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Kentucky Law Survey: Commercial Law

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COMMERCIAL LAW

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INTRODUCTION

The Kentucky Court of Appeals rendered numerous commercial law decisions in the 1979-80 survey period. This Survey will consider a small number of those decisions and will focus on their application of the Uniform Commercial Code (U.C.C.).[1] It will be noted that Kentucky courts have often followed a narrow, "statute by statute" approach to code interpretation rather than considering the underlying purposes and policies of the U.C.C.[2] As a result, Kentucky decisions are often at variance with decisions from other U.C.C. states as well as at odds with the stated policies of the U.C.C.[3]

I. ESTOPPEL AND ARTICLE TWO'S STATUTE OF FRAUDS

Estoppel has long been used by Kentucky courts to reach equitable results in contract cases.[4] Although promissory es-

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[1] The Kentucky version of the Uniform Commercial Code is contained in chapter 355 of the KENTUCKY REVISED STATUTES [hereinafter cited as KRS]. For purposes of this article, the terms "Uniform Commercial Code," "U.C.C." and "code" will be used interchangeably and sections of this body of law will be cited by U.C.C. section number in text. Unless otherwise indicated, all references are to the 1962 official text.

Other cases decided during the survey year worthy of note are: Owensboro Nat'l Bank v. Crisp, 608 S.W.2d 51 (Ky. 1980) (interrelationship of the "imposter rule" and bank negligence under article three); Kentucky Club, Inc. v. Fifth Third Bank, 590 S.W.2d 686 (Ky. 1979) (Court refused to apply article six, bulk transfers, to the sale of a restaurant-bar business); Riley v. West Ky. Prod. Credit Assoc., 603 S.W.2d 916 (Ky. Ct. App. 1980) (emphasizing the aversion of Kentucky courts to awarding attorney's fees under the U.C.C. in the absence of an express contractual provision or a clear statutory mandate independent of code provisions). For an excellent discussion of *Crisp*, see Comment, *The Role of Negligence in Section 3-405 of the Uniform Commercial Code:* Owensboro National Bank v. Crisp, 69 KY. L.J. 143 (1980-81).

[2] These purposes and policies are set out in KRS § 355.1-102 (1972) as well as in the official comments of the National Conference of Commissioners on Uniform State Laws.

[3] For a recent discussion of this problem, see Minahan, *The Eroding Uniformity of the Uniform Commercial Code*, 65 KY. L.J. 799 (1976-77).

[4] *See, e.g.*, Wright v. Williams, 77 S.W. 1128 (Ky. 1904) and cases cited therein. In *Wright*, the Court employed elements of estoppel to deny appellee recovery of a 10-foot alleyway that had been represented to a prior purchaser as part of the parcel

toppel has never been explicitly adopted in Kentucky,[5] the Kentucky Supreme Court used this concept in *Meade Construction Co. v. Mansfield Commercial Electric, Inc.*[6] In *Meade*, a contractor relied upon the oral bid of a subcontractor, who later refused to perform. The defendant subcontractor did not raise a Statute of Frauds defense nor was this defense considered by the Court, which granted relief to the plaintiff contractor on an estoppel theory.

A similar situation arose in *C. G. Campbell & Son v. Comdeq Corp.*,[7] a 1979 Kentucky Court of Appeals case. In *Comdeq*, a contractor relied upon the oral, telephoned bid of a subcontractor, who later discovered an error in his bid price and refused to perform. The contractor sued for damages, and the defendant subcontractor raised a Statute of Frauds defense. The court distinguished *Meade* on this basis[8] and refused to grant equitable relief. The article two statute of frauds, U.C.C. section 2-201,[9] was applied very strictly to find

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but that the deed failed to convey.

[5] *See* Meade Constr. Co. v. Mansfield Commercial Elec., Inc., 579 S.W.2d 105 (Ky. 1979). For a discussion of *Meade*, see Comment, *An "Equivocal Estoppel": The Strange Career of Promissory Estoppel in Kentucky Contract Law*, 68 KY. L.J. 184 (1979-80). While "equitable estoppel" is based upon an affirmative misrepresentation and is available only as a defense, "promissory estoppel" involves a promise of future action and can be both a defense and a cause of action. *Id.* at 186 n.10. *See generally* Annot., 48 A.L.R.2d 1069 (1956) (a discussion of promissory estoppel).

[6] 579 S.W.2d at 105.

[7] 586 S.W.2d 40 (Ky. Ct. App. 1979).

[8] *Id.* at 41.

[9] KRS § 355.2-201 (1972) states:

> (1) Except as otherwise provided in this section a contract for the sale of goods for the price of $500 or more is not enforceable by way of action or defense unless there is some writing sufficient to indicate that a contract for sale has been made between the parties and signed by the party against whom enforcement is sought or by his authorized agent or broker. A writing is not insufficient because it omits or incorrectly states a term agreed upon but the contract is not enforceable under this paragraph beyond the quantity of goods shown in such writing.
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> (2) Between merchants if within a reasonable time a writing in confirmation of the contract and sufficient against the sender is received and the party receiving it has reason to know its contents, it satisfies the requirements of subsection (1) against such party unless written notice of objection to its contents is given within ten (10) days after it is received.
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> (3) A contract which does not satisfy the requirements of subsection (1) but which is valid in other respects is enforceable

there was no contract absent a writing signed by the party to be charged,[10] in this case, the subcontractor.

The *Comdeq* court reasoned that the only legislatively intended exceptions to the harsh general rule in U.C.C. section 2-201(1) are contained in U.C.C. section 2-201(2) and (3)[11] and rejected any attempt "to judicially amend [the] statute."[12] There is no indication, however, that the Kentucky legislature even considered the application of promissory estoppel to the Statute of Frauds in article two. The Legislative Research Commission made no reference to the problem in its comments to U.C.C. section 2-201.[13] Furthermore, there is no discussion in *Comdeq* of section 1-103,[14] which allows general principles of estoppel to supplement other code provisions.[15]

(a) if the goods are to be specially manufactured for the buyer and are not suitable for sale to others in the ordinary course of the seller's business and the seller, before notice of repudiation is received and under circumstances which reasonably indicate that the goods are for the buyer, has made either a substantial beginning of their manufacture or commitments for their procurement; or

(b) if the party against whom enforcement is sought admits in his pleading, testimony or otherwise in court that a contract for sale was made, but the contract is not enforceable under this provision beyond the quantity of goods admitted; or

(c) with respect to goods for which payment has been made and accepted or which have been received and accepted (KRS 355.2-606).

Id.

[10] 586 S.W.2d at 41.

[11] *Id.* The court declared that the *exclusive* exceptions to the general Statute of Frauds provision of KRS § 355.2-201(1) appear in subsections (2) and (3). For the text of this statute, see note 9 *supra.*

[12] 586 S.W.2d at 41.

[13] KENTUCKY LEGISLATIVE RESEARCH COMMISSION, RESEARCH PUBLICATION No. 49, UNIFORM COMMERCIAL CODE: ANALYSIS OF EFFECTS ON EXISTING KENTUCKY LAW 30-32 (1957) [hereinafter cited as LRC].

[14] KRS § 355.1-103 (1972) provides:

Unless displaced by the particular provisions of this chapter, the principles of law and equity, including the law merchant and the law relative to capacity to contract, principal and agent, estoppel, fraud, misrepresentation, duress, coercion, mistake, bankruptcy, or other validating or invalidating cause shall supplement its provisions.

Id.

[15] Other jurisdictions that have considered the specific question of applicability of estoppel to the Statute of Frauds have used § 1-103 to bring those considerations to bear. *See, e.g.,* Warder & Lee Elevator, Inc. v. Britten, 274 N.W.2d 339 (Iowa 1979); Sacred Heart Farmers Coop. Elevator v. Johnson, 232 N.W.2d 921 (Minn. 1975).

In conditioning the use of estoppel principles solely on the illusive concept of legislative intent as gleaned from a strict focus upon the words of the statute, the court misconceives the origins and purposes of estoppel. Equitable considerations are not grounded in legislative intent but rest upon judicially administered concepts of fairness.[16] Although equitable exceptions to legislative determinations should be employed prudently, they should nonetheless be applied when an unfair result would otherwise occur.[17] This is particularly true under the harsh conditions of U.C.C. section 2-201(1), because, as one commentator has noted, "no statute of frauds yet drafted . . . has been able to anticipate every combination of facts which requires decision."[18]

Still further support for the application of estoppel to U.C.C. transactions may be found in two paragraphs of U.C.C. section 1-102(2), which express purposes and policies of the code.[19] Paragraph (b) states the policy of "continued expansion of commercial practices through custom, usage and agreement of the parties." Kentucky courts have recognized the

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For a discussion of the applicability of § 1-103 in introducing general equitable principles into the U.C.C., see Summers, *General Equitable Principles Under Section 1-103 of the Uniform Commercial Code*, 72 NW. L. REV. 906 (1978).

[16] *See, e.g.*, Trimble v. King, 114 S.W. 317 (Ky. 1908). *See generally* 28 AM. JUR.2d *Estoppel and Waiver* § 28 (1966). As the court in Janke Constr. Co. v. Vulcan Materials Co., 386 F. Supp. 687, 697 (W.D. Wis. 1974), stated, "The statute of frauds relates to the enforceability of *contracts*; promissory estoppel relates to *promises* which have no contractual basis and are enforced only when necessary to avoid injustice."

[17] Smith v. Ash, 448 S.W.2d 51 (Ky. 1969).

[18] R. NORDSTROM, HANDBOOK OF THE LAW OF SALES § 30 (1970).

[19] When considering the application of the Statute of Frauds to a particular case, one must "take account of the broader and deeper policy questions that underlie the statute." L. VOLD, HANDBOOK OF THE LAW OF SALES § 14 (1959).

The purposes and policies of the U.C.C. are set out in KRS § 355.1-102 (1972):

> (1) This chapter shall be liberally construed and applied to promote its underlying purposes and policies.
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> (2) Underlying purposes and policies of this chapter are
>
> (a) to simplify, clarify and modernize the law governing commercial transactions;
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> (b) to permit the continued expansion of commercial practices through custom, usage and agreement of the parties;
>
> (c) to make uniform the law among the various jurisdictions.

Id. *See* KRS § 355.1-102 (1972) and comment 1; LRC, *supra* note 13, at 4.

availability of estoppel in a number of areas.[20] Even in the subcontractor bid situation, the Kentucky Supreme Court has sanctioned the use of estoppel.[21] Yet the *Comdeq* court declined to use the principle in a nearly identical fact situation simply because the case arose under the U.C.C.[22] Such a result clearly conflicts with the code's continued expansion policy as well as with its policy of reflecting the commercial transaction as it develops in the reality of modern business dealings.[23]

Paragraph (2)(c) of U.C.C. section 1-102 further states the policy of "making uniform the law among the various jurisdictions."[24] A majority of jurisdictions has applied promissory or equitable estoppel to avoid the harsh effects of U.C.C. section 2-201(1),[25] and most commentators have recommended this approach.[26] Although a minority of jurisdictions

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[20] *See, e.g.*, Wright v. Williams, 77 S.W. 1128 (Ky. 1904) and cases cited therein. *See also* Smith v. Ash, 448 S.W.2d 51 (Ky. 1969). The *Smith* decision addresses the issue of applicability of *equitable* estoppel to the Statute of Frauds requirement for land conveyances. For a discussion of *promissory* estoppel as a basis for the avoidance of Statutes of Frauds, *see generally* Annot., 56 A.L.R.3d 1037 (1974).

[21] 579 S.W.2d at 105.

[22] That this distinction makes no sense on a policy basis was the basic argument of the dissent in C.R. Federick, Inc. v. Borg-Warner Corp., 552 F.2d 852 (9th Cir. 1977) (Wallace, Cir. Judge, dissenting). The Ninth Circuit reasoned that the previous California decision in Drennan v. Star Paving Co., 333 P.2d 757 (Cal. 1958), which applied promissory estoppel to the contractor/subcontractor situation, was inappropriate because *Drennan* involved a bid for both goods and services, and thus U.C.C. § 2-201 would not apply.

[23] This policy is exemplified by the U.C.C.'s emphasis upon transactions "between merchants," KRS § 355.2-104 (1972), and its focus upon "course of dealing" and "usage of trade." KRS § 355.1-205 (1972). Note also the official comments to these sections of the U.C.C.

[24] KRS § 355.1-102(2)(c) (1972).

[25] *See, e.g.*, Janke Constr. Co. v. Vulcan Materials Co., 386 F. Supp. at 687 (contractor/subcontractor bid situation); Jenkins & Boller Co. v. Schmidt Iron Works, Inc., 344 N.E.2d 275 (Ill. App. Ct. 1976) (contractor/subcontractor suit over effect of architect's specifications); Warder & Lee Elevator, Inc. v. Britten, 274 N.W.2d at 339 (grain sale); Decatur Coop. Assoc. v. Urban, 547 P.2d 323 (Kan. 1976) (grain sale); Sacred Heart Farmers Coop. Elevator v. Johnson, 232 N.W.2d at 921 (grain sale); Farmers Coop. Assoc. v. Cole, 239 N.W.2d 808 (N.D. 1976) (grain sale); Farmers Elevator Co. v. Lyle, 238 N.W.2d 290 (S.D. 1976) (grain sale).

[26] R. NORDSTROM, *supra* note 18, at § 30; J. WHITE & R. SUMMERS, HANDBOOK OF THE LAW UNDER THE UNIFORM COMMERCIAL CODE § 206 (2d ed. 1980) [hereinafter cited as WHITE & SUMMERS]; Summers, *supra* note 15, at 906; Note, *Promissory Estoppel, Equitable Estoppel and Farmer as a Merchant: The 1973 Grain Cases and the UCC Statute of Frauds*, 1977 UTAH L. REV. 59; Note, *The "Firm Offer" Problem*

has rejected the application of estoppel to U.C.C. section 2-201(1),[27] this rejection may have been due to "a different view of the doctrine of promissory estoppel rather than because of any perceived statutory bar to its use."[28]

The Kentucky Court of Appeals' strict application of U.C.C. section 2-201 is particularly striking when contrasted with the Kentucky Supreme Court's position in *Meade* and the court of appeals' own decision in *Harry Harris, Inc. v. Quality Construction Co.*[29] Six months after the *Comdeq* decision, the court of appeals, in *Harris,* applied estoppel to assess damages against a breaching subcontractor. The crucial factor and point of departure from the *Comdeq* rationale was the unavailability of the U.C.C. section 2-201 Statute of Frauds defense, since the defendant subcontractor had not raised it.[30] Thus, in two non-U.C.C. cases promissory estoppel principles were applied to enforce oral contracts.[31] The issue of the doc-

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in Construction Bids and the Need for Promissory Estoppel, 10 WM. & MARY L. REV. 212 (1968); Comment, *Promissory Estoppel and the Statute of Frauds in California,* 53 CALIF. L. REV. 590 (1965); Recent Decisions, 48 MISS. L.J. 883 (1977); Comment, 16 WASHBURN L.J. 230 (1976). *Contra,* Note, *Farmer Is Not A Merchant But Promissory Estoppel May Bar the Application of the Statute as a Defense,* 25 KAN. L. REV. 318 (1977).

[27] *See, e.g.,* 552 F.2d at 852; Cox v. Cox, 289 So.2d 609 (Ala. 1974); Farmland Serv. Corp. v. Klein, 244 N.W.2d 86 (Neb. 1976).

[28] 274 N.W.2d at 341 (citing Cox v. Cox, 289 So.2d 609 (Ala. 1974); Del Hayes & Sons, Inc. v. Mitchell, 230 N.W.2d 588 (Minn. 1975); 244 N.W.2d at 86). These cited cases held promissory estoppel inapplicable because the courts perceived promissory estoppel as either a substitute for consideration or as applying when no contract in fact exists.

[29] 593 S.W.2d 872 (Ky. Ct. App. 1979).

[30] "Unlike [Comdeq], the appellant in this case has not raised the application of KRS 355.2-201, and therefore we have not considered it." *Id.* at 874.

[31] It is likely that other variations of the contract bidder situation may arise. For example, KRS § 355.2-201(3)(a) (1972) protects the seller of specially manufactured goods after he has begun the manufacturing process in reliance upon the buyer's order. What if, instead of manufacturing the special goods, the seller who does not keep those special items in stock and does not manufacture them orders them from a third party before the buyer repudiates? *See* Holahan, *Contract Formalities and the Uniform Commercial Code,* 3 VILL. L. REV. 1, 16 (1957). Furthermore, why should protection be extended only to the seller of specially manufactured goods? Does the contractor who must rely upon the good faith of the subcontractor in a construction bidding situation not stand in a similar position to a seller who relies upon the good faith order of the buyer of specially manufactured goods? The *Comdeq* court failed to consider these questions of equity.

trine's application in code cases remains to be resolved by the Kentucky Supreme Court, and it seems clear that the same considerations guiding the Court in *Meade* should control in U.C.C. cases also.[32]

II. KENTUCKY REVISED STATUTES SECTION 446.060(1) AND THE DEFINITION OF "SIGNED" IN U.C.C. SECTION 1-201(39)

In contrast to the *Comdeq* decision, in which the Kentucky Court of Appeals refused to apply extra-code equitable principles to militate against harsh code results, another panel of that court did use extra-code principles of statutory construction in *R. C. Durr Co. v. Bennett Industries, Inc.*[33] Bennett, a fabricator of heavy steel, sent a written offer to supply steel to Durr for construction of two interstate highway overpasses, pursuant to Durr's contract with the Department of Transportation. A Durr official accepted the offer by signing in the space provided. Beneath the signature lines, the following statement appeared: "This quotation is subject to the terms and conditions on the reverse side hereof." On the back of the document were twenty paragraphs and conditions of the offer including a limitation on Bennett's liability for liquidated and consequential damages.[34] Subsequently Bennett supplied the requested steel but, because of alleged delays in delivery and defects in the product, Durr refused to pay the contract price. Bennett instituted suit for payment, and Durr counterclaimed for damages. The circuit court granted summary judgment to Bennett and dismissed the counterclaim.

The court of appeals reversed, focusing on the subscrip-

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[32] Another question the *Comdeq* court did not address was the possible application of KRS § 355.2-201(3)(b) (1972), which provides that if the party against whom enforcement is sought admits that a contract was made, the contract is enforceable. See note 9 *supra* for the text of this provision. The *Comdeq* court indicated that there was no dispute as to the facts. It is unclear however, whether an oral contract was ever formed. If an oral contract *was* formed, admission of this fact in defendant's pleadings would satisfy the Statute of Frauds.

[33] 590 S.W.2d 338, 339 (Ky. Ct. App. 1979).

[34] KRS § 355.2-719 (1972) allows for contractual modifications or limitation of liquidated damages subject to KRS § 355.2-718 (1972), which provides a standard of reasonableness and which provides for consequential damages subject to a standard of unconscionability.

tion requirement of Kentucky Revised Statutes (KRS) section 446.060(1). That section provides: "When the law requires any writing to be signed by a party thereto, it shall not be deemed signed unless the signature is subscribed at the end or close of the writing."[35] The court reasoned that the placement of a signature at the close of a writing raised the inference that the signer intended to authenticate and to be bound by that portion of the writing above the signature.[36] Durr, therefore, was not bound by the clauses limiting Bennett's liability that appeared on the back of the form.

The crucial issue in *Durr* is the relationship of KRS section 446.060(1) to U.C.C. section 1-201(39), the U.C.C.'s definition of "signed." That code section states that " 'signed' includes any symbol executed or adopted by a party with present intention to authenticate a writing."[37] The court of appeals examined U.C.C. section 1-201(39) but concluded that it "relate[d] to what constitutes a valid signature, not to where the signature must be placed."[38] Apparently KRS section 446.060(1) answers the latter question. This simplistic view fails to consider the intent underlying the two provisions.

KRS section 446.060(1) was originally enacted by the 1850 session of the Kentucky General Assembly as a subchapter of "An Act to Revise the Statutes" entitled "Construction of Statutes."[39] No sufficient history of the act is available to determine what the legislature intended this provision to accomplish.[40] Nevertheless, the provision did abro-

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[35] KRS § 446.060(1) (1972).

[36] 590 S.W.2d at 339-40. This is the common interpretation of the purpose of KRS § 446.060(1) (1972). *See* Gentry's Guardian v. Gentry, 293 S.W. 1094 (Ky. 1927).

[37] KRS § 355.1-201(39) (1972). Prior to *Durr* only one other Kentucky case, Childers & Venters, Inc. v. Sowards, 460 S.W.2d 343 (Ky. 1970), had alluded to a possible relationship between KRS § 446.060(1) (1972) and KRS § 355.1-201(39) (1972). This case involved exclusions of implied warranties of fitness appearing on the reverse side of a contract for the sale of a truck. Unlike *Durr*, the provisions incorporating these exclusions into the body of the contract were printed *above* the signature of the buyer. Therefore, the Court found it unnecessary to decide whether the statute was applicable to code transactions, since the doctrine of incorporation by reference, which survived KRS § 446.060(1), brought the addition to the contract into the body. *See* Kelley v. J.R. Rice Realty Co., 32 S.W.2d 28 (Ky. 1930).

[38] 590 S.W.2d at 340.

[39] 1850 Ky. Acts, Vol. 1, 212, 235-38.

[40] Note, *Place of Maker's Signature on Bill or Note,* 16 KY. L.J. 159, 160 (1928).

gate the common law principle that a signature could appear on *any* part of the document if made with the intent and purpose of authenticating or giving effect to the document.[41] Many Kentucky courts, however, refused to require more than "substantial compliance" with the new statute.[42] According to these courts, the purpose underlying KRS section 446.060(1) was to supply a "logical inference that the writing to which it is thus appended expresses all which the signer wished to authenticate and to which he intended to be bound, and that nothing has been added to the writing which the signer did not wish to so authenticate."[43] The requirement eliminated the need to inquire into the signer's intent and allowed courts to avoid questioning whether the writing was a preliminary draft or a completed document.[44] It appears, therefore, that KRS section 446.060(1) was designed as a legislative device to provide the courts with a simple rule for determining the *intent* of the signer and was not intended merely as a rule for placement of signatures.

In modern commercial transactions, and especially those in which merchants are involved,[45] the need to determine when there is "intent" to finalize an agreement has largely vanished. Documents passing from party to party often seek

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[41] 293 S.W. at 1094; Note, *End or Close of Promissory Note Within Meaning of Kentucky Statutes Section 468 (KRS 446.060)*, 31 KY. L.J. 350 (1943). *See generally* 72 AM.JUR.2d *Statute of Frauds* §§ 360-61 (1974).

[42] *See, e.g.*, Zimmerman v. Segal, 155 S.W.2d 20 (Ky. 1941) (signature on a note); 293 S.W. at 1094 (signature on a deed); Lucas v. Brown, 219 S.W. 796 (Ky. 1920) (signature on a will). From the outset the courts did not adopt a literal construction of this statute. Note, *supra* note 41, at 350. A survey of the cases decided under KRS section 446.060(1) (1972) indicates that twice as many cases were excepted from the rule for substantial compliance as were found to come within the rule. The former cases usually relied upon some other indicia of the signer's intent to validate the signature. *See, e.g.*, Antle v. Haas, 251 S.W.2d 290 (Ky. 1952); Parrott v. Parrott's Adm'x, 110 S.W.2d 272 (Ky. 1937); Hays v. Marshall, 48 S.W.2d 540 (Ky. 1932); Graham v. Edwards, 173 S.W. 127 (Ky. 1915). *But see, e.g.*, Miller's Ex'r v. Shannon, 299 S.W.2d 103 (Ky. 1957); Kaiser v. Jones, 163 S.W. 741 (Ky. 1914).

[43] 293 S.W. at 1094.

[44] Teater v. Newman, 472 S.W.2d 696, 699 (Ky. 1971). This reasoning was applied to wills in the *Teater* case but is also applicable to other documents.

[45] See KRS § 355.2-207 (1972), U.C.C. § 2-207 comment 1, and KRS § 355.2-204 (1972) for the U.C.C.'s concept of modern commercial transactions. For a discussion of "The Concept of Professionalism" in the code, see 3 BENDER'S UNIFORM COMMERCIAL CODE SERVICE § 1.02 (1980 and Supp.).

to impose advantageous terms after the basic agreement has been reached and performance has begun. Even when terms of an agreement are not specified, the U.C.C. provides tools to ascertain the actual agreement, or, if that is unascertainable, supplies the missing contract terms through its own gap-filling provisions.[46] For these reasons, it is no longer essential to identify the extent of an agreement through signature placement. Recognizing this, the drafters of U.C.C. section 1-201(39) readopted the common law,[47] making the code provisions antithetical to KRS section 446.060(1).

The use of a formalistic test to determine intent is not only unnecessary, but may disrupt the smooth functioning of the U.C.C. For example, assume that both Durr and Bennett met the requirements of "merchants" under the code.[48] If Durr made no response to the written "confirmation" that Bennett sent and Bennett proceeded to manufacture and deliver the requested steel, Durr could have been bound under U.C.C. section 2-201(2).[49] Furthermore, the terms of the written contract to which Durr failed to object may have been used to establish the terms of the oral agreement.[50] It is ironic

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[46] See part 3 of article 2 for the U.C.C.'s gap-filling provisions.

[47] For a discussion of common law authentication, see the text accompanying note 41 *supra*. "The Code expressly 'deformalizes' the signature requirement." WHITE & SUMMERS, *supra* note 6, at § 2-4.

[48] KRS § 355.2-104(1) (1972) provides:

> "Merchant" means a person who deals in goods of the kind or otherwise by his occupation holds himself out as having knowledge or skill peculiar to the practices or goods involved in the transaction or to whom such knowledge or skill may be attributed by his employment of an agent or broker or other intermediary who by his occupation holds himself out as having such knowledge or skill.

Id.

[49] For the text of § 2-201, see note 9 *supra*.

[50] Shpilberg v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 535 S.W.2d 227 (Ky. 1976). The Court discussed the comment to KRS § 355.2-201 (1972) that states that the receipt of a writing without objection only prevents the Statute of Frauds defense from being claimed, and that the burden is still on the one who seeks performance to prove the contract and terms. The Court stated: "[T]he comment [to KRS § 355.2-201] obviously does not mean that the *writing*, which under the statute is required to be sufficient to 'indicate that a contract has been made,' is not acceptable *evidence* of the fact that a contract was made." The Court continued: "[I]f the writing contains all of the essential elements of a contract . . . it should be treated as conclusive evidence of the existence of the contract, subject to attack only on the grounds on which

that Durr might have been bound to the whole contract by not signing, while under the court of appeals' analysis, after signing, he is liable only for portions of the contract above his signature.

U.C.C. section 1-201(39), like KRS section 446.060(1), was designed to focus on the intent of the signer, but U.C.C. section 1-201(39), unlike KRS section 446.060(1), recognizes that the intent of the signer should not be obscured with undue formalism.[51] The Legislative Research Commission (LRC) explicitly considered the interrelation of KRS section 446.060(1) and U.C.C. section 1-201(39), stating that "[t]he broadening of the terms 'signed' and 'signature' may alter present law."[52] The LRC comment also made reference to the U.C.C. comment that states that the signature "*may be on any part of the document* and in appropriate cases may be found in a billhead or letterhead."[53]

In addition to overlooking the specific comments of the LRC, the court of appeals in *Durr,* as in *Comdeq,* failed adequately to consider the U.C.C.'s underlying policy "to make uniform the law among the various jurisdictions."[54] The Kentucky Supreme Court, in fact, early in the history of the U.C.C. in Kentucky, recognized that adoption of the U.C.C. indicated a "legislative policy to join with other states in achieving uniformity . . . unfettered by anachronisms."[55] The

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a written contract may be attacked." 535 S.W.2d at 229-30.

[51] "The question always is whether the symbol was executed with present intention to authenticate the writing." U.C.C. § 1-201 comment 39.

[52] LRC, *supra* note 13, at 14.

[53] U.C.C. § 1-201 comment 39 (emphasis added). Kentucky courts have frequently referred to the Commissioner's comments regarding questions of interpretation of the U.C.C. *See, e.g.,* Cessna Fin. Corp. v. Skyways Enterprises, 580 S.W.2d 491 (Ky. 1979); General Acc. Fire & Life Assur. Corp. v. Citizens Fid. Bank & Trust Co., 519 S.W.2d 817 (Ky. 1975); White v. Winchester Land Dev. Corp., 584 S.W.2d 56, 59 n.3 (Ky. Ct. App. 1979).

[54] KRS § 355.1-102 (1972). See note 19 *supra* for the text of this provision. For a discussion of the applicability of § 1-102 in another context, see text accompanying notes 24-32 *supra.*

[55] Lincoln Bank & Trust Co. v. Queenan, 344 S.W.2d 383, 385 (Ky. 1961). In *Queenan,* the Court refused to apply the provisions of three pre-code statutes to the KRS § 355.9-402 (1972) requirements of a financing statement. The Court did allow a fourth statute, relating to certificates of title for motor vehicles, to affect code provisions but only after noting several factors that tended to indicate legislative intent.

Court adopted a rule of construction "that the Code is plenary and exclusive except where the legislature has clearly indicated otherwise."[56] Yet, the court of appeals in *Durr*, by applying a strict subscription requirement to section 1-201(39), has adopted a unique position among all U.C.C. jurisdictions.[57]

However unclear the rationale for the decision in *Durr* may be, the implications are quite clear. The court of appeals indicates that a contract required to be written under the Statute of Frauds provision of the U.C.C. must be subscribed at the close of the writing. It is therefore important that practitioners review all documents used in both article two and non-article two commercial transactions to assure that the signature is placed at the physical end of the document unless there is an incorporating provision in the body. Otherwise, only that portion of the document above the signature may be considered as part of the agreement.

III. THE CLOSE CONNECTEDNESS DOCTRINE IN KENTUCKY LAW

The holder in due course (HDC) doctrine was originally intended to facilitate mercantile transactions in a commercial setting where "notes," though not legal tender, were traded much the same as paper currency.[58] The role of the promissory note evolved considerably as the growth of consumer credit accelerated after World War II. Although commercial law continued to adhere to HDC theory,[59] widespread abuse

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See also Corbin Deposit Bank v. King, 384 S.W.2d 302 (Ky. 1964).

[56] 344 S.W.2d at 385.

[57] For a summary of the cases addressing this issue, see 6B BENDER'S UNIFORM COMMERCIAL CODE SERVICE § 1-201(39) (1980 and Supp.).

[58] Miller v. Race, 97 Eng. Rep. 398 (K.B. 1758). This case is widely regarded as the first case recognizing the holder in due course doctrine. *See generally* Rosenthal, *Negotiability—Who Needs It?* 71 COLUM. L. REV. 375, 377-79 (1971).

[59] This doctrine is currently incorporated into article 3 of the Uniform Commercial Code. KRS § 355.3-302(1) (1972) defines an HDC as a holder who takes an instrument: "(a) for value; and (b) in good faith; and (c) without notice that it is overdue or has been dishonored or of any defense against or claim to it on the part of any person." The HDC under article 3 takes the instrument free from "(1) all claims to it on the part of any person; and (2) all defenses of any party to the instrument with whom the holder has not dealt [except certain enumerated defenses]." KRS § 355.3-

of the theory and resulting unfairness to luckless consumers generated harsh criticism demanding its reform.[60] In response, the federal and state legislatures enacted protective legislation in the consumer paper area,[61] and the Federal Trade Commission promulgated controversial regulations to preserve consumer claims and defenses.[62]

Prior to legislative efforts, however, the courts began to attack blatant abuses of HDC status.[63] The close connectedness doctrine developed out of judicial abhorrence of the cruel effects rendered at times by the HDC doctrine in consumer cases.[64] Close connectedness focuses upon the financer's connection with the business operation of the seller of goods involving credit transactions.[65] When a court finds the requisite suspect relationship, it denies HDC status to the holder of the

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305 (1972). While the protection provided by HDC status historically covered holders of consumer notes, many sellers added a "waiver of defense" clause to the conditional sales agreement, whereby the buyer agreed not to assert any defense against an *assignee* of the consumer paper that could be asserted against the seller. KRS § 355.9-206 (1972) makes such agreements enforceable by the assignee subject to any statute or decision that establishes a different rule for buyers of consumer goods. For the text of KRS § 355.9-206, see note 67 *infra*. The FTC rule, 16 C.F.R. §§ 433.1-.3 (1980), is designed to render inapplicable this protection to assignees in consumer credit sales.

[60] *See, e.g.*, Johnston, Unico v. Owen—*Judicial Mastery of the "Hard Case"*, 24 RUTGERS L. REV. 500 (1970); Littlefield, *The Continuing Demise of the Holder in Due Course Concept*, 79 COM. L.J. 41 (1974); Rosenthal, *supra* note 58, at 375; Note, *Attempts to Preserve Consumer Defenses in Kentucky and Under the FTC*, 15 J. FAM. L. 770 (1976-77); Note, *The Federal Trade Commission Rule on the Preservation of Consumers' Claims and Defenses—What Price Protection?*, 16 SANTA CLARA L. REV. 815 (1976) (particularly those articles cited at 816 n.9); Note, *The FTC's Holder-in-Due-Course Rule: An Ineffective Means of Achieving Optimality in the Consumer Credit Market*, 25 U.C.L.A. L. REV. 821 (1978); Note, *The FTC's Preservation of Consumers' Claims and Defenses: Consumer Security or Consumer Fraud?*, 11 VAL. L. REV. 263 (1977).

[61] *See, e.g.*, Federal Truth in Lending Act, 15 U.S.C. §§ 1601-93r (1976 & Supp. 1979); Kentucky Consumer Protection Act, KRS §§ 367.110-.390 (Cum. Supp. 1980).

[62] 16 C.F.R. § 433.1-.3 (1980). For review and criticism of the FTC rule, see the authorities cited in note 60 *supra*.

[63] *See* Commercial Credit Co. v. Childs, 137 S.W.2d 260 (Ark. 1940); Western Elec. Co. v. Uhlrig, 273 P. 417 (Kan. 1929); Davis v. Commercial Credit Corp., 94 N.E.2d 710 (Ohio Ct. App. 1950). *See generally* Annot., 44 A.L.R.2d 8 (1955) (a discussion of defenses which the purchaser of chattels may raise against the holders of his commercial paper).

[64] *See* Unico v. Owen, 232 A.2d 405 (N.J. 1967).

[65] *Id.* at 411. *See also* American Plan Corp. v. Woods, 240 N.E.2d 886, 888-89 (Ohio Ct. App. 1968).

note.

Massey-Ferguson, Inc. v. Utley[66] is the only Kentucky case to apply the close connectedness doctrine; there the Court held that the manufacturer who regularly purchased consumer paper from a dealer of its own equipment was the true vendor in the transaction and could not claim HDC status as a defense to the implied warranties available under the code.[67] The Court declared that the policy of the U.C.C. was "to encourage the supplying of credit for the buying of goods by insulating the lender from lawsuits over the quality of the goods . . . [but] that the insulation was intended primarily for *financial institutions* rather than the manufacturer who

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[66] 439 S.W.2d 57 (Ky. 1969).

[67] KRS § 355.2-314 (1972) provides in relevant part:

> (1) Unless excluded or modified, (KRS 355.2-316) a warranty that the goods shall be merchantable is implied in a contract for their sale if the seller is a merchant with respect to goods of that kind . . . .
>
> (2) Goods to be merchantable must be at least such as . . .
>
> . . . .
>
> (c) are fit for the ordinary purposes for which such goods are used
>
> . . . .

Id. KRS § 355.2-315 (1972) provides:

> Where the seller at the time of contracting has reason to know any particular purpose for which the goods are required and that the buyer is relying on the seller's skill or judgment to select or furnish suitable goods, there is unless excluded or modified under KRS § 355.2-316 an implied warranty that the goods shall be fit for such purpose.

Id.

The Court also found that the manufacturer was a "seller" rather than an "assignee" within the terms of KRS § 355.9-206 (1972), which provides:

> (1) Subject to any statute or decision which establishes a different rule for buyers or lessees of consumer goods, an agreement by a buyer or lessee that he will not assert against an assignee any claim or defense which he may have against the seller or lessor is enforceable by an assignee who takes his assignment for value, in good faith and without notice of a claim or defense, except as to defenses of a type which may be asserted against a holder in due course of a negotiable instrument under the article on commercial paper (article 3). A buyer who as part of one (1) transaction signs both a negotiable instrument and a security agreement makes such an agreement.
>
> (2) When a seller retains a purchase money security interest in goods the article on sales (article 2) governs the sale and any disclaimer, limitation or modification of the seller's warranties.

Id. Therefore, the manufacturer could not claim the protection of the "waiver of defense" clause in the purchase contract. For a discussion of this kind of clause, see note 59 *supra*.

finances his own sales."[68]

In *Sullivan v. United Dealers Corp.*,[69] the Court suggested that the close connectedness doctrine, when applicable, will deny HDC status to a seller's business associate who is not primarily an independently acting lending institution.[70] In *Sullivan*, the issue was whether United Dealers Corporation, a finance company, was an HDC of a promissory note executed by the Sullivans in payment for building materials furnished by the contractor-payee of the note. When the Sullivans defaulted, United Dealers instituted action against them. The Sullivans charged that United Dealers was not an HDC of the note and that it was therefore subject to the defense that the contractor-payee of the note constructed the Sullivan home in a unworkmanlike manner. The Court did not apply the close connectedness doctrine, however, because it found no evidence of any direct connection between the contractor-payee and the finance company other than a frequent course of dealing between the two. Thus the close connectedness doctrine, as applied by Kentucky's highest court, depends both upon the *type* of lending institution involved and the *relationship* between the financing institution and the seller. In light of statutory and administrative controls,[71] application of the close connectedness doctrine in the consumer credit area may be redundant; the possibility of extending the doctrine to nonconsumer credit transactions, however, is worthy of note.

The Kentucky Court of Appeals addressed the scope of the close connectedness doctrine in *Citicorp Leasing, Inc. v. Whitaker*,[72] in which a creditor holding a promissory note and security agreement covering two bulldozers claimed HDC status. Primarily this case involved a nascent coal-mining partnership that, in order to purchase the bulldozers, schemed with a local auction company to deceive the financial institution into loaning money. After the fraud was discovered, the partnership refused to make payment on the loan contract,

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[68] 439 S.W.2d at 60.

[69] 486 S.W.2d 699 (Ky. 1972).

[70] *Id.* at 701.

[71] For examples of such controls, see notes 61 and 62 *supra*.

[72] 605 S.W.2d 24 (Ky. Ct. App. 1980).

claiming the financer was closely connected with the auction company and thus subject to the defenses of failure of title and failure of consideration that the partnership possessed against the auction company. The court, however, refused to apply the close connectedness doctrine under these circumstances.

In its analysis, the court first examined the financial lender to determine whether it was a "manufacturer" or rather an institution that the *Massey-Ferguson* court considered worthy of protection under U.C.C. policy.[73] It concluded that Citicorp was not a manufacturer and that it qualified for insulation from liability. The court found no precedent in Kentucky for a broader application of the close connectedness doctrine[74] and refused to adopt a more liberal interpretation for the *Citicorp* facts. Further, the court found no sufficient evidence of a close association between the auction company and Citicorp to impugn the good faith position of Citicorp.[75] The furnishing of forms, performance of credit checks, and some previous course of dealing between the auction company and Citicorp were, according to the court, "nothing out of the ordinary in this type of business."[76]

The *Citicorp* court implied that the close connectedness doctrine is limited to cases involving consumer goods.[77] An examination of cases decided in other jurisdictions, however, clearly indicates a contrary interpretation.[78] The close connectedness doctrine has been applied to many situations that, although exhibiting some of the indicia of consumer transactions, did not involve consumer goods or consumers.[79] In fact,

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[73] *Id.*

[74] *Id.*

[75] *Id.*

[76] *Id.*

[77] "[T]hese holdings have invariably been in cases where there is a consumer involved who has been given a raw deal." *Id.*

[78] *See, e.g.*, Commercial Credit Corp. v. Orange County Mach. Works, 214 P.2d 819 (Cal. 1950) (equipment); International Harvester Co. v. Carruth, 23 So.2d 473 (La. Ct. App. 1945) (farm equipment); International Fin. Corp. v. Rieger, 137 N.W.2d 172 (Minn. 1965) (equipment).

[79] Consumer goods are specifically defined in U.C.C. article 9. KRS § 355.9-109 (1972) declares: "Goods are (1) 'Consumer goods' if they are used or bought for use primarily for personal, family or household purposes . . . ." *See also* 16 C.F.R. §

the *Massey-Ferguson* case that initially applied the close connectedness doctrine in Kentucky involved farm equipment rather than consumer goods.[80]

It appears that the *Citicorp* court based its decision upon considerations of fairness. As the court stated: "It would be unconscionable for the partnership to take advantage of a situation in [sic] which they did so much to help bring about. The whole transaction between the partnership and [the auction company] fairly reeks with fraud . . . ."[81]

The court of appeals' opinion in *Citicorp*, therefore, fails to resolve the question of whether the close connectedness doctrine is available outside of the consumer credit area to alleviate harsh effects of HDC status. Although the court seeks to limit the doctrine, it is clear that its principles are equally applicable in nonconsumer situations. While, as the court noted, the two previous Kentucky cases addressing the doctrine were themselves limited situations in which manufacturers or sellers financed sales of their own products,[82] the cases do not explicitly reject a wider application of the doctrine under the proper circumstances.

IV. COMMERCIAL REASONABLENESS UNDER U.C.C. SECTION 9-504

Part five of article nine of the U.C.C. establishes the relative rights and duties of the debtor and creditor in the event of default under a valid security agreement.[83] Although the secured party may repossess and under certain conditions retain the collateral,[84] the usual course of action involves a sale or other disposition of the collateral by the secured party, pursuant to U.C.C. section 9-504. This section allows the secured party to dispose of the collateral by either public or pri-

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433.1(b) (1980).

[80] 439 S.W.2d at 58.

[81] 605 S.W.2d at 28.

[82] *Id.*

[83] KRS §§ 355.9-501 to -507 (1972).

[84] KRS §§ 355.9-503, -505(2). The retention procedure is called "strict foreclosure." *See generally* WHITE & SUMMERS, *supra* note 26, at § 26-8; Annot., 55 A.L.R.3d 651 (1974).

vate sale subject to two basic requirements. First, the debtor generally must be given reasonable notification of the time and place for a public sale or of the time after which the collateral may be disposed of in a private transaction. In addition, except where consumer goods are involved, any other person claiming a security interest in the collateral must be notified in like manner. Second, every aspect of the disposition, including the method, time, place, and terms, must satisfy a standard of commercial reasonableness.[85]

Although Kentucky courts have addressed problems associated with the notice requirement of U.C.C. section 9-504,[86]

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[85] KRS § 355.9-504(3) (1972) states:

> Disposition of the collateral may be by public or private proceedings and may be made by way of one or more contracts. Sale or other disposition may be as a unit or in parcels and at any time and place and on any terms but every aspect of the disposition including the method, manner, time, place and terms must be commercially reasonable. Unless collateral is perishable or threatens to decline speedily in value or is of a type customarily sold on a recognized market, reasonable notification of the time after which any private sale or other intended disposition is to be made shall be sent by the secured party to the debtor, and except in the case of consumer goods to any other person who has a security interest in the collateral and who has duly filed a financing statement indexed in the name of the debtor in this state or who is known by the secured party to have a security interests in the collateral. The secured party may buy at any public sale and if the collateral is of a type customarily sold in a recognized market or is of a type which is the subject of widely distributed standard price quotations he may buy at private sale.

Id.

The term "commercially reasonable" is not defined in the U.C.C. According to Grant Gilmore, who was instrumental in drafting article 9, the aims of U.C.C. § 9-504 were to promote easy disposition of collateral at the highest possible price and to encourage the use of regular market channels. Gilmore, *The Secured Transactions Article of the Commercial Code*, 16 LAW & CONTEMP. PROB. 27, 43 (1951). In order to avoid the collusion and unfair dealings by "gangs of thieves" common in repossession sales, the code sought to reduce the standard for recovery by debtors from "fraud" to "commercial reasonableness" and to allow the courts more power to fashion the standard of review. *Id.*

[86] *See* Nelson v. Monarch Inv. Plan, 452 S.W.2d 375 (Ky. 1970). *Nelson* involved a suit by a secured creditor to recover a deficiency on a note executed for the purchase of an automobile. While considering the notice requirement of § 9-504 and its exceptions, including the meaning of "a type customarily sold in a recognized market," the Court found that the debtor was entitled to notification on a specific date after which the creditor could proceed with disposal of the collateral. *Id.* at 377. The notice requirement was designed to allow the debtor to protect his or her interest. *See also* WHITE & SUMMERS, *supra* note 26, at § 26-10; Comment, *Defending Defi-*

there was little discussion of the commercial reasonableness standard before the recent case of *Bank of Josephine v. Conn.*[87] In *Conn,* the debtor defaulted on a promissory note and security agreement covering the balance due on two coal trucks. After an agent of the bank called on the debtor stating that the bank had a buyer for the trucks, the debtor transferred title to the bank under an arrangement which he claimed discharged the indebtedness. The bank therefore took "constructive possession" of the trucks, not having them in its actual physical control. The anticipated sale of the trucks failed to materialize, and the bank did not take physical possession of the collateral until five weeks after the transfer of title, during which time the trucks were stripped of parts and damaged. Six weeks after the transfer of title the bank notified the debtor of a public sale to be held in eleven days. At the sale the bank submitted the only bid, and subsequently resold the trucks for $5,000 more than its bid, leaving a deficit of approximately $7,300 on the note, for which the bank sued the debtor. The Kentucky Court of Appeals upheld a jury verdict finding the bank's actions commercially unreasonable and denied recovery of the deficiency.

The *Conn* decision is significant to several aspects of the commercial reasonableness requirement. First, the court of appeals found, at least where the creditor is seeking to recover a deficiency judgment, that the burden of proving the commercial reasonableness of the liquidation sale will be upon the

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ciency Judgments Suits in Kentucky: Article Nine, Part 5 of the Uniform Commercial Code, 61 KY. L.J. 578, 583-87 (1973). Note, however, that in *Nelson,* although the debtor did not receive adequate notice, he was estopped to claim failure of notice by his own actions after repossession. 452 S.W.2d at 378.

The Court briefly considered the notice requirement in Bank of Josephine v. Hopson, 516 S.W.2d 339 (Ky. 1974), and found that notice sent to the debtor by registered mail was sufficient. A similar superficial reference to the notice requirement was made in Greg Coats Cars, Inc. v. Kasey, 576 S.W.2d 251 (Ky. Ct. App. 1978). Although none of these cases explicitly mentions which party has the burden of proof on the notice issue, the clear implication of *Nelson* is that this responsibility falls on the secured party, an approach consistent with the majority view. *See, e.g.,* National Rep. Bank v. Proctor, 383 N.E.2d 1310 (Ill. App. Ct. 1978); North Carolina Nat'l Bank v. Burnette, 247 S.E.2d 648 (N.C. Ct. App. 1978), *rev'd on other grounds,* 256 S.E.2d 388 (N.C. 1979).

[87] 599 S.W.2d 773 (Ky. Ct. App. 1980).

creditor.[88] Prior to enactment of the U.C.C., the burden of showing that unreasonable sales methods were employed rested upon the debtor.[89] Under the U.C.C., jurisdictions considering the issue have focused on whether the suit was by the creditor for a deficiency or whether it was a suit by the debtor for damages under U.C.C. section 9-507.[90] In the former situation the burden is usually placed upon the secured party, but in the latter there is a split of authority concerning placement of the burden of proof.[91]

An early deficiency case under the U.C.C. in Kentucky[92] declared that the secured party must introduce evidence of a liquidation sale and of a deficiency in order to pursue a deficiency judgment.[93] The issue in that case, however, was not the reasonableness of the liquidation sale but the fact of its occurrence. The issue of the burden of proof in a deficiency suit implicitly surfaced again in *Bank of Josephine v. Hopson.*[94] In rejecting the debtors' claim that the bank dealt with the collateral in a commercially unreasonable manner, the Court stated: "We simply do not feel that the [*debtors*] *have proven* any violation of KRS 355.9-503 to 355.9-505."[95] Although this statement may be interpreted as an implication that a debtor has the burden of showing commercial unrea-

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[88] *Id.* at 774.

[89] Annot., 59 A.L.R.3d 369, 372 (1974). *See* Home Fin. Co. v. Frazier, 380 S.W.2d 91, 93 (Ky. 1964). The *Frazier* court stated: "No effort was made to show bad faith or lack of diligence in the conduct of the sales after repossession. As noted, [the debtor] was present at the sale; he made no bid. Neither did he express any dissatisfaction with the sale or the manner of conducting it." *Id.*

[90] *See, e.g.,* First Nat'l Bank & Trust Co. v. Halston, 559 P.2d 440, 444 (Okla. 1976). *See generally* Annot., 59 A.L.R.3d 369 (1974).

[91] *See* Annot., *supra* note 90, at 375-76.

[92] Cox Motor Car Co. v. Castle, 402 S.W.2d 429 (Ky. 1966). Actually, the purchaser/debtor instituted this suit as a breach of warranty action. The creditor counterclaimed for a deficiency on the promissory note.

[93] *Id.* at 432. That a resale was held must be proven in order to qualify for a deficiency. This follows from KRS § 355.9-505(2) (1972), which provides that the creditor may "retain the collateral in satisfaction of the obligation." If the secured party retains the collateral, the right to a deficiency is lost. Thus in order to claim a deficiency the secured party must demonstrate that the collateral was sold pursuant to KRS § 355.9-504 (1972).

[94] 516 S.W.2d 339 (Ky. 1974). *Hopson* involved a deficiency on a note and security agreement covering a tractor and accessories.

[95] *Id.* at 34 (emphasis added).

sonableness in all situations, the Court offered no explanation of its statement.[96]

Any implication in *Hopson,* however, that the debtor has the burden of proof in deficiency suits has been negated by the court of appeals' decision in *Conn. Conn* established that a secured creditor seeking a deficiency judgment against a debtor after a resale of the collateral has the burden of proving that all elements of the sale were commercially reasonable and the burden of proving notice as well.[97] The *Conn* decision, however, fails to establish which party will have the burden in a suit by the debtor for damages under U.C.C. section 9-507.[98]

A second significant aspect of *Conn* is the court's conclusion that a violation of the commercial reasonableness standard of U.C.C. section 9-504 will result by estoppel in a complete denial of the deficiency.[99] Unreasonable acts by the

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[96] It is possible the Court was merely saying that the debtors had not produced evidence substantial enough to overcome a small presumption in favor of the commercial reasonableness of the sale. *Cf.* Sumner v. Century Nat'l Bank & Trust Co., 402 N.Y.S.2d 285, 289 (N.Y. Sup. Ct. 1978) (declaring that the presumption of commercial reasonableness is not "ordinarily overcome by naked assertions of impropriety").

[97] 599 S.W.2d at 774.

[98] *Id.* Although the Court cited KRS § 355.9-506 (1972), the reference is apparently to KRS § 355.9-507 (1972). KRS § 355.9-506 addresses a right of the debtor to redeem the collateral *before* sale.

In attempting to decide the burden of proof issue in a suit brought by the debtor, the courts should consider the factors and policy considerations raised by some commentators and courts indicating that placement of the burden on the creditor in all situations is ill-advised. For example, one commentator has observed that "the fact that the creditor is under a duty to act in a commercially reasonable manner does not determine that he has the burden of proof." 4 R. ANDERSON, THE UNIFORM COMMERCIAL CODE § 9-504:13.1 (Supp. 1980). Anderson points out the general pre-code principle that placed the burden upon the party who had the affirmative of the issue. Since the debtor would benefit from a finding of unreasonable conduct, he or she should have the burden. Anderson would not place the burden on the creditor even in a deficiency suit, although it would seem that the creditor is the party who stands to benefit in such a situation.

Additionally, unlike the notice requirement where the creditor does have the better access to the proof, the assumption that the creditor has better information than the debtor concerning commercial practices may not be valid outside of consumer goods transactions, especially in light of current discovery techniques. *Id. See also* WHITE & SUMMERS, *supra* note 26, at § 26-11. *See generally* Wells v. Central Bank, 347 So.2d 114 (Ala. Civ. App. 1977); Pruske v. National Bank of Commerce, 533 S.W.2d 931 (Tex. Civ. App. 1976).

[99] 599 S.W.2d at 775.

creditor, however, need not invariably compel this result,[100] although the majority of jurisdictions that have considered the problem have reached a conclusion similar to that reached in *Conn*.[101] It is important to note, however, that the jurisdictions composing the "majority" view may be subdivided into two distinct groups: those that require compliance with U.C.C. provisions as a precondition to any recovery and those that declare that non-compliance raises only a rebuttable presumption that the sale price was unfair.[102] Courts in the first group will never allow the non-complying creditor to recover a deficiency. Within the second group the creditor may recover a deficiency by demonstrating that the sale price was fair and reasonable despite non-compliance with U.C.C. provisions. Because *Conn* bases denial of a deficiency on estoppel, the Kentucky court appears to be adopting the stricter view. Thus, where the creditor acts unreasonably, a deficiency judgment is lost entirely.

A third potentially significant aspect of *Conn* is the court's reference to the fact that the secured creditor was the only bidder at the sale.[103] Although U.C.C. section 9-504(3) authorizes the secured party to purchase at a public sale, and under certain conditions at a private sale,[104] questions may arise as to the reasonableness of a claimed deficiency where the secured party is the ultimate purchaser or sole bidder. A court may scrutinize the result more closely. Several courts have found a secured creditor who purchases at a private sale contrary to the conditions of U.C.C. section 9-504 to be in the

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[100] *See, e.g.*, Clark Leasing Corp. v. White Sands Forest Prods., Inc., 535 P.2d 1077 (N.M. 1975).

[101] For a discussion and listing of the majority and minority positions on this issue, see 4 R. ANDERSON, *supra* note 98, at § 9-504:30; WHITE & SUMMERS, *supra* note 26, at § 26-15.

[102] This distinction is discussed in WHITE & SUMMERS, *supra* note 26, at § 26-15.

[103] 599 S.W.2d at 775. One authority cites BSY Co. v. Fuel Economy Eng'r Co., 399 S.W.2d 308 (Ky. 1965), as a case involving the commercial reasonableness of a sole bid and purchase by the secured party. 6G BENDER'S UNIFORM COMMERCIAL CODE SERVICE § 9-504, Annotation A8 (1980). Nevertheless, it is the better view to construe that case as involving the *retention* of collateral by the secured party in full satisfaction of the debt under KRS § 355.9-505(2) (1972) rather than its purchase at a sale under KRS § 355.9-504(3) (1972).

[104] For the text of KRS § 355.9-504(3) (1972), see note 85 *supra*.

same position as one who engages in commercially unreasonable conduct.[105] Where a creditor purchases at a public sale or satisfies the prerequisites for purchasing at a private sale,[106] courts have imposed a high standard of commercial conduct on the secured party when the price received results in a deficiency.[107] These courts, in viewing the principal aim of the U.C.C. default provisions as encouraging conditions for receipt of the best possible price, have required the secured party actively to pursue competitive bidding. For example, the Supreme Court of Washington has established strict guidelines that the secured party must meet in order to pursue a deficiency judgment after successfully bidding at a resale:

> The sale is valid where notice of the sale is (1) given to the defaulted debtor and to the public sufficiently in advance to allow interested bidders a reasonable opportunity to participate, (2) given to a "public" reasonably expected to have an interest in the collateral to be sold and notifying the public of the exact time of sale and place of sale, reasonably convenient to potential bidders, (3) sufficiently replete with information describing the collateral to be sold and the amount of the obligation for which it is being sold to allow potential bidders a genuine opportunity to make an informed judgment as to whether to bid at the sale and (4) published in a manner reasonably calculated to assure such publicity that the collateral will bring the best possible price from the competitive bidding of a strived-for lively concourse for bidders. If a sale is conducted under these circumstances, "[t]he fact that a better price could have been obtained by a sale at a different time or in a different method from that selected by the secured party is not of itself sufficient to establish that the sale was not made in a commercially reasonable manner."[108]

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[105] Barber v. Leroy, 115 Cal. Rptr. 272 (Ct. App. 1974); Jackson State Bank v. Beck, 577 P.2d 168 (Wyo. 1978).

[106] "Prerequisites" of a private sale apply to the sale of collateral of a type customarily sold in a recognized market or to a sale that is the subject of widely distributed standard price quotations. KRS § 355.9-504(3) (1972).

[107] *See, e.g.*, Connex Press, Inc. v. International Airmotive, Inc., 436 F. Supp. 51 (D.D.C. 1977), *aff'd*, 574 F.2d 636 (D.C. Cir. 1978); Kobuk Eng'r & Contr. Serv., Inc. v. Superior Tank & Constr. Co., 568 P.2d 1007 (Alaska 1977).

[108] Foster v. Knutson, 527 P.2d 1108, 1114-15 (Wash. 1974) (quoting WASH. REV.

Practitioners would benefit from a review of these cases and from consideration of the factors enumerated by the courts herein before advising clients on notice and advertising of the sale, location of the sale, preparation of the collateral and the solicitation of bids if the secured party will also bid.

V. SUFFICIENCY OF DESCRIPTION UNDER ARTICLE NINE

A "sufficiency of description"[109] question may arise under article nine in several ways. Usually the problem involves an examination of the security agreement provisions between the debtor and the creditor regarding items intended to serve as collateral.[110] If their delineation lacks explicitness, the security agreement cannot be enforced against the debtor or third parties.[111] A second type of description problem involves the financing statement and concerns the issue of a subsequent creditor receiving adequate "notice" of the prior secured party's interest in a specific item.[112] Failure here will result in

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CODE § 62A.9-507(2)).

[109] KRS § 335.9-110 (1972) defines "sufficiency of description": "For the purposes of this article any description of personal property or real estate is sufficient whether or not it is specific if it reasonably identifies what is described." *Id.*

[110] This is the problem the Kentucky Supreme Court addressed in Mammoth Cave Prod. Credit Assoc. v. York, 429 S.W.2d 26 (Ky. 1968). The Court found that the descriptions of collateral in the granting and after-acquired property clauses of the security agreement, covering "[a]ll farm equipment" and "[a]ll property similar to that listed above" respectively, were too "vague and indefinite" to reasonably identify the property actually agreed upon as collateral. *Id.* at 29. The Court concluded: "In light of this vague provision it seems doubtful that it was really agreed that tractors and other large farm equipment were to be security for the loan." *Id.*

[111] KRS § 355.9-203(1) (1972) provides in part: [A] security interest is not enforceable against the debtor or third parties unless . . . (b) the debtor has signed a security agreement which contains a *description of the collateral* and in addition, when the security interest covers crops or oil, gas or minerals to be extracted or timber to be cut, a *description of the land* concerned.

Id. (emphasis added).

[112] *See, e.g.*, In re Drane, 202 F. Supp. 221 (W.D. Ky. 1962), where the issue was whether the description of certain pieces of furniture in a security agreement (a security agreement can serve as a financing statement if it meets the formal requisites of a financing statement as set forth in KRS § 355.9-402 (1972)) recorded in the county clerk's office was adequate to allow a third party to easily identify the items covered by the security agreement. *See also* In re Anselm, 344 F. Supp. 544, 547 (W.D. Ky. 1972) (financing statement describing collateral as "tilling and harvesting tools" was held insufficient to give notice of covering a mower, reaper and fertilizer

lack of perfection of the security interest.[113] A third problem centers around the description of land upon which secured crops are either growing or are to be grown. This issue may involve both of the above enforceability and notice questions regarding collateral.[114] In *Bank of Danville v. Farmers National Bank*,[115] the Kentucky Supreme Court considered the first Kentucky case falling into this third category of description issues. The result raises some questions concerning the Court's earlier decision in *Mammoth Cave Production Credit Assoc. v. York*.[116]

Bank of Danville concerned a priority contest between secured creditors over the proceeds from sale of the debtors' 1975 tobacco crop. The Bank of Danville (Bank) recorded a security agreement on February 19, 1975, covering cattle, farm machinery, and the debtors' 1975 tobacco and barley crops. The security agreement declared: "The Collateral will be kept at the address indicated in the heading, otherwise will be located at: on farm of Dale Wilson on Lancaster Road, 4 miles from Danville, Boyle County, Kentucky."[117] On April 8, 1975, the debtors executed a financing statement and security

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because this description failed to adequately indicate the type of collateral held).

[113] KRS § 355.9-402(1) (1972) provides in part: (1) A financing statement is sufficient if it is signed by the debtor and the secured party, gives an address of the secured party from which information concerning the security interest may be obtained, gives a mailing address of the debtor and contains a statement *indicating the types*, or *describing the items*, of collateral . . . . When the financing statement covers crops growing or to be grown . . . the statement must also contain a *description of the real estate* concerned.

Id. (emphasis added).

KRS § 355.9-402(4) (1972) provides an example of the proper form of the financing statement.

[114] For relevant portions of KRS § 355.9-203(1), -402(1) (1972), see notes 111 and 113 *supra*.

[115] 602 S.W.2d 160 (Ky. 1980).

[116] 429 S.W.2d 26 (Ky. 1968). See note 110 *supra* and the text accompanying notes 127-29 *infra* for a discussion of the *Mammoth Cave* case.

[117] 602 S.W.2d at 160-61. Both the Supreme Court and the court of appeals apparently viewed the security agreement *filed* by the Bank as filling the role of the financing statement as well. In any event, the requirement that the real estate be described when crops are covered applies equally to the security agreement and the financing statement, and failure under either will defeat perfection of the security interest. KRS §§ 355.9-203(1), -303 (1972).

agreement to Farmers National Bank (Farmers). The collateral was described as "one-half interest in 48,900 lb. tobacco to be grown on Kenneth Bailey (formerly Dale Wilson) farm, Lancaster Road, Danville, Ky. 40422."[118] Farmers sent certified notification to all the tobacco warehouses in Danville of its "mortgage." Unlike Farmers, the Bank made no attempt to advise these warehouses. Thus, after sale of the tobacco, Farmers received more than $22,000 from one of the warehouses by checks made payable to the debtor, his lessor and Farmers. Farmers applied the money to retire the debtors' note and disbursed the remainder, with the debtors' consent, to pay off other creditors, not including the Bank.[119] The Bank brought suit against Farmers to recover sums received upon sale of the tobacco, claiming it had a valid and enforceable security agreement that had priority over Farmers'. Farmers contended, however, that the Bank's security interest was not enforceable due to the insufficiency of the description of the land contained in the security agreement. The circuit court held for the Bank, but the Kentucky Court of Appeals reversed.[120]

The Supreme Court affirmed the circuit court's decision, holding the description adequate for "notice" purposes. The Court declared: "The description contemplated by the statutes is not required to be by metes and bounds. It does not have to be meticulous. It is only required to be in such words

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[118] 602 S.W.2d at 161.

[119] Farmers received a total of $22,619.77 as proceeds from the sale. It applied $8,741.34 to satisfy the debtors' note and disbursed $13,878.43 to other creditors and to the debtor. The circuit court held Farmers liable to the Bank for the entire amount received, a decision that the Supreme Court subsequently affirmed. 602 S.W.2d at 164.

[120] Farmers Nat'l Bank v. Bank of Danville, No. 79-CA-80-MR (Ky. Ct. App. August 24, 1979). The court of appeals, in reviewing the Bank's security agreement and financing statement, could find "no description of the real estate on which these crops are to be grown." *Id.* at 4. The court relied upon First Nat'l Bank v. Calvin Pickle Co., 516 P.2d 265 (Okla. 1973), but that case is clearly distinguishable since the financing statement there contained no reference at all to the real estate upon which the crops listed as collateral were to be grown. The Bank of Danville's description did make at least some mention of the real estate—referring to the "farm of Dale Wilson"—but the court of appeals interpreted that reference as applying only to the non-crops collateral, since the language "will be kept at" did not suggest the location of crops.

and terms that it can be readily located."[121] The description contained in the Bank's security agreement filed with the county clerk was adequate. This conclusion is in accord with the majority of those jurisdictions that have considered the same issue.[122] In reaching this conclusion, however, the Court confused the purpose of a financing statement with that of a security agreement. By holding that the security agreement was adequate to provide *notice,* the Court misconceived the purpose of the security agreement, which is evidentiary in nature and is designed to protect against future disputes as to what collateral was intended to secure the debt.[123] It is the function of the financing statement to provide notice to third parties of prior security interests.[124]

The Uniform Commercial Code contains one test for descriptions in general: they must reasonably identify what they describe.[125] Although circumstances in which the sufficiency question arises may affect a court's analysis, the test itself remains constant. Therefore, a court might examine different factors in deciding whether a description contained in a security agreement reasonably identifies the collateral than it would in assessing the notice requirement of the financing statement. For example, a financing statement might reasonably be less specific in describing collateral, since its primary purpose is to provide notice to third parties.[126] In light of its liberal decision in *Bank of Danville,* the Court's previous decision in *Mammoth Cave* might be questioned. In *Mammoth*

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[121] 602 S.W.2d at 162-63.

[122] *See* Annot., 67 A.L.R.3d 308 (1975).

[123] U.C.C. § 9-203 comment 3.

[124] U.C.C. § 9-402 comment 2.

[125] See note 109 *supra* for the definition of "sufficiency of description" in KRS § 355.9-110 (1972).

[126] U.C.C. § 9-110 comment states: "The requirement of description of collateral (see Section 9-203 and Comment thereto) is evidentiary. The test of sufficiency of a description . . . [is] that it *makes possible* the identification of the thing described." *Id.* (emphasis added). U.C.C. § 9-203 comment 3 continues: "The requirement of a written record minimizes the possibility of future dispute as to the terms of a security agreement and as to what property stands as collateral for the obligation secured." U.C.C. § 9-203 comment 5 further explains: "The formal requisite of a writing stated in this section is not only a condition to the enforceability of a security interest against third parties, it is in the nature of a Statute of Frauds."

Cave, the Court concluded from the face of the security agreement that the description "[all] farm equipment" and the reference in the after-acquired property clause to "all property similar" was too vague to indicate agreement that a tractor was covered as after-acquired property.[127] This case has been criticized because of the Court's failure to establish the actual intent of the agreement between the creditor and debtor,[128] and because of its failure to apply the liberal approach of U.C.C. section 9-110 (Sufficiency of Description).[129] In contrast, *Bank of Danville* implies that when there is some ambiguity or vagueness in a description, the court may examine extraneous factors. *Bank of Danville* required only that the land be "readily located" by reference to the description,[130] declaring "that is certain which can be made certain . . . ."[131] This proposition of law is more consistent with the code's basic philosophy than is the Court's reasoning in *Mammoth Cave.* The *Bank of Danville* case, however, concerned a land description, rather than a collateral description. Whether the Court will apply the liberal approach taken in *Bank of Danville* to a description of collateral in a future *Mammoth Cave* situation and whether the Court will distinguish the requirements and differing purposes of security agreements and financing statements, however, remains to be seen.

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[127] 429 S.W.2d at 29.

[128] *See, e.g.,* United States v. First Nat'l Bank, 470 F.2d 944 (8th Cir. 1973); Skilton, *Security Interests in After-Acquired Property Under the Uniform Commercial Code,* 1974 WIS. L. REV. 925, 937-41; Note, *Agricultural Financing Under the U.C.C.,* 12 ARIZ. L. REV. 391, 394 (1970); Note, *Description of Collateral in a Financing Statement: Should It be Required?,* 4 VAL. L. REV. 205, 216 (1969).

[129] See note 109 *supra* for text of this section.

[130] 602 S.W.2d at 162-63.

[131] *Id.* at 163 (quoting Ken-Tex Exploration Co. v. Conner, 251 S.W.2d 280, 281 (Ky. 1952)).