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.


This case involves a conversion action against buyers of collateral. While the court correctly treated the buyers as liable for conversion, it improperly held them responsible for the attorney’s fees incurred by the secured party in bringing the action.

The facts are relatively straightforward. The debtor, John Chorley, granted BancorpSouth a security interest in equipment, including a bulldozer, an excavator, and a backhoe. BancorpSouth perfected its interest by filing a financing statement. Subsequently, the debtor sold the three items to two buyers, who later resold the items to their own customers. Chorley defaulted on the debt to BancorpSouth and sought bankruptcy protection. BancorpSouth then brought a claim for conversion against the two buyers.

Included in BancorpSouth’s action was a request for attorney’s fees. The trial court ruled that there was no statutory or contractual basis for an award of attorney’s fees. The Tennessee Court of Appeals reversed, concluding that both a statutory and contractual basis existed for awarding attorney’s fees.
For the statutory basis, the court relied on § 9-607(d), which authorizes a secured party to deduct from commercially reasonable collections on collateral the reasonable expenses it incurred in collecting, including attorney’s fees. But for several reasons this provision was not properly applicable. First, as comment 3 makes clear, § 9-607 deals with collections from an account debtor or other person obligated on collateral. In other words, it applies only when the collateral consists of a right to payment. Here, the collateral was equipment in the hands of the original debtor and inventory in the hands of the buyers; equipment is not a receivable. Even if § 9-607 had been applicable, subsection (d) would authorize the secured party to subtract its attorney’s fees only from the amounts collected. In other words, it allows a secured party to effectively charge the debtor for attorney’s fees by allowing the secured party to recover those fees from the proceeds of the collateral. Subsection (d) does not impose liability on the account debtor for attorney’s fees incurred in collecting. Of course, the agreement giving rise to the receivable could provide for recovery of attorney’s fees from the account debtor. But if it does not, the account debtor should not be responsible for those fees. After all, an account debtor has no control over whether its creditor – the debtor – uses the receivable as collateral. See § 9-406. If the conclusion of the court of appeals were correct, an account debtor that expressly bargained not to be liable to its creditor for attorney’s fees would find its bargain undermined by the creditor’s unilateral action of using the receivable as collateral. Article 9 does not so lightly interfere with parties’ contract rights.

With respect to the contractual basis for awarding attorney’s fees, the court relied on § 9-201(a), which provides that “a security agreement is effective according to its terms between the parties, against purchasers of the collateral, and against creditors.” The court read this language literally, concluding that it made the debtor’s security agreement, which included a provision on attorney’s fees, binding on the buyers. But this literalist approach leads to absurd results. It would make a buyer of collateral obligated to perform all kinds of covenants that the debtor promised to perform – such as providing periodic financial information – even though the buyer had no knowledge of the security interest or of the terms of the security agreement. Indeed, the court’s literalist approach would bind not only buyers, but all creditors of the debtor, which would include involuntary creditors, such as tort victims.

More important, the court’s conclusion is belied by comment 2 to § 9-201. That comment reminds the reader that the “security agreement” referenced in the section is merely “an agreement that creates or provides for a security interest.” See § 9-102(a)(73). Thus, the only thing that § 9-201(a) makes binding on third parties is the portion of the agreement that creates or provides for a security interest. Indeed, as the comment further explains, § 9-201(a) does not make other terms in a record that constitutes a security agreement binding on third parties. The court of appeals’ decision is simply wrong.


This case involved perfection of a security interest in accessions: that is, in goods that become physically united with other goods in such a way that the identity of the goods is not lost.
Wells Fargo Equipment Finance, Inc. (“Wells Fargo”) issued a $4 million line of credit to Negus-Sons, Inc., a company that performed earth-moving work for construction projects. The debt was secured by numerous items of the debtor’s equipment. The debtor used the line of credit to purchase a customized, heavy-duty truck with separately purchased service body and crane attachments. In connection with the draw on the line of credit, the parties amended the loan agreement to add the truck, service body, and crane to the list of collateral and Wells Fargo filed an amendment to its financing statement to cover the truck and “all attachments, replacements, substitutions, additions and accessions” thereto. The debtor later applied for a certificate of title for the truck. Neither the application nor the certificate indicated Wells Fargo’s security interest.

Two years later, the debtor filed for bankruptcy protection. The truck was sold and litigation ensued between Wells Fargo and the trustee about who was entitled to the sale proceeds. The court treated the case as involving two issues: (i) whether Wells Fargo had a perfected security interest in the truck; and (ii) whether Wells Fargo had a perfected security interest in the service body and crane installed on the truck.

On the first issue, the court correctly ruled that Wells Fargo’s interest in the truck was unperfected because the interest was not noted on the certificate of title. See § 9-311(a)(2). Wells Fargo argued that its interest was nevertheless perfected pursuant to a Nebraska statute that provides that “a purchase-money security interest . . . in a vehicle is perfected against the rights of judicial lien creditors and execution creditors on and after the date the purchase-money security interest attaches.” Neb. Rev. Stat. § 60–164(2). However, the court indicated that the purpose of this provision was merely to clarify that lienholders who advance funds for the purchase of a motor vehicle are protected between the time the lien attached and is perfected. More important, the provision was enacted the year after Wells Fargo acquired its security interest in the truck and the court concluded that there was no basis for giving the enactment retroactive effect.

On the second issue, Wells Fargo argued that its amended financing statement, by expressly covering the truck and accessions thereto, perfected its security interest in the service body and crane. It is on this issue that the court went astray. The court looked to § 9-335(d), which provides that “a security interest in an accession is subordinate to a security interest in the whole which is perfected by compliance with the requirements of a certificate-of-title statute.” Interpreting this provision, the court ruled that because the truck was titled after the service body and crane were installed and thereby became accessions, “any perfection by title controls so that subsequent creditors need check only the title records, rather than the title records and the U.C.C. records.” Based on this ruling, the court concluded that the bankruptcy trustee’s rights as a lien creditor with respect to the service body and crane take priority.

The court’s analysis is flawed. Section 9-335(d) is a priority rule, not a perfection rule. Indeed, it is about priority among secured parties, not priority between a secured party and a lien creditor. Thus, it has no relevance to a bankruptcy trustee’s rights. Indeed, § 9-335 as a whole says very little about perfection. Its only clause relevant to perfection is subsection (b), which provides

See § 9-102(a)(1). Unfortunately, the court confused rules on priority with rules on perfection and may have reached the wrong result.
that “[i]f a security interest is perfected when the collateral becomes an accession, the security interest remains perfected in the collateral."

In fact, Wells Fargo argued that subsection (b) applied, claiming that the truck was not subject to perfection under the titling statutes when it filed the amendment to its financing statement because no certificate of title had been issued and no application for a certificate had been delivered to the proper authorities. However, on this point, Wells Fargo confused the rule on governing law with the rule on perfection. Prior to submission of an application for a certificate of title, the law governing perfection is the law of the debtor’s location; after submission of the application, the governing law is the law of the state in which the application is submitted. See § 9-303. But in either case, if the applicable law requires compliance with a certificate of title statute, then filing a financing statement will not be effective to perfect the security interest. See § 9-311(a)(2). Thus, subsection (b) was simply not relevant to the perfection issue and the court was correct in so ruling.

However, that ruling does not dispose of the issue. Whether Wells Fargo’s security interest in the service body and crane was perfected is actually an interesting and difficult question. The debtor took possession of the truck, with the service body and crane installed thereon, before Wells Fargo filed its amended financing statement. Thus, Wells Fargo’s security interest in the service body and crane would be perfected only if filing remained an effective perfection step after those items of equipment became accessions to the truck. Because Article 9 defers to certificate of title laws only to the extent that those laws require notation on a certificate of title as a condition or result of perfection, see § 9-311(a)(2), presumably this is an issue on which Nebraska’s certificate of title statute must be consulted. If the act is silent as to accessions to titled vehicles, then filing a financing statement should remain a proper way to perfect a security interest in those accessions and Wells Fargo’s filing would have been sufficient. Thus, Wells Fargo’s security interest in the service body and crane may or may not have been perfected. What is clear, however, is that nothing in § 9-335 speaks to this issue and certainly not the provision the court relied upon: § 9-335(d).

_In re Wilkinson_,
2012 WL 1192780 (Bankr. N.D.N.Y. 2012)

_In re Miller Brothers Lumber Co._,
2012 WL 1601316 (Bankr. M.D.N.C. 2012)

These two cases concerned the effect of a lapse in perfection of a security interest after the debtor entered bankruptcy. The Wilkinson court ruled that priority is settled as of the petition date, and thus the lapse in perfection did not affect priority over a competing secured party. The Miller Brothers court ruled that priority was not settled as of the petition date and that therefore the debtor in possession could use the strong arm powers to avoid the security interest. In fact, despite the seemingly inconsistent rulings, both decisions are wrong. Each court failed to appreciate how a loss of perfection affects priority under Article 9. Specifically, it can affect priority against a competing secured party but has no impact on the rights of a judicial lien creditor whose interest was acquired while the security interest was perfected.
The facts of the Wilkinson case can be summarized as follows. The debtor ran a dairy farm on his mother’s property. He purchased his mother’s dairy herd in 2005 and she retained a purchase-money security interest in the herd to secure the unpaid portion of the purchase price. The mother perfected the security interest by filing a proper financing statement in 2006. In 2009, the Farm Service Agency (“FSA”) acquired a security interest in the debtor’s herd and also perfected by filing.

The debtor filed for bankruptcy protection in 2010, when both security interests were perfected. In 2011, with the bankruptcy case still pending, the mother’s perfection lapsed. A few months later, the debtor sold the cows and an issue arose about who was entitled to the sale proceeds.

The FSA claimed that, under § 9-322(a)(2), it now had the senior security interest. In doing so, the FSA noted that revised Article 9 omitted from § 9-515 the bankruptcy tolling provision that had been included in former § 9-403(2), and that § 362(b)(3) provides that filing a continuation statement does not violate the automatic stay. Thus, nothing in the law prevented the mother from maintaining perfection or insulated her from the consequences of failing to do so. In response, the mother cited judicial opinions for the proposition that bankruptcy principles control priority and fix the rights of the debtor, creditors, and the trustee as of the time of the bankruptcy filing.

The court sided with the mother. In doing so, it relied in part on § 9-515 comment 4, which states that “if the debtor enters bankruptcy before lapse, the provisions of this Article with respect to lapse would be of no effect to the extent that federal bankruptcy law dictates a contrary result (e.g., to the extent that the Bankruptcy Code determines rights as of the date of the filing of the bankruptcy petition).” The court then cited to In re Bond Enterprises, Inc., 54 B.R. 366 (Bankr. D.N.M. 1985), and a case it relied upon, Lockhart v. Garden City Bank & Trust Co., 116 F.2d 658 (2d Cir. 1940), for the proposition that priorities are indeed established on the petition date.

What the court failed to realize, however, was that neither of these cases dealt with the rights of a competing secured party. Lockhart dealt with the rights of the trustee and Bond Enterprises dealt with the rights of the debtor in possession. Thus, each dealt with the rights of a person claiming the status of a lien creditor. But Article 9 itself treats lien creditors and secured parties very differently with respect to a competing secured party’s loss of perfection. When perfection lapses, the originally perfected security interest is deemed never to have been perfected as against “a purchaser of the collateral for value.” § 9-515(c). A secured party is a purchaser for value but a lien creditor is not. See § 1-201(b)(29), (30). Thus, a person who becomes a lien creditor when a security interest is perfected takes subject to that security interest and remains subject to it even if perfection subsequently lapses. See § 9-515 comment 3, ex. 2. See also § 9-317(a); In re Stetson & Assocs., Inc., 330 B.R. 613 (Bankr. E.D. Tenn. 2005). However, a competing secured party will find that its originally junior security interest has moved into a senior position. See § 9-515 comment 3, ex. 1. In short, by citing to and relying upon old and inapposite cases, the Wilkinson court misapplied the law.

Moreover, the court’s decision creates an anomalous result: the relative priority of the security interests will depend on whether the collateral is sold in bankruptcy or outside of it. According to the court’s decision, if the collateral is sold during bankruptcy, priority will be
accorded to the senior secured party whose perfection lapsed. Presumably, however, if the case is dismissed or relief from the stay is granted, and one or both of the secured parties disposes of the collateral outside of bankruptcy, Article 9 will control the priority issue, with the result that the senior secured party whose perfection lapsed will lose. Assuming this is correct, the parties will then have incentive to fight in bankruptcy about whether and when to allow the collateral to be sold. If the estate has no equity – which is when priority matters most – then the court has no reason to be involved in the sale and no basis on which to decide whether to sustain or overrule an objection to it.

The facts of the Miller Brothers case are even simpler. American Bank had a security interest in some of the debtor’s equipment and that interest was perfected by a financing statement filed in October 2006. The debtor filed a Chapter 11 bankruptcy petition in September 2011 and American Bank never filed a continuation statement. When American Bank filed a motion for relief from the stay or adequate protection, the debtor in possession objected.

The court’s analysis was quite brief. After noting that nothing in revised Article 9 prevents a financing statement from lapsing during the debtor’s bankruptcy and that § 362(b)(3) allows the secured party to file a continuation statement without violating the automatic stay, the court concluded that the bank’s perfection had lapsed. The court then added, without any analysis and despite that fact that the matter before it was not an avoidance action, that the debtor “may avoid American Bank’s security interest pursuant to its strong arm powers under Section 544.”

The court’s first conclusion – that perfection had lapsed – was correct. Its second conclusion about avoidance was wrong. The debtor in possession’s strong arm powers are based on its status as a lien creditor. See §§ 544(a)(1), 1107(a). But, as discussed above, a creditor who acquires a judicial lien on property subject to a perfected security interest does not obtain priority even if the security interest subsequently becomes unperfected.

For these reasons, the decisions in these cases were misguided and should not be relied upon.

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