The purpose of this column is to identify some of the most disconcerting judicial decisions interpreting the Uniform Commercial Code or related commercial laws. The purpose of the column is not to be mean. It is not to get judges recalled, law clerks fired, or litigators disciplined for incompetence. Instead, it is to shine a spotlight on analytical errors, and thereby provide practitioners and judges with reason to disregard the decisions.


In this case, the court correctly concluded that a creditor enforcing an Article 9 security interest need not comply with the procedures for enforcing the statutory lien that the creditor also held. However, the court failed to consider whether the creditor complied with Article 9.

The case involved the owner of a self-storage facility. Most states provide the owners of such facilities with a statutory lien on the contents of a storage unit to secure payment of the rent for the unit. Alabama, where the case arose, is no exception. See Ala. Code § 8-15-33. After the corporate tenant stopped paying rent, the storage facility unsuccessfully attempted to contact the tenant. Several months later, the storage facility sold the contents. The tenant sued for, among other things, violation of the Alabama Self-Service Storage Act by failing to provide notice of default by certified or registered mail, failing to advertise the sale, failing to provide an opportunity to cure, and failing to make an inventory of the property sold. The court rejected the claim. It concluded that the rental contract gave the facility owner a consensual lien on the unit’s contents (thus implicating Article 9, see § 9-109(a)(1) & cmt. 2) – in addition to the statutory lien that the law provided – and that the Storage Act did not require the storage facility to comply with the Act’s procedures when enforcing a consensual lien.

The court’s conclusion is undoubtedly correct. Not only is it well grounded in the language of the Storage Act itself, but it is also consistent with the rules and principles of Article 9, which expressly indicates that a secured party’s various rights are cumulative and the pursuit of one does not interfere with the exercise of others. See U.C.C. § 9-601(a), (c). See also Spencer v. Public Storage, 2012 WL 4479002 (No. 2:11–cv–00357–JEO, N.D. Ala. Sept. 24, 2012) (storage company with a contractual lien on personal property in storage unit did not have to comply with sale procedures under the Alabama Self–Service Storage Act and its sale of the unit’s contents was not conversion).

Unfortunately, the court then missed what should have been the real question: whether the storage facility conducted the disposition in compliance with Article 9. Article 9 requires the
secured party in most cases to send the debtor reasonable notification of the planned disposition. See § 9-611(b), (c). The failure of the court – and, apparently, the parties – to address this issue is a bit perplexing given that the provision of the Alabama Code that they discussed, § 8-15-33, expressly refers to Article 9’s notification provisions. Article 9 also requires that the disposition be conducted in a commercially reasonable manner. See § 9-610(b). In this case, the storage facility allegedly sold for $500 the contents of the plaintiff’s unit – claimed to be worth in excess of $350,000 – without taking an inventory or advertising the sale. While a low sales price is not by itself sufficient to prove that the sale was commercially unreasonable, see § 9-627(a), it is sufficient to raise a red flag, see § 9-627 cmt. 2, and combined with the other allegations should have been more than enough to avoid summary judgment in favor of the storage facility.

A few additional thoughts about self-storage facilities and the liens that secure payment of the rent due to them may be of interest. In general, self-storage facilities prefer to be regarded as renters of space rather than as bailees of goods. If they were bailees, their statutory liens would probably have priority over any previously created and perfected security interests in the goods stored, see §§ 7-209, 9-333. However, the facilities would have a duty to care for the goods, see §§ 7-204, 9-207, and these duties would be non-waivable, see §§ 1-302, 7-204 cmt. 2. Moreover, as a bailee, any sale of the goods would be governed by § 2-710, which requires commercial reasonableness. As a renter of space, in contrast, the storage facility need merely comply with the procedures mandated by the applicable state statute. Some of those statutes insulate the storage facility from liability if they conduct the sale in a commercially reasonable manner but stop short of placing an affirmative duty on the storage facility to conduct the sale in such a manner. See, e.g., Ala. Code § 8-15-34(13), (14); Utah Code § 38-8-3(10), (11).

Other states expressly require that the contents of a self-service storage facility be sold in a commercially reasonable manner to enforce the facility owner’s statutory lien for rent. Amazingly, one of these states is California, see Cal. Bus. & Prof. Code § 21707, the location where the television show Storage Wars is based. According to that show, the contents of self-storage units are sold as a single lot and the bidders are not permitted to enter the unit or handle the contents before bidding, with the result that they usually have only a vague idea what goods are in the unit. It is not clear how that can possibly be a commercially reasonable procedure. Whether this is an example of Hollywood obscuring reality, storage facility owners ignoring the law, or defaulting renters unaware of their rights is unknown.


This case presented an issue of priority under both the Food Security Act and Article 9. Given the arguments made, the court reached the correct result but its reasoning on the Article 9 issue was slightly flawed. However, the court and the parties overlooked a point that should have led them to a contrary result.
The facts can be summarized as follows. In 2009, an Oklahoman cattleman named Smith obtained a loan from Great Plans National Bank and in return granted the bank a security interest in his existing and after-acquired cattle. Great Plains perfected its security interest by filing a financing statement in Oklahoma.

In 2009, a Colorado cattleman named Mount purchased 206 cattle from Smith. That purchase was financed by Cattle Consultants, LLC, which acquired a security interest in the cattle and perfected by filing a financing statement in Colorado. Thus, the parties’ relationships can be diagrammed as follows:

Smith covered the sale to Mount using cattle he purchased the day before from supplier in Missouri. Smith paid with a check drawn on insufficient funds but Great Plains honored the check. When Great Plains was unable to collect from Smith, it sought to enforce its security interest in the cattle and filed a financing statement against Smith in Colorado.

In the resulting litigation, the trial court granted summary judgment for Great Plains. The court of appeals affirmed. In doing so, it first noted that Mount could not take free of Great Plains’ security interest under § 9-320(a), the provision that generally protects buyers in ordinary course of business, because that section does not apply to “a person buying farm products from a person engaged in farming operations.” There was no dispute that the cattle were farm products in Smith’s hands or that Smith was engaged in farming operations.

Under the Food Security Act, buyers of farm products can take free of a security interest created by the seller. However, this general rule is subject to an exception if: (i) the farm products are “produced in a State that has established a central filing system”; (ii) the buyer has failed to register with the Secretary of State of such State prior to the purchase; and (iii) the secured party has filed an effective financing statement that covers the farm products being sold. 7 U.S.C.
There was no dispute that Great Plains had filed in Oklahoma and that Mount had failed to register there. So, the question became whether the cattle were “produced” in Oklahoma, where Smith was located, or in Missouri, where the cattle had been raised until the day before Smith acquired and resold them.

The court of appeals concluded that the term “produced” deals with the location from which the farm products are sold, not their geographic origin, since that is the only location of which the buyer is likely to be aware. Interpreting the FSA to mean where the goods were grown or raised would leave buyers with no practical method of discovering prior security interests or knowing where to file, the precise problem that the FSA was designed to address. Indeed, Mount himself had thought that he was acquiring Oklahoma cattle and discovered they came from Missouri only much later. This portion of the court’s analysis – and the court’s conclusion that Mount acquired the cattle subject to Great Plains’ security interest – makes perfect sense.

As for the priority dispute between Great Plains and Cattle Consultants, the court looked to the first-to-file-or-perfect rule of § 9-322(a). Great Plains had filed against Smith in Oklahoma in 2009, re-filed in Colorado within one year of the sale to Mount, and thus, the court concluded, Great Plains’ priority dated back to 2009. Cattle Consultants filed and perfected in 2010 and thus was junior.

To avoid this argument, Cattle Consultants claimed purchase-money priority. There was no dispute that Cattle Consultants did in fact have a purchase-money security interest (PMSI). It had, after all, financed Mount’s purchase of the collateral. However, the court concluded that Cattle Consultants was not entitled to priority under § 9-324(d) because Cattle Consultants perfected its interest after Mount received possession, not before, cf. § 9-324(d)(1), and because Cattle Consultants had not given prior notification of its PMSI financing to Great Plains, cf. § 9-324(d)(2)-(4).

There are at least three problems with this analysis. First, even if Cattle Consultants had complied with the rules of § 9-324(d), it would still not have been entitled to priority. As the diagram above illustrates, this is a classic case of the so-called “double-debtor” problem. Great Plains’ debtor was Smith but Cattle Consultant’s debtor was Mount. As long as Mount acquired the cattle subject to Great Plains’ perfected security interest – which he did – and that security interest remained perfected – the court so ruled, but more on this below – then even if Cattle Consultant would normally qualify for PMSI priority, section 9-325 would subordinate it. Indeed, even if Cattle Consultants would have won under the first-to-file-or-perfect rule of § 9-322(a)(1) – is it might if it had filed against Mount before Great Plains had filed against Smith – its interest would nevertheless be subordinated by § 9-325. So, while the court’s discussion of § 9-324 was interesting, it was irrelevant to the resolution of the case.

Second, in part because § 9-325 trumps § 9-324 in the cases involving the double-debtor problem, it is not clear that the court was correct in concluding that Cattle Consultants was required to give advance notification of its financing plans to Great Plains in order to obtain priority under § 9-324(d). That provision requires the PMSI lender to give notification to the holder of the “conflicting” security interest. It is not clear that the interest granted by a former owner is really
conflicting for this purpose of this rule. After all, the reason underlying for the notification requirements in § 9-324(b) and (d) – dealing with inventory and farm products, respectively – is to allow the prior lenders against such property to avoid making further advances to their debtor in reliance on PMSI collateral. But that rationale does not apply in the double-debtor scenario in which the prior debtor already owns the collateral. Moreover, the collateral may not even be inventory or farm products in the hands of the prior debtor, so the concerns relating to the financing of such types of collateral may be completely inapposite.

Neither of these first two criticisms is material to the court’s ultimate conclusion. The final criticism, though, may be. Recall that Great Plains re-filed in Colorado, where Mount is located, within one year after the sale to Mount. This is required under § 9-316(a)(3) to maintain perfection, and failure to do so results in a loss of perfection that is retroactive with respect to purchasers for value. See § 9-316(b). Such a loss of perfection would normally allow the buyer to then take free of the security interest. See § 9-317(b). What the court glossed over – presumably because no one argued about it – was that Great Plains filed in Colorado against Smith, not against Mount.

Section 9-316 is conspicuously silent about whether a re-filing in the state in which the collateral buyer is located should be under the original debtor’s name or the buyer’s name. The statutory text does not speak directly to the issue, although there is an oblique statement in the comments suggesting that the filing should be against the buyer. See § 9-316 cmt. 2, ex. 4. Several good arguments support this suggestion. First, financing statements are supposed to be filed against the “debtor.” Upon purchase of the collateral, the buyer becomes the debtor. See § 9-102(a)(28). See also § 9-509(c) (providing that acquisition of property subject to a security interest gives the secured party authorization to file against the acquirer). Second, the whole filing system is based around the name and location of the debtor. Searchers search for financing statements filed against the debtor’s name in the state where the debtor is located. Smith is located in Oklahoma. No one would think to look for a filing against him in Colorado. More important, the collateral is now owned by Mount in Colorado. Searchers would normally search for filings against him in Colorado, but would not really have reason to search against the names of former owners there. If the purpose of re-filing in the new state is to give notice of the security interest to people who search in the new state – that is, to alleviate the burden of searching against former owners if the current owner acquired it more than one year ago – then that only works if the searchers know what name to search against. They know the name of the new owner but may not know the names of former owners. If the law is going to require that they search under the names of former owners, as the court’s decision implicitly suggests, it might as well require that they search where the former owners are located. In other words, the court’s analysis makes § 9-316 a trap for prior secured parties without doing much of anything to alleviate the burden on current searchers. Still, it is hard to fault the court for making this error given that Article 9 provides little guidance on the point and the parties apparently missed it as well.
In re Doctors Hospital of Hyde Park, Inc.,
474 B.R. 576 (Bankr. N.D. Ill. 2012)

This case involved a creditor’s claim to proceeds from the trustee’s settlement of avoidance actions brought against other parties. In August 1997, the debtor, Doctors Hospital of Hyde Park (“Doctors Hospital”) granted a security interest in its tangible and intangible property to guaranty a $50 million loan. The note, guaranty, and security interest were later assigned to LaSalle National Bank (“LaSalle”). Doctors Hospital subsequently filed for Chapter 11 bankruptcy protection. In that proceeding, the Chapter 11 trustee filed an avoidance action against a number of individuals and entities for fraudulent transfers, breach of fiduciary duty, and wrongful payment of dividends.

Prior to trial, the trustee settled with several of the defendants in return for payments exceeding $6.6 million. LaSalle claimed that the settlement proceeds were subject to its security interest. The trustee, asserting that the security agreement did not cover the settlement proceeds and that, even if it did, the version of Article 9 in effect in New York at the time when the security agreement was executed barred any interest in commercial tort claims.

In addressing the first issue, the court first ruled that because the security agreement was complete on its fact, the court would not consider the other documents executed by Doctors Hospital in association with the loan. Apparently applying the parol evidence rule, the court limited its inquiry to the security agreement itself. The court then concluded that the language of the security agreement, which granted a security interest in “General Intangibles” and defined them as “intangible personal property of Operator with respect to the Facility,” included things relating to the operation of the Facility, not merely things related to the physical structure. The court supported this conclusion by pointing out that the security agreement also included inventory “relating to the Facility” and it would make no sense to limit that clause to inventory related to the physical structure.

In resolving the second issue the court’s analysis became confused but the decision seems to make the following points (although not in this order). First, some of the settled claims were contract claims, not tort claims. As to these claims, the court agreed that settlement proceeds were subject to LaSalle bank’s security interest. As to the settled tort claims, however, the court reached the opposite conclusion for two erroneous reasons.

First, citing to old Article 9, which was in effect at the time the debtor executed the security agreement, the court stated that § 9-104(k) “prohibited the taking of a security interest in tort claims.” That is emphatically not true. Old § 9-104 was – like revised § 9-109 is – a scope rule, not an attachment rule. It said merely that Article 9 did not apply to the assignment of a tort claim, not that such assignments were illegal or ineffective. It may well be that applicable law did prohibit such an assignment, but that law was not – and is not – part of Article 9. More to the point, and as the court itself noted, once a tort claim is settled, the settlement agreement gives rise to a general intangible that can be collateralized under Article 9 even if the original tort claim could not be. This point is made expressly in revised § 9-109 comment 15 but was also true under the proper interpretation of old Article 9.
Second, the court ruled that even if revised Article 9 were applicable, the security agreement failed to describe the tort claims with the specificity required by § 9-108(e). Unfortunately, this statement immediately followed the court’s correct observation that a right to payment under a settlement agreement “becomes a payment intangible and ceases to be a claim arising in tort.” Thus, the court’s continued treatment of the rights under the settlement agreement as a commercial tort claim does not make sense. Put simply, although the court correctly observed what § 9-108(e) does, that provision was completely inapposite, given that the court had already — and correctly — concluded that the settled claims should be treated as arising in contract rather than tort.

_In re Delta-T Corp.,_


This is the first of two cases dealing generally with when an account arises or accrues. Although the court’s opinion is lengthy, the facts are reasonably simple and the issue fairly easy to frame.

In June 2009, the debtor, Delta-T Corp., granted a security interest in its accounts to secure a $7.2 million promissory note. The secured party perfected the security interest. Six months later, a different creditor obtained a $6 million judgment against the debtor and, shortly thereafter, garnished one of the debtor’s deposit accounts. The deposit account had a $650,000 balance, all of which was traceable to payments the debtor received in connection with its sale of steel to some scrap dealers. The bankruptcy trustee, who received an assignment of the perfected security interest, asserted priority over the garnishing judgment creditor, claiming that the deposit account was proceeds of accounts. The judgment creditor resisted, arguing that the debtor’s sales were cash sales that never generated accounts because the buyers paid on either the same day or the day after they picked up the steel.

To answer this question, the court looked closely at the steel sale transactions, specifically at when title to the steel passed. Because: (i) the steel was identified to the contract when the debtor accepted the purchase order therefor; (ii) the buyers were to pick up the steel at the debtor’s place of business, and thus the steel was to be delivered to the purchasers without being moved; (iii) no document of title was required; and (iv) the parties had not otherwise agreed, title passed when the contract was made. _See_ § 2-401(3)(b). This, the court reasoned, was when the debtor acquired a right to payment, and because that right preceded actual payment, the sales had generated accounts.

The court’s conclusion is undoubtedly correct but its analysis was unnecessarily complicated. When title to the steel passed does not matter. A right to payment for goods sold is an account as long as the right is not evidenced by an instrument or chattel paper. _See_ § 9-102(a)(3). Even if the right to payment is conditioned on the passage of title or some other type of performance by the obligee, the payment right is an account. In other words, the existence of a condition does not prevent the right to payment from qualifying as an account. Article 9 makes this point clearly when it states that a right to payment qualifies as an account regardless of whether it has or has not been “earned by performance.” Thus, because the right to payment arises when the agreement to purchase
is entered into, that is when an account is created. In short, once the debtor accepted the purchase orders for the steel, the debtor had accounts. The payments made days later were identifiable proceeds of the accounts and remained subject to the perfected security interest later assigned to the trustee.

The judgment creditor correctly asserted that a true cash sale does not generate an account. But for this purpose a cash sale is a transaction in which payment either precedes or is simultaneous with the formation of the sales contract. The paradigm example is the purchase of foodstuffs at a supermarket. In such a case, there is no agreement to buy and sell prior to when the customer offers payment – whether in cash or by some other means – to the sales clerk. Delta-T’s sales of steel were not cash sales. So the court was correct, but the focus on the passage of title was unnecessary and is regrettable.

Puritan Finance Corp. v. Bechstein Constr. Corp.,

This second case dealing with when an account arises involves the right of an account debtor to assert defenses and claims against an assignee of the account. Pursuant to § 9-404(a), an account debtor is entitled to assert against an assignee: (i) any defense or claim in recoupment arising from the transaction that gave rise to the account; and (ii) any other defense or claim of the account debtor against the assignor “which accrues before the account debtor receives a notification of the assignment.” For this purpose, when does such an unrelated defense or claim “accrue”?

The case pitted Puritan Finance, which had a security interest in the debtor’s accounts, against Bechstein Construction, one of the debtor’s account debtors. Bechstein admittedly owed the debtor $22,000 on several cartage contracts. However, prior to notification of the assignment to Puritan Finance, Bechstein performed similar services for the debtor. Apparently, Bechstein and the debtor regularly perform cartage work for one another and swapped checks periodically to settle their outstanding invoices. Accordingly, Bechstein sought to reduce its liability to Puritan by the amount of its claim against the debtor.

The court rejected this partial defense. After looking to Black’s Law Dictionary for the definition of “claim,” the court concluded that a claim “accrues” when a cause of action exists under applicable law. Applying this standard, the court held that Bechstein could not set off against its obligation the amounts the debtor owed to it because even though Bechstein had fully performed its duties under the cartage contracts before it received notification of the assignment, it did not yet have a cause of action, presumably because no invoice had yet been issued and payment was not yet due.

Relying on a 1989 decision from Kansas, the court’s analysis and rationale looked at the issue primarily from the perspective of the secured party. After noting that “accrue” could mean either when the obligation to pay is incurred or when the obligation becomes due and payable, the court concluded that the policies of simplicity and commercial certainty underlying the UCC favor the second definition. The court reasoned that, if incurrence of the claim was when it accrued, the value
of accounts assigned as security could never be accurately determined because the accounts would always be subject to an independent claim arising against the assignor after the assignment is made, but accruing beforehand. In contrast, if “accrues” means “becomes due and payable,” the value of accounts can be determined with reasonable certainty at the time of the assignment. *Id.* at *3 (quoting *Bank of Kansas v. Hutchinson Health Servs., Inc.*., 773 P.2d 660, 665 (Kan. Ct. App. 1989)).

This rationale is suspect. It is highly doubtful that the difference between the two meanings of when an account debtor’s claim accrues significantly affects a potential assignee’s ability to value the accounts. In either case, due diligence would require conferring with the account debtors to confirm the accuracy of the account and the nonexistence of any defense or setoff claim. More important, an assignee typically values accounts before deciding to buy or lend against them. Only after making that decision – indeed, after entering the actual assignment – is notification of the assignment given to the account debtors. Thus, there will always be some time lag between when the accounts are valued and when the account debtor receives notification of the assignment. As a result, the assignee will always bear some risk that it has paid or loaned too much because, in the interim, some defense or claim has accrued.

More to the point, this focus on the secured party’s ability to value the account confuses the rule’s effect with its purpose. The *effect* of a notification of assignment is to cut off some of the account debtor’s setoff rights. The *purpose* of the notification – a purpose the court ignored – is to inform the account debtor of the assignment, and thus is best understood from the perspective of the account debtor. The notification alerts the account debtor to no longer rely on its outstanding obligation to the debtor (i.e., not to rely on its setoff rights) when deciding whether to enter into a non-cash transaction that generates the debtor’s reciprocal obligation to the account debtor. Viewed in that light, an account debtor’s claim should arise when the debtor’s obligation is created, not some time later when a cause of action accrues. The court’s analysis was faulty and its conclusion wrong.

**Stephen L. Sepinuck**
Professor, Gonzaga University School of Law
Director, Commercial Law Center
ssepinuck@lawschool.gonzaga.edu

**Kristen D. Adams**
Professor & Associate Dean for Academics
Stetson University College of Law
adams@law.stetson.edu