The following constitutes the ruling of the court and has the force and effect therein described.

Signed March 31, 2022

United States Bankruptcy Judge

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF TEXAS
AMARILLO DIVISION

In re:	§	
	§	
WAGGONER CATTLE, LLC, et al.[1]	§	Case No. 18-20126-RLJ-11
	§	Jointly Administered
Debtor.	§	
	§	
LONE STAR STATE BANK OF WEST TEXAS,	§	
	§	
Plaintiff,	§	
	§	
v.	§	Adversary No. 18-02007 (Civil Action No. 2:19-cv-00098-Z)
	§	
RABO AGRIFINANCE, LLC,	§	
	§	
Defendant.	§	
	§	

REPORT AND RECOMMENDATION TO DISTRICT COURT

[1] The Debtors in this jointly administered chapter 11 case are Waggoner Cattle, LLC (18-20126), Circle W of Dimmitt, Inc. (18-20127), Bugtussle Cattle, LLC (18-20128), and Cliff Hanger Cattle, LLC (18-20129).

The District Court, the Honorable Matthew J. Kacsmaryk presiding, issued its order of October 23, 2020 adopting the Report and Recommendation [ECF No. 3] that this court, the bankruptcy court, made to the District Court on defendant Rabo AgriFinance LLC's Motion for Withdrawal of Reference [ECF No. 1].[1]

The District Court thereby ordered that the reference of this case to the bankruptcy court be withdrawn upon certification by the bankruptcy court that the case is ready for trial. ECF No. 7. The order further provided that the bankruptcy court hear all pretrial matters and submit dispositive motions to the District Court with a report and recommendation. Both the plaintiff Lone Star State Bank of West Texas and defendant Rabo filed motions for summary judgment—Lone Star's motion [Bankruptcy ECF No. 260] was filed on September 17, 2021; Rabo's motion [Bankruptcy ECF No. 275] was filed on October 15, 2021.[2] Hearing on the motions was held on December 21, 2021. The causes and defenses addressed by the motions are based on Lone Star's Third Amended Complaint [Bankruptcy ECF No. 240], Rabo's Answer to Plaintiff's Third Amended Complaint [Bankruptcy ECF No. 242], Rabo's First Amended Counterclaim and Jury Demand [Bankruptcy ECF No. 247], and Lone Star's Answer to Defendant Rabo's First Amended Counterclaim [Bankruptcy ECF No. 249].

This court here submits its Memorandum Opinion (Report and Recommendation) on the parties' respective motions for summary judgment.

Respectfully submitted,

/s/ Robert L. Jones

ROBERT L. JONES
U.S. BANKRUPTCY JUDGE

DATED: March 31, 2022

[1] "ECF No." refers to the numbered docket entry on the District Court's docket for Civil Case No. 2:19-cv-00098-Z, unless otherwise stated.
[2] "Bankruptcy ECF No." refers to the numbered docket entry on the bankruptcy court's docket for Adversary No. 18-02007.

This Report and Recommendation shall be entered on the docket by the Bankruptcy Clerk.

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF TEXAS
AMARILLO DIVISION

In re:	§	
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v.	§	Adversary No. 18-02007
	§	(Civil Action No. 2:19-cv-00098-Z)
RABO AGRIFINANCE, LLC,	§	
	§	
Defendant.	§	

MEMORANDUM OPINION
(Report and Recommendation)

[1] The Debtors in this jointly administered chapter 11 case are Waggoner Cattle, LLC (18-20126), Circle W of Dimmitt, Inc. (18-20127), Bugtussle Cattle, LLC (18-20128), and Cliff Hanger Cattle, LLC (18-20129).

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BACKGROUND

This adversary proceeding arises in connection with the jointly administered chapter 11 bankruptcies of debtors Waggoner Cattle, LLC ("**Waggoner Cattle**"), Cliff Hanger Cattle, LLC ("**Cliff Hanger**"), Bugtussle Cattle, LLC ("**Bugtussle**"), and Circle W of Dimmit, Inc. ("**Circle W**") (collectively the "**Waggoner Entities**"). Each of these entities were owned and operated by Quint Waggoner, who also filed bankruptcy under chapter 11 of the Bankruptcy Code. The plaintiff in this case, Lone Star State Bank of West Texas ("**Lone Star**"), and the defendant, Rabo Agrifinance, LLC ("**Rabo**"), are both creditors of the Waggoner Entities. This adversary proceeding concerns the priority of liens held by Lone Star and Rabo against the property of Waggoner Cattle and Cliff Hanger.

The Waggoner Entities' Operations

The Waggoner Entities initially functioned collectively as a Holstein cattle feeding operation. (Holstein cattle will be referred to as "**Holstein Calves**" or "**Holstein Cattle**.") Waggoner Cattle began operations in 2011. It would purchase day-old Holstein Calves from local dairies; the calves were then taken to a calf ranch owned by Bugtussle and operated by Circle W (the "**Calf Ranch**"), where they were fed and raised until they were weaned once they reached 300-350 pounds. At that weight, they were able to be fed-out for slaughter at a feedyard. From 2011 to 2013, the weaned calves were sold-off to third parties that completed the feeding process by placing them in commercial feedyards.

In 2013, Quint Waggoner decided to retain ownership of the Holstein Cattle through slaughter. For this, he started Cliff Hanger. Once Cliff Hanger was created, the weaned Holstein Calves owned by Waggoner Cattle at the Calf Ranch were no longer sold to third parties, but instead were sold to Cliff Hanger. Cliff Hanger placed the calves in third-party feedyards,

retaining ownership until slaughter. Cliff Hanger then sold its product to packers for further marketing and collected the proceeds from its sales.

In response to the declining market for "fed" Holstein Calves, Quint Waggoner decided to diversify his operations by also raising beef calves. Sometime around June 2015, Cliff Hanger began purchasing under-300-pound beef calves and placing them at the Calf Ranch with the Holstein Calves. But unlike the Holstein Calves, once the beef calves were weaned, they were placed for seven months in pastures owned by either Bugtussle or other, unaffiliated parties and were cared for by Circle W. Some cattle were sold to third parties directly from the pastures (the "**Pasture Cattle**"). Others were raised on pasture until they were feeder-cattle weight—750-900 pounds—at which point they remained under Cliff Hanger's ownership and were taken to a feedyard with the Holstein Cattle until slaughter (the "**Beef Cattle**").

The Tyler-and-Tucker Cattle

Beginning in 2014, Quint Waggoner began to "sell" some of Waggoner Cattle's Holstein Calves to his sons, Tyler and Tucker Waggoner (the "**Tyler-and-Tucker Cattle**"). (Lone Star contends that these sales were fraudulent, sham transactions but assumes for the purposes of this motion that the sales were legitimate.) When Waggoner Cattle's newly purchased Holstein Calves arrived at the Calf Ranch, Quint Waggoner and his sons would select certain of the calves for sale to Tyler and Tucker and place them in designated lots. Waggoner Cattle would then book a receivable owed by Tyler and Tucker. At Quint Waggoner's direction, Cliff Hanger financed the purchase, feed, and care of the cattle sold to Tyler and Tucker.

The sales of the Tyler-and-Tucker Cattle were directed by Quint Waggoner. Quint Waggoner determined the number of cattle to be purchased by Tyler and Tucker and their price. Once purchased, the Tyler-and-Tucker Cattle were raised alongside other Waggoner Entities'

cattle—they were raised on the Calf Ranch together, shipped to and fed in the feedyards together, and sold and slaughtered together. Once the fed Tyler-and-Tucker Cattle were sold after slaughter, Quint Waggoner directed the disposition of their proceeds back to the Waggoner Entities.

The Loans and Security Agreements

From 2011 to 2016, Lone Star made a series of loans to the Waggoner Entities and was initially their primary lender. Lone Star's debt was secured by all cattle owned by Waggoner Cattle and Cliff Hanger and their proceeds, as well as other items of personal property. Lone Star's security agreements were perfected by financing statements filed on August 3, 2011, and March 18, 2014, respectively. According to Lone Star, as of September 13, 2021, its outstanding liquidated secured debt owed by Waggoner Cattle and Cliff Hanger was $13,387,300.36, with interest accruing at $4,239.5981 per day. Lone Star says it has incurred $3,147,520.11 in attorney's and expert fees, which sum has accrued $1,067,309.14 in interest.

Once Cliff Hanger began operations, it was originally financed by a mix of loans from Lone Star, the feedyards who fed-out the Cliff Hanger cattle, and another bank. In August 2014, Quint Waggoner decided to consolidate the financing of Cliff Hanger's operations. For this, he sought out Rabo. Rabo was interested in financing all the Waggoner Entities' cattle but decided to initially finance only Cliff Hanger's. It intended, however, to eventually refinance Lone Star's loans and thus take-over financing of all the Waggoner Entities' cattle operations if it became more comfortable with Quint Waggoner and his business affairs through the Cliff Hanger financing.

Rabo made an initial loan of $31,362,904.62 to Cliff Hanger on November 26, 2014; part of the loan proceeds was used to pay-off the debt with the feedyards and the other bank. Rabo's

loan to Cliff Hanger was secured by all cattle owned by Waggoner Cattle and Cliff Hanger and their proceeds (and other personal property). Rabo's security interests against the Waggoner-Cattle cattle and Cliff Hanger cattle were perfected on December 3, 2014.

Despite its original intent, Rabo never financed the pay-off of Lone Star's loans to the Waggoner Entities nor became the financier for all the Waggoner Entities' cattle operations.

Here, Rabo asserts it believed that once the Tyler-and-Tucker Cattle were acquired (by Tyler and Tucker) from Waggoner Cattle, such cattle were not, or were no longer, subject to the security interest held by Lone Star—this despite Lone Star holding a lien on all cattle owned by Waggoner Cattle. In January 2016, Tyler and Tucker, at the direction of Quint Waggoner and Rabo, pledged the Tyler-and-Tucker Cattle to Rabo.

The Intercreditor Agreement

Because Lone Star perfected its security interests in the Waggoner Entities' cattle before Rabo perfected its security interests against the same cattle, Lone Star had a superior lien on the Waggoner Entities' cattle. As a condition to its financing Cliff Hanger and to adequately protect its interests, Rabo required a subordination from Lone Star to alter the priority of their security interests so that Rabo had the senior lien on certain collateral. To this end, Rabo, Lone Star, Cliff Hanger, and Waggoner Cattle entered into an intercreditor agreement, effective November 26, 2014 (the "**Intercreditor Agreement**").

The Intercreditor Agreement defines collateral in two separate categories: "**Cliff Hanger Collateral**" and "**Waggoner Collateral**." Waggoner Collateral is defined as "that portion of the Collateral that is located on the Waggoner Calf Ranch, is related to, or arises from or in connection with Waggoner's operations on the Waggoner Calf Ranch." Pl's. Summ. J. Mot. Ex. 3. Cliff Hanger Collateral is defined as "that portion of the Collateral that is located in the Cliff

Hanger Feedyards, is related to, or arises from or in connection with Cliff Hanger's operations in the Cliff Hanger Feedyards." *Id*. The effect of the Intercreditor Agreement is that Lone Star had a first-priority security interest against Waggoner Collateral and Rabo had a first-priority security interest against Cliff Hanger Collateral.

At the time the Intercreditor Agreement was entered into, Cliff Hanger owned approximately 33,387 cattle, which it acquired from Waggoner Cattle. The parties do not dispute that, under the Intercreditor Agreement's definition of Cliff Hanger Collateral, Rabo obtained the senior lien on all those cattle owned by Cliff Hanger at that time. However, after the Intercreditor Agreement was entered into, per the Waggoner Entities' regular operations, Waggoner Cattle continued to sell its cattle to Cliff Hanger, and the parties needed a mechanism to distinguish when the status of those cattle transitioned from Waggoner Collateral to Cliff Hanger Collateral. The Intercreditor Agreement addresses this under the clause stating that "[u]pon delivery of the Collateral to the Cliff Hanger Feedyards and receipt of payment in full by Waggoner, thereafter all Collateral located in the Cliff Hanger Feedyards shall be owned by and in possession of Cliff Hanger and shall be Cliff Hanger Collateral" (the "**Transfer Clause**"). *Id*. The term "payment in full" is not defined by the Intercreditor Agreement.

The parties dispute whether, at the time the Intercreditor Agreement was entered into, the Waggoner Entities were only raising Holstein Calves or whether Quint Waggoner had expanded his business to include beef calves. Regardless, the Intercreditor Agreement does not address any specific type of cattle, whether Holstein or beef. (Holstein cattle are typically raised for the dairy industry.)

The Cattle Financing and Proceeds of Cattle Sales

As the primary lender to Waggoner Cattle, Lone Star financed Waggoner Cattle's purchase of Holstein Calves. As the primary lender to Cliff Hanger, Rabo financed Cliff Hanger's purchase of Pasture Cattle and Beef Cattle, as well as the purchase of Holstein Calves from Waggoner Cattle.

The proceeds of the sales of Cliff Hanger's cattle to packers—including the Holstein Cattle, the Pasture Cattle, and the Beef Cattle—were placed in Cliff Hanger's bank account at Rabobank, N.A. (an entity separate from Rabo). Under an agreement between Rabobank and Cliff Hanger, Rabobank would frequently "sweep" Cliff Hanger's account, taking all funds in the account and transferring them to Rabo who applied the funds to its note with Cliff Hanger. Rabo therefore obtained the majority of proceeds of the Holstein Cattle, the Pasture Cattle, and the Beef Cattle sold by Cliff Hanger. But before sweeps would exhaust Cliff Hanger's account, Cliff Hanger would make payments to Waggoner Cattle for the Holstein Calves it purchased from it. Waggoner Cattle made payments to Lone Star on its note, and proceeds of various sales were thereby funneled to Lone Star.

Rabo's Syndication Efforts

As Rabo's lending relationship with Cliff Hanger progressed, Rabo became concerned that Cliff Hanger would not be able to pay off its loan to Rabo. Rabo began attempts to "syndicate" its loan—that is, to find other lenders to purchase some or all of its loan to Cliff Hanger. To advertise the loan, Rabo would provide potential syndicate partners with the Waggoner Entities' financial information. During this time, Rabo would also occasionally provide Lone Star with Cliff Hanger borrowing base reports, which estimated the value of Rabo's collateral owned by Cliff Hanger. Lone Star now asserts that the Cliff Hanger borrowing

base reports and financial information provided to Lone Star and potential syndicate partners were purposely falsified to obtain syndication and induce Lone Star to continue funding the Waggoner Entities despite their shaky financial condition.

Waggoner Entities File Bankruptcy and Lone Star Sues Rabo

On April 9, 2018, the Waggoner Entities filed for bankruptcy under chapter 11 of the Bankruptcy Code. The Waggoner Entities now operate under the terms of a confirmed chapter 11 plan.[1] On June 29, 2018, Lone Star filed its complaint in the present suit against Rabo. After a series of amendments, on December 22, 2020, Lone Star filed its third amended complaint, which is Lone Star's live pleading. Lone Star claims that Rabo received the sales proceeds of the Cliff Hanger cattle upon which Lone Star had a senior lien and that its lien was not subordinated under the terms of the Intercreditor Agreement. By this suit, Lone Star seeks to recover those sales proceeds from Rabo. Lone Star argues that the Intercreditor Agreement only subordinated Lone Star's senior lien over Holstein Cattle transferred to Cliff Hanger and for which Waggoner Cattle received "payment in full." It says that the Intercreditor Agreement does not apply to the Pasture Cattle, Beef Cattle, or the Tyler-and-Tucker Cattle.

On February 23, 2021, Rabo filed its answer to Lone Star's first amended complaint and, on March 22, 2021, filed its first amended counterclaim, which pleadings are Rabo's presently live pleadings. Rabo asserts that the Intercreditor Agreement applies to Holstein Calves, Pasture Cattle, and Beef Cattle and denies that it collected any cattle proceeds from Cliff Hanger that were not subject to liens subordinated under the terms of the Intercreditor Agreement. It additionally argues that, under the terms of the Intercreditor Agreement, Cliff Hanger overpaid

[1] The Waggoner Entities' consolidated plan was confirmed by the Court on August 5, 2019.

Waggoner Cattle for certain cattle using Rabo's collateral. It now seeks to recover the value of that collateral from Lone Star.

Lone Star and Rabo Move for Summary Judgment

Both Lone Star and Rabo move for summary judgment. They both request summary judgment, as declaratory relief, on their respective constructions of the Intercreditor Agreement. Lone Star also seeks summary judgment on its causes of action for conversion and attorney's fees and costs, and on Rabo's causes of action for fraud by non-disclosure, breach of the Intercreditor Agreement, unjust enrichment, and conversion. Rabo also seeks summary judgment on Lone Star's causes of action for conversion, attorney's fees and costs, and fraud.

DISCUSSION

I. Standard for Summary Judgment

"The court shall grant summary judgment if the movant shows that there is no genuine dispute as to any material fact and the movant is entitled to judgment as a matter of law." Fed. R. Civ. P. 56(a).[2] "A fact issue is material if its resolution could affect the outcome of the action." *Peel & Co. v. Rug Mkt.*, 238 F.3d 391, 394 (5th Cir. 2001). The movant bears the initial burden of identifying portions of the pleadings and discovery that demonstrate the absence of a genuine issue of material fact. *Celotex Corp. v. Catrett*, 477 U.S. 317, 323 (1986). "If the movant does meet its burden, the nonmovant must go beyond the pleadings and designate specific facts showing that a genuine issue of material fact exists for trial." *Roberson v. Game Stop, Inc.*, 395 F. Supp. 2d 463, 468 (N. D. Tex. 2005), *aff'd*, 152 F. App'x 356 (5th Cir. 2005).

"[T]he court must review all of the evidence in the record, but make no credibility determinations or weigh any evidence." *Peel & Co.*, 238 F.3d at 394. The facts and inferences

[2] Rule 7056 of the Federal Rules of Bankruptcy Procedure makes Rule 56 of the Federal Rules of Civil Procedure applicable in bankruptcy proceedings.

to be drawn from the evidence must be viewed in the light most favorable to the nonmoving party. *Id*.

II. Lone Star's Senior Lien

Lone Star perfected a security interest in all cattle owned by Waggoner Cattle and Cliff Hanger before Rabo perfected its security interest in the same cattle. Pl's. Summ. J. Mot. Ex. 14 (Lone Star credit agreements); Ex. 13 (Lone Star UCC financing statements); Def.'s Summ. J. Mot. Exs. 1–4 (Rabo credit agreements); Ex. 10 (Rabo UCC financing statements). While Rabo disputes this claim, it has presented no evidence to contradict the proof presented by Lone Star. "Conflicting perfected security interests and agricultural liens rank according to priority in time of filing or perfection." TEX. BUS. & COM. CODE § 9.322(a)(1). Therefore, because Lone Star perfected its security interests first, Lone Star held the senior lien on all Waggoner Entities' cattle. Lone Star's senior lien was subordinated only if the terms of the Intercreditor Agreement so dictated. Lone Star's lien over the Waggoner Entities' cattle also attached to the identifiable proceeds of the cattle after they were sold by Cliff Hanger. TEX. BUS. & COM. CODE § 9.315(a)(2).

By its counterclaim, Rabo contends that, despite Lone Star's first-in-time lien over the Waggoner Entities' cattle, it (Rabo) held a senior lien over certain cattle as holder of a purchase money security interest ("**PMSI**").

> A purchase money security interest is a security interest … taken in the goods or software by a lender who advances funds to the debtor to pay for the collateral … . An important feature of purchase money security interests is that they are accorded a priority status superior to that of other secured parties who have ordinary security interests in the same goods. If the goods are … livestock, the purchase money secured party must give notice to other secured parties of record that the purchase money party intends to take a purchase money security interest in described inventory. The notice must be given and the purchase money security interest must be perfected before the debtor receives possession of the inventory.

Purchase Money Priorities, 12 TEX. PRAC., TEXAS METHODS OF PRACTICE § 34:23 (3d ed.) (citing TEX. BUS. & COM. CODE ANN. § 9.324(b)–(e)). "[A] secured party claiming a purchase-money security interest has the burden of establishing the extent to which the security interest is a purchase-money security interest." TEX. BUS. & COM. CODE ANN. § 9.103(g).

On summary judgment, Rabo has essentially abandoned its PMSI claim. It has presented no evidence proving that its loans to Cliff Hanger were used directly by Cliff Hanger to purchase cattle. It also has failed to prove that it provided notice to Lone Star that it intended to take a PMSI before Cliff Hanger purchased any cattle, as required by the Texas UCC. *See* TEX. BUS. & COM. CODE ANN. § 9.324(d). Rabo says that the Intercreditor Agreement constituted sufficient notice, but the Intercreditor Agreement says nothing about a PMSI nor does it describe any cattle which Cliff Hanger would purchase from third parties—the only cattle Rabo claims a PMSI over. Rather, the Intercreditor Agreement exclusively addresses cattle that Cliff Hanger purchased from Waggoner Cattle. Therefore, even if Rabo could muster colorable evidence that its loans were used directly to purchase certain cattle, it cannot prove that, through the Intercreditor Agreement, it provided Lone Star adequate notice under TEX. BUS. & COM. CODE ANN. § 9.324(d). The undisputed facts therefore show that Rabo did not obtain a PMSI over any of the Waggoner Entities' cattle. Summary judgment should be granted to Lone Star holding that before the creation of the Intercreditor Agreement, Lone Star had the senior lien on all the Waggoner Entities' cattle and that Rabo thereafter never obtained a PMSI over any of the Waggoner Entities' cattle.

III. Construction of the Intercreditor Agreement

Lone Star says that Rabo converted millions of dollars of proceeds of Lone Star's collateral. Lone Star argues that its first-in-time lien over thousands of head of cattle that were

acquired by Cliff Hanger, either from Waggoner Cattle or third parties, was not subordinated to Rabo's second-in-time lien under the terms of the Intercreditor Agreement. Lone Star contends that it retained its senior lien on the proceeds of the sale of these cattle and, when Rabo accepted these proceeds, it committed conversion. The parties dispute the meaning of the Intercreditor Agreement; determining its effect is critical in deciding which party had the senior lien over the cattle and the cattle proceeds collected by Rabo. Specifically, Lone Star and Rabo disagree on the interpretation of the definition of Cliff Hanger Collateral, the interpretation of the phrase "payment in full," and the scope of the Transfer Clause.

A. Provisions of the Intercreditor Agreement

Paragraph E of the "Recitals" section of the Intercreditor Agreement states the purpose of the contract—"The Creditors desire to enter this Agreement in order to set forth the relative priorities of the liens and security interests securing the Indebtedness [of Waggoner Cattle and Cliff Hanger]." Pl's. Summ. J. Mot. Ex. 3. Paragraph 1 under the "Agreement" section of the Intercreditor Agreement provides certain definitions. "Collateral" is defined as "any and all personal property of Waggoner or Cliff Hanger which is subject to a perfected security interest or lien in favor of any one or more of the Creditors to secure all or any portion of the Indebtedness." *Id*. "Waggoner Collateral" is defined as "that portion of the Collateral that is located on the Waggoner Calf Ranch, is related to, or arises from or in connection with Waggoner's operations on the Waggoner Calf Ranch." *Id*. "Cliff Hanger Collateral" is defined as that portion of the Collateral that is located in the Cliff Hanger Feedyards, is related to, or arises from or in connection with Cliff Hanger's operations in the Cliff Hanger Feedyards." *Id*.

Paragraph 2 under the Agreement section of the Intercreditor Agreement addresses the priority of security interests in the Collateral. Paragraph 2(a) states:

> Any Lone Star security interest in, or lien or encumbrance on, or claim to Cliff Hanger Collateral including proceeds thereof or rights relating thereto shall be junior in priority to the security interest in, lien, encumbrance on, claims or rights of [Rabo] to the Cliff Hanger Collateral. **Upon delivery of the Collateral to the Cliff Hanger Feedyards and receipt of payment in full by Waggoner, thereafter all Collateral located in the Cliff Hanger Feedyards shall be owned by and in possession of Cliff Hanger and shall be Cliff Hanger Collateral**.

Id. (emphasis added for the Transfer Clause).

Paragraph 2(b) states:

> Any [Rabo] security interest in, or lien or encumbrance on, or claim to Waggoner Collateral including proceeds thereof or rights relating thereto shall be junior in priority to the security interest in, lien, encumbrance on, claims or rights of Lone Star to the Waggoner Collateral.

Id.

B. Principles of Contract Interpretation

The interpretation of a contract is normally a question of law, but if the interpretation depends on certain disputed facts, the interpretation becomes a factual matter unresolvable by a court at summary judgment. *Breck Const. Co. v. Air Liquide Am. Corp.*, 281 F.3d 1278, 2001 WL 1692426, at *3 (5th Cir. Nov. 21, 2001). If the meaning of a contract is ambiguous, then the interpretation of the contract is a factual matter, and summary judgment is inappropriate. *Fireman's Fund Ins. Co. v. Murchison*, 937 F.2d 204, 207 (5th Cir. 1991). A contract is not ambiguous if it is worded in a manner that reveals a definite or certain legal meaning. *Gonzalez v. Denning*, 394 F.3d 388, 392 (5th Cir. 2004). Grammatical errors in a contract do not necessarily render it ambiguous. *Golden Spread Coop., Inc. v. Emerson Process Mgmt. Power & Water Sols., Inc.*, 360 F. Supp. 3d 494, 510 n.12 (N.D. Tex. 2019), *aff'd*, 954 F.3d 804 (5th Cir. 2020).

When interpreting a contract, courts "must ascertain and give effect to the parties' intentions as expressed in the writing itself." *El Paso Field Servs., L.P. v. MasTec N. Am., Inc.*,

389 S.W.3d 802, 805 (Tex. 2012). To discern the parties' intent, courts must "give effect to all the provisions of [a] contract so that none will be rendered meaningless." *Id*. (quoting *Italian Cowboy Partners, Ltd. v. Prudential Ins. Co. of Am.*, 341 S.W.3d 323, 333 (Tex. 2011)). "Even if different parts of [a contract] appear contradictory or inconsistent, the court must strive to harmonize all of the parts, construing the instrument to give effect to all of its provisions." *Luckel v. White*, 819 S.W.2d 459, 462 (Tex. 1991). Courts should avoid, when possible, "unreasonable, inequitable, or oppressive" constructions, or those that "would lead to an absurd result." *Pavecon, Inc. v. R-Com, Inc.*, 159 S.W.3d 219, 222 (Tex. App.—Fort Worth 2005, no pet.).

Courts should give words in a contract "their common and generally accepted meanings unless the contract specifies its own meanings." 17A Am. Jur. 2d *Contracts* § 349 (2021). Courts may "consider[] extrinsic evidence of the facts and circumstances surrounding the contract's execution as 'an aid in the construction of the contract's language.'" *URI, Inc. v. Kleberg Cnty.*, 543 S.W.3d 755, 765 (Tex. 2018) (quoting *Sun Oil Co. (Del.) v. Madeley*, 626 S.W.2d 726, 731 (Tex. 1981)). But evidence of surrounding circumstances "may only 'give the words of a contract a meaning consistent with that to which they are reasonably susceptible, i.e., to 'interpret' contractual terms.'" *Id*. (quoting *Nat'l Union Fire Ins. Co. of Pittsburgh, PA v. CBI Indus., Inc.*, 907 S.W.2d 517, 521 (Tex. 1995)).

C. Definition of Cliff Hanger Collateral

The parties disagree on how to interpret the definition of Cliff Hanger Collateral under the Intercreditor Agreement. Since Rabo is granted a first lien on Cliff Hanger Collateral under the Intercreditor Agreement, the construction of this definition is essential to Lone Star's conversion claim—its claim that is based on the contention that Lone Star, not Rabo, had the first

lien over cattle that arguably fall within the definition of Cliff Hanger Collateral. Both parties believe the definition is unambiguous but reach starkly differing constructions.

1. Lone Star's Interpretation

Lone Star concludes that only Holstein Cattle meet the definition of Cliff Hanger Collateral and comes to this conclusion through two primary arguments.

First, Lone Star argues that the terms "operations" and "feedyards" used in the definition must exclusively apply to the operations and feedyards used by the Waggoner Entities at the time the Intercreditor Agreement was entered into. It relies on the interpretive principle that, "[u]nder Texas law, … a contract is viewed as of the time it was made and not in light of subsequent events." *Texas v. Am. Tobacco Co.*, 463 F.3d 399, 407 (5th Cir. 2006) (citing *Ervay, Inc. v. Wood*, 373 S.W.2d 380, 384 (Tex. Civ. App.—Dallas 1963, writ ref'd n.r.e.)). Since the only "operation" in existence and known to the parties at the time the Intercreditor Agreement was drafted was the Holstein Cattle operation, Lone Star argues the term "operation" as used in the definitions of "Waggoner Collateral" and "Cliff Hanger Collateral" must relate to the Holstein operation exclusively, not to the Beef Cattle and Pasture Cattle operations. It also argues that only the feedyards used at the time the Intercreditor Agreement was drafted inform the meaning of the term "feedyard"—the pastures used in the Beef Cattle and Pasture Cattle operations are thus excluded from the term.

Second, Lone Star argues that there is a missing conjunction—either "and" or "or"—between the locational and relational conditions of the definition. It contends the definition must be read: "'Cliff Hanger Collateral' means that portion of the Collateral that is located in the Cliff Hanger Feedyards, **[AND/OR]** is related to, or arises from or in connection with Cliff Hanger's

operations in the Cliff Hanger Feedyards." Lone Star concludes that the definition can only reasonably be read with an "and," not an "or."

Without an "and," the locational condition would be rendered meaningless, Lone Star contends. It points out that Cliff Hanger owned beef cattle that were placed on the Calf Ranch. If the definitions were read with an "or," those cattle would simultaneously meet the definition of both Cliff Hanger Collateral and Waggoner Collateral. They would meet the Cliff Hanger Collateral definition because they meet its relational requirement (being owned by Cliff Hanger), and they would meet the Waggoner Collateral definition because they meet its locational requirement (the Calf Ranch). Such a construction is unworkable—effectively granting duplicative first-liens against the same cattle is not only legally impossible but is patently contrary to the Intercreditor Agreement's purpose of setting relative lien priorities between the parties. Therefore, Lone Star argues, the only reasonable construction of the definitions is to read-in "and" as the missing conjunction so that cattle must meet the locational and relational requirements of each definition to qualify under the definition. Based on this interpretation, the Pasture Cattle could not meet the definition of Cliff Hanger Collateral because they never met the locational requirement of the definition as they were sold from pasture before ever reaching a feedyard.

2. Rabo's Interpretation

Rabo argues that the definition of Cliff Hanger Collateral is not limited to only Holsteins—the Intercreditor Agreement makes no mention of *Holstein* Cattle. Rabo disregards the missing conjunction question and submits that the Court need not read into the contract either "and" or "or." Rather, Rabo argues that the definition of Cliff Hanger Collateral is met based on whether Cliff Hanger purchased the cattle in question. If so, then the cattle are "related to …

Cliff Hanger's operations" and are Cliff Hanger Collateral. While not explicitly stating so, by arguing the locational requirement is unnecessary, Rabo effectively reads an "or" into the definition.

Rabo also relies on the principle of interpretation that courts, "[w]hen possible, [should] avoid a construction that is unreasonable, inequitable, or oppressive, or would lead to an absurd result." *Pavecon, Inc. v. R-Com, Inc.*, 159 S.W.3d 219, 222 (Tex. App.—Fort Worth 2005, no pet.). Rabo says that limiting the definition of Cliff Hanger Collateral to only the Holstein operation or to only those cattle that meet both the relational and locational requirements in the definition would be unjust and absurd; it would result in cattle financed by Rabo—Beef Cattle and Pasture Cattle—falling outside the purview of the Intercreditor Agreement and thus subject to Lone Star's first lien. Rabo asserts the parties could have never intended such an inequitable result.

3. Court's Construction of Definition

The purpose of the Intercreditor Agreement was to "set forth the relative priorities of the liens and security interests" securing the collective indebtedness owed by Waggoner Cattle and Cliff Hanger to Lone Star and Rabo. Pl's. Summ. J. Mot. Ex. 3 ¶ E. The Intercreditor Agreement identifies the "Collateral" as *all personal property* that Waggoner Cattle and Cliff Hanger pledged to secure the loans made by Lone Star and by Rabo. *Id*. at 2. While this suit concerns the alleged conversion of cattle, the coverage of the Intercreditor Agreement is not limited to just cattle—it concerns "all personal property"—much less any type of cattle.

Lone Star had the first-in-time lien against the cattle. By the Intercreditor Agreement, Lone Star subordinated its first-lien position to Rabo's liens against a part of the Collateral—the

so-defined Cliff Hanger Collateral. This was necessary to ensure Rabo was adequately secured for its substantial loan to Cliff Hanger.

The definitions of Waggoner Collateral and Cliff Hanger Collateral each contain two conditions for identifying what portion of the cattle would serve as the primary security for each creditor. The first condition is locational—on the Waggoner Calf Ranch or in the Cliff Hanger Feedyards; the second condition is relational—"is related to, or arises from or in connection with" either Waggoner Cattle's or Cliff Hanger's cattle operations. Neither definition contains the conjunction "and" or "or."

First, a conjunction is not necessary to the definition. Read this way, both the locational and relational conditions of each definition must be met. Satisfying only the first condition is not helpful because it concerns "the Collateral," which means all collateral that secures both Lone Star and Rabo and thus may include cattle owned by both debtors and financed by both lenders. But also requiring that the relational condition be met allows the parties to identify, for example, the cattle at the Cliff Hanger Feedyards that were acquired by Cliff Hanger with Rabo's financing. The same construction applies to identifying the cattle that primarily secure Lone Star—the cattle owned by Waggoner Cattle that were financed by Lone Star and placed on the Waggoner Calf Ranch in conjunction with Waggoner Cattle's operations.

The Recitals of the Intercreditor Agreement, in describing the loans of Lone Star and Rabo, underscore the importance of both conditions: Lone Star's "credit facilities . . . used by Waggoner [Cattle] to finance . . . Waggoner [Cattle's] cattle operations located on . . . premises specifically owned and operated by Waggoner [Cattle]"; and Rabo's "credit facilities . . . used by Cliff Hanger to finance Cliff Hanger's cattle operations including the feeding and caring of . . . its cattle in certain feedyards" that were then named and identified as the Cliff Hanger

Feedyards. *Id*. ¶¶ A, B. Both conditions must be met. This is consistent with there being no conjunction in either definition. It is not necessary—in effect, it is the same as if "and" were the conjunction.

Reading out the locational condition, as Rabo suggests, would be unreasonable. The Court must "give effect to all the provisions of [a] contract so that none will be rendered meaningless." *Italian Cowboy Partners, Ltd. v. Prudential Ins. Co. of Am.*, 341 S.W.3d 323, 333 (Tex. 2011). Excluding the locational condition in the definition would impermissibly render express language in the Intercreditor Agreement meaningless.

Alternatively, including an "or" in the definitions would likewise be unreasonable. Many of the Pasture Cattle and Beef Cattle owned by Cliff Hanger were placed at the Calf Ranch before reaching a certain weight. At this stage, they simultaneously met the locational condition of the Waggoner Collateral definition and the relational condition of the Cliff Hanger Collateral definition. Thus, if only one condition from each definition was necessary to meet the definition's requirements, then certain cattle could simultaneously fall under both definitions, creating the impossible situation of both parties obtaining a "senior" lien on the same cattle. Including an "or" in the definitions is therefore unreasonable.

Construing the Intercreditor Agreement to cover only Holstein Cattle, as Lone Star argues, is contrary to the clear wording of the agreement. It applies to all personal property and thus all cattle regardless the type. And identifying the cattle by which party financed their purchase—Lone Star or Rabo—as Rabo contends, is similarly imposing a phantom condition. The definition of Cliff Hanger Collateral is unambiguous, having only one reasonable interpretation—all cattle, whether Holstein or other, are subject to that definition if they meet both the locational and relational conditions.

Not to be lost in the above analysis is that the Intercreditor Agreement adds one clarification for Lone Star's subordination of its liens to that of Rabo's against the Cliff Hanger Collateral: that upon delivery of cattle "to the Cliff Hanger Feedyards and receipt of payment in full by Waggoner [Cattle], thereafter all Collateral located in the Cliff Hanger Feedyards shall be owned by and in possession of Cliff Hanger and shall be Cliff Hanger Collateral." Pl's. Summ. J. Mot. Ex. 3 ¶ 2(a). In addition to their disagreement over the definition of Cliff Hanger Collateral, the parties contest the scope of this phrase and the meaning of its terms.

D. The Transfer Clause—"Delivery" and "Payment in Full"

The Transfer Clause states, "Upon delivery of the Collateral to the Cliff Hanger Feedyards and receipt of payment in full by Waggoner, thereafter all Collateral located in the Cliff Hanger Feedyards shall be owned by and in possession of Cliff Hanger and shall be Cliff Hanger Collateral." *Id*. The parties agree that, under this provision, both delivery and receipt of payment in full was necessary for the subordination of Lone Star's lien against Holstein Cattle. Lone Star additionally argues that these requirements are necessary conditions for Lone Star's lien against *any* cattle to be subordinated, including Beef Cattle and Pasture Cattle purchased by Cliff Hanger from third-parties with Rabo's financing. Rabo argues that the provisions of these Transfer Clause are limited to cattle sold by Waggoner Cattle to Cliff Hanger.

1. Necessity of Delivery and Payment

The text of the Intercreditor Agreement and the circumstances surrounding its formation make clear that the Transfer Clause's additional requirements for lien subordination only apply to cattle sold from Waggoner Cattle to Cliff Hanger, *not* to cattle purchased by Cliff Hanger from third parties. At the time the Intercreditor Agreement was entered into, the Waggoner Entities' complicated operations included selling Holstein Calves from Waggoner Cattle to Cliff

Hanger. Without the Transfer Clause, and under the Intercreditor Agreement's definition of "Cliff Hanger Collateral," Lone Star's lien over these cattle would be subordinated once Cliff Hanger took possession of the transferred calves and placed them in feedyards, even if Cliff Hanger made no payment to Waggoner Cattle. Such result would be patently inequitable, as Lone Star would lose its senior lien position without ever being paid. The Transfer Clause prevents this inequity by including important requirements that Cliff Hanger must satisfy before Lone Star's first lien against the transferred cattle is subordinated: "delivery" and "payment in full."

2. Expansion of Waggoner Entities' Operations

The Waggoner Entities' operations expanded to include Beef Cattle and Pasture Cattle. These cattle were purchased by Cliff Hanger from third parties—not Waggoner Cattle—and their purchase was funded by Rabo's loan. As discussed above, the definition of "Cliff Hanger Collateral" readily determines whether these cattle are the collateral of Lone Star or Rabo. But adding the additional requirements of "delivery" and "payment in full" to these cattle to determine lien priority would make no sense. Of course, Waggoner Cattle cannot receive "payment in full" for these cattle as it is not the seller of the cattle. It would be economically absurd for Cliff Hanger to pay Waggoner Cattle for cattle it already purchased from third parties using Rabo-loan funds. Lone Star and Waggoner Cattle would realize an undeserved windfall payment for cattle neither owned by Waggoner Cattle nor financed by Lone Star.

Levying the requirements of "delivery" and "payment in full" on cattle not purchased from Waggoner Cattle also nullifies the definition of "Cliff Hanger Collateral." By requiring "delivery" and that cattle "be located in the Cliff Hanger Feedyards," the Transfer Clause subsumes the relational and locational requirements of "Cliff Hanger Collateral." But for cattle

sold from Waggoner Cattle to Cliff Hanger, the requirement of "payment in full" is added. Imposing the requirement of "payment in full" on *all* cattle would mean the Transfer Clause subsumes the definition of "Cliff Hanger Collateral" at all times. A court "must examine and consider the entire [contract] in an effort to harmonize and give effect to all the provisions of the contract so that none will be rendered meaningless." *Italian Cowboy Partners*, 341 S.W.3d at 333. The only way the definition of "Cliff Hanger Collateral" has any purpose or meaning is if the Transfer Clause only applies to a subset of cattle—those sold from Waggoner Cattle to Cliff Hanger. Holding it applies to *all* cattle impermissibly renders the definition of "Cliff Hanger Collateral" meaningless.

The only interpretation of the Transfer Clause that sensibly applies to the Waggoner Entities' operations and avoids rendering the definition of "Cliff Hanger Collateral" meaningless is that the Transfer Clause applies only to cattle transferred from Waggoner Cattle to Cliff Hanger. The Court concludes that, going forward under the Intercreditor Agreement, the requirements of "delivery" and "payment in full" apply to cattle transferred from Waggoner Cattle to Cliff Hanger; these requirements do not apply to the Beef Cattle and the Pasture Cattle; and only the definitions of "Waggoner Collateral" and "Cliff Hanger Collateral" contained in the Intercreditor Agreement determine the lien priority of the Beef Cattle and the Pasture Cattle, which were purchased by Cliff Hanger from third parties.

E. Meaning of "Payment in Full"

Even concluding that the Transfer Clause only applies to Holstein Cattle, the meaning of the phrase "payment in full" within that clause is still disputed by the parties—Rabo argues that the phrase unambiguously refers to a set price, while Lone Star contends the phrase is ambiguous and cannot be interpretated on summary judgment. Determination of this price is critical to Lone

Star's claims for conversion and breach of the Intercreditor Agreement and Rabo's claims for conversion, unjust enrichment, and breach of the Intercreditor Agreement as each of these claims rests on the contention that Cliff Hanger either underpaid or overpaid Waggoner Cattle for transferred cattle under the meaning of "payment in full."

1. Incorporation of Credit Agreement

Rabo argues that "payment in full" is defined in the credit agreement entered into between Cliff Hanger and Rabo in October 2014 ("October Credit Agreement"), which Rabo says was incorporated into the Intercreditor Agreement. Through the October Credit Agreement, Rabo argues, the Intercreditor Agreement's plain terms define "payment in full." The October Credit Agreement states, "The transfer-price that Cliff Hanger Cattle, LLC is to purchase 300 pound Holstein calves from Waggoner Cattle, LLC shall be equal to 75% of the average price reported for 300 pound Holstein calves from the most recent sale at Overland Stockyard in Hanford, CA, as determined by and acceptable to Lender."[3] Def's. Summ. J. Mot. Ex. 14 ¶ 6.11.

Documents may be incorporated into a signed contract if the contract plainly refers to the document. *Bob Montgomery Chevrolet, Inc. v. Dent Zone Cos.*, 409 S.W.3d 181, 189 (Tex. App.—Dallas 2013, no pet.). "Plainly referring to a document requires more than merely mentioning the document. The language in the signed document must show the parties intended for the other document to become part of the agreement." *Id*. (citations omitted). It must be clear through the language of the contract that "the parties to the agreement had knowledge of and assented to the incorporated terms." *Id*. (quoting 17A C.J.S. *Contracts* § 402 (2011)).

The Intercreditor Agreement states in Paragraph (B) of the "Recitals":

> [Cliff Hanger] together with other named Borrowers and [Rabo] have entered into a Credit Agreement dated of even date herewith (the "*Cliff Hanger Credit*

[3] The "average price reported for 300 pound Holstein calves from the most recent sale at Overland Stockyard in Hanford, CA" will hereinafter be referred to as the "**Overland Auction Price**."

> *Agreement*"), under which certain credit facilities and other accommodations have been extended to Cliff Hanger … , which will be used by Cliff Hanger to finance Cliff Hanger's cattle operations.

Pl's. Summ. J. Mot. Ex. 3 (emphasis in original). While the Intercreditor Agreement thus mentions the October Credit Agreement, there is no surrounding language that would indicate the parties intended for the terms of the October Credit Agreement to become terms of the Intercreditor Agreement. The Intercreditor Agreement nowhere mentions any terms of the October Credit Agreement, nor does it indicate what function the October Credit Agreement might serve to the Intercreditor Agreement. "Instead, this language indicates that the [October Credit Agreement] contained informative material only, not binding terms and conditions intended to be part of the parties' contract." *Bob Montgomery Chevrolet*, 409 S.W.3d at 190.

The fact that the language mentioning the October Credit Agreement is in the "Recitals" is also significant. "Recitals in a contract are not strictly part of the contract … . A 'recital' is '[a] preliminary statement in a contract or deed explaining the reasons for entering into it or the background of the transaction, showing the existence of particular facts.'" *Furmanite Worldwide, Inc. v. NextCorp, Ltd.*, 339 S.W.3d 326, 336 (Tex. App.—Dallas 2011, no pet.) (alteration in original) (quoting BLACK'S LAW DICTIONARY 1289 (8th ed. 2004)). Therefore, the fact that the October Credit Agreement was mentioned in the "Recitals" indicates that it was never intended to be part of the Intercreditor Agreement. Rather, it was intended to provide background information explaining why the parties needed the Intercreditor Agreement's terms.

Also critical, "[r]ecitals in a contract do not control the operative clauses of the contract unless the latter are ambiguous." *Country Cmty. Timberlake Vill., L.P. v. HMW Special Util. Dist. of Harris*, 438 S.W.3d 661, 669 (Tex. App.—Houston [1st Dist.] 2014, pet. denied). Thus, the Court could not possibly hold on summary judgment that the October Credit Agreement

informs the definition of "payment in full"—if that phrase is ambiguous, the Court cannot interpret it on summary judgment, and if it is unambiguous, then the Court cannot use the October Credit Agreement, contained in the "Recitals," to control the phrase's meaning. The October Credit Agreement simply was not incorporated into the Intercreditor Agreement and has no bearing on the phrase "payment in full."

Even if the October Credit Agreement was incorporated, it still does not define payment in full. The Agreement merely refers to a "transfer-price" but nowhere uses the language "payment in full." It is entirely possible that these two phrases have different meanings and serve different purposes, and there is nothing in either the October Credit Agreement or the Intercreditor Agreement that indicates the terms "transfer-price" and "payment in full" are synonymous. For these reasons, the Court finds that the October Credit Agreement does not inform the Court of the meaning of "payment in full."

2. Payment Due According to Quint Waggoner

Additionally, Rabo says that the buyer and seller of the Holstein Calves (both being Quint Waggoner) also agreed that "payment in full" for Holstein Calves was 75% of the Overland Auction Price. As an alternative to its argument that the incorporation of the October Credit Agreement determines the meaning of "payment in full," Rabo argues that the phrase unambiguously refers to whatever payment was due. Therefore, Quint Waggoner's understanding of what price was due to Waggoner Cattle from Cliff Hanger for the Holstein Calves controls the meaning of "payment in full." Even assuming that "payment in full" means whatever payment was due according to Quint Waggoner (which Lone Star rejects, asserting "payment in full" is a reasonable price per TEX. BUS. & COM. CODE § 2.305), there is a genuine

dispute of material fact as to what Quint Waggoner, or his lenders for that matter, believed was due payment for the Holstein Calves.

Quint Waggoner and DeNise Merritt, accountant for the Waggoner Entities, both testified in their depositions that they believed Cliff Hanger was to pay 75% of the Overland Auction Price for Waggoner Cattle Holsteins. Def's. Summ. J. Mot. Exs. 18, 19. But Lone Star has presented evidence which shows that Quint Waggoner and his lenders actually believed that the full payment due was fair market value; although Cliff Hanger would make advance payments of 75% of the Overland Auction Price, it would later make "trailing payments" to Waggoner Cattle which brought total payments on the transferred calves to around 100% of the Overland Auction Price. Pl's. Summ. J. Mot. Ex. 102 (Email from Paul Strouhal, Rabo's primary loan officer, to Quint Waggoner and DeNise Merritt to discuss transfer pricing in addition to "distributions back to Waggoner Cattle"; attached spreadsheet showing 75% advances and 25% distributions from Cliff Hanger to Waggoner Cattle); Exs. 19, 41, and 47 (Rabo credit memos mentioning additional payments to be made from Cliff Hanger to Waggoner Cattle); Ex. 113 (Accounting of DeNise Merritt showing additional distributions to Waggoner Cattle).

Based on this conflicting evidence, there is a factual dispute as to the actual payment due from Cliff Hanger to Waggoner Cattle. Some evidence shows the price was 75% of the Overland Auction Price, while other evidence shows 75% was just an advance to be followed by a "trailing payment." Therefore, even if the Court were to accept Rabo's interpretation of "payment in full" being equal to the price due according to Quint Waggoner, it still could not hold on summary judgment that "payment in full" is equal to 75% of the Overland Auction Price. Summary judgment should be denied to Rabo to the extent it seeks a declaration that "payment in full" is equal to or less than 75% of the Overland Auction Price.

F. Conclusions on Construction of the Intercreditor Agreement

For cattle to qualify as Cliff Hanger Collateral, they must meet both the locational and relational conditions of that definition. For Holstein Cattle to qualify as Cliff Hanger Collateral, the requirements of "delivery" and "payment in full" must also be met; such conditions are not required for Beef Cattle or Pasture Cattle to qualify as Cliff Hanger Collateral. The meaning of "payment in full" is ambiguous and cannot be decided at summary judgment.

Based on this interpretation of the Intercreditor Agreement, the Beef Cattle qualify as Cliff Hanger Collateral because they meet both the relational and locational conditions—they were owned by Cliff Hanger and were sold from the feedyards. The Pasture Cattle do not qualify as Cliff Hanger Collateral because they only meet the relational condition—they were owned by Cliff Hanger but were never placed in the feedyards. Because the Pasture Cattle do not qualify as Cliff Hanger Collateral, Lone Star's senior lien against them was never subordinated. Whether some or all the Holstein Cattle qualify as Cliff Hanger Collateral should not be decided on summary judgment because the meaning of "payment in full" is ambiguous, and it is thus impossible to determine if they meet that necessary requirement.

IV. The Tyler-and-Tucker Cattle

During the course of the Waggoner Entities' operations, Waggoner Cattle "sold" numerous head of cattle to Quint Waggoner's sons, Tyler and Tucker ("**Tyler-and-Tucker Sales**"). Once acquired, Tyler and Tucker then granted a lien on these cattle to Rabo. Lone Star alleges in its complaint that the Tyler-and-Tucker Sales were illegitimate sham transactions but concedes for the sake of this summary judgment motion that the sales were legitimate. Nonetheless, Lone Star argues that its first-in-time lien survived the Tyler-and-Tucker Sales and it therefore has priority over Rabo's later-granted lien by Tyler and Tucker. Lone Star says that

when Rabo collected proceeds from the sale of the Tyler-and-Tucker Cattle to packers, it therefore converted Lone Star's collateral. Rabo first argues that Lone Star's conversion claims relating to the Tyler-and-Tucker Cattle should be dismissed because Tyler and Tucker are indispensable parties that have not been joined in this action. It further argues that even if the Court does not dismiss the Tyler-and-Tucker conversion claims for failure to join an indispensable party, it should still find that Lone Star's lien on the cattle did not survive the Tyler-and-Tucker Sales, and Rabo therefore did not convert collateral of Lone Star.

A. Indispensable Parties

"An indispensable party is one whose joinder is vital to avoid serious prejudice to that person or the parties already joined." *ADT, L.L.C. v. Richmond*, 18 F.4th 149, 155 (5th Cir. 2021). Determining whether to dismiss a claim for failure to join an indispensable party requires a two-step inquiry. First, courts must determine whether the party is a "necessary" party under Rule 19(a).[4] *Hood v. City of Memphis, Tenn.*, 570 F.3d 625, 628 (5th Cir. 2009). Second, if a party is necessary, but its joinder is not feasible, it must be determined under Rule 19(b) whether the party is "indispensable;" that is, "whether litigation can be properly pursued without the absent party." *Id*. at 629.

Even if the Court finds that Tyler and Tucker are necessary parties, there is no reason to decide whether they are indispensable because there is no indication that Tyler and Tucker could not be joined in this action. Their joinder would not destroy diversity jurisdiction in this matter, as Tyler and Tucker are presumably, like Lone Star, citizens of Texas. And Rabo has provided no other reason as to why they cannot be joined. Therefore, Rabo has presented no basis for dismissal of the Tyler-and-Tucker conversion claims under Rule 19(b). Still, even if they are not

[4] "Rule" refers to the Federal Rules of Civil Procedure. Rule 7019 of the Federal Rules of Bankruptcy Procedure makes Rule 19 applicable in bankruptcy proceedings.

indispensable parties, the Court should determine whether Tyler and Tucker should be joined in this proceeding as necessary parties.

> A party should be joined in an action if:
>
> (A) in that person's absence, the court cannot accord complete relief among existing parties; or
> (B) that person claims an interest relating to the subject of the action and is so situated that disposing of the action in the person's absence may:
> (i) as a practical matter impair or impede the person's ability to protect the interest; or
> (ii) leave an existing party subject to a substantial risk of incurring double, multiple, or otherwise inconsistent obligations because of the interest.

Rule 19(a). "Within Rule 19, there are two main considerations if a third party is absent from the litigation and their joinder is sought: prejudice to the initial parties (see Fed. R. Civ. P. 19(a)(1)(A)), and prejudice to the interest of the proposed party to be joined (see Fed. R. Civ. P. 19(a)(1)(B)(i))." *Banks, Next friend of W.B. v. St. James Par. Sch. Bd.*, 757 F. App'x 326, 331 (5th Cir. 2018). Federal district courts have broad discretion to determine if a party should be joined under Rule 19. *Nat'l Liab. & Fire Ins. Co. v. Young*, No. 6:19-CV-031-H, 2020 WL 6122545, at *1 (N.D. Tex. Mar. 3, 2020).

In *United States v. Fullpail Cattle Sales, Inc.*, the defendant seized and removed from a debtor-couple's farm forty-two head of cattle upon which the defendant held a security interest. 617 F. Supp. 73, 74 (E.D. Wis. 1985). Another creditor of the debtors asserted that it held the first lien on the forty-two head of cattle and that the defendant's seizure of the cattle was therefore conversion of its collateral. *Id*. The defendant argued that the case should be dismissed because the debtors were indispensable parties that had not been joined in the action. *Id*. at 75. The court noted that because the claim was not against the debtors, complete relief could be granted without their joinder; the debtors would not be bound by res judicata and therefore were not unable to protect their interests as a result of the action; the plaintiff was not

able to receive duplicate recovery against the debtors; and the defendant could move to join the debtors if it believed they shared liability. *Id*. at 76. For these reasons, the court held the debtors were not necessary parties under rule 19(a). *Id*. at 75.

The facts here closely parallel those of *Fullpail Cattle*; Lone Star is suing Rabo for conversion of the proceeds of cattle sales upon which Lone Star claims it has the senior lien, and Rabo now argues that the original owners of the cattle are indispensable parties. Like in *Fullpail Cattle*, full relief may be granted to Lone Star without Tyler and Tucker's joinder; Tyler and Tucker are not barred from pursuing any claims they may have as a result of this action (and it is unlikely they have any, as they expressly disclaimed any interest in their cattle, *see* Pl.'s Resp. to Def.'s Summ. J. Mot., Ex. 114); Lone Star may not receive duplicate recovery from Tyler and Tucker; and Rabo may join Tyler and Tucker in this action for any claims Rabo has against them. *See* Rule 14.

Rabo argues that if Lone Star is successful on its conversion claim, then Rabo will have a substantial damage claim back against Tyler and Tucker for, among other things, defrauding Rabo. First, this possibility is not markedly significant as it is the threat of inconsistent obligations, *not* multiple litigation, that bears on Rule 19 analysis. *Boone v. Gen. Motors Acceptance Corp.*, 682 F.2d 552, 554 (5th Cir. 1982). And second, as mentioned, even if Rabo may have a subsequent claim against Tyler and Tucker, Rabo may permissively join Tyler and Tucker in this action to pursue that claim. *See* Rule 14.[5] But in the three years since this litigation began, Rabo has not done so. Tyler and Tucker are neither necessary nor indispensable parties. They need not be joined in this action, and Lone Star's conversion claims should not be dismissed on account of their nonjoinder.

[5] Rule 7014 of the Federal Rules of Bankruptcy Procedure makes Rule 14 applicable in bankruptcy proceedings.

B. Ordinary Course Exception for Liens Against Farm Products

Under Texas law, a lien continues to encumber collateral after the collateral is sold to another party. TEX. BUS. & COM. CODE § 9.315. Section 9.315 is preempted, however, by the Food Security Act ("**FSA**"), which was enacted to protect purchasers of farm products from the secured creditors of sellers. *Nelson v. Am. Nat. Bank of Gonzales*, 921 S.W.2d 411, 416 (Tex. App.—Corpus Christi 1996, no writ). Under the FSA, "a buyer who in the ordinary course of business buys a farm product from a seller engaged in farming operations shall take free of a security interest created by the seller, even though the security interest is perfected; and the buyer knows of the existence of such interest." 7 U.S.C. § 1631(d).

Lone Star contends that the Tyler-and-Tucker Sales were not made in the ordinary course of business under the FSA and thus the FSA does not apply to the transaction. The FSA defines a "buyer in the ordinary course" as "a person who, in the ordinary course of business, buys farm products from a person engaged in farming operations who is in the business of selling farm products." 7 U.S.C. § 1631(c)(1). But a definition of the phrase "ordinary course of business" is absent from the FSA.

Courts have looked to the Uniform Commercial Code ("UCC") to define terms in the FSA undefined by the FSA itself. *First State Bank of Athens Mabank Branch v. Purina Ag Capitol Corp.*, 113 S.W.3d 1, 7 (Tex. App.—Tyler 1999, no pet.) (using Texas UCC to define term "sale" from FSA); *In re Hatfield 7 Dairy, Inc.*, 425 B.R. 444, 454 (Bankr. S.D. Ohio 2010) (following *First State Bank of Athens* to use Ohio UCC to define term "buyer" from FSA). Within its definition of "buyer in the ordinary course of business," the Texas UCC states that "[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." TEX. BUS. & COM. CODE § 1.201(b)(9). Under this definition, a transaction is conducted in the ordinary course of business if it is ordinary (1) within the industry of the seller or (2) within the seller's particular business. *Id.*

The undisputed facts reveal that under any general understanding of regular business transactions, the Tyler-and-Tucker Sales were highly unusual. Cattle sales should be documented in some way, either through a contract, invoice, or some other means. The only notation of the Tyler-and-Tucker Sales were in the internal records of Waggoner Cattle. Pl's. Summ. J. Mot. Ex. 42 at 2–3; Ex. 43. at 2. Tyler and Tucker never paid for the cattle from the Tyler-and-Tucker Sales. Assuming the legitimacy of the Tyler-and-Tucker Sales, they were thus effectively owner-financed 100% by Waggoner Cattle at no interest. Pl's. Summ. J. Mot. Ex. 42 at 3–4; Ex. 43 at 3. It is ordinary that owners control the disposition of their cattle and proceeds. But Quint Waggoner had complete control over how the ultimate proceeds of the Tyler-and-Tucker Cattle were disbursed and spent. Pl's. Summ. J. Mot. Ex. 42 at 5; Ex. 43 at 3–4. It is expected that the quantity and price of sales should result from an arms-length agreement. Quint Waggoner directed all aspects of the Tyler-and-Tucker Sales. Pl's. Summ. J. Mot. Ex. 43 at 4. And most important, it is ordinary for a buyer (here, Tyler and Tucker) to act in the buyer's interest, not in the seller's interest. Millions of dollars of proceeds from the Tyler-and-Tucker Cattle went back to the Waggoner Entities. Pl's. Summ. J. Mot. Ex. 42 at 4–5; Ex. 43 at 4. These facts are undisputed by Rabo and, taken together, show that the Tyler-and-Tucker Sales were highly unusual.

The Tyler-and-Tucker Sales were also unusual in light of Quint Waggoner and the Waggoner Entities' normal sale practices. Paragraph 2(a) of the Intercreditor Agreement reveals that Cliff Hanger was required to make "payment in full" for cattle it acquired from Waggoner

Cattle; Tyler and Tucker never made payments for the cattle they acquired from Waggoner Cattle. Pl's. Summ. J. Mot. Ex. 42 at 3; Ex. 43 at 3–4; Ex. 3. Cliff Hanger's sales to packers were well documented, Pl's. Summ. J. Mot. Ex. 28B; the Tyler-and-Tucker Sales were only ever notated in Waggoner Cattle's records. Pl's. Summ. J. Mot. Ex. 42 at 2–3; Ex. 43. And Cliff Hanger's cattle sales were to third parties unaffiliated with Quint Waggoner; Tyler and Tucker's "businesses" were entirely subsumed by, and indistinguishable from, the Waggoner Entities. Pl's. Summ. J. Mot. Ex. 42 at 2. These facts are undisputed by Rabo and, taken together, show that the sales of cattle to Tyler and Tucker were highly unusual in light of Quint Waggoner and the Waggoner Entities' normal sale practices. Because the Tyler-and-Tucker Sales were neither ordinary within the cattle industry nor in light of the Waggoner Entities' business practices, the sales were not completed in the ordinary course of business.

Rabo argues that focusing on the nature of the transactions is inappropriate in determining whether they concerned ordinary-course sales. Instead, Rabo submits that the *status* of the buyer—as one in the business of buying farm products—is the critical factor under the FSA's definition of "buyer in the ordinary course." But it is the status of the *seller*, not the buyer, that matters under the definition; a buyer in the ordinary course is one who "buys farm products *from a person* engaged in farming operations *who is in the business of selling farm products*." 7 U.S.C. § 1631(c)(1) (emphasis added). The only qualifier the definition places on the buyer is that he buys farm products "*in the ordinary course of business*." *Id*. (emphasis added). And, as explained, to determine if a transaction was completed in the ordinary course of business under the UCC, scrutiny of the nature of the transactions is essential. *See* Tex. Bus. & Com. Code § 1.201(9); *Wells Fargo Bank Nw., N.A. v. RPK Cap. XVI, L.L.C.*, 360 S.W.3d 691, 704–05 (Tex. App.—Dallas 2012, no pet.) (comparing transaction to past practices of seller to

determine if transaction completed in "ordinary course of business"); *TRC Tire Sales, LLC v. Triple S Tire Co.*, No. H-13-1539, 2014 WL 4274077, at *2 (S.D. Tex. Aug. 28, 2014) (finding evidence of "usual or customary practices" of seller essential in determining if transaction was completed in "ordinary course of business); *Assocs. Disc. Corp. v. Rattan Chevrolet, Inc.*, 462 S.W.2d 546, 550 (Tex. 1970) (analyzing whether transactions occurred in "usual or customary manner" to determine if completed in "ordinary course of business").

Rabo also argues that the applicable exceptions to subsection (d) of the FSA are found in subsection (e) and that Lone Star failed to follow the procedures required to take advantage of those exceptions. Under subsection (e), a buyer of farm products takes subject to a security interest if the secured party either provided the buyer with written notice of the security interest with certain required statutory information or filed an effective financing statement with the secretary of state. 7 U.S.C. § 1631(e). Lone Star did neither. But this argument is a red herring—Lone Star does not claim that it retains a lien subject to an exception of the FSA. Rather, it argues that the FSA's exception never applied to its lien in the first place because the Tyler-and-Tucker Sales were not completed in the ordinary course of business as required by subsection (d). The subsection (e) exceptions are irrelevant to this analysis.

The Tyler-and-Tucker Sales did not comport with ordinary practices within the cattle industry nor within the Waggoner Entities' business; they were not completed within the ordinary course of business under the Texas UCC. (Indeed, the sales were so irregular that they cannot be considered as having been completed in the ordinary course of business under *any* reasonable definition of that phrase). Tyler and Tucker were not "buyers in the ordinary course" under the FSA. The FSA thus does not apply to the Tyler-and-Tucker Sales. Texas law,

however, remains applicable; under § 9.315 of the Texas UCC, Lone Star's first lien on the Tyler-and-Tucker Cattle survived the Tyler-and-Tucker Sales.

V. The Offset Cattle

Lone Star alleges that there were certain lots of Holstein Cattle transferred from Waggoner Cattle to Cliff Hanger for which Cliff Hanger only provided Lone Star an offset of debt owed by Waggoner Cattle to Cliff Hanger ("**Offset Cattle**").[6] While Lone Star does not seek summary judgment on the interpretation of the phrase "payment in full" in the Intercreditor Agreement, it does argue that under any interpretation of that phrase, an offset cannot constitute a payment. Lone Star reasons that because "payment in full" was never made to Waggoner Cattle for the Offset Cattle, its senior lien on those cattle was never subordinated and it can therefore pursue a conversion action for the proceeds of the Offset Cattle.

But under the definitions of "payment" and "offset" provided *by Lone Star* in its own summary judgment brief, an offset may constitute a payment. Black's Law Dictionary defines "payment" as "[p]erformance of an obligation by the delivery of money or some other valuable thing accepted in partial or full discharge of the obligation." *Payment*, BLACK'S LAW DICTIONARY (11th ed. 2019). It defines "offset" as "[s]omething (such as an amount or claim) that balances or compensates for something else." *Offset*, BLACK'S LAW DICTIONARY (11th ed. 2019). Certainly, "something … that balances or compensates for something else," *Id.*, constitutes a "valuable thing," *Payment*, BLACK'S LAW DICTIONARY (11th ed. 2019), because it reduces what one party owes another. Lone Star additionally argues that because under the

[6] There were some cattle transferred from Waggoner Cattle to Cliff Hanger which Lone Star distinguishes in some form, claiming Waggoner Cattle received "no payment" for them. Pl's. Summ. J. Mot. Br. at 47. Presumably this means not even an offset was granted for these cattle, but that is not entirely clear from the motion because Lone Star asserts an offset is not a payment. Regardless, it would be inappropriate to address a conversion claim for cattle for which not even an offset was provided, as Lone Star's damages calculation does not distinguish these cattle from those for which an offset was provided.

Texas UCC a "'[b]uyer in the ordinary course' does not include a person that acquires goods … in total or partial satisfaction of a money debt," an offset cannot constitute a payment. TEX. BUS. & COM. CODE § 1.201(b)(9). But that definition only stands for the proposition that an offset may be a type of transaction that is outside the ordinary course of business; it still implies that a recipient of an offset may be a "seller" who received a payment.

Lone Star's argument that an offset is not a payment is unavailing. An offset constitutes a payment. But the issue remains whether such payment was "payment in full" to thereby trigger the subordination of Lone Star's liens under the Intercreditor Agreement. And without a determination of which party held the senior lien against the Offset Cattle, the Court cannot, on summary judgment, decide if Rabo converted proceeds of the Offset Cattle. Both Lone Star's and Rabo's summary judgment motions on Lone Star's conversion claim to recover the proceeds of the Offset Cattle should be denied.

VI. Lone Star's Conversion Claim

Lone Star argues that it is entitled to summary judgment on its conversion claims. It asserts that it retained the senior security interest in the proceeds of the Tyler-and-Tucker Cattle, the Offset Cattle, the Beef Cattle, and the Pasture Cattle.[7] Lone Star argues that when Rabobank swept Cliff Hanger's bank account where the proceeds of the cattle sales were and transferred the proceeds to Rabo, Rabo committed conversion.

"Conversion is the unauthorized and unlawful assumption and exercise of dominion and control over the personal property of another to the exclusion of, or inconsistent with, the owner's rights." *Freezia v. IS Storage Venture, LLC*, 474 S.W.3d 379, 386 (Tex. App.—Houston [14th Dist.] 2015, no pet.). A security interest is an interest in property, TEX. BUS. &

[7] Lone Star additionally has a conversion claim for the Holstein Cattle but has not sought summary judgment on that claim, ostensibly because Lone Star argues that the term "payment in full" is ambiguous.

COM. CODE § 1.201, and "[a] properly perfected security interest extends to the identifiable cash proceeds of a sale of collateral subject to that security interest." *ITT Com. Fin. Corp. v. Bank of the W.*, 166 F.3d 295, 305 (5th Cir. 1999); *see also* TEX. BUS. & COM. CODE § 9.315(a). "The holder of the security interest is entitled to recover cash proceeds from unauthorized subsequent transferees." *ITT Com. Fin. Corp.*, 166 F.3d at 305. Critically, a security interest only attaches to *identifiable* proceeds. TEX. BUS. & COM. CODE § 9.315(a)(2). Cash proceeds comingled with other property are identifiable "to the extent that the secured party identifies the proceeds by a method of tracing, including application of equitable principles, that is permitted under law other than this chapter with respect to commingled property of the type involved." TEX. BUS. & COM. CODE § 9.315(b)(2).

Lone Star's pursuit of a conversion action to recover the identifiable proceeds of its collateral over which Rabo assumed control is therefore appropriate. Based on the Court's interpretation of the Intercreditor Agreement, Rabo had the senior lien on the Beef Cattle. There are thus no identifiable proceeds of the Beef Cattle that Lone Star is entitled to, and summary judgment should be granted in Rabo's favor barring Lone Star's conversion action to recover proceeds from the Beef Cattle sales. Because the Court cannot interpret the meaning of "payment in full" under the Intercreditor Agreement, it cannot determine if Lone Star's lien over the Offset Cattle was subordinated, and summary judgment should therefore be denied to Lone Star on Lone Star's conversion action to recover proceeds from the Offset Cattle sales. But based on the Court's interpretation of the Intercreditor Agreement and its findings on the Tyler-and-Tucker Cattle, Lone Star retained a senior lien on the identifiable proceeds of the Tyler-and-Tucker Cattle and the Pasture Cattle. Lone Star therefore has a colorable claim for conversion to

recover the identifiable proceeds of the Tyler-and-Tucker Cattle and the Pasture Cattle. Rabo puts forth several arguments for why Lone Star's conversion claims must fail, nonetheless.

A. Economic Loss Rule

Rabo alleges that Lone Star's conversion claims are barred by the economic loss rule, also known as the independent injury rule, because, Rabo argues, Lone Star seeks to recover through its conversion claim purely economic losses covered by the subject matter of the Intercreditor Agreement.

> The economic loss rule generally precludes recovery in tort for economic losses resulting from a party's failure to perform under a contract when the harm consists only of the economic loss of a contractual expectancy. But it does not bar all tort claims arising out of a contractual setting. As we have said, "a party [cannot] avoid tort liability to the world simply by entering into a contract with one party [otherwise the] economic loss rule [would] swallow all claims between contractual and commercial strangers." Thus, a party states a tort claim when the duty allegedly breached is independent of the contractual undertaking and the harm suffered is not merely the economic loss of a contractual benefit.

Chapman Custom Homes, Inc. v. Dallas Plumbing Co., 445 S.W.3d 716, 718 (Tex. 2014) (alterations in original) (quoting *Sharyland Water Supply Corp. v. City of Alton*, 354 S.W.3d 407, 419 (Tex. 2011)).

1. Disparities Among Texas Courts

"When applying state law, '[a federal court should] interpret the state statute the way [it] believe[s] the state Supreme Court would, based on prior precedent, legislation, and relevant commentary.'" *Vielma v. Eureka Co.*, 218 F.3d 458, 462 (5th Cir. 2000) (alterations added) (quoting *F.D.I.C. v. Shaid*, 142 F.3d 260, 261 (5th Cir. 1998)). While the Texas Supreme Court has provided the general principles supporting the economic loss doctrine, it has not specifically addressed how the doctrine impacts conversion claims. "If a state's highest court has not spoken on the issue, [a federal court should] look to the intermediate appellate courts for guidance." *Id.*

While Texas courts of appeals have addressed whether the economic loss rule bars conversion claims, they have come to widely differing conclusions on the matter.

Some courts have held that the economic loss rule did not bar the conversion claims before them, even when a concurrent breach-of-contract claim was raised. In *MSMTBR, Inc. v. Mid-Atlantic Finance Co.*, the court held that the economic loss rule did not bar a conversion claim even though the same facts underlying the conversion claim could also support a claim for breach of contract because the conversion claim rested on a concurrent legal duty independent of the contract. No. 01-12-00501-CV, 2014 WL 3697736, at *5 (Tex. App.—Houston [1st Dist.] July 24, 2014, no pet.). In *Cass v. Stephens*, the court held that the economic loss rule did not bar a conversion claim from proceeding alongside a breach-of-contract claim in part because, unlike *MSMTBR, Inc.*, the facts underlying the conversion claim could *not* support a claim for breach of contract. 156 S.W.3d 38, 69 (Tex. App.—El Paso 2004, pet. denied).

Other courts have found that the economic loss rule did bar the conversion claims before them. In *ConocoPhillips Co. v. Koopmann*, the court held that the economic loss rule barred a conversion claim in part because the liability for conversion arose only because of the breach of contract. 542 S.W.3d 643, 666 (Tex. App.—Corpus Christi 2016), *aff'd on other grounds*, 547 S.W.3d 858 (Tex. 2018). In *Exxon Mobil Corp. v. Kinder Morgan Operating L.P. "A"*, the court held that the economic loss rule barred a conversion claim even though the legal duty underlying conversion existed notwithstanding the existence of the contract. 192 S.W.3d 120, 128 (Tex. App.—Houston [14th Dist.] 2006, no pet.). Texas courts have thus expressed a broad and contradictory view of how the economic loss rule impacts conversion claims, ranging from an understanding that the rule *never* bars conversion claims to an understanding that the rule *always* bars conversion claims when a contract supplies identical duties to conversion.

Federal courts applying Texas law have only further muddied the water. *Compare Nat'l Union Fire Ins. Co. of Pittsburgh, Pa. v. Care Flight Air Ambulance Serv., Inc.*, 18 F.3d 323, 326 (5th Cir. 1994) ("Texas courts have specifically recognized that because the law of conversion and bailment imposes legal duties outside any contractual agreements, separate causes of action for breach of contract and conversion may arise from the same facts."), *SPP SWD Burns Ranch, LLC v. Kent*, No. 5:14-CV-88, 2015 WL 12841097, at *3 (S.D. Tex. Jan. 8, 2015) ("Texas law imposes no limitation on bringing both conversion and breach of contract claims based on a single set of facts and a single injury, nor is there a requirement that the damages stemming from such claims be separate and distinct."), *and Bates Energy Oil & Gas v. Complete Oilfield Servs.*, 361 F. Supp. 3d 633, 656 (W.D. Tex. 2019) (quoting *Kent*), *with Reed v. Carecentric Nat'l, LLC (In re Soporex, Inc.)*, 446 B.R. 750, 787 (Bankr. N.D. Tex. 2011) ("The Court agrees … that the economic loss rule (or independent injury doctrine)… requires more analysis than a simple incantation that the rule does, or does not, apply to bar any claim asserted on a conversion theory…. [T]he Court concludes that the allegations of the Complaint, taken as true, establish that the Trustee's remedy lies in contract, not conversion. Accordingly, the conversion claim must be dismissed.").

If one thing is clear, it is that there is no consensus in the Texas courts on precisely how a court should apply the economic loss rule to conversion claims. Nonetheless, even assuming that the Texas Supreme Court would hold that the economic loss rule could be used to bar conversion claims in some circumstances, applying the general principles supplied by the Texas Supreme Court and Texas appellate courts, the economic loss rule cannot be used here to bar Lone Star's conversion claim.

2. Application of General Principles

"Courts consider two factors to determine whether a cause of action sounds in contract or tort: (i) the source of the duty giving rise to the injury and (ii) the nature of the injury itself." *Dixie Carpet Installations, Inc. v. Residences at Riverdale, LP*, 599 S.W.3d 618, 635 (Tex. App.—Dallas 2020, no pet.).

Here, the duty breached by Lone Star arises *only* from state law and *not* from the Intercreditor Agreement. The Intercreditor Agreement is a subordination agreement that modifies the parties' existing statutory property rights in their collateral. It does not describe the rights associated with a first-priority lien, which are determined by state law. It does not impose any affirmative obligation on either party, except to provide further assurances upon request and some notices, and it does not address any remedies. Therefore, while the Intercreditor Agreement modifies Lone Star's property rights, which Lone Star brought the conversion claims to enforce, Lone Star did not bring the claims to enforce the Intercreditor Agreement. Rather, it brought the conversion claims to assert its state-law rights to a first-priority lien. "A duty to refrain from unlawfully or wrongfully appropriating the property of another arises under statutory and common law." *MSMTBR, Inc.*, 2014 WL 3697736, at *5. "[T]he source of the duty giving rise to the injury" therefore rests exclusively in state law, not the Intercreditor Agreement. *Dixie*, 599 S.W.3d at 635.

In this way, this case resembles *Cass*, which did not allow the economic loss rule to bar a conversion claim, where the facts underlying the conversion claim *could not* justify a claim for breach of contract. And it is distinguishable from *Exxon Mobil Corp.* and *ConocoPhillips Co.*, which held the economic loss rule barred conversion claims but in circumstances where the same duty underlying the conversion claims *also* justified claims for breach of contract.

The nature of Lone Star's injury also does not resemble the Intercreditor Agreement's contractual damages. Whatever damages the Intercreditor Agreement could allow would be limited to remedying a breach of the few affirmative duties outlined in the Intercreditor Agreement. Instead, Lone Star's damages reflect the proceeds Rabo allegedly converted. The source of duty giving rise to Lone Star's conversion claims derives from state law, not the Intercreditor Agreement, and the nature of Lone Star's injury does not resemble the Intercreditor Agreement's contractual damages. Even assuming that Texas law allows the economic loss rule to bar conversion claims in some circumstances, it cannot bar Lone Star's conversion claim here.

B. Statute of Limitations

Rabo asserts that Lone Star's Pasture-Cattle conversion claim is barred by the statute of limitations. Conversion claims under Texas law are governed by a two-year statute of limitations: "a person must bring suit for … conversion of personal property … not later than two years after the day the cause of action accrues." TEX. CIV. PRAC. & REM. CODE § 16.003. "Generally, the limitations period for a conversion claim begins to run at the time of the unlawful taking." *Pipes v. Hemingway*, 358 S.W.3d 438, 450 (Tex. App.—Dallas 2012, no pet.). Lone Star's Pasture-Cattle conversion claim rests on a final payment made to Rabo in July 2017 for the sale of Pasture Cattle. Therefore, under the relevant statute of limitations, Lone Star had until July 2019 to raise a claim for conversion of proceeds of Pasture Cattle. Lone Star did not raise its Pasture-Cattle conversion claim until October 16, 2019, in its second amended complaint, after the statute of limitations had run.

In some circumstances, an amended pleading may relate back to the date of an original pleading. Rule 15(c).[8] Relation back may occur when "the amendment asserts a claim or

[8] Rule 7015 of the Federal Rules of Bankruptcy Procedure makes Rule 15 applicable in bankruptcy proceedings.

defense that arose out of the conduct, transaction, or occurrence set out—or attempted to be set out—in the original pleading." Fed. R. Civ. P. 15(c)(1)(B). "Rule 15(c) serves as a useful guide to 'help, not hinder, persons who have a legal right to bring their problems before the courts.'" *Sanders-Burns v. City of Plano*, 594 F.3d 366, 375 (5th Cir. 2010) (quoting *Hill v. Shelander*, 924 F.2d 1370, 1375 (7th Cir. 1991)). "[I]f a plaintiff seeks to correct a technical difficulty, state a new legal theory of relief, or amplify the facts alleged in the prior complaint, then relation back is allowed," *F.D.I.C. v. Conner*, 20 F.3d 1376, 1386 (5th Cir. 1994); "[s]o long as the original and amended petitions state claims that are tied to a common core of operative facts, relation back will be in order." *Mayle v. Felix*, 545 U.S. 644, 664 (2005). "[T]he focus is 'not ... the caption given a particular cause of action, but ... the underlying facts upon which the cause of action is based.'" *Johnson v. Crown Enters., Inc.*, 398 F.3d 339, 342 (5th Cir. 2005) (quoting *Watkins v. Lujan*, 922 F.2d 261, 265 (5th Cir. 1991)). "The purpose of the rule is accomplished if the initial complaint gives the defendant fair notice that litigation is arising out of a specific factual situation." *Id.* (quoting *Longbottom v. Swaby*, 397 F.2d 45, 48 (5th Cir. 1968)).

In *Yaeger v. Magna Corp.*, a trustee for the chapter 7 bankruptcy case of a corporate debtor brought conversion actions against a couple for depositing funds of the debtor in a private bank account. *(In re Magna Corp.)*, No. 01-80763 C-7D, 2003 WL 23211571, at *1–2 (Bankr. M.D.N.C. Nov. 28, 2003). The trustee's original complaint alleged that the couple converted "large sums of money, in the amount of at least $94,894.78." *Id*. at *4. The trustee later amended the complaint, providing specific amounts and dates of deposited funds constituting conversion, but did so after the statute of limitations for conversion had run. *Id.*

The court held that the amended complaint related back to the date of the original complaint. *Id*. Relying on Fifth Circuit precedent, the court noted that so long as there is a

"factual nexus" between the original and amended complaint, and the purpose of the amended complaint is to "amplify … the original pleading," or "set forth facts with greater specificity," relation back is appropriate. *Id*. (citing *McClellon v. Lone Star Gas Co.*, 66 F.3d 98, 102–03 (5th Cir. 1985); *United States v. Randall & Blake*, 817 F.2d 1188, 1191 (5th Cir. 1987)). The court held that because specifying the specific transactions which constituted conversion merely "amplified the allegations" in the original complaint, and because "the allegations in the original complaint were broad enough to provide the [defendant] with notice of all of the claims that [were] included in the amended complaint such that the [defendant was] not prejudiced by the amendment," the amended complaint related back to the date of the original complaint. *Id.*

Here, like *Yaeger*, the addition of the Pasture Cattle to Lone Star's conversion claim merely amplified the original pleading. While it specified additional proceeds that were allegedly converted, the claim of conversion of the Pasture Cattle still rests on the same "common core of operative facts" as the original complaint, *Mayle*, 545 U.S. at 664—both complaints allege that Lone Star held a first-in-time lien on all Cliff Hanger cattle, both allege that the Intercreditor Agreement allowed for conditional subordination of that lien, and both allege Rabo converted the proceeds of Cliff Hanger cattle upon which Lone Star's lien was not subordinated by the Intercreditor Agreement. Like *Yaeger*, Lone Star's amended complaint merely adds specificity to the types and amounts of proceeds converted by Rabo under "the same pattern of conduct identified in the original complaint." *F.D.I.C. v. Conner*, 20 F.3d at 1386. By pleading in its original complaint that Rabo converted proceeds that were subject to Lone Star's senior lien, Lone Star adequately provided "fair notice" to Rabo that litigation was arising out of Rabo's receipt of Cliff Hanger cattle proceeds. *Johnson.*, 398 F.3d at 342. For these reasons, Lone Star's conversion claim predicated on conversion of Pasture-Cattle proceeds should relate

back to the date of Lone Star's original complaint and thus not be barred by the statute of limitations.

C. Immediate Right to Possession

Rabo argues that Lone Star did not have an immediate right to possession of the proceeds of the cattle Cliff Hanger sold because it did not take any affirmative action, such as issuing a levy, to enforce its lien. Because an immediate right to possession is an essential element of a conversion claim, Rabo argues that Lone Star's conversion claims must fail.

While Rabo is correct that a "an immediate right to possession at the time of conversion" is typically required to recover for conversion, *Christian v. First Nat'l Bank of Weatherford*, 531 S.W.2d 832, 841 (Tex. Civ. App.—Fort Worth 1975, writ ref'd n.r.e.), that requirement has been relaxed for lienholders suing to recover for conversion of their collateral. "Generally, a lienholder may sue for conversion of encumbered property *even though the lienholder is not entitled to possession at the time of the conversion*." *Elite Towing, Inc. v. LSI Fin. Grp.*, 985 S.W.2d 635, 644 (Tex. App.—Austin 1999, no pet.) (emphasis added); *see also John Deloach Enters., Inc. v. Telhio Credit Union, Inc.*, 582 S.W.3d 590, 596 (Tex. App.—San Antonio 2019, no pet.); *Hart v. Meadows*, 302 S.W.2d 448, 451 (Tex. Civ. App.—Texarkana 1957, writ ref'd n.r.e.); *Scaling v. First Nat'l Bank of Wichita Falls*, 39 Tex. Civ. App. 154, 159, 87 S.W. 715, 717 (Fort Worth 1905, writ ref'd). Therefore, Lone Star's entitlement to possession of the allegedly converted proceeds has no bearing on its claims for conversion.

Rabo relies on *U.S. v. Boardwalk Motor Sports, Ltd.* for the contentions that (1) an immediate right to possession is an essential element of a claim for conversion of collateral; and (2) a lienholder must take affirmative action to enforce its rights to hold an immediate right of possession. 692 F.3d 378, 381 (5th Cir. 2012). In *Boardwalk*, the IRS sought to recover for

conversion against a party who sold a car upon which the IRS held a statutory tax lien. *Id.* at 380. The court held that, even though the IRS was a lienholder suing for conversion of collateral, it still had to prove it had a right to immediate possession of the collateral at the time of conversion. *Id*. at 381. The court further held that "[u]ntil the IRS takes additional action, such as serving a levy or instituting foreclosure proceedings, it does not have the right to take possession of the property." *Id.*

The court in *Boardwalk*, however, expressly distinguished statutory lienholders from those that hold a lien under a security agreement, *Id*. at 383; it recognized that the court in *Elite Towing* held that lienholders with a lien under a security agreement, "and not a lien created by statute," need not prove a right to immediate possession. *Id*. (quoting *Elite Towing*, 985 S.W.2d at 644). Because *Boardwalk*'s holding was limited to statutory lienholders, and Lone Star holds its liens under security agreements, *Boardwalk*'s rationale does not apply to Lone Star here. Texas law is otherwise clear that a lienholder through a security agreement need not prove a right to immediate possession to recover for conversion of collateral. *Elite Towing*, 985 S.W.2d at 644. Lone Star therefore need not prove here that it had a right to immediate possession of the cattle-sales proceeds to recover for conversion against Rabo.

D. Consent

Rabo asserts that Lone Star consented to Cliff Hanger's sale of its collateral in its credit agreements and therefore is barred from pursuing a conversion claim to recover the proceeds from the collateral. As a general rule, "[if a] mortgagee consents to the sale of [] mortgaged property, the purchaser takes it free of the lien, and the mortgagee can have neither foreclosure nor damages for conversion." *Cartwright v. Flatt*, 244 S.W.2d 523, 525 (Tex. Civ. App.—Waco 1951, no writ) (quoting *Oats v. Dublin Nat'l Bank*, 127 Tex. 2, 90 S.W.2d 824, 827 (Tex. 1936)).

Lone Star's security agreement with Cliff Hanger states, "Grantor represents and warrants to Lender that Grantor will sell, consign, lease, license, exchange, or transfer the Collateral only to those persons whose names and addresses have been set forth on sales schedules delivered to Lender." Def's. Summ. J. Mot. Ex. 11 at 2. Lone Star thus did provide limited, conditional consent to Cliff Hanger to sell its collateral. But the credit agreement also says, "All proceeds of any sale … or other disposition [of collateral] *shall be made immediately available to Lender* in a form jointly payable to Grantor and Lender. No provisions in this Agreement shall be interpreted to authorize any sale or disposition of Collateral unless authorized by the Lender in writing." *Id*. (emphasis added). Thus, while Lone Star conditionally consented to sale of its collateral, it retained its security interest in the proceeds of the collateral, and it did *not* consent in the credit agreement to a transfer of the proceeds.

The cases which hold that consent of a sale bars recovery for conversion involve a lienholder suing to recover the collateral from the transferee. *See Cartwright*, 244 S.W.2d at 525; *Amarillo Nat'l Bank v. Komatsu Zenoah Am., Inc.*, 991 F.2d 273, 274 (5th Cir. 1993); *Oats*, 90 S.W.2d at 827–29. Here, however, Lone Star is not suing to recover cattle from transferees who received cattle through sales Lone Star consented to; rather, Lone Star is suing to recover proceeds sent to Rabo by transfers it did *not* consent to. The fact that the proceeds came from a sale of collateral to which Lone Star consented is therefore not salient; it never consented to abandoning its security interest in the collateral proceeds nor to the transfer of the proceeds to Rabo, and consent therefore cannot be a bar to Lone Star's conversion claims.

E. Innocence

Rabo argues that Lone Star's conversion claim must fail because Cliff Hanger was the true culprit if any conversion occurred—it was the party with possession of cattle and the party

that placed the proceeds into the swept account. Rabo says Rabobank's sweeps of the bank account with the proceeds was automatically completed by contract, and Rabo made no affirmative, intentional attempt to take proceeds which rightfully belonged to Lone Star. This defense is unavailing for "[i]t is well established under Texas law that acting with good faith or innocence does not constitute a defense to conversion." *Smith v. Maximum Racing, Inc.*, 136 S.W.3d 337, 343 (Tex. App.—Austin 2004, no pet.). Rabo's claim that it acted in good faith when acquiring the swept proceeds has no bearing on Lone Star's conversion claims.

F. Tracing

Rabo argues that there is a genuine dispute of material fact as to whether the proceeds Lone Star seeks to recover are *identifiable* proceeds. A security interest only attaches to identifiable proceeds of collateral. TEX. BUS. & COM. CODE § 9.315(a)(2). Cash proceeds commingled with other property are identifiable "to the extent that the secured party identifies the proceeds by a method of tracing, including application of equitable principles, that is permitted under law other than this chapter with respect to commingled property of the type involved." TEX. BUS. & COM. CODE § 9.315(b)(2).

1. Funds Acquired by Sweep

Much of the proceeds of the Tyler-and-Tucker Cattle and the Pasture Cattle were deposited in a Cliff Hanger bank account commingled with other funds. Rabobank would then sweep that account daily and transfer the funds to Rabo. Rabo then controlled both the proceeds of Lone Star's collateral as well as other funds. For Lone Star to recover its proceeds swept by Rabo, it therefore must "identif[y] the proceeds by a method of *tracing*, including application of equitable principles, that is permitted under law other than this chapter." *Id*. (emphasis added).

Lone Star's forensic accounting expert, Gregg Morgan, employed a "pro rata" tracing method to calculate Lone Star's damages, which he says is appropriate in this case. Pl's. Summ. J. Mot. Ex. 28B. Under this method, Morgan tracked the cattle proceeds deposited into Cliff Hanger's account, which also included other funds, and calculated the percentage of the total account funds that were proceeds. When Rabobank swept the account, it may not have swept every dollar that had been deposited in the account because Cliff Hanger used the account for expenditures. However, whatever percentage of funds in the account before expenditures constituted proceeds, Morgan applied to the sweep. That pro-rata share of the sweeps, Morgan contends, are the traceable proceeds owed to Lone Star.

Rabo's forensic accounting expert, Steve Dawson, disputes the claims of Morgan and alleges that tracing is *not* possible. Def's. Resp. to Pl.'s Summ. J. Motion., Dawson Decl. ¶¶ 11–14. Dawson claims that tracing is impossible without an identifiable res to apply tracing methods to, and there is no identifiable res available now because Cliff Hanger's accounts were repetitively swept. *Id*. The parties have therefore presented competing experts who have come to the opposite conclusion on whether the proceeds of Cliff Hanger's cattle sales are traceable. "In a battle of competing experts, it is the sole obligation of the jury to determine the credibility of the witnesses and to weigh their testimony." *Cooke v. United States*, No. 3:07-CV-1120-G, 2008 WL 3876035, at *9 (N.D. Tex. Aug. 18, 2008) (quoting *Morrell v. Finke*, 184 S.W.3d 257, 282 (Tex. App.—Fort Worth 2005, pet. denied)). Whether the proceeds of Cliff Hanger's collateral are traceable is a critical fact issue in this case, since it determines if Lone Star's lien survived Rabo's sweeps, and thus, if Lone Star has verifiable conversion damages. Because weighing the credibility of competing experts is inappropriate for the Court on summary

judgment, it cannot decide here whether the proceeds of Cliff Hanger cattle sales swept by Rabo are traceable.

2. Direct Payments

Not all proceeds of Cliff Hanger cattle sales were placed in Cliff Hanger's account and then swept by Rabobank. Some proceeds were paid directly to Rabo from the cattle purchasers. Gregg Morgan has summarized these payments, and they include $2,201,729 in proceeds from Tyler-and-Tucker Cattle and $2,312,567 in proceeds from Pasture Cattle. Pl's. Summ. J. Mot. Ex. 28B. Morgan testifies that these sums were compiled from a thorough review of the loan statements maintained by Rabo, check copies from Rabo, the QuickBooks accounting ledger for Cliff Hanger; and shipping, receiving, and performance records from the Cliff Hanger third-party feedyards, among other sources. *Id*. While Rabo objected to Lone Star's pro-rata tracing method, it never objected to Morgan's tracing of these cattle proceeds. Because these proceeds can be traced, Lone Star retained its first lien over them, *see* TEX. BUS. & COM. CODE § 9.315(b)(2), and may pursue a conversion action for their recovery.

G. Damages, Attorney's Fees, and Costs

As the undisputed facts show that Rabo received direct payments for the sales of a portion of Tyler-and-Tucker Cattle and Pasture Cattle, Lone Star's first lien survived the sale of these cattle, and Lone Star may thus recover on its conversion action the proceeds of those sales, which equal $4,514,296. Lone Star argues, however, that it is additionally entitled to recover attorney's fees and costs for prosecuting its conversion claim.

"In Texas, attorney's fees may be recovered from an opposing party only as authorized by statute or by contract between the parties. Attorney's fees are generally not available for conversion claims." *Wiese v. Pro Am Servs., Inc.*, 317 S.W.3d 857, 861 (Tex. App.—Houston

[14th Dist.] 2010, no pet.). The Fifth Circuit in *Permian Petroleum Co. v. Petroleos Mexicanos*, applying Texas law, found an exception to this general rule when a plaintiff sues for conversion of collateral. 934 F.2d 635, 652 (5th Cir. 1991). The court held that a secured creditor seeking to recover converted collateral "may recover as actual damages either the outstanding principal balance plus the outstanding interest obligation, costs, and attorneys' fees or it may recover the value of the collateral, whichever is less." *Id.* (citing *Hodges v. Leach*, 214 S.W.2d 837, 842 (Tex. Civ. App.—Amarillo 1948); *Metal Window Prods. Co. v. Nored*, 535 S.W.2d 711, 713 (Tex. Civ. App.—Beaumont 1976, no writ); *Ochoa v. Evans*, 498 S.W.2d 380, 386 (Tex. Civ. App.—El Paso 1973, no writ)). The value of the collateral is calculated on the date of conversion. *Id*.

At least two courts of appeals in Texas have held after the *Permian* decision that a plaintiff seeking to recover for conversion of collateral was *not* entitled to attorney's fees. *John Deloach Enters.*, 582 S.W.3d at 601–02; *Silver Lion, Inc. v. Martinez*, No. 14-05-00746-CV, 2007 WL 665253, at *4 (Tex. App.—Houston [14th Dist.] Mar. 6, 2007, no pet.). Nevertheless, the Court is bound by the state law interpretations of the Fifth Circuit. *Cornelius v. Philip Morris Inc.*, No. CIV.A.3:99-CV-2125G, 2000 WL 233292, at *1 (N.D. Tex. Feb. 29, 2000), *aff'd*, 234 F.3d 705 (5th Cir. 2000). Because the Texas Supreme Court has not directly addressed the issue of attorney's fees for claims of conversion of collateral since *Permian*, this Court defers to the Fifth Circuit's *Permian* decision.

Under *Permian*'s holding, Lone Star may be entitled to attorney's fees for its conversion claims. *Permian* held that, "[u]nder Texas law, a secured party may recover as actual conversion damages the value of the secured interest in the collateral *up to the value of the collateral*." 934

F.2d at 652 (emphasis added).[9] Here, the collateral that Lone Star seeks to recover through its conversion claims are proceeds. But Lone Star can only recover such proceeds up to the amount of the debt owed to Lone Star. Thus, under *Permian*, Lone Star may recover its attorney's fees accrued after conversion if the amount of converted proceeds exceeds the debt owed Lone Star and, then, up to the amount of available proceeds. Because judgment has not been granted on all of Lone Star's conversion claims, it is not clear at this stage whether the value of the converted proceeds will exceed Lone Star's secured debt plus attorney's fees and costs. But that remains a possibility.

Lone Star also asserted a right to attorney's fees under TEX. CIV. PRAC. & REM. CODE §§ 37.009, 38.001 but abandoned those bases on summary judgment. Because the value of converted collateral may exceed the value of Lone Star's secured debt plus attorney's fees and costs, summary judgment should be denied both parties on Lone Star's claim for attorney's fees and costs.

H. Conclusions on Conversion

The Court finds that Rabo held the senior lien on the Beef Cattle. Lone Star therefore cannot recover for conversion of the proceeds of Cliff Hanger's sales of Beef Cattle, and summary judgment should be granted to Rabo on Lone Star's Beef-Cattle conversion claim. The Court cannot interpret the meaning of "payment in full" under the Intercreditor Agreement; it thus cannot determine if Lone Star's lien over the Offset Cattle was subordinated, and summary judgment should be denied both parties on Lone Star's Offset-Cattle conversion claim. The Court finds that Lone Star retained a senior lien on the Pasture Cattle and the Tyler-and-Tucker Cattle. The undisputed facts show that Rabo received direct payments for the sales of a portion

[9] There is language in *Permian* that allows for the recovery of prejudgment interest above the value of the collateral at conversion. *Permian*, 934 F.2d at 652. But that holding is limited to interest, not attorney's fees or costs.

of these cattle. Lone Star's first lien survived the sale of these cattle, and Lone Star may therefore recover on its conversion action the proceeds of those sales that were paid directly to Rabo. Summary Judgment should therefore be granted to Lone Star on its claim for conversion of the proceeds of Tyler-and-Tucker Cattle and Pasture Cattle sales where proceeds were paid directly to Rabo. Based on this holding, Lone Star should be granted judgment in the amount of $4,514,296.

Because the parties have presented competing experts, there are genuine issues of material fact on the tracing of proceeds that were deposited in Cliff Hanger's bank account and swept by Rabobank. Summary judgment should thus be denied both parties on Lone Star's conversion claims to the extent Lone Star seeks to recover proceeds that were swept from Cliff Hanger's account, as the issue of tracing must be determined by a trier of fact at trial.

VII. Rabo's Fraud-By-Nondisclosure Claim

Rabo's counterclaim alleges that Lone Star fraudulently induced Rabo into financing Cliff Hanger's operations and entering into the Intercreditor Agreement. Specifically, Rabo claims Lone Star committed fraud by nondisclosure by withholding certain information from Rabo that Lone Star had a duty to disclose. If Lone Star had disclosed certain information about the Waggoner Entities' financial condition, Rabo argues it would have never entered into the Intercreditor Agreement or funded its loan to Cliff Hanger and thus avoided the loss it has now accrued resulting from the Waggoner Entities' bankruptcies.

> To establish fraud by non-disclosure, the plaintiff must show: (1) the defendant deliberately failed to disclose material facts; (2) the defendant had a duty to disclose such facts to the plaintiff; (3) the plaintiff was ignorant of the facts and did not have an equal opportunity to discover them; (4) the defendant intended the plaintiff to act or refrain from acting based on the nondisclosure; and (5) the plaintiff relied on the non-disclosure, which resulted in injury.

Bombardier Aerospace Corp. v. SPEP Aircraft Holdings, LLC, 572 S.W.3d 213, 219–20 (Tex. 2019).

A. Duty

To establish fraud by nondisclosure, Rabo must prove that Lone Star had a duty to disclose certain facts to Rabo. *Id.* at 219. Generally, a duty to disclose only arises amid a confidential or fiduciary relationship. *Id* at 220. Rabo does not assert that Rabo and Lone Star were in such a relationship. But a duty to disclose may also arise when the defendant: "(1) discovered new information that made its earlier representation untrue or misleading; (2) made a partial disclosure that created a false impression; or (3) voluntarily disclosed some information, creating a duty to disclose the whole truth." *Id*. Rabo claims that at least one of these circumstances arose amid Rabo and Lone Star's relationship, which placed a duty of disclosure on Lone Star.

Before approval of Rabo's loan to Cliff Hanger, Lone Star had no substantive communications with Rabo. Pl's. Summ. J. Mot. Ex. 84. Between approval and funding, the only communications between Lone Star and Rabo were emails between Rabo's primary loan officer, Paul Strouhal, and Lone Star's primary loan officer, Bart Schilling, regarding the preparation of the Intercreditor Agreement. These emails consist of drafts of the Intercreditor Agreement and brief communications regarding proposed edits and a timeframe for drafting. Pl's. Summ. J. Mot. Ex. 85. Before Rabo funded its loan to Cliff Hanger, the Waggoner Entities did request numerous documents from Lone Star, and some of those documents were then forwarded by the Waggoner Entities to Rabo. But those documents were never disclosed to Rabo directly from Lone Star. In sum, no substantive information was ever communicated directly from Lone Star to Rabo. Pl's. Summ. J. Mot. Ex. 60. The emails, deposition transcripts,

and affidavits presented by Lone Star to support this conclusion have not been rebutted by Rabo with any contradictory evidence.

The emails and drafts of the Intercreditor Agreement sent from Lone Star to Rabo—Lone Star's only pre-funding communication with Rabo—did not create a false impression or disclose a partial truth. Rabo condemns Lone Star for failing to disclose the whole truth about its lending relationship with the Waggoner Entities. But "the 'whole truth' must relate to the same topic about which the information was voluntarily disclosed." *McKenzie v. Cmty. Cmty. Nat'l Bank*, No. 04-14-00540-CV, 2015 WL 3616601, at *3 (Tex. App.—San Antonio June 10, 2015, no pet.). The details of Lone Star's lending relationship with the Waggoner Entities had no relevance to the terms that Lone Star sought to be included in the Intercreditor Agreement. There is no evidence that supports the conclusion that Lone Star owed a duty of disclosure to Rabo before Rabo funded its loan to Cliff Hanger.

For the first time, Rabo argues in its response to Lone Star's motion for summary judgment that Lone Star's duty to disclose is actually contractual, arising from Paragraph 5 of the Intercreditor Agreement. But this legal theory is entirely different from the one posited by its counterclaim, where Rabo contended that Lone Star owed a duty of disclosure under common law, not contract.

Raising a new legal theory for the first time in a response to a summary judgment motion is improper and should not be considered by the Court. *See Dixon v. Ally Bank,* 853 F. App'x 977, 978 (5th Cir. 2021). Rabo's initial theory from its counterclaim was that Lone Star had a common-law duty to disclose certain information to Rabo before Rabo funded its loan to Cliff Hanger. For this theory, Rabo has presented no evidence in support, and Lone Star has presented uncontroverted evidence that such a duty was never owed.

Furthermore, even considering Rabo's late-raised argument, Rabo's counterclaim states that it suffered harm on account of the alleged nondisclosures because it would have never made the loan to Cliff Hanger *or entered into the Intercreditor Agreement* had the allegedly required disclosures been made. First, Rabo funded its loan to Cliff Hanger almost immediately after it signed the Intercreditor Agreement. It would be absurd to assert that the Intercreditor Agreement would have imposed on Lone Star a duty to disclose salient financial information in the brief window between signing of the Intercreditor Agreement and funding. And second, it is impossible that Lone Star, by following its duty under the Intercreditor Agreement, could have prevented Rabo from entering the Intercreditor Agreement *after it was already entered into and in force*. Rabo has thus failed to show Lone Star owed it a duty of disclosure under both its original and late-brought theories.

B. Equal Opportunity to Discover the Truth

To establish fraud by nondisclosure, Rabo must prove that it did not have an equal opportunity to discover the truth, which Lone Star allegedly withheld. *Bombardier*, 572 S.W.3d at 219. Most of the information that Rabo lists in its counterclaim as necessitating disclosure by Lone Star are subjective internal evaluations of the Waggoner Entities by Lone Star officers. First, Lone Star never had a duty to disclose its confidential subjective evaluations to Rabo. *See Callinan v. Lexicon Pharms., Inc.*, 479 F. Supp. 3d 379, 418 (S.D. Tex. 2020), *aff'd*, 858 F. App'x 162 (5th Cir. 2021). And second, the subjective evaluations were based on the same financial information that Rabo also received. Pl's. Summ. J. Mot. Ex. 60. Lone Star and Rabo both were in communication with the Waggoner Entities and requested financial information from them to assess the wisdom of funding their operations. Both parties were on equal footing to gain financial information from the Waggoner Entities, and both parties were equally capable

of forming subjective evaluations of that data. Furthermore, Lone Star's evaluations were largely based on industry-wide trends, of which Rabo was also aware. Pl's. Summ. J. Mot. Exs. 8, 19.

Rabo has presented no evidence refuting its equal opportunity to discover information about the Waggoner Entities or formulate subjective evaluations.

The uncontested evidence shows that Lone Star had no duty to disclose any information to Rabo, and Rabo had an equal opportunity to discover the truth regarding the Waggoner Entities' operations.[10] Therefore, as a matter of law, Lone Star did not commit fraud by nondisclosure against Rabo, and summary judgment should be granted in favor of Lone Star on Rabo's fraud-by-nondisclosure counterclaim.

VIII. Lone Star's Fraud Claim

Lone Star asserts that Rabo committed fraud by providing Lone Star with false information that induced Lone Star into continuing business as usual with the Waggoner Entities. Through such inducement, Lone Star alleges Rabo was able to continue to convert Lone Star's collateral. Lone Star alleges that without the false information presented to it, it would have ended its lending relationship with the Waggoner Entities, proactively protecting its interests from Rabo's bad acts. Lone Star alleges Rabo committed fraud by: (1) delivering false Cliff Hanger borrowing base reports to Lone Star; (2) having knowledge of false Waggoner Cattle borrowing base reports sent from the Waggoner Entities to Lone Star; (3) promising that Rabo

[10] Lone Star also argues that Rabo did not rely on any disclosures from Lone Star in funding its loan to Cliff Hanger. But the relevant inquiry is whether Rabo relied on Lone Star's *nondisclosures.* *Bombardier*, 572 S.W.3d at 219–20. Regardless, because Lone Star did not owe a duty to disclose and because Rabo had an equal opportunity to discover the truth, proving Rabo relied on Lone Star's nondisclosures is not essential for summary judgment to be granted in favor of Lone Star.

would "take out" Lone Star's loans to the Waggoner Entities; and (4) communicating misrepresentations to potential buyers of a syndicate interest in Rabo's loan to Cliff Hanger.

> To prevail on a fraud claim, a plaintiff must show: (1) the defendant "made a material representation that was false"; (2) the defendant "knew the representation was false or made it recklessly as a positive assertion without any knowledge of its truth;" (3) the defendant intended to induce the plaintiff to act upon the representation; and (4) the plaintiff actually and justifiably relied upon the representation and suffered injury as a result.

JPMorgan Chase Bank, N.A. v. Orca Assets G.P., L.L.C., 546 S.W.3d 648, 653 (Tex. 2018). Rabo argues that summary judgment should be granted in its favor dismissing Lone Star's fraud claim on several grounds.

A. Texas Statute of Frauds

Rabo told Lone Star that Rabo would purchase or "take out" Lone Star's loans to the Waggoner Entities. Lone Star alleges that Rabo made this representation fraudulently because Rabo made this promise when it knew it would never take out Lone Star's loan. Lone Star says that through this misrepresentation, Rabo induced Lone Star into continuing its relationship with the Waggoner Entities to the detriment of Lone Star and benefit of Rabo. Rabo now asserts that Lone Star is impermissibly using its fraud claim to, in effect, recover under an oral contract with Rabo to take-out Lone Star's loan. The statute of frauds prevents this, Rabo says.

> The Texas statute of frauds provides that:
>
> [A] promise by one person to answer for the debt, default, or miscarriage of another person … is not enforceable unless the promise or agreement, or a memorandum of it, is (1) in writing; and (2) signed by the person to be charged with the promise or agreement or by someone lawfully authorized to sign for him.

TEX. BUS. & COM. CODE § 26.01. The statute further provides that "[a] loan agreement in which the amount involved in the loan agreement exceeds $50,000 in value is not enforceable unless the agreement is in writing and signed by the party to be bound or by that party's authorized

representative." TEX. BUS. & COM. CODE § 26.02. Therefore, under the statute of frauds, any promise by Rabo to either answer for the Waggoner Entities' debt to Lone Star or provide a loan to the Waggoner Entities to pay-off the Waggoner Entities' debt to Lone Star would have to be in writing to be enforceable. The parties agree that no such writing exists.

The statute of frauds also prevents a plaintiff from using a fraud claim to enforce an otherwise unenforceable contract. *Haase v. Glazner*, 62 S.W.3d 795, 799 (Tex. 2001). Therefore, a plaintiff may not recover the benefit of an unenforceable bargain through a fraud claim, though it may still recover out-of-pocket damages. *Baylor Univ. v. Sonnichsen*, 221 S.W.3d 632, 636 (Tex. 2007). "The 'out of pocket' or 'reliance' measure of damages is the difference between the value paid and the value received and seeks to put the plaintiff in as good a position as he would have been had the contract (or misrepresentation) not been made." *Reed v. Carecentric Nat'l, LLC (In re Soporex, Inc.)*, 446 B.R. 750, 784 (Bankr. N.D. Tex. 2011) (citing *Aquaplex, Inc. v. Rancho La Valencia, Inc.*, 297 S.W.3d 768 (Tex. 2009)).

Lone Star cannot claim as damages the entirety of the Waggoner Entities' unpaid debt to Lone Star or the value of a takeout loan, as that would be its benefit-of-the-bargain damages. But, if successful on its fraud claim, it may still recover for economic losses it suffered in reliance on Rabo's promise, such as, potentially, the lost value of cattle transferred from Waggoner Cattle to Cliff Hanger, assuming Lone Star could have otherwise prevented those transfers, or the value of additional debts accrued after Rabo made its promise. Lone Star's complaint does not specify whether Lone Star seeks reliance damages exclusively or additional benefit-of-the-bargain damages. Pl.'s Third Am. Compl. at Section X ¶ 11. But because reliance damages are still potentially available to Lone Star, its "fraud claim may survive [Rabo's]

motion for summary judgment to the extent that [Lone Star] seeks to recover … out-of-pocket damages." *Haase*, 62 S.W.3d at 800.[11]

B. Misrepresentations Related to Syndication

Lone Star says, with supporting evidence, that once Rabo began to realize its loan to Cliff Hanger was at risk, it began attempts to syndicate the loan—that is, it sought out other lenders to purchase some or all of the Cliff Hanger loan. Lone Star alleges that Rabo committed fraud through its syndication efforts by (1) adjusting its loan covenants; and (2) falsifying its borrowing base reports. Lone Star says Rabo made these adjustments to make the Cliff Hanger loan appear more attractive to potential syndicate partners. The falsified borrowing base reports were shared with potential syndicate partners and Lone Star, and Lone Star asserts its reliance on these fraudulent misrepresentations caused it damage. Rabo now argues that the syndication-fraud claim must fail because it rests on misrepresentations made to third parties, not Lone Star. Lone Star's complaint says, "[t]he damage to Lone Star was a known consequence of Rabo's attempt to defraud prospective syndication partners." Pl.'s Third Am. Compl. ¶ 270. While not entirely clear, the complaint appears to rest its fraud claim on misrepresentations made to potential syndicate partners as well as Lone Star.

"[A] misrepresentation made through an intermediary is actionable if it is intended to influence a third person's conduct." *Ernst & Young, L.L.P. v. Pac. Mut. Life Ins. Co.*, 51 S.W.3d 573, 578 (Tex. 2001). "[A] person who makes a misrepresentation is liable to the person or class of persons the maker intends or 'has reason to expect' will act in reliance upon the misrepresentation." *Id.* (quoting RESTATEMENT (SECOND) OF TORTS § 531 (1977)). Lone Star

[11] Rabo also alleges that the statute of frauds bars Lone Star's fraud claim regarding the syndication attempts. But Lone Star never alleged in its complaint that Rabo entered into an agreement with Lone Star for syndication. The statute of frauds is therefore inapplicable to the syndication fraud claim, and summary judgment should not be granted on that claim on the basis of the statute of frauds.

has presented no evidence that Rabo intended for Lone Star to rely on its misrepresentations to potential syndicate partners or that Rabo had reason to expect Lone Star would rely on Rabo's third-party misrepresentations. To the extent Lone Star's fraud claim relies on third-party misrepresentations, summary judgment should therefore be granted to Rabo. But Lone Star's syndication-fraud claim also rests on the transmission of the allegedly fraudulent Cliff Hanger borrowing base reports sent directly from Rabo to Lone Star. To the extent Lone Star's fraud claim relies on such allegedly false Cliff Hanger borrowing base reports, summary judgment should be denied to Rabo.

C. Justifiable Reliance

To establish fraud, Lone Star must prove that it "justifiably relied" upon misrepresentations made by Rabo. *JPMorgan Chase Bank*, 546 S.W.3d at 653. Rabo argues that summary judgment should be granted in its favor on Lone Star's fraud claim because Lone Star, as a sophisticated lender in the business of making agricultural loans, could not have justifiably relied on any of the alleged misrepresentations made by Rabo.

"Justifiable reliance usually presents a question of fact. But the element can be negated as a matter of law when circumstances exist under which reliance cannot be justified." *Id*. at 654. In an arms-length transaction, each party is charged with exercising ordinary diligence in the protection of its interests. *Id*. "And when a party fails to exercise such diligence, it is 'charged with knowledge of all facts that would have been discovered by a reasonably prudent person similarly situated.'" *Id.* (quoting *AKB Hendrick, LP v. Musgrave Enterprises, Inc.*, 380 S.W.3d 221, 232 (Tex. App.—Dallas 2012, no pet.)). A party cannot justifiably rely on a representation if there are "red flags" indicating that reliance is unwarranted. *Id*. at 655. A party is held

responsible for ignoring "red flags" if "its knowledge, experience, and background called for further investigation." *Id*. at 657.

Rabo has presented no evidence of any "red flags" that should have caused Lone Star to investigate Rabo's claims, nor has it presented any evidence that shows Rabo's position as an agricultural lender warranted further investigation. It merely rests on blind assertions in its motion that Lone Star's sophistication and experience obligated it to investigate and verify the representations made by Rabo.

Lone Star, on the other hand, has presented evidence that shows Lone Star's reliance on Rabo's representations was reasonable. Bart Schilling, the primary loan officer for Lone Star, testified in his deposition that he knew Rabo was a sophisticated lender with broad experience with cattle financing and that Rabo had inspected Cliff Hanger's cattle. Schilling said that he accepted Rabo's representations based on that reputation. Pl's. Summ. J. Mot. Ex. 68 at 248, 320, 347–356. He also testified that there was nothing to indicate the borrowing base reports were false and he had never received reports that were false in the past. *Id*. at 319–320. Lone Star's expert, Pat McElroy, also testified that of the thousands of bank loans he had reviewed in his career, this was the first time he had encountered a bank falsifying a borrowing base report. Pl's. Summ. J. Mot. Ex. 123 at 220. This testimony in sum supports the position that Lone Star's reliance was reasonable and justified.

Lone Star is certainly a sophisticated lender, and Rabo may be correct that Lone Star's experience warranted further investigation of Rabo's claims. But Rabo has presented no evidence to support that contention, nor any evidence of "red flags" that would have put Lone Star on notice of potential misrepresentations. Lone Star has presented evidence of justifiable

reliance on its part. Rabo has failed to disprove the element of justifiable reliance, and summary judgment should be denied Rabo on such grounds.

D. Duty to Disclose

Rabo argues that, even if it knew the borrowing base reports sent to Lone Star were false, it had no duty to disclose that information to Lone Star. But a duty to disclose is only relevant to a fraud-*by-nondisclosure* claim. *Bombardier*, 572 S.W.3d at 219–20. Lone Star does not allege that Rabo withheld information that it had a duty to disclose; rather, it argues Rabo did disclose information that it knew was false. Knowledge, falsity, intent, and justifiable reliance are all that must be proven in a regular fraud claim; a "duty" is simply not an element of such claim. *See JPMorgan Chase Bank*, 546 S.W.3d at 653. Summary Judgment should therefore be denied on Rabo's claim that it owed no duty of disclosure to Lone Star.

E. Waggoner Cattle's Borrowing Base Reports

Lone Star asserts in its complaint that Rabo committed fraud because its officers must have known that the Waggoner Entities were providing Lone Star with fraudulent Waggoner Cattle borrowing base reports. But, unlike the Cliff Hanger borrowing base reports, Lone Star has not presented any evidence that Rabo played any role in the creation of the Waggoner Cattle borrowing base reports, nor any evidence that Rabo even knew the Waggoner Cattle borrowing base reports were false. Rather, both parties agree that it was the Waggoner Entities that created the Waggoner Cattle borrowing base reports and that the Waggoner Entities supplied the reports directly to Lone Star. An essential element of a fraud claim is that the defendant made a material misrepresentation. *Id*. Lone Star has presented no evidence that Rabo made a material misrepresentation to Lone Star through the Waggoner Cattle borrowing base reports. Summary

Judgment should be granted to Rabo dismissing Lone Star's fraud claim to the extent it relies on the transmission of Waggoner Cattle borrowing base reports.

F. Conclusions on Lone Star's Fraud Claim

Summary judgment should be granted in part and denied in part to Rabo on Lone Star's fraud claim. Lone Star's fraud claim should be barred to the extent it relies on misrepresentations made by Rabo to potential syndicate partners and to the extent Lone Star relies on misrepresentations in the Waggoner Cattle borrowing base reports. Lone Star should also be barred from recovering benefit-of-the-bargain damages. Summary judgment on all other bases related to Lone Star's fraud claim should be denied.

IX. Rabo's Claims for Conversion, Unjust Enrichment, and Breach of the Intercreditor Agreement

By its counterclaim, Rabo sues for conversion, unjust enrichment, and breach of the Intercreditor Agreement. Lone Star now seeks summary judgment on each of these claims. The claims are based on two premises: (1) Rabo's assertion that Cliff Hanger used proceeds of Rabo's collateral to overpay for cattle transferred from Waggoner Cattle to Cliff Hanger—both parties agree that some funds transferred from Cliff Hanger for Waggoner-Cattle cattle payments went to Lone Star, either directly from Cliff Hanger or through Waggoner Cattle; and (2) Rabo's assertion that some of the Cliff-Hanger overpayments that constituted Rabo's collateral were used by Waggoner Cattle to improve the Calf Ranch owned by Bugtussle. Lone Star held the senior lien on the Calf Ranch; therefore, Rabo's claims are also based on the argument that Lone Star wrongfully obtained the benefit of improvement of Lone Star's collateral—the Calf Ranch—with funds that constituted Rabo's collateral. This is a convoluted argument.

Rabo's claims for conversion, unjust enrichment, and breach of the Intercreditor Agreement should not be dismissed on summary judgment outright because Lone Star has not

refuted the first basis for Rabo's claims—that Lone Star received funds, either through Waggoner Cattle or directly from Cliff Hanger, that constituted Rabo's collateral. The ultimate determination of whether the funds were wrongfully paid to Lone Star through overpayments rests on the interpretation of "payment in full," which, as addressed above, the Court cannot decide here on summary judgment.

But Lone Star has attacked the factual allegations for Rabo's other basis for its claims—that funds constituting Rabo's collateral were used to improve Lone Star's collateral position. Lone Star has presented evidence that Quint Waggoner, independent of Lone Star, directed the Calf-Ranch improvements and that Lone Star did not have control over the Calf Ranch when the improvements were made. Pl's. Summ. J. Mot. Ex. 83 (Affidavit of Bart Schilling); Ex. 97 (Affidavit of Melisa Roberts). Lone Star has presented evidence that it did not receive the benefit of any improvements; the Calf Ranch was valued at $4,100,000 in February 2014, before Rabo began any funding to the Waggoner Entities, but Lone Star assigned its lien to another party in August 2019 for $2,800,000. *Id*. Ex. 97.

In response, Rabo presented no evidence showing that Lone Star's collateral position was improved through the use of Rabo's collateral, and merely asserts that a trier of fact should determine these issues. When a party "fails to make a showing sufficient to establish the existence of an element essential to that party's case, … there can be 'no genuine issue as to any material fact,' since a complete failure of proof concerning an essential element of the nonmoving party's case necessarily renders all other facts immaterial." *Celotex*, 477 U.S. at 322–23. Summary judgment should therefore be granted in Lone Star's favor on Rabo's claims for conversion, unjust enrichment, and breach of the Intercreditor Agreement to the extent they rely on the use of Rabo's collateral to improve Lone Star's collateral position.

X. Conclusion

Summary judgment should be granted in part and denied in part on both parties' causes of action for construction of the Intercreditor Agreement. The Court concludes for the Intercreditor Agreement:

- that Lone Star subordinated its senior lien on cattle (and their proceeds) to Rabo's lien against *all* cattle (and their proceeds) that satisfy both conditions of the Intercreditor Agreement's definition of Cliff Hanger Collateral—those cattle located on the Cliff Hanger Feedyards and related to Cliff Hanger's operations—including the cattle delivered from Waggoner Cattle to Cliff Hanger *and* paid for in full by Cliff Hanger.
- there are genuine issues of material fact that preclude the Court from determining that the term "payment in full" equals 75% of the Overland Auction Price.

Summary judgment should be granted in Lone Star's favor:

- finding that Lone Star held the senior lien on all cattle owned by Waggoner Cattle and by Cliff Hanger before the Intercreditor Agreement was entered into, that such lien continued in the proceeds realized upon the sales of those cattle, and that Rabo did not obtain a PMSI on cattle owned by the Waggoner Entities;
- holding that Lone Star retained its first lien on the Tyler-and-Tucker Cattle;
- on Lone Star's claim for conversion, to the extent Lone Star seeks to recover proceeds of the Tyler-and-Tucker Cattle and the Pasture Cattle that were paid to Rabo directly from feedyards; for these cattle, Lone Star should recover $4,514,296 from Rabo;
- on Rabo's claim for fraud by nondisclosure; and

- on Rabo's claims for breach of the Intercreditor Agreement, conversion, and unjust enrichment to the extent such causes rely on the use of Rabo's collateral to improve the Calf Ranch.

Summary judgment should be granted in Rabo's favor:

- on Lone Star's claim for conversion to the extent Lone Star seeks to recover proceeds of Beef Cattle; and
- on Lone Star's claim for fraud (i) to the extent Lone Star seeks benefit-of-the-bargain damages and (ii) to the extent it is based on misrepresentations by Rabo to potential syndicate partners and for misrepresentations within the Waggoner Cattle borrowing base reports.

All other grounds for summary judgment requested by the parties should be denied.

End of Memorandum Opinion