duration of a written warranty of reasonable duration” if properly disclosed and conscionable. *See* 15 U.S.C. § 2308. “Duration” of an implied UCC warranty presents its own conceptual issues. *See, e.g.,* Safeway Stores, Inc. v. Certainteed Corp. 710 S.W.2d 544, 546 (Tex. 1986) (“Implied warranties relate to the condition, kind, characteristics, suitability, etc. of sold goods at the time of sale . . . . Therefore, only *express* warranties may explicitly extend to future performance.”). Note that both the federal warranty definition, 15 U.S.C. § 2301(6), and the terms of § 2.313(a) on express warranty include a “basis of the bargain” element.

654. Curtis R. Reitz, *Manufacturers’ Warranties of Consumer Goods*, 75 WASH. U. L.Q. 357, 363-70 (1997).

655. *See* 15 U.S.C. § 2301(6).

656. *See infra* app. I, § 2.312A; *see also* U.C.C. § 2-313A (amended 2003), 1 U.L.A. 430 (2004). The “obligation” under that provision is not a UCC warranty so as to avoid the “basis of the bargain” question.

657. TEX. BUS. & COM. CODE ANN. § 2.725 (Vernon 1994).

658. *Id.* § 2.725(b) (footnote added). This rule is retained and modified in amended § 2.725(b)(1). *See infra* app. I, § 2.725(b)(1).

659. TEX. BUS. & COM. CODE ANN. § 2.725(b). Proposed § 2.725(b)-(c) uses these principles, with modifications, in its revision of UCC limitations. *See infra* app. I, § 2.725.

660. *See infra* app. I, § 2.725.

for the sale of goods.<sup>661</sup> The Magnuson-Moss Act borrows this limitation period for claims under that Act, as it does not prescribe its own limitations period.<sup>662</sup> Thus, it is important, for example, to know if a “repair warranty” that extends for three years is a “warranty of future performance,” so that limitations may extend up to seven years, rather than four years.<sup>663</sup>

### 3. Some “Remedial Promise” Cases

A few consumer cases illustrate the issues and judicial responses in the remedial promise-warranty area. *Mydlach v. DaimlerChrysler Corp.* arose under the Magnuson-Moss Act when, according to the plaintiff, the dealer was unable to repair problems covered by the “Basic Warranty” quoted above.<sup>664</sup> The plaintiff’s claims included breach of express warranties under the federal Act.<sup>665</sup> The defendant succeeded in obtaining a summary judgment on limitations at the trial court: the vehicle was delivered to the original owner in 1996; the plaintiff’s suit was filed in 2001; the basic UCC four-year limitation period on breach of sales warranties began to run with that delivery of the vehicle to the initial owner some five years earlier.<sup>666</sup>

The plaintiff sued under § 2310 of the Act: “[A] consumer who is damaged by the failure of a supplier, warrantor, or service contractor to comply with an obligation . . . under a written warranty . . . may bring suit for damages and other legal and equitable relief . . . .”<sup>667</sup> The parties agreed that the “Basic Warranty” was a Magnuson-Moss “written warranty.”<sup>668</sup> The issues in *Mydlach* were as follows: (1) is the Basic Warranty a UCC express warranty (an affirmation or promise which relates to the goods) so as to cause the UCC limitations rules to apply, and (2) if it is an express warranty, does it explicitly extend to future performance (so as to lengthen the limitations period)?<sup>669</sup>

The Illinois court started with the definitional proposition that an express UCC warranty, by definition, relates “to the quality or description of the goods” and “obligates the seller to deliver goods that conform” to the warranty.<sup>670</sup>

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661. *Infra* app. I, § 2.725(a)-(b).

662. *Mydlach v. DaimlerChrysler Corp.*, 875 N.E.2d 1047, 1055 (Ill. 2007) (“Where a federal statute fails to specify a limitations period for suits under it, ‘courts apply the most closely analogous statute of limitations under state law.’” (quoting *Del Costello v. Int’l Bhd. of Teamsters*, 462 U.S. 151, 158 (1983))).

663. TEX. BUS. & COM. CODE ANN. § 2.725 (Vernon 1994).

664. *Mydlach*, 875 N.E.2d at 1051.

665. *See id.* at 1051-52.

666. *Id.* at 1052. The intermediate appellate court had reversed the limitations decision, and the defendant appealed to the Illinois Supreme Court. *Id.*

667. *See* 15 U.S.C. § 2310(d) (2000).

668. *See Mydlach*, 875 N.E.2d at 1051-52.

669. *See* TEX. BUS. & COM. CODE ANN. §§ 2.313(a), 2.725(b) (Vernon 1994). The plaintiff did not assert implied warranty claims on appeal. *Mydlach*, 875 N.W.2d at 1053.

670. *Mydlach*, 875 N.E.2d at 1058. As one commentator observes, “All [Article 2 warranties] go to the quality of the goods at tender. None goes to the remedies, which come about only if a warranty is breached.” Larry T. Garvin, *Uncertainty and Error in the Law of Sales: The Article Two Statute of Limitations*, 83 B.U. L. REV. 345, 379 (2003).

When it tested the Basic Warranty against that standard of “warranty-ness,” the court made the fundamental decision that the Basic Warranty was not an affirmation or promise that the vehicle would *conform* to a standard, but rather was an undertaking to repair, replace, or refund that the federal Act simply classified as a warranty for its purposes.<sup>671</sup> As the warranty was not a UCC express warranty, the court held the “accrual on delivery” rule and four-year warranty limitation period, predicated on breach occurring at the time of delivery, did not apply.<sup>672</sup> From there, the Illinois court “borrowed” for Magnuson-Moss claims the general limitations provisions of § 2-725(2) and concluded that a cause of action for breach of a *contractual duty* (to repair a product) accrues only when performance is due but not provided.<sup>673</sup> The Illinois Supreme Court affirmed reversal of summary judgment for the defendant on limitations and allowed the plaintiff to go forward with her federal “warranty” claim.<sup>674</sup>

In contrast to *Mydlach* and its application of a “breach on non-performance” rule to a Magnuson-Moss Act “warranty” claim, *Muss v. Mercedes-Benz of North America, Inc.*, decided almost twenty years earlier, held a similar “repair warranty” to have been breached on delivery, resulting in a UCC warranty claim being barred by limitations.<sup>675</sup> The 1977 warranty for the automobile in *Muss* provided: “Any authorized Mercedes-Benz dealer [will] perform warranty repairs made necessary because of defects in material or workmanship.”<sup>676</sup>

The plaintiff sued for breach of express warranty and for deceptive trade practice claims, and the manufacturer asserted, among other defenses, the four-year limitations defense under § 2.725 based on date of delivery. The dispute in *Muss* was “whether this is such a warranty as ‘explicitly extends to future performance of the goods’ within the exception appearing in §2.725(b).”<sup>677</sup> Within this warranty framework, the court of appeals easily concluded that there was no “future performance” aspect to the “warranty” as the very terms of the document anticipated there would be problems: “[T]he bare-bones language presages the likelihood that the goods *will fail to perform* and specifies a particular remedy in that eventuality.”<sup>678</sup> Even though the *Muss* court

671. *Mydlach*, 875 N.E.2d at 1058. The defendant confirmed that view: “[The] limited warranty was not a promise that the vehicle would be defect free . . .” *Id.* (quoting the defendant’s brief).

672. *See id.* at 1059.

673. *See id.* The court illustrated the logic of its approach by hypothesizing a five-year repair warranty that would have expired before the last performance is due if the “breach on delivery” principle applied. *See id.*

674. *See id.* at 1061.

675. *Muss v. Mercedes-Benz of N. Am., Inc.*, 734 S.W.2d 155 (Tex. App.—Dallas 1987, writ ref’d n.r.e.). The trial court judge in *Muss* is now a justice on the Texas Supreme Court—Justice Nathan Hecht. *See id.*

676. *Id.* at 157-58.

677. *Id.* at 158. The time of delivery in *Muss* was more than four years before suit was filed, but the repairs, ultimately unsuccessful in the plaintiff’s eyes, continued until within four years of suit. *Id.*

678. *Id.* The *Muss* decision mixes the conceptual apples of warranty with the conceptual oranges of remedy. *Cf. Garvin, supra* note 670, at 377-81 (discussing the split in courts’ decisions). At one point, *Muss*

differentiated, in its analysis of the future performance warranty issue, between a warranty and an agreement for specified remedy under § 2.719, it never moved beyond the “warranty” limitation issues to the more general “breach of contract” issues, for which the UCC times accrual from “when the breach occurs,” rather than the warranty-specific rule that breach occurs on delivery. *Muss* held that a “warranty” for repair is breached on the delivery of the vehicle, as the warranty does not explicitly extend to future performance of the goods.<sup>679</sup>

*Woolums v. National RV* presents yet another aspect of the remedial promise issues seen in *Muss*.<sup>680</sup> The one-year limited warranty in *Woolums* covered “the cost of parts and labor needed to correct Covered Defects related to materials or workmanship” but, as in *Muss*, made no representation that the materials or workmanship would conform to any standard nor guaranteed them to be free from defects for the period.<sup>681</sup> *Woolums* asserted separate UCC express warranty and Magnuson-Moss Act “written warranty” claims.<sup>682</sup> The defendant moved for summary judgment, apparently on the ground that the plaintiff could not recover under the UCC on a warranty theory for at least some of the claims based on the scope of coverage of the repair warranty.<sup>683</sup>

*Woolums* classified the repair warranty as an express warranty for purposes of the UCC under Pennsylvania law.<sup>684</sup> In support, the court noted that the text of § 2-313 applies to “[a]ny affirmation of fact or promise” that relates to the goods, an indication that the statutory language should be broadly construed, and that National described its undertaking as a “warranty” so that it would be unfair (as seen by that court) for National to change the warranty into “merely a remedial promise of repair.”<sup>685</sup> Thus, a court following *Muss* would treat a repair or replace warranty as a “point in time” warranty, while a court following *Woolums* would treat that same warranty as a “future performance” warranty; and finally, a court following *Mydlach* would treat the same warranty as a non-warranty obligation breached by (and at the time of) non-performance.

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states that it holds “*Muss*’ cause of action for breach of written warranty accrued when the car was delivered.” *Muss*, 734 S.W.2d at 158. Later, the court says, “[Mercedes-Benz’s] limited warranty qualifies as an exclusive remedy of repair under § 2.719 . . .” *Id.* at 160.

679. *Muss*, 734 S.W.2d at 160. As the point of error in *Muss* “[claimed] benefit of the ‘discovery rule’ under the exception appearing in § 2.725(b)” of the Texas Business & Commerce Code, the court of appeals (and counsel) would have been reaching to shift to a different theory (which later succeeded in *Mydlach*), that the repair warranty was not a warranty at all but a contractual obligation breached when not performed. *Id.* at 157; see TEX. R. APP. P. 38.1(e). However, illustrating the problems with finding a consistent theory among these types of claims, as the manufacturer of a motor vehicle seldom contracts directly with the retail purchaser, lack of privity often limits the availability of contractual remedies to a plaintiff, absent a statutory override such as the Magnuson-Moss Act or favorable case law on privity issues. At a minimum, these problems indicate the virtues in the explicit treatment of remedial promise issues proposed in the 2007 Bill.

680. See *Woolums v. Nat’l RV*, 530 F. Supp. 2d 691, 693 (M.D. Pa. 2008).

681. *Id.* at 693.

682. See *id.*

683. See *id.*

684. See *id.* at 698.

685. See *id.* at 696-98. The limitations issues did not arise in *Woolums*. See *id.* at 696.

*Woolums* and *Mydlach* would defer the time a claim accrued; *Muss* treats the breach as occurring and claim accruing on delivery.<sup>686</sup>

#### 4. Case Law on Limitations for Remedial Promises

As the above review of cases indicates, when courts construe the “future performance” elements of warranties, they do not reach consistent results on whether contract provisions that contain similar language do or do not extend to future performances so as to extend the point at which limitations begin to run.<sup>687</sup> The courts’ inconsistency is a result of their disagreement on how to identify a warranty that explicitly extends to future performance.<sup>688</sup> Most courts construe the future performance exception narrowly.<sup>689</sup> Thus, courts usually hold that unless the warranty clearly manifests an intent to extend to future performance, the statute of limitations begins to run (breach occurs) upon delivery of goods.<sup>690</sup>

Courts generally agree that a warranty solely providing that the goods will not be defective on tender does not explicitly extend to future performance.<sup>691</sup> On the other hand, a warranty that provides that a good will not be defective for a stated period does explicitly extend to future performance.<sup>692</sup> But when a warranty provides (perhaps indirectly) that the goods will not be defective *and* the seller will replace or repair the good if defects exist—in other words, if there is a remedial promise—the courts are split on how to treat the accrual of the limitations period for a breach of that combined promise.<sup>693</sup> Because of this

686. *Muss*, therefore, also had to resolve a claim that the “vanishing claim” construction violated Article 1, § 13 of the Texas Constitution. *Muss v. Mercedes-Benz of N. Am., Inc.*, 734 S.W.2d 155, 159 (Tex. App.—Dallas 1987, writ ref’d n.r.e.). The court of appeals held that § 2.725 is constitutional under its analysis of the open courts clause. *Id.*

687. *See Joswick v. Chesapeake Mobile Homes, Inc.*, 765 A.2d 90, 94 (Md. 2001) (“There have been dozens—perhaps hundreds—of cases throughout the country construing § 2-725(2) with respect to whether a warranty . . . constitutes a warranty explicitly extending to future performance . . . . [A] number of the cases do go in different directions and cannot easily be reconciled.”).

688. *See id.*

689. *See Controlled Envtl. Constr. v. Key Indus. Refrigeration Co.*, 670 N.W.2d 771, 779 (Neb. 2003) (stating that when determining whether a warranty explicitly extends to future performance, “courts reason that [the exception] should be interpreted quite narrowly”).

690. *See, e.g., id.* at 779-80 (holding four-year statute of limitations on implied warranty claims against supplier and manufacturer began to run on date of delivery); *Heller v. U.S. Suzuki Motor Corp.*, 477 N.E.2d 434 (N.Y. 1984) (holding cause of action for breach of implied warranty accrues on date of delivery); *Safeway Stores, Inc. v. Certainteed Corp.*, 710 S.W.2d 544 (Tex. 1986) (statute of limitations runs from date of sale).

691. *See, e.g., Controlled Envtl. Constr.*, 670 N.W.2d at 778-79 (stating that a warranty that did not guarantee a good for any specific number of years was not a warranty that explicitly extends to future performance).

692. *See, e.g., id.* at 780 (“A warranty that goods will have a certain quality or be free from defects for a stated time thus . . . explicitly extends to future performance . . . .” (quoting *Joswick*, 765 A.2d at 96-97)). The important Texas case of *PPG Industries, Inc. v. JMB/Houston Centers Partners Ltd.* dealt in part with this type of provision but focused on the differences between a warranty of goods and a warranty of repair. *See PPG Indus., Inc. v. JMB/Houston Ctr. Partners Ltd.*, 146 S.W.3d 79, 92-93, 96 (Tex. 2004).

693. *See, e.g., Joswick*, 765 A.2d at 94 (“[I]t seem[s] clear . . . that a [remedial promise] . . . does not serve either to convert a separate warranty that does not otherwise explicitly extend to future performance into

confusion, courts apply different rules on commencement of the limitations period to contracts that contain similar remedial promise language.<sup>694</sup> There are three options for when the limitations period should begin to accrue for a breach of a remedial promise.<sup>695</sup> The limitations period for a remedial promise could begin to run upon any of the following events: (1) the delivery of the goods, (2) the buyer's discovery of a breach of warranty, or (3) the seller's failure to perform under the promise.<sup>696</sup>

One analysis of the split in the cases regarding how to treat "warranties" in the middle area (where a "repair and replace" clause is used) identifies three analytical frameworks that the courts apply to those problems. The likely plurality of decisions considered in that analysis treats the repair or replacement warranty as a warranty or other contractual undertaking under Article 2 but not as a future performance warranty, with breach from the time the goods are tendered to the buyer.<sup>697</sup> The second approach concludes the repair and replace warranty is a warranty explicitly extending to future performance, with breach occurring at the time of discovery, again mixing remedy and warranty concepts.<sup>698</sup> And finally, other courts consider the repair and replace warranty to be a remedial provision that is a part of an Article 2 contract and governed by its limitations rules, even though not a warranty.<sup>699</sup>

### 5. *The Remedial Promise Accrual Rule of § 2-725*

The rule set out by amended § 2-725 adopts the position that the limitations period for a breach of a remedial promise begins upon failure to repair or replace the defective good.<sup>700</sup> Sections 2.102(2)(n) and 2.313(3)(d) of

one that does so or, conversely, convert a warranty that *does* extend to future performance into one that does not do so.").

694. See Gavin, *supra* note 670, at 380.

695. See *id.*

696. See, e.g., *R.W. Murray Co. v. Shatterproof Glass Corp.*, 697 F.2d 818 (8th Cir. 1983) (accrual begins on delivery); *Mydlach v. DaimlerChrysler Corp.*, 875 N.E.2d 1047, 1061 (Ill. 2007) (seller's failure to perform); *PPG Indus., Inc.*, 146 S.W.3d 79 (buyer's discovery); *Flagg Energy Dev. Corp. v. Gen. Motors Corp.*, 709 A.2d 1075, 1086 (Conn. 1998) ("[The] repair or replacement clause contains no terms that, as a matter of law, would constitute an explicit warranty of future performance as § [2-725] requires."); *Nowalski v. Ford Motor Co.*, 781 N.E.2d 578 (Ill. App. Ct. 2002) (delivery); *Poli v. DaimlerChrysler Corp.*, 793 A.2d 104, 110 (N.J. Super. Ct. App. Div. 2002) (seller's failure to perform).

697. See Garvin, *supra* note 670, at 377-78. As Article 2 has different provisions on warranty disclaimers and remedy limitations, it implies a need to distinguish between them. *Id.* at 378 n.149.

698. *Id.* at 379-80.

699. *Id.* at 380-81. Somewhat at odds with the summary in Garvin, the Texas Supreme Court in *PPG Industries* commented, "A warranty to make repairs is a warranty for services, not of goods, and thus falls outside the UCC." *PPG Indus. Inc.*, 146 S.W.3d at 96; see Garvin, *supra* note 670, at 380-81. This comment is perhaps dicta, as the court then observes that the plaintiff there "asserted no claim for breach of a repair warranty," as the last thing the plaintiff wanted was more of the [defective] windows through replacement. *PPG Indus. Inc.*, 146 S.W.3d at 96. That comment appears to be based on the goods-services analysis as to whether a transaction is, or is not, a Chapter 2 transaction under the "predominant purpose" test; use of that analysis in a dispute over warranty-remedy issues in what is clearly a "sale of windows" seems confusing.

700. See U.C.C. § 2-725(2)(c) (amended 2003), 1 U.L.A. 556 (2004).

the 2007 Bill distinguish between a warranty and a remedial promise on that point. Proposed § 2.313(3)(d) would provide as follows: “Any remedial promise made by the seller to the immediate buyer creates an *obligation* that the promise will be performed upon the happening of the specific event.”<sup>701</sup> This statement makes it clear that a remedial promise does not create a warranty; instead, under the new provision, a remedial promise creates an obligation of the seller to act as promised.

Then, proposed § 2.725(b)(3) provides that the right of action for a breach of a remedial promise accrues “when the remedial promise is not performed when performance is due.”<sup>702</sup> This new provision adopts the accrual rule of jurisdictions finding that the statute of limitations for a breach of a remedial promise begins to run upon the seller’s failure to repair or replace defective goods.<sup>703</sup> The result is that a buyer’s limitations period for a breach of a remedial promise begins to run and the right of action accrues, except as may be affected by a discovery rule, when the seller does not perform as promised.<sup>704</sup>

#### D. *The Remote Purchaser Warranty and Remedial Promise*

##### 1. *The Privity Element in Express Warranties*

Early in the work on revising Article 2, the problem of “remote seller warranties” surfaced. Express warranties arise as provided by current § 2.313, quoted above.<sup>705</sup> Proposed § 2.313(4) would now establish an “obligation” under a remedial promise.<sup>706</sup> As current § 2.313 identifies the topic of its provisions as “[e]xpress warranties *by the seller*,” how do warranties (or remedial promises) of manufacturers not selling directly to the user fit into the current and amended section?<sup>707</sup>

The present section 2-313 does not directly address the issue of warranties made by remote sellers, and Comment 2 shows that the drafters finessed the issue. Thus, despite the fact that many such warranties are

701. See *infra* app. I, § 2.313(3)(d) (emphasis added).

702. See *infra* app. I, § 2.725(b)(3).

703. See *Poli v. DaimlerChrysler Corp.*, 793 A.2d 104, 110 (N.J. Super. Ct. App. Div. 2002) (stating that the amended § 2-725 takes the position that “a promise by a seller to repair or replace a defective part under a specified warranty period ‘is not a warranty at all and therefore is not subject to either the time of tender [rule of 725(1)] or [the] discovery rule [of 725(2)]’” (alteration in original)).

704. See *id.*

705. See TEX. BUS. & COM. CODE ANN. § 2.313 (Vernon 1994); see *infra* text accompanying note 653 (quoting § 2.313).

706. See *infra* app. I, § 2.313(d). In contrast to the elements for creation of an express warranty, a remedial promise need not be “made part of the basis of the bargain” to create obligations. See *infra* app. I, § 2.313(d).

707. TEX. BUS. & COM. CODE ANN. § 2.313; see also U.C.C. § 2-313 (amended 2003), 1 U.L.A. 426-27 (2004) (emphasis added).

regularly enforced by the courts, the language of the [statutory] provision does not really fit the situation.<sup>708</sup>

The re-evaluation of the express warranty provisions took several turns during the work of the original (and reconstituted) Article 2 Drafting Committee, including a series of changes relating to how a warranty from a person not a party to the immediate transaction could arise under a statutory provision (§ 2.313) that included a “basis of the bargain” element for the creation and enforcement of an express warranty.<sup>709</sup>

As Comment 2 to amended § 2-313 observes, there are cases that deal with enforcement of a remote vendor warranty.<sup>710</sup> *United States Pipe & Foundry Co. v. City of Waco* is an early example.<sup>711</sup> In the course of the city’s preparation of the specifications for construction of a water line, “the manufacturer, in order to secure to itself the benefits of a large sale of its pipe, induced the city by representations as to its fitness and quality, to specify same.”<sup>712</sup> The city, when the line failed, sued the manufacturer, contractor, and engineer on several theories, including an express warranty claim against the manufacturer, which had not contracted directly with the city.<sup>713</sup> The Texas Supreme Court identified “the tendency of modern courts [to move] away from the narrow legalistic view of the necessity of formal immediate privity of contract in order to sue for breach of an express or implied warranty.”<sup>714</sup> The court held the manufacturer could be liable on an express warranty theory, having “voluntarily made itself a party to the transaction” and received “a sufficient consideration” for a warranty.<sup>715</sup>

Case law and business practices have evolved over the years, but the principle is still recognized. “Of course, if manufacturers make representations or warranties directly to consumers, the latter may sue directly (despite the absence of privity) for breach of express warranty . . . .”<sup>716</sup> The practical

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708. ABA Task Force, *Appraisal*, *supra* note 57, at 1103; *see* U.C.C. § 2-313 cmt. 2 (amended 2003), 1 U.L.A. 427 (2004) (“Although this section is limited in its scope and direct purpose to warranties made by the seller to the buyer . . . [the provisions] . . . are not designed in any way to disturb those lines of case law . . . [that recognize] warranties need not be confined . . . to the direct parties . . .”).

709. U.C.C. § 2-313 (amended 2003), 1 U.L.A. 426 (2004); *see also* WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 93-97; Reitz, *supra* note 654, at 360-63; James J. White, *Revised Article 1 and the Warranty Provisions of Amended Article 2*, 3 DEPAUL BUS. & COM. L.J. 519, 529-31 (2005).

710. *See* U.C.C. § 2-313 cmt. 2.

711. *U.S. Pipe & Foundry Co. v. City of Waco*, 108 S.W.2d 432 (Tex. 1937).

712. *Id.* at 434.

713. *Id.* at 433.

714. *Id.* at 435.

715. *Id.*; *see* Millard H. Ruud, *Manufacturers’ Liability for Representations Made by Their Sales Engineers to Subpurchasers*, 8 UCLA L. REV. 251, 258-61 (1961).

716. *PPG Indus. Inc. v. JMB/Houston Ctrs. Partners Ltd.*, 146 S.W.3d 79, 90 (Tex. 2004) (citing *U.S. Pipe & Foundry*, 108 S.W.2d at 434-45). But also note the discussion by the court in *PPG* of reliance issues in warranty: “While ‘particular’ reliance may not be necessary, we have held several times that something rather like it is.” *Id.* at 99; *see also* TEX. BUS. & COM. CODE ANN. § 2.318 (Vernon 1994) (leaving scope of implied and express warranty beneficiaries for judicial determination); *Henry Schein, Inc. v. Stromboe*, 102

reasons for enforcing (and for a manufacturer to honor) the express warranty to remote purchasers are clear:

[W]here Dell deals directly with the consumer and there's stuff in the box, this is a 2-313 case because the immediate [seller] and the end user/buyer have a contract.

In the second case, there is a contract between Dell and Sears and another contract between Sears and the consumer, but no contract between [the] consumer and Dell. Of course, Dell puts contract-like documents in the box . . . but there is no contract. The question then is well, what do those terms do? . . . [W]hen the CEO gets up on the witness stand, is she going to say, "Oh, yeah. These terms we put in the box . . . we're not bound by that"? No, they're not going to say that . . .<sup>717</sup>

## 2. *The Warranty or Remedial Promise to Remote Purchasers Under § 2-313A*

The 2003 Amendments provide an answer to the privity and basis of the bargain questions that current § 2.313 analysis commonly encounters in both commercial and consumer transaction patterns.<sup>718</sup> The essential points of this new § 2.313A are as follows:<sup>719</sup>

- (1) The terms "immediate buyer" and "remote purchaser" are defined in § 2.313A(1)(a) and (b).<sup>720</sup>
- (2) Section 2.313A "applies only to new goods and goods sold or leased as new goods in a transaction of purchase in the normal chain of distribution."<sup>721</sup>
- (3) If, in a record that is provided with the new goods, a seller (even if not an immediate seller) makes an affirmation, promise, or description that would be an express warranty under § 2.313 in a direct sale, or the seller makes a remedial promise, then the seller *has an obligation* to ensure that the goods will conform or the remedial promise will be performed. Goods must conform unless "a reasonable person in the position of the remote purchaser would not believe that the affirmation of fact, promise, or description created an obligation."<sup>722</sup>

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S.W.3d 675, 686 (Tex. 2002) (noting that reliance is an element of "plaintiffs' claims of breach of express warranty (to a certain extent)").

717. White, *supra* note 709, at 531.

718. See TEX. BUS. & COM. CODE ANN. (Vernon 1994); U.C.C. § 2-313 (amended 2003), 1 U.L.A. 426 (2004).

719. For the full text of proposed § 2.313A, see *infra* app. I, § 2.313A.

720. See *infra* app. I, § 2.313A. The definition of immediate buyer is also used in amended § 2.313, for warranties and remedial promises made directly by the seller. See *infra* app. I, § 2.313A(1).

721. See *infra* app. I, § 2.313A(b).

722. See *infra* app. I, § 2.313A(c)(1).

- (4) The seller may, no later than the time of purchase under § 2.313A, also “modify or limit the remedies available to the remote purchaser.”<sup>723</sup> Unless the seller modifies or limits the remedy, the seller may be liable for incidental or consequential damages but not lost profits.<sup>724</sup>
- (5) An obligation other than a remedial promise (i.e., a warranty-like obligation) is breached if the goods fail to conform “when the goods left the seller’s control.”<sup>725</sup> The Texas Subcommittee also included a non-standard subsection 2.313A(g) in the 2007 Bill to tie these statutory obligations and benefits to the Texas version of § 2.318. That non-standard subsection (g) reiterates the Texas option in § 2.318 that the range of persons who may maintain actions for breach of warranty or remedial promise is left to the courts except to the extent the UCC has provided a rule in the operative sections.<sup>726</sup>

### 3. Some Aspects of § 2.313A of the 2007 Bill

First, the interplay of amended §§ 2.313 and 2.313A deserves comment. The customer who buys *directly* from Dell or Gateway must look to § 2.313 for the rules about express warranties and remedial promises.<sup>727</sup> As to express warranties, § 2.313 retains the “basis of the bargain” as an element of the express warranty but not for a remedial promise.<sup>728</sup> “The meaning of ‘the basis of the bargain’ standard is somewhat amorphous and has caused difficulty to both courts and commentators.”<sup>729</sup> The courts may focus on reliance or “something rather like it” as an element a direct buyer must prove for an express warranty claim.<sup>730</sup> In an ironic turn, a remote purchaser does not have a basis of the bargain component for its express warranty claim under § 2.313A.<sup>731</sup> The substitute standard, which assumes reliance by a recipient, is directed at the delivery process and looks at whether “the seller reasonably expects the record to be, and the record is, furnished to the remote purchaser.”<sup>732</sup> If the remote purchaser receives the warranty or remedial promise document as described, the customer has the basis for a claim even if,

723. See *infra* app. I, § 2.313A(e)(1).

724. See *infra* app. I, § 2.313A(e)(2). The clear expectation seems to be that a seller will always take this option. Note that the requirements for warranty disclaimers of proposed § 2.316 would apply here, and the disclaimers would be in a record, so conspicuousness is applicable. See *infra* app. I, § 2.316.

725. See *infra* app. I, § 2.313A(f).

726. See *infra* app. I, § 2.313A(g).

727. See *infra* app. I, §§ 2.313A(g), 2.318.

728. See U.C.C. § 2-313(2)(a)-(c) (amended 2003), 1 U.L.A. 426 (2004); *infra* app. I, § 2.313(b)(1)-(3).

729. ANDERSON, BARTLETT & EAST, *supra* note 299, at 143.

730. PPG Indus., Inc. v. JMB/Houston Ctrs. Partners Ltd., 146 S.W.3d 79, 99 (Tex. 2004).

731. See U.C.C. § 2-313A(3) (amended 2003), 1 U.L.A. 430 (2004); *infra* app. I, § 2.313A(c).

732. *Id.*

for example, the customer first saw it in a document with an arbitration form being challenged on § 2.207 grounds.<sup>733</sup>

Second, the “warranty” to the remote purchaser and the remedial promise (both to remote and immediate purchasers) are “obligations.”<sup>734</sup> This careful use of “obligation” removes any inference that the “basis of the bargain” is a component of a remote purchaser’s express warranty.<sup>735</sup> This “obligation” usage is then reflected in amended § 2.725, which treats breach of remedial promise as a breach of contract claim and treats an “obligation” under § 2.313A separately from a § 2.313 warranty.<sup>736</sup>

Third, potential issues arise from the targeted “consequential damages” exclusion of § 2.313A(e)(2). That subsection excludes, whether remedies are otherwise limited or not, seller liability for lost profits for breach of a § 2.313A obligation (a warranty-equivalent or a remedial promise).<sup>737</sup> Although the normal setting for an obligation to a remote purchaser is the consumer, mass-market transaction, those remote obligations may also arise in a commercial setting where consequential damages may be quite significant, particularly in relation to the price for the component.<sup>738</sup> Because proposed § 2.313A is a new effort to bring structure to an area of uncertainty, this exclusion may reflect a balance of concerns:

It can be argued that section 2-313A balances the imposition of liability on sellers against the [exclusion of the] unlimited scope of the loss of profits of the remote purchaser. In other words, a remote seller cannot predict the scope of usage of the product he sells or its benefit to the remote purchaser. Therefore, the drafters tried to balance [the seller’s risks] through not allowing the remote purchaser to recover the lost profits . . . .<sup>739</sup>

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733. See *infra* app. I, §§ 2.207, 2.313A. The realities of current mass market practices cut both ways on the enforcement of “in the box” terms; as Professor White observed, a manufacturing executive is not likely to disavow what is included with a product. See White, *supra* note 709, at 530-31. At the same time, the consumer who invokes a warranty “is not well positioned to say” that the related arbitration clause is not effective. *Hill v. Gateway 2000*, 105 F.3d 1147, 1149 (7th Cir. 1997).

734. See *infra* app. I, §§ 2.313(d), 2.313A(c) (showing how the seller has or creates obligations).

735. See U.C.C. §§ 2-313(4), 2-313A cmt. 1 (amended 2003), 1 U.L.A. 427, 434-35 (2004); see also *infra* app. I, §§ 2.313, 2.313A. Both for immediate buyers and remote purchasers, a remedial promise claim does not require proof of some type of reliance. Cf. *supra* note 716 and accompanying text (discussing *PPG Indus. Inc.*, 146 S.W.3d at 90); *Henry Schein, Inc. v. Stromboe*, 102 S.W.3d 675, 686 (Tex. 2002)). As *Henry Schein, Inc.* would suggest, the changes on that proof element may affect class action certification cases if the 2007 Bill were enacted. The statute, thus, would put into place the practical analysis of Professor White, quoted above, on business practices and legal theory. See text accompanying *supra* note 717.

736. See *infra* app. I, § 2.725.

737. See *infra* app. I, § 2.313A(e)(2).

738. See TEX. BUS. & COM. CODE ANN. § 2.715 (Vernon 1994); ANDERSON, BARTLETT & EAST, *supra* note 299, at 331 (“The courts have historically had great difficulty with the provocative case where a plaintiff seeks recovery for a great magnitude of consequential loss [where] the defendant received a comparatively miniscule consideration.”).

739. Nazmi Orkun Akseli, *Advertising and “Pass-Through” Warranties Under Revised Article 2*, 106 COM. L.J. 65, 77 (2001).

Fourth, the context of § 2-313A is the same “terms in the box” situation that was so controversial in the drafting of § 2-207.<sup>740</sup> How do the two work together? According to Professor White, who was on the Drafting Committee, “[t]he poverty of our imagination is shown by the fact that no one on the Drafting Committee appears ever to have noticed that [a proposed subsection on the terms in the box] to Section 2-207 and Section 2-313A . . . addressed the same question.”<sup>741</sup> The only interconnection appears to be by a cross-reference. Because Comment 5 to § 2-207 makes clear that § 2-207 “omits any specific treatment of terms . . . in or on the container,” it must leave at least that subset of a seller’s “affirmation of fact or promise that relates to the goods, provides a description that relates to the goods, or makes a remedial promise” to amended § 2-313A.<sup>742</sup> That, of course, is a large part of the universe of what buyers and sellers care about, save perhaps mandatory arbitration and the difficulties over goods-information and sale-license. It does appear clear that for the subset of terms and remedies that are under § 2-313A, there will be no “rolling contract” argument under § 2-207.

#### 4. Approval of § 2-313A and Removal of § 2-313B

The 2003 Amendments proposed a paired set of new “remote purchaser” warranty and remedial promise provisions—§ 2-313A, in which the obligations arise from a record with the goods, and § 2-313B, in which the obligations arise from communications to the public.<sup>743</sup> More specifically, § 2-313B would, in a manner very similar to § 2-313A, deal with an affirmation of fact or promise that relates to goods, a description of goods, or remedial promises that a seller makes “in an advertisement or a similar communication to the public.”<sup>744</sup> If that advertisement or communication is made and a remote purchaser then buys the goods with knowledge of the affirmation, promise, description, or remedial promise and an expectation that the goods will conform or that the promise will be performed, the seller would have an obligation similar to those of § 2-313A.<sup>745</sup> This “advertising” section operates on pre-transaction events, in contrast to the “in the box” timing of § 2-313A.<sup>746</sup> Further, the “knowledge” and “expectation” requirements of amended § 2-313B(3) are reminiscent of the

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740. See *infra* note 741 and accompanying text.

741. WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 193.

742. Compare U.C.C. § 2-207 cmt. 4 (amended 2003), 1 U.L.A. 399 (2004), with U.C.C. § 2-313A(3) (amended 2003), 1 U.L.A. 430-31 (2004).

743. See U.C.C. §§ 2-313A, 2-313B (amended 2003), 1 U.L.A. 430-31, 433 (2004); Reitz, *supra* note 654, at 386-92 (describing proposals on both topics).

744. See U.C.C. § 2-313B(c). There remains a reference to express warranty from advertising in § 2-313, Comment 4: “An express warranty to an immediate buyer may also arise through a medium for communication to the public if the elements of this section are satisfied.” *Id.* § 2-313 cmt. 4 (amended 2003), 1 U.L.A. 427 (2004).

745. See *id.* §§ 2-313A(3), 2-313B(3).

746. *Id.*

traditional § 2-313 “basis of the bargain” element.<sup>747</sup> Of course, the interpretation of advertising and public communications for purposes of assessing whether an obligation arises would present unusual challenges.<sup>748</sup>

Not surprisingly, proposals for advertising-based obligations similar to warranties and remedial promises drew criticism.<sup>749</sup> Again, the concept of a warranty or remedial promise obligation arising from advertising is not new.<sup>750</sup> There were also concerns that a major consequence would be increased expense in review of advertising by legal counsel for advertisers.<sup>751</sup> The Texas Subcommittee recommended against inclusion of § 2-313B, and the 2007 Bill does not include that provision.<sup>752</sup> As White and Summers put it, “section 2-313A is good law, built on firm ground”; however, “[t]he same cannot be said of Section 2-313B.”<sup>753</sup> Also, the comments to § 2-313 in place after the amendments continue to provide that § 2-313 itself “is not designed in any way to disturb those lines of case law which have recognized that warranties need not be confined to contracts within the scope of this Article.”<sup>754</sup> Development of case law in the area of warranty (or other obligation) from advertising may continue, although the limitation of § 2.313 to “immediate buyers” may have some effect.<sup>755</sup>

### E. Disclaimers of Implied Warranties

At the beginning of the Article 2 review process, some participants proposed changes in the “disclaimer” rules of § 2-316.<sup>756</sup> For current purposes, we consider three aspects of the changes: the requirement of conspicuousness for an “as is” disclaimer, the terminology required for disclaimers of implied warranties in consumer contracts, and the relationship of UCC disclaimers to requirements of the Magnuson-Moss Act for consumer warranties.<sup>757</sup>

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747. U.C.C. §§ 2-313(2)(a), 2-313B(3).

748. See generally *Am. Tobacco Co. v. Grinnell*, 951 S.W.2d 420, 436-37 (Tex. 1991) (discussing express warranty in advertising).

749. See Memorandum from Patricia D. Tauchert to Stephanie Heller, *supra* note 109, at 2; Memorandum from Jeff Dodd to Stephanie Heller, *supra* note 98, at 3.

750. See, e.g., *PPG Indus., Inc. v. JMB/Houson Ctrs. Partners Ltd.*, 146 S.W.3d 79, 98-100 (Tex. 2004). The plaintiff in *PPG Industries* asserted claims under, and obtained a trial court judgment for breach of, a twenty-year limited warranty originating with an advertisement in an architectural publication. *Id.* at 98. The Texas Supreme Court held that the question of whether this became part of the basis of the bargain as an express warranty should have been for the jury and not determined as a matter of law. *Id.* at 99-100; see also *Safeway Stores, Inc. v. Certaineed Corp.*, 710 S.W.2d 544, 545 (Tex. 1986) (addressing an advertised warranty).

751. See WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 110.

752. See *infra* app. II.

753. WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 102.

754. U.C.C. § 2-313 cmt. 4 (amended 2003), 1 U.L.A. 427 (2004) (regarding a warranty to an “immediate buyer”).

755. See *infra* Part III.E.2.

756. See *infra* Part III.E.2.

757. See *infra* Part III.E.2.

### 1. Current Provisions

Section 2.316 is the provision that permits sellers to disclaim or limit warranties, just as §§ 2.718 and 2.719 provide for contractual liquidation or limitation of damages and limitation or modification of remedies upon breach.<sup>758</sup> As noted earlier in discussing a remedial promise, remedies and warranties differ: “[R]emedies are what you get when warranties are breached; they are not warranties. A limitation on remedies does not affect the warranty . . . though it may vitiate its effect . . . .”<sup>759</sup> Of course vendors will also prefer to reduce the risk at the outset by limiting or disclaiming warranty obligations before one reaches the limitation of remedies.

Section 2.316 permits disclaimer or limitation of express and implied warranties.<sup>760</sup> Section 2.316(a) concerns express warranties and requires words or conduct creating, negating, or limiting express warranties to be construed as consistent with each other “wherever reasonable,” but subject to § 2.202 on extrinsic and parol evidence; a negation or limitation of an express warranty is ineffective insofar as such a negating or limiting construction is unreasonable.<sup>761</sup>

### 2. Proposed Changes in § 2.316 Disclaimer Rules

With respect to disclaimers of the implied warranties of merchantability and of fitness for a particular purpose, the 2003 Amendments and 2007 Bill propose changes.<sup>762</sup> The first change concerns the disclaiming seller’s trump card, the “as is” disclaimer of § 2.316(c)(1).<sup>763</sup> The PEB Study Group and the ABA Task Force both included the requirements for use of an “as is” disclaimer as a point for amendment.<sup>764</sup> The trump card is that the current, and proposed, § 2.316 permit, “unless the circumstances indicate otherwise,” the exclusion of *all implied warranties* by use of “expressions like ‘as is,’ ‘with all faults,’ or other language that in common understanding . . . makes plain that there is no implied warranty.”<sup>765</sup> Recall that the more explicit and extensive requirements of § 2.316(b) on implied warranty disclaimers are, and are proposed to be, “[s]ubject to” § 2.316(c), where “as is” resides.<sup>766</sup> Consequently, the pure statutory terms might allow a seller, under the right

758. TEX. BUS. & COM. CODE ANN. §§ 2.316-.319 (Vernon 1994).

759. Wladis, *supra* note 169, at 1767.

760. TEX. BUS. & COM. CODE ANN. § 2.316(a)-(c).

761. TEX. BUS. & COM. CODE ANN. § 2.316(a). This is retained, slightly edited, in proposed § 2.316(a) of the 2007 Bill. *See infra* app. I, § 2.316(a). Proposed changes to Section 2.202, the parol and extrinsic evidence section of the Code, are not covered in this Article. *See infra* app. I, § 2.202.

762. *See* U.C.C. § 2-316 (amended 2003), 1 U.L.A. 441 (2004); *infra* app. I, § 2-316.

763. TEX. BUS. & COM. CODE ANN. § 2.316(c)(1); *see infra* app. I, § 2.316(c)(1).

764. PEB STUDY GROUP, PRELIMINARY REPORT, *reprinted in* ABA Task Force, *Appraisal*, *supra* note 57, at 1108; ABA Task Force, *Appraisal*, *supra* note 57, at 1108-09.

765. *See* TEX. BUS. & COM. CODE ANN. § 2.316(c)(1); *infra* app. I, § 2.316(c)(1).

766. TEX. BUS. & COM. CODE ANN. § 2.316(b); *see infra* app. I, § 2.316(b).

facts, to disclaim all implied warranties by use of the “as is” term in the proper circumstances, and current § 2.316(c) does not by its terms require the “as is” disclaimer to be conspicuous.<sup>767</sup> Although it is possible that an “as is” term by itself might effectively disclaim implied warranties, that result is not assured.<sup>768</sup> As one commentator observed in assessing the reluctance of courts to give full rein to an “as is” clause, the Code supplies a check in that Comments 6 and 7 to § 2.316 “make clear that subsection (c) applies only to ‘common factual situations in which the circumstances surrounding the transaction are in themselves sufficient to call the buyer’s attention to the fact that no implied warranties are made.’”<sup>769</sup> To provide some additional protection against overreaching use of “as is” disclaimers, proposed § 2.316(c) will require that an “as is” disclaimer in a “consumer contract evidenced by a record” be conspicuous.<sup>770</sup>

This requirement of conspicuousness under the consumer contract rule of proposed § 2.316(c) for “as is” disclaimers has obvious parallels in the proposed changes to the requirements for disclaimers of the implied warranties of merchantability and of fitness for a particular purpose.<sup>771</sup> For the content of a “consumer contract,” refer to proposed §§ 2.102(b)(11) and 2.103(a)(4): “[c]onsumer” means an individual who enters into a transaction primarily for personal, family, or household purposes,<sup>772</sup> and “[c]onsumer contract” means a contract between a merchant seller and a consumer.<sup>773</sup>

For consumer contracts, the 2007 Bill would not only require that an “as is” disclaimer of implied warranties be conspicuous but also add requirements that disclaimers of implied warranties of fitness for a particular purpose or of merchantability (1) be in a record, (2) be conspicuous, and (3) use statutory terminology.<sup>774</sup> The requirements that these disclaimers be *in a record* and be *conspicuous* corrects (for consumer contracts) an inconsistency under present § 2.316, which requires a disclaimer of an implied warranty of fitness for a purpose to be set out in an exclusion that is “by a writing and conspicuous” but requires a disclaimer of merchantability to mention only merchantability and

767. See ABA Task Force, *Appraisal*, *supra* note 57, at 1108-09 (“[Amend this section] to require that any such language contained in a writing be conspicuous, thus resolving an acknowledged problem.”). For changes to the definition of “conspicuous” for purposes of Chapter 2, see *infra* app. I, § 2.102(a)(2). Cf. TEX. BUS. & COM. CODE ANN. § 1.201(b)(10) (Vernon Supp. 2008) (general definition).

768. See WHITE & SUMMERS, *UNIFORM COMMERCIAL CODE*, *supra* note 226, at 803-07 (commenting that if conspicuousness is not required for an “as is” disclaimer then other disclaimer requirements of conspicuousness would be ineffective).

769. ANDERSON, BARTLETT & EAST, *supra* note 299, at 168.

770. See *infra* app. I, § 2.316(c)(1).

771. See *infra* app. I, § 2.316(b).

772. TEX. BUS. & COM. CODE ANN. § 1.201(b)(11) (Vernon Supp. 2008). The Texas Subcommittee recommends a cross reference to this existing definition rather than enactment of the proposed Chapter 2 specific definition of “consumer” in § 2-102(1)(c) of the 2003 Amendments.

773. See *infra* app. I, § 2.103(a)(4).

774. See *infra* app. I, § 2.316.

“in case of a writing” be conspicuous.<sup>775</sup> The proposed amendment treats both types of disclaimers alike in the consumer context.<sup>776</sup>

In addition, the proposed amendment of § 2.316(c) sets out language that is *required* in a consumer contract for disclaimers of the implied warranties of fitness and merchantability and then provides three requirements for these disclaimers in *non-consumer* contracts.<sup>777</sup> For non-consumer contracts, the required compliance points are as follows:

- (1) for a disclaimer as to merchantability, the disclaimer language must mention merchantability and, *if in a record*, be conspicuous;
- (2) for a disclaimer as to fitness, the disclaimer language must be in a record and be conspicuous, and is sufficient textually if, for example, it states, “there are no warranties that extend beyond the description on the face hereof”; and
- (3) for a disclaimer as to warranties both of merchantability and fitness, if the non-consumer contract uses the required consumer forms of disclaimers, these terms will satisfy the textual requirements of the section.<sup>778</sup>

Certain text is required for disclaimers in consumer contracts. For the exclusion of an implied warranty of merchantability, “[t]he seller undertakes no responsibility for the quality of the goods except as otherwise provided in this contract.” For the exclusion of an implied warranty of fitness, “[t]he seller assumes no responsibility that the goods will be fit for any particular purpose for which you may be buying the goods, except as otherwise provided in the contract.”<sup>779</sup>

As the required disclaimer text for consumer contract warranty disclaimers differs from present practice, commercial advocates have opposed incurring the costs to change existing transaction forms.<sup>780</sup> The adoption of the proposed amendments also would produce a period of non-uniformity, as enactment of the 2003 Amendments in a significant number of states is presently unlikely.

In practical terms, the required consumer disclaimer texts will improve, to a degree, the level of information conveyed to a consumer about a warranty disclaimer. The present requirement that a disclaimer of the implied warranty of merchantability mention merchantability probably does little beyond caution the buyer that *something* is being limited. Indeed, a lawyer thinking in real estate terms could well start from the incorrect, but understandable, idea that

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775. TEX. BUS. & COM. CODE ANN. § 2.316(b) (Vernon 1994).

776. See *infra* app. I, § 2.316.

777. See *infra* app. I, § 2.316(c).

778. See *infra* app. I, § 2.316(b).

779. *Id.*

780. See Memorandum from Holly K. Towle to Stephanie Heller, *supra* note 99, at 3.

the disclaimer concerns “title” to the goods.<sup>781</sup> That usage is much different from Code merchantability.<sup>782</sup> The proposed required disclaimers do a better job of describing what the seller is disclaiming and are worthy of approval on the merits.<sup>783</sup>

With respect to the cost of compliance issues due to a multiplicity of laws to which a large commercial manufacturer might be subject, one should remember that Article 2 *already* has a significant number of state-specific, non-uniform amendments for the consumer implied warranty disclaimer that sellers have been able to cope with thus far.<sup>784</sup> These additional variations do not seem unmanageable, particularly if an adequate transition period is provided.

Finally, as to the disclaimer of implied warranties under the UCC, both current and proposed, recall that the Magnuson-Moss Act (1) prevents a supplier from *disclaiming any* implied warranty to a consumer if a written warranty or service contract is provided by the supplier and (2) allows an implied warranty in a federal “limited warranty” to be “limited in duration to the duration of a written warranty of reasonable duration” if done clearly and prominently in unmistakable language.<sup>785</sup> As we have seen, a “warranty” under the UCC has “no duration” (in terms of a “time before” a cause of action accrues) as the breach occurs upon delivery, unless an express warranty “explicitly extends” to future performance.<sup>786</sup> Frisch and Leary argue that warranties of fitness for a particular purpose and fitness for the ordinary purposes of goods have implicit future performance qualities.<sup>787</sup> And from the framework of the Magnuson-Moss Act, where a warranty includes “any undertaking . . . to refund, repair, replace or take other remedial action,”<sup>788</sup> there is perhaps an indirect endorsement of the Frisch and Leary concept. It is sufficient to say that the proposed 2007 Bill does not solve the interconnection

781. *See, e.g.*, First Am. Title Co. v. Prata, 783 S.W.2d 697, 702-03 (Tex. App.—El Paso 1989, writ denied) (describing merchantable, marketable title).

782. TEX. BUS. & COM. CODE ANN. § 2.314(b) (Vernon 1994).

783. “Title” is not part of UCC “merchantability.” Section 2.312 provides a warranty of title and a warranty against infringement and guidance on its disclaimer. The 2003 Amendments and 2007 Bill propose amendments to § 2.312. The warranty of title and against infringement under § 2.312 are statutory but are not “implied warranties.” U.C.C. § 2-312 cmt. 6 (amended 2003), 1 U.L.A. 425 (2004); *see infra* app. I, § 2.312.

784. *See, e.g.*, CONN. GEN. STAT. ANN. § 42a-2-316(5) (2003) (“[Provisions on disclaimers] shall not apply to sales of new or unused consumer goods, except for those goods clearly marked ‘irregular’ . . . . Any language . . . which attempts to exclude or modify any implied warranties of merchantability and fitness . . . or to exclude or modify the consumer’s remedies for breach of those warranties shall be unenforceable.”); D.C. CODE ANN. § 28:2-316.01 (2002); ME. REV. STAT. ANN. Title 11, § 2-316(2) (1994); MD. CODE ANN. COM. LAW § 2-316.1 (2001); WASH. REV. CODE ANN. § 62A.2-316(4) (West 2003); Leary & Frisch, *supra* note 55, at 415, n.65.

785. 15 U.S.C. § 2308(a)-(b) (2000). In a federal “full warranty,” the supplier may not impose any duration limit on the implied warranty. 15 U.S.C. § 2304(a)(2).

786. TEX. BUS. & COM. CODE ANN. § 2.725(B) (Vernon 1994); *see infra* app. I, § 2.725(c)(3).

787. Leary & Frisch, *supra* note 55, at 412. *Contra* Safeway Stores, Inc. v. Certaineed Corp., 710 S.W.2d 544 (Tex. 1986).

788. 15 U.S.C. § 2301 (2006).

and interpretative issues between the Code and the federal Act, but it also does not create particular new problems on that point.

Two ancillary notes should be added to the coverage of warranty disclaimers. First, proposed § 2.314 proposes a subtle but important change in the definition of the “ordinary purposes” component.<sup>789</sup> This measure of “merchantability” is now “the ordinary purposes for which goods *of that description*” are used, not “ordinary purposes for which such goods are used.”<sup>790</sup> This means the terms of the agreement—specifications in an order, for example—may have more weight.<sup>791</sup>

The second note concerns a much debated change in the comments to proposed § 2.314 that is not remarked upon in the Texas Subcommittee’s Bill Analysis.<sup>792</sup> This change deserves a warning label based on the *Fetter* decision and the lack of weight it gave to a Texas State Bar Committee Comment concerning a recent amendment of the UCC.<sup>793</sup> The § 2.314 issue, affected by proposed Comment 7 within the comments to that section, is one that arises from the close connection between the UCC implied warranty of merchantability and strict tort liability: is there a difference in the standards of proof required for liability for breach of an implied warranty of merchantability, on the one hand, and for liability under strict tort principles, where the damages are sought for injury to person or property, on the other?<sup>794</sup> White and Summers review the issue and provide a transcript of the debate at the ALI.<sup>795</sup> The result of the debate on rewritten Comment 7 is that the standards are to be the same: “If a manufacturer is liable in strict tort, it should also be liable for breach of the warranty of merchantability, if the warranty was made, and vice versa.”<sup>796</sup>

#### F. Consequential Damage Claims Against Buyers

The PEB Study Group and ABA Task Force concurred in their initial work that §§ 2-706 through 2-710 should provide for recovery of consequential damages by *sellers*.<sup>797</sup> Problems in the determination of consequential damages

789. See *infra* app. I, § 2.314; cf. TEX. BUS & COM. CODE ANN. § 2.314 (Vernon 1994).

790. Compare TEX. BUS & COM. CODE ANN. § 2.314(b)(3), with *infra* app. I, § 2.314(b)(3).

791. See WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 113.

792. For a section with few textual changes, the principal one being the change to refer to the purposes of “goods of that description,” the comments to § 2.314 show substantial re-writing.

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

794. See *Denny v. Ford Motor Co.*, 662 N.E.2d 730 (N.Y. 1995) (creating the *Denny* question in the case in which a plaintiff sued for breach of implied warranty and on strict tort liability grounds).

795. WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 113-16, 223-41.

796. *Id.* at 116.

797. PEB STUDY GROUP, PRELIMINARY REPORT, reprinted in ABA Task Force, *Appraisal*, *supra* note 57, at 1226 (“If this recommendation [to § 2-710] is adopted . . . [ §§ 2-706 through 2-709 ] should be revised to say ‘together with any incidental and consequential damages as provided in [ § 2-710 ].’”); ABA Task Force, *Appraisal*, *supra* note 57, at 1227.

are numerous and complex, not the least of which are those of the “lost volume seller.”<sup>798</sup>

The structure of the UCC requires that consequential damages be expressly permitted in order to be recoverable under the overall principle of § 1.305: “The remedies provided by [the UCC] must be liberally administered to the end that the aggrieved party may be put in as good a position as if the other party had fully performed but neither consequential nor special damages . . . may be had except as specifically provided in this title or by other rule of law.”<sup>799</sup>

Current §§ 2.712, 2.713, and 2.714 have long provided for the *buyer’s* recovery of consequential damages.<sup>800</sup> The disparity of providing for recovery of consequential damages by buyers, but excluding such recovery by sellers, is striking: “There is no reason in logic or fairness for treating the consequential loss of one party, the seller, as penal damages while simultaneously treating such a loss by the buyer as compensatory.”<sup>801</sup>

The 2007 Bill follows the 2003 Amendments in allowing sellers to recover consequential damages. Each of §§ 2.706 (Seller’s Resale), 2.708 (Seller’s Damages for Nonacceptance or Repudiation), and 2.709 (Action for the Price) in the 2007 Bill add appropriate references to the seller’s recovery of consequential damages, in addition to the other existing damages and remedies.<sup>802</sup> Proposed § 2.710(b) provides a definition of the seller’s consequential damages: “Consequential damages resulting from the buyer’s breach include any loss resulting from general or particular requirements and needs of which the buyer at the time of contracting had reason to know and which could not reasonably be prevented by resale or otherwise.”<sup>803</sup>

This definition of seller’s consequential damages tracks the definition of consequential damages for buyers in § 2.715(b), with the omission of a reference to injury to person or property.<sup>804</sup> Section 2.710(c) then provides that a seller may not recover consequential damages from a consumer.<sup>805</sup> Comment 3 to § 2.710 observes this is a nonwaivable provision.<sup>806</sup>

The revision to permit recovery of a seller’s consequential damages certainly provides a new theory of liability, a consistent theme from critics of the 2003 Amendments. As most commercial enterprises are both buyers and

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798. See Anderson, *supra* note 118, at 128-41; Leary & Frisch, *supra* note 55, at 443-44 (noting extensive commentary on allowing seller recovery of consequential damages); see also Anderson, *supra* note 157, at 833 (regarding lost volume sellers).

799. TEX. BUS & COM. CODE ANN. § 1.305(a) (Vernon Supp. 2008).

800. TEX. BUS & COM. CODE ANN. §§ 2.713-.714 (Vernon 1994).

801. Anderson, *supra* note 118, at 128.

802. See *infra* app. I, §§ 2.706(a), 2.708(a), 2.709(a).

803. See *infra* app. I, § 2.710(b).

804. See TEX. BUS & COM. CODE ANN. § 2.715(b) (Vernon 1994).

805. *Id.* § 2.710(c).

806. *Id.*; see *infra* app. I, § 2.710(3) cmt. 3.

sellers, the level of criticism of the change to allow recovery by sellers of consequential damages has been less than on other changes.<sup>807</sup>

The overall assessment of the seller consequential damage revisions is favorable. First is fairness: “[A]llowing sellers recovery for consequential damages on appropriate facts is well justified by the basic compensation principle in Article 2 and by the obvious injustice reflected by the current case law that categorically denies sellers that recovery.”<sup>808</sup> Second, the factual situation in which a seller might actually seek consequential damages that could not be reasonably prevented are few: “Allowing consequential damages for sellers is unlikely to open the proverbial litigation floodgates.”<sup>809</sup> These changes are not only focused but also fair.<sup>810</sup>

### *G. Priorities Between Competing Purchasers of Entrusted Goods*

The PEB Study Group’s initial report included comments on modification of § 2-102, and the “scope” provision of Article 2 with respect to the identification of “other laws” that are not affected by the UCC.<sup>811</sup> Texas law makes clear that the UCC does not “impair or repeal any statute regulating sales to consumers, farmers or other specified classes of buyers.”<sup>812</sup> The Study Group recommended “that a list of either particular statutes or types of statutes be provided in the text of § 2-102” to provide a better guide to problems of statutory construction, while using § 2A-104 of Article 2A as a model.<sup>813</sup> Proposed § 2.108 of the 2007 Bill, following the provisions of § 2-108 in the 2003 Amendments, includes a more complete statement of other applicable laws that the UCC is not to preempt.<sup>814</sup> The particular provision addressed here is that relating to the interplay of the UCC and certificate of title laws.<sup>815</sup> As proposed, § 2.108 would state the following:

A transaction subject to this chapter is also subject to any applicable:  
 (1) certificate of title statute of this state, *including Chapter 501, Transportation Code*, relating to the certificate of title for motor vehicles . . .

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807. *But cf.* Memorandum from Holly K. Towle to Stephanie Heller, *supra* note 99, at 3 (“Another example is § 2-710(3) which creates a devastating rule for information companies which may or may not find themselves in Article 2 . . . . [T]he new rule precludes them from recovering consequential damages from consumers, thereby removing the consumer’s incentive to comply with the agreement.”). This comment may not address trade secret and misappropriation law issues under other statutes.

808. Anderson, *supra* note 157, at 820; *see also* WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 146-47.

809. Anderson, *supra* note 157, at 819.

810. For a summary of some proposed damage revisions that the Texas Subcommittee did not include in the 2007 Bill, see *infra* Part II.B.8.

811. See PEB STUDY GROUP, PRELIMINARY REPORT, *reprinted in* ABA Task Force, *Appraisal*, *supra* note 57, at 1024.

812. TEX. BUS. & COM. CODE ANN. § 2.102 (Vernon 1994).

813. ABA Task Force, *Appraisal*, *supra* note 57, at 1024.

814. See *infra* app. II, § 2.108.

815. See *infra* app. II, § 2.108.

*except with respect* to the rights of a buyer in ordinary course of business under Section 2.403(b) which arise before a certificate of title covering the goods is effective in the name of any other buyer.<sup>816</sup>

The current provisions of § 2.403(b), so referenced, deal with the rights of buyers where the true owner has “entrusted” goods to another: “Any entrusting of possession of goods to a merchant who deals in goods of that kind gives him power to transfer all rights of the entruster to a buyer in ordinary course of business.”<sup>817</sup>

Automobile transactions seem to produce a high number of entrusting and multiple buyer disputes, where each buyer has an understandable story about the competing claims to the same vehicle.<sup>818</sup> The cases in Texas are split and often unhelpful.<sup>819</sup>

As for the UCC, the parallel universe in Texas for motor vehicle transactions is the Certificate of Title Act, as referenced in proposed § 2.108(a)(1).<sup>820</sup> Under that Act’s standards, “a motor vehicle may not be the subject of a subsequent sale unless the owner designated in the certificate of title transfers the certificate of title at the time of the sale.”<sup>821</sup> A following section reinforces the principle: “A sale made in violation of this chapter is void and title may not pass until the requirements of this chapter are satisfied.”<sup>822</sup>

After an early clash between the Certificate of Title Act and the UCC over security interest perfection and the status of a “sale” in which the certificate of title was not transferred in accordance with the then predecessor of the Certificate of Title Act,<sup>823</sup> the Texas Legislature adopted what is now § 501.005 of the Certificate of Title Act: “Chapters 1-9, Business & Commerce Code, control over a conflicting provision of this chapter.”<sup>824</sup>

Even with this general rule to resolve conflicts, the confusion between the Code and the Certificate of Title Act continues.<sup>825</sup> Section 2.401 of the Code, as now in effect, should affect the disposition of at least some cases with Code and Certificate of Title Act conflicts (particularly as § 501.005 already indicates the Code should control): “Unless otherwise explicitly agreed title passes to the buyer at the time and place at which the seller completes his performance with

816. See *infra* app. I, § 2.108 (emphasis added).

817. TEX. BUS. & COM. CODE ANN. § 2.403(b) (Vernon 1994). This section is edited in the 2007 Bill, but not amended in substance. See *infra* app. I, § 2.403(b).

818. See Clark, *supra* note 124 (gathering and reviewing cases and different lines of authority in Texas).

819. See *id.*

820. TEX. TRANSP. CODE ANN. §§ 501.001-.159 (Vernon 2007).

821. *Id.* § 501.071(a). However, an auction exception is also provided. *Id.* § 503.039.

822. *Id.* § 501.073.

823. Phil Phillips Ford, Inc. v. St. Paul Fire & Marine Ins. Co., 465 S.W.2d 933 (Tex. 1971) (holding that § 2.401 of the Texas Business & Commerce Code did not control and thus the transfer of title without certificate of title was void).

824. TEX. TRANSP. CODE ANN. § 501.005. When adopted, the bill amended the Certificate of Title Act in detailed ways to coordinate security interest perfection rules. Millard H. Ruud, *Amendment of the Texas Certificate of Title To Conform It to the Uniform Commercial Code*, 33 TEX. B.J. 968 (1970).

825. See Clark, *supra* note 124.

reference to the physical delivery of the goods . . . .”<sup>826</sup> Section 2.401 has already applied in a variety of cases to support the validity of the “sale” to the subsequent purchaser.<sup>827</sup> A conflict among the courts of appeals presently exists; however, one route to resolution is the enactment of the Uniform Certificate of Title Act proposed by NCCUSL.<sup>828</sup>

The inclusion of a specific reference to the Certificate of Title Act and the priority for rights of buyers in ordinary course arising before a certificate of title to another is issued as proposed in § 2.108(a)(1), will help by providing another reference point in the Code to determine whether a transaction validly passes title to a motor vehicle.<sup>829</sup> It may not, however, affect the methodology (and outcome) in cases courts that adopt the *Gallas* view, that there is *no conflict* because the Certificate of Title Act precludes a “sale” from occurring.<sup>830</sup>

A further cautionary word on the sweep of the proposed rule under § 2.108(a)(1) is that it operates only in the case of a buyer in the ordinary course whose rights under § 2.403(b) arise “before a certificate of title . . . is effective in the name of any other buyer.”<sup>831</sup> Thus, a further interpretive issue with the Certificate of Title Act will arise. If the § 2.403(b) rights of a buyer in the ordinary course prevail only when the rights from an entrusting buyer arise “before a certificate of title . . . is effective in the name of any other buyer,” a court will need to construe “buyer” to mean “a person other than the current-named owner,” i.e., to mean one buying at the time in question and not before.<sup>832</sup> Otherwise, for all “subsequent sales” under § 501.071 of the Transportation Code there will *always* be a certificate of title “effective in the name” of the entrusting owner, a construction that would restrict the operation of proposed § 2.108(a)(1) to entrustment of only unregistered or dealer-titled vehicles.<sup>833</sup>

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826. TEX. BUS. & COM. CODE ANN. § 2.401(b) (Vernon 1994). The 2007 Bill makes some editing changes to this section but does not alter the substance. See *infra* app. I, § 2.401(b). A “document of title” referred to in § 2.401(b) and (c) is not a certificate of title, which includes that the document be “issued by or addressed to” a bailee. See TEX. BUS. & COM. CODE ANN. §§ 1.201(b)(16), 2.401(b)-(c) (Vernon 1994 & Supp. 2008). If the goods are to be delivered without moving them *and* the seller is to deliver a document of title, then title passes with the document of title. § 2.401(c).

827. Compare *Vibbert v. PAR, Inc.*, 224 S.W.3d 317, 317 (Tex. App.—El Paso 2006, no pet.) (concluding that sale with delivery of vehicle but not title certificate did transfer ownership under § 2.401 and was not void), and *Hudson Buick Pontiac, GMC Truck Co. v. Gooch*, 7 S.W.3d 191, 197 (Tex. App.—Tyler 1999, pet. denied) (concluding that sale between dealers effective upon delivery of possession), with *Gallas v. Car Biz, Inc.*, 914 S.W.2d 592, 592 (Tex. App.—Dallas 1995, writ denied) (holding sale of title void when no title passed under Certificate of Title Act).

828. See Clark, *supra* note 124.

829. See *infra* app. II, § 2.108.

830. See *Gallas*, 914 S.W.2d at 594-95. “A sale made in violation of this chapter is void and title may not pass until the requirements of this chapter are satisfied.” TEX. TRANSP. CODE ANN. § 501.073 (Vernon 2007).

831. See *infra* app. I, § 2.108(a)(1).

832. See *infra* app. II, § 2.108(a)(1).

833. TEX. TRANSP. CODE ANN. § 501.071; *infra* app. I, § 2.108(a)(1). *Gallas* and other decisions that use § 501.071 of the Transportation Code to “void” a sale often refer to § 2.106(a) of the U.C.C., which states, “A ‘sale’ consists of the passing of title from the seller to the buyer for a price . . . .” TEX. BUS. &

### H. Changes in Limitations Provisions of § 2.725

The final portion of the 2007 Bill and 2003 Amendments covered in this Article is § 2.725, the Code's statute of limitations for Chapter 2 causes of action. The revisions proposed in the 2007 Bill are extensive, partly as a result of the need to provide rules that will include the remedial promise and the obligations to a remote purchaser as proposed in other sections.<sup>834</sup> Beyond coverage of new types of claims, the length of the amended section reflects work on some old problems: "In fairness, it is longer because it solves problems created by its terser predecessor."<sup>835</sup> Some answers to problems under current § 2-725 were included in changes considered by the PEB Study Group for Code limitations provisions, and the Study Group even considered creating a much longer statute of repose, but no initial recommendations were in the initial report or its *Executive Summary*.<sup>836</sup> The ABA Task Force provided more concrete ideas on changes in limitations, but its *Appraisal* emphasized that the Task Force considered "[t]he root cause of the different results in the cases is the perceived injustice caused by [selecting] . . . tender of delivery as the time when a breach of warranty occurs and a cause of action accrues."<sup>837</sup> Proposed § 2.725 appears to expand from four operative subsections to five, but new subsections (b) and (c) have multiple sub-parts, so this amendment is appreciably longer than the current provision and reflects "a greater degree of specialization" in limitations rules, consistent with a principle recommended for updating general rules of Article 2 for use in more specialized times.<sup>838</sup> As the proposed changes are substantial, a fairly detailed outline of them is useful.

#### 1. The Basic Period of Limitation: § 2.725(a)

The basic rule, unless otherwise provided by a subpart of proposed § 2.725, is that

an action for breach of any contract of sale must be commenced within the later of four years after the right of action has accrued [under subsections 2.725(b) and (c)] or one year after the breach was or should have been discovered, but no longer than five years after the right of action accrued.<sup>839</sup>

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COM. CODE ANN. § 2.106(a) (Vernon 1994); *Gallas*, 914 S.W.2d at 594-95. Code provisions as to the rights of a person under Chapter 2 operate "irrespective of title to the goods except where the provision [of Chapter 2] refers to such title"; § 2.403 can operate in that manner. TEX. BUS. & COM. CODE ANN. § 2.401.

834. Leary & Frisch, *supra* note 55, at 465.

835. Larry T. Garvin, *supra* note 670, at 347.

836. See ABA Task Force, *Appraisal*, *supra* note 57, at 1246-1250.

837. See *id.* at 1248.

838. See Leary & Frisch, *supra* note 55, at 465 (speaking of problems in applying Article 2 provisions in ever more specialized situations); *infra* app. I, § 2.725.

839. U.C.C. § 2-725(b) (amended 2003), 1 U.L.A. 556 (2004); *infra* app. I, § 2.725(a). No editorial punctuation has been added to the proposed text as it appears above so as not to influence the reader's interpretation.

For purposes of analysis, if we posit for simplicity a cause of action for breach of warranty that accrues on the delivery of goods, the obvious change from current § 2.725(a) is the inclusion of an extended period for suit (up to five years from four) where a statutory discovery term applies. How will this new rule of “four years plus one for discovery” operate? White and Summers offer an illustration:

Assume that a buyer buys goods on January 5, 2005 . . . .

. . . First assume that this buyer discovers the breach immediately [receiving a red car instead of yellow] . . . . The buyer has until January 4, 2009 to sue. The one-year discovery rule does not limit the time because of the assured four years.

Assume the buyer discovers the defect on December 10, 2008—the wrong piston rings were installed and one fails in early December 2008. Now the one-year rule gives the buyer until December 9, 2009 . . . .

What if the piston rings fail and the engine seizes in February of 2009? Here the buyer can argue that January 4, 2010 is the last date suit can be brought. In this case, of course, the assured time of four years had already run . . . . The discovery rule might still be read to resurrect the dead cause of action, but we doubt it.<sup>840</sup>

Comment 2 to amended § 2-725 provides support for the position that White and Summers take as to the “[non]resurrection” of a claim: “Subsection [a] continues the four-year limitation period . . . but provides a possible one-year extension to accommodate a discovery of the breach *late* in the four year period after accrual.”<sup>841</sup> This is also the view of Professor Garvin: “Perhaps most critically, the general limitations period would become one year from discovery or four years from accrual, whichever is longer, but in any event not more than five years from accrual. This effectively retains the old four-year period, save for actions discovered late in the fourth year.”<sup>842</sup>

Since amended § 2-725 retains the essence of the current basic rule for accrual of standard warranty causes of action—a right of action accrues on tender of delivery (and completion of agreed installation or assembly), setting aside warranties that explicitly extend to future performance—then “normal” limitations on the standard warranty cause of action expire after four years.

Does the “one year after discovery if later” option allow a cause of action to revive, after limitations have apparently run, if discovery follows the end of four years? First, consider that the basic rule of proposed § 2.725(a)—an action must be commenced within four years “after the right of action has accrued”

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840. WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 125. In this example, the cause of action (for breach of warranty) accrued on delivery, a rule provided by current § 2.725(a) and continued by proposed § 2.725(c)(1). Recall that a claim for breach of a warranty that “explicitly extends” to future performance would currently accrue on discovery through the end of the future performance period under *PPG Industries, Inc. v. JMB/Houston Ctrs. Partners Ltd.*, 146 S.W.3d 79, 92–93 (Tex. 2004).

841. U.C.C. § 2-725 cmt. 2 (amended 2003), 1 U.L.A. 558 (2004) (emphasis added).

842. Garvin, *supra* note 670, at 397.

under subsections (b) and (c)—would apply to those causes of action that accrue on *discovery*, as well as to actions that accrue at the time of an event (e.g., delivery).<sup>843</sup> Thus the simple case for analysis under proposed § 2.725 is determining the limitation period for those causes of action that *accrue on discovery*. The claimant there will use the “four years after accrual” period, as that will always be longer than one year after discovery, and the no extension rule would come into play. A limitation period tied to “accrual on discovery” will apply to claims for (1) breach of an express warranty under proposed § 2.313(b) or of an obligation under proposed § 2.313A (other than a § 2.313A remedial promise) that “explicitly extends” to future performance and as to which discovery must await performance, and (2) breach of a warranty under § 2.312 as to title or against infringement (but with an outside limit of six years from tender of delivery for infringement claims to be brought).<sup>844</sup> For remedial promises, a cause of action accrues when the remedial promise is not performed when performance is due.<sup>845</sup>

There is a subsidiary question for future performance warranty claims that accrue on discovery, rather than on delivery, under current and proposed § 2.725: does the beneficiary have four years from discovery within the period for which future performance is warranted, or could the period run from the time of discovery even if after the warranty period has expired? In *PPG*, the Texas Supreme Court adopted a “within the warranty period” rule: “Thus, warranty claims against PPG accrued not upon initial delivery, but when a reasonably buyer should have discovered any defects, up until the end of the five-year warranty period (when ‘the time of such performance’ expired).”<sup>846</sup>

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843. See *infra* app. I, § 2.725(a)–(c); U.C.C. § 2-725(1)–(3) (amended 2003), 1 U.L.A. 556-57 (2004). For convenience in discussion, the statutory phrase of “discovers or should have discovered” is simplified to “discovers” or “discovery.” The “should have discovered” component still applies in this usage.

844. See *infra* app. I, § 2.725(a)–(c); U.C.C. § 2-725(1)–(3). By its reference to § 2.313(b) for accrual on discovery, § 2.725(c)(3) would exclude implied warranties from the “accrual on discovery” standard. This is consistent with current Texas case law. See *Safeway Stores, Inc. v. Certainteed Corp.*, 710 S.W.2d 544, 547-48 (Tex. 1986) (“We hold, based on the rationale of the previous cases and the clear, unambiguous language of section 2.725(b), that an implied warranty cannot be explicitly extended to future performance.”); see also *Martinez v. Humble Sand & Gravel, Inc.*, 940 S.W.2d 139 (Tex. App.—El Paso 1996), *aff’d sub nom*, *Childs v. Haussecker*, 974 S.W.2d 31 (Tex. 1998). Whether an express warranty “explicitly extends” to future performance is a separate and sometimes cloudy question. See *Safeway Stores*, 710 S.W.2d at 548 (holding fact issue precluding summary judgment was presented as to whether express warranty explicitly extended to future performance).

845. See *infra* app. I, § 2.725(b)(3).

846. *PPG Indus., Inc. v. JMB/Houston Ctrs. Partners Ltd.*, 146 S.W.3d 79, 93 (Tex. 2004). The court subsequently stated a corollary of the rule that the cause of action in *PPG* accrued on discovery: The five-year warranty “was breached upon delivery . . . (although it [the cause of action] did not *accrue* until discovery within those five years).” *Id.* at 100 (emphasis added). *PPG* also explicitly addresses the nature of discovery in complex cases: “But the discovery rule does not linger until a claimant learns of actual causes and possible cures. Instead it only tolls limitations until a claimant learns of a wrongful injury; the party responsible for it, the full extent of it; of the chances of avoiding it.” *Id.* at 93-94. Professor Garvin observes that the case law is in line with the view that limitations must start to run no later than the end of the period for which future performance is warranted, but he argues that a literal reading of the current statute would permit accrual to start on discovery *after* the expiration of the period of warranted performance. Garvin, *supra* note 670, at 368.

With that explicit statement from the Texas Supreme Court, the rule under proposed § 2.725(a) and (c)(3) would conform to that statement as the proposed 2007 Bill does not express a purpose to change that existing interpretation of like language.

Returning to the operation of the amended statute in the case posited by White and Summers of a cause of action that accrued on delivery (or at another set time), would the “one year after discovery, if later” option allow a cause of action to revive, after limitations have apparently run, if discovery of breach (*but not* the accrual of a cause of action) follows the end of four years? Once a cause of action has *accrued* and limitations have run, it would take a very explicit statutory statement to support the resurrection of an accrued cause of action based on discovery *after* the limitation period had run.<sup>847</sup> A period of limitation “seeks to balance two conflicting social policies. If [liability extends indefinitely], merchants will not be able to close their books with certainty; yet, if merchants are allowed to close their books with certainty[,] buyers who later discover defects will have no remedy.”<sup>848</sup> With proposed § 2.725 keeping the same four-years-from-accrual balance as struck before for limitations generally, without a general discovery rule to defer accrual, a balance that has been upheld by Texas decisions such as *Safeway Stores*, the application of the late discovery extension only to those “accrued” causes of action that are “discovered” within the period of limitations is consistent with prior law and with the text of proposed § 2.725, which does not identify the late discovery as causing a new cause of action to arise or accrue in itself. The cause of action having accrued (as indicated in specific subsections of § 2.725 summarized below), the right of action does not *re-accrue* upon discovery, and the discovery event does not start a new or additional limitation period; it only extends the period for suit on a right that existed within the basic four year period.

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847. Proposed § 2.725(a) links its general four-year rule to the time when the “right of action has accrued.” As noted above, some causes of action “accrue” on “discovery” and others on the occurrence of an event. For neither type of cause of action does the extension clause (“one year after the breach was or should have been discovered”) alter the time of *accrual* of causes of action. Proposed § 2.725 thus adopts a uniform rule of accrual for all cases and provides an extension of time to bring an *accrued* action in certain situations—where it has accrued under the rules of § 2.725 without “discovery.” *Infra* app. I, § 2.275. This is in keeping with the usual expression of what a “discovery rule” in limitations cases does: “The discovery rule exception defers *accrual* of a cause of action until the plaintiff knew or, exercising reasonable diligence, should have known of the facts giving rise to the cause of action.” *Computer Assocs. Int’l Inc. v. Altai, Inc.*, 918 S.W.2d 453, 455 (Tex. 1996) (emphasis added).

848. *Safeway Stores, Inc.*, 710 S.W.2d at 546 (refusing to apply “explicitly extends” discovery rule to implied warranty). The Texas court has observed that applying a discovery rule because of “the ‘shocking results’ of barring a plaintiff’s suit before the injury has even been discovered [would, if] carried to its logical conclusion . . . mandate applying the discovery rule exception to every case, thus eviscerating the whole notion of an absolute time bar to litigation.” *Computer Assocs. Int’l Inc.*, 918 S.W.2d at 457. The UCC breach of contract cause of action currently accrues “when the breach occurs, regardless of the aggrieved party’s knowledge of the breach.” TEX. BUS & COM. CODE ANN. § 2.725(b) (Vernon 1994). The existing general result is summarized by Garvin: “Consistent with most cases in most jurisdictions, section 2-725 thus rejects a discovery rule.” Garvin, *supra* note 670, at 349. This statutory text is carried forward as the baseline rule in proposed § 2.725(b)(1) for non-warranty breach of contract claims, with some specific modifications in that subsection.

In contrast, *PPG Industries* states, as to an explicit five-year-future-performance warranty with accrual on discovery by statute, that such “warranty claims *accrue[] not upon initial delivery*, but when a reasonable buyer should have discovered any defects, up until the end of the five-year warranty period (when ‘the time of such performance’ expired).”<sup>849</sup> Thus, *PPG* makes clear that accrual of a cause of action in future-performance warranties occurs on discovery within, but not after, the warranty period.<sup>850</sup> If discovery is the event that causes the cause of action to accrue and limitations to commence to run in those particular cases, it makes sense for warranties that speak only at the time of delivery to accrue, once and for all, under the “accrual upon breach upon delivery” principle: discovery after year four, during year five, does not revive of action for which limitations has run.<sup>851</sup>

With extreme caution in light of the complexity of Texas law on the discovery rule and limitations and the opportunity for legislative changes, one final set of comments concerning shadows that may be cast over the discovery rule included in proposed § 2.725 may be helpful. First, as proposed § 2.725 calls statutorily for a particular and limited application of a discovery rule, the cases that address *whether* a discovery rule should apply to a case in the absence of statutory directive can be set aside.<sup>852</sup> It is worth noting, however, in the context of the discovery extension provision of proposed § 2.725(a) and the specific discovery provisions of proposed § 2.725(c)(3)-(4), that the discovery rule outside the UCC is described as “‘a very limited exception to statutes of limitations’ and [that its use is] condoned . . . only when the nature of the plaintiff’s injury is both inherently undiscoverable and objectively verifiable.”<sup>853</sup> This case law has now limited the more hospitable application of discovery rules seen in earlier cases where, in the absence of a discovery rule,

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849. *PPG Indus. Inc.*, 146 S.W.3d at 93. The court subsequently stated the converse: The five-year warranty “was breached upon delivery . . . (although it did not *accrue* until discovery within those five years).” *Id.* at 100.

850. *See id.* at 93.

851. *See* U.C.C. § 2-725 cmt. 2 (amended 2003), 1 U.L.A. 558 (2004). For a more extreme example of the consequences of limitations having run on a claim, see *Baker Hughes, Inc. v. Keco R & D, Inc.*, 12 S.W.3d 1, 4 (Tex. 1999): “In this connection, it is the settled law that, after a cause of action had become barred by the statute of limitation, the defendant has a vested right to rely on such statute as a defense.” *Id.* *Baker Hughes* refused to give retroactive effect to a statute taking effect after the trial but during its appeal that would have extended limitations to the benefit of the plaintiff. *See id.*

852. These cases, arising outside the UCC, recognize that the discovery rule “defers accrual of a cause of action until the plaintiff knew or, exercising reasonable diligence, should have known of the facts giving rise to the cause of action.” *Computer Assocs. Int’l Inc.*, 918 S.W.2d at 457. The case law in Texas allows a discovery rule to apply where fraud or concealment are alleged or, without the presence of fraud or concealment, “in certain limited circumstances . . . where the nature of the injury is inherently undiscoverable and the evidence of injury is objectively verifiable.” *Id.* at 456; *see also* *Wagner & Brown, Ltd. v. Horwood*, 58 S.W.3d 732 (Tex. 2001); *S.V. v. R.V.*, 933 S.W.2d 1 (Tex. 1996); *Diesel Fuel Injection Serv., Inc. v. Gabourel*, 893 S.W.2d 610, 612 (Tex. App.—Corpus Christi 1994, no writ).

853. *Wagner*, 58 S.W.3d at 734 (quoting *Computer Assocs. Int’l Inc.*, 918 S.W.2d at 455-56).

the plaintiff's claims might be barred by limitations before discovery of the claim itself.<sup>854</sup>

## 2. *The Accrual Rules: § 2.725(b)-(c)*

In a detailed sequence of provisions, § 2.725(b)-(c) sets out the accrual provisions for claims under Chapter 2. The sequence goes as follows:

(b) Except as otherwise provided in Subsection (c), the following rules apply:

(1) Except as otherwise provided in this subsection, a right of action for breach of a contract accrues when the breach occurs, even if the aggrieved party did not have knowledge of the breach.

(2) For breach of a contract by repudiation, a right of action accrues at the earlier of when the aggrieved party elects to treat the repudiation as a breach or when a commercially reasonable time for awaiting performance has expired.

(3) For breach of a remedial promise, a right of action accrues when the remedial promise is not performed when performance is due.

(4) In an action by a buyer against a person that is answerable over to the buyer for a claim asserted against the buyer, the buyer's right of action

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854. See Don R. Richards & Melba Herron Richards, Note, *The UCC Statute of Limitations' Conflict with the Equitable Rule of Discovery in Texas*, 15 TEX. TECH. L. REV. 417, 418 (1984) ("Texas courts historically have avoided this injustice [of a claim being barred by § 2.725's accrual on delivery rule, before discovery] by applying an equitable theory of law known as the 'discovery rule.'"). Both as to implied and express warranty (setting aside express future performance warranties), more recent Texas decisions have refused to apply the discovery rule, even if the claim may have accrued and become barred by limitations before discovery. See, e.g., *Am. Tobacco Co., Inc. v. Grinnell*, 951 S.W.2d 420, 435 (Tex. 1997) ("The four year statute of limitations on implied warranties began to run at the time of delivery [of cigarettes], not when Grinnell discovered he had cancer."); *Winters v. Diamond Shamrock Chem. Co.*, 941 F. Supp. 617 (E.D. Tex. 1996), *aff'd*, 149 F.3d 387 (5th Cir. 1998); *Safeway Stores Inc. v. Certainteed Corp.*, 710 S.W.2d 544, 546 (Tex. 1986) ("[T]hus, the statute of limitations on implied warranties runs from the date of sale."); *PPG Indus., Inc.*, 146 S.W.3d at 92 ("The UCC generally requires suit on breach of [express] warranty claims within four years of delivery, regardless of when the buyer discovers defects in the goods."); *Martinez v. Humble Sand & Gravel, Inc.*, 940 S.W.2d 139, 147 (Tex. App.—El Paso, 1996) ("Thus, Martinez' causes of action for breach of warranty, express or implied, accrued on the date the relevant products were delivered to Martinez' employer . . . . The discovery rule does not apply to claims based on breach of warranty." (citations omitted)), *aff'd*, 974 S.W.2d 31 (Tex. 1998). For an earlier case that applied a discovery rule to an implied warranty of "suitability" of caps used in bottling, see *Puretex Lemon Juice, Inc. v. S. Riekes & Sons*, 351 S.W.2d 119 (Tex. Civ. App.—San Antonio 1961, writ ref'd n.r.e.).

A suggested revision of § 2.725(a) of the 2007 Bill to clearly state the "no resurrection" position would read as follows:

Except as otherwise provided in this section, an action for breach of any contract for sale must be commenced within the later of (i) four years after the right of action has accrued under Subsection (b) or (c) or (ii) one year after the breach was or should have been discovered, but in no event, whether under clause (i) or clause (ii), later than five years after the right of action accrued, and clause (ii) shall apply only to a breach that first was or should have been discovered within four years after the right of action accrued.

against the person answerable over accrues at the time the claim was originally asserted against the buyer.

(c) If a breach of a warranty arising under Section 2.312, 2.313(b), 2.314, or 2.315, or a breach of an obligation, other than a remedial promise, arising under Section 2.313A, is claimed, the following rules apply:

(1) Except as otherwise provided in Subdivision (3), a right of action for breach of a warranty arising under Section 2.313(b), 2.314, or 2.315 accrues when the seller has tendered delivery to the immediate buyer, as defined in Section 2.313, and has completed performance of any agreed installation or assembly of the goods.

(2) Except as otherwise provided in Subdivision (3), a right of action for breach of an obligation, other than a remedial promise, arising under Section 2.313A accrues when the remote purchaser, as defined in Section 2.313A, receives the goods.

(3) If a warranty arising under Section 2.313(b) or an obligation, other than a remedial promise, arising under Section 2.313A explicitly extends to future performance of the goods and discovery of the breach must await the time for performance, the right of action accrues when the immediate buyer as defined in Section 2.313 or the remote purchaser as defined in Section 2.313A discovers or should have discovered the breach.

(4) A right of action for breach of warranty arising under Section 2.312 accrues when the aggrieved party discovers or should have discovered the breach. However, an action for breach of the warranty of noninfringement may not be commenced more than six years after tender of delivery of the goods to the aggrieved party.<sup>855</sup>

Finally subsections (d) and (e) provide for suits to be brought within six months after a timely suit is terminated (other than for voluntary dismissal or failure or neglect to prosecute) for preservation of tolling of limitations and for non-application to claims previously accrued.<sup>856</sup>

As before, the parties to the contract may, in their original agreement, reduce the limitation period to one year but may not extend the period.<sup>857</sup> In a consumer contract, however, the limitation period may not be reduced from the statutory period.<sup>858</sup>

Note that the final provision of § 2.725(c)(4) (“An action for breach of the warranty of noninfringement may not be commenced more than six years after tender of delivery of the goods to the aggrieved party”) would be construed as a “statute of repose.”<sup>859</sup> “Unlike traditional limitations provisions, which begin running upon accrual of a cause of action, a statute of repose runs from a

855. See *infra* app. I, § 2.725(b)-(c); see also U.C.C. § 2-725(2)-(3) (amended 2003), 1C U.L.A. 565-648 (2004); UNIF. COMPUTER INFO. TRANSACTIONS Act § 805 (amended 2002), 7.II U.L.A. 180-81 (Supp. 2008).

856. See *infra* app. I, § 2.725(d)-(e); see also U.C.C. § 2-725(4)-(5) (amended 2003), 1C U.L.A. 565-648 (2004).

857. See *infra* app. I, § 2.725.

858. See *infra* app. I, § 2.725(a).

859. *Infra* app. I, § 2.725(c)(4).

specified date without regard to accrual of any cause of action.”<sup>860</sup> This provision of § 2.725, dealing with a particularly complex area of intellectual property law, would be treated as “a fair balance between the legislative purpose of protecting against stale claims and the rights of litigants to obtain redress for injuries” and “rationally related” to legitimate state purposes.<sup>861</sup>

The Texas Subcommittee endorsed these amendments, finding them sensible and designed to clarify problems.<sup>862</sup> Although others are more reserved, the changes are useful and will bring the right issues to the foreground.<sup>863</sup> As with all of the Code and the 2007 Bill, these amendments mean parties “must choose their tools with care” and “draft appropriate contract language” to achieve desired results.<sup>864</sup>

#### IV. A TAILORED AND WORTHWHILE PROPOSAL

“Long and arduous” still applies to the efforts to amend Article 2 nationally and Chapter 2 in Texas. In practical, political terms, “the real problem for the revision of Article 2 is that there were no strong industrial or financial advocates of the statute.”<sup>865</sup> In public commentary, though, the advocates—principally the sponsoring associations, law professors, bar groups, and lawyers associated with those bar groups—have not succeeded in framing the public debate to favor adoption. The critics of the proposals have done better at finding and highlighting issues than the proponents have done in illustrating the improvements, not to mention that there may not be a succinct sound-bite summary of exactly how any particular amendment works. The easiest criticism to make, and one that attracts a supporting nod, is that the

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860. *Trinity River Auth. v. URS Consultants, Inc.*, 889 S.W.2d 259, 261 (Tex. 1994) (sustaining TEX. CIV. PRAC. & REM. CODE ANN. § 16.008 under various constitutional grounds). It is worth noting that *Trinity River Authority* reserved the question of constitutionality under an open courts challenge of a statute of repose as to a plaintiff who sustained damage *after* the period of repose. The particular plaintiff in *Trinity River Authority* was held to have sustained damage (to the structure that was improperly designed) upon the completion of the work, even though the damage was not immediately discovered or discoverable. *Id.* at 262-63. A thoroughly litigated “statute of repose” is that for architects, engineers, and persons constructing improvements to realty, codified in Texas at TEX. CIV. PRAC. & REM. CODE ANN. §§ 16.008-.009 (Vernon 2002). The history of that type of statute and its varying degrees of success when challenged are covered in E. Mabry Rogers, *The Constitutionality of Alabama’s Statute of Limitations for Construction Litigation: The Legislature Tries Again*, 11 CUMB. L. REV 1 (1980). See also *Trinity River Auth.*, 889 S.W.2d at 261.

861. *Trinity River Auth.*, 889 S.W.2d at 264-65.

862. See generally *infra* app. II.

863. See WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 128. Garvin is certainly reserved: “Amended Article Two does solve some of the problems discussed in this Article. . . . [But, there] is just time to finish the job—time to tinker with section 2-725 until it solves all of the problems created by current law, rather than solving a few at the cost of added complexity.” Garvin, *supra* note 670, at 395-99. This comment, of course, brings us full circle, if we recall the comments from Mr. Keeton noted by White & Summers: “Mr. Keeton became known for detailed, heavily footnoted critiques of every draft. These always concluded with a denunciation of the committee’s ‘needless tinkering.’” WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 50.

864. WHITE & SUMMERS, SUPPLEMENT, *supra* note 2, at 128

865. White, *supra* note 709, at 521.

amendments will limit freedom of contract, a foundation of a free market economy that cannot be imperiled. On examination of amended § 2-207, however, the opposite is the case. As under present rules, that section is clear: Terms the parties actually agree on are included. What changes is whether unwanted and unread terms come into a contract; the amendments make that less likely. The increasing use of a knock out rule in cases of contracts with differing terms in exchanged documents, and its application under current § 2.207(c), suggests that the proposed amendments to § 2.207 would not undermine actual freedom of contract.

The review here of only some of the amendments, admittedly incomplete, shows that the 2003 Amendments and the 2007 Bill deserve an actual and detailed hearing on the merits, as the amendments do good things in the main. As part of the Texas Subcommittee's efforts, the co-chairmen and participating committee members have consistently taken time to confer with critics of the legislation. As seen in the Bill Analysis and summary of "National Provisions Not Included in the 2007 Bill" at the beginning of this Article, the Texas Subcommittee has deleted provisions that "don't make sense" for Texas and has made alterations to the pre-cut provisions of the statute so it will fit Texas well. If a house or senate sponsor of the 2007 Bill were to introduce it at a committee hearing or on the floor of the legislature, the sponsor could fairly start with the traditional statement endorsing the legislation, "Members, this is a good bill."

APPENDIX I: BILL DRAFT<sup>866</sup>**AN ACT**

Relating to uniform law on sales, leases and certain other transactions in goods.  
BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF TEXAS:

SECTION 1: Section 2.103, Business & Commerce Code, is amended to read as follows:

Sec. 2.103. Definitions and Index of Definitions

(a) In this chapter unless the context otherwise requires

(1) “Buyer” means a person ~~who~~ that buys or contracts to buy goods.

(2) ~~Reserved.~~ “Conspicuous,” with reference to a term, means so written, displayed, or presented that a reasonable person against which it is to operate ought to have noticed it. A term in an electronic record intended to evoke a response by an electronic agent is conspicuous if it is presented in a form that would enable a reasonably configured electronic agent to take it into account or react to it without review of the record by an individual. Whether a term is “conspicuous” or not is a decision for the court. Conspicuous terms include the following:

(A) for a person:

(i) a heading in capitals equal to or greater in size than the surrounding text, or in contrasting type, font, or color to the surrounding text of the same or lesser size; and

(ii) language in the body of a record or display in larger type than the surrounding text, or in contrasting type, font, or color to the surrounding text of the same size, or set off from surrounding text of the same size by symbols or other marks that call attention to the language; and

(B) for a person or an electronic agent, a term that is so placed in a record or display that the person or electronic agent may not proceed without taking action with respect to the particular term.

(3) ~~Reserved.~~

(4) “Consumer contract” means a contract between a merchant seller and a consumer.

(5) “Delivery” means the voluntary transfer of physical possession or control of goods.

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866. W. David East, Professor of Law and Director of the Transactional Practice Center at South Texas College of Law, prepared this draft on January 5, 2007, for a subcommittee of the Commercial Code Committee of the State Bar of Texas’s Business Law Section. See e-mail from W. David East to author (Jan. 5, 2007) (on file with author). The *Texas Tech Law Review* has incorporated one additional change to § 123 based on a subsequent revision by the subcommittee. See e-mail from Wendy B. Johnston to author (Feb. 1, 2007) (on file with author).

(6) “Electronic” means relating to technology having electrical, digital, magnetic, wireless, optical, electromagnetic, or similar capabilities.

(7) “Electronic agent” means a computer program or an electronic or other automated means used independently to initiate an action or respond to electronic records or performances in whole or in part, without review or action by an individual.

(8) “Electronic record” means a record created, generated, sent, communicated, received, or stored by electronic means.

(9) “Foreign exchange transaction” means a transaction in which one party agrees to deliver a quantity of a specified money or unit of account in consideration of the other party’s agreement to deliver another quantity of a different money or unit of account either currently or at a future date, and in which delivery is to be through funds transfer, book entry accounting, or other form of payment order, or other agreed means to transfer a credit balance. The term includes a transaction of this type involving two or more moneys and spot, forward, option, or other products derived from underlying moneys and any combination of these transactions. The term does not include a transaction involving two or more moneys in which one or both of the parties is obligated to make physical delivery, at the time of contracting or in the future, of banknotes, coins, or other form of legal tender or specie.

(10) Reserved.

(11) “Goods” means all things that are movable at the time of identification to a contract for sale. The term includes future goods, specially manufactured goods, the unborn young of animals, growing crops, and other identified things attached to the realty as described in Section 2.107. The term does not include the money in which the price is to be paid, investment securities under Chapter 8, the subject matter of foreign exchange transactions, or choses in action.

(12) “Receipt” of goods means taking physical possession of them.

(13) Reserved.

(14) “Remedial promise” means a promise by the seller to repair or replace goods or to refund all or part of the price of goods upon the happening of a specified event.

(15) “Seller” means a person who that sells or contracts to sell goods.

(16) “Sign” means, with present intent to authenticate or adopt a record:

(A) to execute or adopt a tangible symbol; or

(B) to attach to or logically associate with the record an electronic sound, symbol, or process.

(b) Other definitions applying to this chapter or to specified subchapters thereof, and the sections in which they appear are:

“Acceptance”. Section 2.606.

“Banker’s credit”. Section 2.325.

“Between merchants”. Section 2.104.  
 “Cancellation”. Section 2.106(d).  
 “Commercial unit”. Section 2.105.  
~~“Confirmed credit”. Section 2.325.~~  
 “Conforming to contract”. Section 2.106.  
 “Contract for sale”. Section 2.106.  
 “Cover”. Section 2.712.  
 “Entrusting”. Section 2.403.  
 “Financing agency”. Section 2.104.  
 “Future goods”. Section 2.105.  
 “Goods”. Section 2.103 ~~2.105~~.  
 “Identification”. Section 2.501.  
 “Installment contract”. Section 2.612.  
~~“Letter of credit”. Section 2.325.~~  
 “Lot”. Section 2.105.  
 “Merchant”. Section 2.104.  
~~“Overseas”. Section 2.323.~~  
 “Person in position of seller”. Section 2.707.  
 “Present sale”. Section 2.106.  
 “Sale”. Section 2.106.  
 “Sale on approval”. Section 2.326.  
 “Sale or return”. Section 2.326.  
 “Termination”. Section 2.106.

(c) The following definitions in other chapters apply to this chapter:

“Check”. Section 3.104.  
 “Consignee”. Section 7.102.  
 “Consignor”. Section 7.102.  
 “Consumer goods”. Section 9.102.  
 “Control”. Section 7.106.  
 “Dishonor”. Section 3.502.  
 “Draft”. Section 3.104.  
“Honor”. Section 5.102.  
“Injunction against honor”. Section 5.109.  
“Letter of credit”. Section 5.102.

(d) In addition Chapter 1 contains general definitions and principles of construction and interpretation applicable throughout this chapter.

SECTION 2: Section 2.104, Business & Commerce Code, is amended to read as follows:

Sec. 2.104. Definitions: “Merchant”; “Between Merchants”; “Financing Agency”

(a) “Merchant” means a person ~~who~~ that deals in goods of the kind or otherwise ~~by his occupation holds himself out~~ holds itself out by occupation as having knowledge or skill peculiar to the practices or goods involved in the transaction or to ~~whom~~ which ~~such~~ the knowledge or skill may be attributed by

his the person's employment of an agent or broker or other intermediary ~~who by his occupation holds himself out~~ that holds itself out by occupation as having ~~such~~ the knowledge or skill.

(b) "Financing agency" means a bank, finance company or other person ~~who~~ that in the ordinary course of business makes advances against goods or documents of title or ~~who~~ that by arrangement with either the seller or the buyer intervenes in ordinary course to make or collect payment due or claimed under the contract for sale, as by purchasing or paying the seller's draft or making advances against it or by merely taking it for collection whether or not documents of title accompany or are associated with the draft. "~~Financing agency~~" The term includes also a bank or other person ~~who~~ that similarly intervenes between persons ~~who~~ that are in the position of seller and buyer in respect to the goods (Section 2.707).

(c) "Between merchants" means in any transaction with respect to which both parties are chargeable with the knowledge or skill of merchants.

SECTION 3. Section 2.105, Business & Commerce Code, is amended to read as follows:

Sec. 2.105. Definitions: Transferability; "~~Goods~~"; "Future" Goods; "Lot"; "Commercial Unit"

(a) "~~Goods~~" means 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. "Goods" also includes the unborn young of animals and growing crops and other identified things attached to realty as described in the section on goods to be severed from realty (Section 2.107).~~

(~~b~~) (a) Goods must be both existing and identified before any interest in them ~~can~~ may pass. Goods ~~which~~ that are not both existing and identified are "future" goods. A purported present sale of future goods or of any interest therein operates as a contract to sell.

(~~c~~) (b) There may be a sale of a part interest in existing identified goods.

(~~d~~) (c) An undivided share in an identified bulk of fungible goods is sufficiently identified to be sold although the quantity of the bulk is not determined. Any agreed proportion of ~~such a~~ the bulk or any quantity thereof agreed upon by number, weight, or other measure may to the extent of the seller's interest in the bulk be sold to the buyer ~~who~~ that then becomes an owner in common.

(~~e~~) (d) "Lot" means a parcel or a single article which is the subject matter of a separate sale or delivery, whether or not it is sufficient to perform the contract.

(~~f~~) (e) "Commercial unit" means such a unit of goods as by commercial usage is a single whole for purposes of sale and division of which materially impairs its character or value on the market or in use. A commercial unit may be a single article (as a machine) or a set of articles (as a suite of furniture or an

assortment of sizes) or a quantity (as a bale, gross, or carload) or any other unit treated in use or in the relevant market as a single whole.

SECTION 4. Section 2.108 is added to the Business & Commerce Code, to read as follows:

Sec. 2.108. Transactions Subject to Other Law

(a) A transaction subject to this chapter is also subject to any applicable:

(1) certificate of title statute of this state, including Chapter 501, Transportation Code, relating to the certificates of title for motor vehicles; Chapter 31, Parks and Wildlife Code, relating to the certificates of title for vessels and outboard motors; Chapter 1201, Occupations Code, relating to the documents of title for manufactured homes, except with respect to the rights of a buyer in ordinary course of business under Section 2.403(b) which arise before a certificate of title covering the goods is effective in the name of any other buyer;

(2) rule of law that establishes a different rule for consumers; or

(3) statute of this state applicable to the transaction, such as a statute dealing with:

(A) the sale or lease of agricultural products;

(B) the transfer of human blood, blood products, tissues, or parts;

(C) the consignment or transfer by artists of works of art or fine prints;

(D) distribution agreements, franchises, and other relationships through which goods are sold;

(E) the misbranding or adulteration of food products or drugs; and

(F) dealers in particular products, such as automobiles, motorized wheelchairs, agricultural equipment, and hearing aids.

(b) Except for the rights of a buyer in ordinary course of business under Subsection (a)(1), in the event of a conflict between this chapter and a law referred to in Subsection (a), that law governs.

(c) For purposes of this chapter, failure to comply with a law referred to in Subsection (a) has only the effect specified in that law.

(d) This chapter modifies, limits, and supersedes the federal Electronic Signatures in Global and National Commerce Act, 15 U.S.C. Section 7001 et seq., except that nothing in this chapter modifies, limits, or supersedes Section 7001(c) of that Act or authorizes electronic delivery of any of the notices described in Section 7003(b) of that Act.

SECTION 5. Section 2.201, Business & Commerce Code, is amended to read as follows:

Sec. 2.201. Formal Requirements; Statute of Frauds

~~(a) Except as otherwise provided in this section a~~ (a) A contract for the sale of goods for the price of ~~\$500~~ \$5,000 or more is not enforceable by way of action or defense unless there is some ~~writing~~ writing record sufficient to indicate that a

contract for sale has been made between the parties and signed by the party against ~~whom~~ which enforcement is sought or by ~~his~~ the party's authorized agent or broker. A writing record is not insufficient because it omits or incorrectly states a term agreed upon, but the contract is not enforceable under this ~~paragraph~~ subsection beyond the quantity of goods shown in ~~such~~ the writing record.

(b) Between merchants if within a reasonable time a writing record 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~~ the recipient unless ~~written~~ notice of objection to its contents is given in a record within 10 days after it is received.

(c) A contract ~~which that~~ does not satisfy the requirements of Subsection (a) but which is valid in other respects is enforceable:

(1) if the goods are to be specially manufactured for the buyer and are not suitable for sale to others in the ordinary course of the seller's business and the seller, before notice of repudiation is received and under circumstances ~~which that~~ reasonably indicate that the goods are for the buyer, has made either a substantial beginning of their manufacture or commitments for their procurement; ~~or~~

(2) if the party against ~~whom~~ which enforcement is sought admits in ~~his~~ the party's pleading, or in the party's testimony or otherwise ~~in court~~ under oath that a contract for sale was made, but the contract is not enforceable under this ~~provision~~ paragraph beyond the quantity of goods admitted; or

(3) with respect to goods for which payment has been made and accepted or which have been received and accepted (Section 2.606).

(d) A contract that is enforceable under this section is not unenforceable merely because it is not capable of being performed within one year or any other period after its making.

SECTION 6. Section 2.202, Business & Commerce Code, is amended to read as follows:

Section 2.202. Final ~~Written~~ Expression in a Record: Parol or Extrinsic Evidence

(a) Terms with respect to which the confirmatory ~~memoranda~~ records of the parties agree or which are otherwise set forth in a writing record intended by the parties as a final expression of their agreement with respect to such terms as are included therein may not be contradicted by evidence of any prior agreement or of a contemporaneous oral agreement but may be ~~explained or~~ supplemented by evidence of:

(1) ~~by~~ course of performance, course of dealing, or usage of trade (Section 1.303); and

(2) ~~by evidence of~~ consistent additional terms unless the court finds the writing record to have been intended also as a complete and exclusive statement of the terms of the agreement.

(b) Terms in a record may be explained by evidence of course of performance, course of dealing, or usage of trade without a preliminary determination by the court that the language used is ambiguous.

SECTION 7. Section 2.203, Business & Commerce Code, is amended to read as follows:

Sec. 2.203. Seals Inoperative

The affixing of a seal to a ~~writing record~~ evidencing a contract for sale or an offer to buy or sell goods does not constitute the ~~writing record~~ a sealed ~~instrument and the instrument~~. The law with respect to sealed instruments does not apply to such a contract or offer.

SECTION 8. Section 2.204, Business & Commerce Code, is amended to read as follows:

Sec. 2.204. Formation in General

(a) A contract for sale of goods may be made in any manner sufficient to show agreement, including

(1) offer and acceptance,

(2) conduct by both parties which recognizes the existence of such a contract,

(3) the interaction of electronic agents, and

(4) the interaction of an electronic agent and an individual.

(b) An agreement sufficient to constitute a contract for sale may be found even ~~though~~ if the moment of its making is undetermined.

(c) Even ~~though~~ if one or more terms are left open, a contract for sale does not fail for indefiniteness if the parties have intended to make a contract and there is a reasonably certain basis for giving an appropriate remedy.

SECTION 9. Section 2.205, Business & Commerce Code, is amended to read as follows:

Sec. 2.205. Firm Offers

An offer by a merchant to buy or sell goods in a signed ~~writing which record that~~ by its terms gives assurance that it will be held open is not revocable, for lack of consideration, during the time stated or if no time is stated for a reasonable time, but in no event may ~~such the~~ period of irrevocability exceed three ~~months, but any~~ months. Any such term of assurance ~~on a form in a form~~ supplied by the offeree must be separately signed by the offeror.

SECTION 10. Section 2.206, Business & Commerce Code, is amended to read as follows:

Sec. 2.206. Offer and Acceptance in Formation of Contract

(a) Unless otherwise unambiguously indicated by the language or circumstances;

(1) an offer to make a contract shall be construed as inviting acceptance in any manner and by any medium reasonable in the circumstances;

(2) an order or other offer to buy goods for prompt or current shipment shall be construed as inviting acceptance either by a prompt promise to ship or by the prompt or current shipment of conforming or ~~non-conforming~~

~~nonconforming~~ goods, but ~~such a the~~ shipment of ~~non-conforming~~ ~~nonconforming~~ goods ~~does not constitute~~ is not an acceptance if the seller seasonably notifies the buyer that the shipment is offered only as an accommodation to the buyer.

(b) ~~Where~~ If the beginning of a requested performance is a reasonable mode of acceptance, an offeror ~~who~~ that is not notified of acceptance within a reasonable time may treat the offer as having lapsed before acceptance.

(c) A definite and seasonable expression of acceptance in a record operates as an acceptance even if it contains terms additional to or different from the offer, unless acceptance is expressly made conditional on assent to the additional or different terms.

SECTION 11. Section 2.207, Business & Commerce Code, is amended to read as follows:

Sec. 2.207. Additional Terms in Acceptance or Confirmation—Terms of Contract; Effect of Confirmation

Subject to Section 2.202, if a contract is [i] formed in any manner permitted by this chapter, or [ii] confirmed by a record that contains terms additional to or different from those in the contract being confirmed, the terms of the contract are:

- (1) terms that appear in the records of both parties;
- (2) terms, whether in a record or not, to which both parties agree; and
- (3) terms supplied or incorporated under any provision of this chapter.

~~(a) A definite and seasonable expression of acceptance or a written confirmation which is sent within a reasonable time operates as an acceptance even though it states terms additional to or different from those offered or agreed upon, unless acceptance is expressly made conditional on assent to the additional or different terms.~~

~~(b) The additional terms are to be construed as proposals for addition to the contract. Between merchants such terms become part of the contract unless:~~

- ~~(1) the offer expressly limits acceptance to the terms of the offer;~~
- ~~(2) they materially alter it; or~~
- ~~(3) notification of objection to them has already been given or is~~

~~given within a reasonable time after notice of them is received.~~

~~(c) Conduct by both parties which recognizes the existence of a contract is sufficient to establish a contract for sale although the writings of the parties do not otherwise establish a contract. In such case the terms of the particular contract consist of those terms on which the writings of the parties agree, together with any supplementary terms incorporated under any other provisions of this title.~~

SECTION 12. Section 2.208, Business & Commerce Code, is added to read as follows:

Sec. 2.208. Reserved

SECTION 13. Section 2.209, Business & Commerce Code, is amended to read as follows:

## Sec. 2.209. Modification, Rescission and Waiver

(a) An agreement modifying a contract within this chapter needs no consideration to be binding.

(b) ~~A signed agreement~~ An agreement in a signed record which excludes modification or rescission except by a signed ~~writing cannot~~ record may not be otherwise modified or rescinded, but except as between merchants such a requirement ~~on a form in a form~~ supplied by the merchant must be separately signed by the other party.

(c) The requirements of ~~the statute of frauds section of this chapter (Section 2.201)~~ Section 2.201 must be satisfied if the contract as modified is within its provisions.

(d) Although an attempt at modification or rescission does not satisfy the requirements of Subsection (b) or (c), it ~~can~~ may operate as a waiver.

(e) A party ~~who~~ that has made a waiver affecting an executory portion of ~~the~~ a contract may retract the waiver by reasonable notification received by the other party that strict performance will be required of any term waived, unless the retraction would be unjust in view of a material change of position in reliance on the waiver.

SECTION 14. Section 2.210, Business & Commerce Code, is amended to read as follows:

## Sec. 2.210. Delegation of Performance; Assignment of Rights

(a) If the seller or buyer assigns rights under a contract, the following rules apply:

(1) Subject to Subdivision (2) and except as otherwise provided in Section 9.406 or as otherwise agreed, all rights of the seller or the buyer may be assigned unless the assignment would materially change the duty of the other party, increase materially the burden or risk imposed on that party by the contract, or impair materially that party's chance of obtaining return performance. A right to damages for breach of the whole contract or a right arising out of the assignor's due performance of its entire obligation may be assigned despite an agreement otherwise.

(2) The creation, attachment, perfection, or enforcement of a security interest in the seller's interest under a contract is not an assignment that materially changes the duty of or materially increases the burden or risk imposed on the buyer or materially impairs the buyer's chance of obtaining return performance under Subdivision (1) unless, and only to the extent that, enforcement of the security interest results in a delegation of a material performance of the seller. Even in that event, the creation, attachment, perfection, and enforcement of the security interest remain effective. However, the seller is liable to the buyer for damages caused by the delegation to the extent that the damages could not reasonably be prevented by the buyer, and a court may grant other appropriate relief, including cancellation of the contract or an injunction against enforcement of the security interest or consummation of the enforcement.

(b) If the seller or buyer delegates performance of its duties under a contract, the following rules apply:

(1) A party may perform its duties through a delegate unless otherwise agreed or unless the other party has a substantial interest in having the original promisor perform or control the acts required by the contract. Delegation of performance does not relieve the delegating party of any duty to perform or liability for breach.

(2) Acceptance of a delegation of duties by the assignee constitutes a promise to perform those duties. The promise is enforceable by either the assignor or the other party to the original contract.

(3) The other party may treat any delegation of duties as creating reasonable grounds for insecurity and may without prejudice to its rights against the assignor demand assurances from the assignee under Section 2.609.

(4) A contractual term prohibiting the delegation of duties otherwise delegable under Subsection (a) is enforceable, and an attempted delegation is not effective.

(c) An assignment of "the contract" or of "all my rights under the contract" or an assignment in similar general terms is an assignment of rights and unless the language or the circumstances, as in an assignment for security, indicate the contrary, it is also a delegation of performance of the duties of the assignor.

(d) Unless the circumstances indicate the contrary, a prohibition of assignment of "the contract" is to be construed as barring only the delegation to the assignee of the assignor's performance.

~~(a) A party may perform his duty through a delegate unless otherwise agreed or unless the other party has a substantial interest in having his original promisor perform or control the acts required by the contract. No delegation of performance relieves the party delegating of any duty to perform or any liability for breach.~~

~~(b) Unless otherwise agreed all rights of either seller or buyer can be assigned except where the assignment would materially change the duty of the other party, or increase materially the burden or risk imposed on him by his contract, or impair materially his chance of obtaining return performance. A right to damages for breach of the whole contract or a right arising out of the assignor's due performance of his entire obligation can be assigned despite agreement otherwise.~~

~~(c) The creation, attachment, perfection, or enforcement of a security interest in the seller's interest under a contract is not a transfer that materially changes the duty of or increases materially the burden or risk imposed on the buyer or impairs materially the buyer's chance of obtaining return performance within the purview of Subsection (b) unless, and then only to the extent that, enforcement actually results in a delegation of material performance of the seller. Even in that event, the creation, attachment, perfection, and enforcement of the security interest remain effective, but (i) the seller is liable to the buyer~~

for damages caused by the delegation to the extent that the damages could not reasonably be prevented by the buyer, and (ii) a court having jurisdiction may grant other appropriate relief, including cancellation of the contract for sale or an injunction against enforcement of the security interest or consummation of the enforcement.

~~(d) Unless the circumstances indicate the contrary a prohibition of assignment of "the contract" is to be construed as barring only the delegation to the assignee of the assignor's performance.~~

~~(e) An assignment of "the contract" or of "all my rights under the contract" or an assignment in similar general terms is an assignment of rights and unless the language or the circumstances (as in an assignment for security) indicate the contrary, it is a delegation of performance of the duties of the assignor and its acceptance by the assignee constitutes a promise by him to perform those duties. This promise is enforceable by either the assignor or the other party to the original contract.~~

~~(f) The other party may treat any assignment which delegates performance as creating reasonable grounds for insecurity and may without prejudice to his rights against the assignor demand assurances from the assignee (Section 2.609).~~

SECTION 15. Section 2.302, Business & Commerce Code, is amended to read as follows:

Sec. 2.302. Unconscionable Contract or Clause Term

(a) If the court as a matter of law finds the contract or any clause term of the contract to have been unconscionable at the time it was made, the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable clause term, or it may so limit the application of any unconscionable clause term as to avoid any unconscionable result.

~~(b) When~~ If it is claimed or appears to the court that the contract or any clause term thereof may be unconscionable, the parties shall be afforded a reasonable opportunity to present evidence as to its commercial setting, purpose, and effect to aid the court in making the determination.

SECTION 16. Section 2.304, Business & Commerce Code, is amended to read as follows:

Sec. 2.304. Price Payable in Money, Goods, Realty, or Otherwise

(a) The price ~~can~~ may be made payable in money or otherwise. If it is payable in whole or in part in goods, each party is a seller of the goods ~~which he~~ that the party is to transfer.

(b) Even ~~though~~ if all or part of the price is payable in an interest in ~~realty~~ real property the transfer of the goods, and the seller's obligations with reference to them, are subject to this chapter, but not the transfer of the interest in ~~realty~~ real property or the transferor's obligations in connection therewith.

SECTION 17. Section 2.305, Business & Commerce Code, is amended to read as follows:

Sec. 2.305. Open Price Term

(a) The parties if they so intend ~~can~~ may conclude a contract for sale even ~~though~~ if the price is not settled. In such a case the price is a reasonable price at the time for delivery if:

- (1) nothing is said as to price; ~~or~~
- (2) the price is left to be agreed by the parties and they fail to agree;

or

(3) the price is to be fixed in terms of some agreed market or other standard as set or recorded by a third person or agency and it is not so set or recorded.

(b) A price to be fixed by the seller or by the buyer means a price ~~for him to fix~~ to be fixed in good faith.

(c) ~~When~~ If a price left to be fixed otherwise than by agreement of the parties fails to be fixed through fault of one party, the other may at ~~his~~ the party's option treat the contract as canceled or ~~himself~~ the party may fix a reasonable price.

(d) ~~Where~~ If, however, the parties intend not to be bound unless the price ~~be is~~ is fixed or agreed and it is not fixed or agreed, there is no contract. In such a case the buyer must return any goods already received or if unable ~~so~~ to do so must pay their reasonable value at the time of delivery and the seller must return any portion of the price paid on account.

SECTION 18. Section 2.308, Business & Commerce Code, is amended to read as follows:

Sec. 2.308. Absence of Specified Place for Delivery

Unless otherwise agreed:

(1) the place for delivery of goods is the seller's place of business or if ~~he has~~ none, his the seller's residence; but

(2) in a contract for sale of identified goods ~~which~~ that to the knowledge of the parties at the time of contracting are in some other place, that place is the place for their delivery; and

(3) documents of title may be delivered through customary banking channels.

SECTION 19. Section 2.309, Business & Commerce Code, is amended to read as follows:

Sec. 2.309. Absence of Specific Time Provisions; Notice of Termination

(a) The time for shipment or delivery or any other action under a contract if not provided in this chapter or agreed upon shall be a reasonable time.

(b) ~~Where~~ If the contract provides for successive performances but is indefinite in duration, it is valid for a reasonable time but unless otherwise agreed may be terminated at any time by either party.

(c) Termination of a contract by one party except on the happening of an agreed event requires that reasonable notification be received by the other party and an agreement dispensing with notification is invalid if its operation would be unconscionable. A term specifying standards for the nature and timing of notice is enforceable if the standards are not manifestly unreasonable.

SECTION 20. Section 2.310, Business & Commerce Code, is amended to read as follows:

Sec. 2.310. Open Time for Payment or Running of Credit; Authority to Ship Under Reservation

Unless otherwise agreed:

(1) payment is due at the time and place at which the buyer is to receive the goods even though the place of shipment is the place of delivery; ~~and~~

(2) if the seller is required or authorized to send the goods, ~~he the~~ seller may ship them under reservation, and may tender the documents of title, but the buyer may inspect the goods after their arrival before payment is due unless ~~such the~~ the inspection is inconsistent with the terms of the contract (Section 2.513); ~~and~~

(3) if tender of delivery is ~~authorized and~~ agreed to be made by way of documents of title otherwise than by Subdivision (2), then payment is due regardless of where the goods are to be received:

(A) at the time and place at which the buyer is to receive delivery of the tangible documents; or

(B) at the time the buyer is to receive delivery of the electronic documents and at the seller's place of business or if none, the seller's residence; and

(4) ~~where~~ if the seller is required or authorized to ship the goods on credit, the credit period runs from the time of shipment but ~~post-dating~~ postdating the invoice or delaying its dispatch will correspondingly delay the starting of the credit period.

SECTION 21. Section 2.311, Business & Commerce Code, is amended to read as follows:

Sec. 2.311. Options and Cooperation Respecting Performance

(a) An agreement for sale which is otherwise sufficiently definite ~~(Subsection (e) of Section 2.204)~~ (Section 2.204(c)) to be a contract is not made invalid by the fact that it leaves particulars of performance to be specified by one of the parties. Any such specification must be made in good faith and within limits set by commercial reasonableness.

(b) Unless otherwise agreed, specifications relating to assortment of the goods are at the buyer's option and ~~except as otherwise provided in Subsections (a)(3) and (e) of Section 2.319~~ specifications or arrangements relating to shipment are at the seller's option.

(c) ~~Where such~~ If the specification would materially affect the other party's performance but is not seasonably made or ~~where~~ if one party's cooperation is necessary to the agreed performance of the other but is not seasonably forthcoming, the other party in addition to all other remedies:

(1) is excused for any resulting delay in ~~his own~~ that party's performance; and

(2) may also either proceed to perform in any reasonable manner or after the time for a material part of ~~his~~ that party's own performance treat the failure to specify or to cooperate as a breach by failure to deliver or accept the goods.

SECTION 22. Section 2.312, Business & Commerce Code, is amended to read as follows:

Sec. 2.312. Warranty of Title and Against Infringement; Buyer's Obligation Against Infringement

(a) Subject to Subsection ~~(b)~~(c), there is in a contract for sale a warranty by the seller that:

(1) the title conveyed shall be ~~good~~, good and its transfer rightful and shall not unreasonably expose the buyer to litigation because of any colorable claim to or interest in the goods; and

(2) the goods shall be delivered free from any security interest or other lien or encumbrance of which the buyer at the time of contracting has no knowledge.

(b) Unless otherwise agreed, a seller that is a merchant regularly dealing in goods of the kind warrants that the goods shall be delivered free of the rightful claim of any third person by way of infringement or the like but a buyer that furnishes specifications to the seller must hold the seller harmless against any such claim that arises out of compliance with the specifications.

(c) A warranty under this section may be disclaimed or modified only by specific language or by circumstances that give the buyer reason to know that the seller does not claim title, that the seller is purporting to sell only the right or title as the seller or a third person may have, or that the seller is selling subject to any claims of infringement or the like.

~~(b) A warranty under Subsection (a) will be excluded or modified only by specific language or by circumstances which give the buyer reason to know that the person selling does not claim title in himself or that he is purporting to sell only such right or title as he or a third person may have.~~

~~(c) Unless otherwise agreed a seller who is a merchant regularly dealing in goods of the kind warrants that the goods shall be delivered free of the rightful claim of any third person by way of infringement or the like but a buyer who furnishes specifications to the seller must hold the seller harmless against any such claim which arises out of compliance with the specifications.~~

SECTION 23. Section 2.313, Business & Commerce Code, is amended to read as follows:

Sec. 2.313. Express Warranties by Affirmation, Promise, Description, Sample; Remedial Promise

(a) In this section, "immediate buyer" means a buyer that enters into a contract with the seller.

~~(a)~~ (b) Express warranties by the seller to the immediate buyer are created as follows:

(1) Any affirmation of fact or promise made by the seller ~~that to the buyer which~~ relates to the goods and becomes part of the basis of the bargain creates an express warranty that the goods shall conform to the affirmation or promise.

(2) Any description of the goods ~~that which~~ is made part of the basis of the bargain creates an express warranty that the goods shall conform to the description.

(3) Any sample or model ~~that which~~ is made part of the basis of the bargain creates an express warranty that the whole of the goods shall conform to the sample or model.

~~(b)~~ (c) It is not necessary to the creation of an express warranty that the seller use formal words such as “warrant” or “guarantee” or that ~~he~~ the seller have a specific intention to make a warranty, but an affirmation merely of the value of the goods or a statement purporting to be merely the seller’s opinion or commendation of the goods does not create a warranty.

(d) Any remedial promise made by the seller to the immediate buyer creates an obligation that the promise will be performed upon the happening of the specified event.

SECTION 24. Section 2.313A is added to the Business & Commerce Code, to read as follows:

Sec. 2.313A. Obligation to Remote Purchaser Created by Record Packaged With or Accompanying Goods

(a) In this section:

(1) “Immediate buyer” means a buyer that enters into a contract with the seller.

(2) “Remote purchaser” means a person that buys or leases goods from an immediate buyer or other person in the normal chain of distribution.

(b) This section applies only to new goods and goods sold or leased as new goods in a transaction of purchase in the normal chain of distribution.

(c) If in a record packaged with or accompanying the goods the seller makes an affirmation of fact or promise that relates to the goods, provides a description that relates to the goods, or makes a remedial promise, and the seller reasonably expects the record to be, and the record is, furnished to the remote purchaser, the seller has an obligation to the remote purchaser that:

(1) the goods will conform to the affirmation of fact, promise, or description unless a reasonable person in the position of the remote purchaser would not believe that the affirmation of fact, promise, or description created an obligation; and

(2) the seller will perform the remedial promise.

(d) It is not necessary to the creation of an obligation under this section that the seller use formal words such as “warrant” or “guarantee” or that the seller have a specific intention to undertake an obligation, but an affirmation merely of the value of the goods or a statement purporting to be merely the seller’s opinion or commendation of the goods does not create an obligation.

(e) The following rules apply to the remedies for breach of an obligation created under this section:

(1) The seller may modify or limit the remedies available to the remote purchaser if the modification or limitation is furnished to the remote purchaser no later than the time of purchase or if the modification or limitation is contained in the record that contains the affirmation of fact, promise, or description.

(2) Subject to a modification or limitation of remedy, a seller in breach is liable for incidental or consequential damages under Section 2.715, but not for lost profits.

(3) The remote purchaser may recover as damages for breach of a seller's obligation arising under Subsection (c) the loss resulting in the ordinary course of events as determined in any reasonable manner.

(f) An obligation that is not a remedial promise is breached if the goods did not conform to the affirmation of fact, promise, or description creating the obligation when the goods left the seller's control.

(g) Whether a remote purchaser may maintain a cause of action for breach of warranty or remedial promise under circumstances other than as provided by this section is left to determination by the courts (Section 2.318).

SECTION 25. Section 2.314, Business & Commerce Code, is amended to read as follows:

Sec. 2.314. Implied Warranty: Merchantability; Usage of Trade

(a) Unless excluded or modified (Section 2.316), a warranty that the goods shall be merchantable is implied in a contract for their sale if the seller is a merchant with respect to goods of that kind. Under this section the serving for value of food or drink to be consumed either on the premises or elsewhere is a sale.

(b) Goods to be merchantable must be at least such as:

(1) pass without objection in the trade under the contract description; ~~and~~

(2) in the case of fungible goods, are of fair average quality within the description; ~~and~~

(3) are fit for the ordinary purposes for which ~~such~~ goods of that description are used; ~~and~~

(4) run, within the variations permitted by the agreement, of even kind, quality and quantity within each unit and among all units involved; ~~and~~

(5) are adequately contained, packaged, and labeled as the agreement may require; and

(6) conform to the promise or affirmations of fact made on the container or label if any.

(c) Unless excluded or modified (Section 2.316) other implied warranties may arise from course of dealing or usage of trade.

SECTION 26. Section 2.316, Business & Commerce Code, is amended to read as follows:

## Sec. 2.316. Exclusion or Modification of Warranties

(a) Words or conduct relevant to the creation of an express warranty and words or conduct tending to negate or limit warranty shall be construed wherever reasonable as consistent with each other; but subject to ~~the provisions of this chapter on parol or extrinsic evidence (Section 2.202)~~ Section 2.202, negation or limitation is inoperative to the extent that such construction is unreasonable.

(b) Subject to Subsection (c), to exclude or modify the implied warranty of merchantability or any part of it in a consumer contract the language must be in a record, be conspicuous, and state “The seller undertakes no responsibility for the quality of the goods except as otherwise provided in this contract,” and in any other contract the language must mention merchantability and in case of a writing record must be conspicuous, and to. Subject to Subsection (c), to exclude or modify the implied warranty of fitness, the exclusion must be ~~by a writing~~ in a record and be conspicuous. Language to exclude all implied warranties of fitness in a consumer contract must state “The seller assumes no responsibility that the goods will be fit for any particular purpose for which you may be buying these goods, except as otherwise provided in the contract,” and in any other contract the language is sufficient if it states, for example, that “There are no warranties ~~which~~ that extend beyond the description on the face hereof.” Language that satisfies the requirements of this subsection for the exclusion or modification of a warranty in a consumer contract also satisfies the requirements for any other contract.

(c) Notwithstanding Subsection (b):

(1) unless the circumstances indicate otherwise, all implied warranties are excluded by expressions like “as is”, “with all faults” or other language ~~which that~~ in common understanding calls the buyer’s attention to the exclusion of warranties ~~and~~, makes plain that there is no implied warranty, and, in a consumer contract evidenced by a record, is set forth conspicuously in the record; and

(2) ~~when~~ if the buyer before entering into the contract has examined the goods or the sample or model as fully as ~~he~~ desired or has refused to examine the goods after a demand by the seller there is no implied warranty with regard to defects ~~which that~~ an examination ~~ought~~ in the circumstances to ~~should~~ have revealed to him the buyer; and

(3) an implied warranty ~~can~~ may also be excluded or modified by course of dealing or course of performance or usage of trade.

(d) Remedies for breach of warranty can may be limited in accordance with ~~the provisions of this chapter on liquidation or limitation of damages and on contractual modification of remedy (Sections 2.718 and 2.719)~~ Sections 2.718 and 2.719.

(e) The implied warranties of merchantability and fitness shall not be applicable to the furnishing of human blood, blood plasma, or other human tissue or organs from a blood bank or reservoir of such other tissues or organs.

Such blood, blood plasma or tissue or organs shall not for the purpose of this Title be considered commodities subject to sale or barter, but shall be considered as medical services.

(f) The implied warranties of merchantability and fitness do not apply to the sale or barter of livestock or its unborn young.

SECTION 27. Section 2.318, Business & Commerce Code, is amended to read as follows:

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

This chapter does not provide whether anyone other than an “immediate buyer,” which means a buyer that enters into a contract with the seller, ~~a buyer~~ may take advantage of an express or implied warranty of quality or a remedial promise made to the immediate buyer or whether the immediate buyer or anyone entitled to take advantage of a warranty or remedial promise made to the immediate buyer may sue a third party other than the immediate seller for deficiencies in the quality of the goods or for breach of a remedial promise made to the immediate buyer. These matters are left to the courts for their determination.

SECTION 28. Section 2.319, Business & Commerce Code, is amended by deleting the text of that section and reserving the section number, to read as follows:

Sec. 2.319. Reserved F.O.B. and F.A.S. Terms

~~(a) Unless otherwise agreed the term F.O.B. (which means “free on board”) at a named place, even though used only in connection with the stated price, is a delivery term under which~~

~~(1) when the term is F.O.B. the place of shipment, the seller must at that place ship the goods in the manner provided in this chapter (Section 2.504) and bear the expense and risk of putting them into the possession of the carrier; or~~

~~(2) when the term is F.O.B. the place of destination, the seller must at his own expense and risk transport the goods to that place and there tender delivery of them in the manner provided in this chapter (Section 2.503);~~

~~(3) when under either Subdivision (1) or (2) the term is also F.O.B. vessel, car or other vehicle, the seller must in addition at his own expense and risk load the goods on board. If the term is F.O.B. vessel the buyer must name the vessel and in an appropriate case the seller must comply with the provisions of this chapter on the form of bill of lading (Section 2.323).~~

~~(b) Unless otherwise agreed the term F.A.S. vessel (which means “free alongside”) at a named port, even though used only in connection with the stated price, is a delivery term under which the seller must~~

~~(1) at his own expense and risk deliver the goods alongside the vessel in the manner usual in that port or on a dock designated and provided by the buyer; and~~

~~(2) obtain and tender a receipt for the goods in exchange for which the carrier is under a duty to issue a bill of lading.~~

~~(e) Unless otherwise agreed in any case falling within Subsection (a)(1) or (3) or Subsection (b) the buyer must seasonably give any needed instructions for making delivery, including when the term is F.A.S. or F.O.B. the loading berth of the vessel and in an appropriate case its name and sailing date. The seller may treat the failure of needed instructions as a failure of cooperation under this chapter (Section 2.311). He may also at his option move the goods in any reasonable manner preparatory to delivery or shipment.~~

~~(d) Under the term F.O.B. vessel or F.A.S. unless otherwise agreed the buyer must make payment against tender of the required documents and the seller may not tender nor the buyer demand delivery of the goods in substitution for the documents.~~

SECTION 29. Section 2.320, Business & Commerce Code, is amended by deleting the text of that section and reserving the section number, to read as follows:

Sec. 2.320. Reserved C.I.F. and C. & F. Terms

~~(a) The term C.I.F. means that the price includes in a lump sum the cost of the goods and the insurance and freight to the named destination. The term C. & F. or C.F. means that the price so includes cost and freight to the named destination.~~

~~(b) Unless otherwise agreed and even though used only in connection with the stated price and destination, the term C.I.F. destination or its equivalent requires the seller at his own expense and risk to~~

~~(1) put the goods into the possession of a carrier at the port for shipment and obtain a negotiable bill or bills of lading covering the entire transportation to the named destination; and~~

~~(2) load the goods and obtain a receipt from the carrier (which may be contained in the bill of lading) showing that the freight has been paid or provided for; and~~

~~(3) obtain a policy or certificate of insurance, including any war risk insurance, of a kind and on terms then current at the port of shipment in the usual amount, in the currency of the contract, shown to cover the same goods covered by the bill of lading and providing for payment of loss to the order of the buyer or for the account of whom it may concern; but the seller may add to the price the amount of the premium for any such war risk insurance; and~~

~~(4) prepare an invoice of the goods and procure any other documents required to effect shipment or to comply with the contract; and~~

~~(5) forward and tender with commercial promptness all the documents in due form and with any indorsement necessary to perfect the buyer's rights.~~

~~(e) Unless otherwise agreed the term C. & F. or its equivalent has the same effect and imposes upon the seller the same obligations and risks as a C.I.F. term except the obligation as to insurance.~~

~~(d) Under the term C.I.F. or C. & F. unless otherwise agreed the buyer must make payment against tender of the required documents and the seller may not tender nor the buyer demand delivery of the goods in substitution for the documents.~~

SECTION 30. Section 2.321, Business & Commerce Code, is amended by deleting the text of that section and reserving the section number, to read as follows:

Sec. 2.321. Reserved C.I.F. or C. & F.: "Net Landed Weights"; "Payment on Arrival"; Warranty of Condition on Arrival

~~Under a contract containing a term C.I.F. or C. & F.~~

~~(a) Where the price is based on or is to be adjusted according to "net landed weights", "delivered weights", "out turn" quantity or quality or the like, unless otherwise agreed the seller must reasonably estimate the price. The payment due on tender of the documents called for by the contract is the amount so estimated, but after final adjustment of the price a settlement must be made with commercial promptness.~~

~~(b) An agreement described in Subsection (a) or any warranty of quality or condition of the goods on arrival places upon the seller the risk of ordinary deterioration, shrinkage and the like in transportation but has no effect on the place or time of identification to the contract for sale or delivery or on the passing of the risk of loss.~~

~~(c) Unless otherwise agreed where the contract provides for payment on or after arrival of the goods the seller must before payment allow such preliminary inspection as is feasible; but if the goods are lost delivery of the documents and payment are due when the goods should have arrived.~~

SECTION 31. Section 2.322, Business & Commerce Code, is amended by deleting the text of that section and reserving the section number, to read as follows:

Sec. 2.322. Reserved Delivery "Ex Ship"

~~(a) Unless otherwise agreed a term for delivery of goods "ex ship" (which means from the carrying vessel) or in equivalent language is not restricted to a particular ship and requires delivery from a ship which has reached a place at the named port of destination where goods of the kind are usually discharged.~~

~~(b) Under such a term unless otherwise agreed~~

~~(1) the seller must discharge all liens arising out of the carriage and furnish the buyer with a direction which puts the carrier under a duty to deliver the goods; and~~

~~(2) the risk of loss does not pass to the buyer until the goods leave the ship's tackle or are otherwise properly unloaded.~~

SECTION 32. Section 2.323, Business & Commerce Code, is amended by deleting the text of that section and reserving the section number, to read as follows:

Sec. 2.323. Reserved Form of Bill of Lading Required in Overseas Shipment; "Overseas"

~~(a) Where the contract contemplates overseas shipment and contains a term C.I.F. or C. & F. or F.O.B. vessel, the seller unless otherwise agreed must obtain a negotiable bill of lading stating that the goods have been loaded on board or, in the case of a term C.I.F. or C. & F., received for shipment.~~

~~(b) Where in a case within Subsection (a) a bill of lading has been issued in a set of parts, unless otherwise agreed if the documents are not to be sent from abroad the buyer may demand tender of the full set; otherwise only one part of the bill of lading need be tendered. Even if the agreement expressly requires a full set~~

~~(1) due tender of a single part is acceptable within the provisions of this chapter on cure of improper delivery (Subsection (a) of Section 2.508); and~~

~~(2) even though the full set is demanded, if the documents are sent from abroad the person tendering an incomplete set may nevertheless require payment upon furnishing an indemnity which the buyer in good faith deems adequate.~~

~~(c) A shipment by water or by air or a contract contemplating such shipment is "overseas" insofar as by usage of trade or agreement it is subject to the commercial, financing or shipping practices characteristic of international deep water commerce.~~

SECTION 33. Section 2.324, Business & Commerce Code, is amended by deleting the text of that section and reserving the section number, to read as follows:

Sec. 2.324. Reserved "No Arrival, No Sale" Term

~~Under a term "no arrival, no sale" or terms of like meaning, unless otherwise agreed;~~

~~(1) the seller must properly ship conforming goods and if they arrive by any means he must tender them on arrival but he assumes no obligation that the goods will arrive unless he has caused the non arrival; and~~

~~(2) where without fault of the seller the goods are in part lost or have so deteriorated as no longer to conform to the contract or arrive after the contract time, the buyer may proceed as if there had been casualty to identified goods (Section 2.613).~~

SECTION 34. Section 2.325, Business & Commerce Code, is amended to read as follows:

Sec. 2.325. "Letter of Credit" Term; "Confirmed Credit" Failure to Pay by Agreed Letter of Credit

If the parties agree that the primary method of payment will be by letter of credit, the following rules apply:

(a) The buyer's obligation to pay is suspended by seasonable delivery to the seller of a letter of credit issued or confirmed by a financing agency of good repute in which the issuer and any confirmer undertake to pay against presentation of documents that evidence delivery of the goods.

(b) Failure of a party seasonably to furnish a letter of credit as agreed is a breach of the contract for sale.

(c) If the letter of credit is dishonored or repudiated, the seller, on reasonable notification, may require payment directly from the buyer.

~~(a) Failure of the buyer seasonably to furnish an agreed letter of credit is a breach of the contract for sale.~~

~~(b) The delivery to seller of a proper letter of credit suspends the buyer's obligation to pay. If the letter of credit is dishonored, the seller may on reasonable notification to the buyer require payment directly from him.~~

~~(e) Unless otherwise agreed the term "letter of credit" or "banker's credit" in a contract for sale means an irrevocable credit issued by a financing agency of good repute and, where the shipment is overseas, of good international repute. The term "confirmed credit" means that the credit must also carry the direct obligation of such an agency which does business in the seller's financial market.~~

SECTION 35. Section 2.326, Business & Commerce Code, is amended to read as follows:

Sec. 2.326. Sale on Approval and Sale or Return; ~~Rights of Creditors~~

(a) Unless otherwise agreed, if delivered goods may be returned by the buyer even ~~though~~ if they conform to the contract, the transaction is:

(1) a "sale on approval" if the goods are delivered primarily for ~~use~~, use; and

(2) a "sale or return" if the goods are delivered primarily for resale.

(b) Goods held on approval are not subject to the claims of the buyer's creditors until acceptance; goods held on sale or return are subject to such claims while in the buyer's possession.

(c) Any "or return" term of a contract for sale is to be treated as a separate contract for sale ~~within the statute of frauds section of this chapter (Section 2.201) under Section 2.201 and as contradicting the sale aspect of the contract within the provisions of this chapter on parol or extrinsic evidence (Section 2.202) under Section 2.202.~~

SECTION 36. Section 2.328, Business & Commerce Code, is amended to read as follows:

Sec. 2.328. Sale by Auction

(a) In a sale by auction, if goods are put up in lots, each lot is the subject of a separate sale.

(b) A sale by auction is complete when the auctioneer so announces by the fall of the hammer or in other customary manner. ~~Where~~ If a bid is made ~~while the hammer is falling in acceptance of~~ during the process of completing the sale but before a prior bid is accepted, the auctioneer ~~may in his~~ has discretion to reopen the bidding or to declare the goods sold under the prior bid ~~on which the hammer was falling~~.

(c) A sale by auction is subject to the seller's right to withdraw the goods unless at the time the goods are put up or during the course of the auction it is

announced in express terms that the right to withdraw the goods is not reserved. In an auction in which the right to withdraw the goods is reserved, the auctioneer may withdraw the goods at any time until completion of the sale is announced by the auctioneer. In an auction in which the right to withdraw the goods is not reserved, after the auctioneer calls for bids on an article or lot, the article or lot may not be withdrawn unless no bid is made within a reasonable time. In either case a bidder may retract a bid until the auctioneer's announcement of completion of the sale, but a bidder's retraction does not revive any previous bid. Such a sale is with reserve unless the goods are in explicit terms put up without reserve. In an auction with reserve the auctioneer may withdraw the goods at any time until he announces completion of the sale. In an auction without reserve, after the auctioneer calls for bids on an article or lot, that article or lot cannot be withdrawn unless no bid is made within a reasonable time. In either case a bidder may retract his bid until the auctioneer's announcement of completion of the sale, but a bidder's retraction does not revive any previous bid.

(d) If the auctioneer knowingly receives a bid on the seller's behalf or the seller makes or procures such a bid, and notice has not been given that liberty for such bidding is reserved, the buyer may at ~~his~~ the buyer's option avoid the sale or take the goods at the price of the last ~~good faith~~ good-faith bid prior to the completion of the sale. This subsection shall not apply to any bid at a ~~forced sale~~ an auction required by law.

SECTION 37. Section 2.401, Business & Commerce Code, is amended to read as follows:

Sec. 2.401. Passing of Title; Reservation for Security; Limited Application of This Section

Each provision of this chapter with regard to the rights, obligations, and remedies of the seller, the buyer, purchasers, or other third parties applies irrespective of title to the goods except where the provision refers to such title. Insofar as situations are not covered by the other provisions of this chapter and matters concerning title become material, the following rules apply:

(a) Title to goods cannot pass under a contract for sale prior to their identification to the contract (Section 2.501), and unless otherwise explicitly agreed, the buyer acquires by their identification a special property as limited by this title. Any retention or reservation by the seller of the title (property) in goods shipped or delivered to the buyer is limited in effect to a reservation of a security interest. Subject to these provisions and to ~~the provisions of the chapter on Secured Transactions (Chapter 9)~~ Chapter 9, title to goods passes from the seller to the buyer in any manner and on any conditions explicitly agreed on by the parties.

(b) Unless otherwise explicitly agreed title passes to the buyer at the time and place at which the seller completes ~~his~~ performance with reference to the ~~physical~~ delivery of the goods, despite any reservation of a security interest and even ~~though~~ if a document of title is to be delivered at a different time or place;

and in particular and despite any reservation of a security interest by the bill of lading:

(1) if the contract requires or authorizes the seller to send the goods to the buyer but does not require ~~him~~ the seller to deliver them at destination, title passes to the buyer at the time and place of shipment; but

(2) if the contract requires delivery at destination, title passes on tender there.

(c) Unless otherwise explicitly agreed, ~~where~~ if delivery is to be made without moving the ~~goods,~~ goods:

(1) if the seller is to deliver a tangible document of title, title passes at the time when and the place where ~~he~~ the seller delivers ~~such documents~~ the document, and if the seller is to deliver an electronic document of title, title passes when the seller delivers the document; or

(2) if the goods are at the time of contracting already identified and no documents of title are to be delivered, title passes at the time and place of contracting.

(d) A rejection or other refusal by the buyer to receive or retain the goods, whether or not justified, or a justified revocation of acceptance revests title to the goods in the seller. Such revesting occurs by operation of law and is not a “sale”.

SECTION 38. Section 2.402, Business & Commerce Code, is amended to read as follows:

Sec. 2.402. Rights of Seller’s Creditors Against Sold Goods

(a) Except as provided in Subsections (b) and (c), rights of unsecured creditors of the seller with respect to goods ~~which that~~ have been identified to a contract for sale are subject to the buyer’s rights to recover the goods under ~~this chapter (Sections 2.502 and 2.716)~~ Sections 2.502 and 2.716.

(b) A creditor of the seller may treat a sale or an identification of goods to a contract for sale as void if as against ~~him~~ the creditor a retention of possession by the seller is fraudulent under any rule of law of the state where the goods are ~~situated, except that~~ situated. However, retention of possession in good faith and current course of trade by a merchant-seller for a commercially reasonable time after a sale or identification is not fraudulent.

(c) ~~Nothing~~ Except as otherwise provided in Section 2.403(b), nothing in this chapter shall be deemed to impair the rights of creditors of the seller:

(1) ~~under the provisions of the chapter on Secured Transactions (Chapter 9)~~ Chapter 9; or

(2) ~~where~~ if identification to the contract or delivery is made not in current course of trade but in satisfaction of or as security for a ~~pre-existing~~ preexisting claim for money, security, or the like and is made under circumstances ~~which that~~ under any rule of law of the state where the goods are situated would apart from this chapter constitute the transaction a fraudulent transfer or voidable preference.

SECTION 39. Section 2.403, Business & Commerce Code, is amended to read as follows:

Sec. 2.403. Power to Transfer; Good Faith Purchase of Goods; “Entrusting”

(a) A purchaser of goods acquires all title ~~which his~~ that the purchaser’s transferor had or had power to transfer except that a purchaser of a limited interest acquires rights only to the extent of the interest purchased. A person with voidable title has power to transfer a good title to a ~~good-faith~~ good-faith purchaser for value. ~~When~~ If goods have been delivered under a transaction of purchase, the purchaser has such power even ~~though~~ if:

(1) the transferor was deceived as to the identity of the ~~purchaser,~~  
~~or purchaser;~~

(2) the delivery was in exchange for a check ~~which~~ that is later ~~dishonored,~~  
~~or dishonored;~~

(3) it was agreed that the transaction was to be a “cash ~~sale~~”, sale”;  
or

(4) the delivery was procured through criminal fraud ~~punishable as~~  
~~larcenous under the criminal law.~~

(b) Any entrusting ~~of possession~~ of goods to a merchant ~~who~~ that deals in goods of that kind gives ~~him~~ the merchant power to transfer ~~all rights of the~~  
~~entruster~~ all of the entruster’s rights to the goods and to transfer the goods free  
of any interest of the entruster to a buyer in ordinary course of business.

(c) “Entrusting” includes any delivery and any acquiescence in retention of possession regardless of any condition expressed between the parties to the delivery or acquiescence and regardless of whether the procurement of the entrusting or the possessor’s disposition of the goods ~~have been such as to be~~  
~~larcenous~~ was punishable under the criminal law.

(d) The rights of other purchasers of goods and of lien creditors are governed by ~~the chapters on Secured Transactions (Chapter 9) and Documents~~  
~~of Title (Chapter 7)~~ Chapters 7 and 9.

SECTION 40. Section 2.501, Business & Commerce Code, is amended to read as follows:

Sec. 2.501. Insurable Interest in Goods; Manner of Identification of Goods

(a) The buyer obtains a special property and an insurable interest in goods by identification of existing goods as goods to which the contract refers even ~~though~~ if the goods so identified are ~~non-conforming~~ nonconforming and ~~he~~ the buyer has an option to return or reject them. Such identification ~~can~~ may be made at any time and in any manner explicitly agreed to by the parties. In the absence of explicit agreement identification occurs;

(1) when the contract is made if it is for the sale of goods already existing and identified;

(2) if the contract is for the sale of future goods other than those described in Subdivision (3), when goods are shipped, marked, or otherwise designated by the seller as goods to which the contract refers;

(3) when the crops are planted or otherwise become growing crops or the young are conceived if the contract is for the sale of unborn young to be born within ~~twelve~~ 12 months after contracting or for the sale of crops to be harvested within ~~twelve~~ 12 months or the next normal harvest season after contracting whichever is longer.

(b) The seller retains an insurable interest in goods so long as title to or any security interest in the goods remains in ~~him and where~~ the seller. If the identification is by the seller alone, ~~he~~ the seller may until default or insolvency or notification to the buyer that the identification is final substitute other goods for those identified.

(c) Nothing in this section impairs any insurable interest recognized under any other statute or rule of law.

SECTION 41. Section 2.502, Business & Commerce Code, is amended to read as follows:

Sec 2.502. Buyer's Right to Goods on Seller's Repudiation, Failure to Deliver, or Insolvency

(a) Subject to subsections (b) and (c) and even ~~though if~~ the goods have not been shipped, a buyer ~~who that~~ has paid a part or all of the price of goods in which ~~he~~ the buyer has a special property under ~~the provisions of the immediately preceding section~~ Section 2.501 may on making and keeping good a tender of any unpaid portion of their price recover them from the seller if:

(1) in the case of goods bought ~~for personal, family, or household purposes by a consumer~~, the seller repudiates or fails to deliver as required by the contract; or

(2) in all cases, the seller becomes insolvent within 10 days after receipt of the first installment on their price.

(b) The buyer's right to recover the goods under Subsection (a)(1) vests upon acquisition of a special property, even if the seller had not then repudiated or failed to deliver.

(c) If the identification creating ~~his a~~ a special property has been made by ~~the buyer he~~ the buyer, ~~the buyer~~ the buyer acquires the right to recover the goods only if they conform to the contract for sale.

SECTION 42. Section 2.503, Business & Commerce Code, is amended to read as follows:

Sec. 2.503. Manner of Seller's Tender of Delivery

(a) Tender of delivery requires that the seller put and hold conforming goods at the buyer's disposition and give the buyer any notification reasonably necessary to enable ~~him~~ the buyer to take delivery. The manner, time, and place for tender are determined by the agreement and this chapter, and in particular:

(1) tender must be at a reasonable hour, and if it is of goods they must be kept available for the period reasonably necessary to enable the buyer to take possession; but

(2) unless otherwise agreed the buyer must furnish facilities reasonably suited to the receipt of the goods.

(b) ~~Where~~ If the case is within ~~the next section respecting shipment~~ Section 2.504, tender requires that the seller comply with its provisions.

(c) ~~Where~~ If the seller is required to deliver at a particular destination, tender requires that ~~he the seller~~ the seller comply with Subsection (a) and also in any appropriate case tender documents as described in Subsections (d) and (e) of this section.

(d) ~~Where~~ If goods are in the possession of a bailee and are to be delivered without being moved:

(1) tender requires that the seller either tender a negotiable document of title covering such goods or procure acknowledgment by the bailee to the buyer of the buyer's right to possession of the goods; but

(2) tender to the buyer of a ~~non-negotiable~~ nonnegotiable document of title or of a ~~written direction to a record directing~~ record directing the bailee to deliver is sufficient tender unless the buyer seasonably objects, and except as otherwise provided in Chapter 9 receipt by the bailee of notification of the buyer's rights fixes those rights as against the bailee and all third persons; but risk of loss of the goods and of any failure by the bailee to honor the ~~non-negotiable~~ nonnegotiable document of title or to obey the direction remains on the seller until the buyer has had a reasonable time to present the document or ~~direction,~~ direction, ~~and a refusal~~ direction. Refusal by the bailee to honor the document or to obey the direction defeats the tender.

(e) ~~Where~~ If the contract requires the seller to deliver documents:

(1) ~~he the seller~~ the seller must tender all such documents in correct form; ~~except as provided in this chapter with respect to bills of lading in a set (Subsection (b) of Section 2.323);~~ and

(2) tender through customary banking channels is sufficient and dishonor of a draft accompanying or associated with the documents constitutes ~~non-acceptance~~ nonacceptance or rejection.

SECTION 43. Section 2.504, Business & Commerce Code, is amended to read as follows:

Sec. 2.504. Shipment by Seller

~~Where~~ If the seller is required or authorized to send the goods to the buyer and the contract does not require ~~him~~ the seller to deliver them at a particular destination, then unless otherwise agreed ~~he the seller~~ the seller must:

(1) put ~~the~~ conforming goods in the possession of ~~such~~ such a carrier and make ~~such~~ such a proper contract for their transportation, ~~as may be reasonable~~ having regard to the nature of the goods and other circumstances of the case; ~~and~~

(2) obtain and promptly deliver or tender in due form any document necessary to enable the buyer to obtain possession of the goods or otherwise required by the agreement or by usage of trade; and

(3) promptly notify the buyer of the shipment.

Failure to notify the buyer under Subdivision (3) or to make a proper contract under Subdivision (1) is a ground for rejection only if material delay or loss ensues.

SECTION 44. Section 2.505, Business & Commerce Code, is amended to read as follows:

Sec. 2.505. Seller's Shipment Under Reservation

(a) ~~Where~~ If the seller has identified goods to the contract by or before shipment:

(1) ~~his~~ The seller's procurement of a negotiable bill of lading to ~~his the seller's~~ own order or otherwise reserves in ~~him the seller~~ a security interest in the goods. ~~His~~ The seller's procurement of the bill to the order of a financing agency or of the buyer indicates in addition only the seller's expectation of transferring that interest to the person named.

(2) ~~a non-negotiable~~ A nonnegotiable bill of lading to ~~himself the seller or his the seller's~~ nominee reserves possession of the goods as ~~security but security~~. ~~However, except in a case of conditional delivery unless a seller has a right to reclaim the goods under (Subsection (b) of Section 2.507) Section 2.507(b)~~ a non-negotiable nonnegotiable bill of lading naming the buyer as consignee reserves no security interest even ~~though~~ if the seller retains possession or control of the bill of lading.

(b) ~~When~~ If shipment by the seller with reservation of a security interest is in violation of the contract for sale, ~~it constitutes an improper contract for transportation within the preceding section under Section 2.504~~ but impairs neither the rights given to the buyer by shipment and identification of the goods to the contract nor the seller's powers as a holder of a negotiable document of title.

SECTION 45. Section 2.506, Business & Commerce Code, is amended to read as follows:

Sec. 2.506. Rights of Financing Agency

(a) ~~A~~ Except as otherwise provided in Chapter 5, a financing agency by paying or purchasing for value a draft ~~which that~~ relates to a shipment of goods acquires to the extent of the payment or purchase and in addition to its own rights under the draft and any document of title securing it any rights of the shipper in the goods including the right to stop delivery and the shipper's right to have the draft honored by the buyer.

(b) The right to reimbursement of a financing agency ~~which that~~ has in good faith honored or purchased the draft under commitment to or authority from the buyer is not impaired by subsequent discovery of defects with reference to any relevant document ~~which that~~ was apparently regular.

SECTION 46. Section 2.507, Business & Commerce Code, is amended to read as follows:

Sec. 2.507. Effect of Seller's Tender; Delivery on Condition

(a) Tender of delivery is a condition to the buyer's duty to accept the goods and, unless otherwise agreed, to ~~his the buyer's~~ duty to pay for them.

Tender entitles the seller to acceptance of the goods and to payment according to the contract.

(b) ~~Where~~ If payment is due and demanded on the delivery to the buyer of goods or documents of title, ~~his right as against the seller to retain or dispose of them is conditional upon his making the payment due~~ the seller may reclaim the goods delivered upon a demand made within a reasonable time after the seller discovers or should have discovered that payment was not made.

(c) The seller's right to reclaim under Subsection (b) is subject to the rights of a buyer in ordinary course of business or other good-faith purchaser for value under Section 2.403.

SECTION 47. Section 2.508, Business & Commerce Code, is amended to read as follows:

Sec. 2.508. Cure by Seller of Improper Tender or Delivery; Replacement

(a) If the buyer rejects goods or a tender of delivery under Section 2.601 or 2.612 or, except in a consumer contract, justifiably revokes acceptance under Section 2.608(a)(2) and the agreed time for performance has not expired, a seller that has performed in good faith, upon reasonable notice to the buyer and at the seller's own expense, may cure the breach of contract by making a conforming tender of delivery within the agreed time. The seller shall compensate the buyer for all of the buyer's reasonable expenses caused by the seller's breach of contract and subsequent cure.

(b) If the buyer rejects goods or a tender of delivery under Section 2.601 or 2.612 or, except in a consumer contract, justifiably revokes acceptance under Section 2.608(a)(2) and the agreed time for performance has expired, a seller that has performed in good faith, upon reasonable notice to the buyer and at the seller's own expense, may cure the breach of contract, if the cure is appropriate and timely under the circumstances, by making a tender of conforming goods. The seller shall compensate the buyer for all of the buyer's reasonable expenses caused by the seller's breach of contract and subsequent cure.

~~(a) Where any tender or delivery by the seller is rejected because non-conforming and the time for performance has not yet expired, the seller may seasonably notify the buyer of his intention to cure and may then within the contract time make a conforming delivery.~~

~~(b) Where the buyer rejects a non-conforming tender which the seller had reasonable grounds to believe would be acceptable with or without money allowance the seller may if he seasonably notifies the buyer have a further reasonable time to substitute a conforming tender.~~

SECTION 48. Section 2.509, Business & Commerce Code, is amended to read as follows:

Sec. 2.509. Risk of Loss in the Absence of Breach

(a) ~~Where~~ If the contract requires or authorizes the seller to ship the goods by carrier:

(1) if it does not require ~~him~~ the seller to deliver them at a particular destination, the risk of loss passes to the buyer when the goods are

duly delivered to the carrier even ~~though~~ if the shipment is under reservation (Section 2.505); but

(2) if it does require ~~him~~ the seller to deliver them at a particular destination and the goods are there ~~duly~~ tendered while in the possession of the carrier, the risk of loss passes to the buyer when the goods are there ~~duly~~ so tendered as to enable the buyer to take delivery.

(b) ~~Where~~ If the goods are held by a bailee to be delivered without being moved, the risk of loss passes to the buyer:

(1) on the buyer's receipt of possession or control of a negotiable document of title covering the goods; ~~or~~

(2) on acknowledgment by the bailee to the buyer of the buyer's right to possession of the goods; or

(3) after the buyer's receipt of possession or control of a ~~non-~~negotiable nonnegotiable document of title or other ~~written~~ direction to deliver in a record, as provided in ~~Subsection (d)(2) of~~ Section 2.503(d)(2).

(c) In any case not within Subsection (a) or (b), the risk of loss passes to the buyer on ~~his~~ the buyer's receipt of the goods ~~if the seller is a merchant; otherwise the risk passes to the buyer on tender of delivery.~~

(d) The provisions of this section are subject to contrary agreement of the parties and to the provisions of this chapter on sale on approval (Section 2.327) and on effect of breach on risk of loss (Section 2.510) Sections 2.327 and 2.510.

SECTION 49. Section 2.510, Business & Commerce Code, is amended to read as follows:

Sec. 2.510. Effect of Breach on Risk of Loss

(1) ~~Where~~ If a tender or delivery of goods so fails to conform to the contract as to give a right of rejection, the risk of their loss remains on the seller until cure or acceptance.

(2) ~~Where~~ If the buyer rightfully revokes acceptance, ~~he~~ the buyer may to the extent of any deficiency in ~~his~~ the buyer's effective insurance coverage treat the risk of loss as having rested on the seller from the beginning.

(3) ~~Where~~ If the buyer as to conforming goods already identified to the contract for sale repudiates or is otherwise in breach before risk of their loss has passed to ~~him~~ the buyer, the seller may to the extent of any deficiency in ~~his~~ the seller's effective insurance coverage treat the risk of loss as resting on the buyer for a commercially reasonable time.

SECTION 50. Section 2.511, Business & Commerce Code, is amended to read as follows:

Sec. 2.511. Tender of Payment by Buyer; Payment by Check

(a) Unless otherwise agreed tender of payment is a condition to the seller's duty to tender and complete any delivery.

(b) 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.

(c) Subject to the provisions of this title on the effect of an instrument on an obligation (~~Section 3.310~~)(~~Section 3.802~~), payment by check is conditional and is defeated as between the parties by dishonor of the check on due presentment.

SECTION 51. Section 2.512, Business & Commerce Code, is amended to read as follows:

Sec. 2.512. Payment by Buyer Before Inspection

(a) ~~Where~~ If the contract requires payment before inspection, ~~non-conformity~~ nonconformity of the goods does not excuse the buyer from so making payment unless:

(1) the ~~non-conformity~~ nonconformity appears without inspection;

or

(2) despite tender of the required documents the circumstances would justify injunction against honor under this title (Section 5.109(b)).

(b) Payment pursuant to Subsection (a) does not constitute an acceptance of goods or impair the buyer's right to inspect or any of ~~his~~ the buyer's remedies.

SECTION 52. Section 2.513, Business & Commerce Code, is amended to read as follows:

Sec. 2.513. Buyer's Right to Inspection of Goods

(a) Unless otherwise agreed and subject to Subsection (c), ~~where~~ if goods are tendered or delivered or identified to the contract for sale, the buyer has a right before payment or acceptance to inspect them at any reasonable place and time and in any reasonable manner. ~~When~~ If the seller is required or authorized to send the goods to the buyer, the inspection may be after their arrival.

(b) Expenses of inspection must be borne by the buyer but may be recovered from the seller if the goods do not conform and are rejected.

(c) Unless otherwise agreed ~~and subject to the provisions of this chapter on C.I.F. contracts (Subsection (c) of Section 2.321)~~, the buyer is not entitled to inspect the goods before payment of the price ~~when~~ if the contract provides:

(1) for delivery "C.O.D." or on other like terms on terms that under applicable course of performance, course of dealing, or usage of trade are interpreted to preclude inspection before payment; or

(2) for payment against documents of title, except where ~~such~~ the payment is due only after the goods are to become available for inspection.

(d) A place ~~or method~~, method, or standard of inspection fixed by the parties is presumed to be exclusive, but unless otherwise expressly agreed it does not postpone identification or shift the place for delivery or for passing the risk of loss. If compliance becomes impossible, inspection shall be as provided in this section unless the place ~~or method~~, method, or standard fixed was clearly intended as an indispensable condition failure of which avoids the contract.

SECTION 53. Section 2.514, Business & Commerce Code, is amended to read as follows:

Sec. 2.514. When Documents Deliverable on Acceptance; When on Payment

Unless otherwise agreed and except as otherwise provided in Chapter 5, documents against which a draft is drawn are to be delivered to the drawee on acceptance of the draft if it is payable more than three days after presentment; otherwise, only on payment.

SECTION 54. Section 2.601, Business & Commerce Code, is amended to read as follows:

Sec. 2.601. Buyer's Rights on Improper Delivery

Subject to ~~the provisions of this chapter on breach in installment contracts (Section 2.612)~~ Sections 2.504 and 2.612, and unless otherwise agreed under ~~the sections on contractual limitations of remedy (Sections 2.718 and 2.719)~~ Sections 2.718 and 2.719, if the goods or the tender of delivery fail in any respect to conform to the contract, the buyer may:

- (1) reject the whole; ~~or~~
- (2) accept the whole; or
- (3) accept any commercial unit or units and reject the rest.

SECTION 55. Section 2.602, Business & Commerce Code, is amended to read as follows:

Sec. 2.602. Manner and Effect of ~~Rightful~~ Rejection

(a) Rejection of goods must be within a reasonable time after their delivery or tender. It is ineffective unless the buyer seasonably notifies the seller.

(b) Subject to ~~the provisions of the two following sections on rejected goods (Sections 2.603 and 2.604)~~, Sections 2.603, and 2.604:

- (1) after rejection any exercise of ownership by the buyer with respect to any commercial unit is wrongful as against the seller; and
- (2) if the buyer has before rejection taken physical possession of goods in which ~~he~~ the buyer does not have a security interest under ~~the provisions of this chapter (Subsection (e) of Section 2.711)~~ Section 2.711(c), ~~he~~ the buyer is under a duty after rejection to hold them with reasonable care at the seller's disposition for a time sufficient to permit the seller to remove them; but
- (3) the buyer has no further obligations with regard to goods rightfully rejected.

(c) The seller's rights with respect to goods wrongfully rejected are governed by the provisions of this chapter on Seller's remedies in general (Section 2.703).

SECTION 56. Section 2.603, Business & Commerce Code, is amended to read as follows:

Sec. 2.603. Merchant Buyer's Duties as to ~~Rightfully~~ Rejected Goods

(a) Subject to any security interest in the buyer (~~Subsection (e) of Section 2.711~~) under Section 2.711(c), ~~when~~ if the seller has no agent or place of business at the market of rejection, a merchant buyer is under a duty after rejection of goods in ~~his~~ the buyer's possession or control to follow any

reasonable instructions received from the seller with respect to the goods and in the absence of such instructions to make reasonable efforts to sell them for the seller's account if they are perishable or threaten to decline in value speedily. ~~Instructions~~ In the case of a rightful rejection, instructions are not reasonable if on demand indemnity for expenses is not forthcoming.

(b) ~~When~~ If the buyer sells goods under Subsection (a) following a rightful rejection, he the buyer is entitled to reimbursement from the seller or out of the proceeds for reasonable expenses of caring for and selling them, and if the expenses include no selling commission then to such commission as is usual in the trade or if there is none to a reasonable sum not exceeding ~~ten~~ 10 per cent on the gross proceeds.

(c) In complying with this section the buyer is held only to good faith, and ~~good faith~~ good-faith conduct hereunder under this section is neither acceptance nor conversion nor the basis of an action for damages.

SECTION 57. Section 2.604, Business & Commerce Code, is amended to read as follows:

Sec. 2.604. Buyer's Options as to Salvage of ~~Rightfully~~ Rejected Goods

Subject to the provisions of ~~the immediately preceding section~~ Section 2.603 on perishables, if the seller gives no instructions within a reasonable time after notification of rejection, the buyer may store the rejected goods for the seller's account or reship them to ~~him the seller~~ or resell them for the seller's account with reimbursement as provided in ~~the preceding section~~ Section 2.603. Such action is not acceptance or conversion.

SECTION 58. Section 2.605, Business & Commerce Code, is amended to read as follows:

Sec. 2.605. Waiver of Buyer's Objections by Failure to Particularize

(a) ~~The~~ A buyer's failure to state in connection with rejection a particular defect or in connection with revocation of acceptance a defect that justifies revocation which is ascertainable by reasonable inspection precludes ~~him the buyer~~ from relying on the unstated defect to justify rejection or ~~to establish breach~~ revocation of acceptance if the defect is ascertainable by reasonable inspection:

(1) ~~where~~ if the seller had a right to cure the defect and could have cured it if stated seasonably; or

(2) between merchants, ~~when~~ if the seller has after rejection or revocation of acceptance made a request in writing a record for a full and final ~~written~~ statement in a record of all defects on which the buyer proposes to rely.

(b) ~~Payment~~ A buyer's payment against documents tendered to the buyer made without reservation of rights precludes recovery of the payment for defects apparent in the documents.

SECTION 59. Section 2.606, Business & Commerce Code, is amended to read as follows:

Sec. 2.606. What Constitutes Acceptance of Goods

(a) Acceptance of goods occurs when the buyer:

(1) after a reasonable opportunity to inspect the goods signifies to the seller that the goods are conforming or that ~~he~~ the buyer will take or retain them in spite of their ~~non-conformity~~ nonconformity; or

(2) fails to make an effective rejection (~~Subsection (a) of Section 2.602~~) under Section 2.602(a), but such acceptance does not occur until the buyer has had a reasonable opportunity to inspect them; or

(3) does any act inconsistent with the seller's ownership; but if such act is wrongful as against the seller it is an acceptance only if ratified by him.

(b) Acceptance of a part of any commercial unit is acceptance of that entire unit.

SECTION 60. Section 2.607, Business & Commerce Code, is amended to read as follows:

Sec. 2.607. Effect of Acceptance; Notice of Breach; Burden of Establishing Breach After Acceptance; Notice of Claim or Litigation to Person Answerable Over

(a) The buyer must pay at the contract rate for any goods accepted.

(b) Acceptance of goods by the buyer precludes rejection of the goods accepted and if made with knowledge of a ~~non-conformity~~ cannot nonconformity may not be revoked because of it unless the acceptance was on the reasonable assumption that the ~~non-conformity~~ nonconformity would be seasonably cured, but acceptance does not of itself impair any other remedy provided by this chapter for ~~non-conformity~~ nonconformity.

(c) ~~Where~~ If a tender has been accepted:

(1) the buyer must within a reasonable time after ~~he~~ the buyer discovers or should have discovered any breach notify the seller of breach or be barred from any remedy; and

(2) if the claim is one for infringement or the like (~~Subsection (e) of Section 2.312~~) under Section 2.312(b) and the buyer is sued as a result of such a breach, ~~he~~ the buyer must so notify the seller within a reasonable time after ~~he~~ the buyer receives notice of the litigation or be barred from any remedy over for liability established by the litigation.

(d) The burden is on the buyer to establish any breach with respect to the goods accepted.

(e) ~~Where~~ If the buyer is sued for indemnity, breach of a warranty, or other obligation for which ~~his seller~~ another party is answerable over:

(1) ~~he~~ the buyer may give ~~his seller~~ the other party ~~written~~ notice of the ~~litigation~~. If litigation in a record, and if the notice states that the ~~seller~~ other party may come in and defend and that if the ~~seller~~ other party does not do so ~~he~~ the other party will be bound in any action against ~~him~~ the other party by ~~his~~ the buyer by any determination of fact common to the two litigations, then unless the ~~seller~~ other party after seasonable receipt of the notice does come in and defend ~~he~~ the other party is so bound.

(2) if the claim is one for infringement or the like (~~Subsection (e) of Section 2.312~~) under Section 2.312(b), the original seller may demand in writing a record that ~~his~~ its buyer turn over to ~~him~~ it control of the litigation including settlement or else be barred from any remedy over and if ~~he~~ it also agrees to bear all expense and to satisfy any adverse judgment, ~~then the buyer is so barred~~ unless the buyer after seasonable receipt of the demand does turn over control ~~the buyer is so barred~~.

(f) ~~The provisions of Subsections~~ Subsections (c), (d), and (e) apply to any obligation of a buyer to hold the seller harmless against infringement or the like (~~Subsection (e) of Section 2.312~~) under Section 2.312(b).

SECTION 61. Section 2.608, Business & Commerce Code, is amended to read as follows:

Sec. 2.608. Revocation of Acceptance in Whole or in Part

(a) ~~The~~ A buyer may revoke ~~his~~ acceptance of a lot or commercial unit whose ~~non-conformity~~ nonconformity substantially impairs its value to ~~him~~ the buyer if ~~he~~ the buyer has accepted it:

(1) on the reasonable assumption that its ~~non-conformity~~ nonconformity would be cured and it has not been seasonably cured; or

(2) without discovery of ~~such non-conformity~~ the nonconformity if ~~his~~ the buyer's acceptance was reasonably induced either by the difficulty of discovery before acceptance or by the seller's assurances.

(b) Revocation of acceptance must occur within a reasonable time after the buyer discovers or should have discovered the ground for it and before any substantial change in condition of the goods which is not caused by their own defects. ~~It~~ The revocation is not effective until the buyer notifies the seller of it.

(c) A buyer ~~who~~ that so revokes has the same rights and duties with regard to the goods involved as if ~~he~~ the buyer had rejected them.

(d) If a buyer uses the goods after a revocation of acceptance, the following rules apply:

(1) Any use by the buyer that is unreasonable under the circumstances is wrongful as against the seller and any revocation of acceptance is ineffective.

(2) Any use of the goods that is reasonable under the circumstances is not wrongful as against the seller, but in an appropriate case the buyer is obligated to the seller for the value of the use to the buyer.

SECTION 62. Section 2.609, Business & Commerce Code, is amended to read as follows:

Sec. 2.609. Right to Adequate Assurance of Performance

(a) A contract for sale imposes an obligation on each party that the other's expectation of receiving due performance will not be impaired. ~~When~~ If reasonable grounds for insecurity arise with respect to the performance of either party, the other may ~~in writing~~ demand in a record adequate assurance of due performance and until ~~he~~ the party receives such assurance may if commercially

reasonable suspend any performance for which ~~he~~ it has not already received the agreed return.

(b) Between merchants, the reasonableness of grounds for insecurity and the adequacy of any assurance offered shall be determined according to commercial standards.

(c) Acceptance of any improper delivery or payment does not prejudice the aggrieved party's right to demand adequate assurance of future performance.

(d) After receipt of a justified demand, failure to provide within a reasonable time not exceeding ~~thirty~~ 30 days such assurance of due performance as is adequate under the circumstances of the particular case is a repudiation of the contract.

SECTION 63. Section 2.610, Business & Commerce Code, is amended to read as follows:

Sec. 2.610. Anticipatory Repudiation

(a) ~~When~~ If either party repudiates the contract with respect to a performance not yet due the loss of which will substantially impair the value of the contract to the other, the aggrieved party may:

(1) for a commercially reasonable time await performance by the repudiating party; or

(2) resort to any remedy for breach (Section 2.703 or Section 2.711), even ~~though he~~ if the aggrieved party has notified the repudiating party that ~~he~~ it would await the latter's performance and has urged retraction; and

(3) in either case suspend ~~his own~~ performance or proceed in accordance with the provisions of this chapter on the seller's right to identify goods to the contract notwithstanding breach or to salvage unfinished goods (Section 2.704).

(b) Repudiation includes language that a reasonable person would interpret to mean that the other party will not or cannot make a performance still due under the contract or voluntary, affirmative conduct that would appear to a reasonable person to make a future performance by the other party impossible.

SECTION 64. Section 2.611, Business & Commerce Code, is amended to read as follows:

Sec. 2.611. Retraction of Anticipatory Repudiation

(a) Until the repudiating party's next performance is due, ~~he can~~ that party may retract ~~his~~ the repudiation unless the aggrieved party has since the repudiation cancelled or materially changed ~~his~~ position or otherwise indicated that ~~he considers~~ the repudiation is final.

(b) Retraction may be by any method ~~which~~ that clearly indicates to the aggrieved party that the repudiating party intends to perform, but must include any assurance justifiably demanded under ~~the provisions of this chapter~~ (Section 2.609) Section 2.609.

(c) Retraction reinstates the repudiating party's rights under the contract with due excuse and allowance to the aggrieved party for any delay occasioned by the repudiation.

SECTION 65. Section 2.612, Business & Commerce Code, is amended to read as follows:

Sec. 2.612. "Installment Contract"; Breach

(a) An "installment contract" is one ~~which that~~ requires or authorizes the delivery of goods in separate lots to be separately accepted, even ~~though if~~ the contract contains a clause "each delivery is a separate contract" or its equivalent.

(b) The buyer may reject any installment ~~which that is non-conforming nonconforming~~ if the ~~non-conformity nonconformity~~ substantially impairs the value of that installment ~~and cannot be cured to the buyer~~ or if the ~~non-conformity nonconformity~~ is a defect in the required ~~documents; but documents~~. However, if the ~~non-conformity nonconformity~~ does not fall within Subsection (c) and the seller gives adequate assurance of its cure the buyer must accept that installment.

(c) ~~Whenever non-conformity~~ If nonconformity or default with respect to one or more installments substantially impairs the value of the whole contract, there is a breach of the whole. But the aggrieved party reinstates the contract if ~~he the party~~ accepts a ~~non-conforming nonconforming~~ installment without seasonably notifying of cancellation or if ~~he the party~~ brings an action with respect only to past installments or demands performance as to future installments.

SECTION 66. Section 2.613, Business & Commerce Code, is amended to read as follows:

Sec. 2.613. Casualty to Identified Goods

~~Where~~ If the contract requires for its performance goods identified when the contract is made, and the goods suffer casualty without fault of either party before the risk of loss passes to the buyer, ~~or in a proper case under a "no arrival, no sale" term (Section 2.324)~~ then:

(1) if the loss is total the contract is ~~avoided~~ terminated; and

(2) if the loss is partial or the goods have so deteriorated as ~~that they~~ no longer ~~to~~ conform to the contract, the buyer may nevertheless demand inspection and at ~~his the buyer's~~ option either treat the contract as ~~avoided terminated~~ or accept the goods with due allowance from the contract price for the deterioration or the deficiency in quantity but without further right against the seller.

SECTION 67. Section 2.614, Business & Commerce Code, is amended to read as follows:

Sec. 2.614. Substituted Performance

(a) ~~Where~~ If without fault of either party the agreed berthing, loading, or unloading facilities fail or an agreed type of carrier becomes unavailable or the agreed manner of ~~delivery performance~~ otherwise becomes commercially

impracticable but a commercially reasonable substitute is available, ~~such~~ the substitute performance must be tendered and accepted.

(b) If the agreed means or manner of payment fails because of domestic or foreign governmental regulation, the seller may withhold or stop delivery unless the buyer provides a means or manner of payment which is commercially a substantial equivalent. If delivery has already been taken, payment by the means or in the manner provided by the regulation discharges the buyer's obligation unless the regulation is discriminatory, oppressive or predatory.

SECTION 68. Section 2.615, Business & Commerce Code, is amended to read as follows:

Sec. 2.615. Excuse by Failure of Presupposed Conditions

Except ~~so far as to the extent that~~ a seller may have assumed a greater obligation and subject to ~~the preceding section on substituted performance~~ Section 2.614:

(1) ~~Delay in delivery or non-delivery performance or nonperformance~~ in whole or in part by a seller ~~who~~ that complies with Subdivisions (2) and (3) is not a breach of ~~his~~ the seller's duty under a contract for sale if performance as agreed has been made impracticable by the occurrence of a contingency the ~~non-occurrence~~ nonoccurrence of which was a basic assumption on which the contract was made or by compliance in good faith with any applicable foreign or domestic governmental regulation or order whether or not it later proves to be invalid.

(2) ~~Where~~ If the causes mentioned in Subdivision (1) affect only a part of the seller's capacity to perform, ~~he~~ the seller must allocate production and deliveries among ~~his~~ its customers but may at ~~his~~ its option include regular customers not then under contract as well as ~~his~~ its own requirements for further manufacture. ~~He~~ The seller may so allocate in any manner ~~which~~ that is fair and reasonable.

(3) The seller must notify the buyer seasonably that there will be delay or ~~nonperformance non-delivery~~ and, ~~when~~ if allocation is required under Subdivision (2), of the estimated quota thus made available for the buyer.

SECTION 69. Section 2.616, Business & Commerce Code, is amended to read as follows:

Sec. 2.616. Procedure on Notice Claiming Excuse

(a) ~~Where the~~ If a buyer receives notification of a material or indefinite delay or an allocation justified under ~~the preceding section~~ Section 2.615, ~~the buyer~~ may by ~~written~~ notification in a record to the seller as to any ~~delivery performance~~ concerned, and ~~where~~ if the prospective deficiency substantially impairs the value of the whole contract under ~~the provisions of this chapter relating to breach of installment contracts (Section 2.612)~~ Section 2.612, then also as to the ~~whole~~, whole:

(1) terminate and thereby discharge any unexecuted portion of the contract; or

(2) modify the contract by agreeing to take ~~his~~ the buyer's available quota in substitution.

(b) If after receipt of ~~such~~ notification from the seller the buyer fails ~~so~~ to modify the contract within a reasonable time not exceeding ~~thirty~~ 30 days, the contract ~~lapses~~ is terminated with respect to any ~~deliveries~~ performance affected.

(c) The provisions of this section may not be negated by agreement except insofar as the seller has assumed a greater obligation under ~~the preceding section~~ Section 2.615.

SECTION 70. Section 2.702, Business & Commerce Code, is amended to read as follows:

Sec. 2.702. Seller's Remedies on Discovery of Buyer's Insolvency

(a) ~~Where~~ If the seller discovers ~~the buyer to be~~ that the buyer is insolvent, ~~he~~ the seller may refuse delivery except for cash including payment for all goods theretofore delivered under the contract, and stop delivery under ~~this chapter (Section 2.705)~~ Section 2.705.

(b) ~~Where~~ If the seller discovers that the buyer has received goods on credit while insolvent, ~~he~~ the seller may reclaim the goods upon demand made within ~~ten days~~ a reasonable time after the buyer's receipt of the goods, ~~but if misrepresentation of solvency has been made to the particular seller in writing within three months before delivery the ten day limitation does not apply.~~ Except as provided in this subsection, the seller may not base a right to reclaim goods on the buyer's fraudulent or innocent misrepresentation of solvency or of intent to pay.

(c) The seller's right to reclaim under Subsection (b) is subject to the rights of a buyer in ordinary course of business or other good-faith purchaser for value under ~~this chapter (Section 2.403)~~ Section 2.403. Successful reclamation of goods excludes all other remedies with respect to them.

SECTION 71. Section 2.703, Business & Commerce Code, is amended to read as follows:

Sec. 2.703. Seller's Remedies in General

(a) A breach of contract by the buyer includes the buyer's wrongful rejection or wrongful attempt to revoke acceptance of goods, wrongful failure to perform a contractual obligation, failure to make a payment when due, and repudiation.

(b) If the buyer is in breach of contract the seller, to the extent provided for by this title or other law, may:

- (1) withhold delivery of the goods;
- (2) stop delivery of the goods under Section 2.705;
- (3) proceed under Section 2.704 with respect to goods unidentified to the contract or unfinished;
- (4) reclaim the goods under Section 2.507(b) or 2.702(b);
- (5) require payment directly from the buyer under Section 2.325(c);
- (6) cancel;

(7) resell and recover damages under Section 2.706;  
(8) recover damages for nonacceptance or repudiation under Section 2.708(a);

(9) recover lost profits under Section 2.708(b);  
(10) recover the price under Section 2.709;  
(11) obtain specific performance under Section 2.716;  
(12) recover liquidated damages under Section 2.718;  
(13) in other cases, recover damages in any manner that is reasonable under the circumstances.

(c) If the buyer becomes insolvent, the seller may:

- (1) withhold delivery under Section 2.702(a);
- (2) stop delivery of the goods under Section 2.705;
- (3) reclaim the goods under Section 2.702(b).

(d) An aggrieved seller must take such measures as are reasonable under the circumstances to mitigate damages resulting from the breach. If the seller fails to take such measures, the buyer may claim a reduction in damages in the amount by which the loss should have been mitigated.

~~Where the buyer wrongfully rejects or revokes acceptance of goods or fails to make a payment due on or before delivery or repudiates with respect to a part or the whole, then with respect to any goods directly affected and, if the breach is of the whole contract (Section 2.612), then also with respect to the whole undelivered balance, the aggrieved seller may~~

- ~~(1) withhold delivery of such goods;~~
- ~~(2) stop delivery by any bailee as hereafter provided (Section 2.705);~~
- ~~(3) proceed under the next section respecting goods still unidentified to the contract;~~
- ~~(4) resell and recover damages as hereafter provided (Section 2.706);~~
- ~~(5) recover damages for non-acceptance (Section 2.708) or in a proper case the price (Section 2.709);~~
- ~~(6) cancel.~~

SECTION 72. Section 2.704, Business & Commerce Code, is amended to read as follows:

Sec. 2.704. Seller's Right to Identify Goods to the Contract Notwithstanding Breach or to Salvage Unfinished Goods

(a) An aggrieved seller under the preceding section may, may in an appropriate case involving breach by the buyer:

- (1) identify to the contract conforming goods not already identified if at the time ~~he~~ the seller learned of the breach ~~they~~ the goods are in ~~his~~ the seller's possession or control;
- (2) treat as the subject of resale goods ~~which~~ that have demonstrably been intended for the particular contract even ~~though~~ if those goods are unfinished.

(b) ~~Where~~ If the goods are unfinished, an aggrieved seller may in the exercise of reasonable commercial judgment for the purposes of avoiding loss and of effective realization either complete the manufacture and wholly identify the goods to the contract or cease manufacture and resell for scrap or salvage value or proceed in any other reasonable manner.

SECTION 73. Section 2.705, Business & Commerce Code, is amended to read as follows:

Sec. 2.705. Seller's Stoppage of Delivery in Transit or Otherwise

(a) ~~The A~~ seller may stop delivery of goods in the possession of a carrier or other bailee ~~when he if the seller~~ discovers the buyer to be insolvent (Section 2.702) ~~and may stop delivery of carload, truckload, plane load or larger shipments of express or freight or when if~~ the buyer repudiates or fails to make a payment due before delivery or if for any other reason the seller has a right to withhold or reclaim the goods.

(b) As against such buyer the seller may stop delivery until:

- (1) receipt of the goods by the buyer; ~~or~~
- (2) acknowledgment to the buyer by any bailee of the goods, except a carrier, that the bailee holds the goods for the buyer; ~~or~~
- (3) such acknowledgment to the buyer by a carrier by reshipment or as warehouse; or
- (4) negotiation to the buyer of any negotiable document of title covering the goods.

(c)(1) To stop delivery the seller must so notify as to enable the bailee by reasonable diligence to prevent delivery of the goods.

(2) After such notification the bailee must hold and deliver the goods according to the directions of the seller but the seller is liable to the bailee for any ensuing charges or damages.

(3) If a negotiable document of title has been issued for goods, the bailee is not obliged to obey a notification to stop until surrender of possession or control of the document.

(4) A carrier ~~who that~~ has issued a ~~non-negotiable~~ nonnegotiable bill of lading is not obliged to obey a notification to stop received from a person other than the consignor.

SECTION 74. Section 2.706, Business & Commerce Code, is amended to read as follows:

Sec. 2.706. Seller's Resale Including Contract for Resale

(a) ~~Under the conditions stated in Section 2.703 on seller's remedies~~ In an appropriate case involving breach by the buyer, the seller may resell the goods concerned or the undelivered balance thereof. ~~Where~~ If the resale is made in good faith and in a commercially reasonable manner, the seller may recover the difference between the contract price and the resale price ~~and the contract price~~ together with any incidental or consequential damages allowed under ~~the provisions of this chapter (Section 2.710)~~ Section 2.710, but less expenses saved in consequence of the buyer's breach.

(b) Except as otherwise provided in Subsection (c) or unless otherwise agreed, resale may be at public or private sale including sale by way of one or more contracts to sell or of identification to an existing contract of the seller. Sale may be as a unit or in parcels and at any time and place, and on any terms, but every aspect of the sale including the method, manner, time, place and terms must be commercially reasonable. The resale must be reasonably identified as referring to the broken contract, but it is not necessary that the goods be in existence or that any or all of them have been identified to the contract before the breach.

(c) ~~Where~~ If the resale is at private sale, the seller must give the buyer reasonable notification of ~~his~~ an intention to resell.

(d) ~~Where~~ If the resale is at public sale:

(1) only identified goods ~~can~~ may be sold ~~except where~~ unless there is a recognized market for a public sale of futures in goods of the kind; ~~and~~

(2) it must be made at a usual place or market for public sale if one is reasonably available and except in the case of goods which are perishable or threaten to decline in value speedily the seller must give the buyer reasonable notice of the time and place of the resale; ~~and~~

(3) if the goods are not to be within the view of those attending the sale, the notification of sale must state the place where the goods are located and provide for their reasonable inspection by prospective bidders; and

(4) the seller may buy.

(e) A purchaser ~~who that~~ buys in good faith at a resale takes the goods free of any rights of the original buyer even ~~though if~~ the seller fails to comply with one or more of the requirements of this section.

(f) The seller is not accountable to the buyer for any profit made on any resale. A person in the position of a seller (Section 2.707) or a buyer ~~who that~~ has rightfully rejected or justifiably revoked acceptance must account for any excess over the amount of ~~his~~ the buyer's security interest, ~~as hereinafter defined (Subsection (c) of Section 2.711) under Section 2.711(c).~~

(g) Failure of a seller to resell under this section does not bar the seller from any other remedy, but to the extent the seller makes a proper resale under this section the seller may not recover greater damages based on market price under Section 2.708.

SECTION 75. Section 2.707. Business & Commerce Code, is amended to read as follows:

Sec. 2.707. "Person in the Position of a Seller"

(a) A "person in the position of a seller" includes as against a principal an agent ~~who that~~ has paid or become responsible for the price of goods on behalf of ~~his~~ the principal or ~~anyone~~ a person ~~who that~~ otherwise holds a security interest or other right in goods similar to that of a seller.

(b) A person in the position of a seller may as provided in this chapter withhold or stop delivery (Section 2.705) and resell (Section 2.706) and recover

incidental damages (Section 2.710) has the same remedies as a seller under this chapter.

SECTION 76. Section 2.708, Business & Commerce Code, is amended to read as follows:

Sec. 2.708. Seller's Damages for ~~Non-Acceptance~~ Nonacceptance or Repudiation

(a) Subject to Subsection (b) and to the provisions of this chapter with respect to proof of market price (Section 2.723), Section 2.723:

(1) the measure of damages for ~~non-acceptance or repudiation~~ nonacceptance by the buyer is the difference between the contract price and the market price at the time and place for tender and the unpaid contract price together with any incidental or consequential damages provided in this chapter (Section 2.710) Section 2.710, but less expenses saved in consequence of the buyer's ~~breach.~~ breach; and

(2) the measure of damages for repudiation by the buyer is the difference between the contract price and the market price at the place for tender at the expiration of a commercially reasonable time after the seller learned of the repudiation, but no later than the time stated in Subdivision (1), together with any incidental or consequential damages provided in Section 2.710, less expenses saved in consequence of the buyer's breach.

(b) If the measure of damages provided in Subsection (a) or in Section 2.706 is inadequate to put the seller in as good a position as performance would have ~~done then done,~~ the measure of damages is the profit (including reasonable overhead) which that the seller would have made from full performance by the buyer, together with any incidental or consequential damages provided in this chapter (Section 2.710), due allowance for costs reasonably incurred and due credit for payments or proceeds of resale.

SECTION 77. Section 2.709, Business & Commerce Code, is amended to read as follows:

Sec. 2.709. Action for the Price

(a) ~~When~~ If the buyer fails to pay the price as it becomes due, the seller may recover, together with any incidental or consequential damages under ~~the next section~~ Section 2.710, the price:

(1) of goods accepted or of conforming goods lost or damaged within a commercially reasonable time after risk of their loss has passed to the buyer; and

(2) of goods identified to the contract if the seller is unable after reasonable effort to resell them at a reasonable price or the circumstances reasonably indicate that such effort will be unavailing.

(b) ~~Where~~ If the seller sues for the price, ~~he~~ the seller must hold for the buyer any goods ~~which that~~ have been identified to the contract and are still in ~~his the seller's control except that~~ control. However, if resale becomes possible, ~~he~~ the seller may resell them at any time prior to the collection of the

judgment. The net proceeds of any such resale must be credited to the buyer, and payment of the judgment entitles ~~him~~ the buyer to any goods not resold.

(c) After the buyer has wrongfully rejected or revoked acceptance of the goods or has failed to make a payment due or has repudiated (Section 2.610), a seller ~~who~~ that is held not entitled to the price under this section shall nevertheless be awarded damages for nonacceptance under ~~the preceding section~~ Section 2.708.

SECTION 78. Section 2.710, Business & Commerce Code, is amended to read as follows:

Sec. 2.710. Seller's Incidental and Consequential Damages

(a) Incidental damages to an aggrieved seller include any commercially reasonable charges, expenses or commissions incurred in stopping delivery, in the transportation, care, and custody of goods after the buyer's breach, in connection with return or resale of the goods or otherwise resulting from the breach.

(b) Consequential damages resulting from the buyer's breach include any loss resulting from general or particular requirements and needs of which the buyer at the time of contracting had reason to know and which could not reasonably be prevented by resale or otherwise.

(c) In a consumer contract, a seller may not recover consequential damages from a consumer.

SECTION 79. Section 2.711, Business & Commerce Code, is amended to read as follows:

Sec. 2.711. Buyer's Remedies in General; Buyer's Security Interest in Rejected Goods

(a) A breach of contract by the seller includes the seller's wrongful failure to deliver or to perform a contractual obligation, making of a nonconforming tender of delivery or performance, and repudiation.

(b) If the seller is in breach of contract under Subsection (a), the buyer, to the extent provided for by this title or other law, may:

(1) in the case of rightful cancellation, rightful rejection, or justifiable revocation of acceptance, recover so much of the price as has been paid;

(2) deduct damages from any part of the price still due under Section 2.717;

(3) cancel;

(4) cover and have damages under Section 2.712 as to all goods affected whether or not they have been identified to the contract;

(5) recover damages for nondelivery or repudiation under Section 2.713;

(6) recover damages for breach with regard to accepted goods or breach with regard to a remedial promise under Section 2.714;

(7) recover identified goods under Section 2.502;

(8) obtain specific performance or obtain the goods by replevin or similar remedy under Section 2.716;

(9) recover liquidated damages under Section 2.718;

(10) in other cases, recover damages in any manner that is reasonable under the circumstances.

~~(a) Where the seller fails to make delivery or repudiates or the buyer rightfully rejects or justifiably revokes acceptance then with respect to any goods involved, and with respect to the whole if the breach goes to the whole contract (Section 2.612), the buyer may cancel and whether or not he has done so may in addition to recovering so much of the price as has been paid~~

~~(1) “cover” and have damages under the next section as to all the goods affected whether or not they have been identified to the contract; or~~

~~(2) recover damages for non-delivery as provided in this chapter (Section 2.713);~~

~~(b) Where the seller fails to deliver or repudiates the buyer may also~~

~~(1) if the goods have been identified recover them as provided in this chapter (Section 2.502); or~~

~~(2) in a proper case obtain specific performance or replevy the goods as provided in this chapter (Section 2.716);~~

(c) On rightful rejection or justifiable revocation of acceptance a buyer has a security interest in goods in ~~his~~ the buyer’s possession or control for any payments made on their price and any expenses reasonably incurred in their inspection, receipt, transportation, care and custody and may hold such goods and resell them in like manner as an aggrieved seller (Section 2.706).

(d) An aggrieved buyer must take such measures as are reasonable under the circumstances to mitigate damages resulting from the breach. If the buyer fails to take such measures, the seller may claim a reduction in damages in the amount by which the loss should have been mitigated.

SECTION 80. Section 2.712, Business & Commerce Code, is amended to read as follows:

Sec. 2.712. “Cover”; Buyer’s Procurement of Substitute Goods

~~(a) After a breach within the preceding section~~ If the seller wrongfully fails to deliver or repudiates or the buyer rightfully rejects or justifiably revokes acceptance, the buyer may “cover” by making in good faith and without unreasonable delay any reasonable purchase of or contract to purchase goods in substitution for those due from the seller.

~~(b) The A~~ A buyer may recover from the seller as damages the difference between the cost of cover and the contract price together with any incidental or consequential damages ~~as hereinafter defined (Section 2.715)~~ under Section 2.715, but less expenses saved in consequence of the seller’s breach.

~~(c) Failure of the buyer to effect cover within this section does not bar him~~ the buyer from any other remedy, but to the extent the buyer makes a proper cover under this section the buyer may not recover damages based on market price under Section 2.713.

SECTION 81. Section 2.713, Business & Commerce Code, is amended to read as follows:

Sec. 2.713. Buyer's Damages for ~~Non-Delivery~~ Nondelivery or Repudiation

(a) ~~Subject to the provisions of this chapter with respect to proof of market price (Section 2.723), Section 2.723, if the seller wrongfully fails to deliver or repudiates or the buyer rightfully rejects or justifiably revokes acceptance:~~

(1) the measure of damages for non-delivery or repudiation in the case of wrongful failure to deliver by the seller or rightful rejection or justifiable revocation of acceptance by the buyer is the difference between the market price at the time when the buyer learned of the breach and the contract price together with any incidental and or consequential damages provided in this chapter (Section 2.715) under Section 2.715, but less expenses saved in consequence of the seller's breach; breach; and

(2) the measure of damages for repudiation by the seller is the difference between the market price at the expiration of a commercially reasonable time after the buyer learned of the repudiation, but no later than the time for tender under the contract, and the contract price together with any incidental or consequential damages provided in this chapter (Section 2.715), less expenses saved in consequence of the seller's breach.

(b) Market price is to be determined as of the place for tender or, in cases of rejection after arrival or revocation of acceptance, as of the place of arrival.

SECTION 82. Section 2.714, Business & Commerce Code, is amended to read as follows:

Sec. 2.714. Buyer's Damages for Breach in Regard to Accepted Goods

(a) ~~Where~~ If the buyer has accepted goods and given notification ~~(Subsection (e) of Section 2.607) he~~ pursuant to Section 2.607(c), the buyer may recover as damages for any ~~non-conformity~~ nonconformity of tender the loss resulting in the ordinary course of events from the seller's breach as determined in any reasonable manner ~~which is reasonable~~.

(b) The measure of damages for breach of warranty is the difference at the time and place of acceptance between the value of the goods accepted and the value they would have had if they had been as warranted, unless special circumstances show proximate damages of a different amount.

(c) In a proper case any incidental and consequential damages under ~~the next section~~ Section 2.715 may also be recovered.

SECTION 83. Section 2.716, Business & Commerce Code, is amended to read as follows:

Sec. 2.716. ~~Buyer's Right to Specific Performance or;~~ Buyer's Right to Replevin

(a) Specific performance may be decreed ~~where~~ if the goods are unique or in other proper circumstances. In a contract other than a consumer contract, specific performance may also be decreed if the parties have agreed to that remedy. However, even if the parties agree to specific performance, specific

performance may not be decreed if the breaching party's sole remaining contractual obligation is the payment of money.

(b) The decree for specific performance may include such terms and conditions as to payment of the price, damages, or other relief as the court may deem just.

(c) The buyer has a right of replevin or similar remedy for goods identified to the contract if after reasonable effort ~~he~~ the buyer is unable to effect cover for such goods or the circumstances reasonably indicate that such effort will be unavailing or if the goods have been shipped under reservation and satisfaction of the security interest in them has been made or tendered. ~~In the case of goods bought for personal, family, or household purposes, the buyer's right of replevin vests upon acquisition of a special property, even if the seller had not then repudiated or failed to deliver.~~

(d) The buyer's right under Subsection (c) vests upon acquisition of a special property, even if the seller had not then repudiated or failed to deliver.

SECTION 84. Section 2.717, Business & Commerce Code, is amended to read as follows:

Sec. 2.717. Deduction of Damages from the Price

The buyer on notifying the seller of ~~his~~ the intention to do so may deduct all or any part of the damages resulting from any breach of the contract from any part of the price still due under the same contract.

SECTION 85. Section 2.718, Business & Commerce Code, is amended to read as follows:

Sec. 2.718. Liquidation or Limitation of Damages; Deposits

(a) Damages for breach by either party may be liquidated in the agreement but only at an amount ~~which~~ that is reasonable in the light of the anticipated ~~and~~ or actual harm caused by the breach, the difficulties of proof of loss, and the inconvenience or nonfeasibility ~~non-feasibility~~ of otherwise obtaining an adequate remedy. A term fixing unreasonably large liquidated damages is void as a penalty. Section 2.719 determines the enforceability of a term that limits but does not liquidate damages.

(b) ~~Where~~ If the seller justifiably withholds delivery of goods or stops performance because of the buyer's breach or insolvency, the buyer is entitled to restitution of any amount by which the sum of ~~his~~ the buyer's payments exceeds ~~(1)~~ the amount to which the seller is entitled by virtue of terms liquidating the seller's damages in accordance with Subsection (a), ~~or (2) in the absence of such terms, twenty per cent of the value of the total performance for which the buyer is obligated under the contract or \$500, whichever is smaller.~~

(c) The buyer's right to restitution under Subsection (b) is subject to offset to the extent that the seller establishes:

(1) a right to recover damages under the provisions of this chapter other than Subsection ~~(a)~~, (a); and

(2) the amount or value of any benefits received by the buyer directly or indirectly by reason of the contract.

(d) ~~Where~~ If a seller has received payment in goods, their reasonable value or the proceeds of their resale shall be treated as payments for the purposes of Subsection ~~(b); but~~ (b). ~~However,~~ if the seller has notice of the buyer's breach before reselling goods received in part performance, ~~his~~ the resale is subject to the conditions ~~laid down in~~ of this chapter on resale by an aggrieved seller (Section 2.706).

SECTION 86. Section 2.722, Business & Commerce Code, is amended to read as follows:

Sec. 2.722. Who ~~Can~~ May Sue Third Parties for Injury to Goods

~~Where~~ If a third party so deals with goods ~~which that~~ have been identified to a contract for sale as to cause actionable injury to a party to that contract:

(1) a right of action against the third party is in either party to the contract for sale ~~who that~~ has title to or a security interest or a special property or an insurable interest in the ~~goods;~~ goods, and if the goods have been destroyed or converted, a right of action is also in the party ~~who that~~ either bore the risk of loss under the contract for sale or has since the injury assumed that risk as against the other;

(2) if at the time of the injury the party plaintiff did not bear the risk of loss as against the other party to the contract for sale and there is no arrangement between them for disposition of the recovery, ~~his~~ the party plaintiff's suit or settlement is, subject to ~~his~~ its own interest, as a fiduciary for the other party to the contract; and

(3) either party may with the consent of the other sue for the benefit of whom it may concern.

SECTION 87. Section 2.723, Business & Commerce Code, is amended to read as follows:

Sec. 2.723. Proof of Market: Time and Place

~~(a) If an action based on anticipatory repudiation comes to trial before the time for performance with respect to some or all of the goods, any damages based on market price (Section 2.708 or Section 2.713) shall be determined according to the price of such goods prevailing at the time when the aggrieved party learned of the repudiation.~~

~~(b)~~ (a) If evidence of a price prevailing at the times or places described in this chapter is not readily available, the price prevailing within any reasonable time before or after the time described or at any other place ~~which that~~ in commercial judgment or under usage of trade would serve as a reasonable substitute for the one described may be used, making any proper allowance for the cost of transporting the goods to or from ~~such~~ the other place.

~~(c)~~ (b) Evidence of a relevant price prevailing at a time or place other than the one described in this chapter offered by one party is not admissible unless and until ~~he~~ the party has given the other party such notice as the court finds sufficient to prevent unfair surprise.

SECTION 88. Section 2.724, Business & Commerce Code, is amended to read as follows:

## Sec. 2.724. Admissibility of Market Quotations

~~Whenever~~ If the prevailing price or value of any goods regularly bought and sold in any established commodity market is in issue, reports in official publications or trade journals or in newspapers ~~or periodicals, periodicals, or other means of communication in~~ of general circulation published as the reports of ~~such~~ the market ~~shall be~~ are admissible in evidence. The circumstances of the preparation of such a report may be shown to affect its weight but not its admissibility.

SECTION 89. Section 2.725, Business & Commerce Code, is amended to read as follows:

## Sec. 2.725. Statute of Limitations in Contracts for Sale

~~(a) An action for breach of any contract for sale must be commenced within four years after the cause of action has accrued. By the original agreement the parties may reduce the period of limitation to not less than one year but may not extend it.~~

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

(a) Except as otherwise provided in this section, an action for breach of any contract for sale must be commenced within the later of four years after the right of action has accrued under Subsection (b) or (c) or one year after the breach was or should have been discovered, but no longer than five years after the right of action accrued. By the original agreement the parties may reduce the period of limitation to not less than one year but may not extend it. However, in a consumer contract, the period of limitation may not be reduced.

(b) Except as otherwise provided in Subsection (c), the following rules apply:

(1) Except as otherwise provided in this subsection, a right of action for breach of a contract accrues when the breach occurs, even if the aggrieved party did not have knowledge of the breach.

(2) For breach of a contract by repudiation, a right of action accrues at the earlier of when the aggrieved party elects to treat the repudiation as a breach or when a commercially reasonable time for awaiting performance has expired.

(3) For breach of a remedial promise, a right of action accrues when the remedial promise is not performed when performance is due.

(4) In an action by a buyer against a person that is answerable over to the buyer for a claim asserted against the buyer, the buyer's right of action against the person answerable over accrues at the time the claim was originally asserted against the buyer.

(c) If a breach of a warranty arising under Section 2.312, 2.313(b), 2.314, or 2.315, or a breach of an obligation, other than a remedial promise, arising under Section 2.313A, is claimed, the following rules apply:

(1) Except as otherwise provided in Subdivision (3), a right of action for breach of a warranty arising under Section 2.313(b), 2.314, or 2.315 accrues when the seller has tendered delivery to the immediate buyer, as defined in Section 2.313, and has completed performance of any agreed installation or assembly of the goods.

(2) Except as otherwise provided in Subdivision (3), a right of action for breach of an obligation, other than a remedial promise, arising under Section 2.313A accrues when the remote purchaser, as defined in Section 2.313A, receives the goods.

(3) If a warranty arising under Section 2.313(b) or an obligation, other than a remedial promise, arising under Section 2.313A explicitly extends to future performance of the goods and discovery of the breach must await the time for performance, the right of action accrues when the immediate buyer as defined in Section 2.313 or the remote purchaser as defined in Section 2.313A discovers or should have discovered the breach.

(4) A right of action for breach of warranty arising under Section 2.312 accrues when the aggrieved party discovers or should have discovered the breach. However, an action for breach of the warranty of noninfringement may not be commenced more than six years after tender of delivery of the goods to the aggrieved party.

~~(e)(d)~~ ~~Where~~ If an action commenced within the time limited by Subsection (a) is so terminated as to leave available a remedy by another action for the same breach, ~~such~~ the other action may be commenced after the expiration of the time limited and within six months after the termination of the first action unless the termination resulted from voluntary discontinuance or from dismissal for failure or neglect to prosecute.

~~(d)(e)~~ This section does not alter the law on tolling of the statute of limitations nor does it apply to causes of action ~~which have~~ that accrued before this title becomes effective.

SECTION 90. Section 2A.103, Business & Commerce Code, is amended to read as follows:

Sec. 2A.103. Definitions and Index of Definitions

(a) In this chapter, unless the context otherwise requires:

(1) ~~“Buyer in ordinary course of business” means a person who in good faith and without knowledge that the sale to him or her is in violation of the ownership rights or security interest or leasehold interest of a third party in the goods buys in ordinary course from a person in the business of selling goods of that kind but does not include a pawnbroker. “Buying” may be for cash or by exchange of other property or on secured or unsecured credit and includes receiving goods or documents of title under a preexisting contract for~~

~~sale but does not include a transfer in bulk or as security for or in total or partial satisfaction of a money debt.~~

~~(2)~~(1) “Cancellation” occurs when either party puts an end to the lease contract for default by the other party.

~~(3)~~(2) “Commercial unit” means such a unit of goods as by commercial usage is a single whole for purposes of lease and division of which materially impairs its character or value on the market or in use. A commercial unit may be a single article, as a machine, or a set of articles, as a suite of furniture or a line of machinery, or a quantity, as a gross or carload, or any other unit treated in use or in the relevant market as a single whole.

~~(4)~~(3) “Conforming” goods or performance under a lease contract means goods or performance that are in accordance with the obligations under the lease contract.

(4) “Conspicuous”, with reference to a term, means so written, displayed, or presented that a reasonable person against which it is to operate ought to have noticed it. A term in an electronic record intended to evoke a response by an electronic agent is conspicuous if it is presented in a form that would enable a reasonably configured electronic agent to take it into account or react to it without review of the record by an individual. Whether a term is “conspicuous” or not is a decision for the court. Conspicuous terms include the following:

(A) for a person:

(i) a heading in capitals equal to or greater in size than the surrounding text, or in contrasting type, font, or color to the surrounding text of the same or lesser size; and

(ii) language in the body of a record or display in larger type than the surrounding text, or in contrasting type, font, or color to the surrounding text of the same size, or set off from surrounding text of the same size by symbols or other marks that call attention to the language; and

(B) for a person or an electronic agent, a term that is so placed in a record or display that the person or electronic agent cannot proceed without taking action with respect to the particular term.

(5) Reserved.

~~(5)~~(6) “Consumer lease” means a lease that a lessor regularly engaged in the business of leasing or selling makes to a lessee ~~who is an individual and who takes under the lease primarily for a personal, family, or household purpose, if the total payments to be made under the lease contract, excluding payments for options to renew or buy, do not exceed \$25,000 a consumer.~~

(7) “Delivery” means the voluntary transfer of physical possession or control of goods.

(8) “Electronic” means relating to technology having electrical, digital, magnetic, wireless, optical, electromagnetic, or similar capabilities.

(9) “Electronic agent” means a computer program or an electronic or other automated means used independently to initiate an action or respond to electronic records or performances in whole or in part, without review or action by an individual.

(10) “Electronic record” means a record created, generated, sent, communicated, received, or stored by electronic means.

~~(6)~~(11) “Fault” means wrongful act, omission, breach, or default.

~~(7)~~(12) “Finance lease” means a lease with respect to which:

(A) the lessor does not select, manufacture, or supply the goods;

(B) the lessor acquires the goods or the right to possession and use of the goods in connection with the lease or, in the case of goods that have been leased previously by the lessor and are not being leased to a consumer, in connection with another lease; and

(C) one of the following occurs:

(i) the lessee receives a copy of the agreement by which the lessor acquired, or proposes to acquire, the goods or the right to possession and use of the goods before signing the lease agreement;

(ii) the lessee’s approval of the agreement or of the general contractual terms under which the lessor acquired or proposes to acquire the goods or the right to possession and use of the goods is a condition to the effectiveness of the lease contract;

(iii) the lessee, before signing the lease agreement, receives an accurate and complete statement designating the promises and warranties, and any disclaimers of warranties, limitations or modifications of remedies, or liquidated damages, including those of a third party, such as the manufacturer of the goods, provided to the lessor by the person supplying the goods in connection with or as part of the contract by which the lessor acquired the goods or the right to possession and use of the goods; or

(iv) if the lease is not a consumer lease, before the lessee signs the lease agreement, the lessor informs the lessee in a record:

(a) of the identity of the person supplying the goods to the lessor, unless the lessee has selected that person and directed the lessor to acquire the goods or the right to possession and use of the goods from that person;

(b) that the lessee is entitled under this chapter to the promises and warranties, including those of any third party, provided to the lessor by the person supplying the goods in connection with or as part of the contract by which the lessor acquired the goods or the right to possession and use of the goods; and

(c) that the lessee may communicate with the person supplying the goods to the lessor and receive an accurate and complete statement of those promises and warranties, including any disclaimers and limitations of them, or a statement of remedies.

~~“Finance lease” means a lease with respect to which:~~

~~(A) the lessor does not select, manufacture, or supply the goods;~~

~~(B) the lessor acquires the goods or the right to possession and use of the goods in connection with the lease; and~~

~~(C) one of the following occurs:~~

~~(i) the lessee receives a copy of the contract by which the lessor acquired the goods or the right to possession and use of the goods before signing the lease contract;~~

~~(ii) the lessee’s approval of the contract by which the lessor acquired the goods or the right to possession and use of the goods is a condition to effectiveness of the lease contract;~~

~~(iii) the lessee, before signing the lease contract, receives an accurate and complete statement designating the promises and warranties, and any disclaimers of warranties, limitations or modifications of remedies, or liquidated damages, including those of a third party, such as the manufacturer of the goods, provided to the lessor by the person supplying the goods in connection with or as part of the contract by which the lessor acquired the goods or the right to possession and use of the goods; or~~

~~(iv) if the lease is not a consumer lease, the lessor, before the lessee signs the lease contract, informs the lessee in writing (a) of the identity of the person supplying the goods to the lessor, unless the lessee has selected that person and directed the lessor to acquire the goods or the right to possession and use of the goods from that person, (b) that the lessee is entitled under this chapter to the promises and warranties, including those of any third party, provided to the lessor by the person supplying the goods in connection with or as part of the contract by which the lessor acquired the goods or the right to possession and use of the goods, and (c) that the lessee may communicate with the person supplying the goods to the lessor and receive an accurate and complete statement of those promises and warranties, including any disclaimers and limitations of them or of remedies.~~

(13) Reserved.

~~(8)(14) “Goods” means all things that are movable at the time of identification to a lease contract or that are fixtures (Section 2A.309) but the term does not include money, documents, instruments, accounts, chattel paper, general intangibles, or minerals and the like, including oil and gas, before extraction. The term includes future goods, specially manufactured goods, and the unborn young of animals. The term does not include the money in which the price is to be paid, investment securities under Chapter 8, or choses in action. The term also includes the unborn young of animals.~~

~~(9)(15) “Installment lease contract” means a lease contract that authorizes or requires the delivery of goods in separate lots to be separately accepted, even though the lease contract contains a clause “each delivery is a separate lease” or its equivalent.~~

~~(10)~~(16) “Lease” means a transfer of the right to possession and use of goods for a term period in return for consideration, but a sale, including a sale on approval or a sale or return, ~~or~~ retention or creation of a security interest, or license of information is not a lease. Unless the context clearly indicates otherwise, the term includes a sublease.

~~(11)~~(17) “Lease agreement”, as distinguished from “lease contract”, means the bargain, with respect to the lease, of the lessor and the lessee in fact as found in their language or inferred by implication from other circumstances including course of performance, course of dealing, or usage of trade dealing or usage of trade or course of performance as provided in Section 1.303, this chapter. Unless the context clearly indicates otherwise, the term includes a sublease agreement.

~~(12)~~(18) “Lease contract”, as distinguished from “lease agreement”, means the total legal obligation that results from the lease agreement as determined by this title as supplemented by affected by this chapter and any other applicable rules of law. Unless the context clearly indicates otherwise, the term includes a sublease contract.

~~(13)~~(19) “Leasehold interest” means the interest of the lessor or the lessee under a lease contract.

~~(14)~~(20) “Lessee” means a person ~~who~~ that acquires the right to possession and use of goods under a lease. Unless the context clearly indicates otherwise, the term includes a sublessee.

~~(15)~~(21) “Lessee in ordinary course of business” means a person that leases goods in good faith, without knowledge that the lease violates the rights of another person, and in the ordinary course from a person, other than a pawnbroker, in the business of selling or leasing goods of that kind. A person leases in ordinary course if the lease to the person comports with the usual or customary practices in the kind of business in which the lessor is engaged or with the lessor’s own usual or customary practices. A lessee in ordinary course of business may lease for cash, by exchange of other property, or on secured or unsecured credit, and may acquire goods or documents of title under a preexisting lease contract. Only a lessee that takes possession of the goods or has a right to recover the goods from the lessor under this chapter may be a lessee in ordinary course of business. A person that acquires goods in a transfer in bulk or as security for or in total or partial satisfaction of a money debt is not a lessee in ordinary course of business.

~~“Lessee in ordinary course of business” means a person who in good faith and without knowledge that the lease to him or her is in violation of the ownership rights or security interest or leasehold interest of a third party in the goods, leases in ordinary course from a person in the business of selling or leasing goods of that kind but does not include a pawnbroker. “Leasing” may be for cash or by exchange of other property or on secured or unsecured credit and includes receiving goods or documents of title under a preexisting lease~~

contract but does not include a transfer in bulk or as security for or in total or partial satisfaction of a money debt.

~~(16)~~(22) “Lessor” means a person ~~who~~ that transfers the right to possession and use of goods under a lease. Unless the context clearly indicates otherwise, the term includes a sublessor.

~~(17)~~(23) “Lessor’s residual interest” means the lessor’s interest in the goods after expiration, termination, or cancellation of the lease contract.

~~(18)~~(24) “Lien” means a charge against or interest in goods to secure payment of a debt or performance of an obligation, ~~but the~~ The term does not include a security interest.

~~(19)~~ (25) “Lot” means a parcel or a single article that is the subject matter of a separate lease or delivery, whether or not it is sufficient to perform the lease contract.

~~(20)~~(26) “Merchant lessee” means a lessee that is a merchant with respect to goods of the kind subject to the lease.

~~(21)~~ “Present value” means the amount as of a date certain of one or more sums payable in the future, discounted to the date certain. The discount is determined by the interest rate specified by the parties if the rate was not manifestly unreasonable at the time the transaction was entered into; otherwise, the discount is determined by a commercially reasonable rate that takes into account the facts and circumstances of each case at the time the transaction was entered into.

~~(22)~~ “Purchase” includes taking by sale, lease, mortgage, security interest, pledge, gift, or any other voluntary transaction creating an interest in goods.

(27) “Sign” means, with present intent to authenticate or adopt a record,

(A) to execute or adopt a tangible symbol; or

(B) to attach to or logically associate with the record an electronic sound, symbol, or process.

~~(23)~~ (28) “Sublease” means a lease of goods the right to possession and use of which was acquired by the lessor as a lessee under an existing lease.

~~(24)~~(29) “Supplier” means a person from ~~whom~~ which a lessor buys or leases goods to be leased under a finance lease.

~~(25)~~(30) “Supply contract” means a contract under which a lessor buys or leases goods to be leased.

~~(26)~~(31) “Termination” occurs when either party pursuant to a power created by agreement or law puts an end to the lease contract otherwise than for default.

(b) Other definitions applying to this chapter and the sections in which they appear are:

“Accessions”. Section 2A.310(a).

“Construction mortgage”. Section 2A.309(a)(4).

“Encumbrance”. Section 2A.309(a)(5).

“Fixtures”. Section 2A.309(a)(1).

“Fixture filing”. Section 2A.309(a)(2).

“Purchase money lease”. Section 2A.309(a)(3).

(c) The following definitions in other chapters apply to this chapter:

~~“Account”. Section 9.102(a)(2).~~

“Between merchants”. Section 2.104(c).

“Buyer”. Section 2.103(a)(1).

~~“Chattel Paper”. Section 9.102(a)(11).~~

“Consumer”. Section 1.201(b)(11).

“Consumer goods”. Section 9.102(a)(23)

~~“Document”. Section 9.102(a)(30).~~

“Entrusting”. Section 2.403(c).

~~“General intangible”. Section 9.102(a)(42).~~

“Good faith”. Section 1.201(b)(20).

~~“Instrument”. Section 9.102(a)(47).~~

“Letter of credit”. Section 5.102(a)(10).

“Merchant”. Section 2.104(a).

~~“Mortgage”. Section 9.102(a)(55).~~

“Present value”. Section 1.201(b)(28).

~~“Pursuant to Commitment”. Section 9.102(a)(69).~~

“Receipt” of goods. Section 2.103(a)(3)(12)

“Record”. Section 1.201(b)(31).

“Sale”. Section 2.106(a).

“Sale on approval”. Section 2.326.

“Sale or return”. Section 2.326.

“Seller”. Section 2.103(a)(4)(15).

(d) In addition chapter 1 contains other general definitions and principles of construction and interpretation applicable throughout this chapter.

SECTION 91. Section 2A.104, Business & Commerce Code, is amended to read as follows:

Sec. 2A.104. Leases Subject to Other Laws

(a) A lease, ~~although~~ subject to this chapter, is also subject to any applicable:

(1) certificate of title statute of this state, including Chapter 501, Transportation Code, Chapter 31, Parks and Wildlife Code, and Subchapter E, Chapter 1201, Occupations Code;

(2) certificate of title statute of another jurisdiction (Section 2A.105); or

(3) rule of law that establishes a different rule for consumers ~~consumer law of this state, both decisional and statutory~~, including, to the extent that they apply to a lease transaction, Chapters 17 and 35 of this code and Chapter 1201, Occupations Code.

(b) ~~To the extent there is a In case of conflict between this chapter, other than Sections 2A.105, 2A.304(c) and 2A.305(c), and any statute or law referred to in Subsection (a), that law governs the statute or law controls.~~

(c) ~~Failure to comply with an applicable statute has only the effect specified therein~~ For purposes of this chapter, failure to comply with a law referred to in Subsection (a) has only the effect specified in that law.

(d) This chapter modifies, limits, and supersedes the federal Electronic Signatures in Global and National Commerce Act, 15 U.S.C. Section 7001 et seq., except that nothing in this chapter modifies, limits, or supersedes Section 7001(c) of that Act or authorizes electronic delivery of any of the notices described in Section 7003(b) of that Act.

SECTION 92. Section 2A.105, Business & Commerce Code, is amended to read as follows:

Sec. 2A.105. Territorial Application of Chapter to Goods Covered by Certificate of Title

(a) This section applies to goods covered by a certificate of title, even if there is no other relationship between the jurisdiction under whose certificate of title the goods are covered and the goods or the lessee or lessor.

(b) Goods become covered by a certificate of title when a valid application for the certificate of title and the application fee are delivered to the appropriate authority. Goods cease to be covered by a certificate of title at the earlier of the time the certificate of title ceases to be effective under the law of the issuing jurisdiction or the time the goods become covered subsequently by a certificate of title issued by another jurisdiction.

(c) Subject to Sections 2A.304(c) and 2A.305(c), with respect to goods covered by a certificate of title under a statute of this state or of another jurisdiction, compliance and the effect of compliance or noncompliance with the certificate-of-title statute are governed by the local law of the jurisdiction whose certificate of title covers the goods from the time the goods become covered by the certificate until the goods cease to be covered by the certificate of title.

~~Subject to the provisions of Sections 2A.304(c) and 2A.305(c), with respect to goods covered by a certificate of title issued under a statute of this State or of another jurisdiction, compliance and the effect of compliance or noneompliance with a certificate of title statute are governed by the law (including the conflict of laws rules) of the jurisdiction issuing the certificate until the earlier of~~

~~(1) surrender of the certificate; or~~

~~(2) four months after the goods are removed from that jurisdiction and thereafter until a new certificate of title is issued by another jurisdiction.~~

SECTION 93. Section 2A.107, Business & Commerce Code, is amended to read as follows:

Sec. 2A.107. Waiver or Renunciation of Claim or Right After Default

A claim or right arising out of an alleged default or breach of warranty may be discharged in whole or in part without consideration by ~~a written waiver or renunciation signed and delivered by the aggrieved party in a signed record.~~

SECTION 94. Section 2A.108, Business & Commerce Code, is amended to read as follows:

Sec. 2A.108. Unconscionability

(a) If the court as a matter of law finds a lease contract or any clause of a lease contract to have been unconscionable at the time it was made, the court may refuse to enforce the lease contract, or it may enforce the remainder of the lease contract without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid any unconscionable result.

(b) With respect to a consumer lease, if the court as a matter of law finds that a lease contract or any clause of a lease contract has been induced by unconscionable conduct or that unconscionable conduct has occurred in the collection of a claim arising from a lease contract, the court may grant appropriate relief.

(c) Before making a finding of unconscionability under Subsection (a) or (b), the court, on its own motion or that of a party, shall afford the parties a reasonable opportunity to present evidence as to the setting, purpose, and effect of the lease contract or clause thereof or of the conduct.

(d) In an action in which the lessee claims unconscionability with respect to a consumer lease:

(1) if the court finds unconscionability under Subsection (a) or (b), the court shall award reasonable attorney's fees to the lessee;

(2) if the court does not find unconscionability and the lessee claiming unconscionability has brought or maintained an action ~~the lessee he or she~~ knew to be groundless, the court shall award reasonable attorney's fees to the party against ~~which whom~~ the claim is made; and

(3) in determining attorney's fees, the amount of the recovery on behalf of the claimant under Subsections (a) and (b) is not controlling.

SECTION 95. Section 2A.109, Business & Commerce Code, is amended to read as follows:

Sec 2A.109. Option to Accelerate at Will

(a) A term providing that one party or the party's successor in interest may accelerate payment or performance or require collateral or additional collateral "at will" or "when the party deems ~~itself himself or herself~~ insecure" or ~~in~~ words of similar import ~~must be construed to mean~~ means that the party has power to do so only if the party in good faith believes that the prospect of payment or performance is impaired.

(b) With respect to a consumer lease, the burden of establishing good faith under Subsection (a) is on the party ~~that has exercised who exercises~~ the power; otherwise the burden of establishing lack of good faith is on the party against ~~which whom~~ the power has been exercised.

SECTION 96. Section 2A.201, Business & Commerce Code, is amended to read as follows:

Sec. 2A.201. Statute of Frauds

(a) A lease contract is not enforceable by way of action or defense unless:

(1) the total payments to be made under the lease contract, excluding payments for options to renew or buy, are less than \$1,000; or

(2) there is a ~~writing record~~, signed by the party against ~~whom~~ which enforcement is sought or by that party's authorized agent, sufficient to indicate that a lease contract has been made between the parties and to describe the goods leased and the lease term.

(b) Any description of leased goods or of the lease term is sufficient and satisfies Subsection (a)(2), whether or not it is specific, if it reasonably identifies what is described.

(c) A ~~writing record~~ is not insufficient because it omits or incorrectly states a term agreed upon, but the lease contract is not enforceable under Subsection (a)(2) beyond the lease term and the quantity of goods shown in the ~~writing record~~.

(d) A lease contract that does not satisfy the requirements of Subsection (a), but which is valid in other respects, is enforceable:

(1) if the goods are to be specially manufactured or obtained for the lessee and are not suitable for lease or sale to others in the ordinary course of the lessor's business, and the lessor, before notice of repudiation is received and under circumstances that reasonably indicate that the goods are for the lessee, has made either a substantial beginning of their manufacture or commitments for their procurement;

(2) if the party against ~~whom~~ which enforcement is sought admits in ~~that~~ the party's pleading, ~~testimony or otherwise in court~~ or in the party's testimony or otherwise under oath that a lease contract was made, but the lease contract is not enforceable under this ~~provision~~ subdivision beyond the quantity of goods admitted;

(3) with respect to goods that have been received and accepted by the lessee; or

(4) if the lease contract would otherwise be enforceable under general principles of equitable estoppel, detrimental reliance or unjust enrichment.

(e) The lease term under a lease contract referred to in Subsection (d) is:

(1) if there is a ~~writing record~~ signed by the party against ~~whom~~ which enforcement is sought or by that party's authorized agent specifying the lease term, the term so specified;

(2) if the party against ~~whom~~ which enforcement is sought admits in ~~that~~ the party's pleading, ~~testimony or otherwise in court~~ or in the party's testimony or otherwise under oath a lease term, the term so admitted; or

(3) a reasonable lease term.

(f) A lease contract that is enforceable under this section is not unenforceable merely because it is not capable of being performed within one year or any other period after its making.

SECTION 97. Section 2A.202, Business & Commerce Code, is amended to read as follows:

Sec. 2A.202. ~~Final Written~~ Expression in a Record: Parol or Extrinsic Evidence

(a) Terms with respect to which the confirmatory memoranda of the parties agree or which are otherwise set forth in a ~~writing~~ record intended by the parties as a final expression of their agreement with respect to such terms as are included therein may not be contradicted by evidence of any prior agreement or of a contemporaneous oral agreement but may be ~~explained or~~ supplemented by evidence of :

(1) ~~course of performance, course of dealing, or usage of trade (Section 1.303) by course of dealing or usage of trade or by course of performance;~~ and

(2) ~~by evidence of~~ consistent additional terms unless the court finds the ~~writing~~ record to have been intended also as a complete and exclusive statement of the terms of the agreement.

(b) Terms in a record may be explained by evidence of course of performance, course of dealing, or usage of trade without a preliminary determination by the court that the language used is ambiguous.

SECTION 98. Section 2A.203, Business & Commerce Code, is amended to read as follows:

Sec. 2A.203. Seals Inoperative

The affixing of a seal to a record ~~writing~~ evidencing a lease contract or an offer to enter into a lease contract does not render the record ~~writing~~ a sealed instrument and the law with respect to sealed instruments does not apply to the lease contract or offer.

SECTION 99. Section 2A.204, Business & Commerce Code, is amended to read as follows:

Sec. 2A.204. Formation in General

(a) A lease contract may be made in any manner sufficient to show agreement, including offer and acceptance, conduct by both parties which recognizes the existence of a lease contract, the interaction of electronic agents, and the interaction of an electronic agent and an individual.

(b) An agreement sufficient to constitute a lease contract may be found although the moment of its making is undetermined.

(c) ~~Even if Although~~ one or more terms are left open, a lease contract does not fail for indefiniteness if the parties have intended to make a lease contract and there is a reasonably certain basis for giving an appropriate remedy.

SECTION 100. Section 2A.205, Business & Commerce Code, is amended to read as follows:

Sec. 2A.205. Firm Offers

An offer by a merchant to lease goods to or from another person in a signed ~~writing~~ record that by its terms gives assurance it will be held open is not revocable, for lack of consideration, during the time stated or, if no time is stated, for a reasonable time, but in no event may the period of irrevocability exceed three months. Any such term of assurance ~~on a form~~ in a form supplied by the offeree must be separately signed by the offeror.

SECTION 101. Section 2A.208, Business & Commerce Code, is amended to read as follows:

Sec. 2A.208. Modification, Rescission and Waiver

(a) An agreement modifying a lease contract needs no consideration to be binding.

(b) A signed lease agreement that excludes modification or rescission except by a signed ~~writing~~ record may not be otherwise modified or rescinded, but, except as between merchants, such a requirement ~~on a form~~ in a form supplied by a merchant must be separately signed by the other party.

(c) Although an attempt at modification or rescission does not satisfy the requirements of Subsection (b), it may operate as a waiver.

(d) A party ~~who~~ that has made a waiver affecting an executory portion of a lease contract may retract the waiver by reasonable notification received by the other party that strict performance will be required of any term waived, unless the retraction would be unjust in view of a material change of position in reliance on the waiver.

SECTION 102. Section 2A.211, Business & Commerce Code, is amended to read as follows:

Sec. 2A.211. Warranties Against Interference and Against Infringement; Lessee's Obligation Against Infringement

(a) Except in a finance lease, a lessor in a lease contract warrants that, except for claims by any person by way of infringement or the like, for the duration of the lease no person holds:

(1) a claim to or interest in the goods not attributable to the lessee's own act or omission which will interfere with the lessee's enjoyment of its leasehold interest; or

(2) a colorable claim to or interest in the goods which will unreasonably expose the lessee to litigation.

(b) A finance lessor warrants that, except for claims by way of infringement or the like, for the duration of the lease no person holds:

(1) a claim or interest in the goods that arose from an act or omission of the lessor which will interfere with the lessee's enjoyment of its leasehold interest; or

(2) a colorable claim to or interest in the goods that arose from an act or omission of the lessor which will unreasonably expose the lessee to litigation.

(c) Except in a finance lease, a lessor that is a merchant regularly dealing in goods of the kind warrants that the goods will be delivered free of the

rightful claim of a third party by way of infringement or the like. However, a lessee that furnishes specifications to a lessor or a supplier holds the lessor and the supplier harmless against any claim of infringement or the like that arises out of compliance with the specifications.

(d) A warranty under this section may be excluded or modified only by specific language that is conspicuous and contained in a record, or by circumstances, including course of performance, course of dealing, or usage of trade, that give the lessee reason to know that the lessor purports to transfer only such right as the lessor or a third party may have, or that it is leasing subject to any claims of infringement or the like.

~~(a) There is in a lease contract a warranty that for the lease term no person holds a claim to or interest in the goods that arose from an act or omission of the lessor other than a claim by way of infringement or the like, which will interfere with the lessee's enjoyment of its leasehold interest.~~

~~(b) Except in a finance lease there is in a lease contract by a lessor who is a merchant regularly dealing in goods of the kind a warranty that the goods are delivered free of the rightful claim of any person by way of infringement or the like.~~

~~(c) A lessee who furnishes specifications to a lessor or a supplier shall hold the lessor and the supplier harmless against any claim by way of infringement or the like that arises out of compliance with the specifications.~~

SECTION 103. Section 2A.212, Business & Commerce Code, is amended to read as follows:

Sec. 2A.212. Implied Warranty of Merchantability

(a) Except in a finance lease, a warranty that the goods will be merchantable is implied in a lease contract if the lessor is a merchant with respect to goods of that kind.

(b) Goods to be merchantable must be at least such as:

(1) pass without objection in the trade under the description in the lease agreement;

(2) in the case of fungible goods, are of fair average quality within the description;

(3) are fit for the ordinary purposes for which goods of that description ~~type~~ are used;

(4) run, within the variation permitted by the lease agreement, of even kind, quality, and quantity within each unit and among all units involved;

(5) are adequately contained, packaged, and labeled as the lease agreement may require; and

(6) conform to any promises or affirmations of fact made on the container or label.

(c) Other implied warranties may arise from course of dealing or usage of trade.

SECTION 104. Section 2A.214, Business & Commerce Code, is amended to read as follows:

## Sec. 2A-214. Exclusion or Modification of Warranties

(a) Words or conduct relevant to the creation of an express warranty and words or conduct tending to negate or limit a warranty must be construed wherever reasonable as consistent with each other; but, subject to the provisions of Section 2A.202 ~~on parol or extrinsic evidence~~, negation or limitation is inoperative to the extent that the construction is unreasonable.

(b) Subject to Subsection (c), to exclude or modify the implied warranty of merchantability or any part of it the language must be in a record and be conspicuous. In a consumer lease the language must state “The lessor undertakes no responsibility for the quality of the goods except as otherwise provided in this contract,” and in any other contract the language must mention “merchantability,” be by a writing, and be conspicuous. Subject to Subsection (c), to exclude or modify ~~an~~ the implied warranty of fitness the exclusion must be in a record by a writing and be conspicuous. Language to exclude all implied warranties of fitness in a consumer lease must state “The lessor assumes no responsibility that the goods will be fit for any particular purpose for which you may be leasing these goods, except as otherwise provided in the contract,” and in any other contract the language is sufficient if it is in writing, is conspicuous and states, for example, that “There is are no warranty warranties that the goods will be fit for a particular purpose extend beyond the description on the face hereof.” Language that satisfies the requirements of this subsection for a consumer lease also satisfies its requirements for any other lease contract.

(c) Notwithstanding Subsection (b); ~~but subject to Subsection (d)~~

(1) unless the circumstances indicate otherwise, all implied warranties are excluded by expressions like “as is”, “with all faults”, or ~~by~~ other language that in common understanding calls the lessee’s attention to the exclusion of warranties and makes plain that there is no implied warranty, if in writing a record and conspicuous;

(2) if the lessee before entering into the lease contract has examined the goods or the sample or model as fully as desired or has refused to examine the goods, after a demand by the lessor there is no implied warranty with regard to defects that an examination ought in the circumstances to have revealed to the lessee; and

(3) an implied warranty may also be excluded or modified by course of dealing, or course of performance, or usage of trade.

(d) Remedies for breach of warranty can be limited in accordance with Section 2A.503 and 2A.504.

~~(d) To exclude or modify a warranty against interference or against infringement (Section 2A.211) or any part of it, the language must be specific, be by a writing, and be conspicuous, unless the circumstances, including course of performance, course of dealing, or usage of trade, give the lessee reason to know that the goods are being leased subject to a claim or interest of any person.~~

SECTION 105. Section 2A.219, Business & Commerce Code, is amended to read as follows:

Sec. 2A.219. Risk of Loss

(a) Except in the case of a finance lease, risk of loss is retained by the lessor and does not pass to the lessee. In the case of a finance lease, risk of loss passes to the lessee.

(b) Subject to ~~the provisions of this chapter on the effect of default on risk of loss (Section 2A.220)~~, if risk of loss is to pass to the lessee and the time of passage is not stated, the following rules apply:

(1) If the lease contract requires or authorizes the goods to be shipped by carrier

(A) and it does not require delivery at a particular destination, the risk of loss passes to the lessee when the goods are ~~duly~~ delivered to the carrier; but

(B) if it does require delivery at a particular destination and the goods are there ~~duly~~ tendered while in the possession of the carrier, the risk of loss passes to the lessee when the goods are there ~~duly~~ so tendered as to enable the lessee to take delivery.

(2) If the goods are held by a bailee to be delivered without being moved, the risk of loss passes to the lessee on acknowledgment by the bailee to the lessee of the lessee's right to possession of the goods.

(3) In any case not within Subdivision (1) or (2), the risk of loss passes to the lessee on ~~tender of delivery if the lessee is a merchant; otherwise the risk of loss passes to the lessee on the lessee's receipt of the goods.~~

SECTION 106. Section 2A.221, Business & Commerce Code, is amended to read as follows:

Sec. 2A.221. Casualty to Identified Goods

If a lease contract requires goods identified when the lease contract is made, and the goods suffer casualty without fault of the lessee, the lessor or the supplier before delivery, or the goods suffer casualty before risk of loss passes to the lessee under the lease agreement or Section 2A.219:

(1) if the loss is total, the lease contract is terminated ~~avoided~~; and

(2) if the loss is partial or the goods have so deteriorated as to no longer conform to the lease contract, the lessee may nevertheless demand inspection and at the lessee's option either treat the lease contract as terminated ~~avoided~~ or, except in a finance lease that is not a consumer lease, accept the goods with due allowance from the rent payable for the balance of the lease term for the deterioration or the deficiency in quantity but without further right against the lessor.

SECTION 107. Section 2A.303, Business & Commerce Code, is amended to read as follows:

Sec. 2A.303. Alienability of Party's Interest Under Lease Contract or of Lessor's Residual Interest in Goods; Delegation of Performance; Transfer of Rights

(a) As used in this section, “creation of a security interest” includes the sale of a lease contract that is subject to Chapter 9, ~~Secured Transactions~~, by reason of Section 9.109(a)(3).

(b) Subject to Subsection (c) and except as otherwise provided in Section 9.407 or as otherwise agreed, a provision in a lease agreement which (1) prohibits the voluntary or involuntary transfer, including a transfer by sale, sublease, creation or enforcement of a security interest, or attachment, levy, or other judicial process, of an interest of a party under the lease contract or of the lessor’s residual interest in the goods, or (2) makes such a transfer an event of default, gives rise to the rights and remedies provided in Subsection (d). However, a transfer that is prohibited or is an event of default under the lease agreement is otherwise effective.

(c) A provision in a lease agreement which (1) prohibits a transfer of a right to damages for default with respect to the whole lease contract or of a right to payment arising out of the transferor’s due performance of the transferor’s entire obligation, or (2) makes such a transfer an event of default, is not enforceable, and such a transfer is not a transfer that materially impairs the prospect of obtaining return performance by, materially changes the duty of, or materially increases the burden or risk imposed on, the other party to the lease contract within Subsection (d).

(d) Subject to Subsection (c) and Section 9.407:

(1) if a transfer is made that is an event of default under a lease agreement, the party to the lease contract not making the transfer, unless that party waives the default or otherwise agrees, has the rights and remedies described in Section 2A.501(b):

(2) if Subdivision (1) is not applicable and if a transfer is made that (A) is prohibited under a lease agreement or (B) materially impairs the prospect of obtaining return performance by, materially changes the duty of, or materially increases the burden or risk imposed on, the other party to the lease contract, unless the party not making the transfer agrees at any time to the transfer in the lease contract or otherwise, then, except as limited by contract, (i) the transferor is liable to the party not making the transfer for damages caused by the transfer to the extent that the damages could not reasonably be prevented by the party not making the transfer and (ii) a court having jurisdiction may grant other appropriate relief, including cancellation of the lease contract or an injunction against the transfer.

~~(b) Except as provided in Section 9.407(c), a provision in a lease agreement which (1) prohibits the voluntary or involuntary transfer, including a transfer by sale, sublease, creation or enforcement of a security interest, or attachment, levy, or other judicial process, of an interest of a party under the lease contract or of the lessor’s residual interest in the goods, or (2) makes such a transfer an event of default, gives rise to the rights and remedies provided in Subsection (d), but a transfer that is prohibited or is an event of default under the lease agreement is otherwise effective.~~

~~(e) A provision in a lease agreement which (1) prohibits a transfer of a right to damages for default with respect to the whole lease contract or of a right to payment arising out of the transferor's due performance of the transferor's entire obligation, or (2) makes such a transfer an event of default, is not enforceable, and such a transfer is not a transfer that materially impairs the prospect of obtaining return performance by, materially changes the duty of, or materially increases the burden or risk imposed on, the other party to the lease contract within the purview of Subsection (d).~~

~~(d) Subject to Section 9.407(e):~~

~~(1) if a transfer is made which is made an event of default under a lease agreement, the party to the lease contract not making the transfer, unless that party waives the default or otherwise agrees, has the rights and remedies described in Section 2A.501(b); and~~

~~(2) if Subdivision (1) is not applicable and if a transfer is made that (A) is prohibited under a lease agreement or (B) materially impairs the prospect of obtaining return performance by, materially changes the duty of, or materially increases the burden or risk imposed on, the other party to the lease contract, unless the party not making the transfer agrees at any time to the transfer in the lease contract or otherwise, then, except as limited by contract, (i) the transferor is liable to the party not making the transfer for damages caused by the transfer to the extent that the damages could not reasonably be prevented by the party not making the transfer and (ii) a court having jurisdiction may grant other appropriate relief, including cancellation of the lease contract or an injunction against the transfer.~~

(e) A transfer of "the lease" or of "all my rights under the lease", or a transfer in similar general terms, is a transfer of rights and, unless the language or the circumstances, as in a transfer for security, indicate the contrary, the transfer is a delegation of duties by the transferor to the transferee. Acceptance by the transferee constitutes a promise by the transferee to perform those duties. The promise is enforceable by either the transferor or the other party to the lease contract.

(f) Unless otherwise agreed by the lessor and the lessee, a delegation of performance does not relieve the transferor as against the other party of any duty to perform or of any liability for default.

(g) In a consumer lease, to prohibit the transfer of an interest of a party under the lease contract or to make a transfer an event of default, the language must be specific, by a writing record, and conspicuous.

SECTION 108. Section 2A.304, Business & Commerce Code, is amended to read as follows:

Sec. 2A.304. Subsequent Lease of Goods by Lessor

(a) Subject to Section 2A.303, a subsequent lessee from a lessor of goods under an existing lease contract obtains, to the extent of the leasehold interest transferred, the leasehold interest in the goods that the lessor had or had power to transfer, and except as provided by Subsection (b) or Section 2A.527(d)

takes subject to the existing lease contract. A lessor with voidable title has power to transfer a good leasehold interest to a good faith subsequent lessee for value, but only to the extent set forth in the preceding sentence. If goods have been delivered under a transaction of purchase, the lessor has that power even if though:

- (1) the lessor's transferor was deceived as to the identity of the lessor;
- (2) the delivery was in exchange for a check which is later dishonored;
- (3) it was agreed that the transaction was to be a "cash sale"; or
- (4) the delivery was procured through ~~fraud punishable as larcenous under the criminal law~~ criminal fraud.

(b) A subsequent lessee in ~~the~~ ordinary course of business from a lessor ~~who~~ that is a merchant dealing in goods of that kind to ~~whom~~ which the goods were entrusted by the existing lessee of that lessor before the interest of the subsequent lessee became enforceable against that lessor obtains, to the extent of the leasehold interest transferred, all of that lessor's and the existing lessee's rights to the goods, and takes free of the existing lease contract.

(c) A subsequent lessee from the lessor of goods that are subject to an existing lease contract and are covered by a certificate of title issued under a statute of this state or of another jurisdiction takes no greater rights than those provided both by this section and by the certificate of title statute.

SECTION 109. Section 2A.305, Business & Commerce Code, is amended to read as follows:

Sec. 2A.305. Sale or Sublease of Goods by Lessee

(a) Subject to ~~the provisions of~~ Section 2A.303, a buyer or sublessee from the lessee of goods under an existing lease contract obtains, to the extent of the interest transferred, the leasehold interest in the goods that the lessee had or had power to transfer, and except as provided in Subsection (b) and Section 2A.511(d), takes subject to the existing lease contract. A lessee with a voidable leasehold interest has power to transfer a good leasehold interest to a good faith buyer for value or a good faith sublessee for value, but only to the extent set forth in the preceding sentence. ~~If~~ When goods have been delivered under a transaction of lease the lessee has that power even if though:

- (1) the lessor was deceived as to the identity of the lessee;
- (2) the delivery was in exchange for a check which is later dishonored; or
- (3) the delivery was procured through ~~fraud punishable as larcenous under the criminal law~~ criminal fraud.

(b) A buyer in ~~the~~ ordinary course of business or a sublessee in ~~the~~ ordinary course of business from a lessee ~~who~~ that is a merchant dealing in goods of that kind to ~~whom~~ which the goods were entrusted by the lessor obtains, to the extent of the interest transferred, all of the lessor's and lessee's rights to the goods, and takes free of the existing lease contract.

(c) A buyer or sublessee from the lessee of goods that are subject to an existing lease contract and are covered by a certificate of title issued under a statute of this state or of another jurisdiction takes no greater rights than those provided both by this section and by the certificate of title statute.

SECTION 110. Section 2A.309, Business & Commerce Code, is amended to read as follows:

Sec. 2A.309. Lessor's and Lessee's Rights When Goods Become Fixtures

(a) In this section:

(1) goods are "fixtures" ~~if~~ ~~when~~ they become so related to particular real ~~property estate~~ that an interest in them arises under real ~~property estate~~ law;

(2) a "fixture filing" is the filing, in the office where a ~~record of a~~ mortgage on the real ~~property estate~~ would be filed or recorded, of a financing statement covering goods that are or are to become fixtures and conforming to the requirements of Section 9.502(a) and (b);

(3) a lease is a "purchase money lease" unless the lessee has possession or use of the goods or the right to possession or use of the goods before the lease agreement is enforceable;

(4) a mortgage is a "construction mortgage" to the extent it secures an obligation incurred for the construction of an improvement on land, including the acquisition cost of the land, if a recorded record of the mortgage ~~the recorded writing~~ so indicates; and

(5) "encumbrance" includes real ~~property estate~~ mortgages and other liens on real ~~property estate~~ and all other rights in real ~~property estate~~ that are not ownership interests.

(b) Under this chapter a lease may be of goods that are fixtures or may continue in goods that become fixtures, but no lease exists under this chapter of ordinary building materials incorporated into an improvement on land.

(c) This chapter does not prevent creation of a lease of fixtures pursuant to real ~~property estate~~ law.

(d) The perfected interest of a lessor of fixtures has priority over a conflicting interest of an encumbrancer or owner of the real ~~property estate~~ if:

(1) the lease is a purchase money lease, the conflicting interest of the encumbrancer or owner arises before the goods become fixtures, the interest of the lessor is perfected by a fixture filing before the goods become fixtures or within 10 days thereafter, and the lessee has an interest of record in the real ~~property estate~~ or is in possession of the real ~~property estate~~; or

(2) the interest of the lessor is perfected by a fixture filing before the interest of the encumbrancer or owner is of record, the lessor's interest has priority over any conflicting interest of a predecessor in title of the encumbrancer or owner, and the lessee has an interest of record in the real ~~property estate~~ or is in possession of the real ~~property estate~~.

(e) The interest of a lessor of fixtures, whether or not perfected, has priority over the conflicting interest of an encumbrancer or owner of the real property estate if:

(1) the fixtures are readily removable factory or office machines, readily removable equipment that is not primarily used or leased for use in the operation of the real property estate, or readily removable replacements of domestic appliances that are goods subject to a consumer lease, and before the goods become fixtures the lease contract is enforceable; or

(2) the conflicting interest is a lien on the real property estate obtained by legal or equitable proceedings after the lease contract is enforceable; or

(3) the encumbrancer or owner has consented in a record writing to the lease or has disclaimed an interest in the goods as fixtures; or

(4) the lessee has a right to remove the goods as against the encumbrancer or owner, but if the lessee's right to remove terminates, the priority of the interest of the lessor continues for a reasonable time the lessee has a right to remove the goods as against the encumbrancer or owner. If the lessee's right to remove terminates, the priority of the interest of the lessor continues for a reasonable time.

(f) Notwithstanding Subsection (d)(1) but otherwise subject to Subsections (d) and (e), the interest of a lessor of fixtures, including the lessor's residual interest, is subordinate to the conflicting interest of an encumbrancer of the real property estate under a construction mortgage recorded before the goods become fixtures if the goods become fixtures before the completion of the construction. To the extent given to refinance a construction mortgage, the conflicting interest of an encumbrancer of the real property estate under a mortgage has this priority to the same extent as the encumbrancer of the real property estate under the construction mortgage.

(g) ~~In cases not within the preceding subsections~~ In cases not covered by Subsections (c) through (f), priority between the interest of a lessor of fixtures, including the lessor's residual interest, and the conflicting interest of an encumbrancer or owner of the real property estate ~~who that~~ is not the lessee is determined by the priority rules governing conflicting interests in real property estate.

(h) If the interest of a lessor of fixtures, including the lessor's residual interest, has priority over all conflicting interests of all owners and encumbrancers of the real property estate, the lessor or the lessee may (1) on default, expiration, termination, or cancellation of the lease agreement but subject to the agreement and this chapter, or (2) if necessary to enforce other rights and remedies of the lessor or lessee under this chapter, remove the goods from the real property estate, free and clear of all conflicting interests of all owners and encumbrancers of the real property estate, but the lessor or lessee must reimburse any encumbrancer or owner of the real property estate ~~who that~~ is not the lessee and ~~who that~~ has not otherwise agreed for the cost of repair of

any physical injury, but not for any diminution in value of the real property estate caused by the absence of the goods removed or by any necessity of replacing them. A person entitled to reimbursement may refuse permission to remove until the party seeking removal gives adequate security for the performance of this obligation.

(i) Even ~~if though~~ the lease agreement does not create a security interest, the interest of a lessor of fixtures, including the lessor's residual interest, is perfected by filing a financing statement as a fixture filing for leased goods that are or are to become fixtures in accordance with the relevant provisions of Chapter 9.

SECTION 111. Section 2A.310, Business & Commerce Code, is amended to read as follows:

Sec. 2A.310. Lessor's and Lessee's Rights When Goods Become Accessions

(a) Goods are "accessions" when they are installed in or affixed to other goods.

(b) The lessor's residual interest in the accessions and the interest of a lessor or a lessee under a lease contract entered into before the goods became accessions are superior to all interests in the whole except as stated in Subsection (d).

(c) The lessor's residual interest in the accessions and the interest of a lessor or a lessee under a lease contract entered into at the time or after the goods became accessions are superior to all subsequently acquired interests in the whole except as stated in Subsection (d) but are subordinate to interests in the whole existing at the time the lease contract was made unless the holders of such interests in the whole have in a record writing consented to the lease or disclaimed an interest in the goods as part of the whole.

(d) The lessor's residual interest in the accessions and the interest of a lessor or a lessee under a lease contract described by Subsection (b) or (c) are subordinate to the interest of:

(1) a buyer in the ordinary course of business or a lessee in the ordinary course of business of any interest in the whole acquired after the goods became accessions; or

(2) a creditor with a security interest in the whole perfected before the lease contract was made to the extent that the creditor makes subsequent advances without knowledge of the lease contract.

(e) When under Subsections (b) or (c) and (d) a lessor or a lessee of accessions holds an interest that is superior to all interests in the whole, the lessor or the lessee may (1) on default, expiration, termination, or cancellation of the lease contract by the other party but subject to the provisions of the lease contract and this chapter, or (2) if necessary to enforce the lessor's or lessee's other rights and remedies under this chapter, remove the goods from the whole, free and clear of all interests in the whole, but the lessor or the lessee party must reimburse any holder of an interest in the whole who is not the lessee and who has not otherwise agreed for the cost of repair of any physical injury but not for

any diminution in value of the whole caused by the absence of the goods removed or by any necessity for replacing them. A person entitled to reimbursement may refuse permission to remove until the party seeking removal gives adequate security for the performance of this obligation.

SECTION 112. Section 2A.401, Business & Commerce Code, is amended to read as follows:

Sec. 2A.401. Insecurity: Adequate Assurance of Performance

(a) A lease contract imposes an obligation on each party that the other's expectation of receiving due performance will not be impaired.

(b) If reasonable grounds for insecurity arise with respect to the performance of either party, the insecure party may demand in a record writing adequate assurance of due performance. Until the insecure party receives that assurance, if commercially reasonable, the insecure party may suspend any performance for which the insecure party has not already received the agreed return.

(c) A repudiation of the lease contract occurs if assurance of due performance adequate under the circumstances of the particular case is not provided to the insecure party within a reasonable time, not to exceed 30 days after receipt of a demand by the other party.

(d) Between merchants, the reasonableness of grounds for insecurity and the adequacy of any assurance offered must be determined according to commercial standards.

(e) Acceptance of any nonconforming delivery or payment does not prejudice the aggrieved party's right to demand adequate assurance of future performance.

SECTION 113. Section 2A.402, Business & Commerce Code, is amended to read as follows:

Sec. 2A.402. Anticipatory Repudiation

(a) If either party repudiates a lease contract with respect to a performance not yet due under the lease contract, the loss of which performance will substantially impair the value of the lease contract to the other, the aggrieved party may:

(1) for a commercially reasonable time, await retraction of repudiation and performance by the repudiating party;

(2) make demand pursuant to Section 2A.401 and await assurance of future performance adequate under the circumstances of the particular case; or

(3) resort to any right or remedy upon default under the lease contract or this chapter, even if though the aggrieved party has notified the repudiating party that the aggrieved party would await the repudiating party's performance and assurance and has urged retraction. In addition, whether or not the aggrieved party is pursuing one of the foregoing remedies, the aggrieved party may suspend performance or, if the aggrieved party is the lessor, proceed in accordance with the provisions of this chapter on the lessor's right to identify

goods to the lease contract notwithstanding default or to salvage unfinished goods under (Section 2A.524).

(b) Repudiation includes language that a reasonable person would interpret to mean that the other person will not or cannot make a performance still due under the contract or voluntary, affirmative conduct that would appear to a reasonable party to make a future performance by the other party impossible.

SECTION 114. Section 2A.404, Business & Commerce Code, is amended to read as follows:

Sec. 2A.404. Substituted Performance

(a) If without fault of the lessee, the lessor and the supplier, the agreed berthing, loading, or unloading facilities fail or the agreed type of carrier becomes unavailable or the agreed manner of performance delivery otherwise becomes commercially impracticable, but a commercially reasonable substitute is available, the substitute performance must be tendered and accepted.

(b) If the agreed means or manner of payment fails because of domestic or foreign governmental regulation:

(1) the lessor may withhold or stop delivery or cause the supplier to withhold or stop delivery unless the lessee provides a means or manner of payment that is commercially a substantial equivalent; and

(2) if delivery has already been taken, payment by the means or in the manner provided by the regulation discharges the lessee's obligation unless the regulation is discriminatory, oppressive, or predatory.

SECTION 115. Section 2A.405, Business & Commerce Code, is amended to read as follows:

Sec. 2A.405. EXCUSED PERFORMANCE.

Subject to Section 2A.404 on substituted performance, the following rules apply:

(1) Delay in performance or nonperformance delivery ~~or nondelivery~~ in whole or in part by a lessor or a supplier ~~that who~~ complies with Subdivisions (2) and (3) is not a default under the lease contract if performance as agreed has been made impracticable by the occurrence of a contingency the nonoccurrence of which was a basic assumption on which the lease contract was made or by compliance in good faith with any applicable foreign or domestic governmental regulation or order, whether or not the regulation or order later proves to be invalid.

(2) If the causes mentioned in Subdivision (1) affect only part of the lessor's or the supplier's capacity to perform, the lessor or supplier shall allocate production and deliveries among the lessor's or supplier's customers but at the lessor's or supplier's option may include regular customers not then under contract for sale or lease as well as the lessor's or supplier's own requirements for further manufacture. The lessor or supplier may so allocate in any manner that is fair and reasonable.

(3) The lessor seasonably shall notify the lessee and in the case of a finance lease the supplier seasonably shall notify the lessor and the lessee, if known, that there will be delay or nonperformance ~~nondelivery~~ and, if allocation is required under Subdivision (2), of the estimated quota made available for the lessee.

SECTION 116. Section 2A.406, Business & Commerce Code, is amended to read as follows:

Sec. 2A.406. Procedure on Excused Performance

(a) If the lessee receives notification of a material or indefinite delay or an allocation justified under Section 2A.405, the lessee may by ~~written~~ notification in a record to the lessor as to any goods involved, and with respect to all of the goods if under an installment lease contract the value of the whole lease contract is substantially impaired (Section 2A.510):

(1) terminate the lease contract (Section 2A.505(b)); or

(2) except in a finance lease that is not a consumer lease, modify the lease contract by accepting the available quota in substitution, with due allowance from the rent payable for the balance of the lease term for the deficiency but without further right against the lessor.

(b) If, after receipt of a notification from the lessor under Section 2A.405, the lessee fails to modify the lease agreement within a reasonable time not exceeding 30 days, the lease contract is terminated ~~lapses~~ with respect to any performance deliveries ~~deliveries~~ affected.

SECTION 117. Section 2A.504, Business & Commerce Code, is amended to read as follows:

Sec. 2A.504. Liquidation of Damages

(a) Damages payable by either party for default or any other act or omission, including indemnity for loss or diminution of anticipated tax benefits or loss or damage to lessor's residual interest, may be liquidated in the lease agreement but only at an amount or by a formula that is reasonable in light of the then anticipated harm caused by the default or other act or omission. In a consumer lease, a term fixing liquidated damages that are unreasonably large in light of the actual harm is unenforceable as a penalty. Section 2A.503 determines the enforceability of a term that limits but does not liquidate damages.

(b) If the lease agreement provides for liquidation of damages, and such provision does not comply with Subsection (a) or such provision is an exclusive or limited remedy that circumstances cause to fail of its essential purpose, remedy may be had as provided in this chapter.

(c) If the lessor justifiably withholds delivery of goods or stops performance because of the lessee's default or insolvency, the lessee is entitled to restitution of any amount by which the sum of the lessee's payments exceeds the amount to which the lessor is entitled by virtue of terms liquidating the lessor's damages in accordance with Subsection (a).

~~(c) If the lessor justifiably withholds or stops delivery of goods because of the lessee's default or insolvency (Section 2A.525 or 2A.526), the lessee is entitled to restitution of any amount by which the sum of the lessee's payments exceeds:~~

~~(1) the amount to which the lessor is entitled by virtue of terms liquidating the lessor's damages in accordance with Subsection (a); or~~

~~(2) in the absence of those terms, 20 percent of the then present value of the total rent the lessee was obligated to pay for the balance of the lease term, or, in the case of a consumer lease, the lesser of such amount or \$500.~~

(d) A lessee's right to restitution under Subsection (c) is subject to offset to the extent the lessor establishes:

(1) a right to recover damages under the provisions of this chapter other than Subsection (a); and

(2) the amount of value of any benefits received by the lessee directly or indirectly by reason of the lease contract.

SECTION 118. Section 2A.506, Business & Commerce Code, is amended to read as follows:

Sec. 2A.506. Statute of Limitations

(a) An action for default under a lease contract, including breach of warranty or indemnity, must be commenced within four years after the cause of action accrued. By the original lease contract the parties may not expand such period of limitation but, except in the case of a consumer lease or an action for indemnity, may reduce the period of limitation to not less than one year.

(b) A cause of action for default accrues when the act or omission on which the default or breach of warranty is based is or should have been discovered by the aggrieved party. A cause of action for indemnity accrues:

(1) in the case of an indemnity against liability, when the act or omission on which the claim for indemnity is based is or should have been discovered by the indemnified party; or

(2) in the case of an indemnity against loss or damage, when the person indemnified makes payment thereof.

(c) If an action commenced within the time limited by Subsection (a) is so terminated as to leave available a remedy by another action for the same default or breach of warranty or indemnity, the other action may be commenced after the expiration of the time limited and within six months after the termination of the first action unless the termination resulted from voluntary discontinuance or from dismissal for failure or neglect to prosecute.

(d) This section does not alter the law on tolling of the statute of limitations nor does it apply to causes of action that have accrued before this chapter becomes effective.

SECTION 119. Chapter 2A, Business & Commerce Code, is amended to add Section 2A.507A, to read as follows:

Sec. 2A.507A. Right to Specific Performance or Replevin or the Like

(a) Specific performance may be decreed if the goods are unique or in other proper circumstances. In a contract other than a consumer lease, specific performance may also be decreed if the parties have agreed to that remedy. However, even if the parties agree to specific performance, specific performance may not be decreed if the breaching party's sole remaining contractual obligation is the payment of money.

(b) A decree for specific performance may include any terms and conditions as to payment of the rent, damages, or other relief that the court deems just.

(c) A lessee has a right of replevin or similar remedy for goods identified to the lease contract if after reasonable effort the lessee is unable to effect cover for those goods or the circumstances reasonably indicate that the effort will be unavailing or if the goods have been shipped under reservation and satisfaction of the security interest in them has been made or tendered.

SECTION 120. Section 2A.508, Business & Commerce Code, is amended to read as follows:

Sec. 2A.508. Lessee's Remedies

(a) If a lessor fails to deliver the goods in conformity to the lease contract or repudiates the contract, or a lessee rightfully rejects the goods or justifiably revokes acceptance of the goods, the lessor is in default under the lease contract, and the lessee may do one or more of the following:

(1) cancel the lease contract under Section 2A.505(a);

(2) recover so much of the rent and security as has been paid and is just under the circumstances;

(3) cover and obtain damages under Section 2A.518;

(4) recover damages for nondelivery under Section 2A.519(a);

(5) if an acceptance of goods has not been justifiably revoked, recover damages for default with regard to accepted goods under Section 2A.519(c) and (d);

(6) enforce a security interest under Subsection (d);

(7) recover identified goods under Section 2A.522;

(8) obtain specific performance or obtain the goods by replevin or similar remedy under Section 2A.507A;

(9) recover liquidated damages under Section 2A.504;

(10) enforce limited remedies under Section 2A.503;

(11) exercise any other right or pursue any other remedy as provided in the lease contract.

(a) If a lessor fails to deliver the goods in conformity to the lease contract (Section 2A.509) or repudiates the lease contract (Section 2A.402), or a lessee rightfully rejects the goods (Section 2A.509) or justifiably revokes acceptance of the goods (Section 2A.517), then with respect to any goods involved, and with respect to all of the goods if under an installment lease contract and the value of the whole lease contract is substantially impaired (Section 2A.510), the lessor is in default under the lease contract and the lessee may:

~~(1) cancel the lease contract (Section 2A.505(a));~~  
~~(2) recover so much of the rent and security as has been paid and is just under the circumstances;~~

~~(3) cover and recover damages as to all goods affected whether or not they have been identified to the lease contract (Sections 2A.518 and 2A.520), or recover damages for nondelivery (Sections 2A.519 and 2A.520);~~  
~~or~~

~~(4) exercise any other rights or pursue any other remedies provided in the lease contract.~~

~~(b) If a lessor fails to deliver the goods in conformity to the lease contract or repudiates the lease contract, the lessee may also:~~

~~(1) if the goods have been identified, recover them (Section 2A.522); or~~

~~(2) in a proper case, obtain specific performance, replevin, detinue, sequestration, claim and delivery, or the like for the goods (Section 2A.521).~~

~~(b)(e) If a lessor is otherwise in default under a lease contract, the lessee may exercise the rights and pursue the remedies provided in the lease contract, which may include a right to cancel the lease, and in Section 2A.519(c).~~

~~(c)(d) If a lessor has breached a warranty, whether express or implied, the lessee may recover damages (Section 2A.519(d)).~~

~~(d)(e) On rightful rejection or justifiable revocation or acceptance, a lessee has a security interest in goods in the lessee's possession or control for any rent and security that has been paid and any expenses reasonably incurred in their inspection, receipt, transportation, and care and custody and may hold those goods and dispose of them in good faith and in a commercially reasonable manner, subject to Section 2A.527(e).~~

~~(e)(f) Subject to the provisions of Section 2A.407, a lessee, on notifying the lessor of the lessee's intention to do so, may deduct all or part of the damages resulting from any default under the lease contract from any part of the rent still due under the same lease contract.~~

~~(f) An aggrieved lessee must take such measures as are reasonable under the circumstances to mitigate damages resulting from the default. If the lessee fails to take such measures, the lessor or supplier may claim a reduction in damages in the amount by which the loss should have been mitigated.~~

SECTION 121. Section 2A.509, Business & Commerce Code, is amended to read as follows:

Sec. 2A.509. Lessee's Rights on Improper Delivery; Rightful Rejection

(a) Subject to Sections 2A.503, 2A.504, and 2A.510, if the goods or the tender of delivery fail in any respect to conform to the contract, the lessee may:

(1) reject the whole;

(2) accept the whole; or

(3) accept any commercial unit or units and reject the rest.

(b) Rejection of goods must be within a reasonable time after their delivery or tender. It is ineffective unless the lessee seasonably notifies the lessor or supplier.

(c) Subject to Sections 2A.511, 2A.512, and 2A.517(f):

(1) after rejection any use by the lessee with respect to any commercial unit is wrongful as against the lessor or supplier; and

(2) if the lessee has before rejection taken physical possession of goods in which the lessee does not have a security interest under Section 2A.508(d), the lessee is under a duty after rejection to hold them with reasonable care at the lessor's or supplier's disposition for a time sufficient to permit the lessor or supplier to remove them; but

(3) the lessee has no further obligations with regard to goods rightfully rejected.

(4) The lessor's or supplier's remedies with respect to goods wrongfully rejected are governed by Section 2A.523.

~~(a) Subject to the provisions of Section 2A.510 on default in installment lease contracts, if the goods or the tender or delivery fail in any respect to conform to the lease contract, the lessee may reject or accept the goods or accept any commercial unit or units and reject the rest of the goods.~~

~~(b) Rejection of goods is ineffective unless it is within a reasonable time after tender or delivery of the goods and the lessee seasonably notifies the lessor.~~

SECTION 122. Section 2A.510, Business & Commerce Code, is amended to read as follows:

Sec. 2A.510. Installment Lease Contracts: Rejection and Default

(a) Under an installment lease contract a lessee may reject any delivery that is nonconforming if the nonconformity substantially impairs the value of that delivery ~~to the lessee and cannot be cured~~ or the nonconformity is a defect in the required documents; but if the nonconformity does not fall within Subsection (b) and the lessor or the supplier gives adequate assurance of its cure, the lessee must accept the delivery.

(b) ~~If~~ Whenever a nonconformity or default with respect to one or more deliveries substantially impairs the value of the installment lease contract as a whole there is a default with respect to the whole. But the aggrieved party reinstates the installment lease contract as a whole if the aggrieved party accepts a nonconforming delivery without seasonably notifying of cancellation or brings an action with respect only to past deliveries or demands performance as to future deliveries.

SECTION 123. Section 2A.511, Business & Commerce Code, is amended to read as follows:

Sec. 2A.511. Merchant Lessee's Duties as to ~~Rightfully~~ Rejected Goods

Subject to any security interest of a lessee (Section 2A.508~~(d)(e)~~), if a lessor or a supplier has no agent or place of business at the market of rejection, a merchant lessee, after rejection of goods in the lessee's possession or control,

shall follow any reasonable instructions received from the lessor or the supplier with respect to the goods. In the absence of those instructions, a merchant lessee shall make reasonable efforts to sell, lease, or otherwise dispose of the goods for the lessor's or supplier's account if they threaten to decline in value speedily. ~~In the case of a rightful rejection instructions~~ ~~Instructions~~ are not reasonable if on demand indemnity for expenses is not forthcoming.

SECTION 124. Section 2A.512, Business & Commerce Code, is amended to read as follows:

Sec. 2A.512. Lessee's Duties as to ~~Rightfully~~ Rejected Goods

(a) If the lessor or the supplier gives no instructions within a reasonable time after notification of rejection, the lessee may store the rejected goods for the lessor's or the supplier's account or ship them to the lessor or the supplier or dispose of them for the lessor's or the supplier's account with reimbursement in the manner provided in Section 2A.511.

~~(a) Except as otherwise provided with respect to goods that threaten to decline in value speedily (Section 2A.511) and subject to any security interest of a lessee (Section 2A.508(e)):~~

~~(1) the lessee, after rejection of goods in the lessee's possession, shall hold them with reasonable care at the lessor's or the supplier's disposition for a reasonable time after the lessee's seasonable notification of rejection;~~

~~(2) if the lessor or the supplier gives no instructions within a reasonable time after notification of rejection, the lessee may store the rejected goods for the lessor's or the supplier's account or ship them to the lessor or the supplier or dispose of them for the lessor's or the supplier's account with reimbursement in the manner provided by Subsection (d); but~~

~~(3) the lessee has no further obligations with regard to goods rightfully rejected.~~

(b) Action by the lessee pursuant to Subsection (a) is not acceptance or conversion.

(c) If a merchant lessee (Section 2A.511) or any other lessee disposes of goods following a rightful rejection, the lessee is entitled to reimbursement either from the lessor or the supplier or out of the proceeds for reasonable expenses of caring for and disposing of the goods and, if the expenses include no disposition commission, to such commission as is usual in the trade, or if there is none, to a reasonable sum not exceeding 10 percent of the gross proceeds.

(d) In complying with this section or Section 2A.511, the lessee is held only to good faith. Good faith conduct hereunder is neither acceptance or conversion nor the basis of an action for damages.

(e) A purchaser ~~that who~~ purchases in good faith from a lessee pursuant to this section or Section 2A.511 takes the goods free of any rights of the lessor and the supplier even ~~if though~~ the lessee fails to comply with one or more of the requirements of this chapter.

SECTION 125. Section 2A.513, Business & Commerce Code, is amended to read as follows:

Sec. 2A.513. Cure by Lessor of Improper Tender or Delivery; Replacement

(a) If the lessee rejects goods or a tender of delivery under Section 2A.509 or 2A.510 or, except in a consumer contract, justifiably revokes acceptance under Section 2A.517(a)(2) and the agreed time for performance has not expired, a lessor or a supplier that has performed in good faith, upon reasonable notice to the lessee, and at the lessor's or supplier's own expense, may cure the default by making a conforming tender of delivery within the agreed time. The lessor or supplier shall compensate the lessee for all of the lessee's reasonable expenses caused by the lessor's or supplier's default and subsequent cure.

(b) If the lessee rejects goods or a tender of delivery under Section 2A.509 or 2A.510 or, except in a consumer lease, justifiably revokes acceptance under Section 2A.517(a)(2) and the agreed time for performance has expired, a lessor or supplier that has performed in good faith may, upon reasonable notice to the lessee and at the lessor's or supplier's own expense, cure the default, if the cure is appropriate and timely under the circumstances, by making a tender of conforming goods. The lessor or supplier shall compensate the lessee for all of the lessee's reasonable expenses caused by the lessor's or supplier's default and subsequent cure.

~~(a) If any tender or delivery by the lessor or the supplier is rejected because nonconforming and the time for performance has not yet expired, the lessor or the supplier may seasonably notify the lessee of the lessor's or the supplier's intention to cure and may then make a conforming delivery within the time provided by the lease contract.~~

~~(b) If the lessee rejects a nonconforming tender that the lessor or the supplier had reasonable grounds to believe would be acceptable with or without money allowance, the lessor or the supplier may have a further reasonable time to substitute a conforming tender if the lessor or supplier seasonably notifies the lessee.~~

SECTION 126. Section 2A.514, Business & Commerce Code, is amended to read as follows:

Sec. 2A.514. Waiver of Lessee's Objections

(a) A lessee's failure to state in connection with rejection a particular defect or in connection with revocation of acceptance a defect that justifies revocation precludes the lessee from relying on the unstated defect to justify rejection or revocation of acceptance if the defect is ascertainable by reasonable inspection

(1) if the lessor or supplier had a right to cure the defect and could have cured it if stated seasonably; or

(2) between merchants if the lessor or the supplier after rejection or revocation of acceptance has made a request in a record for a full and final statement in a record of all defects on which the lessee proposes to rely.

~~(a) In rejecting goods, a lessee's failure to state a particular defect that is ascertainable by reasonable inspection precludes the lessee from relying on the defect to justify rejection or to establish default:~~

~~(1) if, stated seasonably, the lessor or the supplier could have cured it (Section 2A.513); or~~

~~(2) between merchants if the lessor or the supplier after rejection has made a request in writing for a full and final written statement of all defects on which the lessee proposes to rely.~~

(b) A lessee's failure to reserve rights when paying rent or other consideration against documents precludes recovery of the payment for defects apparent in the documents.

SECTION 127. Section 2A.515, Business & Commerce Code, is amended to read as follows:

Sec. 2A.515. Acceptance of Goods

(a) Acceptance of goods occurs when the lessee:

(1) after a reasonable opportunity to inspect the goods signifies to the lessor or supplier that the goods are conforming or will be taken or retained in spite of their nonconformity;

(2) fails to make an effective rejection under Section 2A.509(b), but such acceptance does not occur until the lessee has had a reasonable opportunity to inspect them; or

(3) subject to Section 2A.517(f), uses the goods in any manner that is inconsistent with the lessor's or supplier's rights.

~~(a) Acceptance of goods occurs after the lessee has had a reasonable opportunity to inspect the goods and:~~

~~(1) the lessee signifies or acts with respect to the goods in a manner that signifies to the lessor or the supplier that the goods are conforming or that the lessee will take or retain them in spite of their nonconformity; or~~

~~(2) the lessee fails to make an effective rejection of the goods (Section 2A.509(b)).~~

(b) Acceptance of a part of any commercial unit is acceptance of that entire unit.

SECTION 128. Section 2A.516, Business & Commerce Code, is amended to read as follows:

Sec. 2A.516. Effect of Acceptance of Goods; Notice of Default; Burden of Establishing Default After Acceptance; Notice of Claim or Litigation to Person Answerable Over

(a) A lessee must pay rent for any goods accepted in accordance with the lease contract, ~~with due allowance for goods rightfully rejected or not delivered.~~

(b) A lessee's acceptance of goods precludes rejection of the goods accepted. In the case of a finance lease that is not a consumer lease, if made with knowledge of a nonconformity, acceptance may not ~~cannot~~ be revoked because of it. In any other case, if made with knowledge of a nonconformity, acceptance may not ~~cannot~~ be revoked because of it unless the acceptance was

on the reasonable assumption that the nonconformity would be seasonably cured. Acceptance does not of itself impair any other remedy provided by this chapter or the lease agreement for nonconformity.

(c) If a tender has been accepted:

(1) within a reasonable time after the lessee discovers or should have discovered any default, the lessee shall notify the lessor and supplier, if any, or be barred from any remedy against the party not notified;

(2) within a reasonable time after the lessee receives notice of litigation for infringement or the like (Section 2A.211) the lessee shall notify the lessor or be barred from any remedy over for liability established by the litigation; and

(3) the burden is on the lessee to establish any default.

(d) If a lessee is sued for indemnity, breach of a warranty or other obligation for which another party a lessor or a supplier is answerable over, the following rules apply:

(1) The lessee may give the other party lessor or the supplier, or both, written notice of the litigation in a record. If the notice states that the person notified may come in and defend and that if the person notified does not do so that person will be bound in any action against that person by the lessee by any determination of fact common to both litigations, then unless the person notified after seasonable receipt of the notice does come in and defend that person is so bound.

(2) The other party lessor or the supplier may demand in a record writing that the lessee turn over control of the litigation including settlement if the claim is one for infringement or the like (Section 2A.211) or else be barred from any remedy over. If the demand states that the other party lessor or the supplier agrees to bear all expense and to satisfy any adverse judgment, then unless the lessee after seasonable receipt of the demand does turn over control the lessee is so barred.

(e) Subsections (c) and (d) apply to any obligation of a lessee to hold the lessor or the supplier harmless against infringement or the like (Section 2A.211).

(f) Subsection (c) shall not apply to a consumer lease.

SECTION 129. Section 2A.517, Business & Commerce Code, is amended to read as follows:

Sec. 2A.517. Revocation of Acceptance of Goods

(a) A lessee may revoke acceptance of a lot or commercial unit whose nonconformity substantially impairs its value to the lessee if the lessee has accepted it:

(1) except in the case of a finance lease that is not a consumer lease, on the reasonable assumption that its nonconformity would be cured and it has not been seasonably cured; or

(2) without discovery of the nonconformity if the lessee's acceptance was reasonably induced either by the lessor's assurances or, except

in the case of a finance lease that is not a consumer lease, by the difficulty of discovery before acceptance.

(b) A lessee may revoke acceptance of a lot or commercial unit if the lessor defaults under the lease contract and the default substantially impairs the value of that lot or commercial unit to the lessee.

(c) If the lease agreement so provides, the lessee may revoke acceptance of a lot or commercial unit because of other defaults by the lessor.

(d) Revocation of acceptance must occur within a reasonable time after the lessee discovers or should have discovered the ground for it and before any substantial change in condition of the goods which is not caused by the nonconformity. Revocation is not effective until the lessee notifies the lessor.

(e) A lessee ~~that who~~ that so revokes has the same rights and duties with regard to the goods involved as if the lessee had rejected them.

(f) If a lessee uses the goods after a revocation of acceptance, the following rules apply:

(1) Any use by the lessee which is unreasonable under the circumstances is wrongful as against the lessor or supplier and any revocation of acceptance is ineffective.

(2) Any use of the goods which is reasonable under the circumstances is not wrongful as against the lessor or supplier and is not an acceptance, but in an appropriate case the lessee shall be obligated to the lessor or supplier for the value of the use to the lessee.

SECTION 130. Section 2A.521, Business & Commerce Code, is deleted and the section number is reserved to read as follows:

Sec. 2A.521. ~~Reserved Lessee's Right to Specific Performance, Replevin, and Other Remedies~~

~~(a) Specific performance may be decreed if the goods are unique or in other proper circumstances.~~

~~(b) A decree for specific performance may include the terms and conditions as to payment of the rent, damages, or other relief that the court deems just.~~

~~(c) A lessee has a right of replevin, detinue, sequestration, claim and delivery, or the like for goods identified to the lease contract if after reasonable effort the lessee is unable to effect cover for those goods or the circumstances reasonably indicate that the effort will be unavailing.~~

SECTION 131. Section 2A.522, Business & Commerce Code, is amended to read as follows:

Sec. 2A.522. Lessee's Right to Goods on Lessor's Insolvency

(a) Subject to Subsection (b) and even ~~if though~~ if the goods have not been shipped, a lessee ~~who that~~ that has paid a part or all of the rent and security for goods identified to a lease contract (Section 2A.217) on making and keeping good a tender of any unpaid portion of the rent and security due under the lease contract may recover the goods identified from the lessor ~~if the lessor becomes~~

~~insolvent within 10 days after receipt of the first installment of rent and security.~~

(1) in the case of goods leased by a consumer, the lessor repudiates or fails to deliver as required by the lease contract; or

(2) in all cases, the lessor becomes insolvent within 10 days after receipt of the first installment on their rent and security.

(b) A lessee acquires the right to recover goods identified to a lease contract only if they conform to the lease contract.

SECTION 132. Section 2A.523, Business & Commerce Code, is amended to read as follows:

Sec. 2A.523. Lessor's Remedies

(a) If the lessee wrongfully rejects or attempts to revoke acceptance of goods or fails to make a payment when due or repudiates with respect to a part or the whole, the lessee is in default under the lease contract with respect to any goods involved and the lessor may do one or more of the following:

(1) withhold delivery of the goods and take possession of goods previously delivered under Section 2A.525;

(2) stop delivery of the goods by any carrier or bailee under Section 2A.526;

(3) proceed under Section 2A.524 with respect to goods still unidentified to the lease contract or unfinished;

(4) obtain specific performance under Section 2A.507A or recover the rent under Section 2A.529;

(5) dispose of the goods and recover damages under Section 2A.527 or retain the goods and recover damages under Section 2A.528;

(6) cancel the lease contract under Section 2A.505(a);

(7) recover liquidated damages under Section 2A.504;

(8) enforce limited remedies under Section 2A.503;

(9) exercise any other rights or pursue any other remedies provided in the lease agreement.

(b) If a lessee becomes insolvent but is not in default of the lease contract under Subsections (a) or (d), the lessor may:

(1) refuse to deliver the goods under Section 2A.525(a);

(2) take possession of the goods under Section 2A.525(b);

(3) stop delivery of the goods by any bailee or carrier under Section 2A.526(a).

~~(a) If a lessee wrongfully rejects or revokes acceptance of goods or fails to make a payment when due or repudiates with respect to a part or the whole, then, with respect to any goods involved, and with respect to all of the goods if under an installment lease contract, the value of the whole lease contract is substantially impaired (Section 2A.510), the lessee is in default under the lease contract and the lessor may:~~

~~(1) cancel the lease contract (Section 2A.505(a));~~

~~(2) proceed respecting goods not identified to the lease contract (Section 2A.524);~~

~~(3) withhold delivery of the goods and take possession of goods previously delivered (Section 2A.525);~~

~~(4) stop delivery of the goods by any bailee (Section 2A.526);~~

~~(5) dispose of the goods and recover damages (Section 2A.527), or retain the goods and recover damages (Section 2A.528), or in a proper case recover rent (Section 2A.529); or~~

~~(6) exercise any other rights or pursue any other remedies provided in the lease contract.~~

~~(c)(b)~~ If a lessor does not fully exercise a right or obtain a remedy to which the lessor is entitled under Subsection (a), the lessor may recover the loss resulting in the ordinary course of events from the lessee's default as determined in any reasonable manner, together with incidental or consequential damages allowed under Section 2A.530, less expenses saved in consequence of the lessee's default.

~~(d)(e)~~ If a lessee is otherwise in default under a lease contract, the lessor may exercise the rights and pursue the remedies provided in the lease contract, which may include a right to cancel the lease. In addition, unless otherwise provided in the lease contract:

(1) if the default substantially impairs the value of the lease contract to the lessor, the lessor may exercise the rights and pursue the remedies provided by Subsection (a) or (b); or

(2) if the default does not substantially impair the value of the lease contract to the lessor, the lessor may recover as provided by Subsection (b).

(e) An aggrieved lessor must take such measures as are reasonable under the circumstances to mitigate damages resulting from the default. If the lessor fails to take such measures, the lessee may claim a reduction in damages in the amount by which the loss should have been mitigated.

SECTION 133. Section 2A.526, Business & Commerce Code, is amended to read as follows:

Sec. 2A.526. Lessor's Stoppage of Delivery in Transit or Otherwise

(a) A lessor may stop delivery of goods in the possession of a carrier or other bailee if the lessor discovers the lessee to be insolvent ~~and may stop delivery of carload, truckload, planeload, or larger shipments of express or freight if or if~~ the lessee repudiates or fails to make a payment due before delivery, whether for rent, security or otherwise under the lease contract, or for any other reason the lessor has a right to withhold or take possession of the goods.

(b) In pursuing its remedies under Subsection (a), the lessor may stop delivery until:

(1) receipt of the goods by the lessee;

(2) acknowledgement to the lessee by any bailee of the goods, except a carrier, that the bailee holds the goods for the lessee; or

(3) such an acknowledgement to the lessee by a carrier via reshipment or as a warehouse.

(c)(1) To stop delivery, a lessor shall so notify as to enable the bailee by reasonable diligence to prevent delivery of the goods.

(2) After notification, the bailee shall hold and deliver the goods according to the directions of the lessor, but the lessor is liable to the bailee for any ensuing charges or damages.

(3) A carrier ~~that who~~ has issued a nonnegotiable bill of lading is not obligated to obey a notification to stop received from a person other than the consignor.

SECTION 134. Section 2A.527, Business & Commerce Code, is amended to read as follows:

Sec. 2A.527. Lessor's Rights to Dispose of Goods

(a) After a default by a lessee under the lease contract of the type described in Section 2A.523(a) or ~~(c)~~(d)(1) or after the lessor refuses to deliver or takes possession of goods (Section 2A.525 or 2A.526), or, if agreed, after other default by a lessee, the lessor may dispose of the goods concerned or the undelivered balance thereof by lease, sale or otherwise.

(b) Except as otherwise provided with respect to damages liquidated in the lease agreement (Section 2A.504) or otherwise determined pursuant to agreement of the parties (Sections 1.302 and 2A.503), if the disposition is by lease agreement substantially similar to the original lease agreement and the new lease agreement is made in good faith and in a commercially reasonable manner, the lessor may recover from the lessee as damages (1) accrued and unpaid rent as of the date of the commencement of the term of the new lease agreement, (2) the present value, as of the same date, of the total rent for the then remaining lease term of the original lease agreement minus the present value, as of the same date, of the rent under the new lease agreement applicable to that period of the new lease term which is comparable to the then remaining term of the original lease agreement, and (3) any incidental or consequential damages allowed under Section 2A.530, less expenses saved in consequence of the lessee's default.

(c) If the lessor's disposition is by lease agreement that for any reason does not qualify for treatment under Subsection (b), or is by sale or otherwise, the lessor may recover from the lessee as if the lessor had elected not to dispose of the goods and Section 2A.528 governs.

(d) A subsequent buyer or lessee ~~that who~~ buys or leases from the lessor in good faith for value as a result of a disposition under this section takes the goods free of the original lease contract and any rights of the original lessee even ~~if though~~ the lessor fails to comply with one or more of the requirements of this chapter.

(e) The lessor is not accountable to the lessee for any profit made on any disposition. A lessee that ~~who~~ has rightfully rejected or justifiably revoked acceptance shall account to the lessor for any excess over the amount of the lessee's security interest (Section 2A.508~~(d)~~~~(e)~~).

SECTION 135. Section 2A.528, Business & Commerce Code, is amended to read as follows:

Sec. 2A.528. Lessor's Damages for Nonacceptance, Failure to Pay, Repudiation, or Other Default

(a) Except as otherwise provided with respect to damages liquidated in the lease agreement (Section 2A.504) or otherwise determined pursuant to agreement of the parties (Sections 1.302 and 2A.503), if a lessor elects to retain the goods or a lessor elects to dispose of the goods and the disposition is by lease agreement that for any reason does not qualify for treatment under Section 2A.527(b) or is by sale or otherwise, the lessor may recover from the lessee as damages for a default of the type described in Section 2A.523(a) or ~~(d)~~~~(e)~~(1), or, if agreed, for other default of the lessee, (i) accrued and unpaid rent as of the date of default if the lessee has never taken possession of the goods, or, if the lessee has taken possession of the goods, as of the date the lessor repossesses the goods or an earlier date on which the lessee makes a tender of the goods to the lessor, (ii) the present value as of the date determined under clause (i) of the total rent for the then remaining lease term of the original lease agreement minus the present value as of the same date of the market rent at the place where the goods are located computed for the same lease term, and (iii) any incidental or consequential damages allowed under Section 2A.530, less expenses saved in consequence of the lessee's default.

(b) If the measure of damages provided in Subsection (a) is inadequate to put a lessor in as good a position as performance would have, the measure of damages is the present value of the profit, including reasonable overhead, the lessor would have made from full performance by the lessee, together with any incidental or consequential damages allowed under Section 2A.530, due allowance for costs reasonably incurred and due credit for payments or proceeds of disposition.

SECTION 136. Section 2A.529, Business & Commerce Code, is amended to read as follows:

Sec. 2A.529. Lessor's Action for the Rent

(a) After default by the lessee under the lease contract of the type described in Section 2A.523(a) or ~~(d)~~~~(e)~~(1), or, if agreed, after other default by the lessee, if the lessor complies with Subsection (b), the lessor may recover from the lessee as damages:

(1) for goods accepted by the lessee and not repossessed by or tendered to the lessor, and for conforming goods lost or damaged within a commercially reasonable time after risk of loss passes to the lessee (Section 2A.219), (i) accrued and unpaid rent as of the date of entry of judgment in favor of the lessor, (ii) the present value as of the same date of the rent for the

then remaining lease term of the lease agreement, and (iii) any incidental or consequential damages allowed under Section 2A.530, less expenses saved in consequence of the lessee's default; and

(2) for goods identified to the lease contract if the lessor is unable after reasonable effort to dispose of them at a reasonable price or the circumstances reasonably indicate that effort will be unavailing, (i) accrued and unpaid rent as of the date of entry of judgment in favor of the lessor, (ii) the present value as of the same date of the rent for the then remaining lease term of the lease agreement, and (iii) any incidental or consequential damages allowed under Section 2A.530, less expenses saved in consequence of the lessee's default.

(b) Except as provided by Subsection (c) of this section, the lessor shall hold for the lessee for the remaining lease term of the lease agreement any goods that have been identified to the lease contract and are in the lessor's control.

(c) The lessor may dispose of the goods at any time before collection of the judgment for damages obtained pursuant to Subsection (a). If the disposition is before the end of the remaining lease term of the lease agreement, the lessor's recovery against the lessee for damages is governed by Section 2A.527 or 2A.528, and the lessor will cause an appropriate credit to be provided against any judgment for damages to the extent that the amount of the judgment exceeds the recovery available pursuant to Section 2A.527 or 2A.528.

(d) Payment of the judgment for damages obtained pursuant to Subsection (a) entitles the lessee to the use and possession of the goods not then disposed of for the remaining lease term of and in accordance with the lease agreement.

(e) After a lessee has wrongfully rejected or revoked acceptance of goods, has failed to pay rent then due, or has repudiated (Section 2A.402), or after other default by the lessee, a lessor that who is held not entitled to rent under this section must nevertheless be awarded damages for nonacceptance under Section 2A.527 or 2A.528.

SECTION 137. Section 2A.530, Business & Commerce Code, is amended to read as follows:

Sec. 2A.530. Lessor's Incidental and Consequential Damages

(a) Incidental damages to an aggrieved lessor include any commercially reasonable charges, expenses, or commissions incurred in stopping delivery, in the transportation, care and custody of goods after the lessee's default, in connection with return or disposition of the goods, or otherwise resulting from the default.

(b) Consequential damages resulting from a lessee's default include any loss resulting from general or particular requirements and needs of which the lessee at the time of contracting had reason to know and which could not reasonably be prevented by disposition under Section 2A.527 or otherwise.

(c) In a consumer lease contract, a lessor may not recover consequential damages from a consumer.

SECTION 138. Section 2A.531, Business & Commerce Code, is amended to read as follows:

Sec. 2A.531. Standing to Sue Third Parties for Injury to Goods

(a) If a third party so deals with goods that have been identified to a lease contract as to cause actionable injury to a party to the lease contract:

- (1) the lessor has a right of action against the third party; and
- (2) the lessee also has a right of action against the third party if the

lessee:

(A) has a security interest in the goods;

(B) has an insurable interest in the goods;

(C) bears the risk of loss under the lease contract or has since the injury assumed that risk as against the lessor and the goods have been converted or destroyed.

(b) If at the time of the injury the party plaintiff did not bear the risk of loss as against the other party to the lease contract and there is no arrangement between them for disposition of the recovery, the party plaintiff's ~~party's~~ suit or settlement, subject to the party plaintiff's ~~party's~~ own interest, is as a fiduciary for the other party to the lease contract.

(c) Either party with the consent of the other may sue for the benefit of which ~~whom~~ it may concern.

SECTION 139. Subsection (f), Section 1.303, Business & Commerce Code, is amended to read as follows:

(f) Subject to Section 2.209 and Section 2A.208, a course of performance is relevant to show a waiver or modification of any term inconsistent with the course of performance.

SECTION 140. This Act takes effect January 1, 2008.

APPENDIX II: DRAFT BILL ANALYSIS<sup>867</sup>

January 8, 2007 DRAFT

**BILL ANALYSIS  
AMENDMENTS FOR TEXAS BUSINESS AND  
COMMERCE CODE  
CHAPTER 2**

(Article 2, Uniform Commercial Code)

Sales

And

CHAPTER 2A

(Article 2A, Uniform Commercial Code)

Leases

Prepared by:

State Bar of Texas Commercial Code Committee

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## I. BACKGROUND AND PURPOSE

Chapter 2 of the Texas Business and Commerce Code (Article 2 of the Uniform Commercial Code or UCC) is titled “Sales” and governs transactions in goods. Over the past decade, Chapters 1, 3, 4, 5, 8 and 9 of the UCC as originally adopted in Texas by the 1965 legislature were substantially revised,

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<sup>867</sup>. This Bill Analysis is the final version of the draft analysis that circulated among the subcommittee in March 2007. Roy Ryden Anderson, Senior Associate Dean for Academics, Vinson & Elkins Distinguished Teaching Fellow and Professor of Law at SMU Dedman School of Law, was the primary drafter of this analysis.

Chapter 6 was repealed, and Chapters 2A and 4A were added to the Texas UCC. The amendments of Chapter 2 discussed in this analysis fall short of a wholesale revision, but are both pervasive and significant.

These amendments of Chapter 2 have been approved by the American Law Institute and the National Conference of Commissioners on Uniform State Laws. Although the amendments are extensive, most of them are not likely to cause a significant change in the substantive law, because either they reflect the consensus of the better-reasoned judicial opinions that have interpreted the particular provision or they are designed to bring Chapter 2 in line with current related statutory law. An attempt to summarize the amendments at this juncture would not be helpful. Instead, the proposed amendments will be discussed below in a section-by-section analysis grouped consecutively under the seven separate "Subchapters" of Chapter 2. A summary of the relevance of the amendments for each particular subchapter will be provided at the beginning of the analysis for that subchapter.

## **II. SUBCHAPTER A. SHORT TITLE, GENERAL CONSTRUCTION AND SUBJECT MATTER**

The proposed amendments for Subchapter A include several new definitions, most of which are intended to give effect to electronic contracting. A new provision, Section 2.108, specifically excludes certain transactions from coverage.

### **SECTION 2.103. DEFINITIONS AND INDEX OF DEFINITIONS**

**(a)(2) "Conspicuous", with reference to a term, means so written, displayed, or presented that a reasonable person against which it is to operate ought to have noticed it. A term in an electronic record intended to evoke a response by an electronic agent is conspicuous if it is presented in a form that would enable a reasonably configured electronic agent to take it into account or react to it without review of the record by an individual. Whether a term is "conspicuous" or not is a decision for the court. Conspicuous terms include the following:**

**(i) for a person:**

**(A) a heading in capitals equal to or greater in size than the surrounding text, or in contrasting type, font, or color to the surrounding text of the same or lesser size; and**

**(B) language in the body of a record or display in larger type than the surrounding text, or in contrasting type, font, or color to the surrounding text of the same size, or set off from surrounding text of the same size by symbols or other marks that call attention to the language; and**

**(ii) for a person or an electronic agent, a term that is so placed in a record or display that the person or electronic agent may not proceed without taking action with respect to the particular term.**

This provision takes the general definition from Article 1 and expands it by giving specific examples of conspicuousness undoubtedly taken from current case law. The comments<sup>†</sup> make reasonably clear that the listing is to give “guidance” to the courts and is not intended to be exhaustive.

The special provision in subsection (2)(ii) is new and is designed to accommodate electronic contracting.

**(a)(3) “Consumer” means an individual who buys or contracts to buy goods that, at the time of contracting, are intended by the individual to be used primarily for personal, family, or household purposes.**

#### **State Bar Committee Recommendation**

**The Committee recommends that this definition be omitted because it is included in a slightly different form in Revised Chapter 1 as adopted by the Texas Legislature in 2003. See Section 1.201(b)(11). The definition provided for Article 2 places a particular emphasis on the intent of the buyer. There is no good reason to deviate from the Chapter 1 definition for purposes of Chapter 2. It is also recommended that “Consumer” be added to this section merely as a “Definitional Cross Reference.”**

**(a)(4) “Consumer contract” means a contract between a merchant seller and a consumer.**

**(a)(5) “Delivery” means the voluntary transfer of physical possession or control of goods.**

**(a)(6) “Electronic” means relating to technology having electrical, digital, magnetic, wireless, optical, electromagnetic, or similar capabilities.**

**(a)(7) “Electronic agent” means a computer program or an electronic or other automated means used independently to initiate an action or respond to electronic records or performances in whole or in part, without review or action by an individual.**

**(a)(8) “Electronic record” means a record created, generated, sent, communicated, received, or stored by electronic means.**

**(a)(9) “Foreign exchange transaction” means a transaction in which one party agrees to deliver a quantity of a specified money or unit of**

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<sup>†</sup> Author’s Note: In the Texas Subcommittee’s draft Bill Analysis, references to “the comments” or “a comment” will generally mean the Official Comments to Article 2 and 2A as promulgated by the ALI and NCCUSL. All section references in the draft Bill Analysis use the numbering convention of the Texas Business & Commerce Code.

**account in consideration of the other party's agreement to deliver another quantity of a different money or unit of account either currently or at a future date, and in which delivery is to be through funds transfer, book entry accounting, or other form of payment order, or other agreed means to transfer a credit balance. The term includes a transaction of this type involving two or more moneys and spot, forward, option, or other products derived from underlying moneys and any combination of these transactions. The term does not include a transaction involving two or more moneys in which one or both of the parties is obligated to make physical delivery, at the time of contracting or in the future, of banknotes, coins, or other form of legal tender or specie.**

The only purpose of this provision is to define "foreign exchange transaction," which is excluded from the definition of goods in subsection (a)(11) below. A distinction is made between debiting and crediting balances for monetary exchange and physical delivery of money in a currency exchange. Only the latter will be within the scope of Chapter 2. The former does not involve a transaction in goods, but will be governed by other law, such as Chapter 4A.

**(a)(10) "Good faith" means honesty in fact and the observance of reasonable commercial standards of fair dealing.**

#### **State Bar Committee Recommendation**

**This definition was adopted by the Texas Legislature in 2003 as part of Revised Chapter 1 and thus should not be included in Chapter 2. See Revised Section 1.201(b)(20). It is recommended that "Good Faith" be added to this section only as a "Definitional Cross Reference."**

**(a)(11) "Goods" means all things that are movable at the time of identification to a contract for sale. The term includes future goods, specially manufactured goods, the unborn young of animals, growing crops, and other identified things attached to realty as described in Section 2-107. The term does not include information, the money in which the price is to be paid, investment securities under Article 8, the subject matter of foreign exchange transactions, or choses in action.**

This definition is moved from current Section 2.105. The major changes are to exclude "foreign exchange transactions", as defined in subsection (a)(9), and, more importantly, to exclude "information" from the definition of goods. A Prefatory Note to an earlier draft of the proposed amendments to Article 2 advises that this exclusion reflects a compromise after years of struggle by the

drafting committee to determine the extent to which Article 2 should govern transactions that include both goods and information.

The drafting committee ultimately abandoned its attempt to develop a new scope provision for Article 2 and chose instead to confine the scope of Article 2 to “transactions in goods” while making clear that “goods” does not include “information.”

The comments to this new definition suggest that the governance of so-called “hybrid” transactions, for example the sale of “smart goods” such as automobiles that include computer programs and, thus, “information,” will be left to the courts to determine on a case-by-case basis “whether the transaction is entirely within or outside” of Article 2. See Comment 7.

### **State Bar Committee Recommendation**

**The Committee recommends that the reference to information in this amendment be deleted and that the remainder of the amendment be adopted. The amendment would then read as follows.**

**(a)(11) “Goods” means all things that are movable at the time of identification to a contract for sale. The term includes future goods, specially manufactured goods, the unborn young of animals, growing crops, and other identified things attached to the realty as described in Section 2.107. The term does not include the money in which the price is to be paid, investment securities under Article 8, the subject matter of foreign exchange transactions, or choses in action.**

### **State Bar Committee Comment**

**The proposed uniform amendment’s specific reference to “information” as an exclusion to the definition of goods, as well as the explanatory Comment 7, have drawn criticism from commercial and consumer groups alike. The Committee thus recommends that the reference to “information” be deleted. The proposed amendment’s exclusion of “information” from the definition of goods, as an abstract proposition, merely states a truism. The recommended deletion should result in no change in Texas law. The Committee also specifically rejects Comment 7 as ambiguous and, arguably, gratuitous. The Committee recommends that the issues referred to in Comment 7 be left entirely to the courts.**

**(a)(13) “Record” means information that is inscribed on a tangible medium or that is stored in an electronic or other medium and is retrievable in perceivable form.**

### State Bar Committee Recommendation

**The definition for “Record” is included in Revised Article 1 as adopted by the Texas Legislature in 2003 and thus should not be included in Chapter 2. The Committee recommends that “Record” be added to this section only as a “Definitional Cross Reference.”**

**(a)(14) “Remedial promise” means a promise by the seller to repair or replace goods or to refund all or part of the price of goods upon the happening of a specified event.**

As the comments to this provision indicate, the intent of this definition is to distinguish a remedial promise, such as a promise to repair or replace, from a warranty and thereby to resolve an issue that has bothered the courts. See Comment 9. No promise by a seller, other than those specified to repair, replace or refund, qualifies as a remedial promise. A remedial promise is not a warranty, and thus, for example, the statute of limitations for its breach does not begin to run at the time of tender of the goods but only from the time of its breach. See Section 2.725. The comments suggest that a post-sale promise to correct a problem with the goods, which the seller is not obligated to make but is making merely to placate a dissatisfied customer, is not a remedial promise within the definition of this section. This statement may be misleading, and it does not appear to be supported by the text of the definition. It is thus recommended that the “State Bar Committee Comment,” stated below, be adopted. The comments do make clear that a remedial promise is governed by the rules in Section 2.719 regarding limited remedies.

### State Bar Committee Comment:

**The Committee is of the opinion that Official Comment 9 in reference to the definition of “remedial promise” suggests an incorrect or misleading conclusion. It states: “A post-sale promise to correct a problem with the goods that the seller is not obligated to correct that is made to placate a dissatisfied customer is not within the definition of remedial promise.” The Committee finds this statement to be inconsistent both with the right of parties to a contract to modify the agreement in good faith and without additional consideration – as provided in Section 2.209(a) – and with the concept that post-sale statements made by a seller may constitute an express warranty – as suggested by proposed Official Comment 9 to Section 2.313 and by the case law interpreting Official Comment 7 to current Section 2.313. The prevailing law in Texas and elsewhere recognizes that a post-sale affirmation by a seller may constitute an express warranty. The same should be true for a “remedial promise.” See *Harris Packaging Corp. v. Baker Concrete Constr. Co.*, 982 S.W.2d 62 (Tex. App. – Houston [1<sup>st</sup> Dist.] 1998, *pet. denied*) (recognizing that post-sale**

affirmations may constitute express warranties, but holding that those made by manufacturer's employee did not so qualify because no contract of sale existed between contractor and manufacturer).

(a)(16) "Sign" means, with present intent to authenticate or adopt a record:

- (i) to execute or adopt a tangible symbol; or
- (ii) to attach to or logically associate with the record an electronic sound, symbol, or process.

This provision is one of several that are designed to give effect to electronic transactions. The comments to the provision affirm that the definition is consistent with The Uniform Electronic Transactions Act (UETA) and with the federal Electronic Signatures in Global and National Commerce Act (15 U.S.C. §7001 *et seq.*) ("E-Sign").

#### **SECTION 2.108. TRANSACTIONS SUBJECT TO OTHER LAW.**

(a) A transaction subject to this chapter is also subject to any applicable:

(1) [list any certificate of title statutes of this State covering automobiles, trailers, mobile homes, boats, farm tractors, or the like], except with respect to the rights of a buyer in ordinary course of business under Section 2.403(b) which arise before a certificate of title covering the goods is effective in the name of any other buyer;

(2) rule of law that establishes a different rule for consumers;

or

(3) statute of this state applicable to the transaction, such as a statute dealing with:

(i) the sale or lease of agricultural products;

(ii) the transfer of human blood, blood products, human tissues, or parts;

(iii) the consignment or transfer by artists of works of art or fine prints;

(iv) distribution agreements, franchises, and other relationships through which goods are sold;

(v) the misbranding or adulteration of food products or drugs; and

(vi) dealers in particular products, such as automobiles, motorized wheelchairs, agricultural equipment, and hearing aids.

(b) Except for the rights of a buyer in ordinary course of business under subsection (a)(1), in the event of a conflict between this chapter and a law referred to in subsection (a), that law governs.

(c) For purposes of this chapter, failure to comply with a law referred to in subsection (1) has only the effect specified in that law.

**(d) This chapter modifies, limits, and supersedes the federal Electronic Signatures in Global and National Commerce Act, 15 U.S.C. Section 7001 et seq., except that nothing in this chapter modifies, limits, or supersedes Section 7001(c) of that Act or authorizes electronic delivery of any of the notices described in Section 7003(b) of that Act.**

This section is new and is modeled on Section 2A.104. Its most important effects are to exempt Article 2 from “E-Sign” to the extent permitted by the federal act and to resolve the vexing issues that have arisen in many states, including Texas, regarding conflicts between Article 2 and state certificate of title acts. This provision gives primacy to a certificate of title act “except with respect to the rights of a buyer in ordinary course of business under Section 2.403(b) which arise before a certificate of title covering the goods is effective in the name of any other buyer.” Thus, the certificate of title act governs subject only to the entrustment rule in Section 2.403(b) for a buyer in ordinary course of business whose rights arise before a certificate of title is issued in the name of a different buyer.

#### **State Bar Committee Comment**

**Subsection (a)(1) will resolve the inconsistencies in Texas court decisions regarding conflicts between the rights of a holder of a certificate of title as provided by the Texas Certificate of Title Act and those of a buyer in the ordinary course of business as provided by UCC Section 2.403(b). See, for example, *Associates Discount Corp. v. Rattan Chevrolet, Inc.* 462 S.W.2d 546 (Tex. 1970) (conflicts between title act and UCC are governed by the UCC) and *Gallas v. Car Biz, Inc.*, 914 S.W.2d 592 (Tex. App. – Dallas 1995) (title act governs conflicts with UCC). Subsection (a)(1) provides that the UCC will govern in favor of a buyer in the ordinary course of business only in an entrustment situation and only if the buyer’s rights arise before a certificate of title becomes effective in the name of another buyer.**

**By its terms, Subsection (a)(3) is not exhaustive in its listing of applicable Texas statutes. See, for example, UCC Section 1.103(c), which provides that, with limited exception, Section 35.51 of the Title governs an agreement of the parties specifying applicable law.**

### **III. SUBCHAPTER B. FORM, FORMATION, TERMS AND READJUSTMENT OF CONTRACT; ELECTRONIC CONTRACTING**

The noteworthy changes in Subchapter B of Chapter 2 primarily relate to a new provision, Section 2.204(d), and new Sections 2.211, 2.212 and 2.213 which contain the rules for electronic contracting. Section 2.207, the so-called

“battle of the forms” provision in current Chapter 2, has been substantially modified. Section 2.210 on assignment and delegation has been rewritten to conform its rules to those in Revised Article 9. The statute of frauds in Section 2.201 has been amended to raise the baseline to \$5000 and by a new provision pertaining to contracts that are incapable of being performed within a specified period of time.

### **SECTION 2.201. FORMAL REQUIREMENTS; STATUTE OF FRAUDS.**

This section remains unchanged except as follows.

Applicability is for sale of goods contracts for the price of \$5,000 or more rather than for the \$500 currently provided.

The requirement is for a “record” rather than for a “writing” as currently provided.

In subsection (c)(2), dealing with the “in court” admission exception, the words “in court” are replaced by “under oath.” This change would contradict the result in cases that have held that an admission made in response to a request for admissions, interrogatories, and other unsworn documents, such as appendices to pleadings, do qualify as admissions for purposes of this provision.

A new subsection (d) is provided, which states: “A contract that is enforceable under this section is not unenforceable merely because it is not capable of being performed within one year or any other period after its making.” The comments suggest that this provision is intended to repeal statutes to the extent they have been interpreted to apply to contracts for the sale of goods. Thus, statutes of frauds other than Section 2.201 do not apply to a contract for sale of goods. See Comment 8.

The prefatory language in subsection (a) “Except as otherwise provided in this section . . .” is deleted. The comments state that the intent is to make clear that the stated exceptions in subsection (c) are not exclusive and to leave open “the possibility that a promisor will be estopped to raise the statute-of-frauds defense in appropriate cases.” See Comment 2.

### **SECTION 2.202. FINAL EXPRESSION IN A RECORD; PAROL OR EXTRINSIC EVIDENCE.**

The only change that may perhaps be substantive, other than the use of “record” rather than “writing,” is the deletion of the word “explained” from the statement in the current act that the agreement may be “explained or supplemented” by extrinsic evidence. Although no reason is given in the comments for the deletion, a new subsection (b) is added that allows explanation “by evidence of course of performance, course of dealing, or usage of trade without a preliminary determination by the court that the language used

is ambiguous.” Thus, only consistent additional terms may not be used to explain a fully integrated writing. If this interpretation is correct, the amendment represents no change in current law. The reference to “ambiguity” in subsection (b) merely states what is implicit in the current text as explained by existing Official Comment 2.

#### **SECTION 2.204. FORMATION IN GENERAL.**

The substance of this section remains unchanged except for provisions to allow for electronic contracting. Subsection (a) states that a contract may be formed by “the interaction of electronic agents, and the interaction of an electronic agent and an individual.” Subsection (d) then provides as follows:

**(d) Except as otherwise provided in Sections 2.211 through 2.213, the following rules apply:**

**(1) A contract may be formed by the interaction of electronic agents of the parties, even if no individual was aware of or reviewed the electronic agents’ actions or the resulting terms and agreements.**

**(2) A contract may be formed by the interaction of an electronic agent and an individual acting on the individual’s own behalf or for another person. A contract is formed if the individual takes actions that the individual is free to refuse to take or makes a statement, and the individual has reason to know that the actions or statement will:**

**(i) cause the electronic agent to complete the transaction or performance; or**

**(ii) indicate acceptance of an offer, regardless of other expressions or actions by the individual to which the electronic agent cannot react.**

With the exception of (d)(ii), subsection (d) is taken directly from Sections 14(a) and (b) of the Uniform Electronic Transactions Act (UETA). Subsection (d)(ii) is entirely new and is not to be found in UETA, in the Uniform Consumer Information Transactions Act (UCITA), nor in the Electronic Signatures in Global and National Commerce Act (ESIGN). Subsection (d)(ii) has drawn heated criticism, particularly from consumer groups.

#### **State Bar Committee Recommendation**

**The Committee recommends that subsection (d) of the proposed uniform amendment be rejected. For the reasons stated below, the Committee will also recommend that the proposed amendments in Sections 2.211, 2.212, and 2.213 be rejected.**

**State Bar Committee Comment**

Subsection (d), as well as Sections 2.211, 2.212, and 2.213 of the uniform proposed amendments all refer to electronic contracting and, except for subsection (d)(ii), are taken from UETA, ESIGN, and from UCITA, a proposed uniform act that has been adopted in only two states and has otherwise been consistently rejected by all state legislatures that have considered it. Because issues pertaining to electronic contracting are governed by the Texas version of UETA, the Committee finds these proposed amendments to be superfluous and to promise potential future confusion in the event that UETA is amended by the Texas Legislature. The Committee thus recommends that all of these proposed uniform amendments be rejected so that issues pertaining to electronic contracting under Texas law will be left entirely with UETA. No unintended change in Texas law will occur from this rejection, either now or in the future.

CAUTION: In applying the UCC to electronic transactions, current versions of UETA and, to a lesser extent, ESIGN must be consulted.

**State Bar Committee Suggested Amendment**

**A stylistic change is recommended for subsection (a). The provision would be improved if the listed methods of contract formation were specifically enumerated by romanettes so that the provision would read as follows:**

**(a) A contract for sale of goods may be made in any manner sufficient to show agreement, including [i] offer and acceptance, [ii] conduct by both parties which recognizes the existence of a contract, [iii] the interaction of electronic agents, and [iv] the interaction of an electronic agent and an individual.**

**SECTION 2.206. OFFER AND ACCEPTANCE IN FORMATION OF CONTRACT.**

This section adds a new subsection (c) which provides: “A definite and reasonable expression of acceptance in a record operates as an acceptance even if it contains terms additional to or different from the offer.” This provision is taken directly from Section 2.207(a) of current Article 2. The purpose is apparently to provide all the rules for contract formation in Section 2.206 and to have Section 2.207 deal entirely with the question of what terms become part of a contract formed by conduct.

In new subsection (c), the “expressly made conditional” proviso in current Section 2.207(a) is deleted, apparently as superfluous. The Official Comments for the provision nevertheless do make clear that, to constitute an acceptance, “any responsive record must still be reasonably understood as an ‘acceptance’ and not as a proposal for a different transaction.” See Comment 2. Regardless,

there is no good reason for removing the proviso from the text, and retaining it will continue to validate the language in the forms of the large number of merchants who have for many years drafted their forms to track the language in the current statute. The State Bar Committee thus recommends that new subsection (c) be adopted but include the deleted proviso. It would then read as follows.

#### **State Bar Committee Suggested Amendment**

- (c) **A definite and seasonable expression of acceptance in a record operates as an acceptance even if it contains terms additional to or different from the offer, *unless acceptance is expressly made conditional on assent to the additional or different terms.***  
[emphasis added to reflect the recommended change]

#### **State Bar Committee Comment**

The uniform amendment to Section 2.206 includes a new subsection (c), which is taken from current Section 2.207, but deletes the “unless” clause from the current language. This clause provides that an offeree may accept an offer even though the acceptance states additional or different terms “unless acceptance is expressly made conditional on assent to the additional or different terms.” Although Official Comment 3 to the proposed amendment suggests, perhaps correctly, that the “unless” clause is superfluous and that no change in the law is intended by its deletion, the quoted language is reinserted in new subsection (c) in recognition of the fact that many acknowledgement forms in current use by the business community adopt this language to make clear that the form does not constitute an acceptance. Retaining this language will thus remove any uncertainty about the matter that might encourage the business community unnecessarily to incur the expense of amending its standard forms.

#### **SECTION 2.207. TERMS OF CONTRACT; EFFECT OF CONFIRMATION.**

Subject to Section 2.202, if (i) conduct by both parties recognizes the existence of a contract although their records do not otherwise establish a contract, (ii) a contract is formed by an offer and acceptance, or (iii) a contract formed in any manner is confirmed by a record that contains terms additional to or different from those in the contract being confirmed, the terms of the contract are:

- (1) terms that appear in the records of both parties;

- (2) terms, whether in a record or not, to which both parties agree; and**  
**(3) terms supplied or incorporated under any provision of this Act.**

This section provides only for the terms that will govern a contract formed under Section 2.206. Its language parallels Section 2.207(c) of current Article 2, and it thus should not change the results that have been reached by the better-reasoned cases applying that provision to contracts formed by conduct.

The intent of the proposed amendment to this section is not to govern issues of contract formation but to provide for the terms that will govern a contract that has already been formed as provided in Section 2.206. It is confusing, however, that the prefatory language of the proposed amendment differs from that in Section 2.206. The Committee suggests that, since the prefatory language refers to methods of contract formation, it should dovetail with Section 2.206. For this reason, it is recommended that the following language be adopted in place of that proposed by the uniform amendment.

#### **State Bar Committee Suggested Amendment**

**Subject to Section 2.202, if a contract is [i] formed in any manner permitted by this Chapter or [ii] is confirmed by a record that contains terms additional to or different from those in the contract being confirmed, the terms of the contract are: [(1), (2), & (3)].**

#### **State Bar Committee Comment**

**The prefatory language of this section has been changed from the proposed uniform text to conform to Section 2.206, which governs methods of contract formation, in order to make clear that this section governs only the terms of an agreement and does not provide for additional methods of contract formation. See Official Comment 3.**

Conspicuous by its absence from the proposed amendment is any provision for additional or different terms in an acceptance record as provided under current Section 2.207(b). The commentary suggests that this issue is left to the courts on a case-by-case basis. See Comment 3. The stated objective of the subsection is to avoid giving effect to either the first or last form exchanged by the parties.

Comment 5 to the new provision states that the drafting committee did not intend to deal specifically with the so-called “rolling contract” problem presented by several recent cases, the best known of which is *Hill v. Gateway 2000*, 105 F.3d 1147 (7th Cir. 1997), a problem as to which the courts and commentators have divided.

**SECTION 2.208. RESERVED.**

This section in current Article 2 deals with course of performance. It is to be “reserved” in those jurisdictions, such as Texas, that have adopted Revised Article 1, which continues current Section 2.208 with no change in substance. See Revised § 1.303.

**SECTION 2.210. DELEGATION OF PERFORMANCE; ASSIGNMENT OF RIGHTS.**

**(a) If the seller or buyer assigns rights under a contract, the following rules apply:**

**(1) Subject to paragraph (b) and except as otherwise provided in Section 9.406 or as otherwise agreed, all rights of the seller or the buyer may be assigned unless the assignment would materially change the duty of the other party, increase materially the burden or risk imposed on that party by the contract, or impair materially that party’s chance of obtaining return performance. A right to damages for breach of the whole contract or a right arising out of the assignor’s due performance of its entire obligation may be assigned despite an agreement otherwise.**

**(2) The creation, attachment, perfection, or enforcement of a security interest in the seller’s interest under a contract is not an assignment that materially changes the duty of or materially increases the burden or risk imposed on the buyer or materially impairs the buyer’s chance of obtaining return performance under paragraph (a) unless, and only to the extent that, enforcement of the security interest results in a delegation of a material performance of the seller. Even in that event, the creation, attachment, perfection, and enforcement of the security interest remain effective. However, the seller is liable to the buyer for damages caused by the buyer, and a court may grant other appropriate relief, including cancellation of the contract or an injunction against enforcement of the security interest or consummation of the enforcement.**

**(b) If the seller or buyer delegates performance of its duties under a contract, the following rules apply:**

**(1) A party may perform its duties through a delegate unless otherwise agreed or unless the other party has a substantial interest in having the original promisor perform or control the acts required by the contract. Delegation of performance does not relieve the delegating party of any duty to perform or liability for breach.**

**(2) Acceptance of a delegation of duties by the assignee constitutes a promise to perform those duties. The promise is enforceable by either the assignor or the other party to the original contract.**

**(3) The other party may treat any delegation of duties as creating reasonable grounds for insecurity and may without prejudice to**

**its rights against the assignor demand assurances from the assignee under Section 2.609.**

**(4) A contractual term prohibiting the delegation of duties otherwise delegable under paragraph (a) is enforceable, and an attempted delegation is not effective.**

**(c) An assignment of “the contract” or “all my rights under the contract” or an assignment in similar general terms is an assignment of rights and unless the language or the circumstances, as in an assignment for security, indicate the contrary, it is also a delegation of performance of the duties of the assignor.**

**(d) Unless the circumstances indicate the contrary a prohibition of assignment of “the contract” is to be construed as barring only the delegation to the assignee of the assignor’s performance.**

This section has been substantially rewritten. It continues the rules in Section 2.210 of current Article 2 with some changes in substance to conform the rules regarding assignment and delegation to the applicable rules in Revised Article 9. See Comment 1. For example, the comments to this new provision give the following examples:

“Subsection [(a)(1)] is subject to Section 9.406 of revised Article 9. That provision makes rights to payment for goods sold (“accounts”), whether or not earned, freely alienable notwithstanding a contrary agreement or rule of law . . . .

“Subsection [(a)(1)] is subject to Subsection [(a)(2)], which conforms with revised Article 9. If an assignment of rights creates a security interest in the seller’s interest under the contract, including a right to future payments, Subsection [(a)(2)] states that there is no material impairment under Subsection [(a)(1)] unless the creation, attachment, perfection and enforcement ‘results in a delegation of material performance of the seller.’ This is unlikely in most assignments, and the buyer’s basic protection is to demand adequate assurance of due performance from the seller if the assignment creates reasonable grounds for insecurity.” See Comment 2.

**Sections 2.211, 2.212 and 2.213, which follow, are new and are intended to state rules that will give effect to electronic contracting.**

#### **SECTION 2.211. LEGAL RECOGNITION OF ELECTRONIC CONTRACTS, RECORDS AND SIGNATURES.**

**(a) A record or signature may not be denied legal effect or enforceability solely because it is in electronic form.**

**(b) A contract may not be denied legal effect or enforceability solely because an electronic record was used in its formation.**

**(c) This chapter does not require a record or signature to be created, generated, sent, communicated, received, stored, or otherwise processed by electronic means or in electronic form.**

**(d) A contract formed by the interaction of an individual and an electronic agent under Section 2.204(d)(2) does not include terms provided by the individual if the individual had reason to know that the agent could not react to the terms as provided.**

In Section 2.211, subsections (a) and (b) are taken from Section 7(a) and (b) of the Uniform Electronic Transactions Act. Subsection (c) is taken from Section 5(b) of UETA. Subsection (d) is taken from Section 2.206(c) of the Uniform Computer Information Transactions Act. The comments to this new provision affirm that it conforms to the federal Electronic Signatures in Global and National Commerce Act. See Comment 1.

#### **State Bar Committee Recommendation**

**For the reasons stated above regarding proposed Section 2.204(d), the Committee recommends that this proposed amendment be rejected in its entirety as superfluous to the Texas version of UETA.**

**SECTION 2.212. ATTRIBUTION.** An electronic record or electronic signature is attributable to a person if it was the act of the person or the person's electronic agent or the person is otherwise legally bound by the act.

Section 2.212 is taken from Section 9 of UETA.

#### **State Bar Committee Recommendation**

**For the reasons stated above regarding proposed Section 2.204(d), the Committee recommends that this proposed amendment be rejected in its entirety as superfluous to the Texas version of UETA.**

**SECTION 2.213. ELECTRONIC COMMUNICATION.**

**(a) If the receipt of an electronic communication has a legal effect, it has that effect even if no individual is aware of its receipt.**

**(b) Receipt of an electronic acknowledgment of an electronic communication establishes that the communication was received but, in itself, does not establish that the content sent corresponds to the content received.**

Section 2.213 is based upon Section 15(e) and (f) of UETA.

**State Bar Committee Recommendation**

**For the reasons stated above regarding proposed Section 2.204(d), the Committee recommends that this proposed amendment be rejected in its entirety as superfluous to the Texas version of UETA.**

**IV. SUBCHAPTER C. GENERAL OBLIGATION AND CONSTRUCTION OF CONTRACT.**

The major changes in Subchapter C are represented by Sections 2.313A and 2.313B which abandon the requirement of privity for actions for breach of warranty or of a remedial promise. New requirements for exclusion and modification of warranties in consumer contracts have been added to Section 2.316. Section 2.325, pertaining to letters of credit, has been amended to conform to Revised Article 5. The provisions regarding the rights of creditors of a true consignee in current Section 2.325 have been deleted because these matters are now governed by Revised Article 9. The provisions in Sections 2.320 through 2.324 pertaining to agreed shipment terms have been deleted. Section 2.309 has been amended to specify that a term of a contract that specifies the standards for notice of termination is valid unless manifestly unreasonable.

**SECTION 2.309. ABSENCE OF SPECIFIC TIME PROVISIONS; NOTICE OF TERMINATION.**

- (3) **Termination of a contract by one party except on the happening of an agreed event requires that reasonable notification be received by the other party and an agreement dispensing with notification is invalid if its operation would be unconscionable. A term specifying standards for the nature and timing of notice is enforceable if the standards are not manifestly unreasonable.**

**State Bar Committee Comment**

The last sentence to subsection (3) is new, but reflects no substantive change in the law. See Section 1.302(b). The Committee, however, specifically rejects the statement in Comment 11 to Section 2.309 that the standard for notice may be no notice at all. The statement is gratuitous and misleading. The first sentence of subsection (3) deals with an agreement to dispense with notification and subjects it to an unconscionability test. The second sentence deals with standards for notification and allows them if they are not manifestly unreasonable. The statement in Comment 11 noted above would apparently collapse these

separate tests by treating an agreement to dispense with notification as a “standard” subject only to the “manifestly unreasonable” test.

**SECTION 2.312. WARRANTY OF TITLE AND AGAINST INFRINGEMENT; BUYER’S OBLIGATION AGAINST INFRINGEMENT.**

(a) Subject to subsection (c) there is in a contract for sale a warranty by the seller that

(1) the title conveyed shall be good and its transfer rightful and shall not, unreasonably expose the buyer to litigation because of any colorable claim to or interest in the goods; and

(2) the goods shall be delivered free from any security interest or other lien or encumbrance of which the buyer at the time of contracting has no knowledge.

(b) Unless otherwise agreed a seller that is a merchant regularly dealing in goods of the kind warrants that the goods shall be delivered free of the rightful claim of any third person by way of infringement or the like but a buyer that furnishes specifications to the seller must hold the seller harmless against any such claim that arises out of compliance with the specifications.

(c) A warranty under this section may be disclaimed or modified only by specific language or by circumstances that give the buyer reason to know that the seller does not claim title, that the seller is purporting to sell only the right or title as the seller or a third person may have, or that the seller is selling subject to any claims of infringement or the like.

This section has been largely rewritten. It should, however, effect no change in the law. For example, subsection (a)(1) now contains a colorable claim provision which is consistent with the comments to current Article 2 and with the better-reasoned cases.

**SECTION 2.313. EXPRESS WARRANTIES BY AFFIRMATION, PROMISE, DESCRIPTION, SAMPLE; REMEDIAL PROMISE.**

This section is continued without substantive change other than to make clear that it applies only in favor of the “immediate buyer.” The next two sections, Sections 2.313A & B, apply for remote buyers.

Subsection (d) is new. It states that: “Any remedial promise made by the seller to the immediate buyer creates an obligation that the promise will be performed upon the happening of the specified event.” The purpose of this provision is to make clear that a remedial promise, as defined in Section 2.103(a)(14), is a concept distinct from an express warranty. See Comment 11.

**SECTION 2.313A. OBLIGATION TO REMOTE PURCHASER  
CREATED BY RECORD PACKAGED WITH OR ACCOMPANYING  
GOODS.**

**(a) In this section:**

**(1) “Immediate buyer” means a buyer that enters into a contract with the seller.**

**(2) “Remote purchaser” means a person that buys or leases goods from an immediate buyer or other person in the normal chain of distribution.**

**(b) This section applies only to new goods and goods sold or leased as new goods in a transaction of purchase in the normal chain of distribution.**

**(c) If in a record packaged with or accompanying the goods the seller makes an affirmation of fact or promise that relates to the goods, provides a description that relates to the goods, or makes a remedial promise, and the seller reasonably expects the record to be, and the record is, furnished to the remote purchaser, the seller has an obligation to the remote purchaser that:**

**(1) the goods will conform to the affirmation of fact, promise or description unless a reasonable person in the position of the remote purchaser would not believe that the affirmation of fact promise or description created an obligation; and**

**(2) the seller will perform the remedial promise.**

**(d) It is not necessary to the creation of an obligation under this section that the seller use formal words such as “warrant” or “guarantee” or that the seller have a specific intention to undertake an obligation, but an affirmation merely of the value of the goods or a statement purporting to be merely the seller’s opinion or commendation of the goods does not create an obligation.**

**(e) The following rules apply to the remedies for breach of an obligation created under this section:**

**(1) The seller may modify or limit the remedies available to the remote purchaser if the modification or limitation is furnished to the remote purchaser no later than the time of purchase or if the modification or limitation is contained in the record that contains the affirmation of fact, promise or description.**

**(2) Subject to a modification or limitation of remedy, a seller in breach is liable for incidental or consequential damages under Section 2.715, but not for lost profits.**

**(3) The remote purchaser may recover as damages for breach of a seller’s obligation arising under subsection (b) the loss resulting in the ordinary course of events as determined in any reasonable manner.**

**(f) An obligation that is not a remedial promise is breached if the goods did not conform to the affirmation of fact, promise or description creating the obligation when the goods left the seller's control.**

**(g) Whether anyone other than an immediate buyer may maintain a cause of action for a breach of warranty or remedial promise under circumstances other than as provided by this section is left to a determination by the courts (Section 2.318).**

This section, which is new, does away with the requirement of privity of contract for remote purchasers to maintain an action for breach of a seller's express warranty or remedial promise. It applies only to a warranty or promise "in a record packaged with or accompanying the goods." See Subsection (c). It also applies only to new goods sold or leased "in the normal chain of distribution." See Subsection (b). For these reasons, this section reflects rules of good common sense and fairness and is recommended for adoption.

Subsection (e) allows the seller to modify or limit the remedies available for breach and specifically provides that, unless otherwise agreed, the seller is not liable to the remote purchaser for consequential damages in the form of lost profits. The modification or limitation must be furnished to the remote purchaser no later than the time of purchase unless it is contained in the record accompanying the goods.

Although subsection (a)(1) defines "immediate buyer," as distinguished from "remote purchaser," the term "immediate buyer" is not used in either the text of or commentary to this section. Both terms are, however, used in Section 2.725 for rules governing the application of the Article 2 statute of limitations.

#### **State Bar Committee Recommendation**

**The Committee recommends adoption of subsection (g) to Section 2.313 if proposed Section 2.313B is rejected as recommended.**

#### **State Bar Committee Comment**

**Proposed uniform Section 2.313B has been rejected because no logical reason is apparent for treating privity issues for warranties made by advertising differently than for warranties made by other means of communication. Whether someone other than an immediate buyer may maintain a cause of action for a breach of warranty or remedial promise other than as provided in Section 2.313A is appropriately left to the courts by Sections 2.313A(g) and 2.318.**

**SECTION 2.313B. OBLIGATION TO REMOTE PURCHASER  
CREATED BY COMMUNICATION TO THE PUBLIC.**

**(a) In this section:**

**(1) “Immediate buyer” means a buyer that enters into a contract with the seller.**

**(2) “Remote purchaser” means a person that buys or leases goods from an immediate buyer or other person in the normal chain of distribution.**

**(b) This section applies only to new goods and goods sold or leased as new goods in a transaction of purchase in the normal chain of distribution.**

**(c) If in an advertisement or a similar communication to the public a seller makes an affirmation of fact or promise that relates to the goods, provides a description that relates to the goods, or makes a remedial promise, and the remote purchaser enters into a transaction of purchase with knowledge of and with the expectation that the goods will conform to the affirmation of fact, promise, or description, or that the seller will perform the remedial promise, the seller has an obligation to the remote purchaser that:**

**(1) the goods will conform to the affirmation of fact, promise or description unless a reasonable person in the position of the remote purchaser would not believe that the affirmation of fact, promise or description created an obligation; and**

**(2) the seller will perform the remedial promise.**

**(d) It is not necessary to the creation of an obligation under this section that the seller use formal words such as “warrant” or “guarantee” or that the seller have a specific intention to undertake an obligation, but an affirmation merely of the value of the goods or a statement purporting to be merely the seller’s opinion or commendation of the goods does not create an obligation.**

**(e) The following rules apply to the remedies for breach of an obligation created under this section:**

**(1) The seller may modify or limit the remedies available to the remote purchaser if the modification or limitation is furnished to the remote purchaser no later than the time of purchase. The modification or limitation may be furnished as part of the communication that contains the affirmation of fact, promise or description.**

**(2) Subject to a modification or limitation of remedy, a seller in breach is liable for incidental or consequential damages under Section 2.715, but not for lost profits.**

**(3) The remote purchaser may recover as damages for breach of a seller’s obligation arising under subsection (b) the loss resulting in the ordinary course of events as determined in any reasonable manner.**

**(f) An obligation that is not a remedial promise is breached if the goods did not conform to the affirmation of fact, promise or description creating the obligation when the goods left the seller's control.**

This section, which is new, is virtually identical to Section 2.313A, but it applies only to express warranties or remedial promises made by a "communication to the public," such as an advertisement. The remote purchaser has rights under this section only if she purchased or leased the goods "with knowledge of and with the expectation that the goods will conform" to the warranty "or that the seller will perform the remedial promise." See Subsection (c).

#### **State Bar Committee Recommendation**

**This section is similar to Section 2.313. Unlike Section 2.313A, however, this section imposes additional requirements on the remote buyer for no apparent reason. Because the committee can ascertain no relevant difference between affirmations and other statements to buyers made by sellers directly and those authorized by sellers to be made by third parties, such as advertisers, adoption of this section is not recommended.**

#### **SECTION 2.316. EXCLUSION OR MODIFICATION OF WARRANTIES.**

This section codifies the rules in Section 2.316 of current Article 2. For consumer contracts, the section adds these additional requirements:

1. to disclaim the implied warranty of merchantability, the disclaimer must be in a record and conspicuously state that: "The seller undertakes no responsibility for the quality of the goods except as provided in this contract"; and

2. to disclaim the implied warranty of fitness, the record must state that: "The seller assumes no responsibility that the goods will be fit for any particular purpose for which you may be buying these goods, except as otherwise provided in the contract." As under current Article 2, however, the disclaimer of any implied warranty may also be by simple language such as "as is," in which case subsection (c)(1) adds a new requirement that this alternative language be conspicuous in the record.

It should also be noted that, for consumer contracts, a disclaimer of the implied warranty of merchantability may no longer be done orally but must be in a record.

The Committee finds all of these changes to be reasonable and recommends their adoption.

**SECTION 2.318. THIRD PARTY BENEFICIARIES OF WARRANTIES AND OBLIGATIONS.**

**(a) In this section:**

**(1) “Immediate buyer” means a buyer that enters into a contract with the seller,**

**(2) “Remote purchaser” means a person that buys or leases goods from an immediate buyer or other person in the normal chain of distribution.**

*Alternative A to subsection (b)*

**(b) A seller’s warranty to an immediate buyer, whether express or implied, a seller’s remedial promise to an immediate buyer, or a seller’s obligation to a remote purchaser under Section 2.313A or 2.313B extends to any natural person who is in the family or household of the immediate buyer or the remote purchaser or who is a guest in the home of either if it is reasonable to expect that the person may use, consume or be affected by the goods and who is injured in person by breach of the warranty, remedial promise or obligation. A seller may not exclude or limit the operation of this section.**

*Alternative B to subsection (b)*

**(b) A seller’s warranty to an immediate buyer, whether express or implied, a seller’s remedial promise to an immediate buyer, or a seller’s obligation to a remote purchaser under Section 2.313A or 2.313B extends to any natural person who may reasonably be expected to use, consume or be affected by the goods and who is injured in person by breach of the warranty, remedial promise or obligation. A seller may not exclude or limit the operation of this section.**

*Alternative C to subsection (b)*

**(b) A seller’s warranty to an immediate buyer, whether express or implied, a seller’s remedial promise to an immediate buyer, or a seller’s obligation to a remote purchaser under Section 2.313A or 2.313B extends to any person that may reasonably be expected to use, consume or be affected by the goods and that is injured by breach of the warranty, remedial promise or obligation. A seller may not exclude or limit the operation of this section with respect to injury to the person of an individual to whom the warranty, remedial promise or obligation extends.**

This section simply continues the rule alternatives in current Section 2.318 for horizontal privity situations but expands each alternative to include the new obligations pertaining to warranties and remedial promises as provided in Sections 2.313A and 2.313B.

The Texas version of current Section 2.318 is unique in that it adopts none of the alternatives in UCC § 2-318 but instead leaves these matters entirely to the courts. If this approach is to be continued, language should be added to conform to Section 2.313A if that section is adopted.

#### **State Bar Committee Suggested Amendment**

#### **SECTION 2.318. THIRD-PARTY BENEFICIARIES OF WARRANTIES AND OBLIGATIONS.**

**This chapter does not provide whether anyone other than an “immediate buyer,” which means a buyer that enters into a contract with the seller, may take advantage of an express or implied warranty of quality or a remedial promise made to the “immediate buyer” or whether the “immediate buyer” or anyone entitled to take advantage of a warranty or remedial promise made to the “immediate buyer” may sue a third party other than the immediate seller for deficiencies in the quality of the goods or for breach of a remedial promise made to the “immediate buyer.” These matters are left to the courts for their determination.**

#### **SECTION 2.320 - SECTION 2.324.**

These sections have been eliminated. The shipping terms as codified in these sections in current Article 2 may be inconsistent with current commercial practice. Regardless, the commercial meaning of shipping terms should be determined by commercial usage and understanding and should not be legislated.

#### **SECTION 2.325. FAILURE TO PAY BY AGREED LETTER OF CREDIT.**

**If the parties agree that the primary method of payment will be by letter of credit, the following rules apply:**

**(1) The buyer’s obligation to pay is suspended by seasonable delivery to the seller of a letter of credit issued or confirmed by a financing agency of good repute in which the issuer and any confirmer undertake to pay against presentation of documents that evidence delivery of the goods.**

**(2) Failure of a party seasonably to furnish a letter of credit as agreed is a breach of the contract for sale.**

**(3) If the letter of credit is dishonored or repudiated, the seller, on reasonable notification, may require payment directly from the buyer.**

This section has been substantially rewritten. The rules stated are clear and are designed to conform to Revised Article 5.

#### **SECTION 2.326. SALE ON APPROVAL AND SALE OR RETURN.**

The major substantive change is the deletion of subsection (c) of current Article 2, which deals with true consignments and the rights of creditors of the consignee. These matters are now dealt with by Revised Article 9. The comments to this section cite, for example, to Sections 9-109(a)(4), 9-103(d), and 9-319. See Comment 4.

#### **SECTION 2.328. SALE BY AUCTION.**

Although the wording of this section has been changed substantially, the basic rules remain the same. The phrases “with reserve” and “without reserve” are no longer used and are replaced by the phrase “the seller’s right to withdraw the goods.” The amendments also provide a new provision that makes clear that the right to withdraw can either be invoked for the first time or withdrawn during the course of the auction; i.e., after bidding has begun.

### **V. SUBCHAPTER D. TITLE, CREDITORS AND GOOD FAITH PURCHASERS.**

There are no substantive changes of note for Subchapter D.

### **VI. SUBCHAPTER E. PERFORMANCE.**

The noteworthy changes in Subchapter E are to Sections 2.502, 2.507, 2.508 and 2.509. Section 2.502 is amended to give a consumer buyer the right to recover the goods regardless of the seller’s solvency and to specify that a prepaying buyer’s right to recover is not subject to a security interest that attaches after the buyer acquires a special property interest.

Section 2.507 now makes clear that cash-sale and credit-sale transactions stand on equal footing and that the seller’s reclamation right is subject to those of a buyer in the ordinary course or other good faith purchaser.

Section 2.508 on cure has been substantially rewritten. The major change is to give the seller a limited right to cure after a buyer’s revocation of acceptance.

Section 2.509(c) has been amended to provide that risk of loss passes from both merchant and consumer sellers upon receipt of the goods by the buyer.

**SECTION 2.502. BUYER'S RIGHT TO GOODS ON SELLER'S INSOLVENCY.**

There are two substantive revisions to Section 2.502. First, the rights in this section are extended to a pre-paying consumer buyer in any situation where the seller has repudiated or failed to deliver the goods, regardless of the solvency of the seller. Second, subsection (b) provides that: "The buyer's right to recover the goods under subsection (a) (1) vests upon acquisition of a special property, even if the seller had not then repudiated or failed to deliver." The buyer acquires a special property under Section 2.501 upon identification of the goods to the contract. A new Comment 3 to this section explains that, even if the buyer does not buy in ordinary course, she will then "take free of a security interest created by the seller if it attaches to the goods after the goods have been identified to the contract." These amendments are sensible, and the Committee recommends their adoption.

**SECTION 2.507. EFFECT OF SELLER'S TENDER; DELIVERY ON CONDITION.**

**(a) Tender of delivery is a condition to the buyer's duty to accept the goods and, unless otherwise agreed, to the buyer's duty to pay for them. Tender entitles the seller to acceptance of the goods and to payment according to the contract.**

**(b) If payment is due and demanded on the delivery to the buyer of goods or documents of title, the seller may reclaim the goods delivered upon a demand made within a reasonable time after the seller discovers or should have discovered that payment was not made.**

**(c) The seller's right to reclaim under subsection (b) is subject to the rights of a buyer in ordinary course or other good-faith purchaser for value under this Chapter (Section 2.403).**

The changes in this section support the results of the better-reasoned cases that have interpreted Section 2.507. As explained by the Comments, the purposes are to clarify that the seller's reclamation rights are "parallel in credit-sale and cash-sale transactions" and that those rights are "subject to the right of the buyer in the ordinary course of business or other good faith purchaser." See Comments 3 and 4.

**SECTION 2.508. CURE BY SELLER OF IMPROPER TENDER OR DELIVERY; REPLACEMENT.**

**(a) If the buyer rejects goods or a tender of delivery under Section 2.601 or 2.612 or, except in a consumer contract, justifiably revokes acceptance under Section 2.608(a)(2) and the agreed time for performance**

**has not expired, a seller that has performed in good faith, upon reasonable notice to the buyer and at the seller's own expense, may cure the breach of contract by making a conforming tender of delivery within the agreed time. The seller shall compensate the buyer for all of the buyer's reasonable expenses caused by the seller's breach of contract and subsequent cure.**

**(b) If the buyer rejects goods or a tender of delivery under Section 2.601 or 2.612 or, except in a consumer contract, justifiably revokes acceptance under Section 2.608(a)(2) and the agreed time for performance has expired, a seller that has performed in good faith, upon reasonable notice to the buyer at the seller's own expense, may cure the breach of contract, if the cure is appropriate and timely under the circumstances, by making a tender of conforming goods. The seller shall compensate the buyer for all of the buyer's reasonable expenses caused by the seller's breach of contract and subsequent cure.**

Although this section has been substantially rewritten, it provides for only one substantive change of note. Except in a consumer contract, the seller may be allowed to cure after the buyer has properly revoked acceptance. The courts have consistently held under Section 2-508 of current Article 2 that a seller may not cure after a proper revocation.

The amendment permitting post-revocation cure, however, should not change the result in any cases where the seller had previously had the opportunity to cure, but had failed to cure or had refused the opportunity. The amendment should apply only in situations where the buyer seeks to revoke acceptance because of a latent defect and the seller has not previously had an opportunity to cure that defect. Since it is both sensible and fair to allow the seller an opportunity to cure in such a situation and because the cure must not only be conforming but "appropriate and timely under the circumstances," it is unclear why the right should not extend as well to commercial contracts. See Comment 2. The State Bar Committee, however, recommends adoption of the proposed amendment but makes no recommendation regarding whether the new cure right should be extended to commercial sellers.

#### **SECTION 2.509. RISK OF LOSS IN THE ABSENCE OF BREACH.**

The only significant change in substance made by the proposed amendment is that the residual rule in subsection (c) would now provide that risk of loss passes to the buyer on receipt of the goods regardless of whether the seller is a merchant. Under the current provision, risk of loss passes to the buyer upon tender of the goods if the seller is not a merchant.

Although the amendment is of no commercial importance, it will promote greater certainty in non-commercial transactions because receipt is a more concrete concept than is tender, and risk of loss will not pass until the buyer

clearly has control of the goods. Receipt requires taking physical possession. See Section 2.103(a)(12). Further, it is more likely that the buyer will have arranged for insurance of the goods by the time he takes possession of them. The Committee thus recommends adoption of this amendment.

## VII. SUBCHAPTER F. BREACH, REPUDIATION, AND EXCUSE.

The major changes in Subchapter F are as follows.

The requirement of particularization of defects in Section 2.605 is extended to revocation cases, but the buyer's failure to particularize will no longer bar an action for damages.

Section 2.607 has been amended so that a buyer's failure to give timely notice of breach will bar a buyer's remedy only to the extent the seller has been prejudiced by the failure.

Section 2.608 now contains provisions regarding a buyer's reasonable use of the goods following either rejection or revocation.

Section 2.612 has been amended to delete the requirement of noncurability for rejection of an installment and to adopt a subjective standard for determining substantial impairment to the buyer.

### SECTION 2.605. WAIVER OF BUYER'S OBJECTIONS BY FAILURE TO PARTICULARIZE.

The major changes are in Subsection (a), which reads as follows:

**(a) A buyer's failure to state in connection with rejection a particular defect or in connection with revocation of acceptance a defect that justifies revocation precludes the buyer from relying on the unstated defect to justify rejection or revocation of acceptance if the defect is ascertainable by reasonable inspection:**

**(1) if the seller had a right to cure the defect and could have cured it if stated seasonably; or**

**(2) between merchants, if the seller has after rejection or revocation of acceptance made a request in a record for a full and final statement in a record of all defects on which the buyer proposes to rely.**

This provision embodies two changes. First, the buyer's failure under this section will bar only the buyer's remedies of rejection and revocation. The right to damages is now governed by new Section 2.607(c).

Second, the notice requirement in this section is extended to include revocation of acceptance as well as rejection. This change is necessitated by the extension to revocation cases of the seller's right to cure under Section 2.508.

This section also makes clear that it applies only where the seller had both the right and the ability to cure.

#### **SECTION 2.606. WHAT CONSTITUTES ACCEPTANCE OF GOODS.**

With the exception of subsection (a)(3), the amendments to this section are stylistic. The proposed amendment to subsection (a)(3) subjects a buyer's actions that are inconsistent with the seller's ownership to the so-called "continued use doctrine" that is proposed as an amendment to Section 2.608. See proposed Section 2.608(d). As explained below regarding proposed Section 2.608(d), the Committee recommends that the "continued use doctrine" not be extended to situations where the buyer has rejected the goods. If that recommendation is followed, the language subjecting subsection (a)(3) to Section 2.608(d) should not be adopted.

The proposed amendment to subsection (a)(3) also deletes the language in the current provision that makes it clear that a wrongful act against the seller operates as an acceptance of the goods only if ratified by the seller. Presumably the purpose of the current language is to preserve the seller's right to treat the wrongful act as a conversion and to sue the buyer in tort. Deleting this current language would suggest that the buyer's wrongful act would result only in an acceptance, and not in a conversion, and that the seller's sole recourse against the buyer would be an action for the price for accepted goods as provided in Section 2.709. Restricting the seller to a contract action for the unpaid contract price for the goods would honor the seller's full lost expectation from the bargain made with the buyer as provided by Section 1.305 and is thus the better result.

#### **State Bar Committee Recommendation**

**For the reasons stated above, the Committee recommends adoption of the proposed amendment to subsection (a)(3) but without inclusion of the language that makes the provision subject to Section 2.608(d). The provision would thus read as follows:**

**(3) does any act inconsistent with the seller's ownership.**

#### **SECTION 2.607. EFFECT OF ACCEPTANCE; NOTICE OF BREACH; BURDEN OF ESTABLISHING BREACH AFTER ACCEPTANCE; NOTICE OF CLAIM OR LITIGATION TO PERSON ANSWERABLE OVER.**

There is only one major substantive change in this section, but it promises to be controversial because it contravenes the law of sales as applied by the courts both under the UCC and general contract law. The failure of the buyer to give timely notice of breach will now bar any remedy "only to the extent that

the seller is prejudiced by the failure.” *Proposed Section 2.607(c)(1)*. Comment 4 disingenuously refers to this change only in passing and cites only Restatement (Second) of Contracts §229 in its support. The Restatement provision, however, deals solely with the issue of waiver of an agreed express condition and does not address the common law requirement of giving notice of breach.

The wisdom of this new prejudice requirement is questionable because it is the buyer who has unreasonably failed to act properly and because it may place an unreasonable burden on the seller; i.e., to prove what he would have done to protect himself had a fictitious event (timely notice) actually occurred.

### **State Bar Committee Recommendation**

**The Committee recommends that the proposed amendment to Section 2.607(c)(1) be rejected and that the language of the current provision be retained. The provision would then read as follows:**

- (1) The buyer must within a reasonable time after the buyer discovers or should have discovered any breach notify the seller of breach or be barred from any remedy.**

### **SECTION 2.608. REVOCATION OF ACCEPTANCE IN WHOLE OR IN PART.**

The only substantive change in this section is the addition of a new subsection (d), which adopts rules for situations where the buyer uses the goods following a rightful rejection or justifiable revocation of acceptance. It states:

**(d) If a buyer uses the goods after a rightful rejection or justifiable revocation of acceptance, the following rules apply:**

- (1) Any use by the buyer which is unreasonable under the circumstances is wrongful as against the seller and is an acceptance only if ratified by the seller.**

- (2) Any use of the goods which is reasonable under the circumstances is not wrongful as against the seller and is not an acceptance, but in an appropriate case the buyer is obligated to the seller for the value of the use to the buyer.**

These rules affirm the established case law for revocation of acceptance but extend it to apply to situations where the buyer has made a rightful rejection. This means that a buyer who has rightfully rejected may use the goods if reasonably necessary without running the risk of being held to have accepted them. If appropriate, the rejecting or revoking buyer must account to the seller for the value to the buyer of the use of the goods.

### State Bar Committee Recommendation

The Committee recommends that the proposed amendment be adopted only for revocation of acceptance cases. The amendment should be reworded to make clear that the “continued use” doctrine does not extend to rejection cases. In place of the proposed amendment, the Committee recommends the following:

- (d) If a buyer uses the goods after a revocation of acceptance, the following rules apply:
  - (1) Any use by the buyer that is unreasonable under the circumstances is wrongful as against the seller and any revocation of acceptance is ineffective.
  - (2) Any use of the goods that is reasonable under the circumstances is not wrongful as against the seller, but in an appropriate case the buyer is obligated to the seller for the value of the use to the buyer.

### State Bar Committee Comment

The proposed amendment to this section in subsection (d) would codify the reasonable continued use doctrine that is well-established by current case law. The courts, however, have applied the doctrine only to revocation of acceptance cases where the buyer can show that, at the time of tender, a nonconformity in the goods substantially impaired their value. To apply the doctrine generally to rejection cases would reflect a fundamental change in the law that would be justified by no court decision that has been brought to the Committee’s attention. The proposed amendment has thus been reworded to apply only to revocation cases. A wholesale adoption of the continued use doctrine for rejection cases is rejected. Whether the doctrine might be applied appropriately under the facts of a particular rejection case is left to the courts. The Committee thus also rejects language in new Comment 8 to this section to the extent that it suggests allowing the buyer a general right to reject the goods after a reasonable continued use of them.

### SECTION 2.610. ANTICIPATORY REPUDIATION.

The only change in this section is the addition of a new subsection (b), which provides:

(b) Repudiation includes language that a reasonable person would interpret to mean that the other party will not or cannot make a performance still due under the contract or voluntary, affirmative conduct

**that would appear to a reasonable person to make a future performance by the other party impossible.**

This provision is supported by the Comments to current Section 2.610 and by the common law of contract and thus should not be regarded as a change in the law.

#### **SECTION 2.612. "INSTALLMENT CONTRACT"; BREACH.**

The only substantive changes to this section are in subsection (b), which currently allows the buyer to reject an installment if a defect substantially impairs its value and cannot be cured. The proposed modification deletes the non-curability requirement and adopts a subjective standard, "to the buyer," for determining whether the defect substantially impairs the value of the installment. If the seller, however, does give adequate assurance of cure, the buyer must accept the installment. The commentary to the modification states that the adoption of the subjective standard of "to the buyer" is to "clarify" that the standard for rejection in installment contracts is the same as for revocation of acceptance in a single tender contract. See Comment 8. The suggestion that this is merely a "clarification" is questionable, but it does state the better rule. The Committee thus recommends adoption of the proposed amendment.

#### **VIII. SUBCHAPTER G. REMEDIES.**

The amendments to Subchapter G contain several major changes. They are as follows.

First, all of the seller's damages remedy provisions in Sections 2.706, 2.708 and 2.709 have been amended to allow for a seller's recovery of consequential damages as provided in Section 2.710.

Second, Sections 2.708 and 2.713 provide new rules for measuring damages in repudiation cases.

Third, Section 2.718 seeks to implement a dramatic expansion of the use of liquidated damages provisions in non-consumer contracts by deleting the uncertainty and inconvenience principles for their validity.

Fourth, Section 2.725 has been substantially rewritten to provide several new statute of limitations rules, including a new discovery of breach rule.

Changes of lesser importance include the following.

Section 2.702 regarding a seller's reclamation rights has been modified by deleting the "10 days" and misrepresentation of insolvency provisions.

Section 2.707 has been modified to expand the remedies available to a person in the position of a seller.

The "learned of the breach" time for measuring market damages is deleted from Section 2.713 thereby leaving open the question of the time for measuring

market price when the buyer does not learn of the breach until after the time set for performance.

A new provision has been added to Section 2.716 allowing the parties to agree to specific performance as the primary remedy for breach in non-consumer contracts. Section 2.716 also contains a new provision for early vesting of the buyer's right to replevin.

#### **SECTION 2.702. SELLER'S REMEDIES ON DISCOVERY OF BUYER'S INSOLVENCY.**

The only substantive changes of note are in subsection (b), which substitutes a reasonable time for the "ten days" provision in current Article 2 and deletes the current provision regarding a misrepresentation of insolvency. The modified provision reads as follows:

**(b) If the seller discovers that the buyer has rejected goods on credit while insolvent, the seller may reclaim the goods upon demand made within a reasonable time after the buyer's receipt of the goods. Except as provided in this subsection, the seller may not base a right to reclaim goods on the buyer's fraudulent or innocent misrepresentation of solvency or of intent to pay.**

The Comments to the modification explain that the deletions are justified because, if the buyer is in bankruptcy at the time the seller seeks to reclaim, the seller must comply with Section 546(c) of the Bankruptcy Code, which includes a 10-day limitation. See Comment 2. The Comments further suggest that "any receipt of goods on credit by an insolvent buyer amounts to a tacit business misrepresentation of solvency and therefore is fraudulent as against the particular seller." See Comment 3. The Committee recommends adoption of the proposed amendment.

#### **SECTION 2.703. SELLER'S REMEDIES IN GENERAL.**

**(a) A breach of contract by the buyer includes the buyer's wrongful rejection or wrongful attempt to revoke acceptance of goods, wrongful failure to perform a contractual obligation, failure to make a payment when due, and repudiation.**

**(b) If the buyer is in breach of contract the seller, to the extent provided for by this Act or other law, may;**

- (1) withhold delivery of the goods;**
- (2) stop delivery of the goods under Section 2.705;**
- (3) proceed under Section 2.704 with respect to goods unidentified to the contract or unfinished;**
- (4) reclaim the goods under Section 2.507(b) or 2.702(b);**

- (5) require payment directly from the buyer under Section 2.325(c);
  - (6) cancel;
  - (7) resell and recover damages under Section 2.706;
  - (8) recover damages for nonacceptance or repudiation under Section 2.708(a);
  - (9) recover lost profits under Section 2.708(b);
  - (10) recover the price under Section 2.709;
  - (11) obtain specific performance under Section 2.716;
  - (12) recover liquidated damages under Section 2.718;
  - (13) in other cases, recover damages in any manner that is reasonable under the circumstances.
- (c) If a buyer becomes insolvent, the seller may:
- (1) withhold delivery under Section 2.702(a);
  - (2) stop delivery of the goods under Section 2.705;
  - (3) reclaim the goods under Section 2.702(b).

This section has been substantially rewritten. The Comments to this new provision indicate that the listing of remedies in this section is not intended to be exclusive. See Comment 1. The proposed amendments do provide a more helpful and more accurate guide to the remedies available to sellers but should result in no change in current law. The Committee recommends adoption of the proposed amendment.

The Committee notes that neither current Article 2 nor the proposed amendments provides a general provision regarding mitigation of damages. Such a provision was included in prior drafts of the amendments but was deleted without explanation.

#### **State Bar Committee Recommendation**

**Given the paramount importance of the mitigation principle in the law of contract damages, the Committee recommends that the following provision, taken from Article 77 of the Convention on the International Sales of Goods, be adopted as subsection (d).**

- (d) **An aggrieved seller must take such measures as are reasonable under the circumstances to mitigate damages resulting from the breach. If the seller fails to take such measures, the buyer may claim a reduction in damages in the amount by which the loss should have been mitigated.**

**State Bar Committee Comment**

**Subsection (d) states a general mitigation of damages principle for sellers. It codifies the important principle of contract damages that an aggrieved party may not recover any damages that could have been reasonably avoided under the circumstances. This principle has been uniformly applied by the Texas courts and those of other jurisdictions. The language of this subsection is taken from Article 77 of the Convention on the International Sale of Goods, which makes clear that the burden of pleading and proving issues of mitigation rests with the breaching party, in this case the buyer.**

**SECTION 2.705. SELLER'S STOPPAGE OF DELIVERY IN TRANSIT OR OTHERWISE.**

The only change in this section is the deletion of the limitation on the seller's right to stop delivery of only carload, truckload, planeload or larger shipments when the buyer is in breach. This limitation in current Article 2 has always been questionable but has been subjected to little judicial scrutiny. The Committee recommends adoption of the amendment.

**SECTION 2.706. SELLER'S RESALE INCLUDING CONTRACT FOR RESALE.**

The only substantive changes in this section are to recognize the seller's right to recover consequential damages as provided in Section 2.710 and the addition of a new subsection (g) which provides: **"Failure of a seller to resell under this section does not bar the seller from any other remedy."** This new provision parallels the similar provision in current Section 2.712 regarding a buyer's cover remedy. See Comment 11. The intent is to make clear that a seller's decision not to resell will not automatically bar a recovery of damages under Section 2.708. Presumably, however, this freedom is limited implicitly by the compensation principle in Section 1.305 and by other general damage principles, such as mitigation. It would be much better for these limitations to be effectuated by explicitly restricting a seller who has properly resold the goods from recovering damages based on market price in an amount greater than those produced by the resale. Market price damages are intended only as a surrogate remedy for situations in which the seller has not resold the goods.

**State Bar Committee Recommendation**

**The Committee recommends adoption of additional language to proposed subsection (g), as follows.**

(g) Failure of the seller to resell does not bar the seller from any other remedy, but to the extent the seller makes a proper resale under this section the seller may not recover greater damages based on market price under Section 2.708.

#### State Bar Committee Comment

The purpose of subsection (g) of the proposed uniform amendment is to bring the seller's resale remedy in line with the corresponding cover remedy for an aggrieved buyer in Section 2.712 and to implement the general principles of damage law that allow for full compensation to the aggrieved party subject to the aggrieved party's obligation to act reasonably to mitigate damages. *See Section 1.305. See also, Comment 5 to current UCC Section 2-713, which provides that damages based on market price may be recovered "only when and to the extent that the buyer has not covered."* The additional language recommended by the Committee for inclusion after the comma is also consistent with the current rule for aggrieved lessors under Article 2A. *See Section 2A.528(a), which denies the lessor damages based on market rent to the extent the lessor has made a proper disposition (resale) of the goods.* This recommendation furthers these purposes as well as that of making the seller's UCC resale remedy parallel to that provided by the CISG. *See CISG Article 76(1), which provides: "If the contract is avoided and there is a current price for the goods, the party claiming damages may, if he has not made a purchase or resale under article 75, recover the difference between" the contract price and the market price. (emphasis added).*

#### SECTION 2.707. "PERSON IN THE POSITION OF A SELLER"

The only substantive change is to subsection (b), which now reads:

**"A person in the position of a seller has the same remedies as a seller under this Article."**

Current Section 2.707 ostensibly limits the remedies of a person in the position of a seller. As the Comment to the new provision explains, a person in the position of the seller now "has the full range of remedies available to a seller."

#### SECTION 2.708. SELLER'S DAMAGES FOR NON-ACCEPTANCE OR REPUDIATION.

This section has been amended to allow for a seller's recovery of consequential damages as provided in amended Section 2.710. In subsection

(b), the phrase “due allowance for costs reasonably incurred and due credit for payments or proceeds of resale” has been deleted. Although the phrase has never troubled the courts, it made no sense for lost volume situations to which subsection (b) is commonly applied. The phrase, however, is relevant to calculating damages for incomplete goods situations, to which subsection (b) also applies. The Comments to this section do acknowledge that the appropriate due allowance and due credit should continue to be made in incomplete goods situations just as under current Article 2. See Comment 1 (e).

#### **State Bar Committee Recommendation**

**The Committee recommends that the proposed amendment be rejected and that the current language, which states “. . . , due allowance for costs reasonably incurred and due credit for payments or proceeds of resale . . .”, be retained. The application of the current language has been correctly limited by the courts, and deleting it may cause confusion where none presently exists.**

#### **State Bar Committee Comment**

**The deletion of the due allowance and due credit clauses suggested by the uniform amendments is rejected. Although these clauses are arguably confusing if applied to situations involving completed goods, the courts have uniformly and correctly limited their application to uncompleted goods cases and have not applied them to limit damages for “jobbers or middlemen, and other lost-volume sellers.” See Comment 5. To delete these clauses without careful explanation would undoubtedly create confusion where none presently exists.**

The proposed amendments also add a new subsection (a)(2) for measuring damages in repudiation cases. It provides:

**“(2) the measure of damages for repudiation by the buyer is the difference between the contract price and the market price at the place for tender at the expiration of a commercially reasonable time after the seller learned of the repudiation, but no later than the time stated in paragraph (1), together with any incidental or consequential damages provided in this Chapter (Section 2.710), less expenses saved in consequence of the buyer’s breach.”**

This new provision is intended to parallel Section 2.713(a)(2) for buyers, which is discussed in greater detail below. For buyers, the “reasonable time” after the repudiation is clearly for purposes of allowing the buyer an

opportunity to cover. It is unclear what factors will be relevant to determining the seller's reasonable time under this provision. The remedy for sellers that is parallel to the buyer's cover remedy is resale. Presumably this provision is intended to allow the seller a reasonable opportunity to resell and, if the seller does not resell, to measure damages at the time the seller could reasonably have resold had the seller sought that relief. If the seller could not reasonably resell, damages under this provision would be measured at the time set for tender as provided in subsection (a)(1). In that situation, however, the seller might choose instead to pursue an action for the price as provided in Section 2.709 (a)(2).

The last sentence of Comment 1 (b) is a misstatement. It is the "breaching" buyer who may recover in restitution under Section 2.718. An "aggrieved" buyer's right to recover any payment of the contract price is governed by Section 2.711.

#### **SECTION 2.709. ACTION FOR THE PRICE.**

The only substantive change in this section is to allow for a seller's recovery of consequential damages as defined in Section 2.710. See the discussion under Section 2.710.

#### **SECTION 2.710. SELLER'S INCIDENTAL AND CONSEQUENTIAL DAMAGES.**

This section has been amended to define consequential damages for sellers and to deny their recovery from a consumer buyer. New subsections (b) and (c) provide as follows:

**"(b) Consequential damages resulting from the buyer's breach include any loss resulting from general or particular requirements and needs of which the buyer at the time of contracting had reason to know and which could not reasonably be prevented by resale or otherwise.";**

**"(c) In a consumer contract, a seller may not recover consequential damages from a consumer."**

The granting to sellers of the right to recover consequential damages is a justified major change in current law. Although as the Comments to this section acknowledge, sellers rarely suffer compensable consequential damages, the denial of their recovery to sellers for breach of a commercial contract has long been criticized as inconsistent with the fundamental principle in Section 1.305 that remedies should be liberally administered so as to compensate for the full lost expectation of the aggrieved party. The absolute denial of consequential damages in subsection (c), however, is undoubtedly sensible for the significant majority of consumer contracts.

**SECTION 2.711. BUYER'S REMEDIES IN GENERAL; BUYER'S SECURITY INTEREST IN REJECTED GOODS.**

(a) A breach of contract by the seller includes the seller's wrongful failure to deliver or to perform a contractual obligation, making of a nonconforming tender of delivery or performance, or repudiation.

(b) If the seller is in breach of contract under subsection (a) the buyer may, to the extent provided for by this Act or other law:

(1) in the case of rightful cancellation, rightful rejection or justifiable revocation of acceptance recover so much of the price as has been paid;

(2) deduct damages from any part of the price still due under Section 2.717;

(3) cancel;

(4) cover and have damages under Section 2.712 as to all goods affected whether or not they have been identified to the contract;

(5) recover damages for non-delivery or repudiation under Section 2.713;

(6) recover damages for breach with regard to accepted goods or breach with regard to a remedial promise under Section 2.714;

(7) recover identified goods under Section 2.502;

(8) obtain specific performance or obtain the goods by replevin or the like under Section 2.716;

(9) recover liquidated damages under Section 2.718;

(10) in other cases, recover damages in any manner that is reasonable under the circumstances.

(c) On rightful rejection or justifiable revocation of acceptance a buyer has a security interest in goods in the buyer's possession or control for any payments made on their price and any expenses reasonably incurred in their inspection, receipt, transportation, care and custody and may hold such goods and resell them in like manner as an aggrieved seller (Section 2.706).

This section merely provides an index of the buyer's remedies. It is similar in intent to the index for sellers in Section 2.703. As with the seller's provision, the listing here is presumably not intended to be exhaustive. Although this section has been substantially rewritten, it should result in no change in current law.

**State Bar Committee Recommendation**

For the reasons explained above regarding Section 2.703, the Committee recommends adoption of a subsection (d) as follows to codify a general mitigation of damages principle applicable to aggrieved buyers.

- (d) **An aggrieved buyer must take such measures as are reasonable under the circumstances to mitigate damages resulting from the breach. If the buyer fails to take such measures, the seller may claim a reduction in damages in the amount by which the loss should have been mitigated.**

#### **State Bar Committee Comment**

Subsection (d) states a general principle of mitigation of damages applicable to aggrieved buyers. It corresponds to subsection (d) of Section 2.703 regarding sellers' damages, with the uniform common law rule for contract damages, and with Article 77 of the Convention on the International Sale of Goods, from which the provision is derived.

#### **SECTION 2.712. "COVER"; BUYER'S PROCUREMENT OF SUBSTITUTE GOODS.**

The proposed amendments to Section 2.712 are stylistic and should result in no substantive change in the law.

#### **State Bar Committee Recommendation**

For the reasons stated above under Section 2.706, the Committee recommends that subsection (c) be amended by the addition of the language in italics below.

- (c) **Failure of the buyer to effect cover within this section does not bar the buyer from any other remedy, *but to the extent the buyer makes a proper cover under this section the buyer may not recover damages based on market price under the next section.***

#### **State Bar Committee Comment**

This section has been amended to add language that makes clear that a buyer who has properly covered may not recover damages based on market price. The purpose of the amendment is to bring the buyer's cover remedy in line with the seller's resale remedy under Section 2.706 and to have the remedy correspond to the rule in the Convention on the International Sale of Goods. *See CISG Article 76(1)*. The amendment also reflects the unanimous holdings of the courts that have addressed this issue and merely codifies the law currently stated in Comment 5 to UCC Section 2.713. The amendment would also make the damage remedies available to an aggrieved buyer consistent with those for an aggrieved lessee under current Article 2A. *See Article 2A.519(a), which restricts the*

*lessee's right to recover damages based on market rent to situations in which the lessee has not properly covered.*

**SECTION 2.713. BUYER'S DAMAGES FOR NON-DELIVERY OR REPUDIATION.**

Subsection (a) is amended by dividing its provisions into new subsections (a)(1) and (a)(2). Subsection (a)(1) applies to breach situations and states that damages are to be measured by the market price at the time for tender. The current language "when the buyer learned of the breach" is deleted and replaced with "for tender under the contract" in reference to the appropriate time for measuring market price. Although no UCC case has dealt with the issue, the deleted language was intended to apply to situations in which the buyer did not reasonably learn of the seller's breach until after the time set for tender. Should such a case arise after adoption of this amendment, the proper time for measuring damages would be unclear. Comment 1 unfortunately can be read to mean that no exception should be allowed in such a case.

**State Bar Committee Recommendation**

**The Committee recommends that the language emphasized by italics below be retained in lieu of the proposed language "for tender under the contract."**

**(a)(1) The measure of damages in the case of wrongful failure to deliver by the seller or rightful rejection or justifiable revocation of acceptance by the buyer is the difference between the market price at the time *when the buyer learned of the breach* and the contract price together with any incidental or consequential damages under this Chapter (Section 2.715), but less expenses saved in consequence of the seller's breach; and**

**State Bar Committee Comment**

**The proposed uniform amendment to subsection (a)(1) is rejected in part so that the language in current Section 2.713 that measures market price "when the buyer learned of the breach" is retained. The purpose is to codify existing case law that, when the seller breaches other than by an anticipatory repudiation but the buyer does not reasonably learn of the breach until some time later, damages based on market price are to be measured at the later time. This rule appropriately places the post-breach risk of a rise in market price on the seller, and the retention of the appropriate language removes any doubt as to whether the proposed uniform amendment is intended to overrule existing law. The "learned of**

the breach” language in subsection (a) caused confusion only in anticipatory repudiation cases. That confusion is resolved by new subsection (a)(2).

New subsection (a)(2) applies to situations in which the seller has repudiated. It provides:

**“(2) the measure of damages for repudiation by the seller is the difference between the market price at the expiration of a commercially reasonable time after the buyer learned of the repudiation, but no later than the time stated in paragraph (1), and the contract price together with any incidental or consequential damages provided in this Chapter (Section 2.715), but less expenses saved in consequence of the seller’s breach.”**

This provision follows the majority of cases that have applied current Section 2.713. The “reasonable time” is to allow the buyer an opportunity to cover. Damages are to be measured at the end of that time. If the buyer is reasonably unable to cover, damages are to be measured at the time set for tender as provided in subsection (a)(1).

#### **State Bar Committee Recommendation**

If the recommendation of the Committee for retaining the “learned of the breach” language in subsection (a) (1) is adopted, subsection (a) (2) should be amended to make clear that a seller may not await performance beyond the time set for tender by the contract. The recommended amendment is reflected by the italicized language below.

**(2) the measure of damages for repudiation by the seller is the difference between the market price at the expiration of a commercially reasonable time after the buyer learned of the breach, but no later than the time *for tender under the contract*, and the contract price together with any incidental or consequential damages provided in this Article (Section 2.715), less expenses saved in consequence of the seller’s breach.**

#### **State Bar Committee Comment**

Subsection (a)(2) amends the language of the proposed uniform amendment to make clear that a buyer may not measure damages based on a market price later than the time set by the contract for tender. This clarification is necessary in light of the retention in subsection (a)(1) of the language that makes the time “when the buyer learned of the breach” the appropriate time for measuring damages based on market price in situations where the buyer does not reasonably learn of the seller breach

until after the time set for performance. The “learned of the breach” rule does not apply to anticipatory repudiation cases governed by subsection (a)(2).

**SECTION 2.716. SPECIFIC PERFORMANCE; BUYER’S RIGHT TO REPLEVIN.**

Subsection (a) is amended to add the following new language:

**“In a contract other than a consumer contract, specific performance may be decreed if the parties have agreed to that remedy. However, even if the parties agree to specific performance, specific performance may not be decreed if the breaching party’s sole remaining contractual obligation is the payment of money.”**

Except for the payment of money, this new provision allows the parties to a non-consumer contract to agree that specific performance will be the primary remedy for breach. An equitable remedy, however, such as a decree of specific performance, is always discretionary with the court. This provision cannot determine the court’s discretion, but it does suggest that the agreement of the parties may be a primary factor for the court to consider in making its determination.

**State Bar Committee Recommendation**

The Committee recommends that the word “also” be inserted in the second sentence of subsection (a) to make clear that the agreement of the parties is an independent factor for the court to consider in determining whether to grant the specific performance remedy. The provision would then read as follows [emphasis added to reflect the proposed change]:

**(a) Specific performance may be decreed if the goods are unique or in other proper circumstances. In a contract other than a consumer contract, specific performance may *also* be decreed if the parties have agreed to that remedy. However, even if the parties agree to specific performance, specific performance may not be decreed if the breaching party’s sole remaining contractual obligation is the payment of money.**

Subsection (c) adds “similar remedy” to replevin but otherwise remains substantively unchanged. This change is intended simply to acknowledge that replevin is called different things in some jurisdictions, such as “detinue,” “sequestration,” and “claim and delivery.”

A new subsection (d) is added:

**“(d) The buyer’s right under subsection (c) vests upon acquisition of a special property, even if the seller had not then repudiated or failed to deliver.”**

This early vesting right is intended to give the buyer priority over creditors who later acquire rights in the goods. As explained by the Comments, the early vesting rule will favor buyers if a “first in time” priority rule is applicable. See Comment 5. The Committee recommends adoption of the amendment.

### **SECTION 2.718. LIQUIDATION OR LIMITATION OF DAMAGES; DEPOSITS.**

The proposed uniform amendment to Subsection 2.718 (a) proposes an extraordinary change in the law that will undoubtedly prove to be controversial. This amendment seeks to relax the standards for enforceability of liquidated damage provisions currently required by Section 2.718, by the common law of contract, and by longstanding Texas law outside the Uniform Commercial Code.

For non-consumer contracts, the proposed amendment deletes the customary standards of difficulty of proof of loss and inconvenience of obtaining an adequate remedy for determining the validity of liquidated damage provision. The proposed amendment would thus require only that the amount liquidated as damages be reasonable in light of the anticipated or actual harm caused by the breach.

Further, for all contracts, including consumer contracts, the proposed amendment deletes the important current provisions that state: “A term fixing unreasonably large liquidated damages is void as a penalty.”

Finally, the proposed amendment adds an acceptable new provision in its last sentence that merely states that Section 2.719, rather than Section 2.718, controls the enforceability of terms limiting, but not liquidating, damages. For the reasons stated below, the State Bar Committee recommends that, with the exception of this last sentence, the proposed amendment be rejected.

The central objective of contract remedies is to achieve compensation for the aggrieved party without allowing either a windfall recovery or punishment of the breaching party. Liquidated damage provisions can work to provide both windfalls and punitive damages when the amount liquidated is much greater than the readily provable actual damages caused by the breach. The Supreme Court of Texas long ago cogently summarized the proper interaction between the basic principle of compensation for the injury actually caused and the freedom of contracting parties to liquidate damages for breach.

“The right of competent parties to make their own bargains is not unlimited. The universal rule for measuring damages for the breach of a

contract is just compensation for the loss or damage actually sustained. By the operation of that rule a party generally should be awarded neither less nor more than his actual damages. A party has no right to have a court enforce a stipulation which violates the principle underlying that rule. In those cases in which courts enforce stipulations of the parties as a measure of damages for the breach of covenants, the principle of just compensation is not abandoned and another principle substituted therefor[e]. What courts really do in those cases is to permit the parties to estimate in advance the amount of damages, provided they adhere to the principle of just compensation.”

*Stewart v. Basey*, 245 S.W.2d 484, 485-86 (Tex. 1952). Similarly, the Restatement (Second) of Contracts also summarizes the policy considerations as follows:

“The enforcement of such provisions for liquidated damages saves the time of courts, juries, parties and witnesses and reduces the expense of litigation. This is especially important if the amount in controversy is small. However, the parties to a contract are not free to provide a penalty for its breach. The central objective behind the system of contract remedies is compensatory, not punitive. Punishment of a promisor for having broken his promise has no justification on either economic or other grounds and a term providing such a penalty is unenforceable on the grounds of public policy.”

*Restatement (Second) of Contracts Section 356, comment a (1980).*

It is true that the proposed amendment does parallel the current uniform Article 2A provision for leases. Damages for defaults in leases, however, unlike for sales contracts, typically involve the valuation of interests of both parties and the prediction and estimation of future damages that are inherently difficult to quantify. The Article 2A provision thus appropriately relieves the courts from a difficult valuation of the interests involved in more complex lease transactions. Transactions in goods, in contrast, are usually discrete and simple, and their breach is unlikely to cause uncertain damages.

Because the basic touchstone for validating liquidated damage provisions is that the damages likely to be caused by the breach must be uncertain in amount and difficult to quantify, liquidated damage provisions in contracts for the sale of goods are rarely upheld by the courts. As a practical matter, therefore, they are not often used by parties in contracts of sale. Current subsection (a) has thus precipitated very little litigation. The proposed amendment would fundamentally change the law applicable to liquidated damage provisions and would undoubtedly result in a dramatic increase in the use of such provisions in commercial contracts.

The proposed amendment clearly is based on a notion of freedom of contract for commercial parties. The commentary to the amendment simply states that it “respects the parties’ ability to contract for damages while providing some control by requiring that the term be reasonable under the circumstances of the particular case.” See *proposed Comment 2*. This “freedom of contract” principle, however, is unpersuasive in the current context and provides no convincing reason for overturning long-established law by jettisoning the fundamental policy that contract damage remedies must be limited to just compensation for the injury actually caused by the breach. The proposed amendment is perhaps based on the erroneous assumption that all commercial parties are of equal bargaining power. They, of course, are not. The unfortunate result of adoption of this modification would likely be that commercial parties with superior bargaining power would use liquidated damage provisions to coerce performance and to extract penalties for breach.

Regardless, adoption of the proposed amendment would undoubtedly result in a dramatic increase in litigation, requiring the courts of Texas to wrestle with the vexing question of whether a liquidated damage provision is “reasonable” even though both the anticipated and actual damages caused by the breach are readily calculable at a different amount. The Texas courts, in contrast, have long taken the restrictive, but reasonable, view that a liquidated damage provision is not enforceable unless both the anticipated and actual damages are uncertain in amount and difficult to calculate. See *Phillips v. Phillips*, 820 S.W. 2d 785 (Tex. 1991); *Stewart v. Basey*, 245 S.W.2d 484 (Tex. 1952). For all the foregoing reasons, it is recommended that the proposed amendment be rejected and that current Section 2.718 (a) be retained, but that the new last sentence of the proposed amendment be adopted. The Committee also recommends that the disjunctive language “anticipated or actual harm” be changed to the conjunctive “anticipated and actual harm” so as to conform to established Texas law outside the Uniform Commercial Code.

### **State Bar Committee Recommendation**

**For the reasons stated above, the Committee recommends that the proposed uniform amendment be rejected and that current Section 2.718(a) be retained. The Committee also recommends, however, that the new last sentence of the proposed uniform amendment be adopted. It provides that a term that is intended to limit rather than liquidate damages is, in effect, a remedy limitation that should be governed by Section 2.719 on limitation of remedies. This principle is correct and is implicit in the current Official Comments to Section 2.718.**

**The Committee also recommends that the language in the provision be changed to read “anticipated *and* actual harm” rather than “anticipated *or* actual harm. A liquidated damages provision that is unreasonable in**

light of the harm anticipated at the time of the contract in the event of a breach is invalid *ab initio*. This is the law outside the UCC in every jurisdiction, including Texas. See *Semico, Inc. v. Pipefitters Local No. 195*, 538 S.W.2d 273 (Tex. Civ. App. 1976). Texas law, as noted above, also requires that liquidated damages be reasonable in light of the *actual* damages caused by the breach regardless of whether the liquidated damages provision represents a reasonable pre-estimate of *anticipated* damages. See *Phillips v. Phillips*, 820 S.W.2d 785 (Tex. 1991). The current version of Section 2.718(a) would apparently allow enforcement of a liquidated damages provision that is reasonable in light of the anticipated loss even though the actual damages are significantly, and unreasonably, less than the amount liquidated. No Texas court has interpreted Section 2.718 in this regard. This is unsurprising given the current rarity of the use of liquidated damage provisions in contracts for the sale of goods. Whether a Texas court would apply current Section 2.718 in contravention of the rule for all other types of contracts thus remains unclear. The Committee recommends that Section 2.718 be amended to conform to Texas law outside the UCC by requiring that a liquidated damages provision be reasonable in light of both the anticipated and actual harm caused by the breach.

The Committee thus recommends that Section 2.718 be amended to read as follows:

- (a) Damages for breach by either party may be liquidated in the agreement but only at an amount which is reasonable in the light of the anticipated and actual harm caused by the breach, the difficulties of proof of loss, and the inconvenience or non-feasibility of otherwise obtaining an adequate remedy. A term fixing unreasonably large liquidated damages is void as a penalty. Section 2.719 determines the enforceability of a term that limits but does not liquidate damages.

#### State Bar Committee Comment

Subsection (a) is amended to conform to established Texas law outside the Uniform Commercial Code that requires that a liquidated damages provision be reasonable in light of both the anticipated *and* actual harm caused by the breach. See *Phillips v. Phillips*, 820 S.W.2d 785 (Tex. 1991); *Stewart v. Basey*, 245 S.W.2d 484 (Tex. 1952). See also, *Semico, Inc. v. Pipefitters Local No. 195*, 538 S.W.2d 273 (Tex. Civ. App. 1976) (liquidated damages provision held invalid at time of contracting because anticipated damages would have been readily calculable).

The proposed amendment of subsection (b) extends the buyer's restitution rights to insolvency situations and deletes the 20% or \$500 penalty provision. Neither of these changes is significant, and the Committee recommends their adoption.

#### **SECTION 2.723. PROOF OF MARKET: TIME AND PLACE.**

Subsection (a) of current Section 2.723 is deleted because market damages for repudiation situations are governed by new Sections 2.708(a)(2) for sellers and 2.713(a)(2) for buyers.

#### **SECTION 2.725. STATUTE OF LIMITATIONS IN CONTRACTS FOR SALE.**

**(a) Except as otherwise provided in this section, an action for breach of any contract for sale must be commenced within the later of four years after the right of action has accrued under subsection (b) or (c) or one year after the breach was or should have been discovered, but no longer than five years after the right of action accrued. By the original agreement the parties may reduce the period of limitation to not less than one year but may not extend it; however, in a consumer contract, the period of limitation may not be reduced.**

**(b) Except as otherwise provided in subsection (c), the following rules apply:**

**(1) Except as otherwise provided in this subsection, a right of action for breach of a contract accrues when the breach occurs, even if the aggrieved party did not have knowledge of the breach.**

**(2) For breach of a contract by repudiation, a right of action accrues at the earlier of when the aggrieved party elects to treat the repudiation as a breach or when a commercially reasonable time for awaiting performance has expired.**

**(3) For breach of a remedial promise, a right of action accrues when the remedial promise is not performed when performance is due.**

**(4) In an action by a buyer against a person that is answerable over to the buyer for a claim asserted against the buyer, the buyer's right of action against the person answerable over accrues at the time the claim was originally asserted against the buyer.**

**(c) If a breach of a warranty arising under Section 2.312, 2.313(b), 2.314, or 2.315, or a breach of an obligation, other than a remedial promise, arising under Section 2.313A or 2.313B, is claimed the following rules apply:**

**(1) Except as otherwise provided in paragraph (3), a right of action for breach of a warranty arising under Section 2.312(b), 2.314 or 2.315 accrues when the seller has tendered delivery to the immediate**

buyer, as defined in Section 2.313, and has completed performance of any agreed installation or assembly of the goods.

(2) Except as otherwise provided in paragraph (3), a right of action for breach of an obligation, other than a remedial promise, arising under Section 2.313A or 2.313B accrues when the remote purchaser, as defined in Sections 2.313A and 2.313B, receives the goods.

(3) Where a warranty arising under Section 2.313(b) or an obligation, other than a remedial promise, arising under Section 2.313A or 2.313B explicitly extends to future performance of the goods and discovery of the breach must await the time for performance the right of action accrues when the immediate buyer as defined in Section 2.313 or the remote purchase as defined in Sections 2.313A and 2.313B discovers or should have discovered the breach.

(4) A right of action for breach of warranty arising under Section 2.312 accrues when the aggrieved party discovers or should have discovered the breach. However, an action for breach of the warranty of non-infringement may not be commenced more than six years after tender of delivery of the goods to the aggrieved party.

(d) Where an action commenced within the time limited by subsection (a) is so terminated as to leave available a remedy by another action for the same breach such other action may be commenced after the expiration of the time limited and within six months after the termination of the first action unless the termination resulted from voluntary discontinuance or from dismissal for failure or neglect to prosecute.

(e) This section does not alter the law on tolling of the statute of limitations nor does it apply to causes of action which have accrued before this Act becomes effective.

#### **State Bar Committee Recommendation**

**The Committee has recommended that proposed Section 2.313B not be adopted. If that recommendation is followed, the references to Section 2.313B in the proposed amendments to Section 2.725 should be deleted.**

This section has been substantially rewritten to include major substantive changes in the law. The more important changes can be categorized as follows.

First, subsection (a) supplements the four-year limitation period with a discovery rule which permits an action to be brought within one year after the breach was or should have been discovered, but no later than five years after the action would otherwise have accrued.

Second, consumer contracts are excluded from the right to reduce the limitation period by agreement to not less than one year. The period may not be extended by agreement in any contract.

Third, subsection (b) provides new rules for cases of repudiation, for breach of a remedial promise, and for actions where a third party is answerable over. In the latter case, the rule resolves a question that has troubled the courts. The buyer's action against the person answerable over accrues at the time the claim was "originally asserted" against the buyer.

Fourth, subsection (c) provides the rules for breach of an obligation under Sections 2.313A and 2.313B for persons not in privity, for breach of a warranty of title or of quiet enjoyment under Section 2.312, and for breach of a warranty against infringement.

Fifth, except where the obligation explicitly extends to future performance as provided in subsection (c)(3), subsection (c)(1) provides that the limitation period for breach of warranty accrues when tender of delivery has occurred and the seller has completed any agreed installation or assembly of the goods.

These changes are sensible and are designed to clarify numerous problems that have troubled the courts in applying current Section 2.725. The State Bar Committee thus recommends adoption of the proposed amendments.

Respectfully Submitted,