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REVISED ARTICLE 9 OF THE UCC: SCOPE,
PERFECTION, PRIORITIES, AND
DEFAULT*

Barkley Clark†

I. BROADENED SCOPE OF REVISED ARTICLE 9

Revised Article 9 continues to apply to transactions, regardless of form, that create a security interest in personal property or fixtures by contract. Rev. UCC § 9-109(a). It continues to exclude: landlord’s liens; nonagricultural statutory liens; wage assignments; sales of intangibles as part of a sale of the business out of which they arose; assignments of receivables for the purpose of collection only; assignments of receivables in full or partial satisfaction of prior debt; interests in insurance policies other than health care receivables; assignments of rights represented by a judgment; setoff; real-property liens; and assignments of tort claims other than commercial tort claims. Rev. UCC § 9-109(d).

Revised Article 9 does not apply to the extent that a statute, regulation, or treaty of the United States preempts it; this does not mean that Article 9 bows out just because a federal law covers some aspects of the transaction, as some cases under current law suggest. See Rev. UCC § 9-109(c)(1) and Comment 8.

The basic scope of Article 9—coverage of consensual security interests in personal property and fixtures—remains intact. As under current law, the application of Revised Article 9 to a security interest in a secured obligation is not affected by the fact

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that the obligation is itself secured by a transaction or interest to which Article 9 does not apply. Rev. UCC § 9-109(b). Comment 7 to Rev. UCC § 9-109 gives the example of a security interest in a promissory note that is itself secured by real estate. Under the revision, if the note is perfected under Article 9 (probably by possession) and the underlying mortgage is perfected under real estate law, perfection of a security interest in the note automatically carries over to the real estate, without the necessity of any recorded assignment of the mortgage. Conversely, one cannot obtain a security interest in the underlying real estate mortgage without an effective security interest in the note secured by the mortgage. On this last point, the revision rejects cases decided under current law like In re Maryville Savings & Loan Corp.¹

In a fine-tuning of current law, Rev. UCC § 9-109(a) provides that Article 9 applies to:

- Any transaction that creates a security interest in personal property or fixtures by contract (same as current law)
- An agricultural lien (a major change in the law, since the lien is created by statute rather than by contract)
- A sale of accounts, chattel paper, payment intangibles, or promissory notes (the last two categories are new)
- A consignment (same as current law, with some changes)
- Security interests arising under other parts of the UCC (same as current law)

Although security interests generally must be consensual to fall within the scope of Article 9, the revision includes one important nonconsensual interest: statutory agricultural liens. Moreover, the revision expands the scope of Article 9 in several other important respects. This should bring more transactions out of the murky realm of common law liens and into the more predictable framework of the UCC. Several of the expansions are intended to facilitate securitization. Following are the most important expansions of scope brought about by the revision.

A. **Outright Sales of Accounts, Promissory Notes, Chattel Paper, and Payment Intangibles**

Current Article 9 covers outright sales of accounts and chattel paper, but not any other type of collateral. UCC § 9-102(1)(b). The revision covers outright sales of accounts, chattel paper, payment intangibles, and promissory notes. Rev. UCC § 9-109(a)(3). As a drafting convention, it treats these sales as security interests. The term "accounts" is defined more broadly in Rev. UCC § 9-102(a)(2) to include not only payment obligations arising from the sale or lease of goods or the provision of services, but other payment obligations such as license fees payable for the use of software, credit card receivables, and health care insurance receivables. This expanded definition effectively shrinks the residual category of general intangibles, the outright sale of which remains outside the scope of Article 9; this will facilitate securitization transactions involving a wider variety of receivables. Another important contribution of the revision is the clarification that an outright seller of accounts retains no interest in the property sold, thereby rejecting *Octagon Gas Systems v. Rimmer,* which erroneously held that the outright seller of accounts retained sufficient ownership that the transfer did not remove the property from its bankruptcy estate. Rev. UCC § 9-318(a).

Revised Article 9 also covers the outright sale of "promis-
sory notes," a term that excludes checks or certificates of deposit. Rev. UCC § 9-102(a)(65). The purpose behind this expansion of scope is to facilitate securitization of this type of payment instrument.

The outright sale of chattel paper has always been within the scope of Article 9. The revision broadens the definition of chattel paper (Rev. UCC § 9-102(a)(11)) to include obligations secured by software to the extent sold in integrated transactions with specific goods. Outright sales of such hybrid chattel paper will be within the scope of Article 9, as will sales of electronic chattel paper. See Rev. UCC § 9-102(a)(31) and Official Comment 5(b) to that section.

Current Article 9 excludes from its scope the outright sale of general intangibles. While the revision continues this general exclusion, it brings within the scope of Article 9 most sales of payment intangibles, defined in Rev. UCC § 9-102(a)(61) as general intangibles under which the account debtor’s principal obligation is a monetary obligation. This primarily means payment rights that arise out of loan agreements that do not constitute instruments. This important change is intended to facilitate securitizations. Outright sales of payment intangibles are automatically perfected. Rev. UCC § 9-309(a)(3). Automatic perfection permits financial institutions that sell loan participations to avoid having a UCC financing statement filed against them.

B. Insurance Claims

The early drafts of the revision would have brought all insurance claims, including the assignment of cash surrender value of life insurance, within the scope of Article 9. The final draft continues the general exclusion of insurance claims (except as proceeds). Rev. UCC § 9-109(d)(8). The exclusion probably covers related transactions such as insurance premium financing. However, on the theory that originators of insurance receivables arising from the provision of health care services frequently borrow against them or sell them in financing transactions, the new category of health care insurance receivables (Rev. UCC § 9-102(a)(46)) is brought within the scope of Revised Article 9. These
receivables are a subset of accounts. This means that in health care financing transactions, Article 9 will cover both noninsurance receivables (such as Medicare/Medicaid entitlements) and private insurance receivables, facilitating their handling as a collateral package.

C. Commercial Tort Claims

Current law excludes all tort claims from the scope of Article 9. Rev. UCC § 9-109(d)(12) brings the assignment of commercial tort claims within the scope of Article 9 for the first time. This opens up an important new source of collateral for borrowers and lenders alike. The term is defined in Rev. UCC § 9-102(a)(13) to mean all claims arising from commission of a business tort. However, no security interest may be taken in after-acquired commercial tort claims. Rev. UCC § 9-204(b)(2). Article 9 will continue to exclude security interests in tort claims for bodily injury and other nonbusiness tort claims of natural persons; any assignments of such claims will be subject to common law rules. All tort claims, when reduced to a structured settlement form, come back into Article 9 as payment intangibles. Rev. UCC § 9-109, Official Comment 15.

D. Agricultural Liens

Current Article 9 covers only consensual security interests and not statutory liens. Early drafts of the revision would have brought all statutory liens covering personal property within the scope of Article 9. The drafters backed away from this radical position, but the revision still makes a major change by bringing within its scope nonpossessory statutory agricultural liens, including landlord’s liens. Rev. UCC §§ 9-102(a)(5), 9-109(a)(2). In general, perfection of agricultural statutory liens is accomplished by UCC filing (Rev. UCC § 9-310(a)), and priority rules applicable to security interests apply to statutory agricultural liens (Rev. UCC § 9-322(a)), unless the statute expressly gives priority to the agricultural lien (Rev. UCC § 9-322(g)). Law outside of Article 9 will govern the creation and attachment of agricultural liens. An
agricultural lien is not a security interest, so Article 9 applies only to the extent it expressly refers to agricultural liens. These new rules will have a major impact on agricultural states.

In addition, Appendix II to Revised Article 9 contains model definitions and priority rules relating to production-money security interests held by secured parties that give new value used in the production of crops. These provisions give the production-money lender superpriority akin to a PMSI. They would greatly strengthen the priority position of crop production lenders under current UCC § 9-312(2). Because no consensus emerged on these priority rules during the drafting process, Appendix II is optional to each state.

E. Deposit Accounts

Except in a few states (California, Illinois, Louisiana, Hawaii, and Idaho), current Article 9 covers security interests in deposit accounts only as proceeds of other collateral, such as accounts receivable. The revision covers deposit accounts (broadly defined in Rev. UCC § 9-102(a)(29) to include unrestricted transaction accounts) as original collateral, except in consumer transactions. Rev. UCC § 9-109(d)(13). In many cases, this will eliminate the necessity of tracing proceeds into a deposit account. A secured creditor may perfect in a deposit account only by control. Rev. UCC § 9-104.

Revised Article 9 contains several additional new rules governing deposit accounts, including: which state’s law governs perfection and priority (Rev. UCC § 9-304); priority of conflicting security interests and setoff rights against a deposit account (Rev. UCC §§ 9-327, 9-340); rights of transferees of funds from an encumbered deposit account (Rev. UCC § 9-332); the obligations of the depository bank (Rev. UCC § 9-341); enforcement of security interests in a deposit account (Rev. UCC § 9-607(c)); and the duty of a secured party to terminate control of a deposit account (Rev. UCC § 9-208(b)).
F. Consignments

Coverage of consignment transactions by Article 9 has generated a fair amount of litigation over the years. In the name of clarity, the revision brings all consignment transactions (i.e., bailments for the purpose of resale by the bailee, whether called a sale or return or a true consignment) within its scope. Rev. UCC § 9-109(a)(4). The term "consignment" is defined in Rev. UCC § 9-102(a)(20) to mean a transaction, regardless of its form, in which a person delivers goods to a merchant for the purpose of sale. The merchant must deal in goods of that kind under a name other than that of the person making delivery, must not be an auctioneer, and the aggregate value of the goods for each delivery must be $1,000 or more. The revision wisely excludes consumer transactions from Article 9 on the theory that almost no consumer consignor would be aware of the need to file a financing statement.

Current UCC § 2-326 is amended to eliminate its coverage of consignment arrangements, since all such transactions are now within the scope of Article 9. However, the term "consignment" is defined in Rev. UCC § 9-102(a)(20) to exclude transactions where the merchant/consignee is generally known by its creditors to be substantially engaged in selling the goods of others, thereby eliminating the need for the consignor to file a financing statement in these situations. This exclusion has the effect of resurrecting former UCC § 2-326, which has generated an unfortunate amount of fact-specific litigation regarding whether a particular consignee is "generally known by its creditors" to be engaged in the business of selling the goods of others.

Rev. UCC § 9-102, Comment 14, makes this important point:

The definition of 'consignment' requires that the goods be delivered "to a merchant for purposes of sale." If the goods are delivered for another purpose as well, such as milling or processing, the transaction is a consignment nonetheless because a purpose of the delivery is "sale." On the other
hand, if a merchant-processor-bailee will not be selling the goods itself but will be delivering to buyers to which the owner-bailor agreed to sell the goods, the transaction would not be a consignment.

Most important, Revised Article 9 treats all consignments as purchase-money security interests in inventory, requiring the consignor to jump through a tough series of hoops in order to gain priority over financers of the consignee’s inventory or the consignee’s trustee in bankruptcy. Rev. UCC § 9-103(d). This requirement is comparable to former UCC § 9-114.

II. PERFECTION OF SECURITY INTERESTS

Perfection of security interests under Revised Article 9 is accomplished in four ways, depending upon the type of collateral: (1) automatically; (2) by possession; (3) by control; and (4) by filing. The revision makes some changes in all methods, but its most important contribution is extensive use of the concept of control.

A. Choice of Law

The threshold issue regarding perfection of security interests is choice of law. In most cases, this means figuring out in which state to file a financing statement. The rules under current Article 9 are found in UCC § 9-103. The more elaborate rules under the revision are found at Rev. UCC §§ 9-301-9-307. The revision does not address choice of law for purposes other than perfection and priority. Issues such as attachment and enforcement of security interests are expected to be handled by a choice-of-law provision in the security agreement, as allowed under UCC § 1-105. Moreover, for most purposes the law under Article 9 is fairly uniform, minimizing the significance of differences from one jurisdiction to another.

Under Rev. UCC § 9-301(1), the baseline rule is that the law governing perfection of security interests, in both tangible
and intangible collateral, whether perfected by filing or automatically, is the law of the jurisdiction of the debtor's location, as determined by Rev. UCC § 9-307. This means that, with respect to tangible collateral such as equipment and inventory, a financing statement will no longer be filed at the situs of the collateral. This is a major change in the law. The debtor's location is determined as follows under Rev. UCC § 9-307:

- A debtor who is an individual is located at the individual's principal residence.

- A debtor that is an organization and has only one place of business is located at its place of business.

- A debtor that is an organization and has more than one place of business is located at its chief executive office. Although the term "chief executive office" is not defined, Comment 2 to Rev. UCC § 9-307 states that it means "the place from which the debtor manages the main part of its business operations or other affairs. This is the place where persons dealing with the debtor would normally look for credit information, and is the appropriate place for filing."

The debtor location standard has great benefits for debtors and secured creditors alike, as discussed in Comment 4 to Rev. UCC § 9-307. It greatly simplifies the choice-of-law rules for different types of collateral. The law of a single jurisdiction governs perfection with respect to both tangible and intangible collateral, facilitating package treatment in loan documentation. Under current law, different filing rules apply depending on whether the collateral is tangible or intangible. There is no more need for the special rule under current law (UCC § 9-103(1)(c)) concerning PMSIs in tangible collateral that is intended to move from one jurisdiction to another. The new rules will reduce the frequency
of cases in which the governing law changes when collateral is moved across state lines, since moving tangible collateral occurs much more frequently than changing the debtor's location. The new rules also eliminate the need to distinguish between mobile goods and ordinary goods, an issue that has generated a fair amount of litigation under current law.

These baseline debtor location rules only apply if the relevant jurisdiction has a filing office. If it does not, the debtor is deemed located in the District of Columbia. For example, a non-U.S. debtor located in a foreign country that has no filing system for security interests in personal property would require a filing in Washington, D.C. See Rev. UCC § 9-307, Comment 3, with examples.

Of great importance, Rev. UCC § 9-307(c) provides that a registered organization organized under the laws of State X is deemed located in that state. The term “registered organization,” defined in Rev. UCC § 9-102(a)(70), includes corporations, limited partnerships, and limited-liability companies. This means that, for a corporate debtor, the place to file a financing statement covering both tangible and intangible collateral would be the state of the debtor's incorporation. This “birth certificate” standard is a major change from current law. Even though it may seem that Delaware will be inundated with UCC filings under the revision, the fact is that most companies that engage in Article 9 secured lending are incorporated elsewhere. Comment 4 to Rev. UCC § 9-307 discusses the benefits of the new registered organization rule:

Determining the registered organization-debtor's location by reference to the jurisdiction of organization could provide some important side benefits for the filing systems. A jurisdiction could structure its filing system so that it would be impossible to make a mistake in a registered organization-debtor's name on a financing statement. For example, a filer would be informed if a filed record designated an incorrect corporate name for the debtor. Linking filing to the jurisdiction of organization also could re-
duce pressure on the system imposed by transactions in which registered organizations cease to exist—as a consequence of merger or consolidation, for example. The jurisdiction of organization might prohibit such transactions unless steps were taken to ensure that existing filings were refiled against a successor or terminated by the secured party.

The baseline debtor location rule is subject to various exceptions:

- It does not apply to possessory security interests, where the governing law is that of the state where the collateral is physically located. Rev. UCC § 9-307(2).

- While negotiable documents, goods, instruments, money, or tangible chattel paper is located in a jurisdiction, the law of that jurisdiction governs: (1) perfection of a security interest in goods by filing a fixture filing; (2) perfection of a security interest in timber to be cut; and (3) the effect of perfection and priority of a nonpossessory security interest in the collateral. Rev. UCC § 9-307(3).

- For as-extracted collateral such as oil and gas, the law of the jurisdiction in which the wellhead or minehead is located governs perfection and priority. Rev. UCC § 9-307(4).

- The baseline rule does not apply to goods covered by an agricultural lien, where the governing law is that of the jurisdiction where the farm products are located. Rev. UCC § 9-302.

- The baseline rule does not apply to vehicles covered by a certificate of title, where the gov-
erning law is the jurisdiction that issued the certificate. Rev. UCC § 9-303. Rev. UCC § 9-303(a) makes it clear that the rule applies to certificates of title issued by a state having no other contacts with the vehicles or the debtor; this result is consistent with titling practices in the trucking industry. However, if the vehicles are held for sale or lease as inventory, or under lease, the normal filing rules apply. Rev. UCC § 9-311(d). This rule has been a trap for unwary inventory lenders under current law, and will continue to be so under the revision. Comment 6 to Rev. UCC § 9-307 discusses problems faced in coordinating Article 9 with the variety of certificate of title statutes, and in determining priorities where multiple certificates have been issued.

- It does not apply to security interests in deposit accounts, where the governing law is that of the jurisdiction where the depository bank is located. Rev. UCC § 9-304.

- It does not apply to security interests in investment property, where the governing law depends on the nature of the interest. For certificated securities, the governing law is that of the jurisdiction in which the certificate is located. For uncertificated securities, the governing law is that of the issuer’s jurisdiction. For security entitlements, securities accounts, commodity contracts, and commodity accounts, the governing law is that of the intermediary’s jurisdiction. Rev. UCC § 9-305.

- It does not apply to security interests in letters of credit, where the governing law is that of the issuer’s or nominated party’s jurisdiction. Rev.
B. Automatic Perfection

The revision carries forward many of the rules of current law allowing automatic perfection. Such security interests are perfected when they attach. Some new rules expand the situations where a security interest is automatically perfected. Situations providing for automatic attachment under the revision are as follows:

As under current law, a purchase-money security interest in consumer goods is automatically perfected. However, titled motor vehicles require the secured party’s lien on the title. Rev. UCC § 9-309(1). Moreover, filing is required to perfect a non-PMSI in consumer goods, and failure to file for a PMSI in consumer goods exposes the secured party to priming by a consumer BFP under Rev. UCC § 9-320(b). Finally, a fixture filing is required for priority over conflicting interests in fixtures under Rev. UCC § 9-334.

Perfection of a security interest in collateral automatically perfects a security interest in a supporting obligation for the collateral such as a letter of credit or guaranty. Rev. UCC § 9-308(d). This is a new rule. Here is the example given in Comment 5:

Example: Buyer is obligated to pay Debtor for goods sold. Buyer’s president guarantees the obligation. Debtor creates a security interest in the right to payment (account) in favor of Lender. Under Section 9-203(f), the security interest attaches to Debtor’s rights under the guarantee (supporting obligation). Under subsection (d), perfection of the security interest in the account constitutes perfection of the security interest in Debtor’s rights under the guarantee.

In a closely related new rule, perfection of a security interest in a right to payment or performance also perfects a security interest in a security interest, mortgage, or other lien on personal or real property securing the right. Rev. UCC § 9-308(e), Comment 6, gives this example:

Example: Owner gives to Mortgagee a mortgage on Black-acre to secure a loan. Owner’s obligation to pay is evidenced by a
promissory note. In need of working capital, Mortgagee borrows from Financer and creates a security interest in the note in favor of Financer. Section 9-203(g) adopts the traditional view that the mortgage follows the note; i.e., the transferee of the note acquires the mortgage, as well. This subsection adopts a similar principle: perfection of a security interest in the right to payment constitutes perfection of a security interest in the mortgage securing it.

Perfection of a security interest in a securities account also perfects a security interest in the securities entitlements carried in the account. Rev. UCC § 9-308(f). This is a new rule.

In another new rule, perfection of a security interest in a commodities account also perfects a security interest in the commodity contracts carried in the account. Rev. UCC § 9-308(g).

As under current law, perfection is automatic for an assignment of accounts or payment intangibles that does not by itself or in conjunction with other assignments to the same assignee transfer a significant part of the assignor's outstanding accounts or payment intangibles. Rev. UCC § 9-309(2).

Perfection is automatic for the outright sale of a payment intangible or promissory note. Rev. UCC §§ 9-309(3), (4). This would include bank loan participations. These are new rules.

In another new rule, perfection is automatic for a security interest created by the assignment of a health care insurance receivable to the provider of the health care goods or services. Rev. UCC § 9-309(5). When an individual assigns a right to payment under an insurance policy to the provider, the provider has no need to file a financing statement against the individual. However, the normal filing rules apply to other assignments of health care insurance receivables, that is, assignments from the provider to a financer.

Perfection is automatic for security interests created for policy reasons in other parts of the UCC, including aggrieved buyers of defective goods (UCC § 2-711(3)), liens in favor of collecting banks (UCC § 4-210), and the security interest of an issuer or nominated party in a letter of credit (UCC § 5-118). Rev. UCC §§ 9-309(6), (7), (8).

In other new rules, perfection is automatic for a security interest arising in the delivery of a financial asset and a security
interest in investment property created by a securities or commodities intermediary. Rev. UCC §§ 9-309(9), (10), (11). For an elaboration of these new rules, see Comment 6.

In line with current law, perfection is automatic for a security interest created by an assignment for the benefit of creditors. Rev. UCC § 9-309(12).

As under current law, perfection is automatic for a security interest created by an assignment of a beneficial interest in a decedent’s estate. Rev. UCC § 9-309(13). However, the revision changes current law in requiring filing, for the first time, for a collateral assignment of a beneficial interest in a trust. This new filing requirement reflects the fact that beneficial interests in trusts are now used as collateral with increasing frequency in commercial transactions. See Comment 7.

C. Perfection by Possession

As under current law, possession is a permissible method of perfection for negotiable documents of title, goods, instruments, or tangible chattel paper and certificated securities. Rev. UCC § 9-313(a). It is the exclusive method of perfecting a security interest in money. In a departure, the revision provides for possession as a way of perfecting a security interest in a titled motor vehicle, but only in limited circumstances. Rev. UCC §§ 9-313(b), 9-316(d). See also Rev. UCC § 9-316, Comment 5, with examples. Consistent with current law, the term "possession" is not defined in the statute. However, Comment 3 to Rev. UCC § 9-313 tells us that principles of agency apply. If the collateral is clearly in possession of the secured party’s agent, and if the agent is not also an agent of the debtor, the secured party has possession without the need to rely on the acknowledgment of a third-party bailee. The debtor cannot qualify as the secured party’s agent, nor can a person under the debtor’s control. “In a typical escrow arrangement, where the escrowee holds possession of collateral as agent for both the secured party and the debtor, the debtor’s relationship to the escrowee is not such as to constitute retention of possession by the debtor.”

In one of its most important reforms, the revision changes
current law by allowing a security interest in an instrument to be perfected by either possession or filing. Rev. UCC §§ 9-312(a), 9-313(a). As Comment 2 to Rev. UCC § 9-312 states: "The rule is likely to be particularly useful in transactions involving a large number of notes that a debtor uses as collateral but continues to collect from the makers." However, a security interest perfected by possession will have greater protection against the claims of a holder in due course or competing secured creditor who has perfected by filing. Rev. UCC § 9-330(d). In addition, filing does not constitute notice that would preclude a later purchaser from becoming a holder in due course who takes free of all claims and defenses. Rev. UCC § 9-331. In most cases, possession will be the method of choice for instruments, though filing will protect the secured creditor from the debtor’s trustee in bankruptcy.

In some cases, possession will also bring control. For example, a secured party with both possession and a proper indorsement of certificated securities will also have control, which will provide greater priority against competing secured creditors than perfection by possession alone.

The law of the state of the physical location of the collateral governs perfection of a security interest in collateral perfected by possession. Rev. UCC § 9-301(2).

One major change made by the revision is elimination of the "bailee with notice" mechanism. Under current law, a secured party may simply notify a third party of its interest in a promissory note or certificated security held by the third party as pledgee, and its security interest is perfected from the moment the third party receives notice. UCC § 9-305. The revision (Rev. UCC § 9-313(c)(1)) provides that a security interest in collateral in possession of a third party is perfected only when the third party acknowledges in an authenticated record that it holds for the secured party’s benefit. The third party is not required to make such an acknowledgment. That is the bad news for the secured party. The good news is that a security interest in an instrument or certificated security can be perfected by filing, though filing will not protect against subsequent delivery of the collateral to a third party. Under the revision, a lessee of collateral in the ordinary course of the debtor’s business will not qualify as a third
party in possession of the collateral by giving an acknowledgment. This rule rejects cases like *In re Atlantic Systems, Inc.*, holding that notification to debtor-lessee's lessee was sufficient to perfect a security interest in the leased goods.

In an accommodation to real estate mortgage warehouse lending, a secured party need not obtain an acknowledgment from a bailee where the secured party delivers the collateral to a bailee if the secured party instructed the bailee before or at the time of delivery to hold possession of the collateral for the secured party's benefit or to redeliver it. Rev. UCC § 9-313(h). The policy behind this rule is stated in Comment 9:

> [Warehouse lenders] typically send mortgage notes to prospective purchasers under cover of letters advising the prospective purchasers that the lenders hold security interests in the notes. These lenders relied on notification to maintain perfection under former 9-305. Requiring them to obtain authenticated acknowledgments from each prospective purchaser...could be unduly burdensome and disruptive of established practices.

As under current Article 9, Rev. UCC § 9-207 sets forth the rights and duties of a secured party in possession of collateral. The baseline rule is that the secured party use "reasonable care in the custody and preservation of collateral in the secured party's possession. In the case of chattel paper or an instrument, reasonable care includes taking necessary steps to preserve rights against prior parties unless otherwise agreed." As Comment 2 points out, in many cases a secured party in possession of collateral may satisfy this duty by notifying the debtor of action that should be taken and allowing the debtor to take the action itself. The duty to exercise reasonable care cannot be disclaimed by agreement, though the parties remain free to determine by

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agreement standards that are not “manifestly unreasonable” what constitutes reasonable care. This is an area where limited freedom of contract can be quite useful.

Reasonable expenses incurred in the custody, preservation, or operation of the collateral are chargeable to the debtor—including insurance and taxes. The risk of accidental loss is on the debtor to the extent of a deficiency in any effective insurance coverage. The secured party must keep the collateral identifiable, but fungible collateral may be commingled. Finally, the secured party may operate the collateral in limited situations. The secured party may hold as additional collateral any proceeds received from the collateral (except money, which must be applied to the debt or remitted to the debtor).

Of significance, Rev. UCC § 9-207(c)(3) provides that the secured party “may create a security interest in the collateral.” This is the repledge, a transaction that is discussed in detail in Comments 5 and 6. These comments make it clear that a repledge of collateral may not impair the debtor’s right of redemption. One example given in comment 5 is a negotiable note payable to the debtor that Secured Party #1 repledges to Secured Party #2. The debtor retains the right to redeem the note upon payment to Secured Party #1 of all obligations secured by the note. However, the debtor’s unimpaired right to redeem as against Secured Party #1 may not be enforceable as against Secured Party #2. Finally, Rev. UCC § 9-207(d) provides that the general duty of care applies only to true security interests and not to nonrecourse sales of receivables where the seller retains no interest in the collateral and so is not disadvantaged by the secured party’s noncompliance with the requirements of the section.

D. Perfection by Control

With respect to various types of collateral, perfection is accomplished by control over the collateral. The concept of control, which was introduced into Article 9 with the revision of Article 8 governing investment property, has now been expanded to cover deposit accounts (Rev. UCC § 9-104), electronic chattel paper (Rev. UCC § 9-105), investment property (Rev. UCC § 9-106),
and letter-of-credit rights (Rev. UCC § 9-107).

The only way to perfect a security interest in deposit accounts taken as original collateral is by control. Control occurs automatically when the relevant depository institution is the secured party. For third parties, it occurs when: (1) the depository institution (with the consent of the debtor) has agreed that it will follow directions from the secured party without further consent by the debtor; or (2) the secured party becomes the customer by putting the account in its own name. The secured party has control over the deposit account even though the debtor retains the right to access the account. Rev. UCC § 9-104(b).

Control of electronic chattel paper occurs when there is a special electronic identification of the secured party on the electronic copy of the chattel paper. Rev. UCC § 9-105. Unlike deposit accounts, control and filing are alternative methods of perfecting a security interest in electronic chattel paper. Rev. UCC §§ 9-312(a), 9-314(a). Because electronic chattel paper cannot be transferred, assigned, or possessed in the same manner as tangible chattel paper, Rev. UCC § 9-105 defines “control” in a special manner, as the functional equivalent of possession of tangible chattel paper. Comment 3 states:

One requirement for establishing control is that a particular copy be an “authoritative copy.” Although other copies may exist, they must be distinguished from the authoritative copy. This may be achieved, for example, through the methods of authentication that are used or by business practices involving the marking of any additional copies. When tangible chattel paper is converted to electronic chattel paper, in order to establish that a copy of the electronic chattel paper is the authoritative copy it may be necessary to show that the tangible chattel paper is the authoritative copy or it may be necessary to show that the tangible chattel paper no longer exists or has been permanently marked to indicate that it is not the authoritative copy.

Comment 4 goes on to discuss marketplace development of alternative control systems. Filing is another way to perfect on chattel paper, including electronic chattel paper. Rev. UCC § 9-312(a).

The only way to perfect a security interest in letter-of-credit
right is by control. Control over letter-of-credit rights occurs when the issuer (or a nominated person such as a confirming bank) consents to an assignment of proceeds. Rev. UCC § 9-107. By contrast, under current law a security interest in a beneficiary’s right to proceeds from a letter of credit can be perfected only by taking possession of the letter. UCC § 9-304(1). The revision properly shifts away from physical possession of the letter to control over disposition of the proceeds, a method that is more in tune with modern commercial practice. A security interest in letter-of-credit rights can also be perfected automatically by perfecting a security interest in a supported obligation. However, perfecting this way—without control—could make it difficult for the secured party to enforce its claim to the proceeds of the letter. The drafters draw a careful distinction between a beneficiary’s assignment of the proceeds of a letter of credit as collateral for a loan and transfer of the letter itself, by which the transferee becomes the beneficiary and acquires the right to draw. UCC § 5-114(e) provides that the rights of a transferee beneficiary or nominated person are independent of the beneficiary’s assignment of the proceeds of a letter of credit and are superior to the assignee’s right to the proceeds. For this reason, transfer does not appear in Article 9 as a means of control or perfection.

Control over investment property exists when a securities intermediary (with the consent of the debtor) has agreed with the secured party that it will follow directions from the secured party without further consent from the debtor. Rev. UCC §§ 9-106, 8-106. Comment 7 to UCC § 8-106 clarifies that a secured party’s conditional right to instruct the financial intermediary does not preclude control so long as satisfaction of the condition does not require the debtor’s consent. This would allow the debtor to continue directing investments in a securities account without danger to continued perfection of the security interest. With respect to certificated securities, possession plus a proper indorsement yields control. Rev. UCC § 9-314 ensures that a secured party retains control in repledge transactions that are typical in the securities markets. Filing is an alternative way to perfect on investment property, though it is not nearly as safe as control. Rev. UCC § 9-312(a).
Rev. UCC § 9-208 imposes on a secured party with control over a deposit account, investment property, or a letter-of-credit right the duty to relinquish control when there is no secured obligation and no commitment to give value. For deposit accounts, the secured party must send to the depository bank an authenticated statement that releases the bank from any further obligation to comply with instructions from the secured party. For investment property, the secured party must send to the securities intermediary or commodity intermediary an authenticated record that releases the intermediary from any further obligation to comply with entitlement orders originated by the secured party. For letter-of-credit rights, the secured party must send to each person with a duty to pay or deliver proceeds to the secured party an authenticated release from any further obligation.

E. Perfection by Filing

Filing will remain the most important method of perfection. One of the major contributions made by the revision is to reform and modernize the UCC filing system. Following are its most important contributions in this respect.

1. Location of Filings

In sharp contrast to current law, all filings governed by the revision are to be made in the jurisdiction where the debtor is located. This crucial choice-of-law provision, found at Rev. UCC § 9-301(1), replaces the current rule under which the secured party must file in the state where tangible collateral is physically located. Under current law, the debtor's location only controls where the collateral is intangible (such as accounts and general intangibles) or mobile goods. UCC § 9-103. The new rule should reduce transaction costs and legal risk by enabling the secured party to package all types of collateral into a single filing—in the state where the debtor is located.

But where is the debtor located? Rev. UCC § 9-307, following current law, provides that the debtor's location is its place of business (or chief executive office, if the debtor has more than
one place of business). However, there are two important exceptions to the general rule:

A registered organization that is organized under the laws of a state is located in that state. Rev. UCC § 9-307(e). For a corporation, limited partnership, or limited liability company, the place to file is the entity's "birthplace"—that is, its state of incorporation. Although it might appear that this new rule will flood the Delaware UCC filing office, most corporations are registered elsewhere. The birthplace test should be more certain than the current chief executive office standard. If the debtor reincorporates in another state, perfection will lapse after four months. Rev. UCC § 9-307(g) keeps the location intact in spite of suspension of the company's status or its dissolution.

A foreign debtor that would otherwise be located in a foreign jurisdiction without a public filing system is deemed to be located in Washington, D.C. Rev. UCC § 9-307(c). (The current rule under UCC § 9-103 allowing perfection by notification to account debtors is ineffective because it allows secret liens.) This new rule would allow a domestic filing for a non-U.S. debtor by choice-of-law provision. The same is generally true of entities organized under federal law. Rev. UCC § 9-307(f).

An individual debtor is located at his or her principal residence.

Under Rev. UCC § 9-501, all filings are to be central, except: (1) fixture filings; (2) filings covering as-extracted minerals (e.g., oil and gas); or (3) timber to be cut. An alternative way to perfect a security interest in fixtures is to do a central filing, though failure to make a local fixture filing means that the secured party cannot claim purchase-money priority in the fixtures under Rev. UCC § 9-334. However, if fixtures belong to a transmitting utility, filing is central, with the secretary of state; the definition of the term "transmitting utility," found at Rev. UCC § 9-102(a)(80), is somewhat broader than under current law. The theory behind a single, central filing for transmitting utilities is that the "nature of the debtor will inform persons searching the record as to where to make a search." Rev. UCC § 9-501, Comment 5.

Minerals and timber are treated somewhat differently, as
discussed in Comment 3. A filing in the office where a real estate mortgage would be recorded perfects a security interest in as-extracted collateral such as oil and gas. Inasmuch as the security interest does not attach until extraction, the filing continues to be effective after extraction. Timber to be cut, however, may be goods before it is cut; once cut, the filing in the real estate office ceases to be effective. At that point, the timber is subject to the central filing rules governing inventory. Also, once timber is cut, the state of filing is the state of the debtor’s location, not where the timber is located.

Current Article 9 gives states three alternatives for filing; those alternatives are eliminated in the revision. This should reduce the net costs of secured transactions by decreasing the number and uncertainty of required filings. It remains to be seen whether local filing officers will resist this move toward centralization with the secretary of state. In any case, the policy rationale behind more centralized filing is well stated in Comment 2:

The principal advantage of state-wide filing is ease of access to credit information which the files exist to provide. Consider for example the national distributor who wishes to have current information about the credit standing of the thousands of persons he sells to on credit. The more completely the files are centralized on a state-wise basis, the easier and cheaper it becomes to procure credit information; the more the files are scattered in local filing units, the more burdensome and costly.

2. Contents of the Financing Statement—Generally

Under Rev. UCC § 9-502, a financing statement is sufficient only if it:

- Provides the name of the debtor
- Provides the name of the secured party
- Indicates the covered collateral
- A realty-related financing statement (for fix-
tures, as-extracted collateral, and timber to be grown) must also:

- Indicate that it covers this type of collateral
- Indicate that it is to be filed in the realty records
- Provide a description of the realty to enable cross-indexing
- Provide the name of a record owner if the debtor does not have an interest of record

- A real estate mortgage is effective as a UCC financing statement covering the three types of realty-related collateral, but only if the mortgage:
  - Indicates the goods or accounts it covers
  - Satisfies the requirements for a financing statement
  - Is duly recorded

Like its predecessor, Revised Article 9 adopts a simplified notice filing system under which the financing statement contains only skeletal information. If searchers want more detail, Rev. UCC § 9-210 provides a procedure under which the secured party, at the debtor’s request, may be required to make further disclosures. For real estate-related collateral, the description of the realty need not be metes and bounds; the proper test is that a real estate description “must be sufficient so that the financing statement will fit into the real-property search system and be found by a real-property searcher.” Rev. UCC § 9-502, Comment 5. For a mortgage that operates as a fixture filing, Rev. UCC § 9-
515(g) makes the usual five-year duration of the financing statement inapplicable; instead, the UCC filing is effective for the duration of the real-property recording.

One tricky aspect of the revision rules is that, though Rev. UCC § 9-502 does not indicate that the debtor's address is required on the financing statement as a condition of perfection, the filing officer is required to reject a financing statement without the debtor's address. Rev. UCC §§ 9-516(b), 9-520(a). Not surprisingly, the model form includes it. Rev. UCC § 9-521.

In Rev. UCC § 9-505, the revision broadens the concept under current law of a precautionary filing for leases, licenses, outright sales, and other nonsecured transactions. Such a filing is not itself a factor in determining whether the collateral secures an obligation.

3. Contents of the Financing Statement:
   Name of the Debtor

Under the revision, the financing statement must reflect the exact registered name of the debtor if there is one. Rev. UCC § 9-503(a). An incorrect name is seriously misleading if a standard search does not find it. Rev. UCC § 9-506. The drafters thought about providing a specific list of acceptable mistakes (e.g., "Corp." instead of "Corporation") but ended keeping the "seriously misleading" standard. These new rules seek to overturn the maverick line of recent cases holding that a trade name is acceptable even though the security interest would not be discovered by a searcher using the debtor's precise "legal" name. Compare In re Mines Tire Co. with ITT Commercial Finance Corp. v. Bank of the West. The revision also adds some helpful standards for naming debtors that are decedents' estates or trusts. Rev. UCC § 9-503. The revision rejects the nonuniform rule in a handful of states that requires the tax identification number of

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5. ITT Commercial Finance Corp. v. Bank of the West, 166 F3d 295 (5th Cir. 1999), 37 UCC Rep. 2d 855 (result inconsistent with revision).
4. Contents of the Financing Statement: Name of the Secured Party

A financing statement may name a representative of the secured party without indicating the representative capacity. Rev. UCC §§ 9-502(a)(2), 9-503(d). This rule, which should make it easier to perfect in multiparty or syndicated credit transactions, rejects the implicit holding of some decisions that the financing statement must indicate the representative capacity of the secured creditor whose name appears. See Chemical Bank v. Security Pac. Nat'l Bank. Each secured party of record may file amendments with respect to its own interest. Rev. UCC §§ 9-509(c), (d). Comment 3 to Rev. UCC § 9-503 gives a good example of the representative capacity problem:

Example: Debtor creates a security interest in favor of Bank X, Bank Y, and Bank Z, but not to their representative, the collateral agent (Bank A). The collateral agent is not itself a secured party. See Section 9-102. Under Sections 9-502(a) and 9-503(d), however, a financing statement is effective if it names as secured party Bank A and not the actual secured parties, even if it omits Bank A's representative capacity.

5. Contents of the Financing Statement: Supergeneric Collateral Descriptions

Under Rev. UCC § 9-504(2), a supergeneric description of collateral such as "all assets of the debtor, now owned or hereafter acquired" is a sufficient description of the collateral in the financing statement. This changes current law. However, a supergeneric description is not allowed in the security agreement. On a related point, Rev. UCC § 9-502, Comment 2, makes it clear that the collateral description in the financing statement need not include a reference to after-acquired property, even if the collat-

eral is of a type that does not normally turn over—equipment, for example. This liberal treatment of collateral descriptions reflects the code’s notice filing philosophy and is reinforced by use of the concept of simply indicating the collateral in the financing statement.

6. Contents of the Financing Statement:
   Crop Descriptions

Under current law, the collateral description of growing crops in both the security agreement and the financing statement must include a description of the real estate on which the crops are growing or to be grown. This requirement has generated much litigation, including problems relating to leased acreage and harvested crops. See, for example, Farmers Co-op of Ashford, Inc. v. People’s Community Bank of Ashford. Since third parties do not normally search the records on the basis of any real estate description, the requirement makes no commercial sense. Mercifully, the revision eliminates the real estate description requirement for crop loans. Rev. UCC § 9-108.

7. Contents of the Financing Statement:
   The “Minor Error” Rule

Rev. UCC § 9-102(a)(39) defines “financing statement” broadly to include the initial filing and “any filed record relating to the initial financing statement.” This means that continuation statements, amendments, and other subsequent filings are considered to be part and parcel of the original financing statement. It also means that the “minor error” rule of Rev. UCC § 9-506 clearly covers subsequent filings. Under current law, by contrast, the minor error rule arguably applies only to the original financing statement. The cases have gone both ways. Compare Brams Ltd v. Elf Enters., Inc. with In re Kitchin Equip. Co. of Va.

8. Contents of the Financing Statement:
No Debtor Signature

In sharp contrast to current law, the debtor’s signature is not required on a financing statement. Rev. UCC § 9-502. This will facilitate electronic filing. Instead, the revision prohibits the filing of an unauthorized financing statement and imposes liability on those who violate the prohibition. As a practical matter, the secured party will get the debtor’s express authorization for filing in the security agreement. In fact, the authentication of a security agreement automatically authorizes the filing of a conforming financing statement. This is the concept of ipso facto authorization. See Rev. UCC § 9-509(b), Comment 4, with Examples. Although debtor authorization is required for financing statements, it is not required to perfect for agricultural liens; because such liens arise as a matter of law, the debtor’s consent is not required. Rev. UCC § 9-509(a)(2).

9. Medium Neutrality

The elimination of any requirement that the debtor sign the financing statement is consistent with the revision’s embrace of medium neutrality, by which the parties may file and otherwise communicate with a filing office by means of records communicated and stored in media other than paper. The ubiquitous phrase “authenticate a record” reflects this medium neutrality. It permits the use of “signatures” that are not hand written on paper and facilitates electronic agreements, such as electronic chattel paper. In a similar vein, the revision does not care who makes a filing. Instead, it focuses on whose authorization is necessary for a person to file a record with a filing office. This is consistent with elimination from the filing system of signatures or other evidence of authorization, except to the extent that filing offices may

9. In re Kitchin Equip. Co. of Va., 960 F2d 1242, 17 UCC Rep. 2d 322 (4th Cir. 1992) (financing statement termination box checked by mistake instead of partial release; court treats filing as termination even though mistake was obvious from face of filing).
choose to employ authentication procedures in connection with electronic communications. As long as the appropriate person authorizes the filing or the debtor is entitled to the termination, it does not matter who files any given record. Under Rev. UCC § 9-509, the debtor's authorization is required for the filing of the initial financing statement or an amendment that adds collateral. The secured party's authorization is required for other amendments. If the secured party has failed to terminate, the debtor is authorized to do so.

10. Postfiling Changes

As under current law, Rev. UCC § 9-507(a) provides that a filed financing statement remains effective with respect to collateral that is transferred to a third party, unless the secured party consents to the transfer free of the lien. There is no duty to refile under the name of the transferee, creating the risk of secret liens. The third-party searcher must inquire as to the debtor's source of title. However, under a new rule found in Rev. UCC § 9-316(a)(3), the original filing expires after one year if the transferee is located in another jurisdiction. See Rev. UCC § 9-507, Comment 3, Example. If the debtor's name changes in a seriously misleading way, the secured party has four months to file an amendment to reflect the name change. Rev. UCC § 9-507(c). If an amendment is not filed within the four-month grace period, the security interest becomes unperfected as to all collateral acquired by the debtor more than four months after the change. As under current law, failure to meet the four-month deadline would not cause a loss in perfection with respect to collateral that was owned by the debtor under its original name.

The revision makes a security agreement effective against a person who becomes bound by the secured obligation under principles of successor liability. Rev. UCC § 9-203(d). This could happen by contract or by operation of law. As an extension of this rule, an old financing statement is effective to perfect a security interest as against a new debtor who becomes bound by a predecessor's security agreement, assuming that the information in the financing statement is not seriously misleading. Rev. UCC
§ 9-508. If the financing statement is seriously misleading, perfe-
tion lapses with respect to collateral acquired by the new debtor
more than four months after the new debtor becomes bound on
the security agreement, unless the secured party files a new ini-
tial financing statement (not an amendment) before the expira-
tion of the grace period. This new rule, which is parallel to that
governing a single debtor whose name changes, is intended to
cover situations where the debtor changes its business struc-
ture—as when a sole proprietorship incorporates.

11. Filing Office Operations

The revision includes several provisions dealing with fil-
ing office operations:

It prohibits the filing office from bouncing a filing except
in very limited situations; this rule is designed to relieve the fil-
ing office of any duty to evaluate the substance of a financing
statement. Rev. UCC § § 9-516(b), 9-520(a).

The filing officer is obliged to link all subsequent docu-
ments to the original financing statement to which they relate. Rev. UCC § 9-519.

The filing office may expunge a financing statement and
related records from the files no earlier than one year after lapse
(e.g., lapse occurs five years from the last filing date). Rev. UCC
§ § 9-515, 9-519, 9-522. Thus, a financing statement and related
records would be discovered by a search of the files even after
the filing of a termination statement.

Wrongful refusal by a filing officer to accept a financing
statement does not prevent it from being effective, except that a
subsequent secured party who gives value in reasonable reliance
on the absence of the financing statement will have priority. Rev.
UCC § 9-516(b). This change in the law is based on the idea that
the first filer is in the best position to determine whether the fil-
ing office accepted the filing.

If the filing office accepts a financing statement but does
not index it properly, a subsequent searcher who does not find it
will lose to the first secured party. Rev. UCC § 9-517.

The revision provides for the promulgation of filing office
rules to fill in details left out of the statute. Rev. UCC § 9-526.

12. Bogus Filings and Debtor Terminations

In response to the *posse comitatus* problem in some parts of the country, where wild vigilantes file fraudulent financing statements against public officials and other prominent persons for political reasons, the revision gives the debtor the opportunity to file a correction statement. The filing of the correction statement does not affect the related financing statement; it just provides additional information to persons reviewing the record. Rev. UCC § 9-518. This approach is parallel to rights given to aggrieved debtors under the Fair Credit Reporting Act. In a related rule, a debtor may file an effective termination statement if the secured party has a duty to file and has failed to do so. Rev. UCC §§ 9-509(d)(2).

13. Duration of Filing

The revision retains the baseline five-year filing duration, with continuation statements to be filed within six months of the end of the five-year period. Rev. UCC § 9-515(d). A continuation statement filed outside the six-month window is ineffective and the filing office is obligated to reject it. Rev. UCC § 9-510. However, Rev. UCC § 9-515(b) provides that an initial financing statement filed in connection with a public-finance transaction or a manufactured-home transaction is good for 30 years. These are new provisions reflecting special situations where the shorter five-year duration is not appropriate.

Terminations are governed by Rev. UCC § 9-513. As under current law, no duty is imposed on the secured party to terminate unless demanded by the debtor, except in the case of consumer goods. If the debtor did not authorize the filing of a financing statement in the first place, the secured party of record must file a termination statement or suffer penalties just as surely as it would if filing an unauthorized financing statement. See Rev. UCC § 9-625(e). Once a termination statement is filed, the related financing statement ceases to be effective (Rev. UCC § 9-
513(d)), but it will remain of record until at least one year after it lapses with respect to all secured parties of record. Rev. UCC § 9-519(g).

14. Amendments

Rev. UCC § 9-512 addresses changes to financing statements, including addition and deletion of collateral, assignment, continuation, and termination. These are all called amendments though they raise different concerns. An amendment must identify the initial financing statement by its file number. In general, the filing of an amendment does not extend the period of effectiveness of the financing statement. Secured parties of record may make changes in the public record without the need to obtain the debtor's signature; however, the filing of an amendment that adds collateral or adds a debtor must be authorized by the debtor in order to be effective.

15. Assignments

As under current law, no filing of an assignment is required as a condition of continuing the perfected status of the security interest against creditors and transferees of the original debtor. Rev. UCC § 9-310(c). However, if an assignment is not filed, the assignor remains the secured party of record, with power to authorize the filing of effective amendments. Rev. UCC §§ 9-511(c), 9-509(d). An initial financing statement may reflect an assignment of all the secured party's power to authorize an amendment, by providing the name and address of the assignee. Rev. UCC § 9-514(a). A secured party of record may assign its interest in a financing statement under the guidelines set forth in Rev. UCC § 9-514(b).

16. Effectiveness of Filing

Rev. UCC § 9-516(a) follows current law in providing that the tender of a proper financing statement (or amendment) and filing fee constitutes filing. The drafters have included a new
subsection (b) which lists grounds upon which the filing office may reject a filing, including:

- debtor name

- for an amendment, no identification of the initial financing statement to which the amendment relates;

- no real estate description sufficient for cross-indexing;

- no name or mailing address of the secured party;

- no mailing address for the debtor;

- no indication of whether the debtor is an individual or organization;

- if the debtor is an organization, no indication of the type of organization or the jurisdiction of organization;

- no name and mailing address of an assignee in a situation where an assignment was reflected in the initial financing statement; and

- no filing within the six-month window required for continuation statements. Subsection (d) provides that if the filing officer rejects a filing for a reason other than those set forth in subsection (b), the filing is still effective except as against a BFP of the collateral who relied on the absence of the record.
17. Model Forms

Rev. UCC § 9-521 provides for uniform, national written forms of financing statement and related records that must be accepted by a filing office. (See Figure 5.1, UCC Financing Statement; Figure 5.2, UCC Financing Statement Addendum; Figure 5.3, UCC Financing Statement Amendment; Figure 5.4, UCC Financing Statement Amendment Addendum.) It is hoped that these statutory forms will encourage uniformity and efficiency in the filing system.

F. Continuation of Perfection

As under current law with some changes, a perfected security interest in collateral generally continues notwithstanding sale, lease, license, exchange, or other disposition unless the secured party authorized the disposition free of the security interest. Rev. UCC § 9-315(a)(1). If the secured party authorizes disposition but does not indicate that the transfer is free of the security interest, the presumption is that it is only an authorization of disposition subject to the security interest. This clarifies current law. On the other hand, Comment 2 indicates that the revision leaves to the courts the frequently litigated situation in which the effectiveness of the secured party's consent to a disposition is conditioned upon receipt of the proceeds.

Comment 2 also lists the situations in which a transferee takes free of a perfected security interest even though the disposition was not authorized:

Under Rev. UCC § 9-320, a buyer of inventory or minerals in ordinary course of business takes free.

Under Rev. UCC § 9-321(b), a licensee in ordinary course of a general intangible (such as intellectual property) takes free of a perfected security interest granted by the licensor.

Under Rev. UCC § 9-321(c), a lessee of goods in ordinary course of business takes its leasehold interest free of a security interest in the goods granted by the lessor.

Under Rev. UCC § 9-330, good-faith purchasers of chattel paper and holders of instruments take free of security interests
perfected by filing.

Under Rev. UCC § 9-331, special priority is given to holders in due course of negotiable instruments, holders to which a negotiable document of title has been duly negotiated, and protected purchasers of a security.

Under Rev. UCC § 9-332, most transferees of funds from a deposit account and transferees of money take free of a perfected security interest in the deposit account or money.

Under UCC § 2-403, if the secured party entrusts goods to a merchant who deals in goods of that kind and the merchant sells the collateral to a buyer in ordinary course of business, the buyer takes free of the perfected security interest.

As under current law, a disposition of the collateral by the debtor enables the creditor’s perfected security interest to carry over to identifiable proceeds. Rev. UCC § 9-315(a)(2). Even though they are commingled, proceeds can maintain their identifiability through common law tracing principles such as the lowest intermediate balance rule. Rev. UCC § 9-315(b) and Comment 3. In line with current law, a perfected security interest in proceeds becomes unperfected on the 21st day after disposition of the collateral unless: (1) a filed financing statement covers the original collateral, the proceeds are collateral for which filing is appropriate in that same office, and the proceeds are not acquired with cash proceeds; (2) the proceeds are identifiable cash proceeds; or (3) the security interest in proceeds is perfected within 20 days. Rev. UCC § 9-315(d). The rules governing continuation of a perfected security interest in proceeds are discussed in detail in Comment 5, which contains some good examples.

Continued perfection when the governing law changes is handled in Rev. UCC § 9-316. The most important rule is that the secured party has four months in which to refile if the debtor changes its location from one jurisdiction to another. The situations where this will arise should be many fewer than under current law, where a change in governing law occurs not only when the debtor changes location (for intangible collateral) but when tangible collateral is moved to another jurisdiction. A new one-year grace period for refileing is provided when collateral is trans-
ferred to a person who becomes bound as a debtor and is located in another jurisdiction. See also Rev. UCC § 9-507, Comment 3. This longer grace period is justified on the ground that, even with the exercise of due diligence, the secured party may be unable to discover that the collateral has been transferred to a person located in another jurisdiction. Rev. UCC § 9-316 also contains rules covering: (1) continuous perfection of a possessory security interest in collateral that is brought into another jurisdiction; (2) vehicles covered by certificates of title; and (3) changes in jurisdiction of banks (for security interests in deposit accounts), issuers of letters of credit (for security interests in letter-of-credit rights), and securities or commodity intermediaries (for security interests in investment property).

III. DEFAULT AND ENFORCEMENT

No subject under current Article 9 has generated more litigation than default and enforcement of security interests. Part 6 of Revised Article 9 makes a number of important changes in the law governing debtor default and creditor enforcement of security interests, in both consumer and nonconsumer transactions. In terms of the parties against which enforcement is sought, the revision distinguishes among: (1) debtors; (2) obligors; and (3) secondary obligors. The term “debtor” is defined in Rev. UCC § 9-102(a)(28) as the person who owns the collateral (usually the borrower or credit buyer, but possibly a hypothecator). This is the grantor of the security interest. The term “obligor” is defined in Rev. UCC § 9-102(59) as the person who owes the payment obligation. The term “secondary obligor” is defined in Rev. UCC § 9-102(a)(71) as an obligor who stands as guarantor or other surety with a right of recourse. In most cases, the primary obligor and the debtor are the same person. If the collateral is hypothecated by a third person who is not personally obligated on the debt, the borrower is a primary obligor but not a debtor.

A number of the rules found in Part 6 are intended to protect a party who would be prejudiced by a faulty foreclosure sale. The borrower who is also the grantor of the security interest is in that category because such a borrower has a stake in the proper
enforcement of the security interest. In the same category is a secondary obligor, who has a stake based on liability for any deficiency following foreclosure. On the other hand, if a primary obligor gets a hypothecation of collateral from a third party, the hypothecator would be prejudiced by a faulty foreclosure while the borrower—against whom the hypothecator would presumably have a right of recourse and who would owe the full amount of the debt regardless of how the foreclosure is handled—would have no stake. Obligors who are neither debtors nor secondary obligors have no stake in the foreclosure sale. In general, the rights and duties provided by Part 6 affect nondebtor obligors only if they are secondary obligors. See Rev. UCC § 9-102, Comment 2.

A. Secured Party’s Rights After Default

Rev. UCC § 9-601 sets forth as a general matter the rights of the secured party following the debtor’s default. As with current law, the revision does not define “default,” leaving that critical term to definition by the parties in their security agreement. (For agricultural liens, the time of default is to be determined by the statute creating the lien. Rev. UCC § 9-606.) On the flip side, the statute “does not determine whether a secured party’s post-default conduct can constitute a waiver of default in the face of an agreement stating that such conduct shall not constitute a waiver.” Thus, the courts are free to enforce an antiwaiver clause in a security agreement, or conclude that the secured party’s continued acquiescence in effect waives the antiwaiver clause. In any case, the revision recognizes that it is wise for creditors to insert antiwaiver provisions into security agreements, whether the underlying transaction is commercial or consumer in nature.

Subsection (b) makes it clear that a secured party’s rights and duties with respect to collateral in its possession, as set forth in Rev. UCC § 9-207, apply not only to possession before default but to possession after default. Subsection (c) goes one step beyond current law by providing not only that a secured party’s rights after default are cumulative, but that they “may be exercised simultaneously.” For example, the secured party could pur-
sue an Article 9 foreclosure against collateral while at the same time exercising setoff against the debtor’s deposit account and suing a guarantor.

Subsection (e) strengthens current law in favor of the secured party by providing that any judicial lien acquired by the secured party against the collateral is a continuation of the original perfected security interest. The judicial lien relates back to the earlier of the date of filing or the date of perfection. This rule gives the foreclosing secured party maximum protection against competing creditors and insulates it from preference attack by the debtor’s trustee in bankruptcy. Following current law, subsection (f) provides that an execution sale is an appropriate method of foreclosure under Article 9. Finally, subsection (g) states that the duties imposed on foreclosing secured parties do not apply to buyers of accounts, chattel paper, payment intangibles, or promissory notes. Although called secured parties, these buyers own the property and so may enforce their rights without regard to the seller or the seller’s creditors. That same latitude applies to a true consignor.

B. Enforcement Against Guarantors

The revision makes it clear that the default and enforcement rules apply to secondary obligors, including guarantors. Rev. UCC § 9-602. For example, notice of a foreclosure sale must be given to a guarantor just as surely as it must be given to the borrower who granted the security interest in the collateral. This continues the rule of current law. The fighting issue in the cases under current law is whether a guarantor can waive rights given by the statute following default by the borrower or credit buyer, even though the borrower or credit buyer cannot. Earlier drafts of the revision would have allowed a guarantor in a nonconsumer transaction to waive Article 9 defenses, as it could waive traditional suretyship defenses under the common law. However, the final draft of the revision reverses on this important point and generally prohibits predefault waiver by a guarantor or other secondary obligor. For example, a continuing guaranty agreement could not waive the secured party’s duty to hold a
commercially reasonable foreclosure sale or to give notice of the sale to the guarantor. The policy behind this antiwaiver rule is that a guarantor deserves as much protection against creditor misbehavior during foreclosure as the borrower who grants the security interest, since the guarantor is on the hook for any deficiency. The antiwaiver rule follows the weight of case law authority under the current version of Article 9, though it conflicts with the new Restatement of Suretyship.

Rev. UCC § 9-602 includes a laundry list of postdefault protections that the debtor cannot waive. However, the section "does not restrict the ability of parties to agree to settle, compromise, or renounce claims for past conduct that may have constituted a violation or breach of those rights and duties, even if the settlement involves an express 'waiver.'" Comment 3. In a closely related provision, Rev. UCC § 9-603 allows the parties to agree upon standards measuring the fulfillment of the rights of a debtor and duties of a secured party if those standards are not manifestly unreasonable. For example, a security agreement could set forth reasonable guidelines for advertising collateral prior to a private sale. On the other hand, the term "breach of the peace" cannot be tinkered with in the security agreement.

C. Collection of Receivables

Current Article 9 is unclear on whether, in directly collecting receivables following the borrower’s default, the secured party may enforce claims against guarantors of the receivables. The revision (Rev. UCC § 9-607(a)) clearly allows such enforcement rights. In addition, the secured party may step into the shoes of the debtor and enforce all of the debtor’s rights against account debtors, including the settlement of claims and the enforcement of a security interest provided by the account debtor. Comment 3 gives the example of a breach-of-warranty claim arising out of a defect in equipment that is collateral, or an action for an injunction against infringement of a patent that is collateral. Comment 3 also points out that such claims would be proceeds of the original collateral under Rev. UCC § 9-315. For authority to settle and compromise claims against the account debtor, see
Comment 9. Current UCC § 9-502 is fuzzy on these enforcement rights, though the same result can be achieved by properly drafted secured loan documentation.

If the secured party holds a security interest in the debtor's deposit account, it may apply the account to the debt (if the secured party is the depository bank) or it may instruct the bank to pay the balance for its benefit if it has a control agreement. Rev. UCC §§ 9-607(a)(4), (5). These rules illustrate how a depository bank is a specialized kind of account debtor.

A junior secured party may directly collect collateral under this section even though it knows that a senior creditor is ahead of it. However, whether the junior has priority in the collected proceeds depends on whether it qualifies as the purchaser of an instrument (Rev. UCC § 9-330(d)), the holder in due course of an instrument (UCC § 3-305, Rev. UCC § 9-331(a)), or a transferee of money (Rev. UCC § 9-332(a)). Rev. UCC § 9-607, Comment 5. However, since the senior's lien will not "ride through" the junior's foreclosure as would be the case for collateral like equipment, it would seem that the junior who grabs the collections but cannot claim priority proceeds at the peril of a conversion claim.

In a new departure intended to facilitate the foreclosure of notes secured by real estate, Rev. UCC § 9-607(b) allows the secured party to proceed with a nonjudicial foreclosure of the mortgage securing the note even though the secured party is not the assignee of record. The subsection enables the creditor to become the assignee of record by recording in the applicable real property records the security agreement and an affidavit certifying default by the debtor.

Subsection (d) allows the secured party to deduct from collections "reasonable expenses of collection and enforcement, including reasonable attorney's fees and legal expenses incurred by the secured party." Comment 10 points out that this includes only those fees and expenses incurred in proceeding against account debtors or other third parties. This right to recover expenses arises automatically from the statute. If the secured party wants to recover from the proceeds of the collateral those fees and expenses incurred in proceeding against the debtor or obli-
gor, the security agreement must so provide. Rev. UCC §§ 9-608(a)(1)(A), 9-625(a)(1). Comment 10 also tells us that the parties may agree to allocate a portion of the secured party's overhead to collection and enforcement—an opportunity not often seized in security agreements.

D. Application of Proceeds

As under current law, the revision provides for application of foreclosure sale proceeds in the following order: (1) reasonable expenses incurred in handling the foreclosure; (2) satisfaction of obligations secured by the security interest or agricultural lien that is being enforced; (3) satisfaction of any subordinate obligations if the foreclosing creditor receives demand before distribution of the proceeds is completed. The foreclosing creditor must account to the debtor for any surplus, and the obligor is liable for any deficiency. Rev. UCC § 9-608. The application of proceeds does not affect the priority of a creditor senior to the foreclosing creditor. The senior's security interest rides through the sale unscathed. Of course in most cases the senior will be notified by the junior in advance of the sale, as required by Rev. UCC § 9-611, and will make sure that the proceeds are first diverted to it. Alternatively, the competing creditors may enter into some kind of intercreditor agreement regarding application of the foreclosure sale proceeds.

Perhaps the most important change made by the revision in this area is found in Rev. UCC § 9-608(a)(3), which addresses the situation where an enforcing secured party receives noncash proceeds. Comment 4 gives this example:

Example: An enforcing secured party receives a promissory note from an account debtor who is unable to pay an account when it is due. The secured party accepts the note in exchange for extending the date on which the account debtor's obligation is due. The secured party may wish to credit its debtor (the assignor) with the principal amount of the note upon receipt of the note, but probably will prefer to credit the debtor only as and when the note is paid.

Comment 4 also points out that the parties may provide in
the security agreement for the method of application of noncash proceeds. In the absence of such an agreement, "it may well be commercially reasonable for the secured party to credit its debtor's obligations only as and when cash proceeds are collected from the account debtor, especially given the uncertainty that attends the account debtor's eventual payment."

E. Repossession

Under the revision, tangible collateral can still be repossessed by creditor self-help, so long as there is no breach of the peace. Rev. UCC § 9-609. During the early drafting process there was a movement to outlaw self-help repossession, at least in consumer transactions, or to define the term "breach of the peace" with greater specificity. Neither of these initiatives carried the day. However, Rev. UCC § 9-603, which allows the parties to determine by agreement the standards by which a creditor may enforce a security interest so long as the standards are not manifestly unreasonable, does not apply to the duty to refrain from breach of the peace. This is a watered-down compromise on the self-help issue. In a pro-debtor reform, Comment 3 approves of those cases holding under current law that the secured party cannot delegate away to independent contractors its duty to repossess collateral without breach of the peace. A number of cases have imposed vicarious liability on the secured party even for punitive damages, and these cases seem to be approved by the drafters of the revision. See, for example, McCall v. Owens.10

Although the text of Rev. UCC § 9-609 is silent on the point, Comment 5 discusses the problems that can occur if more than one secured party is in the picture:

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 posses-

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sion 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.

Rev. UCC § 9-609(c) validates a debtor's agreement to assemble collateral and make it available at a place the secured party designates. However, the revision goes beyond current law in validating these agreements whether or not they are conditioned on the debtor's default. "For example, a debtor might agree to make available to a secured party, from time to time, any instruments or negotiable documents that the debtor receives on account of collateral." Comment 7.

F. Realty-Related Foreclosures

If a secured creditor is foreclosing on fixtures, case law under current Article 9 indicates that the only remedy after default is removal of the fixtures from the real property. The fixture financer is not allowed to participate in the proceeds of the real estate foreclosure. See, for example, Maplewood Bank & Trust v. Sears, Roebuck & Co.11 In a reform very helpful to fixture financers, the revision overturns this case law. Rev. UCC § 9-604(b). Under the revision, a security interest in fixtures may be enforced under either real-property law or any of the applicable Article 9 provisions. See Comment 3 to Rev. UCC § 9-604.

Rev. UCC § 9-604(a) permits (but does not require) the secured party with a mixed collateral package to proceed as to both real and personal property in accordance with real-property law. That same subsection makes it clear that a secured party who exercises rights under Revised Article 9 with respect to personal property does not prejudice any rights under real estate law. On the other hand, Revised Article 9 does not address "one-form-of-

action” rules found in some states. Comment 2 puts it this way:

For example, under some anti-deficiency laws, creditors risk loss of rights against personal property collateral if they err in enforcing their rights against the real property. Under a “one-form-of-action” rule (or rule against splitting a cause of action), a creditor who judicially enforces a real property mortgage and does not proceed in the same action to enforce a security interest in personalty may (among other consequences) lose the right to proceed against the personalty. Although statutes of this kind create impediments to enforcement of security interests, this Article does not override these limitations under other law.

The bottom line is that secured creditors foreclosing on a mixed package of real estate and personal property still need to be careful about the dangers posed by these special statutes in some states (such as California).

G. Preparation of Collateral

It has never been clear under current case law whether the foreclosing creditor can refuse to process or prepare the collateral prior to sale. UCC § 9-504 allows sale of the collateral “in its then condition or following any commercially reasonable preparation or processing.” Rev. UCC § 9-610(a) continues that permissive language. However, Comment 4 to that section notes that some courts have imposed a duty of preparation or processing on the creditor. It then states:

Although courts should not be quick to impose a duty of preparation or processing on the secured party, subsection (a) does not grant the secured party the right to dispose of the collateral “in its then condition” under all circumstances. A secured party may not dispose of collateral “in its then con-
dition" when, taking into account the costs and probable benefits of preparation or processing and the fact that the secured party would be advancing the costs at its risk, it would be commercially unreasonable to dispose of the collateral in that condition.

This language indicates that the secured party should engage in a cost-benefit analysis of whether some preparation is appropriate. One of the factors should be whether these front-end costs can be recovered from the sale of the collateral or from the debtor personally.

H. Foreclosure Sale Warranties

In a clarification of current law, Rev. UCC §§ 9-610(d) and (e) provide that a foreclosing secured creditor gives implied warranties of title unless disclaimed. Rev. UCC § 9-610(f) provides sample disclaimer language, as follows: "There is no warranty relating to title, possession, quiet enjoyment, or the like in this disposition." The revision is silent with respect to implied warranties of merchantability or fitness, but the courts generally do not find such warranties if the foreclosing creditor is not a merchant with respect to the collateral or has no special expertise. See, for example, Donald v. City Nat'l Bank of Dothan. On the other hand, if the foreclosing creditor is a dealer that does its own financing or has bought back the secured debtor under a recourse obligation, the implied warranty of merchantability may well apply unless disclaimed. See Rev. UCC § 9-610, Comment 11.

I. Application of Noncash Proceeds

Current law is unclear on the duties of the secured creditor when it receives noncash proceeds of a foreclosure sale such as a promissory note from the foreclosure purchaser. Rev. UCC § 9-

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608(a)(3) provides that the foreclosing creditor need not apply noncash proceeds to the debtor's obligation; if it chooses to do so, it must apply them in a commercially reasonable manner. This rule provides flexibility for the creditor to accept a note as proceeds and either: (1) establish a commercially reasonable discount value; or (2) credit the debtor as the secured creditor receives payments on the note. If the secured creditor makes no application of the note to the debt but instead disposes of it to a third party, the subsequent disposition is subject to the Article 9 foreclosure rules.

J. Notice of Foreclosure Sale

As under current law, the revision requires notice of the foreclosure sale to be given to the debtor and any secondary obligor. In a throwback to pre-1972 law, Rev. UCC § 9-611 requires the secured party to give notification also to other secured parties who have filed financing statements covering the same collateral, so long as the collateral is other than consumer goods. Although this rule imposes a new UCC search requirement on the foreclosing creditor, the theory is that such advance notice will limit postforeclosure disputes among competing creditors and encourage inter-creditor agreements. Rev. UCC § 9-613 provides a statutory form of notice of sale that will serve as a safe harbor for foreclosing creditors in other than consumer-goods foreclosures. Since we have seen so much litigation regarding the adequacy of notice, creditors strongly applaud the safe harbor into which they may now sail.

Under current law, some courts have imposed a "second try" duty on creditors who send notification and learn that the debtor did not receive it. The creditor is required to attempt to locate the debtor and send another notification. Revised Article 9 punts on this issue, leaving resolution to the courts under the facts of each case. See Rev. UCC § 9-611, Comment 6. Comment 8 also makes the important point that a secured party may always elect not to follow through on a foreclosure sale after sending notice. Moreover, a secured party may send a revised notice if its plans change for disposition. This flexibility can be important.
In a variation on the notification theme, Comment 8 to Rev. UCC § 9-610 discusses the impact of the federal securities laws on Article 9 foreclosures:

Dispositions of investment property may be regulated by the federal securities laws. Although a "public" disposition of securities under this Article may implicate the registration requirements of the Securities Act of 1933, it need not do so. A disposition that qualifies for a "private placement" exemption under the Securities Act of 1933 nevertheless may constitute a "public" disposition within the meaning of this section. Moreover, the "commercially reasonable" requirements of subsection (b) need not prevent a secured party from conducting a foreclosure sale without the issuer's compliance with federal registration requirements.

Timeliness of notice before disposition of collateral is governed by Rev. UCC § 9-612. What is a reasonable time is generally a question of fact. However, subsection (b) provides a safe harbor, approving notice sent "after default and 10 days or more before the earliest time of disposition set forth in the notification." Like the statutory form of notice, this safe harbor on timing should be of great benefit to secured creditors foreclosing in nonconsumer settings.

K. Recourse and Repurchase Agreements

Under current law, it is unclear whether transfer of collateral from a secured lender to a guarantor under a recourse arrangement or a manufacturer under a repurchase agreement constitutes a foreclosure sale requiring the transferor to give notice under Article 9. See UCC § 9-504(5). Rev. UCC § 9-618 clears muddy waters by providing that a secondary obligor has the rights and assumes the duties of a secured party if it steps into
the shoes of the primary obligor on payment of the obligation. This transfer of collateral to the secondary obligor is not a foreclosure sale, but it relieves the former secured party of further duties. In these recourse, repurchase, or subrogation situations, the subsequent sale by the transferee is the one that must follow the foreclosure rules of Article 9.

But other variations yield different results, as contemplated by Rev. UCC § 9-618. For example, in order to encourage floorplan financing of a distributor or dealer, a manufacturer of durable goods will sometimes agree with the floorplan financer to repurchase the inventory following the dealer’s default. The purchase price is typically the wholesale price of the goods, plus costs incurred by the floorplan financer in enforcing its Article 9 security interest. In this scenario, the manufacturer is not a secondary obligor on the debt, but only has the duty to repurchase the collateral according to the prescribed formula. Such a repurchase agreement would qualify as an Article 9 private foreclosure sale. If the dealer is properly notified of the transfer and it is otherwise considered commercially reasonable based on the preapproved wholesale price buyout, the floorplan lender’s deficiency claim against the dealer should be firmly established.

L. Marshaling

As under current law, after applying the proceeds of sale to its front-end costs and its own debt, the foreclosing creditor must pay over any remaining proceeds to a subordinate secured creditor who has made a demand for payment. However, there is no duty to remit just because the foreclosing creditor was obligated to notify the junior of the sale. Rev. UCC § 9-615(a). Moreover, a junior secured party owes no obligation to apply the proceeds of disposition to the senior, whose lien will ride through the foreclosure. See Rev. UCC § 9-617 and Official Comment 5 to Rev. UCC § 9-610. On the other hand, if the junior receives cash proceeds of a disposition with knowledge that the receipt violates the rights of the senior, it could constitute a conversion. Rev. UCC § 9-615(g).

To what extent will the application of proceeds be gov-
erned by the equitable doctrine of marshaling? Comment 5 to Rev. UCC § 9-610 addresses this issue:

When a secured party’s collateral is encumbered by another security interest or other lien, one of the claimants may seek to invoke the equitable doctrine of marshaling. As explained by the Supreme Court, that doctrine "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." Meyer v. United States, 375 U.S. 233, 236 (1963), quoting Sowell v. Federal Reserve Bank, 268 U.S. 449, 456-57 (1925). 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.” Id. at 237. Because it is an equitable doctrine, marshaling “is applied only when it can be equitably fashioned as to all the parties” having an interest in the property. Id. This Article leaves courts free to determine whether marshaling is appropriate in any given case. See Section 1-103.

M. Calculating the Deficiency: the Rapson Rule

Like current Article 9, the revision allows recovery of a deficiency against the debtor or any secondary obligor, assuming no misbehavior during the foreclosure. Rev. UCC § 9-615(d). However, in order to address the problem of procedurally regular dispositions that bring a very low price, Rev. UCC § 9-615(f) provides a special method of calculating a deficiency if the collateral is sold to the foreclosing secured party, a related entity, or a secondary obligor. If the proceeds are significantly below what would have been fetched had the sale been made to an unrelated third party, the deficiency is calculated not on the basis of what was actually received, but on what would have been received if the sale had been made to an independent third party. The hope is to preclude large deficiencies based on potentially collusive foreclosure sales. This new rule is known as the Rapson rule, named after its distinguished drafter/author, Donald J. Rapson. The rule only applies in circumstances where the other aspects of the sale were commercially reasonable. The revision chose this
approach rather than adopting a flat rule that would treat the price as a term of the sale that must be commercially reasonable. On this last point, the revision follows current Article 9 and the case law under it. However, Official Comment 11 to Rev. UCC § 9-610 states that "a low price suggests that a court should scrutinize carefully all aspects of a disposition...."

N. Foreclosure Transferees

As under current law, a secured party's disposition of collateral default: (1) transfers to a transferee for value all 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. Rev. UCC § 9-617(a). By contrast, a senior security interest normally rides through the foreclosure. Under subsection (b), a good-faith transferee takes free of all but the senior lien even if the procedures surrounding the foreclosure sale are faulty. The revision applies a good-faith standard to both public and private dispositions, whereas current UCC § 9-504(4) imposes a somewhat different standard for public foreclosure sales.

Rev. UCC § 9-619, which is new, provides a handy procedure under which foreclosure buyers of motor vehicles covered by a certificate of title can obtain a transfer statement to obtain clear legal title to the motor vehicle. Under current law, obtaining a clear chain of title can be accomplished only with the consent of the record owner. If the record owner is the debtor after default and refuses to cooperate, the secured party may have great difficulty in obtaining a repo title and disposing of the collateral. The title-clearing mechanism of the transfer statement should solve this problem, not only for titled motor vehicles but also for other types of collateral where the law does not provide such a mechanism.

O. Facilitation of Strict Foreclosure

In some of its most important reforms, the revision encourages the use of strict foreclosure, that is, retaining the collateral in
satisfaction of the debt. This enforcement mechanism is encouraged because in many cases a foreclosure sale is futile where a deficiency claim is worthless, or the expenses and legal risks of a sale are such that strict foreclosure is commercially preferable. For a statement of this policy of encouraging strict foreclosure, see Rev. UCC § 9-620, Comment 2.

The revision encourages strict foreclosure in at least five ways:

Although it still allows the secured party the option to make a proposal to the debtor inviting a response, the secured party may simply accept collateral in satisfaction of the debt if the debtor consents or the secured party does not receive objection within 20 days. Under current law, the secured party must always make a proposal to retain and the debtor has a fixed period to respond. Allowing the acceptance option without a formal proposal eliminates an element of awkwardness under current law. The debtor may consent by agreeing to the acceptance in writing after default. Rev. UCC §§ 9-620, 9-621.

Rev. UCC § 9-620(a) permits a secured party in nonconsumer foreclosures to accept collateral in partial satisfaction of the debt, something that probably cannot be done under current law.

Rev. UCC § 9-620 eliminates the requirement under current law that the secured party use strict foreclosure only when it is in possession of the collateral, at least in nonconsumer foreclosures. This means that the remedy may be used in foreclosing on intangible collateral, an unlikely result under current law. See Comment 7.

Rev. UCC §9-622 provides that acceptance of the collateral in satisfaction of the debt discharges junior claimants, a result unlikely under current law.

The revision rejects the holdings of some courts under current law that a creditor is barred from obtaining a deficiency if it holds collateral too long and thus engages in a constructive strict foreclosure. Instead, delay is a factor relating to whether the secured party acted in a commercially reasonable manner under Rev. UCC §§ 9-607 and 9-610. See Rev. UCC § 9-620, Comment 5. On a related point, the debtor’s voluntary surrender of collateral to the secured party and the secured party’s acceptance of the re-
turn do not, of themselves, raise an implication that the secured party intends or is proposing to accept the collateral in satisfaction of the secured debt.

P. Sanctions for Creditor Misbehavior

As under current law, if it is established that the secured party is violating the rules of Article 9 in enforcement of its security interest, a court may enjoin further enforcement (Rev. UCC § 9-625(a)), or subject the creditor to liability for damages (Rev. UCC § 9-625(b)). For example, if the creditor prematurely undertakes repossession when the debtor is not in default, the repo could be enjoined or the debtor could collect monetary damages. The drafters also suggest that, in a proper case, the secured party might be liable for conversion under non-UCC law—possibly resulting in punitive damages and attorney fees. See Rev. UCC § 9-626, Comment 2.

As a measure of protection for foreclosing secured parties, Rev. UCC § 9-627 continues current law in providing that low price alone is not enough to make a foreclosure sale commercially unreasonable. Except in situations covered by the Rapson rule of Rev. UCC § 9-615(f), the key continues to be procedural irregularity in enforcement of the security interest. Moreover, a disposition of collateral is performed in a commercially reasonable manner if made: (1) in the usual manner on any recognized market; (2) at the price current in any recognized market at the time of disposition; or (3) otherwise in conformity with reasonable commercial practices among dealers in the type of property that was the subject of the disposition. Rev. UCC § 9-627(b). Subsection (c) of Rev. UCC § 9-627 provides that a collection, enforcement disposition, or strict foreclosure is commercially reasonable if it has been approved: (1) in a judicial proceeding; (2) in a bona fide creditors' committee; (3) by a representative of creditors; or (4) by an assignee for the benefit of creditors. These safe harbors are an elaboration of current law.

What is the effect of creditor misbehavior on a deficiency claim? For nonconsumer transactions, the revision adopts the rebuttable presumption rule for creditor misbehavior during fore-
closure. Rev. UCC § 9-626. Under this rule, the value of the collateral is deemed to equal the unpaid balance of the debt, unless the creditor proves otherwise. The burden is shifted to the creditor seeking a deficiency to show that it deserves one; and it must come forth with evidence of collateral value independent of the price obtained on foreclosure. By embracing the rebuttable presumption rule, the revision rejects the absolute bar rule under which the misbehaving creditor’s claim to a deficiency is snuffed out regardless of harm caused by the misbehavior during foreclosure. Under current law, most states have chosen the rebuttable presumption rule, but a fair number take the more Draconian absolute bar approach. Not surprisingly, the rebuttable presumption rule was one of the most sought-after changes by secured creditor groups during the revision process. The rule eliminates unfortunate situations where the misbehaving creditor is denied a multimillion dollar deficiency against the borrower and guarantor because of some technical failure in holding a foreclosure sale on a $50,000 piece of equipment. See, for example, In re Kirkland.13

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13. In re Kirkland, 915 F2d 1236, 12 UCC Rep. 2d 1204 (9th Cir. 1990).