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.

_Sunshine Heifers, LLC v. Moohaven Dairy, LLC_,


This is a fairly simple case in which the court probably reached the correct result but its reasoning was flawed. The case also helps reveal something important about the phrasing and structure of Article 9.

The issue in the case was whether a postpetition lease of 240 cows to a dairy farm for 48 months was a true lease or a disguised sale. The court ruled that the transaction was a true lease because it did not qualify as a secured transaction under the rule of § 1-203(b). Specifically, even though the transaction was not terminable by the dairy farm, the dairy farm had no option or obligation to renew the lease or to buy the cows, and the term of the lease did not exceed the economic life of the cows because data indicates that more than 57% of cows produce milk for longer than four years.

Unfortunately, as explained in a previous edition of this column, when subsection (b) of § 1-203 does not apply, that does not mean that the transaction is a lease; it merely means that the analysis falls back to the general, fact-specific standard of subsection (a). The court therefore erred in terminating the analysis, even if a complete review of the facts would not have changed the result.

It is interesting to note, however, that many courts have made this error. Let’s consider why. The language of § 1-203(b) is that of a major premise in a syllogism: If P, then Q. As we all know, the converse of such a premise – If not P, then not Q – is not necessarily true. Thus, the subsection is merely a sort of safe harbor. It provides a definite answer when the condition (P) is satisfied but no answer when the condition fails.

Article 9 contains quite a few of these safe harbors, see, e.g., §§ 9-504, 9-611(e), 9-612(b), 9-613(1), (5), 9-614(3), 9-627(b), (c), most of which are expressly identified as safe harbors in the comments, see §§ 9-504 cmt. 2, 9-611 cmt. 4, 9-612 cmt. 3, 9-613, cmt. 3, 9-614 cmt. 3. See also § 9-627(d) (making clear that compliance with subsection (c) is not required). Unfortunately, the comments to § 1-203 do not expressly identify subsection (b) of that section as a safe harbor. In fact, they describe the relationship between subsections (b) and (c), but say nothing about the relationship
of subsections (a) and (b). However, that silence in the comments does not alter the structure of the statutory text: subsection (a) is a general rule; subsection (b) is a specific rule for some, but not all cases. Thus, the inapplicability of subsection (b) does not provide an answer to the standard expressed in subsection (a). See also § 1-201(d) (containing another example of a sort of safe harbor: a nonexhaustive description – but not a definition – of what constitutes “nominal consideration”).

On the other hand, courts regularly – and properly – rely on the negative inference that can arise from a limited grant of permission. Consider a statement phrased as: If P, then you may Q. While the converse – If not P, then you may not Q – does not follow logically, it is nevertheless implied. Article 9 has several such rules. Perhaps the most obvious is the rule in § 9-609 that authorizes a secured party to repossess collateral without judicial process “if it proceeds without breach of the peace.” Courts universally understand this rule to mean that the secured party is in fact not authorized to proceed nonjudicially in a manner that does breach the peace. Other examples are contained in §§ 9-207(b)(4), 9-335(e), 9-603(a) and 9-604(c). See also In re Brady, 2014 WL 1330020 at *1 & n.12 (Bankr. E.D. Wash. 2014) (“the logical inference that can be drawn from 9-335 is that a tire merchant may not repossess accessions installed on an automobile if the automobile is subject to a secured claim of a creditor that is listed on the title”).

In essence, conditional rules of permission are best understood as implicitly containing the word “only”: Only if P, then you may Q. Cf. § 9-610(c)(2) (so phrased in describing when a secured party is authorized to buy the collateral at a private disposition). But in rules such as § 1-203(b) that do not grant permission, there is no negative implication and courts should not treat the converse as correct. When the conditions of subsection (b) are not satisfied, the analysis of the sale-lease issue is incomplete and must return to the basic standard of subsection (a).

**Guaranty Bank & Trust Co. v. FGDI Division of Agrex, Inc., 2014 WL 1289466 (N.D. Miss. 2014)**

This case about improper joinder of a party was decided based on the perceived right of grain buyers to take free of a security interest in the grain. Unfortunately, the court overlooked a critical phrase in § 9-320(a) and reached the wrong conclusion.

The facts are relatively straight forward. Guaranty Bank & Trust Company, a citizen of Mississippi, claimed to have a security interest in the grain of a farmer, David Walker. Walker sold the grain to Agrex, Inc., a citizen of Kansas, which in turn sold it to two grain terminals, one or both of which were apparently located in Mississippi. The bank brought a conversion action against Agrex and the two grain terminals in state court. Agrex removed the case to federal court, asserting that the citizenship of the grain terminals should be disregarded because the bank had no reasonable basis for a cause of action against them. The bank sought to have the case remanded.

In considering the bank’s basis for joining the grain terminals, the court looked to § 9-320(a), which provides that a buyer in ordinary course of business, “other than a person buying farm
products from a person engaged in farming operations, takes free of a security interest created by the buyer’s seller, even if the security interest is perfected and the buyer knows of its existence.” Concluding that the grain terminals were buyers in ordinary course of business, the court readily concluded that the grain terminals took free and thus the bank had improperly joined them as defendants. The court’s very brief analysis focused on the fact that the grain terminals had bought from Agrex, not from Walker, and thus had not bought from a person engaged in farming operations.

While the court might well have been correct that the grain terminals were buyers in ordinary course of business, it was clearly wrong in concluding that they took free of the bank’s security interest under § 9-320(a). The very point that the court relied on to show that the grain terminals were protected by § 9-320(a) – that they purchased from Agrex, not Walker – in fact shows just the opposite. Section 9-320(a) allows a buyer to take free only of a security interest “created by the buyer’s seller.” Agrex did not create the security interest, Walker did. The court completely ignored this important limitation in § 9-320(a), even though the situation presented in this case is akin to that in comment 3, example 1 to § 9-320, in which the buyer did not take free from a security interest established by the seller’s seller.

It is possible that the court’s conclusion about priority was correct for a different reason. Although § 9-320(a) does not protect buyers who purchase from a person engaged in farming operations, the federal Food Security Act does. See 7 U.S.C. § 1631; U.C.C. § 9-320 cmt. 4. It is possible, therefore, that Agrex took free of the bank’s security interest under that statute, which would mean that the grain was already unencumbered when sold to the grain terminals. However, Agrex did not make this argument and the court did not consider it.

**Born v. Born,**


This is a case about strict foreclosure of a security interest and redemption rights in collateral. The secured creditor argued for a strict application of the UCC and although the secured creditor won, the court’s application of the UCC was anything but strict.

The facts can be summarized as follows. After a series of intra-family transactions, Sharon Born acquired a security interest in the stock of H.J. Born Stone, Inc. (“Born Stone”) and in Born Stone’s membership interests in a LLC to secure a debt. The promissory notes provided that the death of Sharon’s cousin, John, was an event of default. John died and his widow, Betty, contacted Sharon’s attorney about making payment. Sharon refused, relying on a term in the security agreement that provided:

[Sharon] shall accept the Collateral by giving notice of such fact to Stockholder in which case [Sharon] shall forthwith take possession of the Collateral and all interest of Stockholder therein shall be forfeited and shall cease and terminate, and neither [Sharon] nor Stockholder shall have an[y] further liability to the other under this Agreement.
Betty sued seeking to enjoin Sharon from taking control of the stock and membership interests. The trial court ruled for Sharon and Betty appealed.

The appellate court affirmed. The court began by interpreting the security agreement as limiting Sharon to a single remedy: accepting the collateral in full satisfaction of the debt. Noting that the procedure for conducting an acceptance cannot be waived, see § 9-602(10), the court then examined the parties’ conduct in reference to that procedure. First, the court concluded that Sharon had properly proposed to accept the collateral in satisfaction of the secured obligation even though her post-default letters to the debtor neither expressly stated that the debtor had the right to object nor indicated either the amount due or a means of calculating that amount. This ruling was correct. Nothing in § 9-620 requires that a proposal to accept collateral inform the debtor of the right to object or describe the secured obligation. Although 9-320 comment 4 indicates that a proposal “should specify the amount (or a means of calculating the amount . . . ) of the secured obligations to be satisfied,” the use of “should” rather than “shall” or “must” indicates that this is a permissive standard, not a requirement.

The court then dealt with whether the debtor had objected to the proposal. The trial court had ruled that, because the security agreement limited Sharon’s remedy to acceptance of the collateral in satisfaction of the secured obligation, the only way that the debtor could properly object was if, in addition to expressing objection, it redeemed the collateral within a reasonable time. The appellate court apparently agreed. It then concluded that the debtor’s tender of payment of some of the secured obligation and some of the collateral was not a proper tender. Hence, Sharon was now the owner of the collateral.

There are several problems with this analysis, but let’s begin with what is right. To the extent that the clause in the security agreement could be interpreted as providing for Sharon to automatically become the owner of the collateral upon default, it would be unenforceable. Article 9 does not permit that. The secured party must either conduct a disposition or collection of the collateral, or propose an acceptance of the collateral in satisfaction of the secured obligation. These rules cannot be waived and the latter requires consent after default. See §§ 9-602, 9-620(a)(1). Although a few courts have, without much analysis, ruled to the contrary, e.g., Corsair Special Situations Fund, L.P. v. Engineered Framing Systems, Inc., 694 F. Supp. 2d 449 (D. Md. 2010) (because patent security agreement provided that the creditor’s interest would “become an absolute assignment” after debtor defaulted, and debtor had defaulted, the security interest had become an absolute assignment of the patent), they are simply wrong. Cf., In re Crossover Financial I, LLC, 477 B.R. 196 (Bankr. D. Colo. 2012) (clause in security agreement providing that, upon default, the debtor’s rights as the sole member of limited liability company to vote and give consents, waiver or ratifications shall cease and that the secured party vote any or all of the pledged interest did not operate automatically; Colorado law requires a secured party to enforce the security agreement and become admitted as a member before the secured party may exercise voting rights associated with a membership interest pledged as collateral). Thus, the court correctly looked to whether Sharon had conducted a proper acceptance of the collateral.

To accept the collateral in full or partial satisfaction of the secured obligation, the debtor’s
post-default consent is required. A communication of objection negates consent. Nothing in the Code indicates, however, that the debtor must also redeem the collateral to make a proper objection. To the extent that the security agreement limited Sharon’s rights upon default to accepting the collateral, it might have been a remarkably foolish provision (from Sharon’s perspective), but is hardly a reason to interpret it as requiring redemption. Finally, and most important, the court’s notion that redemption (by tendering full payment of the secured obligation) must occur within a reasonable time is simply not consistent with § 9-623. That section expressly states that the debtor has the right to redeem until the secured party conducts a disposition, collection, or acceptance. § 9-623(c). Moreover, that rule too is not waivable. § 9-602(11). Thus, the debtor’s right to redeem simply does not expire after a reasonable time passes.

In short, while the court may have been correct that the debtor failed to redeem the collateral by tendering less than all of the secured obligation, that failure did not terminate the debtor’s right to redeem. Because a debtor is not required to redeem collateral to properly object to a proposal to accept the collateral, the court’s conclusion that Sharon was now the owner of the collateral was wrong.


This case is about whether the seller of a truck, a trailer, and a bulldozer retained a security interest in all three items even though the buyer did not execute a security agreement and the bill of sale did not mention a security interest.

The court properly observed that all the documents relating to the transaction should be read together. Among these were the title documents for the truck and trailer, which identified the seller as a lienholder. The buyer conceded that those two items were encumbered but claimed there was no security interest in the bulldozer.

In concluding that there was, the court quoted language from § 9-203 comment 3: “a bill of sale, although absolute in form, may be shown in fact to have been given as security.” It then concluded that the bill of sale, coupled with the title documents for the other items and the seller’s testimony, was sufficient.

The court’s error was in its fundamental misunderstanding of the quoted language. Just as a deed of real property might be absolute on its face and yet in reality be given as security – by the grantor to the grantee – a bill of sale might appear to be an outright transfer – by the seller to the buyer – yet in fact be a transfer of less than all rights. That is, the buyer might really be a lender and the seller might be transferring title to property as collateral. In short, the comment acknowledges that a seller might be the debtor in a secured transaction, so that a transaction structured as follows:

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     Seller -> Bill of Sale -> Buyer
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In such a transaction, the bill of sale, which clearly transfers property rights to the buyer, actually transfers fewer rights than it purports to but it nevertheless has rights flowing in the same direction. See also § 9-203 cmt. 3 (“A debtor may show by parol evidence that a transfer purporting to be absolute was in fact for security”). The comment does not state or imply, as the court thought it did, that a bill of sale could cause a security interest to flow in the opposite direction. The court parroted the words of the comment without any understanding about what they mean.

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