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CHAPTER 1: CREDITOR'S REMEDIES UNDER STATE LAW

ASSIGNMENT 1: REMEDIES OF UNSECURED CREDITORS UNDER STATE LAW

Who Is an Unsecured Creditor?

Creditor: Anyone owed a legal obligation that can be reduced to a money judgment.

Unsecured Creditor/General Creditor/Ordinary Creditor: Unless a creditor contracts with the debtor for secured status or is granted it by statute, they are an unsecured creditor.

Judgment Creditor: A creditor who has obtained a money judgment from a court. A money judgment *does not* convert an unsecured creditor to a secured creditor.

How Do Unsecured Creditors Compel Payment

Self-help: in most cases, a self-help remedy is not only prohibited but constitutes the tort of conversion.

Conversion: The wrongful exercise of dominion and control over another's property in denial of or inconsistent with his rights....A plaintiff need not establish that the defendant acted with a wrongful intent. The intent required is not necessarily a matter of conscious wrongdoing. It is rather an intent to exercise a dominion or control over the goods which is *in fact* inconsistent with the plaintiff's rights. *Winkle Chevy-Olds-Pontiac, Inc. v. Condon*.

Demand: The creditor has a right to demand payment, but if he does so in an unreasonable manner, he may be liable for wrongful collection practices.

Steps in the Collection Process

1. File a complaint and serve process.
2. Hearing (if in small claims) or the usual Civ Pro ridiculousness.

Vitale v. Hotel California, Inc.

Facts: Motion for writ of amercement.¹ Vitale had given writ of execution against the property of Hotel California, Inc. to the Sheriff, who made several excuses why it could not be delivered properly (ie the bar was only open late hours, it was dangerous, etc.) At one point, writ was executed and some money recovered plus some furniture. The furniture turned out not to be the property of HCI. Sheriff maintains that it is unreasonable to expect any sheriff to command his officers or deputies to "go forth on an unknown number of occasions, at an unreasonable hour, to seize the proceeds of an establishment such as The Fast Lane."

Issues:

1. Are successive levies possible under one writ of execution?
2. When may a sheriff refuse to levy as instructed by a plaintiff, on the basis that the request is unreasonable or onerous?
3. Was the conduct of Sheriff Lanzaro and his office in respect to the writ such as to subject him to amercement?

Rules:

1. The rule that further levies under one writ are authorized under the same writ before the return day if the initial levy does not satisfy the judgment is recognized universally.

¹ Writ of amercement: writ compelling a public official to pay over the money that should have been collected with a writ of execution for failing to properly execute the writ.

2. Practical operational considerations of a sheriff's office impose an obligation on a plaintiff not to request inordinately frequent and numerous levies. Levy under a writ of execution may be made at any hour of the day.
- 2a. When is physical force appropriate in making a levy?
[an] officer may force an entry into any enclosure except the dwelling house of the judgment debtor in order to levy a fieri facias² on the debtor's goods and even in the case of the debtor's home, when the officer is once inside, he may break open inner doors or trunks to come at the goods.
3. If a sheriff or acting sheriff fails to perform any duty imposed upon him by law in respect to writs of execution resulting in loss or damage to the judgment creditor, he shall be subject to amercement in the amount of such loss and damage to and for the use of the judgment creditor. Such amercement may be made by the court having jurisdiction of the judgment and proceedings for the enforcement thereof in an action or proceeding for amercement or in the nature of an amercement brought for the purpose. The court may proceed in a summary manner or otherwise. The delinquent sheriff or acting sheriff shall also be subject to attachment or punishment for contempt....plaintiff must clearly establish some default of duty.

Reasoning:

1. Had the sheriff returned the writ, the plaintiff would have been able to get an alias writ. Since an alias writ should not issue before the original execution is returned, and may be voidable as irregular if prematurely issued, the plaintiff was under no duty to seek an alias writ, the original writ not having been returned.
2. By extrapolation from the initial seizure, the sheriff might have had to go out nine times. This may be unusual but not by itself unreasonable. Further, seizure of several hundreds of dollars at the first levy demonstrates that it is effective.

Writ of Garnishment: Order forcing a debtor to the original debtor to turn funds over to creditor.

Limitations on Compelling Payments

Discovery: There is an obligation of the judgment creditor to use discovery to discover assets. The creditor has a right to demand information and the sheriff will only act on clear directions about what to get and where to get it. Converse: Creditors have no right to conduct a fishing expedition by showing up at the debtor's home or place of business with a sheriff.

Fraudulent transfers: All states have laws against transfers made simply to avoid payment of debt. This does not include payment of other creditors first or legitimate liquidations of assets. *Without violating any law, the debtor may lose the assets in business operations, exchange them for assets of reasonably equivalent value, or apply them to the payment of other bona fide debts.* **Preference: paying one creditor before another. Absent BK filing, such payments are irreversible.**

Provisional Remedies: Creditors may sometimes attach property that is being disposed of fraudulently. This is severely limited by Due Process and by statutory requirements for prejudgment attachment.

Exemptions (examples from Wis. Stat. § 815.18, 20, 990.01)

1. Provisions for burial.
2. Business and farm property.
Equipment, inventory, farm products and professional books used in the business of a dependent of the debtor, not to exceed \$7,500 in aggregate value.
3. Consumer goods.
Up to \$5000 in household goods.
4. Motor vehicles
Not to exceed \$1,200 in aggregate value. Unused consumer goods exemption may be added.

² Writ of execution

5. Net income.
75% of net income is exempt.
6. Depository Accounts
Up to \$1,000.

Homestead Exemption:

Up to \$40,000 except mortgages, laborers', mechanics' and purchase money liens, and taxes.

Exempt Homestead:

The dwelling, including a building, condominium, mobile home, house trailer, or cooperative and so much of the land surrounding it as is reasonably necessary for its use as a home, but not less than .25 acre, if available, and not exceeding 40 acres.

Wages:

75% of wages for personal services exempt under 15 U.S.C. § 1671. Some states exempt more, FL, TX, PA exempt all.

Fraudulent Transfers

1. Any transfer made with actual intent to hinder, delay, or defraud any creditor. UFTA § 4(a).
2. Any transfer made without receiving a reasonably equivalent value in exchange for the transfer if the debtor was insolvent at the time of the transfer. § 5(a).

Largely impotent. A subsequent transfer to a bona fide purchaser. Remedy is then limited to the debtor and initial transferee as an unsecured claim.

ASSIGNMENT 3: REPOSSESSION OF COLLATERAL

The Importance of Possession Pending Foreclosure

Who has possession of collateral until equity of redemption has been foreclosed?

Creditor View

1. Debtor whose rights in the collateral are extinguished has little incentive to preserve its economic value.
2. The use of the collateral has economic value in itself—why should the debtor be able to extract that value?
3. Collateral in the possession of the debtor is difficult for potential buyers to evaluate.

Debtor View

1. Haven't had their day in court yet.
2. Foreclosure is a legal safeguard to protect from wrongful repossession.

Strategic value of repossession

May use leverage to:

1. Force changes in the relationship
2. Raise the rate of interest.
3. Demand additional collateral.
4. Require waiver of a cause of action

The Right to Possession Pending Foreclosure—Personal Property

UCC § 9-609: Secured Party's Right to Take Possession after Default. Gives right to take possession of the collateral-	(a) [Possession; rendering equipment unusable; disposition on debtor's premises.] After default, a secured party : (1) may take possession of the collateral; and (2) without removal, may render equipment unusable and dispose
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may repossess without court action so long as the peace is not breached. If debtor resists, then file for a writ of replevin.	<p>of collateral on a debtor's premises under Section 9-610.</p> <p>(b) [Judicial and nonjudicial process.] A secured party may proceed under subsection (a):</p> <p>(1) pursuant to judicial process; or</p> <p>(2) without judicial process, if it proceeds without breach of the peace.</p> <p>(c) [Assembly of collateral.] If so agreed, and in any event after default, a secured party may require the debtor to assemble the collateral and make it available to the secured party at a place to be designated by the secured party which is reasonably convenient to both parties.</p>
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Writ of Replevin:

Issued if it is likely that the creditor will win his civil case against the debtor. The writ is usually conditioned on issuance of a bond by the creditor in the event that the debtor prevails in court.

<p>UCC § 9-610: Disposition of Collateral after Default</p> <p>Provides for disposal of repossessed collateral through “commercially reasonable” methods.</p>	<p>(a) [Disposition after default.] After default, a secured party may sell, lease, license, or otherwise dispose of any or all of the collateral in its present condition or following any commercially reasonable preparation or processing.</p> <p>(b) [Commercially reasonable disposition.] Every aspect of a disposition of collateral, including the method, manner, time, place, and other terms, must be commercially reasonable. If commercially reasonable, a secured party may dispose of collateral by public or private proceedings, by one or more contracts, as a unit or in parcels, and at any time and place and on any terms.</p> <p>(c) [Purchase by secured party.] A secured party may purchase collateral:</p> <p>(1) at a public disposition; or</p> <p>(2) at a private disposition only if the collateral is of a kind that is customarily sold on a recognized market or the subject of widely distributed standard price quotations.</p> <p>(d) [Warranties on disposition.] A contract for sale, lease, license, or other disposition includes the warranties relating to title, possession, quiet enjoyment, and the like which by operation of law accompany a voluntary disposition of property of the kind subject to the contract.</p> <p>(e) [Disclaimer of warranties.] A secured party may disclaim or modify warranties under subsection (d):</p> <p>(1) in a manner that would be effective to disclaim or modify the warranties in a voluntary disposition of property of the kind subject to the contract of</p>
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	<p>disposition; or (2) by <u>communicating</u> to the purchaser a <u>record</u> evidencing the contract for disposition and including an express disclaimer or modification of the warranties.</p> <p>(f) [Record sufficient to disclaim warranties.] A <u>record</u> is sufficient to disclaim warranties under subsection (e) if it indicates "There is no warranty relating to title, possession, quiet enjoyment, or the like in this disposition" or uses words of similar import.</p>
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The Article 9 Right to Self-Help Repossession

Use of available judicial procedures is **often mandatory**.

Self-help:

§ 9-609(a)(1) allows self-help repossession if the creditor holds an Article 9 security interest.

Many security agreements require that the debtor turn collateral over on default, but most debtors don't.

Secured creditor COULD file a lawsuit, but much faster to just take the collateral.

The courts generally hold that the duty to refrain from breaching the peace is *non-delegable*, making the secured creditor liable for the consequences of illegal repossession tactics by independent contractors.

The Limits of Self-Help: Breach of the Peace

§ 9-609(b)(2) forbids breach of the peace in a repossession.

Salisbury Livestock Co. v. Colorado Central Credit Union

Facts: CCCU lent money to Young Salisbury. YS defaulted and CCCU sent repossessioners after the collateral. Repo men took some of the vehicles from a ranch owned by Salisbury Livestock Company, a corporation run by Old Salisbury. The vehicles were taken just after dawn from an outdoor area next to the ranch house. No advance notice given to SL, encountered no resistance or opposition. SL sued CCCU for wrongful repossession.

Issue: Whether the entry to repossess was privileged either by the self-help statute or by consent (this is a motion for summary judgment, so standard is whether a reasonable jury could conclude its not.)

Rule: Two primary factors for Breach of Peace: 1. Potential for immediate violence and 2. Nature of the premises intruded on. Use R(2) Torts § 198 reasonableness "If there was no confrontation and the timing and manner, including notice and lack of notice, are found to be reasonable, the entry is privileged. § 198 cmt. d no demand necessary if it would be futile, but there must be a determination if it would have been futile.

Holding: CCCU's actions were in breach of peace.

Reasoning: Entry on to the premises of a third party not privy to the loan agreement. When entry onto third party property is coupled with the second unusual element, the location and setting of this repossession, the possibility of a [breach of the peace] becomes more apparent.

Breaches of the Peace

Walker v. Walthall: Police officer went with creditor to repossess collateral. With officer present, debtor consented to the repossession. Even though the officer said nothing, this was a breach of the peace due to the implied threat of police action.

Morris v. First National Bank & Trust Co.: Three men surrounded debtor's son after he objected to the repossession. He then gave up protest in fear of physical harm. Creditor's agents failed to desist in repossession efforts in the face of clear requests to stop.

Marcus v. McCollum: Marcuses "argued loudly" with reposessor. Repossessor beckoned a cop over, who told the Marcuses to "keep [their] mouth shut, go back in the house, or [they] would indeed go to jail that day. *Police officers cross the line if they affirmatively intervene to aid the reposessor...the plaintiff's resistance to the taking of his property need not be strong. The general rule is that a debtor's request for the financier to leave the car alone must be obeyed. Even polite reposseors breach the peace if they meet resistance from the debtor. If a breach of peace occurs, self-help repossession is statutorily prohibited.*

Laurel Coal Co. v. Walter E. Heller & Co.: Cutting a lock at the debtor's place of business to repossess a bulldozer was a breach of the peace because it left \$350,000 of equipment unsecured and unprotected overnight.

Not Breaches of the Peace

Wallace v. Chrysler Credit Corp: Repossessors followed debtor to Big Stone Gap, VA. At 2:00am, reposessor entered truck, gunned engine, barreled out of the driveway and down the street. The debtors claimed they did not object because they didn't know what was happening and were in a state of fear. No cause of action, because the stealthy manner in which the repossession took place lessened the chance of a confrontation-not a breach of the peace.

Williams v. Ford Motor Credit Co: Woman came out and argued with reposseors when they were driving away. They blocked her from getting in to the vehicle and gave her personal possessions back.

Wade v. Ford Motor Credit Co: On first repossession attempt, the debtor ordered the reposessor off the premises, said she had a gun and would use it if he came back. No confrontation. Debtor did not know the car was being taken until the reposessor had safely departed with it. Despite the previously-communicated threat, no breach of the peace.

K.B. Oil Co. v. Ford Motor Credit Co., Inc: Fraudulent misrepresentation to gain possession of the collateral does not breach the peace.

Self-Help Against Accounts as Collateral

<p>UCC § 9-607</p>	<p>(a) [Collection and enforcement generally.] If so agreed, and in any event after default, a secured party: (1) may notify an account debtor or other person obligated on collateral to make payment or otherwise render performance to or for the benefit of the secured party; (2) may take any proceeds to which the secured party is entitled under Section 9-315; (3) may enforce the obligations of an account debtor or other person obligated on collateral and exercise the rights of the debtor with respect to the obligation of the account debtor or other person obligated on collateral to make payment or otherwise render performance to the debtor, and with respect to any property that secures the obligations of the account debtor or other person obligated on the collateral; (4) if it holds a security interest in a deposit account perfected by control under Section 9-104(a)(1), may apply the balance of the deposit account to the obligation secured by the deposit account; and (5) if it holds a security interest in a deposit account perfected by control under Section 9-104(a)(2) or (3), may instruct the bank to pay the balance of the deposit account to or for the benefit of the secured party.</p> <p>(b) [Nonjudicial enforcement of mortgage.] If necessary to enable a secured party to exercise under subsection (a)(3) the right of a debtor to enforce a mortgage nonjudicially, the secured party may record in the office in which a record of the mortgage is recorded: (1) a copy of the security agreement that creates or provides for a security interest in the obligation secured by the mortgage; and (2) the secured party's sworn affidavit in recordable form stating that: (A) a default has occurred; and (B) the secured party is entitled to enforce the mortgage nonjudicially.</p> <p>(c) [Commercially reasonable collection and enforcement.] A secured party shall proceed in a commercially reasonable manner if the secured party: (1) undertakes to collect from or enforce an obligation of an account debtor or other person obligated on collateral; and (2) is entitled to charge back uncollected collateral or otherwise to full or limited recourse against the debtor or secondary obligor.</p> <p>(d) [Expenses of collection and enforcement.] A secured party may deduct from the collections made pursuant to subsection (c) reasonable expenses of collection and enforcement, including reasonable attorney's fees and legal expenses incurred by the secured party.</p> <p>(e) [Duties to secured party not affected.] This section does not determine whether an account debtor, bank, or other person obligated on collateral owes a duty to a secured party.</p>
<p>UCC § 9-406</p>	<p>(a) [Discharge of account debtor; effect of notification.] Subject to subsections (b) through (i), an account debtor on an account, chattel paper, or a payment intangible may discharge its obligation by paying the assignor until, but not after, the</p>

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ASSIGNMENT 4: JUDICIAL SALE AND DEFICIENCY

“Equity abhors a forfeiture.”

Article 9 Foreclosure is very rare.

Strict Foreclosure

No sale is required

Examples: Contract for Deed or Installment Land Contract

Contract for Deed

Seller must foreclose through the courts, but a majority of states do not require that the foreclosure conclude with a sale of the property.

Foreclosure Sale Procedure

Typically specified by statute.

If high bidder doesn’t make good, may either require the property be sold to the second-highest bidder or a new sale be conducted.

In most foreclosures, the court must review the circumstance and judicially confirm the sale before consummation.

If proceeds of sale less than debt, then the court may enter a deficiency judgment.

ASSIGNMENT 5: ARTICLE 9 SALE AND DEFICIENCY

Sales under Article 9 determine the value of the collateral and convert it to cash.

The requirement that the collateral be offered for sale as part of the personal property foreclosure process cannot be waived or varied in the initial lending contract.

UCC § 9-602	Except as otherwise provided in Section 9-624 , to the extent that they give rights to a debtor or obligor and impose duties on a secured party , the debtor or obligor may not waive or vary the rules stated in the following listed sections:
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Acceptance of Collateral

UCC §9-620	<p>(a) [Conditions to acceptance in satisfaction.]</p> <p>Except as otherwise provided in subsection (g), a secured party may accept collateral in full or partial satisfaction of the obligation it secures only if:</p> <p>(1) the debtor consents to the acceptance under subsection (c);</p> <p>(2) the secured party does not receive, within the time set forth in subsection (d), a notification of objection to the proposal authenticated by:</p> <p>(A) a person to which the secured party was required to send a proposal under Section 9-621; or</p> <p>(B) any other person, other than the debtor, holding an interest in the collateral subordinate to the security interest that is the subject of the proposal;</p> <p>(3) if the collateral is consumer goods, the collateral is not in the possession of the debtor when the debtor consents to the acceptance; and</p> <p>(4) subsection (e) does not require the secured party to dispose of the collateral or the debtor waives the requirement pursuant to Section 9-624.</p>
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	<p>(b) [Purported acceptance ineffective.] A purported or apparent acceptance of collateral under this section is ineffective unless:</p> <p>(1) the secured party consents to the acceptance in an authenticated record or sends a proposal to the debtor; and</p> <p>(2) the conditions of subsection (a) are met.</p> <p>(c) [Debtor's consent.] For purposes of this section:</p> <p>(1) a debtor consents to an acceptance of collateral in partial satisfaction of the obligation it secures only if the debtor agrees to the terms of the acceptance in a record authenticated after default; and</p> <p>(2) a debtor consents to an acceptance of collateral in full satisfaction of the obligation it secures only if the debtor agrees to the terms of the acceptance in a record authenticated after default or the secured party:</p> <p>(A) sends to the debtor after default a proposal that is unconditional or subject only to a condition that collateral not in the possession of the secured party be preserved or maintained;</p> <p>(B) in the proposal, proposes to accept collateral in full satisfaction of the obligation it secures; and</p> <p>(C) does not receive a notification of objection authenticated by the debtor within 20 days after the proposal is sent.</p> <p>(d) [Effectiveness of notification.] To be effective under subsection (a)(2), a notification of objection must be received by the secured party:</p> <p>(1) in the case of a person to which the proposal was sent pursuant to Section 9-621, within 20 days after notification was sent to that person; and</p> <p>(2) in other cases:</p> <p>(A) within 20 days after the last notification was sent pursuant to Section 9-621; or</p> <p>(B) if a notification was not sent, before the debtor consents to the acceptance under subsection (c).</p> <p>(e) [Mandatory disposition of consumer goods.] A secured party that has taken possession of collateral shall dispose of the collateral pursuant to Section 9-610 within the time specified in subsection (f) if:</p> <p>(1) 60 percent of the cash price has been paid in the case of a purchase-money security interest in consumer goods; or</p> <p>(2) 60 percent of the principal amount of the obligation secured has been paid in the case of a non-purchase-money security interest in consumer goods.</p> <p>(f) [Compliance with mandatory disposition requirement.] To comply with subsection (e), the secured party shall dispose of the collateral:</p> <p>(1) within 90 days after taking possession; or</p> <p>(2) within any longer period to which the debtor and all secondary obligors have agreed in an agreement to that effect entered into and authenticated after default.</p> <p>(g) [No partial satisfaction in consumer transaction.] In a consumer transaction, a secured party may not accept collateral in partial satisfaction of the obligation it secures.</p>
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After a default has occurred, the debtor can consent to the secured party retaining the collateral in full or partial satisfaction of the obligation it secures. UCC §9-620(c)(2) implies consent if the secured party sends the debtor a proposal for retention of the collateral in full satisfaction and does not receive *written* notification of objection to the proposal within 20 days.

Subject to Four Conditions:

1. No objection from others holding liens against the collateral § 9-620(a)(2).
2. No acceptance in partial satisfaction in a consumer transaction. § 9-620(g).
3. If the collateral is consumer goods, the debtor can consent to strict foreclosure only after repossession. § 9-620(a).
4. If the debtor has paid 60% of cash price or the original loan amount, the creditor must dispose of the collateral within 90 days (or longer if by agreement) § 9-620(e)

Sale Procedure under Article 9

UCC 9-610 governs the procedure for sale of the collateral.

UCC § 9-610	<p>(a) [Disposition after default.] After default, a secured party may sell, lease, license, or otherwise dispose of any or all of the collateral in its present condition or following any commercially reasonable preparation or processing.</p> <p>(b) [Commercially reasonable disposition.] Every aspect of a disposition of collateral, including the method, manner, time, place, and other terms, must be commercially reasonable. If commercially reasonable, a secured party may dispose of collateral by public or private proceedings, by one or more contracts, as a unit or in parcels, and at any time and place and on any terms.</p> <p>(c) [Purchase by secured party.] A secured party may purchase collateral: (1) at a public disposition; or (2) at a private disposition only if the collateral is of a kind that is customarily sold on a recognized market or the subject of widely distributed standard price quotations.</p> <p>(d) [Warranties on disposition.] A contract for sale, lease, license, or other disposition includes the warranties relating to title, possession, quiet enjoyment, and the like which by operation of law accompany a voluntary disposition of property of the kind subject to the contract.</p> <p>(e) [Disclaimer of warranties.] A secured party may disclaim or modify warranties under subsection (d): (1) in a manner that would be effective to disclaim or modify the warranties in a voluntary disposition of property of the kind subject to the contract of disposition; or (2) by communicating to the purchaser a record evidencing the contract for disposition and including an express disclaimer or modification of the warranties.</p> <p>(f) [Record sufficient to disclaim warranties.] A record is sufficient to disclaim warranties under subsection (e) if it indicates "There is no warranty relating to title, possession, quiet enjoyment, or the like in this disposition" or uses words of similar import.</p>
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The foreclosing creditor has a duty to the debtor to choose a procedure for sale that is commercially reasonable.

The UCC sale procedure is directed towards getting a good price for the collateral.

UCC § 9-623 incorporates the common-law right to redeem. Redemption is accomplished by paying the full amount of the debt, including the secured creditor's attorneys fees and expenses of sale. *NO ADDITIONAL STATUTORY RIGHT TO REDEEM EXISTS UNDER THE UCC-SO NO POST-SALE RIGHT TO REDEEM*

Even if the sale is "commercially unreasonable" the debtor's only relief is money damages. The BFP is protected.

UCC § 9-623	<p>(a) [Persons that may redeem.] A <u>debtor</u>, any <u>secondary obligor</u>, or any other <u>secured party</u> or lienholder may redeem collateral.</p> <p>(b) [Requirements for redemption.] To redeem collateral, a person shall tender: (1) fulfillment of all obligations secured by the collateral; and (2) the reasonable expenses and attorney's fees described in Section <u>9-615(a)(1)</u>.</p> <p>(c) [When redemption may occur.] A redemption may occur at any time before a <u>secured party</u>: (1) has collected collateral under Section <u>9-607</u>; (2) has disposed of collateral or entered into a contract for its disposition under Section <u>9-610</u>; or (3) has accepted collateral in full or partial satisfaction of the obligation it secures under Section <u>9-622</u>.</p>
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These procedures are used whether the creditor obtained possession through replevin or self-help repossession.

Injuries to Debtors Resulting from Insufficient Price Article 9 Sales

1. If the debtor has any equity, it may be forfeited in an insufficient sale. Few debtor's sue over these losses:
 - a) Didn't have equity to begin with.
 - b) Don't have resources to pursue the suit.
 - c) Suit has negative expected value.
2. If the debtor doesn't have equity, there could be a deficiency judgment more than is appropriate.
UCC § 9-615(d): General rule that the debtor is responsible for any deficiency balance.
 - A) UCC § 9-615(f) applies when the secured party buys the collateral. The amount that would have been realized at a complying sale to a third party is treated as the sales price.
 - B) UCC § 9-626(a)(3) applies when the sale does not comply with the requirements of Article 9. The deficiency balance is treated as it would have been if the sale had been a complying sale.

Much more common to litigate these because creditors initiate the suit to recover. They're in better financial condition and they're repeat players.

Typical defenses:

 1. Asserting creditor retained the collateral rather than conducting a sale.
 2. Creditor did not give proper notice of sale.
 3. Creditor conducted the sale in a manner that was not commercially reasonable.

Problems with Article 9 Sale Procedure

Failure to Sell the Collateral

UCC § 9-610(a): a secured party *may* sell the collateral after default, but no provision that they *must* sell the collateral, and other than the § 9-620(f) 90-day requirement for consumer goods no time limit.

Why not sell the collateral?

1. Perhaps the repossession will spur the debtor to cure.
2. Law or regulation might prohibit resale (ex: alcoholic beverages)
3. Simple procrastination.

Issues:

1. Was the creditor attempting to accept the collateral without the debtor's consent? If so, the court can order a sale or award damages for noncompliance. UCC §§9-625(a)-(b).
2. If the secured party was proceeding to sale, was it doing so in a commercially reasonable manner? If not, look to § 9-626(a).

Notice of Sale

UCC § 9-611	<p>(a) ["Notification date."] In this section, "notification date" means the earlier of the date on which:</p> <ol style="list-style-type: none">(1) a <u>secured party</u> <u>sends</u> to the <u>debtor</u> and any <u>secondary obligor</u> an <u>authenticated</u> notification of disposition; or(2) the <u>debtor</u> and any <u>secondary obligor</u> waive the right to notification. <p>(b) [Notification of disposition required.] Except as otherwise provided in subsection (d), a <u>secured party</u> that disposes of collateral under Section <u>9-610</u> shall <u>send</u> to the persons specified in subsection (c) a reasonable <u>authenticated</u> notification of disposition.</p> <p>(c) [Persons to be notified.] To comply with subsection (b), the <u>secured party</u> shall <u>send</u> an <u>authenticated</u> notification of disposition to:</p> <ol style="list-style-type: none">(1) the <u>debtor</u>;(2) any <u>secondary obligor</u>; and(3) if the collateral is other than <u>consumer goods</u>: <p>(A) any other person from which the secured party has received, before the notification date, an <u>authenticated</u> notification of a claim of an interest in the collateral;</p> <p>(B) any other secured party or lienholder that, 10 days before the notification date, held a security interest in or other lien on the collateral perfected by the filing of a <u>financing statement</u> that:</p> <ol style="list-style-type: none">(i) identified the collateral;(ii) was indexed under the <u>debtor's</u> name as of that date; and(iii) was filed in the office in which to file a financing statement against the <u>debtor</u> covering the collateral as of that date; and <p>(C) any other secured party that, 10 days before the notification date, held a security interest in the collateral perfected by compliance with a statute, regulation, or treaty described in Section <u>9-311(a)</u>.</p> <p>(d) [Subsection (b) inapplicable: perishable collateral; recognized market.] Subsection (b) does not apply if the collateral is perishable or threatens to decline speedily in value or is of a type customarily sold on a recognized market.</p> <p>(e) [Compliance with subsection (c)(3)(B).] A <u>secured party</u> complies with the requirement for notification prescribed by subsection (c)(3)(B) if:</p> <ol style="list-style-type: none">(1) not later than 20 days or earlier than 30 days before the notification date, the secured party requests, in a commercially reasonable manner, information concerning <u>financing statements</u> indexed under the <u>debtor's</u> name in the office indicated in subsection (c)(3)(B); and(2) before the notification date, the secured party: <ol style="list-style-type: none">(A) did not receive a response to the request for information; or(B) received a response to the request for information and sent an <u>authenticated</u> notification of disposition to each secured party or other lienholder named in that response whose <u>financing statement</u> covered the collateral.
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Secured party must send notice to the debtor, guarantors, and some lienors. To identify lienors, may have to conduct a search of the public records. Failure to give this notice does not invalidate the sale (§9-617) but is a defect that may reduce the amount of deficiency.

Commercially Reasonable Sale

UCC § 9-610(b) requires that every aspect of a disposition of collateral be reasonable, including the method, manner, time, place and other terms. This is deliberately vague. It means a method

that reasonable owners of the particular type of property would use if their own money was at stake.

Chavers v. Frazier

Facts:	The Chavers repossessed a Lear jet from the Frazier group and claimed a \$400,000 deficiency judgment. The jet was sold to Frazier for \$850,000 3/1985 and sold 4/1986 for \$415,000. The only advertising done for the auction was from 5/20/1986 to 5/29/1986. The ads ran briefly in the Wall Street Journal and Trade-a-Plane. The ads were for a distress sale. Very little information was provided to potential buyers, not even including a log book summary or a copy of the log book. No hot section inspection was performed, which expert witness testimony established was an important part of preparing an aircraft for sale. The price obtained was very low in comparison to what was expected.
Rule:	Although failure to procure the best price for collateral does not in and of itself make a sale commercially unreasonable, and reasonableness is primarily assessed by the procedures employed, a sufficient resale price is the logical focus of the protection given debtors.
Holding:	The hasty sale was unreasonable. The advertising was not adequate. A distress sale auction was not reasonable. The preparation for sale was not reasonable. The purchase price was not reasonable.

UCC §9-626(a)(4): If the secured party fails to give reasonable notice of the sale or to conduct the sale in a commercially reasonable manner, there is a rebuttable presumption that the value of the collateral was at least equal to the amount of the debt.	For purposes of paragraph (3)(B), the amount of <u>proceeds</u> that would have been realized is equal to the sum of the secured obligation, expenses, and attorney's fees unless the secured party proves that the amount is less than that sum.
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Appropriate Remedy for Failure to Give Notice of Sale or Failure to Conduct Sale in a Commercially Reasonable Manner

Majority Rule: Rebuttable presumption that the value of the collateral was *at least* equal to the debt, with the court setting what the sale price would have been if the debtor objects to the amount of the debt.

Minority Rule: Denies any deficiency.

Article 9 Sale Procedure: A Functional Analysis

Because Article 9 preserves both the debtor's right to the surplus and the creditor's right to a deficiency, it is the debtor who directly suffers the effects of a poorly conducted sale that brings a low price.

CHAPTER 2: CREDITOR'S REMEDIES IN BANKRUPTCY

ASSIGNMENT 6: BANKRUPTCY AND THE AUTOMATIC STAY

The Federal Bankruptcy System

Discharge:	The permanent forgiveness of debt through bankruptcy.
Extension:	Rescheduling of payment.
The Code:	Title 11 of the US Code, the Bankruptcy Reform Act of 1978

Filing a Bankruptcy Case

File in PACER (<http://pacer.psc.uscourts.gov>)

Bankruptcy Estate is created

Stay against any collection activities is automatically imposed.

BKC § 362(a)	<p>(a) Except as provided in subsection (b) of this section, a petition filed under section 301, 302, or 303 of this title, or an application filed under section 5(a)(3) of the Securities Investor Protection Act of 1970, operates as a stay, applicable to all entities, of--</p> <p>(1) the commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case under this title, or to recover a claim against the debtor that arose before the commencement of the case under this title;</p> <p>(2) the enforcement, against the debtor or against property of the estate, of a judgment obtained before the commencement of the case under this title;</p> <p>(3) any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate;</p> <p>(4) any act to create, perfect, or enforce any lien against property of the estate;</p> <p>(5) any act to create, perfect, or enforce against property of the debtor any lien to the extent that such lien secures a claim that arose before the commencement of the case under this title;</p> <p>(6) any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the case under this title;</p> <p>(7) the setoff of any debt owing to the debtor that arose before the commencement of the case under this title against any claim against the debtor; and</p> <p>(8) the commencement or continuation of a proceeding before the United States Tax Court concerning a corporate debtor's tax liability for a taxable period the bankruptcy court may determine or concerning the tax liability of a debtor who is an individual for a taxable period ending before the date of the order for relief under this title.</p>
BKC § 541(a)(1)	<p>(a) The commencement of a case under section 301, 302, or 303 of this title creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held:</p> <p>(1) Except as provided in subsections (b) and (c)(2) of this section, all legal or equitable interests of the debtor in property as of the commencement of the case.</p>

Chapter 7

The debtor surrenders all non-exempt assets to a bankruptcy trustee and receives a discharge of all dischargeable debts.

Majority Rule: Exempt property is the same as is exempt from execution under state law.

Minority Rule: May choose between state exemptions and the list of exemptions in §522(d)

BKC § 522(d)	<p>(d) The following property may be exempted under subsection (b)(2) of this section:</p> <p>(1) The debtor's aggregate interest, not to exceed \$21,625¹ in value, in real property or personal property that the debtor or a dependent of the debtor uses as a residence, in a cooperative that owns property that the debtor or a dependent of the debtor uses as a residence, or in a burial plot for the debtor or a dependent of the debtor.</p> <p>(2) The debtor's interest, not to exceed \$3,450¹ in value, in one motor vehicle.</p> <p>(3) The debtor's interest, not to exceed \$550¹ in value in any particular item or \$11,525¹ in aggregate value, in household furnishings, household goods, wearing apparel, appliances, books, animals, crops, or musical instruments, that are held primarily for the personal, family, or household use of the debtor or a dependent of the debtor.</p> <p>(4) The debtor's aggregate interest, not to exceed \$1,450¹ in value, in jewelry held primarily for the personal, family, or household use of the debtor or a dependent of the debtor.</p> <p>(5) The debtor's aggregate interest in any property, not to exceed in value \$1,150¹ plus up to \$10,825¹ of any unused amount of the exemption provided under paragraph (1) of this subsection.</p> <p>(6) The debtor's aggregate interest, not to exceed \$2,175¹ in value, in any implements,</p>
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	<p>professional books, or tools, of the trade of the debtor or the trade of a dependent of the debtor.</p> <p>(7) Any unmatured life insurance contract owned by the debtor, other than a credit life insurance contract.</p> <p>(8) The debtor's aggregate interest, not to exceed in value \$11,525¹ less any amount of property of the estate transferred in the manner specified in section 542(d) of this title, in any accrued dividend or interest under, or loan value of, any unmatured life insurance contract owned by the debtor under which the insured is the debtor or an individual of whom the debtor is a dependent.</p> <p>(9) Professionally prescribed health aids for the debtor or a dependent of the debtor.</p> <p>(10) The debtor's right to receive--</p> <p>(A) a social security benefit, unemployment compensation, or a local public assistance benefit;</p> <p>(B) a veterans' benefit;</p> <p>(C) a disability, illness, or unemployment benefit;</p> <p>(D) alimony, support, or separate maintenance, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor;</p> <p>(E) a payment under a stock bonus, pension, profitsharing, annuity, or similar plan or contract on account of illness, disability, death, age, or length of service, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor, unless--</p> <p>(i) such plan or contract was established by or under the auspices of an insider that employed the debtor at the time the debtor's rights under such plan or contract arose;</p> <p>(ii) such payment is on account of age or length of service; and</p> <p>(iii) such plan or contract does not qualify under section 401(a), 403(a), 403(b), or 408 of the Internal Revenue Code of 1986.</p> <p>(11) The debtor's right to receive, or property that is traceable to--</p> <p>(A) an award under a crime victim's reparation law;</p> <p>(B) a payment on account of the wrongful death of an individual of whom the debtor was a dependent, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor;</p> <p>(C) a payment under a life insurance contract that insured the life of an individual of whom the debtor was a dependent on the date of such individual's death, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor;</p> <p>(D) a payment, not to exceed \$21,625,¹ on account of personal bodily injury, not including pain and suffering or compensation for actual pecuniary loss, of the debtor or an individual of whom the debtor is a dependent; or</p> <p>(E) a payment in compensation of loss of future earnings of the debtor or an individual of whom the debtor is or was a dependent, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor.</p> <p>(12) Retirement funds to the extent that those funds are in a fund or account that is exempt from taxation under (hidden) section 401, 403, 408, 408A, 414, 457, or 501(a) of the Internal Revenue Code of 1986.</p>
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Chapter 11:

The debtor nearly always retains possession of the property of the estate. The debtor continues to run the business and manage his financial affairs. The debtor proposes a plan to restructure the debt. Chapter 11 allows cramdown.

Cramdown: A creditor is forced to accept a restructuring plan even if they vote no. May occur if the priority rights among creditors and shareholders are respected and the creditor voting no receives as much as they would under Chapter 7.

Chapter 13:

May be filed by individual debtors whose unsecured debts are less than \$337,000 and secured debts are less than \$1,000,000.

All of debtor's disposable income is paid to unsecured creditors over a period of three to five years.

Income < state median, 3-5 years.

Income > state median, 5 years.

Disposable Income: Income after allowances for living expenses, including payments to secured creditors for homes and automobiles.

Value of proposed payments must be at least as great as the amount of the dividend they would have received under Chapter 7.

	Chapter 7	Corp. Chapter 11	Individual Ch. 11	Chapter 13
Eligibility	Individuals and Corporations	Corporations	Individuals	Individuals who meet debt limits
Nature of case	Liquidation	Debtor proposes and court confirms a restructuring plan	Debtor proposes and court confirms a debt restructuring plan	Debtor propose and court confirms a debt restructuring plan.
Duration	Not applicable	No limit	Five Years	3-5 years
Possession	Trustee	Debtor usually. Rarely a trustee.	Debtor. Rarely a trustee	Debtor.
Creditor Involvement	Minimal	Creditors may form committees, vote on plan, object to plan	Creditors may form committees, vote on plan, object to plan	Creditors may object to plan
Time discharge is granted	Ca. 90 days post-filing	Plan confirmation	Completion of payments	Completion of payments
Filing Fee	\$299	\$1039	\$1039	\$274

Stopping Creditors' Collection Activities

Once debtors file for bankruptcy, unsecured creditors (*general creditors*) can file their claims and have disputes resolved in the case, but they have few other rights.

The costs of the unified proceedings are paid from the estate, so impact is distributed *pro rata* among the creditors.

Bankruptcy benefits the least aggressive creditors, because they would have lost the race to the courthouse. Without bankruptcy, the aggressive creditor may disrupt the debtor's business, employment, and financial affairs by seizing assets.

Penalties for Violation of Stay

Contempt of Court: inherent power of the court.

Individual right to sue in § 362(k)

BKC § 362(k)	<p>(k)(1) Except as provided in paragraph (2), an individual injured by any willful violation of a stay provided by this section shall recover actual damages, including costs and attorneys' fees, and, in appropriate circumstances, may recover punitive damages.</p> <p>(2) If such violation is based on an action taken by an entity in the good faith belief that subsection (h) applies to the debtor, the recovery under paragraph (1) of this subsection against such entity shall be limited to actual damages.</p> <p>11 U.S.C.A. § 362 (West)</p>
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Actions taken in violation of the stay are void or voidable. Even innocent violations of the stay are subject to forced by the court to undo their violative actions by returning property or correcting records.

Policy Reasons for the Stay: Provides an opportunity to account for all the assets and gives the debtor breathing room to make an orderly liquidation of assets or construct a plan of reorganization.

The language of the stay is broad: "Applicable to all entities" against "any act" to collect a prepetition debt.

11 U.S.C. § 362	(a) Except as provided in subsection (b) of this section, a petition filed under section 301, 302, or 303 of this title, or an application filed under section 5(a)(3) of the
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	<p>Securities Investor Protection Act of 1970, operates as a stay, applicable to all entities, of--</p> <p>(1) the commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case under this title, or to recover a claim against the debtor that arose before the commencement of the case under this title;</p> <p>(2) the enforcement, against the debtor or against property of the estate, of a judgment obtained before the commencement of the case under this title;</p> <p>(3) any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate;</p> <p>(4) any act to create, perfect, or enforce any lien against property of the estate;</p> <p>(5) any act to create, perfect, or enforce against property of the debtor any lien to the extent that such lien secures a claim that arose before the commencement of the case under this title;</p> <p>(6) any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the case under this title;</p> <p>(7) the setoff of any debt owing to the debtor that arose before the commencement of the case under this title against any claim against the debtor; and</p> <p>(8) the commencement or continuation of a proceeding before the United States Tax Court concerning a corporate debtor's tax liability for a taxable period the bankruptcy court may determine or concerning the tax liability of a debtor who is an individual for a taxable period ending before the date of the order for relief under this title.</p>
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Only actions to **collect pre-filing obligations** are stayed. The Bankruptcy Code does **not** halt **criminal proceedings**. § 362(b)(1).

11 U.S.C.A. § 362	<p>(b) The filing of a petition under section 301, 302, or 303 of this title, or of an application under section 5(a)(3) of the Securities Investor Protection Act of 1970, does not operate as a stay--</p> <p>(1) under subsection (a) of this section, of the commencement or continuation of a criminal action or proceeding against the debtor;</p>
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W.R.T General Creditors (Unsecured Creditors) the automatic stay generally remains in effect until the conclusion of the case.

Lifting the Stay for Secured Creditors

Bankruptcy promises secured creditors eventual access either to their collateral or to property or money of equivalent value. A secured creditor is thus assured of recovering the amount of its debt or the value of its collateral, whichever is less.

The holder of an over secured first mortgage on the debtor's home may suffer only minor inconvenience from the automatic stay, while the holder of a second security interest in accounts receivable may stand to lose everything unless the automatic stay issues are dealt with promptly.

Secured Creditors Claim different collateral or different priority	Unsecured Creditors Share pro rata in whatever is left over after secured creditors get done.
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Grounds for Lifting Stay

<p>11 USC § 362</p> <p>(2) is referred to as <u>bankruptcy purposes</u>: either use of the equity to pay other creditors or use of the collateral to effectively reorganize (say its necessary to keep business running).</p>	<p>(d) On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay--</p> <p>(1) for cause, including the lack of adequate</p>
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	<p>protection of an interest in property of such party in interest;</p> <p>(2) with respect to a stay of an act against property under subsection (a) of this section, if--</p> <p>(A) the debtor does not have an equity in such property; and</p> <p>(B) such property is not necessary to an effective reorganization;</p>
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In re Craddock-Terry Shoe Corporation

Facts:	Lincoln and Westinghouse loaned Craddock-Terry \$9,000,000 and took a security interest in the mailing list, customer list, catalogues, and four trademarks of Hill Brothers, the mail-order arm of Craddock-Terry. Not in dispute: L&W have a valid lien on the collateral and debtor has no equity in the collateral. Hill has a serious cash flow problem which has reduced the number of orders that can be filled, creating a serious decline in the value of the collateral. L&W presented evidence that at date of filing, value of mailing list was \$8.7 million, but by 4/30/88 it had declined to \$5.7 million. Debtor's expert testified that FMV of list was \$700,000.
Rule:	11 USC § 362(d)
Issue:	Is there equity in the collateral? § 362(d)(2)(A)
Holding:	No. Parties agree there isn't.
Issue:	Is the collateral necessary to an effective reorganization? §362(d)(2)(B)
Holding:	Yes. Parties agree that it is. Real question is whether reorganization is possible.
Rule:	A court should not precipitously sound the death knell for a debtor by prematurely determining that the debtor's prospects for economic recovery are poor.
Holding:	The court finds no reason to believe that Hill can't recover. Since this is necessary for reorganization, won't lift stay.
Issue:	Has the debtor provided adequate protection for the collateral?
Rule:	Nothing really in the BKC about how to value the collateral for these purposes. Courts have to determine value on a case by case basis (H.R.Rep No 95-595) The purpose of adequate protection is to insure that the secured creditor receives in value essentially what he bargained for. Adequate protection for a secured creditor means that the creditor must receive the same measure of protection in bankruptcy that he could have had outside bankruptcy although the type of protection may differ. The value of the interest in the collateral is equivalent to what they could have recovered through foreclosure had the debtor defaulted but not filed for Chapter 11. The value is the value obtainable from the most commercially reasonable disposition of the collateral within the context of foreclosure proceedings.
Holding:	Value of sale to third party at time of filing was \$700,000. Declined to \$500,000 2/1988, \$330,000 at hearing date. The debtor must provide adequate protection. They offered liens on remaining property worth around \$2,000,000, that'll do pig.

Note: The rule adopted in *In re Craddock-Terry* is a minority rule in that it valued the collateral as of petition date. The majority position is to make the value of the collateral as of the filing date, though the court didn't like this rule as it touches off a race to the courthouse. A small number make it as of hearing date.

Time Limit:

§ 362(e): The stay is automatically lifted unless the Court enters an order continuing the stay within 30 days of motion to lift. If debtor is an individual, stay terminates 60 days after motion unless the court renders a final decision OR extends for "good cause."

ASSIGNMENT 7: THE TREATMENT OF SECURED CREDITORS IN BANKRUPTCY

CHAPTER 3: CREATION OF SECURITY INTERESTS

ASSIGNMENT 8: FORMALITIES FOR ATTACHMENT

Attachment is generally accomplished by contract.

Formalities for Article 9 Security Interests

UCC § 9-203 Attachment and Enforceability of Security Interest; Proceeds; Formal Requisites	<p>(a) [Attachment.] A security interest attaches to collateral when it becomes enforceable against the debtor with respect to the collateral, unless an agreement expressly postpones the time of attachment.</p> <p>(b) [Enforceability.] Except as otherwise provided in subsections (c) through (i), a security interest is enforceable against the debtor and third parties with respect to the collateral only if :</p> <p>(1) value has been given;</p> <p>(2) the debtor has rights in the collateral or the power to transfer rights in the collateral to a secured party; and</p> <p>(3) one of the following conditions is met:</p> <p>(A) the debtor has authenticated a security agreement that provides a description of the collateral and, if the security interest covers timber to be cut, a description of the land concerned;</p> <p>(B) the collateral is not a certificated security and is in the possession of the secured party under Section 9-313 pursuant to the debtor's security agreement;</p> <p>(C) the collateral is a certificated security in registered form and the security certificate has been delivered to the secured party under Section 8-301 pursuant to the debtor's security agreement; or</p> <p>(D) the collateral is deposit accounts, electronic chattel paper, investment property, or letter-of-credit rights, and the secured party has control under Section 9-104, 9-105, 9-106, or 9-107 pursuant to the debtor's security agreement.</p> <p>(c) [Other UCC provisions.] Subsection (b) is subject to Section 4-210 on the security interest of a collecting bank, Section 5-118 on the security interest of a letter-of-credit issuer or nominated person, Section 9-110 on a security interest arising under Article 2 or 2A, and Section 9-206 on security interests in investment property.</p> <p>(d) [When person becomes bound by another person's security agreement.] A person becomes bound as debtor by a security agreement entered into by another person if, by operation of law other than this article or by contract:</p> <p>(1) the security agreement becomes effective to create a security interest in the person's property; or</p> <p>(2) the person becomes generally obligated for the obligations of the other person, including the obligation secured under the security agreement, and acquires or succeeds to all or substantially all of the assets of the other person.</p> <p>(e) [Effect of new debtor becoming bound.] If a new debtor becomes bound as debtor by a security agreement entered into by another person:</p> <p>(1) the agreement satisfies subsection (b)(3) with respect to existing or after-acquired property of the new debtor to the extent the property is</p>
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	<p>described in the agreement; and</p> <p>(2) another agreement is not necessary to make a security interest in the property enforceable.</p> <p>(f) [Proceeds and supporting obligations.] The attachment of a security interest in collateral gives the secured party the right to proceeds provided by Section 9-315 and is also attachment of a security interest in a supporting obligation for the collateral.</p> <p>(g) [Lien securing right to payment.] The attachment of a security interest in a right to payment or performance secured by a security interest or other lien on personal or real property is also attachment of a security interest in the security interest, mortgage, or other lien.</p> <p>(h) [Security entitlement carried in securities account.] The attachment of a security interest in a securities account is also attachment of a security interest in the security entitlements carried in the securities account.</p> <p>(i) [Commodity contracts carried in commodity account.] The attachment of a security interest in a commodity account is also attachment of a security interest in the commodity contracts carried in the commodity account.</p>
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Possession or Authenticated Security Agreement

Authenticated Record: Just a fancy way of saying a signed writing.

UCC § 9-102(a)(69)	"Record", except as used in "for record", "of record", "record or legal title", and "record owner", means information that is inscribed on a tangible medium or which is stored in an electronic or other medium and is retrievable in perceivable form.
UCC § 9-203(b)(3)(B)	the collateral is not a certificated security and is in the possession of the secured party under Section 9-313 pursuant to the debtor's security agreement;

Pawnbroker Statutes: Allow pawnbrokers to sell collateral and retain all proceeds (also requires them to take the full loss if they don't receive amount of loan.

Field Warehousing: Practice of taking possession of the collateral while at the same time allowing debtors to use it. Not used often, most lenders find it too expensive and cumbersome.

Security Agreement-if it contains this, then it satisfies § 9-203(b)(3)(A)

1. Description of the Collateral
2. Description of the Obligation
3. Default
 - a. What is a default?
 - b. What rights does the creditor have in a default?
 - c. Requirements that the debtor keep insurance and care of collateral.

In re Ace Lumber Supply, Inc. (Bankr. D. Mont. 1989)

Facts: Objection to lifting of stay under § 362 of BK Code by Trustee. Trustee alleges that Minot is not a secured creditor. An oral agreement was reached orally between Minot and Ace Lumber Supply that Ace

would pay \$35,000/month plus 1% over prime interest on delinquent balance, would receive cash discounts if payments were being made in a timely fashion, new purchases would be limited to \$10,000/month, and both the delinquent amount and the new purchases would be secured by Ace's inventory, accounts receivable, and equipment. A UCC-1 financing statement was signed by Taylor (Ace's CEO) and filed with the Montana Secretary of State. The Trustee says this does not satisfy the requirements of § 9-203(b).

Rule: When a written security interest is required but there is none, the creditor does not have a security interest in the collateral and cannot enforce an oral agreement that he have such an agreement against the debtor or third person. Anderson, §9-203:18

OR

When the parties have neglected to sign a separate security agreement, it would appear that the better and more practiced view is to look at the transaction as a whole in order to determine if there is a writing, or writings, signed by the debtor describing the collateral which demonstrates an intent to create a security interest in collateral. *Matter of Bollinger Corp.*

OR

Under Montana law the **composite document rule** is available to provide evidentiary support to create a security interest in collateral. That rule, however, does not allow only a financing statement signed by the debtor to satisfy.

The court must first resolve, as a matter of law, whether the language embodied in the writing objectively indicates that the parties *may* have intended to create or provide for a security agreement. If the language crosses this objective threshold...then the factfinder must inquire whether the parties *actually* intended to create a security interest.

Holding: The combination of the financing statement and the telephone notes do not satisfy the requirements of Article 9.

Value Has Been Given

UCC § 1-204	Except as otherwise provided in Articles 3, 4, [and] 5, [and 6], a person gives value for rights if the person acquires them: (1) in return for a binding commitment to extend credit or for the extension of immediately available credit, whether or not drawn upon and whether or not a charge-back is provided for in the event of difficulties in collection; (2) as security for, or in total or partial satisfaction of, a preexisting claim; (3) by accepting delivery under a preexisting contract for purchase ; or (4) in return for any consideration sufficient to support a simple contract.
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Note: This allows a security interest to be given in exchange for PAST consideration.

The Debtor Has Rights in the Collateral

“He who hath not, cannot give”—*nemo dat non habet*.

Two important exceptions:

§ 2-403: Owners who acquire rights by fraud may transfer those “rights” to a bona fide purchaser.	(1) A purchaser of goods acquires all title which his transferor had or had power to transfer except that a purchaser of a limited interest acquires rights only to the extent of the interest purchased. A person with voidable title has power to transfer a good title to a good faith purchaser for value. When goods have been delivered under a transaction of purchase the purchaser has such power even though (a) the transferor was deceived as to the
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	identity of the purchaser, or (b) the delivery was in exchange for a check which is later dishonored, or (c) it was agreed that the transaction was to be a "cash sale", or (d) the delivery was procured through fraud punishable as larcenous under the criminal law.
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A security interest may be granted before acquisition of the property right, but only becomes enforceable at the instant the debtor gains an interest.

Formalities for Real Estate Mortgages

Typical Statute Defining Requirements:

Ohio Revised Code Ann. (2005) §5301.01	A deed, mortgage, land contract...or lease of any interest in real property...shall be signed by the grantor, mortgagor, vendor, or lessor...the signing shall be acknowledged by the grantor, mortgagor, or lessor...before a judge of a court of record in this state or a clerk thereof, a county auditor, county engineer, notary public, mayor, or country court judge, who shall certify the acknowledgement and subscribe the official's name to the certificate of the acknowledgement.
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ASSIGNMENT 9: WHAT COLLATERAL AND OBLIGATIONS ARE COVERED?

A security interest is the right to apply the value of the collateral to the holder's debt.

There is a possibility that a description will be so vague or indefinite that it will be legally insufficient.

In most secured transactions, there will be at least two descriptions of the collateral: one in the security agreement that is the contract between the parties, and one in the financing statement that will be filed in the public records.

Interpreting Security Agreements

Debtor Against Creditor

A security agreement (among other things) is a contract between debtor and creditor.

UCC § 9-102 (a)(73)	"Security agreement" means an agreement that creates or provides for a security interest.
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State Bank of La Crosse v. Elsen

This is an example of reformation of a security interest when the writing results from a mutual mistake. While the security agreement said that a mortgage secured all indebtedness with the bank, other documents indicated that the mortgage would only secure that particular debt. Court held that the mortgage only secured that particular loan.

Rule: Where an agreement is ambiguous, parol evidence may be introduced; where a writing results from mutual mistake, it may be reformed.

Creditor Against Third Party

UCC § 9-201(a)	Except as otherwise provided in the Uniform Commercial Code, a security agreement is effective according to its terms between the parties, against purchasers of the collateral, and against creditors.
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This means a security agreement is effective against a third party in certain cases!

Interpreting Descriptions of Collateral

UCC § 9-102(a)(2)	“Account”, except as used in “account for”, means a right to payment of a monetary obligation, whether or not earned by performance, (i) for property that has been or is to be sold, leased, licensed, assigned, or otherwise disposed of, (ii) for services rendered or to be rendered, (iii) for a policy of insurance issued or to be issued, (iv) for a secondary obligation incurred or to be incurred, (v) for energy provided or to be provided, (vi) for the use or hire of a vessel under a charter or other contract, (vii) arising out of the use of a credit or charge card or information contained on or for use with the card, or (viii) as winnings in a lottery or other game of chance operated or sponsored by a State, governmental unit of a State, or person licensed or authorized to operate the game by a State or governmental unit of a State. The term includes health-care-insurance receivables. The term does not include (i) rights to payment evidenced by chattel paper or an instrument, (ii) commercial tort claims, (iii) deposit accounts , (iv) investment property, (v) letter-of-credit rights or letters of credit, or (vi) rights to payment for money or funds advanced or sold, other than rights arising out of the use of a credit or charge card or information contained on or for use with the card.
UCC § 9-102(a)(33)	“Equipment” means goods other than inventory, farm products, or consumer goods.
UCC § 9-102(a)(48)	“Inventory” means goods, other than farm products, which: (A) are leased by a person as lessor; (B) are held by a person for sale or lease or to be furnished under a contract of service; (C) are furnished by a person under a contract of service; or (D) consist of raw materials, work in process, or materials used or consumed in a business.
UCC § 9-102(a)(47)	“Instrument” means a negotiable instrument or any other writing that evidences a right to the payment of a monetary obligation, is not itself a security agreement or lease, and is of a type that in ordinary course of business is transferred by delivery with any necessary indorsement or assignment. The term does not include (i) investment property, (ii) letters of credit, or (iii) writings that evidence a right to payment arising out of the use of a credit or charge card or information contained on or for use with the card.
UCC § 9-102(a)(23)	“Consumer goods” means goods that are used or bought for use primarily for personal, family, or household purposes.
UCC § 9-102(a)(42)	“General intangible” means any personal property, including things in action, other than accounts, chattel paper, commercial tort claims, deposit accounts, documents, goods, instruments, investment property, letter-of-credit rights, letters of credit, money, and oil, gas, or other minerals before extraction. The term includes payment intangibles and software.

When courts interpret security instruments, they generally give these terms their Article 9 meaning rather than common meaning.

In re Bob Schwermer & Assoc., Inc.: Court held that a racehorse was included in “equipment.”

In re Genuario: Court held that “general intangibles” included liquor license.

Sufficiency of Description: Article 9 Security Agreements

The primary function of the description of collateral in a security agreement is to enable interested parties to identify the collateral.

In re Shirel

(Bankr. W.D. Okla. 2000) **Note: Lee doesn't like this case**

Facts: Shirel purchased a refrigerator on credit with a Sight 'n' Sound credit card. The credit agreement (a 7-page barely-legible document in the words of the court) was signed by Shirel on the first page. The document contained a statement that a security interest in any "merchandise" purchased by Shirel under the plan would be created. This statement was four pages in.

Note: This document is a **contract of adhesion**. A contract of adhesion is a standardized contract prepared entirely by one party to the transaction for the acceptance of the other. Such contracts are interpreted most strongly against the party who prepared the contract. Any inferences from ambiguity are construed against the drafting party.

Rule: § 9-203. A security interest is not enforceable against the debtor or third parties...unless...the debtor has signed a security agreement which contains a description of the collateral. § 9-108. For the purposes of this Article any description of personal property...is sufficient whether or not it is specific if it **reasonably identifies what is described. A creditor may not ignore one of the primary reasons for creating a security agreement, which is to give notice to a third party.**

Holding: This is not an enforceable security interest. Too vague, broad, fails to sufficiently identify a refrigerator. Quite simply, all merchandise is too liberal, too imprecise, and is not a description. A sufficient description might have been "a refrigerator."

Note: Outside of the consumer context, courts generally interpret the description requirement more liberally. Terms of art may be used.

UCC § 9-108	A description of collateral as "all the debtor's assets" or "all the debtor's personal property" or using words of similar import does not reasonably identify collateral.
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Describing After-Acquired Property

After-acquired property: Property that a debtor acquires after the security agreement is authenticated or the security interest is otherwise created.

UCC § 9-204(a)	Except as otherwise provided in subsection (b), a security agreement may create or provide for a security interest in after-acquired collateral.
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Descriptions usually say "after-acquired property", but other terms may be used and may even be implied.

After-acquired property clauses are **ineffective with respect to two kinds of collateral**.

ASSIGNMENT 10: PROCEEDS, PRODUCTS, AND OTHER VALUE-TRACING CONCEPTS

Items of collateral may go through transformations that take them outside the description of the collateral in the security agreement. When a debtor and a creditor anticipate such transformations, they usually choose to have the security interest continue in the collateral as it changes form or to have the security interest attach to whatever the debtor receives in return.

Secured creditors cannot always anticipate the transformations their collateral might undergo or the nature of the property for which it may be exchanged.

Value-tracing Concepts

1. **Proceeds**
2. **Products**
3. **Rents**
4. **Profits**

5. Offspring

Proceeds

Definition

UCC 9-102(a)(64) If the debtor sells the collateral, the security interest will attach to the price paid, whether in the form of an account, a promissory note, or cash. If the debtor leases the collateral, the security interest attaches to the rents received.	"Proceeds" , except as used in Section 9-609(b), means the following property: (A) whatever is acquired upon the sale, lease, license, exchange, or other disposition of collateral ; (B) whatever is collected on, or distributed on account of, collateral ; (C) rights arising out of collateral ; (D) to the extent of the value of collateral , claims arising out of the loss, nonconformity, or interference with the use of, defects or infringement of rights in, or damage to, the collateral; or (E) to the extent of the value of collateral and to the extent payable to the debtor or the secured party , insurance payable by reason of the loss or nonconformity of, defects or infringement of rights in, or damage to, the collateral.
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In re Wiersma

Punitive/compensatory split for loss of cows doesn't matter, as entire award for loss of cows is proceeds.

Searcy Farm Supply, LLC v. Merchants and Planters Bank

Crops are not proceeds of seed.

Farmer's Cooperative Elevator Co. v. Union State Bank

Hogs are not proceeds of the feed they consume.

Important: Courts are quick to infer that the parties intended that the security interest follow the value of the collateral.

McLemore, Trustee v. Mid-South Agri-Chemical Corp.

PIK payments (government program paying farmers to not grow corn) were proceeds of crops that were never planted. "Participation in the PIK program 'disposes' of the debtor's corn crops by precluding their cultivation."

Also Important: Proceeds of proceeds are proceeds (and thus collateral).

Even if the security agreement makes no mention of proceeds, a security interest automatically covers them. *See* UCC §§ 9-203(f) & 9-315(a).

UCC § 9-203(f)	The attachment of a security interest in collateral gives the secured party the rights to proceeds provided by Section 9-315 and is also attachment of a security interest in a supporting obligation for the collateral.
UCC § 9-315(a)	(a) [Disposition of collateral: continuation of security interest or agricultural lien; proceeds.] Except as otherwise provided in this article and in Section 2-403 (2): (1) a security interest or agricultural lien continues in collateral notwithstanding sale, lease, license, exchange, or other disposition thereof unless the secured party authorized the disposition free of the security interest or agricultural lien; and (2) a security interest attaches to any identifiable proceeds of collateral.

Termination of Security Interest in the Collateral After Authorized Disposition

1. Authorization contained in the security agreement.

2. Authorization after signing the security agreement (ex. Bank agrees to let debtor sell the collateral free of security interest.)
3. Implied by circumstances: the creditor may be estopped from asserting his security interest by his conduct (ie he knew the debtor was selling collateral and did not object until later) or the security agreement is silent on sale of inventory.

UCC § 9-315(a)(1) The purchaser takes free of the security interest.	a security interest or agricultural lien continues in collateral notwithstanding sale, lease, license, exchange, or other disposition thereof unless the secured party authorized the disposition free of the security interest or agricultural lien;
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Continuation of Security Interest After Unauthorized Disposition

The security agreement may contemplate that the debtor will attempt to sell the collateral and include a provision that they may do so only with prior authorization.

1. Allows the bank to pass on the nature and adequacy of consideration.
2. Alerts bank that the consideration is about to be paid so they may make a determination on how much should be applied to the secured debt.

Rule: Some states make it a crime to sell collateral and spend the proceeds. Ex. Ill. Rev. Stat. Ch. 26, para. 9-315.01 (2005)
Other states make it a crime to even sell collateral in violation of a security agreement. Ex. N.Y. Pen. Law § 185.05 (2005)

Rule: Even if the security agreement prohibits sale, the debtor may transfer ownership to a buyer. The buyer now owns the property subject to the security interest AND the creditor has a security interest in the proceeds! UCC § 9-315(a)

Associated Industries v. Keystone General, Inc.

Star Bank financed Keystone's inventory under a security agreement that contemplated after-acquired property. Keystone bought inventory from Associated General, then returned it. Star Bank's security interest attached to the inventory and continued pursuant to UCC § 9-315(a).

Gretna State Bank v. Cornbelt Livestock Co.

The bank knew that the debtor had been selling cows without the bank's express written permission in violation of the security agreement. Because they had not objected, the court directed a verdict on the ground that they had waived the prohibition.

Limitations on the Secured Creditor's Ability to Trace Collateral

Rule: Sales of collateral in the ordinary course of business often strip liens from collateral.

Rule: A security interest continues to encumber proceeds only so long as they remain "identifiable."

Note: Just because it's fungible and intermixed doesn't mean it's not identifiable. There may be a legal method of identification.

<<STOP>>

ASSIGNMENT 11: TRACING COLLATERAL VALUE DURING BANKRUPTCY

In the absence of bankruptcy, the relationship between secured party and debtor is almost entirely ruled by K.

Three changes (plus automatic stay) in the SP ↔ Debtor relationship from BK:

1. After-acquired property clauses are ineffective with respect to collateral the debtor acquires during the bankruptcy case.
2. "Based on the equities of the case" the BK court may limit the SP's right to proceeds.
3. Debtors have the right to use the collateral during BK, on the condition that they provide adequate protection to the SP.

After-acquired Property and the Proceeds Dilemma

BKC § 552	<p>(a) Except as provided in subsection (b) of this section, property acquired by the estate or by the debtor after the commencement of the case is not subject to any lien resulting from any security agreement entered into by the debtor before the commencement of the case.</p> <p>(b)(1) Except as provided in sections 363, 506 (c), 522, 544, 545, 547, and 548 of this title, if the debtor and an entity entered into a security agreement before the commencement of the case and if the security interest created by such security agreement extends to property of the debtor acquired before the commencement of the case and to proceeds, products, offspring, or profits of such property, then such security interest extends to such proceeds, products, offspring, or profits acquired by the estate after the commencement of the case to the extent provided by such security agreement and by applicable nonbankruptcy law, except to any extent that the court, after notice and a hearing and based on the equities of the case, orders otherwise.</p> <p>(2) Except as provided in sections 363, 506 (c), 522, 544, 545, 547, and 548 of this title, and notwithstanding section 546 (b) of this title, if the debtor and an entity entered into a security agreement before the commencement of the case and if the security interest created by such security agreement extends to property of the debtor acquired before the commencement of the case and to amounts paid as rents of such property or the fees, charges, accounts, or other payments for the use or occupancy of rooms and other public facilities in hotels, motels, or other lodging properties, then such security interest extends to such rents and such fees, charges, accounts, or other payments acquired by the estate after the commencement of the case to the extent provided in such security agreement, except to any extent that the court, after notice and a hearing and based on the equities of the case, orders otherwise.</p>
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§552 permits the SP to trace the value of its collateral, but the rules on picking up additional collateral are narrower. Once the BK begins, after-acquired property clauses are no longer enforceable.

§552(b) limits value tracing to five concepts: proceeds, product, offspring, rents, or profits.

The secured creditor can keep what collateral value it had at filing, but cannot pick up additional collateral.

Policy rationale: Once bankruptcy stays creditors from exercising state remedies, it tries to safeguard their entitlements. BK law prohibits debtors from favoring one creditor over another in postpetition dealings. Permitting a post-petition after acquired property clause to operate would result in a windfall for the secured party over other creditors.

Under the UCC, “proceeds” includes whatever is received in a transaction in which the debtor disposes of collateral. Bob trades his old car plus \$30,000 for a new one → Bob has a security interest in the new car, even though \$30,000 was added to the deal.

In re Cafeteria Operators, L.P. (2003)

Facts	On April 10, 2001, Debtors opened a \$55,000,000 revolving credit agreement with Fleet and Bank Group. Bank Group was granted a security interest in “[a]ll personal and fixture property of every kind and nature including without limitation all furniture, fixtures, equipment, raw materials, inventory, other goods, accounts, ... deposit accounts, rights to proceeds of letters of credit and all general intangibles. On January 3, 2003, Debtors filed for Chapter 11 reorg. Debtors then moved for an order authorizing use of cash collateral.
Prelim Rules	<p>BKC § 363: A debtor in possession may not use, sell, or lease cash collateral unless 1) each entity with an interest in the cash collateral consents to or 2) the court, after notice and hearing, authorizes the use of, cash collateral.</p> <p>Cash collateral: Cash, negotiable instruments, documents of title, securities, deposit accounts, or other cash equivalents whenever acquired in which the estate and an entity</p>

	<p>other than the estate have an interest and includes the <i>proceeds</i>, products, offspring, rents, or profits of property...whether existing <i>before</i> or <i>after</i> the commencement of a case under this title.</p> <p>Under § 552, post-petition property acquired by the debtor's estate, such as revenues generated from operations, is not subject to any liens resulting from pre-petition security agreements unless the pre-petition security agreements create a security interest in pre-petition property and its proceeds, product, offspring, rents or profits and the post-petition property constitutes such proceeds, product, offspring, rents or profits.</p> <p>Revenues generated post-petition solely as a result of the debtor's labor are not subject to a pre-petition lender's security interest.</p>
Issue	Whether restaurant revenues are § 552 proceeds of property subject to the Bank Group's pre-petition lien.
Holding	Only the portions of revenues that are directly traceable to the consumption of the inventory are subject to the security interest. Since the value of the consumed inventory is about 1/3 that of the total price of the sold food, the remainder is generated by the labor of the Debtor and cannot be collateral. Since the Debtor wants to use the cash to purchase new inventory, the Bank Group is granted a replacement lien in inventory as it is replenished. If inventory levels drop, Bank Group is granted a replacement lien in the other assets of the Debtor, in the highest level of priority...as needed to restore the Bank Group's position in inventory
Reasoning	Congress enacted § 552 to limit legislatively the effect of pre-petition liens on the debtor's post-petition property. Congress sought to preserve the fresh start policy stated in <i>Local Loan</i> by requiring that only security interests in after-acquired property arising from, or connected with, pre-existing property be preserved in bankruptcy.

The Equities of the Case Solution to the Proceeds Dilemma

§ 552 specifically authorizes splitting the proceeds results.

In re Delbridge

$$CC = \frac{D}{D + E + L} \times P$$

Where:

- CC = "Cash Collateral"-the amount of the check encumbered by the lender's lien
- D = The average depreciation of the capital
- E = The average direct expenses
- L = Average market value of the labor
- P = The average dollar proceeds of sale.

Very simply, the larger is the lender's capital contribution to the venture, the larger its share of the proceeds ought to be. Conversely, if the [debtor's] input in the venture is great, the "equities of the case" compel that his share of the proceeds likewise be great.

ASSIGNMENT 12: THE LEGAL LIMITS ON WHAT MAY BE COLLATERAL

Article 9 makes broad descriptions of collateral as "all personal property of the debtor" ineffective, but this is more a limit in *form*, not in *substance*. Secured parties may take interests in such broad categories of expressly sanctioned collateral as "equipment, inventory, accounts, chattel paper, instruments, money, and general intangibles" that will cover everything for a business debtor.

However, certain types of collateral, such as Real Estate and Insurance are excluded from coverage to avoid conflicts of bodies of law.

UCC § 9-109(d)(8)	a transfer of an interest in or an assignment of a claim under a policy of insurance,
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	other than an assignment by or to a health-care provider of a health-care-insurance receivable and any subsequent assignment of the right to payment, but Sections 9-315 and 9-322 apply with respect to proceeds and priorities in proceeds;
UCC § 9-109(d)(11)	the creation or transfer of an interest in or lien on real property, including a lease or rents thereunder, except to the extent that provision is made for: (A) liens on real property in Sections 9-203 and 9-308 ; (B) fixtures in Section 9-334 ; (C) fixture filings in Sections 9-501 , 9-502 , 9-512 , 9-516 , and 9-519 ; and (D) security agreements covering personal and real property in Section 9-604 ;

Two limits on what may serve as collateral: consumer goods acquired more than ten days after the loan, and after acquired property clauses may not attach to commercial tort claims.

UCC § 9-204(b)	A security interest does not attach under a term constituting an after-acquired property clause to: (1) consumer goods , other than an accession when given as additional security, unless the debtor acquires rights in them within 10 days after the secured party gives value; or (2) a commercial tort claim .
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UCC § 1-201(b)(35) defines “security interest” as an interest in “personal property and fixtures.” State law defines fixtures as property. **A security interest may only attach to property.**

Property that Cannot be Collateral

Property of a Personal Nature

It is inappropriate for creditors to take and enforce *nonpossessory, non-purchase-money security interests* in property that is *highly personal* in nature and has little resale value.

Reasoning: It’s kind of mean-spirited. Repossession wasn’t to secure payment but to extort payment by denying the debtor the use of their personal goods. Plus, the chance for confrontation in such repossessions is very high.

Exempt Items: General unsecured creditors may not seize it. Exemptions are not effective against secured creditors.

BKC § 522(f)(1)	Notwithstanding any waiver of exemptions but subject to paragraph (3), the debtor may avoid the fixing of a lien on an interest of the debtor in property to the extent that such lien impairs an exemption to which the debtor would have been entitled under subsection (b) of this section if such lien is... (B) a nonpossessory, nonpurchase-money security interest in any—(i) household furnishings, household goods, wearing apparel, appliances, books, animals, crops, musical instruments, or jewelry that are held primarily for the personal, family, or household use of the debtor or dependent of debtor; (ii) implements, professional books, or tools, of the trade of the debtor or the trade of a dependent of the debtor; or (iii) professional prescribed health aids for the debtor or a dependent of the debtor.
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However: Security interests in property in possession of the creditor is not subject to 522(f) avoidance. PMSI in personal items is also not subject to 522(f) avoidance.

Policy: Creditors in the business of selling personal items of this nature are likely to be able to get a good price for them on resale.

For a security interest to be avoidable under § 522(f), the property must be both exempt and of a type listed in § 522(f).

FTC, Trade Regulation Rules

16 C.F.R. 444 (2005) § 444.2 Unfair Credit Practices	(a) In connection with the extension of credit to consumers in or affecting commerce, as commerce is defined in the Federal Trade Commission Act, it is an unfair act or practice within the meaning of Section 5 of that Act for a lender or retail establishment seller directly or indirectly to take or receive from a consumer an obligation that:...(3) Constitutes or contains an assignment of wages or other earnings unless: (i) the assignment is by its terms revocable at the will of the debtor , or (ii) The assignment is a payroll deduction plan or preauthorized payment plan , commencing at the time of the transaction, in which the consumer authorizes a series of wage deductions as a method of making each payment, or (iii) the assignment applies only to wages or other earnings already earned at the time of the assignment. (4) Constituted or contains a nonpossessory security interest in household goods other than a purchase money security interest .
§ 444.1	(h) <i>Earnings</i> . Compensation paid or payable to an individual or for his or her account for personal services rendered or to be rendered by him or her, whether denominated as wages, salary, commission, bonus, or otherwise, including periodic payments pursuant to a pension, retirement, or disability program. (i) <i>Household goods</i> . Clothing, furniture, appliances, one radio and one television, linens, china, crockery, kitchenware, and personal effects (including wedding rings) of the consumer and his or her dependents, provided that the following are not included within the scope of the term “household goods”: (1) Works of art; (2) Electronic entertainment equipment (except one television and one radio); (3) Items acquired as antiques; and (4) Jewelry (except wedding rings). (j) <i>Antique</i> . Any item over one hundred years of age, including such items that have been repaired or renovated without changing their original form or character.

Enforcement: The FTC can enforce these regulations by bringing actions for civil penalties or for cease and desist orders against violators. No private remedy under federal law, but most states have enacted “little FTC statutes” that allow private actions.

Future Income of Individuals

A direct attempt to create a security interest in future income is an *assignment of wages*.

Limitations on Assignment of Wages

Most states either restrict the assignment of wages or bar it altogether. Those who allow usually restrict with:

1. Not allowed in consumer transactions;
2. Must be already-earned income; or
3. Can't exceed a certain percentage of income.

Policy: Debtors whose income is encumbered have little incentive to work.

Effect of BK on Assignments of Wages

Poof. Gone.

Pension Rights

Qualifying retirement plans under ERISA may not be collateral for a loan.

In Re Green

Facts	Wal-mart has a Profit Sharing Plan, which Green has participated in since 1978, and has been 100% vested since June 1984. The value of his interest is ca. \$100,000. United Savings and
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Issue	Loan lent Green \$45,000 in 1988. Green designated United Savings as beneficiary of his Wal-mart Profit Sharing Plan.
Rule	Does United Savings have a valid security interest in Green's Profit Sharing Plan? (Broadly: May a creditor take a security interest in an ERISA-qualified retirement plan?) Section 206(d) reflects a considered congressional policy choice, a decision to safeguard a stream of income for pensioners...even if that decision prevents others from securing relief for the wrongs done to them. If exceptions to this policy are to be made, it is for Congress to undertake that task. <i>Guidry v. Sheet Metal Workers National Pension Fund</i> . ERISA was intended to allow workers to accumulate monies for retirement by not being taxed on savings until the funds are withdrawn for use. Congress required, as a prerequisite for such preferential tax treatment, that each Plan contain provisions prohibiting the participants from transferring or otherwise alienating their share of Plan assets, and shielding such assets from claims of creditors until such time as the funds are in fact withdrawn.
Holding	United Savings' security interest is invalid.

29 U.S.C. § 1056(d) (2005)	(1) Each pension plan shall provide that benefits provided under the plan may not be assigned or alienated... (3)(A) Paragraph (1) shall apply to the creation, assignment, or recognition of a right to any benefit with respect to a participant pursuant to a domestic relations order. Each pension plan shall provide for the payment of benefits in accordance with the applicable requirements of any qualified domestic relations order.
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Future Property as Collateral

Under both the UCC and real property law, a debtor can grant a security interest in property the debtor does not yet own.

A business debtor may encumber future earnings of the business. However, that encumbrance may be escaped in a bankruptcy.

Valuable Nonproperty

Licenses: Although they are routinely bought and sold, licenses, rights, and medallions are by law "nonproperty". **Public Policy**: the right, license, or medallion only exists for the public convenience. The government may revoke at any time.

Jackson v. Miller

Court held that a purported security interest in a liquor license is void and of no effect. State law "The license shall continue as a personal privilege granted by the board and nothing therein shall constitute the license as property."

Opposing view: The security interest is subject to the government's cancellation of the license

Franchise Agreements: Franchisor has to approve sale of franchise.

In re SRJ Enterprises, Inc.

Facts	3/91, SRJ bought a Nissan franchise and entered into floor plan with NBD. Later that year, got add'l financing from Success. 3/92, closed doors and filed for Ch. 11. 5/92, SRJ filed motion for an order approving sale of assets to Rohrman. SRJ would voluntarily give up franchise on receipt of \$125K from Rohrman. Sale contingent on Rohrman obtaining Nissan franchise.
Issue	Is the \$125k "proceeds" of pre-petition value and encumbered.
Rule	Proceeds are ANY amount received for disposition of collateral, even termination.
Holding	Yep. It's proceeds.
Reasoning	Otherwise is too formalistic. He got money in consideration for termination contingent on Rohrman getting a "new" franchise. This market share value represented by the Nissan franchise became an asset of the estate much like the Nissan automobiles. Recognizing the inherent market share as pre-petition

collateral comports with § 552 of the Bankruptcy Code.

Unencumbered property has the potential to produce encumberable property-so that potential is encumberable.

Defeating the Limits on What May Be Collateral

Assuming that debtors cannot create security interests in licenses and franchises, debtors MAY create security interests in:

1. The proceeds that come into existence when debtors sell those licenses and franchises
2. The revenues that debtors derive from the use of their licenses and franchises.

While an interest in the value of a franchise is valuable, it's not the same thing as an interest in a franchise itself: can't foreclose, take over the franchise, and run the business to maximize profits.

CHAPTER 4: DEFAULT: THE GATEWAY TO REMEDIES

ASSIGNMENT 13: DEFAULT, ACCELERATION, AND CURE UNDER STATE LAW

DEFAULT

UCC § 9-601(a) Creditors have remedies if and only if default occurs.	After default, a secured party has the rights provided in this part and, except as otherwise provided in Section 9-602 , those provided by agreement of the parties. A secured party: (1) may reduce a claim to judgment, foreclose, or otherwise enforce the claim, security interest, or agricultural lien by any available judicial procedure; and (2) if the collateral is documents, may proceed either as to the documents or as to the goods they cover.
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When Is Payment Due?

Most defaults actually acted upon by secured creditors are defaults in payment.

Installment Loans
Single Payment Loans
Lines of Credit

Acceleration and Cure

Acceleration

Absent a contract provision, the common law treats ten installment payments as ten separate obligations.

Most creditors require a provision in an installment loan agreement that opts out of the common law rule. An *acceleration clause* states that in the event of a default in any obligation under the repayment clause, the creditor may declare all payments due and payable.

Even if the contract doesn't require notice by the creditor, some courts will require.

In re Crystal Properties

A creditor must take affirmative action to put the debtor on notice that it intends to exercise its option to accelerate...Both state and federal courts have made clear the unquestionable principle that, even when the terms of a note do not require notice or

demand as a prerequisite to accelerating a note, the holder must take affirmative action to notify the debtor that it intends to accelerate.

Limits on the Enforceability of Acceleration Clauses

UCC § 1-309	A term providing that one party or that party's successor in interest may accelerate payment or performance or require collateral or additional collateral "at will" or when the party "deems itself insecure," or words of similar import, means that the party has power to do so only if that party in good faith believes that the prospect of payment or performance is impaired. The burden of establishing lack of good faith is on the party against which the power has been exercised.
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J.R. Hale Contracting Co. v. United New Mexico Bank at Albuquerque

Facts:	Note at issue executed 11/1982 in the amount of \$400,000, twice what they'd ever loaned to JR Hale before. Near end of 2/1983, Hales went to the bank to borrow more money to cover contracting costs at the Double Eagle II airport. Line of credit was maxed out. Company had failed to make interest payment due on March 1. JR Hale had been carrying a check to pay the interest payment to meetings in March, just forgot to give it to them-even asked a banker to remind him at next meeting. On several previous loans, the bank had not been troubled by multiple late payments-they'd just call the company and ask for a payment, or just deduct from the account. This time, they got antsy, accelerated the note. Grounds for default "The promissory note is in default due to your failure to pay the March 1, 1983 interest payment when due, and also due to the Bank's review of your financial situation which causes the Bank to believe that its prospect for receiving payment on the note is impaired.
Issue:	Did the Bank, by its conduct, waive, modify, or become estopped from exercising their right to accelerate?
Rule:	Waiver: The intentional relinquishment or abandonment of a known right. May be both express and implied in fact. Waiver by estoppel: To prove waiver by estoppel, the party need only show that he was misled to his prejudice by the conduct of the other party into the honest and reasonable belief that such waiver was intended.
Holding:	Silence may form the basis for estoppel if a party stands mute when he has a duty to speak. No waiver (express or implied in fact) from the conduct of the bank. With repetition of acceptance of late payment, could say implied waive, but this was a single payment. Conduct at most meant would forbear for three weeks. HOWEVER, waiver by estoppel presents an issue of fact. Implicit in UCC 1-303 is that one party to a contract will use past commercial dealings with another party as the basis for interpretation of the other's conduct. Under these circumstances, we believe the bank had a duty to inform the company that the bank would enforce performance under the contract. The company might have been induced into not taking the initiative in correcting the delinquency.

Debtor's Right to Cure

A debtor has the right to cure a default by paying the past due payments up until the creditor exercises right to accelerate.

Old Republic Insurance Co. v. Lee

Facts:	Promissory note provided for payments of \$387.85 each. On April 29, 1986, Old Republic declared the note in default since the Lees had not made the March and April 19th payments. On May 16th, Lee sent a certified check for March, April, and May 19th payments. Old Republic returned and proceeded with foreclosure proceedings.
Issue:	Was reinstatement of the mortgage by the trial court error?
Rule:	A mortgagor, prior to the election of a right to accelerate by the mortgage holder upon the occurrence of a default, may tender the arrears due and thereby prevent the mortgage holder

from exercising his option to accelerate. However, once the mortgage holder has exercised his option to accelerate, the right of the mortgagor to tender only the arrears is terminated.
Holding: Trial court can suck it.

This is the majority rule!

Some states permit cure and reinstatement of the original loan terms by payment of arrearages even after creditor has exercised right of acceleration.

Procedures After Default

On default, the secured creditor has a choice of remedies.

1. Judicial remedies such as foreclosure and replevin.
2. Self-help remedies such as repossession without judicial process.

The creditor's choice among remedies is often based on the creditor's assessment of the likelihood that the debtor will resist, the creditor's appraisal of the strength of the debtor's defenses, if any, and the manner in which the sufficiency those defenses will be determined in each remedial procedure.

ASSIGNMENT 14: DEFAULT, ACCELERATION, AND CURE UNDER BANKRUPTCY LAW

UCC § 9-623	<p>(a) [Persons that may redeem.] A <u>debtor</u>, any <u>secondary obligor</u>, or any other <u>secured party</u> or lienholder may redeem collateral.</p> <p>(b) [Requirements for redemption.] To redeem collateral, a person shall tender: (1) fulfillment of all obligations secured by the collateral; and (2) the reasonable expenses and attorney's fees described in Section <u>9-615(a)(1)</u>.</p> <p>(c) [When redemption may occur.] A redemption may occur at any time before a <u>secured party</u>: (1) has collected collateral under Section <u>9-607</u>; (2) has disposed of collateral or entered into a contract for its disposition under Section <u>9-610</u>; or (3) has accepted collateral in full or partial satisfaction of the obligation it secures under Section <u>9-622</u>.</p>
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In re Moffett (Tidewater Finance Co. Moffett)

Facts:	1/22/2001 Moffett bought a 1998 Honda Accord from Hendrick on installment loan for \$20,024.25, 60 payments. Hendrick assigned its rights to Tidewater Finance. Under the purchase contract and state law, Tidewater had the right to repossess the vehicle in the event of default, subject to right of cure (UCC § 9-609, 623) Moffett failed to make 3, 4/2002 payments. Tidewater repossessed on 4/25/2002. Moffett filed for Ch.13 that day, notified Tidewater of the filing on 5/1 and demanded return under turnover and automatic stay of BK code. 11 U.S.C. §§ 362(a) and 542(a).
Issue:	
I.	Whether Tidewater Finance and the repossessed vehicle are subject to the automatic stay and turnover provisions of the bankruptcy code.
A.	What are the nature of Moffett's property interests and are they a part of the bankruptcy estate?
B.	Whether Moffett's right to redeem was sufficient to subject Tidewater Finance to the automatic stay and turnover provisions of the Bankruptcy Code.
Rule A:	Federal bankruptcy law includes "all legal or equitable interests of the debtor in property as of the commencement of the case." BKC § 541(a)(1). However, state law determines the nature and existence of a debtor's rights.

UCC § 9-609 expressly permits a secured creditor to repossess collateral protecting its security interest after default. UCC § 9-623(c)(2).

Once a creditor repossesses the collateral, it is permitted to dispose of it under certain conditions. UCC § 9-610

The debtor has the right to redeem at any time before the collateral is disposed of. UCC § 9-623(c)(2). This right is further protected by a duty to notify at least ten days prior to disposal (UCC §§ 9-611, 612) and to notify of right to redeem (9-614).

The rights of redemption, notification, and surplus—among other rights—are not extinguished until the creditor accepts the collateral or disposes of the collateral.

These interests are unquestionably legal or equitable interests included within a bankruptcy estate. Under BKC 541(a)(1), SCOTUS held that Congress defined property of the estate to include all tangible and intangible property interests of the debtor.

Holding A: The rights of redemption, notification, surplus were all property interests of the estate.

Rule B: A debtor may redeem collateral by tendering fulfillment of all obligations secured by the collateral, as well as reasonable expenses from repossessing and holding the collateral. UCC § 9-623(b).

Even if the creditor exercised an acceleration clause, the Bankruptcy Code allows a debtor to restructure the timing of her payments in order to facilitate her exercise of the right of redemption. §1322(b)(2). 1322(b)(3) allows debtors to cure their defaults.

Holding B: Even though this doesn't provide for a lump sum cure, this plan provides for adequate protection of the creditor's interest. The turnover is proper.

Stage 1: Protection of the Defaulting Debtor Pending Reorganization

Rule: Unless lifted pursuant to BKC § 362(d), the stay of an act against property continues until the property is no longer in the BK estate. The stay of any other act continues until the case is closed or dismissed, or the debtor is granted or denied discharge.

Rule: A debtor who provides adequate protection to its secured creditor typically will be permitted to use the collateral while the case remains pending. BKC §§ 363(b)(2) and (c)(2).

Are Debtors Required to Make Installment Payments Pending Confirmation?

	Chapter 11	Chapter 13
File a Plan		15 days after filing petition, may be extended for "cause shown".
Commence Payment	Once plan has been confirmed-typical time 1 year. (May have to make some interim payments to cover depreciation.)	W/in 30 days of filing plan.

Stage 2: Reinstatement and Cure

Modification Distinguished from Reinstatement and Cure

Modification is sometimes referred to as "rewriting the loan."

Minimum amount the debtor must pay on a modified secured claim:

1. Determine the amount of the allowed secured claim

2. Formulate a schedule for payments that will have a value, as of the effective date of the plan, not less than the amount of the allowed secured claim. (The debtor must propose to pay the full amount of the secured claim plus interest at the “market rate.”)

Period of Time Allowable for Modified Repayment

Chapter 11: Any period of time that is “Fair and Equitable” § 1129(b)(1).

Chapter 13:

Debtors<median income: 3 years, extendible by court for cause to 5.

Debtors>median income: 5 years, unless the debtor can pay all unsecured claims in full within a shorter period. § 1325(b)(4).

Mortgages

The Bankruptcy Code does not allow modification of mortgages secured by principal residences except for exception in § 1322(c)(2) for mortgages with only a few years left to run.

Modification	Cure
Debtor proposes new payment schedule Arrearage included in payments Interest is at market-based rate set by court Debtor pays the unsecured portion to the same extent he pays other unsecured claims	Debtor returns to original payment schedule Arrearage paid separately Interest at the contract rate. Pays unsecured portion in full.

Reinstatement and Cure under Chapter 11

<p>BKC § 1124(2): A debtor’s right to cure and reinstate. Also, a class of claims is unimpaired so long as the treatment under the plan meets four requirements:</p> <ol style="list-style-type: none"> 1. Debtor cures any default occurred before or after the commencement of the BK case. Generally must be a lump sum. 2. Must reinstate the maturity of that part of the claim that remains outstanding after cure as it existed before the default. (Future payments remain due at the times specified in the original contract.) 3. The debtor must compensate the holder of the secured claim for damages incurred through reasonable reliance on the breached repayment contract. 4. The plan does not otherwise alter the legal, equitable, or contractual rights to which the claim entitles its holder. 	<p>(2) notwithstanding any contractual provision or applicable law that entitles the holder of such claim or interest to demand or receive accelerated payment of such claim or interest after the occurrence of a default--</p> <p>(A) cures any such default that occurred before or after the commencement of the case under this title, other than a default of a kind specified in section 365(b)(2) of this title or of a kind that section 365(b)(2) expressly does not require to be cured;</p> <p>(B) reinstates the maturity of such claim or interest as such maturity existed before such default;</p> <p>(C) compensates the holder of such claim or interest for any damages incurred as a result of any reasonable reliance by such holder on such contractual provision or such applicable law;</p> <p>(D) if such claim or such interest arises from any failure to perform a nonmonetary obligation, other than a default arising from failure to operate a nonresidential real property lease subject to section 365(b)(1)(A), compensates the holder of such claim or such interest (other than the debtor or an insider) for any actual pecuniary loss incurred by such holder as a result of such failure; and</p> <p>(E) does not otherwise alter the legal, equitable, or contractual rights to which such claim or interest entitles the holder of such claim or interest.</p>
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If a class of claims is **unimpaired**, then the holder of the claim is conclusively presumed to have accepted the plan and is not entitled to vote on it.

Reinstatement and Cure under Chapter 13.

<p>BKC § 1322(b)(5): Effectively imposes the same requirements as above.</p> <ol style="list-style-type: none">1. The debtor must cure any default that occurred before or after the commencement of the BK. However, they only must cure within a “reasonable time.” Courts have approved cures over years, and all agree that need not be in a lump sum. However, the cure cannot extend beyond the period of the plan.2. The Chapter 13 plan must reinstate the maturity of the claim as it existed before the default.3. No express provision for compensation of damages as a result of the breach, but § 1322(e) directs the court to look at applicable nonbankruptcy law to determine the amount necessary to cure. In most states, that will require payment of interest on arrearages.4. Cannot otherwise alter the legal, equitable, or contractual rights to which the holder is entitled.	<p>(5) notwithstanding paragraph (2) of this subsection, provide for the curing of any default within a reasonable time and maintenance of payments while the case is pending on any unsecured claim or secured claim on which the last payment is due after the date on which the final payment under the plan is due;</p>
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Debtors filing under Chapter 13 are far more likely to use reinstatement and cure than modification to deal with long-term secured obligations (for obvious reasons!)

<p>BKC § 1322(b)(2): Can't modify mortgage on principal residence under Chapter 13 either.</p>	<p>(2) modify the rights of holders of secured claims, other than a claim secured only by a security interest in real property that is the debtor's principal residence, or of holders of unsecured claims, or leave unaffected the rights of holders of any class of claims;</p>
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Nobelman v. American Savings Bank

SCOTUS held that even though the purchase-money mortgage was \$71,000 and the house was worth \$23,500, the Nobelmans had to pay. Stevens (Concurring) gave the public policy argument: “Favorable treatment of residential mortgages was intended to encourage the flow of capital into the home lending market.... The Court’s literal reading of the text of the statute is faithful to the intent of Congress.

When Is It Too Late to File Bankruptcy to Reinstate and Cure or to Modify?

Bankruptcy does not just preserve rights existing under state law; it recognizes rights that state law does not. Even if statutory deadline for cure and reinstatement has passed, can still file bankruptcy.

Mortgage: If before sold at a foreclosure sale that is conducted in accordance with applicable non-bankruptcy law.” Some jurisdictions, when the sheriff identifies a winner of the auction. In others, only when the court enters an order confirming the foreclosure sale and the order has become final. RULE IS NOT CLEAR, but probably the same for all collateral under both 13 and 11.

Binding Lenders in the Absence of a Fixed Schedule for Repayment

Lines of Credit

The debtor’s right to cure and reinstate a line of credit is of no avail if the lender calls the note.

Debtors whose lines of credit were repayable on demand or at a specific time have no contract rights that bankruptcy could restore.
Could modify the loan if it's a substantial amount, otherwise not worth the hassle. However, nothing requires the lender to make more advances on the line of credit during or after the bankruptcy. BKC § 365(c)(2).
Could find a substitute lender, which may not be all that hard -- there's companies who specialize.

CHAPTER 5: THE PROTOTYPICAL SECURED TRANSACTION

ASSIGNMENT 15: THE PROTOTYPICAL SECURED TRANSACTION

The Personal Guarantee

Two reasons:

1. Gives the lender the right to obtain a judgment against the owners and proceed against their assets just as if they were the ones who borrowed the money.
2. Ensures that in the event of a default the lender will cooperation of the owners.

The Floorplan Agreement

Some manufacturers will include a full-price buyback agreement in the floorplan.

1. Incentivizes lenders to give 100% financing on their products.
2. If manufacturer financed boats, they'd have to take them back anyhow.
3. Reduces the risk to manufacturer that boats are stolen, etc. while financed.

Pay-as-Sold Agreement

Under a pay-as-sold (PAS) agreement, the borrower must pay the principal balance of the loan secured by a particular piece of inventory when it is sold.

Random Inspections: A central feature of a PAS agreement. Randomly, the lender will send an inspector to verify that all of the inventory that's financed is actually there. Generally accomplished in one trip to ensure no fraud.

"The check is in the mail"-checker will verify postmark on check and look at check register to make sure it was actually sent before he showed up.

CHAPTER 6: PERFECTION

ASSIGNMENT 16: THE PERSONAL PROPERTY FILING SYSTEM

Competition for the Secured Creditor's Collateral

Many of the contests over rights to collateral are questions of priority.

What Is Priority?

If there is more than one lien against collateral, each has a priority.

A lien with priority higher than another is a *senior* or *prior* lien.

A lien with priority lower than another is a *junior* or *subordinate* lien.

Priority may exist even as among unsecured creditors.

Example: Debentures (bonds) may be subordinate to bank loans.

However, this is likely worthless if all assets are encumbered.

Alternate systems to lien priority:

Each competitor gets a pro-rata share of assets (like unsecured creditors in BK)

Debts deemed "more important" may get priority

Peerless Packing Co. v. Malone & Hyde, Inc.

Facts:	Kizer negotiated an agreement with M&H to purchase “PIC PAC” store with M&H taking a security interest in the present and after-acquired inventory. M&H met UCC requirements for perfecting lien. Kizer sold some goods supplied by M&H and some by appellants (represented by PPC). None of the appellants obtained PMSI in the supplies. In 3/1982 M&H decided Kizer wasn’t going to make a go of it and notified him they were taking the store back. Kizer signed a “Notice of Default and Transfer of Possession Agreement” which transferred all of Kizer’s rights in store, equipment and inventory, bank accounts to M&H. In return, M&H released Kizer from various debts. M&H sent a letter to PPC that they took the inventory without assuming liability to third parties, and would not pay for deliveries before 3/31/1982.
Rule:	Cannot maintain an action in equity for unjust enrichment under Article 9. ‘The purpose and effectiveness of the UCC would be substantially impaired if interests created in compliance with UCC procedure could be defeated by application of the equitable doctrine of unjust enrichment.’ The unsatisfied creditors could have protected themselves either by demanding cash payment for their goods or by taking a purchase money security interest in the goods they delivered....

How Do Creditors Get Priority?

Central to the system of lien priority is the idea that **liens rank in the chronological order in which they were created.**

Why? Priority by chronology makes it possible for a creditor to know how it will fare in later competitions.

Ways in which the law ensures the prospective lender can discover a lien

1. Filing notice in a public records system.
 2. Taking possession of the collateral.
 3. Taking control of the collateral by means of the stake holder’s agreement.
 4. Posting notice on the property or where it will be seen by those using the property.
- (The text cites to UCC §308(a), I have no idea what the fuck that is)

The Theory of the Filing System

Gives both *constructive* and *actual* (in theory) notice to a potential creditor of pre-existing liens. In practice, the system is cumbersome and expensive to use.

BKC § 544 (a)	<p>a) The trustee shall have, as of the commencement of the case, and without regard to any knowledge of the trustee or of any creditor, the rights and powers of, or may avoid any transfer of property of the debtor or any obligation incurred by the debtor that is voidable by--</p> <p>(1) a creditor that extends credit to the debtor at the time of the commencement of the case, and that obtains, at such time and with respect to such credit, a judicial lien on all property on which a creditor on a simple contract could have obtained such a judicial lien, whether or not such a creditor exists;</p> <p>11 U.S.C.A. § 544 (West)</p>
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ASSIGNMENT 17: ARTICLE 9 FINANCING STATEMENTS: THE DEBTOR’S NAME

The Components of the Filing System

Statewide filing systems generally permit the electronic filing of financing statements and other records.

Record: Information that is stored on a tangible medium or which is stored in an electronic or other medium and is retrievable in perceivable form.

Instead of “stamping” a financing statement, filing officers now assign a number to a financing statement to establish priority.

A filing system consists of:

1. Filed Records
2. System for adding new records
3. System for searching the records
4. Removing obsolete records (though most filing systems don’t include this and just let them grow.)

Financing Statements

A big problem with the filing systems is that they were created before electronic media, and even though many of the documents have been converted to an electronic form, they cannot be word-searched. An electronic word-search is of little value if it doesn’t include every record.

The Index

When a financing statement is filed, the filing officer assigns it a file number (or book and page number). This is the means of indexing and retrieving the document.

Types of Index Based on Description of Collateral

These systems can work based on description and discrete numbers because the collateral has a stable identity.

Tract Index: Employed in some real estate systems. Each tract in the county is assigned a unique number, and the numbers are written on maps.

Motor Vehicles: DMVs track titles and liens against motor vehicles by VIN.

Other types of Index (not based on Description of Collateral)

Most types of collateral governed by Article 9 is not easily traceable (like inventory), and it would be impractical to assign serial numbers. It also wouldn’t be practical to index by description. Therefore, Article 9 filing officers index financing statements by the name of the debtor only.

UCC §9-519(c) Requires filing by debtor name	Except as otherwise provided in subsections (d) and (e), the filing office shall: (1) index an initial financing statement according to the name of the debtor and index all filed records relating to the initial financing statement in a manner that associates with one another an initial financing statement and all filed records relating to the initial financing statement; and (2) index a record that provides a name of a debtor which was not previously provided in the financing statement to which the record relates also according to the name that was not previously provided.
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Search Systems

Some systems sort the index entries alphabetically and print hard copies of the index.

This can lead to problems even with correctly spelled names with weird alphabetizing rules.

Other systems are electronic search, but there can be problems with the “search logic”.

Some systems only allow employee access-searches can be cumbersome and depend on the skill of the employer. Other systems allow the public to do so, and the instant feedback can be very helpful.

The financing statement is effective as of the time of the stamp (or assignment of number). However, it may take time to effectively index the record, so there can be several unindexed (and undiscoverable) records *in the basket*. Some office will allow lenders to search the basket, other won't (or its impractical)

Correct Names for Use on the Financing Statement

UCC § 9-506(a)	<p>(a) [Minor errors and omissions.] A financing statement substantially satisfying the requirements of this part is effective, even if it has minor errors or omissions, unless the errors or omissions make the financing statement seriously misleading.</p>
UCC § 9-503: Safe Harbor	<p>(a) [Sufficiency of debtor's name.] A financing statement sufficiently provides the name of the debtor: (1) if the debtor is a registered organization, only if the financing statement provides the name of the debtor indicated on the public record of the debtor's jurisdiction of organization which shows the debtor to have been organized; (2) if the debtor is a decedent's estate, only if the financing statement provides the name of the decedent and indicates that the debtor is an estate; (3) if the debtor is a trust or a trustee acting with respect to property held in trust, only if the financing statement: (A) provides the name specified for the trust in its organic documents or, if no name is specified, provides the name of the settlor and additional information sufficient to distinguish the debtor from other trusts having one or more of the same settlors; and (B) indicates, in the debtor's name or otherwise, that the debtor is a trust or is a trustee acting with respect to property held in trust; and (4) in other cases: (A) if the debtor has a name, only if it provides the individual or organizational name of the debtor; and (B) if the debtor does not have a name, only if it provides the names of the partners, members, associates, or other persons comprising the debtor.</p> <p>(b) [Additional debtor-related information.] A financing statement that provides the name of the debtor in accordance with subsection (a) is not rendered ineffective by the absence of: (1) a trade name or other name of the debtor; or (2) unless required under subsection (a)(4)(B), names of partners, members, associates, or other persons comprising the debtor.</p> <p>(c) [Debtor's trade name insufficient.] A financing statement that provides only the debtor's trade name does not sufficiently provide the name of the debtor.</p> <p>(d) [Representative capacity.] Failure to indicate the representative capacity of a secured party or representative of a secured party does not affect the sufficiency of a financing statement.</p> <p>(e) [Multiple debtors and secured parties.] A financing statement may provide the name of more than one debtor and the name of more than one secured party.</p>

Individual Names

Individual Names: Names of Human Beings

Correct Name: The name by which a person is generally known, for nonfraudulent purposes, in the community.

What community? It might be a different community for different legal purposes.

Upshot: May be no one “correct” name for a debtor, so a search can be complicated.

In re Kinderknecht (Clark v. Deere and Co.)

Facts:	Undisputed that the debtor’s legal name is “Terrance Joseph Kinderknecht” and that he informally goes by “Terry”. Deere took a security interest in two farm implements, timely and promptly filing financing statements under the name “Terry J. Kinderknecht”. Kinderknecht filed BK 7. Petition is under “Terrance J. Kinderknecht” and signed “Terry Kinderknecht”. BK trustee attempting to avoid a lien on Kinderknecht’s farm implements based on BKC § 544(a)(1).
Issue:	Was the name “Terry J. Kinderknecht” sufficient to provide the name of the debtor under the meaning of UCC § 9-503?
Rule:	A legal name is necessary to sufficiently provide the name of an individual debtor within the meaning of § 9-503.
Holding:	By using the debtor’s nickname in a financing statement, Deere failed to provide the name of the debtor under the meaning of § 9-503, so their financing statements are inadequate under § 9-502(a). Since they do not provide the name of the debtor, they are seriously misleading pursuant to § 9-506(b). The § 9-506(c) provision that the filing is sufficient if it would be turned up under that filing office’s search logic using the correct name doesn’t apply, since a search didn’t bring it up.
Reasoning:	The rule is supported by four practical considerations: 1. Sets a clear test so as to simplify the drafting of financing statements. 2. Setting a clear test simplifies the search process. 3. Avoids litigation over the appropriateness of a nickname or whether a reasonable person would have guessed it. 4. Obtaining the debtor’s legal name isn’t difficult and will help the new creditor suss out liens.

Corporate Names

UCC § 9-102(a)(70)	“Registered organization” means an organization organized solely under the law of a single State or the United States and as to which the State or the United States must maintain a public record showing the organization to have been organized.
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Examples: Corporations, LLCs, LPs, LLPs. Lumped together for these purposes as Corporations.

Corporations: Can be formed by obtaining a *charter* or *certificate of incorporation* from the secretary of state of one of the states. This charter will show the *one and only* legal name of the corporation. A corporation will **only have one legal name**.

1. In the **majority** of states, the name must show that the entity is a corporation.
2. **No state** will allow the formation of two corporations with the same name.

Partnership Names

Note: Limited partnerships are covered under corporations.

General partnerships are formed by contract, express or implied. No state registration is required or permitted.

Regardless of the agreement of the partners, **the legal name of a general partnership is the name by which it is generally known in the community.**

Trade names

Trade or fictitious name: A name under which a person or entity conducts business that isn’t their legal name. Most states have a “fictitious name” statute requiring every person or entity doing business in a name other than its own file notice in a public record system provided for that purpose.

Trade names are too uncertain and too likely not to be known to the secured party or the searching party. Trade names are not necessary to file a lien, nor does filing under a trade name alone make a filing sufficient. §§9-503(b) and (c).

The Entity Problem

Who or what can have a name?

UCC § 9-102(a)(28) A debtor is a “person”	(A) a person having an interest, other than a security interest or other lien, in the <u>collateral</u> , whether or not the person is an <u>obligor</u> ;
UCC § 1-201(b)(27) A person is an individual, corporation, or any other legal or commercial entity.	"Person" means an individual, corporation, business trust, estate, trust, partnership, limited liability company, association, joint venture, government, governmental subdivision, agency, or instrumentality, public corporation, or any other legal or commercial entity.

Errors in the Debtors’ Names on Financing Statements

If a searcher uses the correct name of the debtor, but does not find the prior filing because the prior secured party listed an incorrect name for the debtor on the financing statement, the prior filing is ineffective. UCC §§ 9-503(a), 9-506(a), 9-506(c).

If the search is made under the correct name but doesn’t turn anything up because a filing with the correct name was mis-indexed, the prior filings are effective. UCC § 9-517

Rule: When the sufficiency of a debtor’s name as provided in a financing statement is challenged, the test is whether a hypothetical search by a trustee or later lender under the correct name of the debtor *would have found* the financing statement. UCC § 9-506(c)

The hypothetical search should be done records of the filing office using the office’s standard search logic.

IACA Model Administrative Rules

1. Does not distinguish between upper and lower case letters.
2. Disregards punctuation marks and accents.
3. Ignores words such as “corporation, corp, incorporated, LLC, or ‘a Georgia corporation’” that would indicate the existence or nature of a corporation.
4. Ignore the word “the” at the beginning of the name.
5. Ignores spaces
6. Treats an initial as the equivalent of a first or middle name beginning with that letter.
7. Treats no middle name as all middle names.

The test is to enter the correct name and apply the official search logic. Whatever is found is effective, what is not is ineffective.

In re Spearing Tool and Manufacturing Co, Inc. (United States v. Crestmark Bank)

Facts:	4/1998, Spearing Tool and Manufacturing and Crestmark entered into a lending agreement granting Crestmark a security interest in all of Spearing’s assets. Crestmark filed a financing statement under the UCC, identifying Sparing as “Spearing Tool and Manufacturing Co.”, the precise name registered with the Michigan Secretary of State. On October 15, 2001, the IRS filed two notices of federal tax lien against Spearing with the MI Secretary of State, describing Spearing as “SPEARING TOOL & MFG. COMPANY INC.” While this wasn’t the precise name registered with MI SOS, it was the name that Spearing used on a couple of tax filings. Crestmark submitted lien search records to the MI SOS, using Spearing’s exact registered name. MI only has limited search logic that did not pull up the IRS liens. Crestmark advanced more funds to Spearing based on no prior liens.
Issue:	Which entity has lien priority?

Rule:	Form and content of a filing shall be prescribed by the US Treasury Secretary and will be “valid notwithstanding any other provision of law regarding the form or content of a notice of lien.” The plain text of the statute and IRS regulations indicates that Form 668 notice suffices, regardless of state law.
Issue:	How much specificity does federal law require for taxpayer identification on tax liens?
Rule:	The critical issue in determining whether an abbreviated or erroneous name sufficiently identifies a taxpayer is whether a “reasonable and diligent search would have revealed the existence of the federal tax liens under those names.”
Holding:	A reasonable and diligent search of Michigan’s electronic records would have revealed the tax lien.
Reasoning:	<p>Amperands are common abbreviations, as is Mfg. Crestmark knew that Spearing sometimes used these abbreviations. The MI SOS recommended searching using these abbreviations. Combined, these factors indicate that a reasonable, diligent search would have revealed these liens.</p> <p>Also, policy considerations: The purpose of the tax lien statute is to ensure prompt revenue collection, and to weaken that purpose by requiring tax liens to have absolute precision would run counter to Congressional intent. Further, to require the IRS to have 50 different filing standards for 50 different states would run counter to the principle of uniformity. Finally, the IRS is an involuntary creditor and is entitled to special consideration. The IRS interest in prompt, effective tax collection trumps the banks’ convenience in loan collection.</p>

LEE HATES THIS CASE!!!

ASSIGNMENT 18: ARTICLE 9 FINANCING STATEMENTS: OTHER INFORMATION

Introduction

Financing statements are typically pre-printed forms or electronic records entered on electronic forms.

UCC §9-521	In part, § 521 lays out a standard filing form. Not mandatory.
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Why use the standard filing form?

1. Prompts for all required information.
2. Filing fee is typically lower if the standard form is used.
3. The filing office can refuse only for the reasons stated in § 9-516(b)

UCC § 9-516(b)	<p>[Refusal to accept record; filing does not occur.] Filing does not occur with respect to a record that a filing office refuses to accept because:</p> <p>(1) the record is not communicated by a method or medium of communication authorized by the filing office;</p> <p>(2) an amount equal to or greater than the applicable filing fee is not tendered;</p> <p>(3) the filing office is unable to index the record because:</p> <p>(A) in the case of an initial financing statement, the record does not provide a name for the debtor;</p> <p>(B) in the case of an amendment or correction statement, the record:</p> <p>(i) does not identify the initial financing statement as required by Section 9-512 or 9-518, as applicable; or</p> <p>(ii) identifies an initial financing statement whose effectiveness has lapsed under Section 9-515;</p> <p>(C) in the case of an initial financing statement that provides the name of a debtor identified as an individual or an amendment that provides a name of a debtor identified as an individual which was not previously provided in the financing statement to which the record relates, the record does not identify the debtor's last name; or</p> <p>(D) in the case of a record filed [or recorded] in the filing office described in Section 9-501(a)(1), the record does not provide a sufficient description of the real property to which it relates;</p> <p>(4) in the case of an initial financing statement or an amendment that adds a secured party of record, the record does not provide a name and mailing address for the secured party of record;</p>
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	<p>(5) in the case of an initial financing statement or an amendment that provides a name of a debtor which was not previously provided in the financing statement to which the amendment relates, the record does not:</p> <p>(A) provide a mailing address for the debtor;</p> <p>(B) indicate whether the debtor is an individual or an organization; or</p> <p>(C) if the financing statement indicates that the debtor is an organization, provide:</p> <p>(i) a type of organization for the debtor;</p> <p>(ii) a jurisdiction of organization for the debtor; or</p> <p>(iii) an organizational identification number for the debtor or indicate that the debtor has none;</p> <p>(6) in the case of an assignment reflected in an initial financing statement under Section 9-514(a) or an amendment filed under Section 9-514(b), the record does not provide a name and mailing address for the assignee; or</p> <p>(7) in the case of a continuation statement, the record is not filed within the six-month period prescribed by Section 9-515(d).</p>
UCC §9-502(a)	<p>(a) [Sufficiency of financing statement.] Subject to subsection (b), a financing statement is sufficient only if it:</p> <p>(1) provides the name of the debtor;</p> <p>(2) provides the name of the secured party or a representative of the secured party; and</p> <p>(3) indicates the collateral covered by the financing statement.</p> <p>Unif.Commercial Code § 9-502</p>

To be effective, need (502(a)):

1. Name of debtor
2. Name of secured creditor
3. Indication of collateral covered.

Must refuse if 1 and 2 aren't present plus:

4. Mailing address of the secured creditor (9-516(b)(4))
5. Mailing address of the debtor. (9-516(b)(5)(A))
6. Indication of whether the debtor is an individual or corporation (9-516(b)(5)(B))

If a corporation (9-516(b)(5)(C)):

7. Type of corporation
8. Jurisdiction of incorporation
9. Organizational identification number

If any of these requirements are missing other than an indication of the collateral, the filing officer should refuse. **However, the filing officer should not refuse INCORRECT information, even if its implausible.**

UCC § 9-516 cmt. 3	Neither this section nor Section 9-520 requires or authorizes the filing office to determine, or even consider, the accuracy of information provided in a record. For example, the State A filing office may not reject under subsection (b)(5)(C) an initial financing statement indicating that the debtor is a State A corporation and providing a three-digit organizational identification number, even if all State A organizational identification numbers contain at least five digits and two letters.
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Filing Office Errors in Acceptance or Rejection

Wrongly Accepted Filings

If a filing officer mistakenly accepts a filing that contains 1 through 3, but is missing another item that would have required them to reject, the filing is effective.

UCC § 9-520(c)	[When filed financing statement effective.] A filed financing statement satisfying Section 9-502(a) and (b) is effective, even if the filing office is required to refuse to accept it for filing under subsection (a). However, Section 9-338 applies to a filed financing statement providing information described in Section 9-516(b)(5) which is incorrect at the time the financing statement is filed.
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Why?

Nobody can be misled by the filing!

Also, the filer doesn't have good notice of the problem. Had the filing officer done his job, the filer could have corrected.

Wrongly Rejected Filings

A filing officer will stamp a rejected financing statement with the date and time it was received. The failed attempt to file nevertheless perfects the underlying security interest so as to defeat **lien creditors**³. The Drafters felt that lien creditors generally don't search the filing system anyhow, so they're not prejudiced.

UCC § 9-520(b)	[Communication concerning refusal.] If a filing office refuses to accept a record for filing, it shall communicate to the person that presented the record the fact of and reason for the refusal and the date and time the record would have been filed had the filing office accepted it. The communication must be made at the time and in the manner prescribed by filing-office rule but [, in the case of a filing office described in Section 9-501(a)(2),] in no event more than two business days after the filing office receives the record.
UCC § 9-516(d)	[Refusal to accept record; record effective as filed record.] A record that is communicated to the filing office with tender of the filing fee, but which the filing office refuses to accept for a reason other than one set forth in subsection (b), is effective as a filed record except as against a purchaser of the collateral which gives value in reasonable reliance upon the absence of the record from the files.

However, this security interest is not effective against **purchasers**⁴, because they are prejudiced by the failure of the record to appear in the filing system.

This is referred to as **lien-perfected**.

Filer Errors in Accepted Filings

If a filer omits from a financing statement a piece of information required in § 9-516(b), the filing officer can and should reject. However, if the information is merely incorrect, the filing officer should accept it.

Information Necessary Only to Qualify for Filing

If the information in items 4-9 is merely erroneous, the financing statement qualifies for filing. However, it will be of limited effectiveness.

They will be considered **lien perfected** but not against **purchasers for value**.

UCC § 9-338	If a security interest or agricultural lien is perfected by a filed financing statement providing information described in Section 9-516(b)(5) which is incorrect at the time the financing statement is filed: (1) the security interest or agricultural lien is subordinate to a conflicting perfected security interest in the collateral to the extent that the holder of the conflicting security interest gives value in reasonable reliance upon the incorrect information; and (2) a purchaser, other than a secured party, of the collateral takes free of the security interest or agricultural lien to the extent that, in reasonable reliance upon the incorrect
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³ Lien creditors hold judgments. Cf. to contractual creditors.

⁴ Including secured parties!

	information, the purchaser gives value and, in the case of chattel paper, documents, goods, instruments, or a security certificate, receives delivery of the collateral.
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Only a purchaser who gives value in reasonable reliance on the incorrect information defeats the filing!

If the address of the secured party is incorrect, it does not render the financing statement ineffective, nor is it the basis to subordinate the secured party. The only real penalty is that they are deemed to have received any notification mailed to the incorrect address. §9-502, §9-338, §9-516 cmt. 5.

Required Information

If the filing statement substantially complies with the requirement to specify items 1-3, the financing statement will be effective despite minor errors and omissions, unless the errors or omissions make the financing statement seriously misleading.

UCC § 9-506(a)	(a) [Minor errors and omissions.] A financing statement substantially satisfying the requirements of this part is effective, even if it has minor errors or omissions, unless the errors or omissions make the financing statement seriously misleading.
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Seriously Misleading: Depends on the function that information serves in the search process.

Name of the Secured Party

Searchers may need the name of the secured party for two reasons.

1. May need to contact to obtain a termination, releases, subordinations that may be needed for a new loan.
2. May need some information from the secured party.
Secured parties are able to give information regarding their security interest without violating privacy laws, but not required to give to third parties. Must do so on request of debtor. UCC § 9-210.

Indication of Collateral

Difference between an “indication” and a “description.”

Indication is much more vague—all it needs to do is serve notice you might want to check it out.

“All assets” constitutes an indication, while it doesn’t constitute a description.

UCC § 9-504	A financing statement sufficiently indicates the collateral that it covers if the financing statement provides: (1) a description of the collateral pursuant to Section 9-108; or (2) an indication that the financing statement covers all assets or all personal property.
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Example: A lender anticipates multiple loans, files financing statement with “equipment” as description. Each time he advances, he requires the debtor to authenticate a new security agreement detailing the equipment purchased. Under these circumstances, the creditor has a perfected security interest in the equipment described in the security agreement, not all the equipment.

The general standard for adequacy of a financing statement description is that it reasonable identify the collateral. (9-108, 9-504)

“Objectively determinable”

1. What meaning should be assigned to the words?
In the security agreement, it’s intention of the party. The purpose of the financing statement is THIRD PARTY notice-look to the common meaning and require that it makes sense to a complete stranger.
2. How much work are we going to require these third parties to do?
Schmidt: Referring to ACSC records requires the searcher to know what that is and to go look. Upheld.
Shirel: Reference to whether the item was purchased from the store requires a searcher to gain access to the department store records and examine them. No way.

In re Grabowski: Traditional view that a searcher can make an inquiry of the secured creditor. Despite generality, it gave notice that a lien existed on the Debtor's property.

Teel Construction, Inc. v. Lipper, Inc.: Even broader view. Even though the address on the financing statement was nonexistent and the debtor was at another location, it still gave notice sufficient that a searcher would go to the correct address and figure it out, particularly as under facts the searcher knew where debtor was located and it wasn't there.

What, exactly, are these good for? Who knows!

Prof. Morris Shanker: Descriptions of collateral in security agreements and financing statements should be optional. If the parties don't include a description, it covers all property as opposed to none (as now.) Considering the searcher has to inquire beyond the description anyhow, it wouldn't make a difference.

In re Pickle Logging, Inc. (Deere Credit v. Pickle Logging, Inc.)

Facts:	In order to cure an arrearage with Deere, Pickle refinanced eight pieces of equipment. On 4/18/2002, Pickle filed for BK11. One of the financing statements incorrectly described one of the pieces of equipment as a 648G skidder, SN DW648GX568154 when it was really a 548 skidder, SN DW548GX568154.
Issue:	Was Deere's security interest in the 548G skidder perfected despite the mislabeling on the security agreement and the financing statement?
Rule:	The description of collateral is sufficient if it reasonably identifies what is described. § 9-108(a).
Held:	The rights of Pickle, as hypothetical lien creditor, are superior to Deere.
Reas:	Nothing is obviously wrong with the descriptions of the collateral. The serial number is wrong in a way consistent with the model being wrong. The debtor actually owns some skidders of that model number. Nothing alerts a potential creditor that this property doesn't have clear title.

Authorization to File a Financing Statement

The purpose of a financing statement is to advise later lenders of the existence of a prior security interest. The presence of an incorrect or unauthorized financing statement in the filing system can interfere with the ability of the party named as debtor to borrow money.

Clouded Title: Title to possibly encumbered title. Lenders hate to go forward under clouded title-it must be "cleared" first.

Sure, you could file suit, but it's expensive, and dickheads like tax protestors and prisoners (who may be judgment proof) love to file bullshit financing statements. Texas has made it a felony to keep people from pulling this stunt.

Before filing a lien, you must obtain authorization from the debtor. However, the only authorization is an authenticated security agreement.

UCC § 9-509(a)(1)	(a) [Person entitled to file record.] A person may file an initial financing statement, amendment that adds collateral covered by a financing statement, or amendment that adds a debtor to a financing statement only if: (1) the debtor authorizes the filing in an authenticated record or pursuant to subsection (b)
UCC § 9-509(b)	(b) [Security agreement as authorization.] By authenticating or becoming bound as debtor by a security agreement, a debtor or new debtor authorizes the filing of an initial financing statement, and an amendment, covering: (1) the collateral described in the security agreement; and (2) property that becomes collateral under Section 9-315(a)(2), whether or not the security agreement expressly covers proceeds.

UCC § 9-510(a)	(a) [Filed record effective if authorized.] A filed record is effective only to the extent that it was filed by a person that may file it under Section 9-509.
UCC § 9-518(a)	(a) [Correction statement.] A person may file in the filing office a correction

	statement with respect to a record indexed there under the person's name if the person believes that the record is inaccurate or was wrongfully filed.
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So a person can file a correction statement, which will appear in the records on a search. BFD, though. The unauthorized statement was ineffective and remains ineffective after the filing, and it doesn't lift the cloud.

UCC Insurance

Similar to title insurance, but doesn't cover the possibility that the debtor doesn't own the collateral. However, it does cover errors in the filing and search process.

ASSIGNMENT 19: EXCEPTIONS TO THE ARTICLE 9 FILING REQUIREMENT

Four Ways to Perfect:

1. Filing
2. Possession
3. Control
4. Operation of Law

Collateral in the Possession of the Secured Party

Possession Gives Notice Theory

UCC § 9-310(b)(6)	The filing of a financing statement is not necessary to perfect a security interest: in collateral in the secured party's possession under Section 9-313
UCC § 9-313(a)	Except as otherwise provided in subsection (b), a secured party may perfect a security interest in negotiable documents, goods, instruments, money, or tangible chattel paper by taking possession of the collateral. A secured party may perfect a security interest in certificated securities by taking delivery of the certificated securities under Section 8-301.

Grounded on two assumptions:

1. A person who buys or lends against certain kinds of collateral will look at the collateral before lending against it.
2. Looking at collateral in the possession of a secured party will alert the searcher to the possible existence of a security interest.

Under the Possession-Gives-Notice theory, it would be redundant to file as the searcher would have actual notice.

Both Article 9 and real estate recording laws assume that when a secured party is in possession of the collateral, searchers will or should realize there is a security interest.

This reflects an important assumption of secured transactions law: the relatively sophisticated party is favored at the expense of people who don't know what they're doing.

What Is Possession?

possession. 1. The fact of having or holding property in one's power; the exercise of dominion over property. [Cases: Property 10. C.J.S. *Property* §§ 27–31, 33.] 2. The right under which one may exercise control over something to the exclusion of all others; the continuing exercise of a claim to the exclusive use of a material object. Black's Law Dictionary (8th ed. 2004)

The law looks to legal right, not just physical fact, to determine who is in possession.

At the moment someone exercises physical dominion over an object, possession passes to them. This is “naked” possession: the act of physical dominion without legal right.

A secured party may also possess through an agent.

UCC § 9-313 cmt 3	3. “Possession.” This section does not define “possession.” It adopts the general concept as it developed under former Article 9. As under former Article 9, in determining whether a particular person has possession, the principles of agency apply. For example, if the collateral is in possession of an agent of the secured party for the purposes of possessing on behalf of the secured party, and if the agent is not also an agent of the debtor, the secured party has taken actual possession, and subsection (c) does not apply.
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Look at Page 329 for a discussion of possession.

Possession as a Means of Perfection

Possession is an *alternative* means of perfection for some types of collateral, *ineffective* for others, and *sole* form of perfection for placing a security interest in money.

UCC § 9-312(b)(3)	a security interest in money may be perfected only by the secured party's taking possession under Section 9-313.
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With regard to goods, instruments, tangible chattel paper, negotiable documents, and certificated securities, possession is an *alternative* to filing a financing statement. For all of these **but** goods, it is **superior** to perfection by filing.

UCC § 9-312(a)	(a) [Perfection by filing permitted.] A security interest in chattel paper, negotiable documents, instruments, or investment property may be perfected by filing.
UCC § 9-313(a)	(a) [Perfection by possession or delivery.] Except as otherwise provided in subsection (b), a secured party may perfect a security interest in negotiable documents, goods, instruments, money, or tangible chattel paper by taking possession of the collateral. A secured party may perfect a security interest in certificated securities by taking delivery of the certificated securities under Section 8-301.

NOTE: Negotiable documents includes negotiable warehouse receipts, negotiable bills of lading, and similar documents but NOT negotiable promissory notes.

Purchasers who subsequently take possession of negotiable documents generally take priority over secured creditors who previously perfected by filing.

UCC § 9-330(d)	(d) [Instrument purchaser's priority.] Except as otherwise provided in Section 9-331(a), a purchaser of an instrument has priority over a security interest in the instrument perfected by a method other than possession if the purchaser gives value and takes possession of the instrument in good faith and without knowledge that the purchase violates the rights of the secured party.
UCC § 9-331(a)	(a) [Rights under Articles 3, 7, and 8 not limited.] This article does not limit the rights of a holder in due course of a negotiable instrument, a holder to which a negotiable document of title has been duly negotiated, or a protected purchaser of a security. These holders or purchasers take priority over an earlier security interest, even if perfected, to the extent provided in Articles 3, 7, and 8.

However, filing does trump lien creditors and bankruptcy trustees.

However, some types of collateral make perfection by possession impossible:

Accounts

General intangibles. (See UCC 9-313(a) above)

Policy:

By excluding the possibility of perfection by filing, Article 9 protects those who accept money from the possibility that a prior security interest was perfected by filing. The intent is to encourage the free negotiability of money, unhampered by the need to conduct searches in the Article 9 filing system. Both “money” and “instrument” are carefully defined in the UCC and refer only to specialized types of property. (LoPucki and Warren)

UCC § 1-201(b)(24)	(24) “Money” means a medium of exchange currently authorized or adopted by a domestic or foreign government. The term includes a monetary unit of account established by an intergovernmental organization or by agreement between two or more countries.
UCC § 9-102(a)(47)	“Instrument” means a negotiable instrument or any other writing that evidences a right to the payment of a monetary obligation, is not itself a security agreement or lease, and is of a type that in ordinary course of business is transferred by delivery with any necessary indorsement or assignment. The term does not include (i) investment property, (ii) letters of credit, or (iii) writings that evidence a right to payment arising out of the use of a credit or charge card or information contained on or for use with the card.

The perfection of security interests in both instruments and chattel paper by filing is permitted by § 9-312(a). However § 9-330 protects purchasers who subsequently take possession of chattel paper or instruments.

Collateral in the Control of the Secured Party

Control of some types of collateral as a substitute for filing

1. Deposit Accounts
2. Electronic Chattel Paper
3. Investment Property
4. Letter of Credit Rights

UCC § 9-310(b)(8)	[Exceptions: filing not necessary.] The filing of a financing statement is not necessary to perfect a security interest: in deposit accounts, electronic chattel paper, investment property, or letter-of-credit rights which is perfected by control under Section 9-314;
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A “deposit account” is a bank account, but not CDs.

UCC § 9-102(a)(29)	“Deposit account” means a demand, time, savings, passbook, or similar account maintained with a bank. The term does not include investment property or accounts evidenced by an instrument.
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Three ways to take “control” of a bank account:

1. Secured party is the bank
2. The debtor, the secured party, and the bank authenticate a record instructing the bank to comply with the secured party’s instructions with regard to the account.
3. The secured party becomes the bank’s customer by putting their name on the account.

UCC § 9-104	(a) [Requirements for control.] A secured party has control of a deposit account if: (1) the secured party is the bank with which the deposit account is maintained; (2) the debtor, secured party, and bank have agreed in an authenticated record
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	<p>that the bank will comply with instructions originated by the secured party directing disposition of the funds in the deposit account without further consent by the debtor; or</p> <p>(3) the secured party becomes the bank's customer with respect to the deposit account.</p> <p>(b) [Debtor's right to direct disposition.] A secured party that has satisfied subsection (a) has control, even if the debtor retains the right to direct the disposition of funds from the deposit account.</p> <p>Unif.Commercial Code § 9-104</p>
UCC § 4-104(a)(5)	<p>(5) "Customer" means a person having an account with a bank or for whom a bank has agreed to collect items, including a bank that maintains an account at another bank</p> <p>Unif.Commercial Code § 4-104</p>

UCC § 9-104(a)(2) does not require that an agreement be made public. Secret liens are authorized!

UCC § 9-102(c)(49)	<p>"Investment property" means a security, whether certificated or uncertificated, security entitlement, securities account, commodity contract, or commodity account.</p> <p>Unif.Commercial Code § 9-102</p>
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Certificated Securities	Uncertificated
If represented by a paper certificate	Simply acknowledged on monthly statement of account.
<p>Take control by obtaining delivery of the certificate along with any necessary indorsement or by registering the secured party as the owner of the securities on the stock transfer book of the issuing corporation. §8-106(b)</p> <p>Delivery is the transfer of possession § 8-301(a)(1)</p> <p>OR</p> <p>Taking possession without necessary indorsement §8-301(a)(1) and § 9-313(a)</p>	<p>1. Become the registered owner of the security on the books of the issuers. UCC § 8-106(c)(1), 8-301(b).</p> <p>2. Obtain the agreement of the securities intermediary that the intermediary holds control for the secured party. § 8-106(d)</p> <p>OR</p> <p>Filing a financing statement § 9-312(a)</p>

However, the ORS lose to a secured party who perfects by control. UCC § 9-328.

Take control of a securities account by taking control of the securities contained in it.

UCC §9-106(c)	A secured party having control of all security entitlements or commodity contracts carried in a securities account or commodity account has control over the securities account of commodity account.
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Automatic Perfection of a PMSI in Consumer Goods

UCC § 9-309(1)	<p>The following security interests are perfected when they attach:</p> <p>(1) a purchase-money security interest in consumer goods, except as otherwise provided in Section 9-311(b) with respect to consumer goods that are subject to a statute or treaty described in Section 9-311(a);</p>
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A PMSI in consumer goods is perfected when it attaches.

Purchase Money Security Interest

UCC § 9-103(a)	a) [Definitions.] In this section: (1) “purchase-money collateral” means goods or software that secures a purchase-money obligation incurred with respect to that collateral; and (2) “purchase-money obligation” means an obligation of an obligor incurred as all or part of the price of the collateral or for value given to enable the debtor to acquire rights in or the use of the collateral if the value is in fact so used.
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LoPucki likes the former definition better:

A security interest is a “purchase money security interest” to the extent that it is:
(a) taken or retained by the seller of collateral to secure all or part of its purchase price; or
(b) taken by a person who by making advances or incurring an obligation gives value to enable the debtor to acquire rights in or the use of collateral if such value is in fact so used.

Consumer Goods

PMSI is only automatically perfected in **consumer goods**.

Remember: it is not the **nature** of the goods but the use to which they are put or the purpose for which they are bought.

Courts and commentators seem to agree that this only makes sense when we’re looking at small value items, but the UCC does not make that distinction.

Gallatin National Bank v. Lockovich

Facts:	Lockoviches purchased a yacht with loan from Gallatin. They defaulted by failing to make payments. Before Gallatin could repossess, Debtors filed for Chapter 11. Gallatin did not file a financing statement.
Issue:	Whether Gallatin must file a financing statement to perfect its security interest in the boat.
Rule:	To perfect a security interest in collateral under the UCC 9-501, a secured party must file a financing statement in the offices of the Secretary of State. Under UCC 9-309, there are several exceptions to this rule depending on the type of collateral. 9-309(1) allows an exception for PMSI.
Issue1:	What is PMSI?
Held:	Indisputable that what Gallatin held was a PMSI
Issue2:	What are “consumer goods”?
Rule:	Goods are consumer goods if they are used or bought for use primarily for personal, family or household purposes. They are not classified based on design or intrinsic nature, but according to the use the owner puts them.
Issue3:	Can massive and expensive items qualify as consumer goods?
Rule:	Under the clear mandate of the Code, a consumer good subject to the exception from the filing of financing statements is determined by the use or intended use of the good: design, size, weight, shape and cost or irrelevant.
Held:	This was a consumer good.
Reas:	Creditors must be confident that when they enter into a commercial transaction, they will play by the rules as written in the Code. Creditors, subsequent creditors, and subsequent purchasers have options available to them that lend appropriate protection. To determine what protections are available by interstitial lawmaking may defeat the intent of the legislature.

What if goods are bought for one purpose but put to another?

The intended use at the time of purchase should control. Creditors should be able to rely on their debtors’ written representations of intended use.

This may miss the point: future searchers are the ones who will bear the brunt of the debtors’ misrepresentation. (Will they? It seems more likely that a debtor who misrepresents will be in bankruptcy than they will be able to obtain additional financing...)

Goods cannot be consumer goods when owned by a corporation.

CHAPTER 7: MAINTAINING PERFECTION

ASSIGNMENT 22: MAINTAINING PERFECTION THROUGH LAPSE AND BANKRUPTCY

Removing Filings from the Public Record

A filing serves as constructive notice to the world that a security interest may be outstanding against the property of the debtor.

When the debt is paid, both debtor and creditor typically want to remove the filing: the creditor doesn't want to be bothered by inquiries anymore, the debtor doesn't want to have to explain the filing all the time. Can't really remove-just add another document saying the earlier document is no longer in force.

Satisfaction

Real Estate

When a real estate mortgage is paid, the mortgagee executes a *satisfaction of mortgage*.

Both the mortgage and the satisfaction remain in the real estate filing office permanently.

Even if the mortgage is paid, if no satisfaction recorded there is still a cloud on the title.

Because of the satisfaction is so important, many states have penalties for those who do not file satisfactions promptly.

Examples:

A. If any person receiving satisfaction of a mortgage or deed of trust shall, within thirty days, fail to record or cause to be recorded, with the recorder of the county in which the mortgage or deed of trust was recorded, a sufficient release, satisfaction of mortgage or deed of release or acknowledge satisfaction as provided in § 33-707, subsection C, he shall be liable to the mortgagor, trustor or current property owner for actual damages occasioned by the neglect or refusal.

B. If, after the expiration of the time provided in subsection A of this section, the person fails to record or cause to be recorded a sufficient release and continues to do so for more than thirty days after receiving a written request which identifies a certain mortgage or deed of trust by certified mail from the mortgagor, trustor, current property owner or his agent, he shall be liable to the mortgagor, trustor or current property owner for one thousand dollars, in addition to any actual damage occasioned by the neglect or refusal.

Ariz. Rev. Stat. Ann. § 33-712

Whenever the amount of money due on any mortgage, lien, or judgment shall be fully paid to the person or party entitled to the payment thereof, the mortgagee, creditor, or assignee, or the attorney of record in the case of a judgment, to whom such payment shall have been made, shall execute in writing an instrument acknowledging satisfaction of said mortgage, lien, or judgment and have the same acknowledged, or proven, and duly entered of record in the book provided by law for such purposes in the proper county. Within 60 days of the date of receipt of the full payment of the mortgage, lien, or judgment, the person required to acknowledge satisfaction of the mortgage, lien, or judgment shall send or cause to be sent the recorded satisfaction to the person who has made the full payment. In the case of a civil action arising out of the provisions of this section, the prevailing party shall be entitled to attorney's fees and costs.

Fla. Stat. Ann. § 701.04 (West)

R (Mortgages) § 6.4

All courts can order immediate satisfaction, notwithstanding a statute to the contrary.

Release

If a mortgage encumbers more than one parcel of real property, the debtor may wish to sell one parcel without paying off the entire loan. A mortgagee may file a release to accomplish this. However, absent a release provision, the mortgagee is under NO obligation to do so.

Article 9 Termination and Release

If the debtor has paid the obligation and the secured party is not required by K to lend more, the debtor can demand that the secured party file a termination statement within 20 days. If they fail to do so, subject to actual damages + \$500 civil penalty

UCC § 9-513(c)(1)	(c) [Other collateral.] In cases not governed by subsection (a), within 20 days after a secured party receives an authenticated demand from a debtor, the secured party shall cause the secured party of record for a financing statement to send to the debtor a termination statement for the financing statement or file the termination statement in the filing office if: (1) except in the case of a financing statement covering accounts or chattel paper that has been sold or goods that are the subject of a consignment, there is no obligation secured by the collateral covered by the financing statement and no commitment to make an advance, incur an obligation, or otherwise give value; Unif.Commercial Code § 9-513
UCC § 9-625(b)	(b) [Damages for noncompliance.] Subject to subsections (c), (d), and (f), a person is liable for damages in the amount of any loss caused by a failure to comply with this article. Loss caused by a failure to comply may include loss resulting from the debtor's inability to obtain, or increased costs of, alternative financing.
UCC § 9-625(e)(4)	(e) [Statutory damages: noncompliance with specified provisions.] In addition to any damages recoverable under subsection (b), the debtor, consumer obligor, or person named as a debtor in a filed record, as applicable, may recover \$500 in each case from a person that: (4) fails to cause the secured party of record to file or send a termination statement as required by Section 9-513(a) or (c);

Release is accomplished by filing an amendment that identifies file number of the initial financing statement and that the identified financing statement is no longer in effect.

UCC § 9-512(a)	[Amendment of information in financing statement.] Subject to Section 9-509, a person may add or delete collateral covered by, continue or terminate the effectiveness of, or, subject to subsection (e), otherwise amend the information provided in, a financing statement by filing an amendment that:
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Since an amendment is part of the original financing statement, it is subject to the seriously misleading test of 9-506.

“Self Clearing” and Continuation in the Article 9 System

Self-clearing: Financing statements are only effective for five years.

Continuation Statement: A continuation statement must be filed no sooner than six months before the termination of the financing statement in order to retain priority.

UCC § 9-515(a)	[Five-year effectiveness.] Except as otherwise provided in subsections (b), (e), (f), and (g), a filed financing statement is effective for a period of five years after the date of filing.
UCC § 9-515(c)	[Lapse and continuation of financing statement.] The effectiveness of a filed financing statement lapses on the expiration of the period of its effectiveness unless

	before the lapse a continuation statement is filed pursuant to subsection (d). Upon lapse, a financing statement ceases to be effective and any security interest or agricultural lien that was perfected by the financing statement becomes unperfected, unless the security interest is perfected otherwise. If the security interest or agricultural lien becomes unperfected upon lapse, it is deemed never to have been perfected as against a purchaser of the collateral for value.
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Worthen Bank & Trust Co., N.A. v. Hilyard Drilling Co. (In re Hilyard Drilling Co.)

Facts:	4/25/79 Hilyard→(SI)→NC all of its existing and future accounts receivable and proceeds thereof. Perfected by filing on 4/26/79. 4/28/83, Worthen wrote to Hilyard stating “We acknowledge [NBC’s] first lien and would be happy to do so in writing so that it is clear to everyone that our lien is junior to theirs.” NBC did not request. 6/14/83 Hilyard granted Worthen a security interest in the same accounts receivable. Neither Worthen’s loan documents nor their filing statement indicated their security interest was junior. NBC did not file a continuation statement before expiration of financing statement on 4/25/1984. On 7/8/84 Hilyard wrote to Worthen stating that Hilyard had previously assigned security interest in collateral to NBC and that intention of all parties that Worthen would be junior lien. Also on 7/8/1983 NBC filed a new financing statement. Hilyard filed ch. 11 on 1/25/1985.
Issue:	What is the priority of Worthen’s security interest with respect to NBC’s security interest?
Issue1:	Was Worthen’s 7/8/1983 financing statement “harmless error” and as such should be considered a continuation?
Rule:	Financing statements and continuation statements serve distinct and different purposes. A financing statement that does not refer to the original filing cannot suffice as a continuation statement.
Held:	NBC’s failure to file a continuation statement cannot be considered harmless error, because the second financing statement gave no indication that it was filed for the purpose of continuing any other financing statement.
Reas:	Even though Worthen had notice, no other searcher did. The purpose of the UCC requirements is to provide predictability.
Issue2:	Does NBC have priority because its interest was continuously perfected from 4/26/79?
Rule:	UCC 9-515(c) states that if a filing statement isn’t continued, it lapses.
Held:	Worthen’s security interest had first priority pursuant to §9-322(a)(1).
Reas:	When the first perfection lapsed, all others advanced. NBC’s perfection was first and third, Worthen second. When NBC’s first perfection lapsed, Worthen moved into first. Bringing up 9-308(c) is nonsense-it refers to a situation where security interests are perfected first one way then another.

Courts are generally harsh in their treatment of errors in filing continuation statements, even if nobody was prejudiced by the error.

Doctrinal argument: If the financing statement lapsed, there was nothing TO continue.

Upon lapse, a security agreement becomes unperfected, and is deemed never to have been perfected as against a purchaser of the collateral for value. 9-515(c). *This does not apply to a lien creditor or a BK trustee.* However, the security interest will be subordinate to a lien creditor who levies AFTER the lapse or a BK trustee in an action filed after the lapse.

The Effect of Bankruptcy on Lapse and Continuation

A secured party must file continuation statements at five-year intervals to avoid lapse. No exception is made because the debtor has filed bankruptcy. The filing of continuation statements does not violate the automatic stay.

11 USC § 362(b)(3)	under subsection (a) of this section, of any act to perfect, or to maintain or continue the perfection of, an interest in property to the extent that the trustee's rights and powers are subject to such perfection under section
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	546(b) of this title or to the extent that such act is accomplished within the period provided under section 547(e)(2)(A) of this title;
11 USC § 546(b)(1)(B)	(b)(1) The rights and powers of a trustee under sections 544, 545, and 549 of this title are subject to any generally applicable law that-- (A) permits perfection of an interest in property to be effective against an entity that acquires rights in such property before the date of perfection; or (B) provides for the maintenance or continuation of perfection of an interest in property to be effective against an entity that acquires rights in such property before the date on which action is taken to effect such maintenance or continuation.

In re Schwinn Cycling and Fitness, Inc. (Expeditors International of Washington, Inc. v. The Liquidating Trust)

Facts:	Contract between Schwinn and EIWI provided that EIWI had a general lien and security interest in all of the debtor's property in its possession, custody, or control. 7/16/01 Schwinn filed Chapter 11. Within the 20 days pre-petition, EIWI had possession some of Schwinn's goods. EIWI transferred possession of these goods to Schwinn, who sold them. Either shortly before or after petition, Schwinn (or the BK estate) had possession of the cash proceeds from the goods. Parties agreed that prior to the petition date, EIWI had a perfected security interest in the goods and proceeds from the goods. EIWI had perfected by possession of the goods, but did not file a financing statement with respect to the goods within 20 days after it relinquished custody to Schwinn.
Issue:	Did EIWI need to file a financing statement within 20 days in order to perfect its security interest notwithstanding the intervening bankruptcy petition?
Rule:	9-313(a)-A secured party may perfect a security interest in goods by taking possession of the collateral. 9-313(d)-If perfection of a security interest depends on possession of the collateral by a secured party, perfection occurs no earlier than the time the secured party takes possession and <i>continues only while the secured party retains possession</i> . 9-312(f)-a perfected security interest in...goods in possession of a bailee...remains perfected for twenty days without filing if the secured party makes available to the debtor the goods or documents representing the goods for the purpose of ultimate sale or exchange ... 9-312-after the twenty-day period, perfection depends upon compliance with this article.
Held:	Notwithstanding the bankruptcy, to be perfected EIWI should have filed a financing statement.
Reas:	Freezing priorities on the initiation of bankruptcy would lead to secret liens. The provisions referenced don't make mention of an extension based on bankruptcy proceedings.

General Electric Capital Corporation v. Dial Business Forms

Secured creditor's security interest lapsed during bankruptcy. The reorganization plan provided that a class of unsecured creditors held a subordinate interest in the same asset as the secured party held a security interest. The unsecured parties claimed priority, court said no.

A plan of reorganization acts like a contract that binds the parties that participate in the plan, including those who voted against it. A reference to an unsecured creditor's interest as subordinated constitutes a subordination agreement that was independent of the secured creditor's security interest.

ASSIGNMENT 23: MAINTAINING PERFECTION THROUGH CHANGES OF NAME, IDENTITY, AND USE.

Remember: It's not that the law imposes a duty on searchers or filers to do anything, it simply allocates losses in case they don't.

Changes in a Debtor's Name

If a debtor changes names between the time a filing is made against the debtor and the time a search for that filing is made, the change may—or may not—cause the communication to fail.

Even though a change in the debtor's name renders a filed financing statement seriously misleading, the financing statement remains effective with regard to:

1. Collateral owned by the debtor at the time of the name change
2. Collateral acquired by the debtor in the first four months after the change

UCC 9-507(c)	<p>[Change in debtor's name.] If a debtor so changes its name that a filed financing statement becomes seriously misleading under Section 9-506:</p> <p>(1) the financing statement is effective to perfect a security interest in collateral acquired by the debtor before, or within four months after, the change; and</p> <p>(2) the financing statement is not effective to perfect a security interest in collateral acquired by the debtor more than four months after the change, unless an amendment to the financing statement which renders the financing statement not seriously misleading is filed within four months after the change.</p>
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A secured party that is financing the debtor's inventory has to pay close attention.

Most security agreements include a promise by the debtor to inform the secured party of a name change. Then again, most debtors suck and don't do it. It's breach, but if they file on you, tough shit.

Systems created in the United States are designed to function without the cooperation of the debtor.

B.T. Lazarus v. Christofides

Creditor took security interest in the assets of BTL. Creditor didn't file financing statement for four months after signing of the security agreement. In meantime, BTL changed name to Alma Marketing. Filing was ineffective.

Barter Transactions

Barter is the exchange of one commodity for another in a transaction in which no case is involved.

UCC 9-315(d)(1)	<p>[Continuation of perfection.] A perfected security interest in proceeds becomes unperfected on the 21st day after the security interest attaches to the proceeds unless:</p> <p>(1) the following conditions are satisfied:</p> <p>(A) a filed financing statement covers the original collateral;</p> <p>(B) the proceeds are collateral in which a security interest may be perfected by filing in the office in which the financing statement has been filed; and</p> <p>(C) the proceeds are not acquired with cash proceeds;</p>
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Type 0 Barter

Proceeds fall within description of collateral in already-filed financing statement. Example: financing statement describes a Coyote loader, debtor trades for a Caterpillar. Security interest attaches to the Caterpillar loader because "loader" is broad enough to encompass.

UCC § 9-203(f)	<p>[Proceeds and supporting obligations.] The attachment of a security interest in collateral gives the secured party the rights to proceeds provided by Section 9-315 and is also attachment of a security interest in a supporting obligation for the collateral.</p>
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Type 1 Barter

An exchange of collateral for noncash proceeds not covered by the financing statement but fileable in the same office. Per 9-315(d)(1), secured party remains perfected without a new filing.

UCC § 9-315(d)	[Continuation of perfection.] A perfected security interest in proceeds becomes unperfected on the 21st day after the security interest attaches to the proceeds unless: (1) the following conditions are satisfied: (A) a filed financing statement covers the original collateral; (B) the proceeds are collateral in which a security interest may be perfected by filing in the office in which the financing statement has been filed; and (C) the proceeds are not acquired with cash proceeds; (2) the proceeds are identifiable cash proceeds; or (3) the security interest in the proceeds is perfected other than under subsection (c) when the security interest attaches to the proceeds or within 20 days thereafter.
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“Same office rule”—so long as the security interest would be filed in the same office, then remains perfected (for example, if traded inventory for a car, filer is shit out of luck on this.)

Type 2 Barter

An exchange of collateral for noncash proceeds of a type not fileable in the same office as the original collateral. These do not invoke § 9-315(d)(1) exceptions, so to be perfected the secured party must refile. For continuous perfection, the secured party must file within 20 days from the time the debtor receives to proceeds. *See* 9-315(d)(3).

The secured party does not need any additional authorization to file the financing statement necessary to perfect in the proceeds.

UCC § 9-509(b)(2)	[Security agreement as authorization.] By authenticating or becoming bound as debtor by a security agreement, a debtor or new debtor authorizes the filing of an initial financing statement, and an amendment, covering: (1) the collateral described in the security agreement; and (2) property that becomes collateral under Section 9-315(a)(2), whether or not the security agreement expressly covers proceeds.
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National Bank of Alaska v. Erickson (In re Seaway Express Corporation)

Facts:	1985-86, National Bank of Alaska provided a line of credit to Seaway secured by a credit agreement. Credit line was set as a percentage of inventory and AR aged less than 90 days. Seaway granted NBA a security interest in inventory and AR, plus proceeds. Seaway promised not to dispose of secured assets without NBA's permission. AFFS owed Seaway in excess of \$1 million, Seaway agreed to take a parcel of property in Auburn, WA in exchange. NBA did not consent to transfer. NBA asked Seaway to record a deed of trust, Seaway refused. Seaway filed BK 11 and sold the property for \$1 million.
Issue:	Does NBA have a priority interest in the proceeds of sale of the Auburn property as proceeds of proceeds from the sale of the AFFS account.
Rule:	An unrecorded interest in [real] property is not binding on a subsequent purchaser in good faith.
Held:	National Bank of Alaska? Shit out of luck.
Reas:	The UCC doesn't apply to real property, bitch!

Collateral to Cash Proceeds to Noncash Proceeds

Provided it can trace its value through both transactions, the creditor's security interest will reach the new property as proceeds of proceeds.

Type 0 Transactions

Collateral→Cash→ Same Type of Collateral. All good in the hood. See § 9-315(d)(3).

Type 1 Transactions

Collateral→Cash→Different Type of Collateral. Need a financing statement filed within 20 days to maintain priority, otherwise still need financing statement.

Type 2 Transaction

Same as above with respect to filing new lien.

Collateral to Cash Proceeds

UCC § 9-315(d)(2) gives continuous and perpetual perfection in identifiable cash proceeds.

If the debtor uses the identifiable cash proceeds to buy collateral, would still have security interest so long as files within 20 days as proceeds of proceeds.

ASSIGNMENT 24: MAINTAINING PERFECTION THROUGH RELOCATION OF DEBTOR OF COLLATERAL

State-based Filing in a National Economy

The filing system is a means for a secured creditor who takes a nonpossessory security interest in the property of a debtor to communicate the existence of that security interest to others who may later consider extending credit to that debtor.

Later searchers must be able to determine the correct filing system or systems in which to look.

Where to look and file is governed by §§9-301 – 9-307.

Initial Perfection

At the Location of the Debtor

General rule: While a debtor is located in a state, the local law of that state governs perfection. If the law of the state applies, then § 9-501(a)(2) requires filing in the filing office for that state (usually the Secretary of State). If the security interest is possessory, then the law of the state where the collateral is located governs.

UCC § 9-301(1)	Except as otherwise provided in this section, while a debtor is located in a jurisdiction, the local law of that jurisdiction governs perfection, the effect of perfection or nonperfection, and the priority of a security interest in collateral.
UCC § 9-307	(a) ["Place of business."] In this section, "place of business" means a place where a debtor conducts its affairs. (b) [Debtor's location: general rules.] Except as otherwise provided in this section, the following rules determine a debtor's location: (1) A debtor who is an individual is located at the individual's principal residence. (2) A debtor that is an organization and has only one place of business is located at its place of business. (3) A debtor that is an organization and has more than one place of business is located at its chief executive office. (c) [Limitation of applicability of subsection (b).] Subsection (b) applies only if a debtor's residence, place of business, or chief executive office, as applicable, is located in a jurisdiction whose law generally requires information concerning the existence of a nonpossessory security interest to be made generally available in a

	<p>filing, recording, or registration system as a condition or result of the security interest's obtaining priority over the rights of a lien creditor with respect to the collateral. If subsection (b) does not apply, the debtor is located in the District of Columbia.</p> <p>(d) [Continuation of location: cessation of existence, etc.] A person that ceases to exist, have a residence, or have a place of business continues to be located in the jurisdiction specified by subsections (b) and (c).</p> <p>(e) [Location of registered organization organized under State law.] A registered organization that is organized under the law of a State is located in that State.</p> <p>(f) [Location of registered organization organized under federal law; bank branches and agencies.] Except as otherwise provided in subsection (i), a registered organization that is organized under the law of the United States and a branch or agency of a bank that is not organized under the law of the United States or a State are located:</p> <p>(1) in the State that the law of the United States designates, if the law designates a State of location;</p> <p>(2) in the State that the registered organization, branch, or agency designates, if the law of the United States authorizes the registered organization, branch, or agency to designate its State of location; or</p> <p>(3) in the District of Columbia, if neither paragraph (1) nor paragraph (2) applies.</p> <p>(g) [Continuation of location: change in status of registered organization.] A registered organization continues to be located in the jurisdiction specified by subsection (e) or (f) notwithstanding:</p> <p>(1) the suspension, revocation, forfeiture, or lapse of the registered organization's status as such in its jurisdiction of organization; or</p> <p>(2) the dissolution, winding up, or cancellation of the existence of the registered organization.</p> <p>(h) [Location of United States.] The United States is located in the District of Columbia.</p> <p>(i) [Location of foreign bank branch or agency if licensed in only one state.] A branch or agency of a bank that is not organized under the law of the United States or a State is located in the State in which the branch or agency is licensed, if all branches and agencies of the bank are licensed in only one State.</p> <p>(j) [Location of foreign air carrier.] A foreign air carrier under the Federal Aviation Act of 1958, as amended, is located at the designated office of the agent upon which service of process may be made on behalf of the carrier. (hidden)</p>
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Individual Debtor: Located at the individual's principal residence.

Residence: 1. The act or fact of living in a given place for some time 2. The place where one actually lives, as distinguished from a domicile •*Residence* usu. just means bodily presence as an inhabitant in a given place; *domicile* usu. requires bodily presence plus an intention to make the place one's home. A person thus may have more than one residence at a time but only one domicile. Sometimes, though, the two terms are used synonymously.

Registered Organization: An organization organized solely under the laws of one State or the United States and as to which the State or the United States must maintain a public record showing the organization as being organized. §9-170(a)(70) Note: Generally, if Acme, Inc. applies for incorporation under that name in both NY and NJ, two corporations are created, not one corporation in two states. A registered organization organized under the law of a state is located in that state per § 9-307(e).

General Partnerships & Unincorporated Associations

If only one place of business, then located there. § 9-307(b)(2).

If more than one place of business, located at chief executive office. § 9-307(b)(3).

Place of Business: Where a debtor conducts its affairs. § 9-307(a).

Nerve Center Test: The organization is located where it is managed, regardless of where operations are actually located.

At the Location of the Collateral

A fixture filing must be made in the real estate recording office. Exception: filing against a transmitting utility.⁵

UCC 9-501(a)(1)	[Filing offices.] Except as otherwise provided in subsection (b), if the local law of this State governs perfection of a security interest or agricultural lien, the office in which to file a financing statement to perfect the security interest or agricultural lien is: (1) the office designated for the filing or recording of a record of a mortgage on the related real property, if: (A) the collateral is as-extracted collateral or timber to be cut; or (B) the financing statement is filed as a fixture filing and the collateral is goods that are or are to become fixtures;
9-501(b)	[Filing office for transmitting utilities.] The office in which to file a financing statement to perfect a security interest in collateral, including fixtures, of a transmitting utility is the office of []. The financing statement also constitutes a fixture filing as to the collateral indicated in the financing statement which is or is to become fixtures.

Relocation of the Debtor

One must be at least sometimes present in a state to reside there. If a debtor is physically present in two or more states, the debtor's intentions are determinative.

When an individual debtor changes his state of residence, the secured creditor has four months to file in the destination state. § 9-316(a)(2). If he doesn't, then the interest is unperfected and deemed to have never been perfected as against a purchaser for value. § 9-316(b).⁶

UCC § 9-316	(a) [General rule: effect on perfection of change in governing law.] A security interest perfected pursuant to the law of the jurisdiction designated in Section 9-301(1) or 9-305(c) remains perfected until the earliest of: (1) the time perfection would have ceased under the law of that jurisdiction; (2) the expiration of four months after a change of the debtor's location to another jurisdiction; or (3) the expiration of one year after a transfer of collateral to a person that thereby becomes a debtor and is located in another jurisdiction. (b) [Security interest perfected or unperfected under law of new jurisdiction.] If a security interest described in subsection (a) becomes perfected under the law of the other jurisdiction before the earliest time or event described in that subsection, it remains perfected thereafter. If the security interest does not become perfected under the law of the other jurisdiction before the earliest time or event, it becomes unperfected and is deemed never to have been perfected as against a purchaser of the collateral for value.
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Unregistered organizations can move from state to state simply by relocating their chief executive office, which can be problematic. The drafters rejected this test for registered organizations because it's so hard to keep track of chief executive offices for creditors. It's the only way to track unregistered though.

⁵ Power transmission

⁶ Remember, purchasers for value includes secured creditors, but not lien creditors or bankruptcy trustees.

Reincorporation

By Merger

A new corporation is organized in the target state. The new corporation has all the same owners as the old corporation and becomes the owner of record of the old corporation. Presto chango.

By Sale of Assets

The new corporation simply buys all of the assets of the existing corporation.

Rule: If a corporation reincorporates by merger or sale, § 9-316(a)(3) gives the creditor 1 year in which to discover the merger and perfect in the new states.

CHAPTER 8. PRIORITY

ASSIGNMENT 26: THE CONCEPT OF PRIORITY: STATE LAW

To say that one creditor has priority over another is to say that if the value of the collateral is sufficient to pay only one of them, the law requires that value be used to pay the one who has priority.

A. Priority in Foreclosure

Two basic principles govern the timing of the enforcement of competing liens:

1. Absent an agreement to the contrary, any lienholder may foreclose.
2. No lienholder is compelled to foreclose.

Four principles that govern most judicial or foreclosure sales:

1. The sale discharges the lien under which the sale is held and ALL subordinate liens. *See* UCC § 9-617(a)
2. The sale transfers the debtor's interest in the collateral to the purchaser subject to ALL prior liens. The purchaser is not subject to the debt, the collateral is subject to the liens. *See* UCC § 9-617(a)
3. Whoever conducts the sale must apply proceeds first to sale expenses, then to the lien under which the sale was performed, then to *subordinate* liens, then to the debtor. Prior liens don't get paid. *See* UCC § 9-615(a) and (d)(1).
4. Payment to a lienholder from the proceeds reduces the balance owing. The lienholder is entitled to a deficiency judgment if the debt is not satisfied unless statute proscribes otherwise. *See* UCC § 9-615(d)(2).

Remember, if the debtor gets money and a senior lienholder doesn't get paid, the senior lienholder has a security interest in that money as proceeds!

UCC § 9-615(a)	(a) [Application of proceeds.] A secured party shall apply or pay over for application the cash proceeds of disposition under Section 9-610 in the following order to: (1) the reasonable expenses of retaking, holding, preparing for disposition, processing, and disposing, and, to the extent provided for by agreement and not prohibited by law, reasonable attorney's fees and legal expenses incurred by the secured party; (2) the satisfaction of obligations secured by the security interest or agricultural lien under which the disposition is made; (3) the satisfaction of obligations secured by any subordinate security interest in or other subordinate lien on the collateral if: (A) the secured party receives from the holder of the subordinate security interest or other lien an authenticated demand for proceeds before distribution of the proceeds is completed; and (B) in a case in which a consignor has an interest in the collateral, the subordinate security interest or other lien is senior to the interest of the consignor; and
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	(4) a secured party that is a consignor of the collateral if the secured party receives from the consignor an authenticated demand for proceeds before distribution of the proceeds is completed.
UCC § 9-617(a)	[Effects of disposition.] A secured party's disposition of collateral after default: (1) transfers to a transferee for value all of the debtor's rights in the collateral; (2) discharges the security interest under which the disposition is made; and (3) discharges any subordinate security interest or other subordinate lien [other than liens created under [cite acts or statutes providing for liens, if any, that are not to be discharged]].

B. Was Not Assigned

C. The Right to Possession Between Lienholders

The Grocers Supply Co. v. Intercity Investment Properties, Inc.

Facts:	GS perfected a SI > \$600,000 to secure inventory financing against The Grocery Store, Inc. and Cedric Wise. II obtained a judgment against TGS and Wise for \$36,000, and levied a writ of execution on TGS, taking items they knew were subject to GS's security interest without notifying GS.
Issue:	Does GS have the right to possession of their collateral being held by II?
Rule:	Unless otherwise agreed a secured party has on default the right to take possession of the collateral. UCC § 9-609(a). The right of a prior perfected creditor to take possession of its collateral is superior to any right of a mere judgment creditor: the prior perfected secured creditor may regain possession of the collateral from an officer who has levied on the property at the direction of a judgment creditor.
Held:	The right of GS, as a prior secured creditor, to take possession of the collateral was superior to that of II. GS may regain possession of the collateral from the constable who had levied on the property.
Reas:	The opposite rule would take away the right to repossess.
Issue:	May GS recover costs associated with recovering the collateral?
Rule:	A secured creditor with a right of possession of the collateral after default may maintain an action in conversion against one who has exercised unauthorized acts of dominion over the property to the exclusion of the creditor's rights.
Held:	II must pay GS for costs incurred in retrieving the collateral they would not have had II not taken the collateral.
Reas:	II knew of GS's security interest and should have notified them.

UCC § 9-609(a)	[Possession; rendering equipment unusable; disposition on debtor's premises.] After default, a secured party: (1) may take possession of the collateral; and (2) without removal, may render equipment unusable and dispose of collateral on a debtor's premises under Section 9-610.
Cmt. 5	Multiple Secured Parties. More than one secured party may be entitled to take possession of collateral under this section. Conflicting rights to possession among secured parties are resolved by the priority rules of this Article. Thus, a senior secured party is entitled to possession as against a junior claimant. Non-UCC law governs whether a junior secured party in possession of collateral is liable to the senior in conversion. Normally, a junior who refuses to relinquish possession of collateral upon the demand of a secured party having a superior possessory right to the collateral would be liable in conversion.

Frierson v. United Farm Agency, Inc.

Facts:	A priority lienholder refused to foreclose on property while junior lienholders wanted to foreclose.
Issue:	Can a priority lienholder bar junior lienholders from foreclosing?

Rule:	A lienholder may not refuse to exercise its rights under the security interest while impairing the status of other creditors by preventing them from exercising valid liens. The junior creditor may take possession subject to the senior creditor's lien.
Reas:	If a secured creditor with a security interest over all the debtor's property is permitted to rely on a default, whether technical or not, to prevent another creditor from executing on the debtor's property, while treating the loan as not in default with the debtor and others, severe inequities would result.

ASSIGNMENT 27: THE CONCEPT OF PRIORITY: BANKRUPTCY LAW

Bankruptcy can reduce the amount of the lien to an amount equal to the value of the collateral as determined by the court, adjust the interest rate based on a market rate, and extend the time for repayment.

Also in bankruptcy, some kinds of lien can be avoided entirely because they are unperfected or preferences.

Priority: If the value of the collateral is insufficient to pay all of the liens against it, the law will seek to ensure that value is applied to liens with priority over others.

Two basic principles:

1. Absent an agreement to the contrary, any lienholder may foreclose at any time after default.
Automatic Stay contradicts.

11 USC § 372(a)	<p>Except as provided in subsection (b) of this section, a petition filed under section 301, 302, or 303 of this title, or an application filed under section 5(a)(3) of the Securities Investor Protection Act of 1970, operates as a stay, applicable to all entities, of--</p> <p>(1) the commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case under this title, or to recover a claim against the debtor that arose before the commencement of the case under this title;</p> <p>(2) the enforcement, against the debtor or against property of the estate, of a judgment obtained before the commencement of the case under this title;</p> <p>(3) any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate;</p> <p>(4) any act to create, perfect, or enforce any lien against property of the estate;</p> <p>(5) any act to create, perfect, or enforce against property of the debtor any lien to the extent that such lien secures a claim that arose before the commencement of the case under this title;</p> <p>(6) any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the case under this title;</p> <p>(7) the setoff of any debt owing to the debtor that arose before the commencement of the case under this title against any claim against the debtor; and</p> <p>(8) the commencement or continuation of a proceeding before the United States Tax Court concerning a corporate debtor's tax liability for a taxable period the bankruptcy court may determine or concerning the tax liability of a debtor who is an individual for a taxable period ending before the date of the order for relief under this title.</p>
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2. No lienholder can be forced to foreclose its own lien and to force a sale.
In bankruptcy, the trustee can sell the secured creditor's collateral "free and clear" of liens.

Three ways in which the priority rights of secured creditors are diminished in bankruptcy:

1. Trustee (or DIP) ability to sell collateral free and clear of liens.
2. Trustee or DIP ability to grant senior liens
3. Shift in focus from protection of senior liens to junior liens.

A. Bankruptcy Sale Procedure

During a bankruptcy case, the trustee or DIP can sell collateral. They may be judicial sales (held pursuant to an order of the court) or nonjudicial sales held pursuant to the powers vested in the DIPs.

11 USC § 363(b)(1)	The trustee, after notice and a hearing, may use, sell, or lease, other than in the ordinary course of business, property of the estate, except that if the debtor in connection with offering a product or a service discloses to an individual a policy prohibiting the transfer of personally identifiable information about individuals to persons that are not affiliated with the debtor and if such policy is in effect on the date of the commencement of the case, then the trustee may not sell or lease personally identifiable information to any person unless-- (A) such sale or such lease is consistent with such policy; or (B) after appointment of a consumer privacy ombudsman in accordance with section 332, and after notice and a hearing, the court approves such sale or such lease-- (i) giving due consideration to the facts, circumstances, and conditions of such sale or such lease; and (ii) finding that no showing was made that such sale or such lease would violate applicable nonbankruptcy law.
11 USC § 363	(c)(1) If the business of the debtor is authorized to be operated under section 721, 1108, 1203, 1204, or 1304 of this title and unless the court orders otherwise, the trustee may enter into transactions, including the sale or lease of property of the estate, in the ordinary course of business, without notice or a hearing, and may use property of the estate in the ordinary course of business without notice or a hearing.

Sales Subject to Lien

The collateral can be sold subject to the liens of secured creditors. Since the property is outside of the bankruptcy estate, it is now subject to foreclosure by the secured creditor.

11 USC § 362	(c) Except as provided in subsections (d), (e), (f), and (h) of this section-- (1) the stay of an act against property of the estate under subsection (a) of this section continues until such property is no longer property of the estate; (2) the stay of any other act under subsection (a) of this section continues until the earliest of-- (A) the time the case is closed; (B) the time the case is dismissed; or (C) if the case is a case under chapter 7 of this title concerning an individual or a case under chapter 9, 11, 12, or 13 of this title, the time a discharge is granted or denied;
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Burdensome Property If the total amount of liens against the property is more than the value, nobody may be willing to buy subject to the liens. Such property is deemed “burdensome” and may be abandoned by the debtor or the trustee.

11 USC § 554	(a) After notice and a hearing, the trustee may abandon any property of the estate that is burdensome to the estate or that is of inconsequential value and benefit to the estate. (b) On request of a party in interest and after notice and a hearing, the court may order the trustee to abandon any property of the estate that is burdensome to the estate or that is of inconsequential value and benefit to the estate. (c) Unless the court orders otherwise, any property scheduled under section 521(1) of this title not otherwise administered at the time of the closing of a case is abandoned to the debtor and administered for purposes of section 350 of this title. (d) Unless the court orders otherwise, property of the estate that is not abandoned under this section and that is not administered in the case remains property of the estate.
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Abandonment also removes the property from the estate, and reverts the property from the DIP to the debtor. Actions against the **property** are no longer covered by the automatic stay, though actions against the **debtor** are still covered. **A secured party wishing to foreclose abandoned property may still need to have the stay lifted before doing so.**

Sale “Free and Clear” of Lien

The buyer takes the property free and clear of any liens on the property, while the liens are transferred to the proceeds of sale.

11 USC § 363(f)	<p>The trustee may sell property under subsection (b) or (c) of this section free and clear of any interest in such property of an entity other than the estate, only if--</p> <p>(1) applicable nonbankruptcy law permits sale of such property free and clear of such interest;</p> <p>(2) such entity consents;</p> <p>(3) such interest is a lien and the price at which such property is to be sold is greater than the aggregate value of all liens on such property;</p> <p>(4) such interest is in bona fide dispute; or</p> <p>(5) such entity could be compelled, in a legal or equitable proceeding, to accept a money satisfaction of such interest.</p>
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This can be very upsetting to a secured creditor who would receive nothing from an immediate sale but would recover from a later sale due to appreciation or a better market.

In re Oneida Lake Development, Inc.

Facts:	OLD filed voluntary BK11 on 9/11/1989. 11/11/89, OLD K Bloss to sell Wood Pointe Marina for \$750,000 (assuming two mortgages, OLD take 3rd for \$140,000, \$250,000 cash), including inventory and equipment, <i>sans</i> inventory subject to floor plan. Three mortgages, three judgments, and real estate taxes encumber property for \$1.3mm. Three mortgages and property taxes are fine. OLD has commenced motion to set aside 2 of 3 judgments as preferences. 3rd judgment held by WPV for \$600,000. OLD says will commence proceeding to set aside but hasn't yet. Appraisal shows significant decrease in value in property from \$1.25mm in 1987.
Issue:	Has OLD established compliance with 11 USC § 363(f)(3) or (4)?
Issue 1:	What is the value of the liens on the property?
Rule:	11 USC § 506(a)(1): secured status only extends to the value of the creditor's interest in the estate's interest in the property. The value of the liens is only equal to the value of the property. Proposed sales price is the best price available under the circumstances and the court must find special circumstances justifying a sale for less than the amount (vs. value) of liens
Held:	The status of WPV as a non-consensual lien creditor arguably subject to attack under § 547 and the rapid depreciation of the property (from \$1.25mm to \$750,000) are special circumstances.
Issue 2:	Is the lien of WPV in "bona fide dispute" under 11 USC § 363(f)(4)?
Rule:	A potential preference action qualifies as a bona fide dispute whether filed or not.
Held:	WPV's lien is in bona fide dispute.

Circumstance in which free and clear sale is more economically efficient:

1. Where the amounts and priorities of competing liens are in doubt AND
2. The collateral is depreciating rapidly.

Ex: Two competing liens on a shopping center under construction, both in default. If no BK power, one forecloses and they litigate for years while center stays idle. Sale F&C, buyer resumes construction and security interest attaches to the proceeds while everyone sues everyone.

B. The Power to Grant Senior Liens

A Trustee or DIP may elect to keep the property and offer it as collateral for a postpetition loan.

Generally, liens are first in time, first in right. Exceptions under state law: PMSI and property taxes. Minority rule: also mechanic's liens.

A trustee or DIP can borrow additional funds from a postpetition lender secured by a lien prior to existing liens. Two Requirements:

1. The estate is unable to borrow without granting a senior lien.
2. There is adequate protection of the interest of the secured lender being subordinated.

11 USC § 364(d)	(1) The court, after notice and a hearing, may authorize the obtaining of credit or the incurring of debt secured by a senior or equal lien on property of the estate that is
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	subject to a lien only if-- (A) the trustee is unable to obtain such credit otherwise; and (B) there is adequate protection of the interest of the holder of the lien on the property of the estate on which such senior or equal lien is proposed to be granted. (2) In any hearing under this subsection, the trustee has the burden of proof on the issue of adequate protection.
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If a secured creditor gets primed in one of these transactions and ends up not being fully paid because the trustee sold free and clear of liens, he becomes an unsecured creditor (senior to almost all unsecured claims.)

11 USC 507(b)	If the trustee, under section 362, 363, or 364 of this title, provides adequate protection of the interest of a holder of a claim secured by a lien on property of the debtor and if, notwithstanding such protection, such creditor has a claim allowable under subsection (a)(2) of this section arising from the stay of action against such property under section 362 of this title, from the use, sale, or lease of such property under section 363 of this title, or from the granting of a lien under section 364(d) of this title, then such creditor's claim under such subsection shall have priority over every other claim allowable under such subsection.
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In re 495 Central Park Avenue Corporation

Facts:	495 filed BK11 9/5/91. Became DIP. 495 purchased property subject to mortgage from John Hancock in first position for \$3.95mm. Also paid \$202,500 cash and gave purchase money mortgage for \$200,000 to Viewpoint. PM mortgage is subordinate. 495 did not assume the loan. 495 defaulted and JH accelerated and foreclosed 8/1991. Stayed on BK11 filing. 495 wants to borrow money from shareholders in first priority.
Issue:	Is 495 able to grant a priority lien to a postpetition lender?
Rule:	11 USC § 364(d)
Issue1:	Was the DIP unable to obtain such credit otherwise?
Rule:	§ 364(d) does not require the debtor to seek alternate financing from all possible sources. However, the debtor must make an effort to obtain credit without priming a lender.
Held:	Silverman was unable to obtain credit otherwise.
Reas:	The dude went all over town looking for credit. Provided evidence that no commercial bank would lend in second position.
Issue2:	Is there adequate protection for JH if they are primed?
Rule:	11 USC § 361 confers upon “the parties and the courts flexibility by allowing such other relied as will result in the realization by the protected entity of the value of its interest during Chapter 11 reorganization.
Held:	JH’s security interest is adequately protected, because the property will appreciate by more than the amount of the loan because of the proposed improvements.

C. Protection of Subordinate Creditors

Nonbankruptcy law emphasizes protection of senior lien creditors. Bankruptcy shifts the emphasis. Foreclosure by a lienholder will be stayed if:

1. The senior lienholders are adequately protected against loss.
2. The stay is likely to facilitate the collection efforts of subordinate creditors.

Analogy to triage

Triage	Bankruptcy
Those who cannot benefit from care because their injuries are minor.	Creditors who will fully recover regardless have to wait.
Those who cannot benefit from care because they’re going to die anyhow.	Lienholders who are so subordinate that they’re going to lose no matter what.

Those who can benefit from care because their injuries are serious but not fatal with care.	Lienholders with sufficiently high priority that they may be able to get paid through an efficient reorganization.
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CHAPTER 9. COMPETITIONS FOR COLLATERAL

ASSIGNMENT 28: LIEN CREDITORS AGAINST SECURED CREDITORS: THE BASICS

Three competitions:

1. Lien creditor vs. Lien creditor
2. Lien creditor vs. Article 9 Secured Party
3. Lien creditor vs. real estate secured party

A. How Creditors become “Lien Creditors”

Lien: A charge against property to secure performance of an obligation.

Lien Creditor: Any party who has acquired a lien by attachment, levy, or the like. UCC § 9-102(a)(52)

Attachment: Legal process by which the plaintiff in litigation obtains a writ and delivers it to the sheriff. Generally *before* judgment is entered

Execution: Same as attachment post-judgment.

Garnishment: A process to reach debts owed to the debtor by a third party or property held by a third party owned by the debtor.

- Majority: Can garnish before judgment subject to certain restrictions.
- Minority: Can't.
- Can **never** garnish wages before judgment.
- Minority: Can't garnish wages even after judgment.

Recordation of Money Judgment

Real Estate:

- Majority: Creates and perfects a lien against all real property in the county, including after-acquired.

Personal Property:

- Minority: Can be recorded in UCC filing system and creates and perfects a lien against the personal property of the debtor. Alternative to perfection by levy. (CA and FL)

Trustee or DIP: An “ideal” lien creditor who obtains his lien as of the filing of the BK case. An ideal lien creditor has no knowledge of unperfected liens.

11 USC § 544(a)	<p>(a) The trustee shall have, as of the commencement of the case, and without regard to any knowledge of the trustee or of any creditor, the rights and powers of, or may avoid any transfer of property of the debtor or any obligation incurred by the debtor that is voidable by--</p> <p>(1) a creditor that extends credit to the debtor at the time of the commencement of the case, and that obtains, at such time and with respect to such credit, a judicial lien on all property on which a creditor on a simple contract could have obtained such a judicial lien, whether or not such a creditor exists;</p> <p>(2) a creditor that extends credit to the debtor at the time of the commencement of the case, and obtains, at such time and with respect to such credit, an execution against the debtor that is returned unsatisfied at such time, whether or not such a creditor exists; or</p> <p>(3) a bona fide purchaser of real property, other than fixtures, from the debtor, against whom applicable law permits such transfer to be perfected, that obtains the status of a bona fide purchaser and has perfected such transfer at the time of the commencement</p>
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	of the case, whether or not such a purchaser exists.
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B. Priority Among Lien Creditors

Generally first come first serve depending on date of necessary step. Four types of necessary step.

1. **Date of levy.** The lien is granted priority as of the date the sheriff either physically or constructively (by posting a notice, etc.) took possession of the property.
2. **Date of delivery of writ.** Minority rule (IL) Writs of execution rank in the order they are delivered. However, the lien is not created until the actual levy, then it is related back to the delivery of the writ.
3. **Date of service of a writ of garnishment.**
4. **Date of recordation of judgment.**

Example OH statute is date of delivery of writ. Notice if the writs are delivered on the same day, they are given proportional treatment.

C. Priority between Lien Creditors and Secured Creditors

Priority between a lien creditor and a non-PMSI Article 9 secured creditor depends on whether the lien creditor becomes a lien creditor before the secured creditor either:

1. Perfects its security interest
2. Files a financing statement and complies with § 9-203(b)(3)

The important thing here is that filing a financing statement is not necessarily perfection: could file the financing statement before the security interest attaches. Remember that if §9-203(b)(3) is met then it doesn't necessarily have to be perfected. Security Agreement is most often the case here.

UCC § 9-203(b)(3)	One of the following conditions is met: (A) the debtor has authenticated a security agreement that provides a description of the collateral and, if the security interest covers timber to be cut, a description of the land concerned; (B) the collateral is not a certificated security and is in the possession of the secured party under Section 9-313 pursuant to the debtor's security agreement; (C) the collateral is a certificated security in registered form and the security certificate has been delivered to the secured party under Section 8-301 pursuant to the debtor's security agreement; or (D) the collateral is deposit accounts, electronic chattel paper, investment property, or letter-of-credit rights, and the secured party has control under Section 9-104, 9-105, 9-106, or 9-107 pursuant to the debtor's security agreement.
UCC § 9-317(a)(2)	except as otherwise provided in subsection (e), a person that becomes a lien creditor before the earlier of the time: (A) the security interest or agricultural lien is perfected; or (B) one of the conditions specified in Section 9-203(b)(3) is met and a financing statement covering the collateral is filed.

Generally, the issue in this type of case is not when the secured creditor perfected, but whether they perfected at all.

D. Priority Between Lien Creditors and Mortgage Creditors

Real estate law generally gives priority to the first lien created and only reverses if the failure to perfect offends the state's recording statutes.

Lien creditors do not get the benefit of recording statutes (they aren't going to search anyhow.)

Rule: A mortgage granted before a judgment creditor becomes a lien creditor has priority over the judgment lien, even if the judgment lien is perfected first.

E. Purchase-Money Priority

Priming: When a second-in-time interest takes precedence over an earlier interest.

Purchase-money security interests can prime in a very limited circumstance.

If a purchase money security interest **attaches** before the lien creditor obtains the lien against the collateral, then the purchase money secured creditor has 20 days from the debtor's receipt of the collateral to perfect. If the security interest is perfected, it primes the lien creditor.

UCC § 9-317(e)	[Purchase-money security interest.] Except as otherwise provided in Sections 9-320 and 9-321, if a person files a financing statement with respect to a purchase-money security interest before or within 20 days after the debtor receives delivery of the collateral, the security interest takes priority over the rights of a buyer, lessee, or lien creditor which arise between the time the security interest attaches and the time of filing.
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Policy: Facilitates sales of personal property on secured credit. The policy makes it so that sellers can give immediate delivery without first filing a financing statement.

Remember that PMSI in security goods in consumer goods always attaches at delivery and is perfected at attachment. § 9-309.

ASSIGNMENT 29: LIEN CREDITORS AGAINST SECURED CREDITORS: FUTURE ADVANCES

A. Priority of Future Advances: Personal Property

UCC § 9-323(b)	[Lien creditor.] Except as otherwise provided in subsection (c), a security interest is subordinate to the rights of a person that becomes a lien creditor to the extent that the security interest secures an advance made more than 45 days after the person becomes a lien creditor unless the advance is made: (1) without knowledge of the lien; or (2) pursuant to a commitment entered into without knowledge of the lien.
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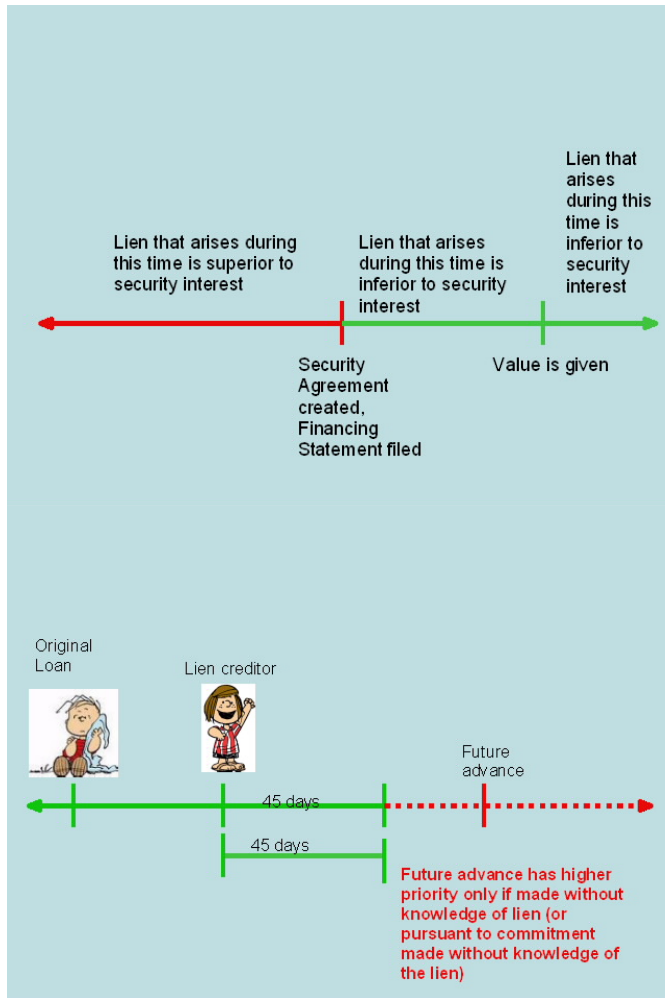
Future advances get priority over lien creditors so long as the secured creditor did not know about the lien OR the advance was made pursuant to a commitment entered into without knowledge of the lien OR it was made within 45 days of the lien.

Reason for the 45 days: Gives maximum protection from tax liens under the Tax Lien Act, 26 USC §§6321 et seq.

When is a future advance perfected?

Under 9-308, a security interest must attach in order to be perfected. Under 9-203, a security interest does not attach until value is given. Therefore, the security interest in the future advance is not perfected until value is given.

What sort of priority does the future advance have versus a lien creditor?



ASSIGNMENT 30: TRUSTEES IN BANKRUPTCY AGAINST SECURED CREDITORS: THE STRONG ARM CLAUSE

Bankruptcy Code § 544(a) is sometimes known as the “strong arm clause.” It allows a trustee or DIP to avoid most security interests that are unperfected at the time of filing of the case.

11 USC § 544	<p>(a) The trustee shall have, as of the commencement of the case, and without regard to any knowledge of the trustee or of any creditor, the rights and powers of, or may avoid any transfer of property of the debtor or any obligation incurred by the debtor that is voidable by--</p> <p>(1) a creditor that extends credit to the debtor at the time of the commencement of the case, and that obtains, at such time and with respect to such credit, a judicial lien on all property on which a creditor on a simple contract could have obtained such a judicial lien, whether or not such a creditor exists;</p> <p>(2) a creditor that extends credit to the debtor at the time of the commencement of the case, and obtains, at such time and with respect to such credit, an execution against the debtor that is returned unsatisfied at such time, whether or not such a creditor exists; or</p> <p>(3) a bona fide purchaser of real property, other than fixtures, from the debtor, against whom applicable law permits such transfer to be perfected, that obtains the status of a bona fide purchaser and has perfected such transfer at the time of the commencement of the case, whether or not such a purchaser exists.</p> <p>(b)(1) Except as provided in paragraph (2), the trustee may avoid any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law by a creditor holding an unsecured claim that is allowable under</p>
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	<p>section 502 of this title or that is not allowable only under section 502(e) of this title.</p> <p>(2) Paragraph (1) shall not apply to a transfer of a charitable contribution (as that term is defined in section 548(d)(3)) that is not covered under section 548(a)(1)(B), by reason of section 548(a)(2). Any claim by any person to recover a transferred contribution described in the preceding sentence under Federal or State law in a Federal or State court shall be preempted by the commencement of the case.</p>
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A. The Purpose of the Bankruptcy Code

§ 544 is usually attributed to a purpose to avoid secret liens. Creditors should give public notice of their liens whenever feasible.

The large majority of attacks on perfection of security interests are by bankruptcy trustees.

If a trustee is successful in avoiding a security interest, it is “preserved for the estate.” That is, the trustee now steps into the shoes of the putative secured creditor and enforces the security interest for the estate (and thus unsecured creditors.)

11 USC § 551	Any transfer avoided under section 522, 544, 545, 547, 548, 549, or 724(a) of this title, or any lien void under section 506(d) of this title, is preserved for the benefit of the estate but only with respect to property of the estate
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B. The Text of Bankruptcy Code § 544(a)

The text creates three hypothetical persons who might compete with unperfected lienholders, then step into the shoes of the person who would have the greatest rights against the particular lienholder. The trustee also becomes the “ideal lien creditor, irreproachable and without notice, armed cap-a-pie with every right and power which is conferred by the law of the state upon its most favored creditor who has acquired a lien by legal or equitable proceedings.” However, since this is a function of state law, the full effect of § 544 can vary from state to state.

§ 544 gives the trustee the power to avoid any “transfer” which could be avoided by one of the three hypothetical persons. **Transfer under the bankruptcy code includes both voluntary security interests granted and involuntary judicial or statutory liens.**

1. The Judicial Lien Creditor of § 544(a)(1)

The trustee can step into the shoes of a hypothetical lien creditor who “extends credit to the debtor at the time of the commencement of the case, and that obtains, at such time and with respect to such credit, a judicial lien on all property on which a creditor on a simple contract could have obtained such a judicial lien.”

Allows trustee to test perfection as of the filing of the case, but no earlier.

What competitions does this hypothetical person win?

Security interest: Look to §§ 9-317(a)(2) and 9-323(b).

2. The Creditor with an Execution Returned Unsatisfied

The trustee can step into the shoes of a hypothetical “creditor that extends credit to the debtor at the time of the commencement of the case, and obtains, at such time and with respect to such credit, an execution against the debtor that is returned unsatisfied at such time.” The purpose was to reach some fraudulent transfers that would not have been reached by 544(a)(1).

3. The Bona Fide Purchaser of Real Property

If the property is real property other than fixtures, the trustee can step into the shoes of a bona fide purchaser for value who bought at the time of the commencement of the case.

The BFP must be one “against whom applicable law permits such transfer to be perfected.”

This allows the trustee to prevail when:

1. The competing creditor was supposed to do something to perfect its lien and
2. Failed to do so.

With regard to fixtures, the trustee only has the rights of a hypothetical judgment lien creditor.

C. The Implementation of Bankruptcy Code § 544(a)

While certain transfers may be avoidable, the trustee or DIP does not always have to avoid them.

1. Exercise of Bankruptcy Code § 544(a) Discretion by Chapter 7 Trustees

Rights: Secured Creditors → Trustee/administrative expenses → Unsecured creditors.

Trustees are required to perform extensive duties in every case under §704, but are only paid reasonable compensation if there’s sufficient funds after satisfying secured creditors.

If a trustee manages to avoid liens on property, the property becomes property of the estate under § 541(a)(3)-(4). The proceeds of sale are available to pay administrative expenses, including the fees of the trustee. If the trustee can’t muster up some unliened assets, all he gets is \$60.

This system provides major “eat what you kill” incentives to trustees.

Proof of Claim

Secured creditors may file proofs of claim in bankruptcy cases, but they are not required to do so.

Unless someone sues the creditor and serves them with process, their lien passes through the bankruptcy unaffected. The creditor can’t violate the stay, and the debt is discharged, but the creditor may still foreclose after the bankruptcy is concluded. *Dewsnup v. Timm*

If the creditor does file a proof of claim, evidence of the security interest must be attached. The trustee then examines the evidence and possibly searches the filing records to ensure the financing statement was filed. Even without a proof of claim, the trustee can demand proof of the validity of a security interest.

Once the trustee has the documentation, they examine it for errors like misspelled names or improper filing place that might show that the lien is unperfected.

A trustee may bring an action under § 544(a) whether or not a proof of claim has been filed. Under § 546(a), the trustee has up to two years from appointment in which to bring the action.

11 USC § 546(a)	(a) An action or proceeding under section 544, 545, 547, 548, or 553 of this title may not be commenced after the earlier of-- (1) the later of-- (A) 2 years after the entry of the order for relief; or (B) 1 year after the appointment or election of the first trustee under section 702, 1104, 1163, 1202, or 1302 of this title if such appointment or such election occurs before the expiration of the period specified in subparagraph (A); or (2) the time the case is closed or dismissed.
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2. Exercise of § 544(a) Discretion by Chapter 11 Debtors in Possession

If a DIP is successful in avoiding a security interest, the effect is to change the creditor from secured to unsecured. However, even an unsecured creditor has priority over shareholders, and the DIP is a shareholder. No real incentive to avoid the security interest there.

Also, if the security interest is granted to the owner-managers themselves, to relatives, or to people with ongoing business relationships, then the DIP doesn't WANT to avoid their security interests-screws themselves or their friends.

The DIP is a fiduciary and is bound to act in the interests of the estate. If the DIP fails to avoid a security interest that should be brought, some courts will allow the unsecured creditors' committee to sue in the DIP's place. In some cases, a fiduciary failure will lead to the appointment of a trustee.

Roughly 70% of BK11 cases are converted to BK7. This leads to a radical shift in priorities. As long as the conversion and appointment occur within 2 years of commencement, under § 546(a)(1)(B) the trustee will have 1 year to bring suit to avoid security interests.

ASSIGNMENT 31: TRUSTEES IN BANKRUPTCY AGAINST UNSECURED CREDITORS: PREFERENCES

A. Priority Among Unsecured Creditors

1. Priority Under State Law: A Review

The grant of a security interest to a previously unsecured creditor is valid and enforceable even if the creditor furnishes no new consideration. §§ 9-203(b)(1) and 1-204(2).

This can have the effect of preferring one creditor over another. Under state law that's OK-you do it all the time when you pay one person before another.

2. Priority Under Bankruptcy Law: A Review

Some unsecured creditors are entitled to priority over general unsecured creditors

1. Wage claimants
 2. Taxing authorities
- §§ 504(a) and 726(a).

Treating unsecured creditors alike is a basic tenet of BK law: general unsecured creditors are paid a pro rata share.

Once the debtor is in bankruptcy, neither the debtor nor the trustee may take any action to prefer one prepetition unsecured creditor over another, including granting a security interest.

However, a bankruptcy estate may grant a security interest for new value furnished to the estate at the time of the grant. § 346(c)-(d)

11 USC § 346	<p>(c) If the trustee is unable to obtain unsecured credit allowable under section 503(b)(1) of this title as an administrative expense, the court, after notice and a hearing, may authorize the obtaining of credit or the incurring of debt--</p> <p>(1) with priority over any or all administrative expenses of the kind specified in section 503(b) or 507(b) of this title;</p> <p>(2) secured by a lien on property of the estate that is not otherwise subject to a lien; or</p> <p>(3) secured by a junior lien on property of the estate that is subject to a lien.</p> <p>(d)(1) The court, after notice and a hearing, may authorize the obtaining of credit or the incurring of debt secured by a senior or equal lien on property of the estate that is subject to a lien only if--</p> <p>(A) the trustee is unable to obtain such credit otherwise; and</p> <p>(B) there is adequate protection of the interest of the holder of the lien on the property of the estate on which such senior or equal lien is proposed to be granted.</p> <p>(2) In any hearing under this subsection, the trustee has the burden of proof on the issue of adequate protection.</p>
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4. *Reconciling State and Bankruptcy Policies*

Preference Period

Creditors who are “insiders” of the debtor: 1 year prior to commencement.

Non-insiders: 90 days prior to commencement.

Bankruptcy Code § 547 authorizes the trustee or DIP to avoid any transfer made during the preference period that would have the effect of preferring one unsecured creditor over another.

11 USC § 547	<p>(a) In this section--</p> <p>(1) “inventory” means personal property leased or furnished, held for sale or lease, or to be furnished under a contract for service, raw materials, work in process, or materials used or consumed in a business, including farm products such as crops or livestock, held for sale or lease;</p> <p>(2) “new value” means money or money's worth in goods, services, or new credit, or release by a transferee of property previously transferred to such transferee in a transaction that is neither void nor voidable by the debtor or the trustee under any applicable law, including proceeds of such property, but does not include an obligation substituted for an existing obligation;</p> <p>(3) “receivable” means right to payment, whether or not such right has been earned by performance; and</p> <p>(4) a debt for a tax is incurred on the day when such tax is last payable without penalty, including any extension.</p> <p>(b) Except as provided in subsections (c) and (i) of this section, the trustee may avoid any transfer of an interest of the debtor in property--</p> <p>(1) to or for the benefit of a creditor;</p> <p>(2) for or on account of an antecedent debt owed by the debtor before such transfer was made;</p> <p>(3) made while the debtor was insolvent;</p> <p>(4) made--</p> <p>(A) on or within 90 days before the date of the filing of the petition; or</p> <p>(B) between ninety days and one year before the date of the filing of the petition, if such creditor at the time of such transfer was an insider; and</p> <p>(5) that enables such creditor to receive more than such creditor would receive if--</p> <p>(A) the case were a case under chapter 7 of this title;</p> <p>(B) the transfer had not been made; and</p> <p>(C) such creditor received payment of such debt to the extent provided by the provisions of this title.</p> <p>(c) The trustee may not avoid under this section a transfer--</p> <p>(1) to the extent that such transfer was--</p> <p>(A) intended by the debtor and the creditor to or for whose benefit such transfer was made to be a contemporaneous exchange for new value given to the debtor; and</p> <p>(B) in fact a substantially contemporaneous exchange;</p> <p>(2) to the extent that such transfer was in payment of a debt incurred by the debtor in the ordinary course of business or financial affairs of the debtor and the transferee, and such transfer was--</p> <p>(A) made in the ordinary course of business or financial affairs of the debtor and the transferee; or</p> <p>(B) made according to ordinary business terms;</p> <p>(3) that creates a security interest in property acquired by the debtor--</p> <p>(A) to the extent such security interest secures new value that was--</p> <p>(i) given at or after the signing of a security agreement that contains a description of such property as collateral;</p> <p>(ii) given by or on behalf of the secured party under such agreement;</p> <p>(iii) given to enable the debtor to acquire such property; and</p> <p>(iv) in fact used by the debtor to acquire such property; and</p> <p>(B) that is perfected on or before 30 days after the debtor receives possession of such</p>
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	<p>property;</p> <p>(4) to or for the benefit of a creditor, to the extent that, after such transfer, such creditor gave new value to or for the benefit of the debtor--</p> <p>(A) not secured by an otherwise unavoidable security interest; and</p> <p>(B) on account of which new value the debtor did not make an otherwise unavoidable transfer to or for the benefit of such creditor;</p> <p>(5) that creates a perfected security interest in inventory or a receivable or the proceeds of either, except to the extent that the aggregate of all such transfers to the transferee caused a reduction, as of the date of the filing of the petition and to the prejudice of other creditors holding unsecured claims, of any amount by which the debt secured by such security interest exceeded the value of all security interests for such debt on the later of--</p> <p>(A)(i) with respect to a transfer to which subsection (b)(4)(A) of this section applies, 90 days before the date of the filing of the petition; or</p> <p>(ii) with respect to a transfer to which subsection (b)(4)(B) of this section applies, one year before the date of the filing of the petition; or</p> <p>(B) the date on which new value was first given under the security agreement creating such security interest;</p> <p>(6) that is the fixing of a statutory lien that is not avoidable under section 545 of this title;</p> <p>(7) to the extent such transfer was a bona fide payment of a debt for a domestic support obligation;</p> <p>(8) if, in a case filed by an individual debtor whose debts are primarily consumer debts, the aggregate value of all property that constitutes or is affected by such transfer is less than \$600; or</p> <p>(9) if, in a case filed by a debtor whose debts are not primarily consumer debts, the aggregate value of all property that constitutes or is affected by such transfer is less than \$5,850¹.</p> <p>(d) The trustee may avoid a transfer of an interest in property of the debtor transferred to or for the benefit of a surety to secure reimbursement of such a surety that furnished a bond or other obligation to dissolve a judicial lien that would have been avoidable by the trustee under subsection (b) of this section. The liability of such surety under such bond or obligation shall be discharged to the extent of the value of such property recovered by the trustee or the amount paid to the trustee.</p> <p>(e)(1) For the purposes of this section--</p> <p>(A) a transfer of real property other than fixtures, but including the interest of a seller or purchaser under a contract for the sale of real property, is perfected when a bona fide purchaser of such property from the debtor against whom applicable law permits such transfer to be perfected cannot acquire an interest that is superior to the interest of the transferee; and</p> <p>(B) a transfer of a fixture or property other than real property is perfected when a creditor on a simple contract cannot acquire a judicial lien that is superior to the interest of the transferee.</p> <p>(2) For the purposes of this section, except as provided in paragraph (3) of this subsection, a transfer is made--</p> <p>(A) at the time such transfer takes effect between the transferor and the transferee, if such transfer is perfected at, or within 30 days after, such time, except as provided in subsection (c)(3)(B);</p> <p>(B) at the time such transfer is perfected, if such transfer is perfected after such 30 days; or</p> <p>(C) immediately before the date of the filing of the petition, if such transfer is not perfected at the later of--</p> <p>(i) the commencement of the case; or</p> <p>(ii) 30 days after such transfer takes effect between the transferor and the transferee.</p> <p>(3) For the purposes of this section, a transfer is not made until the debtor has acquired rights in the property transferred.</p> <p>(f) For the purposes of this section, the debtor is presumed to have been insolvent on and during the 90 days immediately preceding the date of the filing of the petition.</p> <p>(g) For the purposes of this section, the trustee has the burden of proving the avoidability</p>
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	<p>of a transfer under subsection (b) of this section, and the creditor or party in interest against whom recovery or avoidance is sought has the burden of proving the nonavoidability of a transfer under subsection (c) of this section. (hidden)</p> <p>(h) The trustee may not avoid a transfer if such transfer was made as a part of an alternative repayment schedule between the debtor and any creditor of the debtor created by an approved nonprofit budget and credit counseling agency.</p> <p>(i) If the trustee avoids under subsection (b) a transfer made between 90 days and 1 year before the date of the filing of the petition, by the debtor to an entity that is not an insider for the benefit of a creditor that is an insider, such transfer shall be considered to be avoided under this section only with respect to the creditor that is an insider.</p>
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§ 547 does not prohibit a debtor from granting preferences in the period before bankruptcy-heck, he might not even know he's going to file. The purpose of § 547 is to keep debtors from defeating the pro rata distribution to unsecured creditors by pre-liquidating their estate.

B. What Security Interests Can Be Avoided as Preferential

1. Generally

§547(b) says what transfers can be avoided. A transfer can still be avoided under § 547(c).

a. § 547(b). Transfer.

Only a "transfer of an interest of the debtor in property" can be avoided under 547(b). § 101 provides a broad definition of transfer that includes the creation and perfection of a security interest.

b. §547(b)(1), to or for the benefit of a creditor, and § 547(b)(2), for or on account of an antecedent debt.

The transfer must have been to a party who was, at the time the transfer was made, already a creditor.

Note: if the transfer was intended to be contemporaneous and was in fact substantially contemporaneous, then it's not an antecedent debt if the creditor hands over the check right before getting a security interest. 547(c)(1).

c. § 547(b)(3). Insolvency.

If the debtor is solvent at the time of the transfer, then the transfer is not avoidable. Paying or securing one creditor doesn't hurt others, because there's sufficient assets to pay all creditors at the time. If they choose to remain unsecured, they assume the risk of future insolvency.

§ 547(f) creates a rebuttable presumption of insolvency for 90 days pre-filing.

d. § 547(b)(4). Preference period

Duh. The transfer must have occurred during the preference period.

e. § 547(b)(5). The Improvement Test.

To be avoidable, the transfer must have improved the creditor's position. If the transfer does not have the effect of the creditor getting more than its pro rata share, then it's not avoidable. However, nearly all transfers meet this test.

ASSIGNMENT 32: SECURED CREDITORS AGAINST SECURED CREDITORS: THE BASICS

UCC §9-322	<p>(a) [General priority rules.] Except as otherwise provided in this section, priority among conflicting security interests and agricultural liens in the same collateral is determined according to the following rules:</p> <p>(1) Conflicting perfected security interests and agricultural liens rank according to priority in time of filing or perfection. Priority dates from the earlier of the time a filing covering the collateral is first made or the security interest or agricultural lien is first perfected, if there is no period thereafter when there is neither filing nor perfection.</p> <p>(2) A perfected security interest or agricultural lien has priority over a conflicting unperfected security interest or agricultural lien.</p>
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	<p>(3) The first security interest or agricultural lien to attach or become effective has priority if conflicting security interests and agricultural liens are unperfected.</p> <p>(b) [Time of perfection: proceeds and supporting obligations.] For the purposes of subsection (a)(1):</p> <p>(1) the time of filing or perfection as to a security interest in collateral is also the time of filing or perfection as to a security interest in proceeds; and</p> <p>(2) the time of filing or perfection as to a security interest in collateral supported by a supporting obligation is also the time of filing or perfection as to a security interest in the supporting obligation.</p> <p>(c) [Special priority rules: proceeds and supporting obligations.] Except as otherwise provided in subsection (f), a security interest in collateral which qualifies for priority over a conflicting security interest under Section 9-327, 9-328, 9-329, 9-330, or 9-331 also has priority over a conflicting security interest in:</p> <p>(1) any supporting obligation for the collateral; and</p> <p>(2) proceeds of the collateral if:</p> <p>(A) the security interest in proceeds is perfected;</p> <p>(B) the proceeds are cash proceeds or of the same type as the collateral; and</p> <p>(C) in the case of proceeds that are proceeds of proceeds, all intervening proceeds are cash proceeds, proceeds of the same type as the collateral, or an account relating to the collateral.</p> <p>(d) [First-to-file priority rule for certain collateral.] Subject to subsection (e) and except as otherwise provided in subsection (f), if a security interest in chattel paper, deposit accounts, negotiable documents, instruments, investment property, or letter-of-credit rights is perfected by a method other than filing, conflicting perfected security interests in proceeds of the collateral rank according to priority in time of filing.</p> <p>(e) [Applicability of subsection (d).] Subsection (d) applies only if the proceeds of the collateral are not cash proceeds, chattel paper, negotiable documents, instruments, investment property, or letter-of-credit rights.</p> <p>(f) [Limitations on subsections (a) through (e).] Subsections (a) through (e) are subject to:</p> <p>(1) subsection (g) and the other provisions of this part;</p> <p>(2) Section 4-210 with respect to a security interest of a collecting bank;</p> <p>(3) Section 5-118 with respect to a security interest of an issuer or nominated person; and</p> <p>(4) Section 9-110 with respect to a security interest arising under Article 2 or 2A.</p> <p>(g) [Priority under agricultural lien statute.] A perfected agricultural lien on collateral has priority over a conflicting security interest in or agricultural lien on the same collateral if the statute creating the agricultural lien so provides.</p>
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A. Non-Purchase Money Security Interests

1. *The Basic Rule: First to File or Perfect*

The basic rule is § 9-322(a)(1).

Between the holders of two security interests in the same collateral, the first to file OR perfect has priority. The holder who gains priority by first filing retains it so long as the holder remains continuously filed or perfected.

2. *Priority of Future Advances*

Provided that the secured creditor's financing statement "covers the collateral," all advances made by the secured creditor to the debtor have priority as of the filing of the financing statement. The understanding is that the second creditor takes a security interest agrees to do so subject to any amount outstanding under the first security interest and any future advances. An important function is that the lender making future advances doesn't have to check the filing records before doing so.

Who would take a second interest?

1. Lenders who don't understand the rule

2. Creditors who hope to benefit from the second interest and don't advance funds in reliance.
3. Lenders who protect themselves from future advances by contract with the first creditor.

UCC § 9-339	This article does not preclude subordination by agreement by a person entitled to priority.
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A single filing statement is adequate to perfect any number of security interests, to the limits of the description of collateral in the financing statement. Under 9-322(a) and 9-502(d), these security interests have priority.

3. *Priority in After-Acquired Property*

Debtors who grant security interests in after-acquired property often do not even contemplate acquiring any property of the kind described. However, if they do, the security interest attaches under § 9-203(b). As against other Article 9 creditors of the debtor, the lender's priority dates to the time of filing. Many regard the validation of after-acquired property clauses as the most important innovation in Article 9. Modern-day inventory lending could not exist without it.

What about after-acquired property that was already subject to a security interest?

UCC § 9-325	<p>(a) [Subordination of security interest in transferred collateral.] Except as otherwise provided in subsection (b), a security interest created by a debtor is subordinate to a security interest in the same collateral created by another person if:</p> <p>(1) the debtor acquired the collateral subject to the security interest created by the other person;</p> <p>(2) the security interest created by the other person was perfected when the debtor acquired the collateral; and</p> <p>(3) there is no period thereafter when the security interest is unperfected.</p> <p>(b) [Limitation of subsection (a) subordination.] Subsection (a) subordinates a security interest only if the security interest:</p> <p>(1) otherwise would have priority solely under Section 9-322(a) or 9-324; or</p> <p>(2) arose solely under Section 2-711(3) or 2A-508(5).</p>
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B. *Purchase-Money Security Interests*

1. *Purchase-Money Security Interests Generally*

UCC § 9-324(a)	<p>(a) [General rule: purchase-money priority.] Except as otherwise provided in subsection (g), a perfected purchase-money security interest in goods other than inventory or livestock has priority over a conflicting security interest in the same goods, and, except as otherwise provided in Section 9-327, a perfected security interest in its identifiable proceeds also has priority, if the purchase-money security interest is perfected when the debtor receives possession of the collateral or within 20 days thereafter.</p>
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The purchase-money lender is "first" in another important sense: the PML gave the funds to enable the debtor to buy the collateral. If this rule wasn't in place, the PML could just sell the property to a straw purchaser, take a security interest, and have the straw purchaser transfer to the intended debtor. Since the after-acquired property clause wouldn't attach to the property until after the PMSI attached, the PMSI would be first in time. This avoids the straw purchaser problem. This also recognizes that the PMSI lender has a relationship with the collateral before the after-acquired lender does.

Because of these rules, anyone lending against non-inventory collateral in the possession of the debtor must consider:

1. The debtor may have obtained the collateral in the last 20 days
2. The holder of one or more PMSIs in the collateral has not yet filed a financing statement but will do so before the 20 days.

More than one creditor may have a valid PMSI in the same collateral.

A seller's purchase money security interest has priority over a pure lender's. As between two lenders, § 9-322(a) applies: First to file or perfect.

UCC § 9-324(g)	(g) [Conflicting purchase-money security interests.] If more than one security interest qualifies for priority in the same collateral under subsection (a), (b), (d), or (f): (1) a security interest securing an obligation incurred as all or part of the price of the collateral has priority over a security interest securing an obligation incurred for value given to enable the debtor to acquire rights in or the use of collateral; and (2) in all other cases, Section 9-322(a) applies to the qualifying security interests.
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2. *Purchase-Money Security Interests*

There is no 20 day grace period for the filing of a PMSI in 9-324(a) does not apply if the property to be sold will be inventory in the hands of the buyer. Most inventory financing is extended on the understanding that the inventory-secured lender's lien will be the only lien against the inventory. Rationale: If a PM secured lender could obtain priority against inventory by filing within 20 days, they could spend that and the inventory financing long before the inventory lender found out about it.

Rules of §9-324(b)

1. The purchase-money financier must perfect no later than the time the debtor receives collateral.
2. The PM financier must give advance notice to the inventory lender that it expects to take a PMSI in the inventory. The financier must search the record for the names and addresses of all secured parties. Notice expires after five years. The PM financier can avoid expiration by repeating the notice.

UCC § 9-324(b)	(b) [Inventory purchase-money priority.] Subject to subsection (c) and except as otherwise provided in subsection (g), a perfected purchase-money security interest in inventory has priority over a conflicting security interest in the same inventory, has priority over a conflicting security interest in chattel paper or an instrument constituting proceeds of the inventory and in proceeds of the chattel paper, if so provided in Section 9-330, and, except as otherwise provided in Section 9-327, also has priority in identifiable cash proceeds of the inventory to the extent the identifiable cash proceeds are received on or before the delivery of the inventory to a buyer, if: (1) the purchase-money security interest is perfected when the debtor receives possession of the inventory; (2) the purchase-money secured party sends an authenticated notification to the holder of the conflicting security interest; (3) the holder of the conflicting security interest receives the notification within five years before the debtor receives possession of the inventory; and (4) the notification states that the person sending the notification has or expects to acquire a purchase-money security interest in inventory of the debtor and describes the inventory.
Cmt. 4	4. Purchase-Money Security Interests in Inventory. Subsections (b) and (c) afford a means by which a purchase-money security interest in inventory can achieve priority over an earlier-filed security interest in the same collateral. To achieve priority, the purchase-money security interest must be perfected when the debtor receives possession of the inventory. For a discussion of when "the debtor receives possession," see Comment 3, above. The 20-day grace period of subsection (a) does not apply. The arrangement between an inventory secured party and its debtor typically requires the secured party to make periodic advances against incoming inventory or periodic releases of old inventory as new inventory is received. A fraudulent debtor may apply to the secured party for advances even though it has already given a purchase-money security interest in the inventory to another secured party. For this reason, subsections (b)(2) through (4) and (c) impose a second condition for the purchase-money security interest's achieving priority: the purchase-money secured party must give notification to the holder of a conflicting security interest who filed against the same item or type of inventory before the purchase-money secured party filed or its security interest became perfected temporarily under Section 9-312(e) or (f). The notification requirement

	protects the non-purchase-money inventory secured party in such a situation: if the inventory secured party has received notification, it presumably will not make an advance; if it has not received notification (or if the other security interest does not qualify as purchase-money), any advance the inventory secured party may make ordinarily will have priority under Section 9-322. Inasmuch as an arrangement for periodic advances against incoming goods is unusual outside the inventory field, subsection (a) does not contain a notification requirement.
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3. *Purchase-Money Priority in Proceeds*

What happens when the debtor exchanges the collateral for proceeds? The seller must take whatever action is required under § 9-315(d) to continue its perfection in the proceeds. Will it have purchase-money priority over a competing security interest perfected by an earlier filing against the debtor naming those proceeds as original collateral? Generally yes.

Purchase money priority extends to collateral or proceeds under § 9-324(a).

Exception: Inventory. A PMSI in inventory flows only to chattel paper, instruments, and cash proceeds. NOT accounts!

C. *Priority in Commingled Collateral*

Commingling: When collateral is mixed with other property.

- Where the identity of the collateral is lost by commingling as the collateral becomes part of a product or mass.

UCC § 9-336(c)	[Attachment of security interest to product or mass.] If collateral becomes commingled goods, a security interest attaches to the product or mass.
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If more than one security interest attaches to a product or mass as a result of commingling, the interests rank equally and share in the proportion that the cost of each party's contribution bears to the total cost of the product or mass.

Ex.

Farmer Green	Farmer Brown
\$20,000 in wheat to Processing Co.	\$80,000 in wheat to Processing Co.
\$20,000 lien in favor of PCA	\$20,000 lien in favor of WestBank
PCA=entitled to 20% of any sale	WestBank=entitled to 80% of any sale

- Where the identity of the collateral is not lost (ex. part installed in a machine.)

Accession: The physical uniting of goods with other goods in such a manner that the identity of the original goods is not lost. UCC § 9-102(a)(1).

If the secured party has only taken an interest in the replacement part, §9-335 applies. Under §9-335(e), any secured party who has a priority security interest in the whole is entitled to prevent removal of an accession from the whole.

UCC §9-335	<p>(a) [Creation of security interest in accession.] A security interest may be created in an accession and continues in collateral that becomes an accession.</p> <p>(b) [Perfection of security interest.] If a security interest is perfected when the collateral becomes an accession, the security interest remains perfected in the collateral.</p> <p>(c) [Priority of security interest.] Except as otherwise provided in subsection (d), the other provisions of this part determine the priority of a security interest in an accession.</p> <p>(d) [Compliance with certificate-of-title statute.] A security interest in an accession is subordinate to a security interest in the whole which is perfected by compliance with the</p>
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	<p>requirements of a certificate-of-title statute under Section 9-311(b).</p> <p>(e) [Removal of accession after default.] After default, subject to Part 6, a secured party may remove an accession from other goods if the security interest in the accession has priority over the claims of every person having an interest in the whole.</p> <p>(f) [Reimbursement following removal.] A secured party that removes an accession from other goods under subsection (e) shall promptly reimburse any holder of a security interest or other lien on, or owner of, the whole or of the other goods, other than the debtor, for the cost of repair of any physical injury to the whole or the other goods. The secured party need not reimburse the holder or owner for any diminution in value of the whole or the other goods caused by the absence of the accession removed or by any necessity for replacing it. A person entitled to reimbursement may refuse permission to remove until the secured party gives adequate assurance for the performance of the obligation to reimburse.</p>
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ASSIGNMENT 34: MULTIPLE ITEMS OF COLLATERAL, MARSHALING, CROSS-COLLATERALIZATION, AND PURCHASE MONEY PRIORITY

Cross Collateralization: A single item of collateral can secure multiple debts to the same secured party.

Multiple items of collateral can serve as security for multiple debts.

A. Multiple Items of Collateral and Cross-Collateralization Provisions in Security Agreements

The creditor can set this up either with the original security agreement with an after-acquired property clause, or can set it up with a second security agreement (this loan is secured by whatever collateral that also secured the first loan.)

The creditor is then able to avoid a situation where one piece of collateral depreciates rapidly, leaving a deficiency balance, while the other piece of collateral is significantly oversecured, leaving the debtor with lots of cash and the creditor in the shitty position of being unsecured on the deficiency balance while the debtor has a wad of skrilla.

B. The Secured Creditor's Right to Choose Its Remedy

A secured creditor generally has the right to choose when it will foreclose. A creditor secured by more than one item of collateral likewise has the right to choose when it will foreclose against each.

A secured creditor wanting to force a debtor into bankruptcy might file an action in replevin on one item of collateral necessary for the debtor's business.

The opposite rule wouldn't work: if a creditor had to foreclose on everything at once, they'd have to go to multiple jurisdictions, foreclose on worthless shit, etc.

1. Debtor-Enforceable Limits on the Secured Creditor's Right to Choose Its Remedy

These kinds of limits are rare. If a secured party is bringing so many foreclosure actions against a debtor that they qualify as a nuisance, a court might bar further actions.

Minority Rule (CA): The Single Action rule.

There can be only one action to enforce payment on a debt secured by a mortgage on real property. If a creditor forecloses on only one piece of real property when multiple pieces are secured, the lien against the other pieces of property may become unenforceable.

Single action rules NEVER apply to real property.

UCC § 9-604(a)(1)	<p>(a) [Enforcement: personal and real property.] If a security agreement covers both personal and real property, a secured party may proceed:</p> <p>(1) under this part as to the personal property without prejudicing any rights with respect to the real property;</p>
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2. ***Release of Collateral***

All collateral remains encumbered until the debt is paid in full.

Under UCC § 9-320(a), a buyer in the ordinary course of business takes property free of any security interest granted by the seller. However, if the debtor does not sell the collateral in the ordinary course of business, § 9-323(d) controls and they do not take free of the security interest.

The debtor may:

1. Pay the debt in full and demand a termination statement be filed. UCC § 9-513(c)
2. Ask the bank to release. The bank doesn't have to and can be just as big a jerk as it wishes.

Sophisticated debtors will generally negotiate a release clause.

Debtors do not need release clauses for inventory as a default rule. However, parties may contract around this.

C. **Marshalling Assets**

1. ***Marshalling as a Limit on the Secured Creditor's Choice***

Marshalling Assets: An equitable doctrine that limits the senior secured creditor's choice of which collateral to pursue. It requires that a creditor look for its recovery to assets not encumbered by junior liens so that the holders of junior liens can recover against the property available to them.

In re Robert E. Derecktor of Rhode Island, Inc.

Debt: RED

Cred.: FDIC (successor in interest to BNE)
RI Port Authority

Facts: RED filed BK11 on 1/3/1992. RIPA seeks to order marshalling of RED's assets to keep FDIC from foreclosing on Dry Dock III (DDIII). 4/13/1979, RIPA loaned RED \$6.5mm secured by then owned and after-acquired fixtures, furniture, furnishings, equipment, machinery, inventory, and other tangible personal property. 2/15/92, debt still at \$4.975mm. 10/23/1987, BNE lent \$6.5mm to RED to buy DDIII. BNE took PMSI (so was first in priority) and a security interest in all presently-owned and after acquired machinery, docks, equipment, inventory, personal property, and general intangibles. 2/6/92: \$5.8mm due. 12/21/1988 BNE loaned \$2.5mm and took an additional security interest in accounts, contracts, contract rights, inventory, and equipment. This security interest also covered the \$6.5mm loan. 2/6/92: \$1.2mm remained on the loan. Both FDIC and Port Authority have security interests in equipment, inventory, machinery, and DDIII. FDIC is senior on DDIII, and sole security interest in intangibles, accounts, contracts, and contract rights. RED's assets are: DDIII, an assignable contract, an insurance claim, and equipment, machinery, and inventory. DDIII: \$6mm. K: \$2.1mm. Claim: \$650k. Equip.: \$1mm.

Rule: Marshalling is an equitable doctrine which rests upon the principle that a creditor having two funds to satisfy his debt may not, by his application of them to his demand, defeat another creditor, who may resort to only one of the funds. The purpose of the doctrine is to prevent the arbitrary action of a senior lienor from destroying the rights of a junior lienor or a creditor having less security. Equity requires the senior creditor to look first to property which cannot be reached by the junior creditor, but only if the senior creditor or third parties are not prejudiced. To apply the marshalling doctrine, three elements must be present: 1. the existence of two creditors of the Debtor; 2. the existence of two funds by the Debtor; and 3. the ability of one creditor to satisfy its claim from either or both of the funds, while the other creditor can only look to one of the funds.

Held: Marshalling is proper in this instance.

Rat: There's two creditors (obviously). There's two funds. One creditor has a sole lien on some of the property while another does not. Sure the unsecured creditors are getting hosed, but that's their problem—they chose to be unsecured creditors.

The doctrine of marshalling assets can be applied only if the senior creditor is not prejudiced. Prejudice can be as minor as having to wait to receive funds.

Marshalling cannot be used to compel the senior creditor to foreclose against homestead property.

Split on whether the first lienor has the right to seek payment of either or both of two funds and each fund is subject to a subordinate lien.

One approach:

Each of the junior liens are compelled to bear the burden of the first lien in due proportion to the value of the fund to which the junior lienholder has a claim.

Other courts:

The earlier-perfected of the two liens can force marshalling.

Problem 34.2

a.

Without Marshalling:

UCB: \$4,500,000 (building)

CE: \$2,500,000 (yacht) + \$1,500,000 (building) = \$4,000,000

Hurst: \$0 (pro rata share as an unsecured creditor)

Trustee: \$600,000

With Marshalling:

UCB: \$4,500,000 (building)

CE: \$2,100,000 (building) + \$1,900,000 (yacht) = \$4,000,000

Hurst: \$250,000

Trustee: \$350,000

b.

Without Marshalling:

UCB: \$4,500,000 (building)

CR: \$2,000,000 (yacht) + \$2,000,000 (building) = \$4,000,000

Hurst: 0

Trustee: \$100,000

With Marshalling

UCB: \$4,500,000 (building)

CR: \$2,100,000 (building) + \$1,900,000 (yacht) = \$4,000,000

Hurst: \$100,000

Trustee: \$0.

ASSIGNMENT 35: SELLERS AGAINST SECURED CREDITORS

If a debtor buys from the true owner for the property, does so honestly, and pays the purchase price, the transaction doesn't really present any legal issues.

Two kinds of dispute.

1. The debtor buys from someone who has less than full ownership of the collateral.
2. The debtor induces sale through questionable conduct: fraud, misrepresentation, bum check.

A. Limits on the After-Acquired Property Clause

UCC § 9-203(b)(2)	(b) [Enforceability.] Except as otherwise provided in subsections (c) through (i), a security interest is enforceable against the debtor and third parties with respect to the collateral only if :
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	(2) the debtor has rights in the collateral or the power to transfer rights in the collateral to a secured party
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Note: This does not require that the debtor be the owner, simply that they have rights in the collateral.

A transferee of a security interest is, under certain circumstances, able to gain greater rights than the transferor in the collateral.

1. **Rules Governing Title to Personal Property**

Void Title Rule

An outright thief gets no title to the thing he steals. There is a basic assumption of *nemo dat qui non habet* or *nemo dat*.

However, if the seller without good title has been entrusted with the property and sells the property in the *normal course of business*, then good title is transferred to a good faith purchaser for value. As between the purchaser and the original owner, the purchaser has better title.

Even someone who obtains title through fraud or deception can transfer good title to a good faith purchaser for value.

One who grants a security interest is a good faith purchaser for value.

UCC §§ 2-403 (1)-(3)	<p>(1) A purchaser of goods acquires all title which his transferor had or had power to transfer except that a purchaser of a limited interest acquires rights only to the extent of the interest purchased. A person with voidable title has power to transfer a good title to a good faith purchaser for value. When goods have been delivered under a transaction of purchase the purchaser has such power even though</p> <p>(a) the transferor was deceived as to the identity of the purchaser, or</p> <p>(b) the delivery was in exchange for a check which is later dishonored, or</p> <p>(c) it was agreed that the transaction was to be a “cash sale”, or</p> <p>(d) the delivery was procured through fraud punishable as larcenous under the criminal law.</p> <p>(2) Any entrusting of possession of goods to a merchant who deals in goods of that kind gives him power to transfer all rights of the entruster to a buyer in ordinary course of business.</p> <p>(3) “Entrusting” includes any delivery and any acquiescence in retention of possession regardless of any condition expressed between the parties to the delivery or acquiescence and regardless of whether the procurement of the entrusting or the possessor's disposition of the goods have been such as to be larcenous under the criminal law.</p>
UCC §§1-201 (b)(29)-(30)	<p>(29) “Purchase” means taking by sale, lease, discount, negotiation, mortgage, pledge, lien, security interest, issue or reissue, gift, or any other voluntary transaction creating an interest in property.</p> <p>(30) “Purchaser” means a person that takes by purchase.</p>
UCC §1-204	<p>A person gives value for rights if the person acquires them:</p> <p>(4) in return for any consideration sufficient to support a simple contract.</p>

Note: Even a security interest in after-acquired property is considered to be given for value.

In re Samuels

CIT financed the inventory of Samuel’s slaughterhouse. Samuels bought cattle from Stowers with bad checks and filed bankruptcy. Stowers wanted the cattle back. However, CIT had an after-acquired property security interest in the cattle, and CIT won out. Congress, in their infinite wisdom, granted sellers of livestock (but nobody else) in cash sales priority over inventory lenders.

3. **The Filing System as an Exception to Nemo Dat**

The concept of a filing system is inconsistent with *nemo dat*.

B. Suppliers Against Inventory-Secured Lenders

In the general case, suppliers get screwed. However, that's kind of OK. Under the UCC, the supplier is put on notice by the filing of the financing statement by the inventory lender—and even if they don't look it up, they know that's how business works. If they didn't like it, they could have taken a security interest themselves which would have been a PMSI, defeating the after-acquired property security interest.

C. Sellers' Weapons Against the After-Acquired Property Clause

1. Purchase-Money Security Interests

Theoretically, they could file PMSI, but the inventory lenders usually bar the debtor from doing so.

2. Retention of Title

"Hey, let's not sell on credit." OK, you go C.O.D., which pisses off the customer and he goes and buys from someone else. OR, the seller contracts to sell⁷. That doesn't work, though. Under UCC §2-401(1), that's an immediate sale and grant of security interest. If the security interest isn't perfected, then the seller loses—they're subordinate to the after-acquired property clause.

3. Consignment

The UCC recognizes three types of consignment:

1. The group excluded from Article 9 coverage by excepting from the Article 9 definition of consignment.

UCC § 9-109(a)(4)	(a) [General scope of article.] Except as otherwise provided in subsections (c) and (d), this article applies to: (4) a consignment;
UCC § 9-102(a)(20)	(20) "Consignment" means a transaction, regardless of its form, in which a person delivers goods to a merchant for the purpose of sale and: (A) the merchant: (i) deals in goods of that kind under a name other than the name of the person making delivery; (ii) is not an auctioneer; and (iii) is not generally known by its creditors to be substantially engaged in selling the goods of others; (B) with respect to each delivery, the aggregate value of the goods is \$1,000 or more at the time of delivery; (C) the goods are not consumer goods immediately before delivery; and (D) the transaction does not create a security interest that secures an obligation.

- a. Consignments in which the consignee does business under the name of the consignor.
 - b. Small consignments where shipments are under \$1000.
 - c. The consignor is a consumer, not a merchant.
 - d. Any other consignment that doesn't create a security interest.
2. The consignment is a disguised security interest. A security interest is an interest in property contingent on nonpayment of a debt. Example: An arrangement where the consignee could not return the goods. Why? Because the seller would have no interest in the property unless the consignee failed to sell them and failed to pay for them.
 3. § 9-102(a)(20) consignments that are included in the definition of security interest.

4. The Seller's Right of Reclamation

If a buyer receives goods while insolvent, the seller can reclaim subject to the rights of buyer's secured creditors that attached while the goods were in the hands of the buyer.

UCC § 2-702(2)	Where the seller discovers that the buyer has received goods on credit while insolvent he may reclaim the goods upon demand made within ten days after the receipt, but if misrepresentation of solvency has been made to the particular seller in writing within three months before delivery the ten day limitation does not apply. Except as provided
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⁷ A contract for sale is where S gives possession of the goods pursuant to an agreement that S retains ownership of the goods and that B will purchase the goods on installment.

	in this subsection the seller may not base a right to reclaim goods on the buyer's fraudulent or innocent misrepresentation of solvency or of intent to pay.
11 USC § 546(c)	<p>(1) Except as provided in subsection (d) of this section and in section 507(c), and subject to the prior rights of a holder of a security interest in such goods or the proceeds thereof, the rights and powers of the trustee under sections 544(a), 545, 547, and 549 are subject to the right of a seller of goods that has sold goods to the debtor, in the ordinary course of such seller's business, to reclaim such goods if the debtor has received such goods while insolvent, within 45 days before the date of the commencement of a case under this title, but such seller may not reclaim such goods unless such seller demands in writing reclamation of such goods--</p> <p>(A) not later than 45 days after the date of receipt of such goods by the debtor; or</p> <p>(B) not later than 20 days after the date of commencement of the case, if the 45-day period expires after the commencement of the case.</p> <p>(2) If a seller of goods fails to provide notice in the manner described in paragraph (1), the seller still may assert the rights contained in section 503(b)(9).</p>

Big differences:

UCC 2-702(2) only allows 10 days and doesn't require writing.

BKC 546(c) allows 45 days or 20 days of the commencement of the case, whichever is earlier, and DOES require writing.

However, in most cases, the buyer has granted a security interest in the property that attached at the identification of the goods in the sale contract because of an after-acquired property clause. The seller loses.

In re M. Paoletta & Sons, Inc.

Facts:

1/26/1982: MPS entered into a financing agreement with MNC secured by receivables, inventory, and equipment. This financing agreement is in effect until 1/26/1986.

10/82: MNC permitted MPS to increase their credit line to participate in a special deal from tobacco companies. This brought the loan "out of formula" and it remained out of formula for the remainder of the timeline.

MNC exercised "considerable control" over the day to day operations of MPS, including frequent audits of inventory.

Early 1984, MNC became worried about MPS' ability to pay.

5-85: MNC discussed plans to liquidate and repay all creditors with MPS.

9-85: MPS began to liquidate assets.

Paoletta told some tobacco companies that he wouldn't renew his personal guarantees of MPS' loans.

American Tobacco had a letter of credit from MPS secured by MDNB.

1/3/86, MDNB told AmTob that they would no longer honor the letter of credit for invoices after 1/10/86.

1/9/86 AmTob called MDNB to find out if letter of credit was terminated by MPS or MDNB. They referred to MNC.

1/15/86 MNC told AmTob that the decision was MPS' (though it was really MPC). AmTob continued to sell to MPS.

1/28/86 MNC started dishonoring MPS checks.

1/29 MNC told MPS that they weren't honoring checks.

1/30 MNC informed MPS they were in default and took possession of inventory.

Five tobacco cos. filed proofs of claim.

Issue: Whether the tobacco companies may reclaim the inventory they sold to MPS?

Rule: § 2-207(2): Where seller discovers that the buyer has received goods on credit while insolvent he may reclaim the goods upon demand made within ten days of receipt. § 2-204 "Subject to the rights of a buyer in ordinary course or other good faith purchaser under § 2-403."

Narr.

Issue:	Is MNC a good faith purchaser for purposes of § 2-207?
Rule:	A creditor that enforces a financing agreement in a manner consistent with the clear terms of the agreement and the expectations of the parties acts in “good faith.”
Held:	The BK judge did not find that MNC acted outside the scope of the financing agreement. Therefore, they acted in good faith and the tobacco companies may not reclaim the goods.

It’s fairly rare that a debtor’s inventory isn’t encumbered. 2-702(3) effectively guts 2-702(2).

The right to reclaim in BKC §546(c) doesn’t even have the “good faith” requirement. The secured creditor only needs to have “prior rights” to prevail over a reclaiming seller. Those rights are in the after-acquired property clauses.

“Feeding the Lien”: An inventory supplier keeps putting inventory into a failing business where the inventory is subject to another creditor’s lien.

5. ***Express or Implied Agreement with the Secured Creditor***

Of course, the seller could enter into an agreement with the secured lender. The secured lender could disburse directly to the seller. However, this eliminates float, and many businesses aren’t going to want to do this. Not only that, but the lender may want their lien fed.

6. ***Equitable Subordination***

In re M. Paolella & Sons, Inc

Facts:	BK Courts, sitting in equity, have the authority to subordinate claims on equitable grounds. 11 USC § 510(c) codifies case law allowing BK courts to adjust the status of claims on equitable grounds. The clear intent of Congress was to codify the extant principles, most courts have adopted the three-prong test from <i>In re Mobile Steel</i> :
1.	The claimant must have engaged in some kind of inequitable conduct
2.	The misconduct must have resulted in injury to the creditors of the bankrupt or conferred an unfair advantage on the claimant.
3.	Equitable subordination of the claim must not be inconsistent with the provisions of the Bankruptcy Act.
	In applying these principles, the courts differentiate between insiders and non-insiders. For non-insiders, a much higher standard of misconduct is required. However, courts look beyond the statutory definition of insider and look to see whether the party has attained fiduciary status by exercising control over the debtor.
Issue:	Whether MNC has attained fiduciary status over MPS by exercising control.
Rule:	A non-insured will be held to a fiduciary standard only where his ability to command the debtor’s obedience to his policy directives is so overwhelming that there has been, to some extent, a merger of identity.
Held:	MNC is neither an insider or fiduciary of the debtor.
Rat:	MNC did not participate in the debtor’s management, determine operating decisions, or have a presence on the board. Paolella controlled the debtor, who decided that the debtor would participate in tobacco purchase programs, and who decided that the debtor would expand and then liquidate.
Issue:	Was the conduct of MNC enough to support equitable subordination?
Rule:	The non-insider’s misconduct must be “gross or egregious.”
Held:	That wasn’t this.

7. *Unjust Enrichment*

Since *Peerless Packing Co, Inc. v. Malone & Hyde, Inc.* courts have become more receptive to unjust enrichment claims.

Whether a creditor that holds a perfected security interest can be held liable to an unsecured creditor based on a theory of unjust enrichment for benefits that enhance the value of the collateral... When an unsecured creditor confers a benefit upon a secured creditor by adding to or enhancing the creditor's collateral and a claim for unjust enrichment is recognized, the secured creditor in effect loses its priority status despite its compliance with the procedures set out in Article 9... The UCC priority system thus reflects the legislative judgment that the value of a predictable system of priorities ordinarily outweighs the disadvantage of the system's occasional inequities... **In a situation where a secured creditor initiates or encourages transactions between the debtor and suppliers of goods or services, and benefits from the goods or services supplied to produce such debts, equitable principles requires that the secured creditor compensate even an unsecured creditor to avoid being unjustly enriched... A secured creditor can protect itself from unjust enrichment claims by remaining uninvolved or by informing the proper parties of its intent not to pay for debts incurred in maintaining, enhancing, or making additions to secured collateral.**

ASSIGNMENT 36: BUYERS AGAINST SECURED CREDITORS

A. Introduction

UCC § 9-401	(a) [Other law governs alienability; exceptions.] Except as otherwise provided in subsection (b) and Sections 9-406, 9-407, 9-408, and 9-409, whether a debtor's rights in collateral may be voluntarily or involuntarily transferred is governed by law other than this article. (b) [Agreement does not prevent transfer.] An agreement between the debtor and secured party which prohibits a transfer of the debtor's rights in collateral or makes the transfer a default does not prevent the transfer from taking effect.
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UCC § 9-401: A security agreement doesn't restrict the free alienability of property.

The rules on who takes subject to a security interest are based around expectations.

For example, we expect to search real estate records when purchasing a house, so if we fail to find a recorded security interest, we will take subject to the security interest.

However, we don't expect to search when we buy groceries, so we would not take subject to a security interest granted by the seller.

B. Buyers of Personal Property

General Rule: Buyers of personal property take subject to pre-existing security agreements.

UCC § 9-201(a)	[General effectiveness.] Except as otherwise provided in [the Uniform Commercial Code], a security agreement is effective according to its terms between the parties, against purchasers of the collateral, and against creditors.
UCC § 9-315(a)	[Disposition of collateral: continuation of security interest or agricultural lien; proceeds.] Except as otherwise provided in this article and in Section 2-403(2): (1) a security interest or agricultural lien continues in collateral notwithstanding sale, lease, license, exchange, or other disposition thereof unless the secured party authorized the disposition free of the security interest or agricultural lien; and (2) a security interest attaches to any identifiable proceeds of collateral.

1. *The Buyer-in-the-Ordinary-Course Exception: UCC § 9-320(a)*

UCC § 9-320(a)	[Buyer in ordinary course of business.] Except as otherwise provided in subsection (e), a buyer in ordinary course of business, other than a person buying farm products
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	from a person engaged in farming operations, takes free of a security interest created by the buyer's seller, even if the security interest is perfected and the buyer knows of its existence.
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Why this distinction between personal property and real property? It's probably just an accident of history codified by the UCC (according to LoPucki & Warren). I disagree. There would be massive transaction costs associated with a contrary rule, to the point where society would stop recognizing security interests in inventory altogether.

Search is still required for certain types of personal property:

Intellectual Property

Automobiles

Aircraft

Important: § 9-320(a) is not limited to *consumer* buyers.

The Ordinary Course of Business

UCC § 9-201(b)(9)	“Buyer in ordinary course of business” means a person that buys goods in good faith, without knowledge that the sale violates the rights of another person in the goods, and in the ordinary course from a person, other than a pawnbroker, in the business of selling goods of that kind. A person buys goods in the ordinary course if the sale to the person comports with the usual or customary practices in the kind of business in which the seller is engaged or with the seller's own usual or customary practices. A person that sells oil, gas, or other minerals at the wellhead or minehead is a person in the business of selling goods of that kind. A buyer in ordinary course of business may buy for cash, by exchange of other property, or on secured or unsecured credit, and may acquire goods or documents of title under a preexisting contract for sale. Only a buyer that takes possession of the goods or has a right to recover the goods from the seller under Article 2 may be a buyer in ordinary course of business. “Buyer in ordinary course of business” does not include a person that acquires goods in a transfer in bulk or as security for or in total or partial satisfaction of a money debt.
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The Buyer's Knowledge

§ 9-201(b)(9) says that knowledge that a sale violates the rights of another person makes a purchase not in the ordinary course of business. This doesn't mean that knowledge of a security interest makes a buyer not in the ordinary course of business. The buyer must know that the security agreement prohibits sale.

Created by His Seller

The purchaser only takes free of a security interest granted by the seller. If the property is subject to a security interest granted by the seller's seller, then the purchaser in the ordinary course of business takes subject to that security interest regardless.

The Farm Products Exception

§ 9-320(a) excludes buyers of farm products from the exception. However, the Food Security Act gives the protection right back to them.

11 USC § 1631(d)	Except as provided in subsection (e) of this section and notwithstanding any other provision of Federal, State, or local law, 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.
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When Does a Buyer Become a Buyer?

If a person has given the seller money but isn't yet a buyer, then they're just an unsecured creditor. It's enormously important WHEN someone becomes a buyer sometimes.

Under UCC § 1-201(b)(9), only a buyer who takes possession of the goods or has a right to recover the goods is a buyer in the ordinary course of business.

Who is entitled to recover the goods?

UCC § 2-502	(1) Subject to subsections (2) and (3) and even though the goods have not been shipped a buyer who has paid a part or all of the price of goods in which he has a special property under the provisions of the immediately preceding section may on making and keeping good a tender of any unpaid portion of their price recover them from the seller if: (a) in the case of goods bought for personal, family, or household purposes, the seller repudiates or fails to deliver as required by the contract; or (b) in all cases, the seller becomes insolvent within ten days after receipt of the first installment on their price. (2) The buyer's right to recover the goods under subsection (1)(a) vests upon acquisition of a special property, even if the seller had not then repudiated or failed to deliver. (3) If the identification creating his special property has been made by the buyer he acquires the right to recover the goods only if they conform to the contract for sale.
UCC § 2-716	(1) Specific performance may be decreed where the goods are unique or in other proper circumstances. (2) The decree for specific performance may include such terms and conditions as to payment of the price, damages, or other relief as the court may deem just. (3) The buyer has a right of replevin for goods identified to the contract if after reasonable effort he is unable to effect cover for such goods or the circumstances reasonably indicate that such effort will be unavailing or if the goods have been shipped under reservation and satisfaction of the security interest in them has been made or tendered. In the case of goods bought for personal, family, or household purposes, the buyer's right of replevin vests upon acquisition of a special property, even if the seller had not then repudiated or failed to deliver.

First National Bank of El Campo v. Buss

Several buyers had purchased autos from Greg's Auto Sales. Each buyer had paid for and taken possession of a vehicle. Even though FNB had possession of the titles to the vehicle, and Texas law provided that no sale of an auto would be valid if there wasn't a transfer of title, the provisions of Article 9 were held to supersede the Texas law. FNB was forced to give over the titles.

Sales of Goods in the Possession of the Secured Party

Tanbro Fabrics Corp. v. Deering Milliken, Inc.

Deering had possession of 267,000 yards of fabric as security for an account owed by Mill Fabrics. Mill Fabrics sold the fabric to Tanbro. Since Tanbro was familiar with the industry practice of leaving cloth possession of the seller's seller as security, they didn't think it was odd that they were buying cloth in the possession of another. After Tanbro paid Mill Fabrics, Mill Fabrics went out of business and didn't pay Deering. The court held that Tanbro was a purchaser in the ordinary course of business and was entitled to the fabric.

The result of *Tanbro Fabrics* led to revised UCC § 9-320.

§ 9-320(e) "Rejects the holding of *Tanbro Fabrics*" cmt. 8.

Remember that if a “seller” is an agent of the seller’s seller because of an agreement that they hold the good for the benefit of the seller’s seller, the goods are still in the possession of the seller’s seller.

2. *The Buyer-Not-in-the-Ordinary-Course Exception: UCC §§ 9-323(d)-(e) and 9-317(b)*

Perfected Security Interest	Not Perfected Security Interest
Is it not in the ordinary course of business? Is it not authorized by the secured party? Buyer takes subject.	Is the purchaser a good-faith purchaser for value? Buyer takes free

UCC § 9-323(d)-(e)	(d) [Buyer of goods.] Except as otherwise provided in subsection (e), a buyer of goods other than a buyer in ordinary course of business takes free of a security interest to the extent that it secures advances made after the earlier of: (1) the time the secured party acquires knowledge of the buyer's purchase; or (2) 45 days after the purchase. (e) [Advances made pursuant to commitment: priority of buyer of goods.] Subsection (d) does not apply if the advance is made pursuant to a commitment entered into without knowledge of the buyer's purchase and before the expiration of the 45-day period.
UCC § 9-317(b)	[Buyers that receive delivery.] Except as otherwise provided in subsection (e), a buyer, other than a secured party, of tangible chattel paper, documents, goods, instruments, or a security certificate takes free of a security interest or agricultural lien if the buyer gives value and receives delivery of the collateral without knowledge of the security interest or agricultural lien and before it is perfected.

3. *The Authorized Disposition Exception*

UCC § 9-315(a)(1)	(a) [Disposition of collateral: continuation of security interest or agricultural lien; proceeds.] Except as otherwise provided in this article and in Section 2-403(2): (1) a security interest or agricultural lien continues in collateral notwithstanding sale, lease, license, exchange, or other disposition thereof unless the secured party authorized the disposition free of the security interest or agricultural lien;
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1. The authorized disposition exception does not depend on the equities: it doesn’t matter if the buyer searched the public record or if he knew of the security interest.
2. Authorization may be either express or implied.

Gretna State Bank v. Cornbelt Livestock Co.

Gretna had a security interest in the debtor’s hogs and cows (farm products under § 9-102(a)(34)). The security agreement prohibited sale without prior written consent. However, since the debtor had sold cattle and hogs without written consent but with the bank’s knowledge in the past, and the bank had never objected to the sales, the bank was held to have authorized sales implicitly.

3. The authorization must be to sell free and clear of the security interest

Conditional Authorizations

There’s a split of authority on conditional authorizations.

If the secured party authorizes sale on the condition that the proceeds be applied to the loan, some courts hold that the buyer takes free of the interest regardless of whether the debtor complies. Other courts may rule that the buyer takes subject to the security interest. Courts are more likely to rule that the buyer takes clear if the buyer had no knowledge of the condition.

RFC Capital Corporation v. Earthlink

Facts: RFC loaned \$12mm to ICC, taking a security interest in (among other things) all of ICC’s customer base.
2000: ICC in financial trouble, agreed to sell customer base to EL. Bryant(EL) asked if RFC knew about the sale. Hanson(ICC) said they did and had agreed to it. At the time, RFC had not agreed to sale. After review of ICC financials, RFC and ICC executed an amendment to the Security Agreement,

	stating that RFC consented to the sale of the customer base by ICC, and that they would release their security interest when ICC performed their obligations under the Security Agreement (paying the loan off, basically.) Hansen(ICC) forbade RFC from telling EL about the terms of the amendment. RFC followed Hansen's dick move even though they knew that EL expected to take the customer base free.
5/24/02:	Only 25,144 ICC customers paid for EL service. EL had paid a bounty for 40,000, so refused to pay ICC anything more. RFC then filed suit against EL alleging that EL had damaged their collateral without obtaining a release.
Issue 1:	Did RFC expressly authorize the release of its security interest when it consented to the sale in the amendment to the security agreement?
Rule:	UCC § 9-315: A security interest continues in the collateral unless the secured party authorizes the disposition free of security interest.
Held:	This was a conditional release.
Rat:	When you read the amendment, RFC said they'd release the security interest only after they'd been paid in full. This can't really be construed as an actual and express release.
Issue 2:	Is the condition contained in the amendment binding upon EL as a good-faith purchaser for value who had no control over whether the condition was met?
Rule:	Any and all conditions a secured party places upon its consent must be satisfied for the consent to be effective.
Held:	RFC's consistent position was that it had to be paid off to release their security interest. ICC did not satisfy the condition. Therefore, RFC never agreed to release their security interest.
Rat:	A third party purchaser has to ensure that any security interest is released, which places a burden on them. However, it's not that great a burden: just talk to the creditor and see what it takes to make sure this gets done. If it's too risky, don't go through with the purchase.

4. *The Consumer-to-Consumer-Sale Exception*

When a sale is outside of the normal course of business, even consumers have to play the search and file game.

UCC § 9-320(b)	<p>[Buyer of consumer goods.] Except as otherwise provided in subsection (e), a buyer of goods from a person who used or bought the goods for use primarily for personal, family, or household purposes takes free of a security interest, even if perfected, if the buyer buys:</p> <ul style="list-style-type: none"> (1) without knowledge of the security interest; (2) for value; (3) primarily for the buyer's personal, family, or household purposes; and (4) before the filing of a financing statement covering the goods.
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Notice that this exception doesn't apply if a financing statement has been filed. Mainly only works if the seller's seller relied on an automatically-perfected PMSI.

ASSIGNMENT 38: COMPETITIONS INVOLVING FEDERAL TAX LIENS: THE BASICS

There's several different ways in which the government enters the competition for collateral:

1. Taxes
2. Criminal Fines
3. SBA loans
4. Accidental overpayment of Social Security benefits

Income taxes are not the principal source of tax losses for the U.S. Government. Tax losses are usually incurred from underpayment of payroll taxes.

A. **The Creation and Perfection of Federal Tax Liens**

1. *Creation*

26 USC § 6321	If any person liable to pay any tax neglects or refuses to pay the same after demand, the
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	amount (including any interest, additional amount, addition to tax, or assessable penalty, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person.
26 USC § 6322	Unless another date is specifically fixed by law, the lien imposed by section 6321 shall arise at the time the assessment is made and shall continue until the liability for the amount so assessed (or a judgment against the taxpayer arising out of such liability) is satisfied or becomes unenforceable by reason of lapse of time.

Assessment: The time at which the government determines that tax is owing.

Demand: The government notifies the debtor of the owed tax. This is when the lien comes into existence, but it relates back to the time of assessment.

2. *Perfection*

The Federal Tax Lien Act uses the word “valid” instead of “perfection” but it kind of means the same thing. I.R.C. § 6323(f) defers to state law as to where the tax lien is filed.

26 USC § 6323(f)	<p>(f) Place for filing notice; form.--</p> <p>(1) Place for filing.--The notice referred to in subsection (a) shall be filed--</p> <p>(A) Under State laws.--</p> <p>(i) Real property.--In the case of real property, in one office within the State (or the county, or other governmental subdivision), as designated by the laws of such State, in which the property subject to the lien is situated; and</p> <p>(ii) Personal property.--In the case of personal property, whether tangible or intangible, in one office within the State (or the county, or other governmental subdivision), as designated by the laws of such State, in which the property subject to the lien is situated, except that State law merely conforming to or reenacting Federal law establishing a national filing system does not constitute a second office for filing as designated by the laws of such State; or</p> <p>(B) With clerk of district court.--In the office of the clerk of the United States district court for the judicial district in which the property subject to the lien is situated, whenever the State has not by law designated one office which meets the requirements of subparagraph (A); or</p> <p>(C) With Recorder of Deeds of the District of Columbia.--In the office of the Recorder of Deeds of the District of Columbia, if the property subject to the lien is situated in the District of Columbia.</p>
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If a tax lien is not filed when a debtor sells the property, grants a security interest in the property, or loses possession to a sheriff holding a writ of execution, then the tax lien is not valid with respect to that creditor.

Tax liens use the language “valid” and “not valid” versus another interest instead of priority, but it kind of amounts to the same thing.

The Federal Government had the power to grant über-priority to federal taxes like state property taxes. Why not?

1. It would deter commercial lending.
2. Hey, fuck it. They can still grant über-priority if they want. Canada does.

However, they do play by a different set of rules: under the IRC, a security interest only exists if its perfected.

26 USC § 6323(h)(1)	<p>Security interest.--The term “security interest” means any interest in property acquired by contract for the purpose of securing payment or performance of an obligation or indemnifying against loss or liability. A security interest exists at any time (A) if, at such time, the property is in existence and the interest has become protected under local law against a subsequent judgment lien arising out of an unsecured obligation, and (B) to the extent that, at such time, the holder has parted with money or money's worth.</p>
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3. Remedies for Enforcement

The Federal Tax Lien Act provides the remedy for enforcement if the debtor doesn't pay within 10 days of demand.

1. The IRS can physically seize the debtor's property without the use of a marshal or sheriff.
2. The IRS can serve a notice of levy on banks or any third party who holds the debtor's property.

State exemptions to execution against property don't apply to the IRS. The FTLA does contain a set of exemptions. A tax sale is subject to prior liens, but discharges subordinate liens.

4. Maintaining Perfection of a Tax Lien

26 USC § 6323(g)	<p>Refiling of notice.--For purposes of this section--</p> <p>(1) General rule.--Unless notice of lien is refiled in the manner prescribed in paragraph (2) during the required refiling period, such notice of lien shall be treated as filed on the date on which it is filed (in accordance with subsection (f)) after the expiration of such refiling period.</p> <p>(2) Place for filing.--A notice of lien refiled during the required refiling period shall be effective only--</p> <p>(A) if--</p> <p>(i) such notice of lien is refiled in the office in which the prior notice of lien was filed, and</p> <p>(ii) in the case of real property, the fact of refiling is entered and recorded in an index to the extent required by subsection (f)(4); and</p> <p>(B) in any case in which, 90 days or more prior to the date of a refiling of notice of lien under subparagraph (A), the Secretary received written information (in the manner prescribed in regulations issued by the Secretary) concerning a change in the taxpayer's residence, if a notice of such lien is also filed in accordance with subsection (f) in the State in which such residence is located.</p> <p>(3) Required refiling period.--In the case of any notice of lien, the term "required refiling period" means--</p> <p>(A) the one-year period ending 30 days after the expiration of 10 years after the date of the assessment of the tax, and</p> <p>(B) the one-year period ending with the expiration of 10 years after the close of the preceding required refiling period for such notice of lien.</p> <p>(4) Transitional rule.--Notwithstanding paragraph (3), if the assessment of the tax was made before January 1, 1962, the first required refiling period shall be the calendar year 1967.</p>
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Must refile a tax lien in the one year period ending ten years and thirty days after the assessment of the tax.

If not renewed, then the lien lapses. It may be revived, but loses its "priority."

A tax lien may be maintained in perpetuity, but is invalid if the statute of limitations on the underlying liability has run.

In re Eschenbach

Facts:	9/22/97, Eschenbach lived in Martin County, FL and received a notice of a federal tax lien. Eschenbach then moved to Tarrant County, TX. On 10/2/2000, filed BK13. IRS filed a proof of secured claim for \$5,906.12. Eschenbach claims that he only owned \$3,000 of property when he moved to Texas. On 5/31/01, Eschenbach objected to the proof of secured claim. Eschenbach claims that the IRS lien as to the property acquired in Tarrant County is invalid because they did not file the tax lien in Texas as required under Texas law.
Issue:	Does the IRS have a valid lien on property acquired after a debtor moves when the IRS has only filed their tax lien as required in the first state of residence?
Rule:	A federal tax lien attaches to any property owned by the delinquent at any time during the life of the lien.
Held:	Lien is good. The notice of tax lien filed 9/27/1997 captures all the debtor's personal property.

Rat:	Under the IRC, any after-acquired property is deemed to be located in the place where the tax lien was first filed. This prevents the IRS from having to file tax liens in every dang county in the country.
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B. Competitions Involving Federal Tax Liens

26 USC § 6323(a)	Purchasers, holders of security interests, mechanic's lienors, and judgment lien creditors. --The lien imposed by section 6321 shall not be valid as against any purchaser, holder of a security interest, mechanic's lienor, or judgment lien creditor until notice thereof which meets the requirements of subsection (f) has been filed by the Secretary.
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Poorly worded: this should be read to mean that priority (validity) is only effective as of the date of filing. The idea of first in time is first in right is so obvious the drafters didn't include it.

1. Security Interest

26 USC § 6323(h)(1) (above) defines security interest.

A security interests exists under 6323(h)(1) when:

- A. The property must exist and be identified.
- B. The holder of the security interest must have parted with money or other value.

The security interest beats the tax lien if it "exists" before the Notice of Tax Lien is filed.

2. Purchaser

To prevail over a tax lien, a purchaser must acquire his status before the government files its tax lien.

26 USC § 6323(h)(6)	Purchaser. --The term "purchaser" means a person who, for adequate and full consideration in money or money's worth, acquires an interest (other than a lien or security interest) in property which is valid under local law against subsequent purchasers without actual notice. In applying the preceding sentence for purposes of subsection (a) of this section, and for purposes of section 6324-- (A) a lease of property, (B) a written executory contract to purchase or lease property, (C) an option to purchase or lease property or any interest therein, or (D) an option to renew or extend a lease of property, which is not a lien or security interest shall be treated as an interest in property.
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Basically, if the purchaser does whatever he has to do to prevail over a second, later good faith purchaser for value, then he prevails over the IRS tax lien.

Possession alone gives actual notice to the IRS that would defeat a tax lien.

Mayer-Dupree v. Internal Revenue Service

Facts:	1991, the government seized a vehicle in satisfaction of a tax lien noticed in 1988 and 1990. M-D says she purchased the vehicle from the debtor in 1986, but didn't register until after the seizure.
Rule:	A federal tax lien is not valid against a purchaser until the government files proper notice. A purchaser is one who acquires an interest (other than lien or security interest) in property which is valid in local law against subsequent purchasers without actual notice.
Held:	You didn't register, you're not a purchaser. So sorry.

If local law requires filing/recording of a transfer, that's what will protect against a tax lien.

- 1. Automobiles
- 2. Aircraft
- 3. Trademarks
- 4. Copyrights

5. Accounts receivable
6. Chattel paper

Generally, a purchase becomes effective when it becomes effective against the seller, which is when the contract provides.

However, a purchaser who leaves the property with a seller who deals in goods of that sort still loses to the IRS, because they would lose to a later buyer in the ordinary course of business.

United States v. McDermott

Facts: 12/9/86, IRS assessed McDermott for unpaid federal taxes from 1977-1981. The lien created wasn't valid against a judgment lien creditor until it was filed. The lien was filed in Salt Lake County Recorder's office on 9/9/1987. On 7/6/1987 Zions FNB docketed a state-court judgment in the Salt Lake County Recorder's office, creating a judgment lien on all of McDermott's real property in Salt Lake County, including after-acquired property. 9/23/87 McDermott bought some real property. This is an interpleader by McDermott to adjudicate rights to the proceeds of sale of that property between the IRS and ZFNB.

Issue: Whether the lien of ZFNB was perfected with regard to this property before the IRS lien.

Rule: A security interest in after-acquired property is generally not considered perfected when the financing statement is filed, but only when the security interest has attached to particular property upon the debtor's acquisition of the property.

Held: Since the security interest in the after-acquired property did not attach until the property was acquired, it was not perfected before the filing of the lien.

Issue: Is the IRS lien first in time before the attachment?

Rule: The filing of notice renders the federal tax lien extant for "first in time" priority purposes regardless of whether it has yet attached to identifiable property.

Rat: Under 26 USC § 6323(c)(1) exempts certain after-acquired property security interests. Affording special priority to these security interests presupposes they'd need it—it assumes that without it, the tax lien would have priority. Further, the Government, as an unwilling creditor, should be afforded special deference that a willing creditor is not afforded.