

Personal Property Security Interests In Washington—Adoption Of The 1972 Official Text Of The Uniform Commercial Code Will Make A Good Law Better

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I. INTRODUCTION

The purpose of this article is to review the Washington State law of personal property security interests under the existing 1962 Text¹ of Article 9 of the Uniform Commercial Code (U.C.C.) adopted by the legislature in 1965² and to introduce the reader to the substantive and procedural improvements adoption of the 1972 Text³ would make in existing Washington practice. This article advocates the approval of the 1972 Text at the next session of the Washington Legislature. In addition, the article proposes several nonuniform amendments and changes in

1. The Uniform Commercial Code is the product of collaboration between the American Law Institute and the National Conference of Commissioners on Uniform State Laws. It was begun in the 1940's as a project to harmonize state laws on commercial transactions and has evolved through a number of drafts of Official Texts. The 1962 Official Text was adopted by the large majority of state legislatures between 1962 and 1966 and either is currently, or has been, in effect in 49 states.

2. Uniform Commercial Code, ch. 157, 1965 Wash. Laws 2333 (codified at WASH. REV. CODE tit. 62A (1979)). Citations to the 1962 Text of the Uniform Commercial Code as adopted in Washington are in the form, *e.g.*, WASH. REV. CODE § 62A.9-102 (1979); citations to the 1972 amendments to the 1962 Text are cited as, *e.g.*, U.C.C. § 9-102 (1972 version).

3. Even before the Uniform Commercial Code became the law in Washington on July 1, 1967, an Article 9 Review Committee was already at work dealing with problems which had surfaced in the legal literature and in the substantial U.C.C. case law from those jurisdictions which had earlier enacted the Code. The committee's work resulted in suggested revisions to the 1962 Text, which were promulgated in 1972 as a new Official Text. The changes are directed at filling the gaps, correcting the errors, and resolving the uncertainties in the 1962 Official Text.

existing Washington nonuniform provisions, which would improve the functioning of the personal property security system in Washington, and which, therefore, should be considered by the legislature in conjunction with the 1972 Text. These proposals include elimination of all special provisions in Article 9 relating to farm credit; extension of existing nonuniform subsection 9-204(6) to protect all cash sellers, not just sellers of livestock, from loss of their goods to the buyer's inventory financier on dishonor of the buyer's check; and modification of the language of the second paragraph of subsection 9-501(1) to prohibit a deficiency judgment against a consumer after repossession in all cases of consumer purchase money financing, and not just in the case of conditional sales. Finally, the article surveys the interpretations of the existing text of Article 9 given by the Washington Supreme Court and Court of Appeals in the approximately three dozen Washington appellate cases reported⁴ in the twelve years since the Code became effective in Washington and discusses how these cases will be affected by the adoption of the 1972 Text.

By July, 1979, twenty-six states had adopted the 1972 Text, including Oregon, Idaho, and California, and the leading commercial states of New York, Michigan, Illinois, and Texas.⁵ Yet through the end of the 1979 Extraordinary Session of the Washington Legislature, no bill to enact the 1972 Text in Washington has ever been introduced. That the 1972 Text, which apparently has generated no active opposition, is noncontroversial and intended to make an already good law even better is an explanation, but not an excuse, for why the legislature has overlooked the 1972 Text. For the very same reasons, it is not a cause that generates vocal support, and even the Washington State Bar Association appears not to have undertaken active sponsorship. This article has been prepared in the hope that it will explain the 1972 amendments to Article 9 in the context of the existing Washington law. Its passage would not only improve Washington

4. A LEXIS computer search of Washington appellate cases reveals 37 opinions through September, 1979, that cite one or more provisions of the Washington Text of Article 9. In several of these, reference to Article 9 is incidental to the issues presented and mention of these cases has been omitted in the article. A computer search revealed no reported decisions from other states interpreting the Washington Text of Article 9 and one opinion each from the Ninth Circuit Court of Appeals and the United States District Court for the Eastern District of Washington.

5. UNIFORM COMMERCIAL CODE REPORTING SERVICE: STATE CORRELATION TABLES (Pike & Fischer, Inc. ed. 1979 & Supp. 1980).

commercial law but also harmonize Washington law with that of the majority of other states.

II. THE SCOPE OF ARTICLE NINE

Under subsection 9-102(1)(a), Article 9 extends to transactions⁶ well beyond what are normally thought of as security interests.⁷ The Code expressly recognizes, for example, that a transaction in the form of a lease may actually be a security interest disguised in an effort to hide it from public view.⁸ Because the rights of a lessor of personal property historically have been enforced against a creditor of the lessee by an action of replevin based upon the lessor's title, either at common law or under modern statute a lease of personal property does not have to be recorded to avoid conflict with the rules against fraudulent

6. The rules for the transactional scope of Article 9, contained in WASH. REV. CODE § 62A.9-102 (1979), remain unchanged from the 1962 to the 1972 Text. As noted in the discussion of multistate transactions, a clause dealing with territorial choice of law has been deleted from § 9-102 in the 1972 Text. See text accompanying notes 183-87 *infra*.

The significant issue relating to the transactional scope of Article 9, as with Article 2 on sales, is whether the principles of Article 9 may be applied by analogy to transactions which bear functional similarities to those transactions covered by the Article. Washington and a number of other jurisdictions have extended Article 2 protections to cases not involving sales. *E.g.*, *Mieske v. Bartell Drug Co.*, 92 Wash. 2d 40, 593 P.2d 1308 (1979); *Baker v. City of Seattle*, 79 Wash. 2d 198, 484 P.2d 405 (1971). See generally Fransworth, *Implied Warranties of Quality in Non-Sales Cases*, 57 COLUM. L. REV. 653 (1957); Comment, *The Extension of Article 2 of the Uniform Commercial Code to Leases of Goods*, 12 TULSA L.J. 556 (1977). But extension of Article 2 warranties has been denied in other cases. *E.g.*, *Aegis Prods., Inc. v. Arriflex Corp.*, 25 A.D.2d 639, 268 N.Y.S. 2d 185 (1966) (no warranty on repair of personal property).

In *Merchants Leasing Co. v. Clark*, 14 Wash. App. 317, 540 P.2d 922 (1975), the court of appeals raised on its own motion, but left undecided, the question of whether the default provisions of Part 5 of Article 9 should be applicable to regulate the rights of lessor and lessee under a long-term lease of personal property. That case involved a non-cancellable five-year lease, which the lessee had an option to extend to a maximum of eight years but, significantly, had no option to purchase. See WASH. REV. CODE § 62A.1-201(37)(last sent.) (1979). The lessor sought to recover a deficiency judgment from the lessee after the lessor had repossessed and sold the property without giving notice to the lessee. The court decided the issue of the effect of lack of notice on the sale in the same manner as similar U.C.C. cases had been decided in Washington, but without direct application of the rules of Part 5 of Article 9. See *Commercial Credit Corp. v. Wollgast*, 11 Wash. App. 117, 521 P.2d 1191, *pet. rev. denied*, 84 Wash. 2d 1004 (1974); *Grant County Tractor Co. v. Nuss*, 6 Wash. App. 866, 496 P.2d 966 (1972). For a discussion of these cases, see notes 279-86 *infra*. Despite the invitation of the court of appeals in *Clark* for future litigants to raise the application of Article 9 in non-Code cases, no subsequent reported case appears to have dealt with this issue.

7. "Security interest" is defined in WASH. REV. CODE § 62A.1-201(37) (1979) as "an interest in personal property or fixtures which secures payment or performance of an obligation."

8. WASH. REV. CODE § 62A.1-201(37)(last sent.) (1979).

conveyances. Thus, the lessor's right to recover his property from the lessee's creditors creates, in fact, a secret, or unrecorded, interest in what is ostensibly the lessee's property. To prevent the public notice requirements imposed upon nonpossessory security devices from being undercut, the Code, in subsection 1-201(37), sets out objective standards for judging whether a lease is a true lease or shall be deemed to be a security interest and thus subject to the provisions of Article 9.

Subsection 9-102(1)(b) also includes all *sales* of accounts receivable within the scope of the Article.⁹ The Code recognizes the functional similarity between the borrowing against and the selling of accounts receivable in the financing of a business¹⁰ and imposes upon the account buyer the same third-party notice requirements under Article 9 as fall upon the account lender. In doing so, the provision continues the practice begun by statutes such as Washington's assignment of accounts receivable statute,¹¹ which mandated filing of notice to perfect assignments of accounts. Under the earlier common law, a sale of accounts was treated as merely a special case of the assignment of choses in action, which required the creditor to notify the account debtor in order to claim priority against subsequent purchasers.¹² Although such notification may be effective protection for the account debtor against requests for payment by a later assignee, it is not only a cumbersome method of perfection in large scale financing, but also is frequently for business reasons objectionable. Thus, because of the need for providing adequate notice, simplifying the procedure, and making information concerning accounts receivable financing more easily accessible to third parties, the drafters followed the tendency of modern law by including all accounts transactions within Article 9 filing provisions.

9. *Id.* § 62A.9-102(1)(b) also includes within the scope of Article 9 sales of chattel paper, a type of collateral first introduced by Article 9. See text accompanying notes 25-26 *infra*.

10. See U.C.C. § 9-102, Official Comment 2 (1972 version). The Official Comments are neither the law nor the reports of a legislative committee but rather the comments of the drafters of the Article. Although they have no legal status, they are extremely helpful to an understanding of the Code.

11. Ch. 8, §§ 1-12, 1947 Wash. Laws 20 (repealed 1966).

12. In *Corn Exch. Nat'l Bank v. Klauder*, 318 U.S. 434 (1943), the United States Supreme Court cast doubt on accounts receivable financing by declaring the assignee's interest vulnerable to the avoidance powers of the debtor's trustee in bankruptcy under § 60 of the Bankruptcy Act of 1898 unless the account debtors had been notified of the assignment. Statutes such as Washington's were passed in response to the need for a practical perfection technique, and § 60 was subsequently amended to overrule the result in *Klauder*. See 11 U.S.C. § 96 (1976) (repealed 1978) (repeal effective Oct. 1, 1979).

III. CLASSIFICATION OF PERSONAL PROPERTY

The methods required for perfection against the claim of third parties of a secured party's rights in the debtor's property vary according to the kind of property, or collateral,¹³ involved. Also, if the filing of a financial statement is the required method of perfection, the place where filing is required may vary depending on the nature of the collateral subject to the security interest. In addition, with certain kinds of collateral third parties can obtain rights that will defeat even a perfected security interest. Hence, an accurate classification of the collateral is essential.

A. Goods

Collateral can be categorized as either tangible personal property (goods)¹⁴ or intangible property.¹⁵ Goods are further subdivided in section 9-109 according to their use by the debtor. The four classifications of goods are consumer goods, equipment, farm products, and inventory. Inventory includes not only raw materials and products held for sale, but also property held for lease.¹⁶ Equipment is property used in a business; it also forms the residual category for all goods that do not fit within any of the other three categories.¹⁷

The proper classification of goods, under the definitions in section 9-109, depends upon their use by the debtor granting the security interest, and the method of perfection (*i.e.*, whether filing is required or not, and if so, where) depends upon the classification. Problems with respect to perfection can arise when the debtor's use of the goods changes *after* the security interest is properly perfected according to the rules relating to the debtor's original use. Will the new use require a new filing? Subsection 9-401(3) attempts to meet this difficulty by declaring that a security interest properly perfected by filing according to the debtor's original use remains perfected even though a change in use might demand filing in a different location.¹⁸

13. WASH. REV. CODE § 62A.9-302(1) (1979).

14. U.C.C. § 9-105(h) (1972 version).

15. See text accompanying notes 24-34 *infra*.

16. WASH. REV. CODE § 62A.9-109(4) (1979).

17. *Id.* § 62A.9-109(2).

18. Washington has adopted this alternative of § 9-401(3). The other proposed alternative would continue perfection by a correct original filing for only four months after the change in use, after which time the interest would become unperfected unless a filing proper for the new use was made. U.C.C. § 9-401(3), Alternative Subsection (1972 version). The rule of § 9-401(3) is necessitated by the filing location rules of § 9-401(1).

Further difficulties arise if the debtor makes representation to a purchase money lender as to his *intended* use and immediately upon receipt of the collateral subjects it to a different use. Will the objective manifestations of the debtor's intent or the debtor's subjective intent control the classification of the goods? The Washington Supreme Court has recognized in dicta in *Commercial Credit Equipment Corp. v. Carter*,¹⁹ that such problems may exist but has expressly reserved the question whether the creditor may rely on such representations in determining classification for perfection purposes.

In addition to belonging to one of these four categories, goods may also be fixtures, *i.e.*, while retaining their character as personal property they are sufficiently attached to real estate that an interest in them may be acquired under the law of real property.²⁰ Because of this overlap between real and personal property law, the U.C.C. contains provisions requiring the filing of claims to personal property interests in fixtures in the real property recording system. The Code also regulates the relative rights of creditors whose conflicting claims to the same fixtures arise from real property law on the one hand, and from personal property law on the other.²¹

One particular facet of the 1972 definition of goods may substantially affect Washington practice. Subsection 9-105(h) of the 1972 Text adds standing timber "which is to be cut and removed under a conveyance or contract for sale" to the list of goods in which a personal property security interest may be created. This

Washington adopted Alternative 2 of § 9-401(1), which provides for filing at the county level for interests in farm products and consumer goods and filing in a central index under the control of the Secretary of State for interests in equipment and inventory. Hence, a change in use from consumer goods to equipment, or vice versa, would render a correct original filing incorrect if measured by the new use.

WASH. REV. CODE § 62A.9-401(3) (1979) does *not* resolve the problem of continued perfection if the goods originally were used as consumer goods and the security interest was created as a purchase money interest in the goods, perfected *without* filing (as permitted by *id.* § 62A.9-302(1)(d)) and, thereafter, the use is changed, for example, to equipment.

19. 83 Wash. 2d 136, 516 P.2d 767 (1973). In this case, the use of the goods determined the legal effects of the relationship *between the parties*, rather than the proper manner of perfection. The question was whether a deficiency judgment after repossession of the collateral upon default would be allowed under WASH. REV. CODE § 62A.9-501(1) (1979). The court held that the initial use fixed the nature of the parties' agreement, but it did not differentiate clearly between use determining rights *inter partes* and use determining duties to third parties. For further discussion of the case, see text accompanying notes 227-28 *infra*.

20. U.C.C. § 9-313(1)(a) (1972 version).

21. WASH. REV. CODE § 62A.9-313 (1979).

addition, consistent with the inclusion of standing timber in subsection 2-107(2) of the 1972 Text of the Sales Article as property that can be sold under a contract for sale of goods (no matter who cuts the timber),²² should simplify timber sales and financing practices. As with fixtures, to protect persons who may claim an interest in standing timber under non-Code real estate law, the U.C.C. timber financier is required to file in the real property recording system rather than the central U.C.C. system.²³

22. The only change promulgated in Article 2 under the 1972 Text is in subsections 1 and 2 of § 2-107. The effect of the change is to classify as goods, and therefore within Article 2, standing timber sold under contract to cut and remove, no matter who will do the cutting. Under the 1962 Text the contract is under the Sales Article only if the timber would be cut by the landowner. In all other cases the sale would be a sale of an interest in real estate and subject to the formalities and substantive law of real estate transactions. Under both the 1962 and 1972 Texts, § 2-107(3) allows a timber buyer's qualifying Article 2 interest to be recorded as a real estate conveyance to preserve his rights against a conflicting real estate purchaser claiming under the real property recording system. The language of the section does not make clear whether the Article 2 timber sales contract must be in recordable form under the real estate law. (The cautious attorney, of course, would make certain that it is.) The major effect of inclusion of timber sales contracts within Article 2 is to subject the contract to the terms of Article 2, including, of course, U.C.C. express and implied warranties under §§ 2-312 through 2-315.

In a 1957 article, Professor Johnson speculated that adoption of the U.C.C. under the then proposed § 2-107 (identical to present WASH. REV. CODE § 62A.2-107 (1979)) would have little effect on Washington rules concerning timber sales because for thirty years the Washington Supreme Court had ignored the inclusion of timber as goods in the Uniform Sales Act. Johnson, *Sales—A Comparison of the Law in Washington and the Uniform Commercial Code*, 34 WASH. L. REV. 78 (1959).

Neither the Washington Supreme Court nor the Court of Appeals has yet decided a case turning on an interpretation of § 2-107. In *Clarke v. Alstores Realty Corp.*, 11 Wash. App. 942, 527 P.2d 698 (1974), the court of appeals acknowledged that the "real or personal character of 'timber, minerals or the like'" would be determined by § 2-107 for transactions entered into after the Code's effective date. *Id.* at 945, 527 P.2d at 701. The contract at issue, one for the removal of peat, predated the Code, however, and the court held the contract was subject to real property law. *Id.* at 944, 527 P.2d at 701.

In *Layman v. Ledgett*, 89 Wash. 2d 906, 577 P.2d 970 (1978), the supreme court held in a five to four decision that a 1934 conveyance of "all the timber standing and growing" upon a parcel of land for a span of 40 years meant that at the end of the 40 years all uncut timber reverted to the then owner of the land. The court stated in the course of the majority opinion that the conveyee's right to enter and cut timber was a real property interest and that the "trees remain a part of the land until severed, at which time they are converted into personalty." *Id.* at 911, 577 P.2d at 972. The court noted that the present Washington Text of § 2-107 treats sales of timber as sales of goods only when the seller will do the cutting. *Id.* at 913, 577 P.2d at 973. Based on the reaffirmation of previous Washington law in *Layman*, adoption of § 2-107 of the 1972 Text would affect Washington rules on timber cutting deeds. Speculation on such changes, however, is beyond the scope of this article.

23. WASH. REV. CODE § 62A.9-401(1) (1979).

B. Intangibles

The 1972 Code defines five kinds of intangible collateral. Two of these are claims the law has come to view as embodied in paper of particular form. The first kind, collectively defined as instruments in subsection 9-105(1)(i), includes negotiable instruments and investment securities, the subject matter of Articles 3 and 8, respectively. The second kind consists of documents of title, which are the subject matter of Article 7. To protect rights granted by these Articles to the party-in-possession against adverse claimants, Article 9 restricts claims to a security interest in these kinds of intangibles by anyone other than the person in possession of the paper that evidences the chose.²⁴

A third type of intangible collateral is chattel paper. This concept, introduced for the first time in Article 9, relates to the practice of a lender financing his debtor, a merchant of goods, by accepting as collateral a combination of the merchant's security interest in, and the buyer's promise to pay for, goods the merchant sells on credit. Chattel paper is thus a combination of a security interest in goods together with the buyer's payment obligation.²⁵ Chattel paper is significant particularly as proceeds of the sale of higher value consumer goods, in which sales on open account (*i.e.*, on the buyer's unsecured promise to pay) are not often made. The lender who takes chattel paper as collateral is thus obtaining two-tiered protection against loss should his borrower, the seller, not repay the advance. First, he has the promise of the buyer to pay for the goods he has purchased, and second, he has the further protection of the security interest the buyer has created in the goods themselves. Chattel paper financing may occur by virtue of a financier's purchase of, or lending on, the chattel paper as collateral for an original loan or by virtue of an inventory lender's taking an interest in chattel paper as proceeds. Although Article 9 permits a security interest in chat-

24. *Id.* §§ 62A.9-308-.9-309.

25. *Id.* § 62A.9-105(1)(b). Chattel paper may also consist of a lease of specific goods and the lessee's obligation to pay rent. *Id.* § 62A.9-105(b). Chattel paper of this nature arises when a lessor assigns to his lender his rights in a lease as security for an advance used to finance the purchase of the leased goods. Perfecting an interest in chattel paper taken from a lessor presents difficulty under both the 1962 and 1972 Texts, as illustrated by *In re Leasing Consultants*, 486 F.2d 367 (2d Cir. 1973). The financier should always file a financing statement against the lessor, naming the leased goods as collateral, in addition to perfecting his interest in the chattel paper itself. In this manner, the financier is perfected in the residual rights of the lessor in the goods and also is protected in the event of the lessor's bankruptcy.

tel paper to be perfected either by filing against the paper or by possession, the Code indicates a preference for possessory security interests.²⁶

The fourth and fifth kinds of intangible collateral, accounts and general intangibles, are not rights the law considers to be embodied in any particular writing but are merely choses in action. Section 9-106 of the 1972 Text defines an account as a promise to pay arising out of a contract for the sale or lease of goods or the performance of services. General intangible is the residual category of personal property (other than money) not included in the definition of goods or the other four kinds of intangibles. The only significant differences in the treatment of accounts and general intangibles are that a sale of general intangibles is not a transaction within the scope of Article 9, while a sale of accounts is.²⁷ Also, a security interest in general intangibles must always be perfected by filing, while a security interest in accounts "which does not alone or in conjunction with other assignments to the same assignee transfer a significant part of the outstanding accounts of the assignor" is perfected automatically without the need to file a financing statement.²⁸ Because in some cases it may be difficult to differentiate between accounts and general intangibles, a sound rule of thumb is to file a financing statement to evidence every assignment of a chose in action not clearly and explicitly excluded from the scope of Article 9 by section 9-104 or subsection 9-302(3).²⁹

26. Chattel paper financing is not for the unsophisticated. In addition to perfecting his own interest in the chattel paper, the financier must verify that the component security interest in the underlying goods granted by the buyer to his transferor, the seller, has itself been properly perfected by filing against the buyer; also the lender must file a financing statement to perfect his interest in the merchant's residual claims to the underlying goods as against the merchant's other creditors should the goods be repossessed or otherwise returned to the merchant's possession. See note 25 *supra*.

27. WASH. REV. CODE § 62A.9-102(1)(b) (1979). See text accompanying notes 9-12 *supra*.

28. WASH. REV. CODE § 62A.9-302(1)(e) (1979).

29. Section 9-104 lists specific transactions excluded from the scope of Article 9, and § 9-302(3) eliminates the need for a U.C.C. filing when evidence of an assignment must be recorded in some other existing registration system set up under federal or state law, as in the case of copyrights. See, e.g., 17 U.S.C. § 408 (1976). The distinction between an account and a general intangible proved the difference between a perfected and an unperfected security interest in *Friedman, Lobe & Block v. C.L.W. Corp.*, 9 Wash. App. 319, 512 P.2d 769 (1973). The secured party took an assignment of the right to recover in a cause of action brought by his assignor against a third party as security for a loan but had not filed a financing statement when a creditor of the assignor levied on the action. The court of appeals awarded the collateral to the levying creditor because the assignment was of a general intangible, to which WASH. REV. CODE § 62A.9-302(1)(e) (1979)

Under the 1972 definition of account, it makes no difference whether the contract giving rise to the promise to pay has been performed. The 1962 Text, however, differentiates between rights arising out of executory contracts and rights that are unconditionally due because the counterperformance has been rendered.³⁰ All rights to payment in cases where the counterperformance is still due are defined under section 9-106 of the 1962 Text as contract rights. If the contract right arises out of an executory contract for the sale or lease of goods or for the performance of services, the contract right matures into an account when the performance is rendered. But if the contract right arises under any other executory contract (for example, rights to rental payments from an executory lease of real estate), the contract right matures into a general intangible.

This divergence upon maturity of contract rights leads to a potential trap for the unwary secured creditor under the 1962 Text. First, no security interest is conferred if the collateral is not specifically covered in the written agreement.³¹ The creditor claiming security in contract rights might fail to include the words accounts or general intangibles in the description of his collateral and therefore lose his security if the contract rights matured while his advance was still outstanding. Second, in the case of a debtor with business locations in more than one state, a perfected security interest in contract rights might become unperfected upon the maturity of the contract right into a general intangible, unless filing of the financing statement had been accomplished in more than one state.³² The category of contract rights has been abolished and the definition of accounts broadened in the 1972 Text to eliminate these problems.

Another important definition of Part 1 is that of the

does not apply, and, therefore, the assignment was unperfected.

For the meaning of § 9-302(1)(e)'s phrase "significant part of the outstanding accounts of the assignor," see note 79 *infra*.

30. Compare WASH. REV. CODE § 62A.9-106 (1976) with U.C.C. § 9-106 (1972 version).

31. For discussion of attachment under § 9-203, see text accompanying notes 37-38 *infra*.

32. See WASH. REV. CODE § 62A.9-103(1), (2) (1979). Under these provisions, interests in contract rights and accounts are perfected by filing in the state where the debtor keeps his records concerning them; general intangibles are perfected, in contrast, in the state where the debtor has his chief place of business. If these are located in two different states, multiple filings are required. Since it is sometimes difficult to tell where these locations are, problems under these provisions can be compounded, defeating even the creditor who had tried to comply with § 9-103(1) and (2). For a discussion of multistate transactions, see text accompanying notes 183-220 *infra*.

purchase money security interest in section 9-107. This definition relates to the circumstances under which a security interest is created rather than to the kind of collateral involved. As in pre-Code law,³³ Article 9 recognizes special rights of a seller of property who delivers on credit and retains a security interest in the property to insure payment of the purchase price. Under common law the seller's rights were based upon his reservation of title, notwithstanding the fact his rights constituted a secret interest in goods in his debtor's possession.³⁴ Under present law the seller's claim is treated as is any other security interest in terms of perfection requirements, but his priority over the buyer's other creditors in the goods that he has supplied is preserved in the U.C.C. The justification is that the seller has furnished to the debtor's estate the value to which he makes his claim, so that to recognize his interest is not to diminish assets otherwise available to other creditors.

With reservation of title no longer the basis for recognizing the seller's favored status in the property transferred to the buyer, the significant departure of section 9-107 from prior law is easily explained. For the first time, the definition of purchase money security interest includes an interest taken by a *lender* of the purchase price of the collateral which secures the lender's interest. Of course, as stated in the definition itself, the lender's interest is a purchase money interest only if the lender's advance is so used. To protect themselves, lenders who plan to take a purchase money interest frequently arrange to make the advance by means of payment directly to the seller.

IV. CREATING AN ENFORCEABLE SECURITY INTEREST

A. *The Contract Aspects—Attachment*

A security interest combines a contract allowing a secured party to seek satisfaction out of the collateral upon a debtor's default with a property right enabling the secured party to enforce his claims in the collateral against the debtor's other creditors. Part 2 of Article 9 regulates the "contract" aspect of security interests.

Subsection 9-203(1) of the 1972 Text states three conditions

33. See, e.g. *Conditional Sales and Leases of Personal Property*, ch. 106, 1893 Wash. Laws 253 (repealed 1965).

34. See generally Starr, *Conditional Sales and Chattel Mortgages*, 9 WASH. L. REV. 143 (1934).

which must be fulfilled before an enforceable security interest can arise: (1) a written agreement signed by the debtor containing a description of the collateral, or, alternatively, an agreement accompanied by delivery of the collateral to the secured party or his agent; (2) an advance of value by the secured party; and (3) acquisition of rights in the collateral by the debtor. When all conditions have been met, the security interest is said to have "attached" to the collateral.³⁵

When the debtor, as opposed to the creditor,³⁶ retains possession of the collateral, the parties must execute a written agreement. Official Comment 5 to section 9-203 states that the requirement of a writing should be interpreted as a statute of frauds. Courts faced with the question of validating a nonpossessory security interest have nearly unanimously held no enforceable security interest exists when the creditor could not produce a signed writing containing language granting the creditor an interest in the collateral.³⁷ Some creditors have attempted unsuccessfully to substitute for a security agreement a properly filed financing statement.³⁸ Many courts have rejected such a substitution on the ground that the form developed for filing as required in section 9-402 does not contain language of agreement, notwithstanding the presence of a description of the collateral and the debtor's signature.³⁹ Such cases, however, overzealously apply the requirement of a writing as a precondition of enforceability; a public memorandum reciting the collateral and signed by the debtor should be adequate evidence of

35. U.C.C. § 9-203(2) (1972 version). The 1972 Text of §§ 9-203 and 9-204 varies from the 1962 Text both in arrangement and in substantive content. Under the 1962 Text a security interest will attach on oral agreement, WASH. REV. CODE § 62A.9-204(1) (1979), but will not be enforceable unless the statute of frauds contained in § 9-203(1), requiring a written instrument or delivery of possession of the collateral to the secured party, is satisfied. The 1972 Text in effect merges the concepts of attachment and enforceability.

36. When a security agreement is accompanied by delivery of the collateral to the secured party, the need for evidence of the agreement is satisfied by the secured party's possession of the collateral itself. WASH. REV. CODE § 62A.9-203(1)(a) (1979).

37. In *Warren Tool Co. v. Stephenson*, 11 Mich. App. 274, 161 N.W.2d 133 (1968), the Michigan Court of Appeals held the doctrine of equitable lien was alive and well in Michigan, despite the passage of the U.C.C. some four years earlier. The court validated the security interest despite the absence of any written agreement. *Id.* at 301-03, 161 N.W.2d at 148-49. The holding in this case appears to remain a minority of one. See U.C.C. § 9-203, Official Comment 5 (1972 version).

38. See, e.g., *American Card Co. v. H. M. H. Co.*, 97 R.I. 59, 196 A.2d 150 (1963). For a discussion of such cases, see 1 G. GILMORE, SECURITY INTERESTS IN PERSONAL PROPERTY § 11.4 (1965).

39. See, e.g., *General Elec. Credit Corp. v. Bankers Comm. Corp.*, 244 Ark. 984, 429 S.W.2d 60 (1968).

agreement between the parties.⁴⁰

Under Washington case law, a certificate of title application can qualify as a written agreement under subsection 9-203(1) in certain situations. In *Kreiger v. Hartig*,⁴¹ the creditor claimed a nonpossessory security interest in a vehicle pursuant to an oral security agreement and produced a title certificate showing the record of her lien on its face.⁴² Upon the debtor's objection to the interest's enforceability, the Washington Court of Appeals held that the *application* for issuance of a new title certificate bearing the lien, which by statute was required to contain both the debtor's signature and a description of the vehicle, constituted a writing satisfying subsection 9-203(1). The court specifically rejected the assertion that the signed statement was insufficient because it contained no words granting a security interest.⁴³ Certainly this decision is more within the intent and fair construction of the Code.⁴⁴

The Code contains in Article 1 a complex definition of value, the second condition of enforceability. In addition to delivery of money or an extension of credit contemporaneous with the creation of the security interest, this definition includes the cancellation of a preexisting indebtedness, a binding obligation by the secured party to extend future credit, or any promise or act by the secured party which would form consideration for a simple contract.⁴⁵

The third condition, that the debtor have rights in the collateral, is satisfied immediately if the property already belongs to the debtor at the time the agreement is made. In many cases, however, a security agreement is signed in anticipation of the debtor receiving the property that is to serve as collateral. Such

40. See, e.g., *Evans v. Everett*, 279 N.C. 352, 183 S.E.2d 109 (1971).

41. 11 Wash. App. 898, 527 P.2d 483 (1974).

42. The Washington Text does not require the filing of a financing statement in collateral, such as motor vehicles, for which a lien may be recorded on the face of a title certificate. WASH. REV. CODE § 62A.9-302(3) (1979). For example, Washington law provides for issuance of motor vehicle title certificates and for recording liens on the face of such certificates. *Id.* ch. 46.12.

43.

[W]hether any particular writing was intended to create or provide for a security interest is . . . a question of fact. In view of the Code's general policy to avoid technical formalities, we hold that the evidence permitted the trial judge to find Hartig's written application for transfer of title to Kreiger was sufficient to "create" a security interest in compliance with the requirements of section 9-203.

11 Wash. App. at 902, 527 P.2d at 486.

44. See WASH. REV. CODE § 62A.1-102(1) (1979).

45. *Id.* § 62A.1-201(44).

is usually the case with a purchase money security interest, in which arrangements are made between the prospective buyer and either the seller or lender for a security interest prior to the completion of the sale and delivery of the collateral to the buyer-debtor.⁴⁶ This will always be the case in inventory or accounts receivable financing in which the security interest is intended to cover inventory not yet acquired or accounts not yet created ("floating lien").⁴⁷

B. After-Acquired Property Clauses

One difficulty with earlier statutes dealing with security interests in personal property was that they did not explicitly recognize the validity of clauses purporting to create a security interest in collateral not yet belonging to the debtor. If the validity of a security interest in subsequently acquired property could not be assured, a financier of inventory or accounts receivable would be required to enter into a new agreement (and to file a new notice) with each shipment of inventory acquired by the debtor and with each account created by the debtor, or risk loss of his security interest upon attack by the debtor's other creditors. Section 9-204 specifically recognizes the validity of clauses extending the security interest to property first acquired by the debtor subsequent to the execution of the agreement,⁴⁸ subject only to an exception for consumer goods.⁴⁹ This section makes possible inventory and accounts receivable financing arrangements where the security interest will continue to attach to subsequently acquired inventory or subsequently created accounts without requiring either a new agreement or new steps to perfect.

The 1972 Text of section 9-204 eliminates subsections 9-204(2) and 9-204(4)(a) of the 1962 Text, a series of confusing provisions purporting to indicate when a security interest can first attach to certain kinds of property. In each case the drafters of the 1962 Text are reminding the reader that the collateral mentioned is either not yet personal property (*e.g.*, oil, gas, minerals in the

46. If the collateral consists of goods to be acquired in a contract of sale, Article 2 gives the buyer a "special property" in goods even prior to their delivery or to the acquisition of title by the buyer. *Id.* § 62A.2-501. This special property is sufficient for the attachment of a security interest. See *Rex Fin'l, Corp. v. Mobile America Corp.*, 119 Ariz. 176, 580 P.2d 8 (Ct. App. 1978) (a purchase money security interest attached upon the buyer's signing of a binding purchase agreement, even though buyer had not taken delivery).

48. WASH. REV. CODE § 62A.9-204(3) (1979).

49. *Id.* § 62A.9-204(4)(b).

ground, uncut timber) or not yet property at all (e.g., unplanted crops, unconceived animals, uncaught fish, an accord before the contract creating it is signed). Realizing that effective rules on borderline situations cannot be easily drawn by the legislature, the drafters of the 1972 amendments wisely left to the courts the matter of determining when a security interest can first attach.

The Washington Text of section 9-204, which otherwise conforms to the Official 1962 Text, was amended in 1974 to include a nonuniform subsection (6).⁵⁰ That subsection prevents attachment (and therefore perfection under section 9-303) of an inventory financier's security interest to livestock or meat products purchased by a packer or similar person for a period of up to ten days after they have been sold to a debtor who pays by check. Obviously inspired by the litigation culminating in the 1974 United States Supreme Court decision in *Mahon v. Stowers*,⁵¹ subsection 9-204(6) is clearly intended to permit a cattleman to accept a check from his purchaser and be assured of protection against the lien of the buyer's inventory financier should the buyer's check bounce. Article 2 provides limited but inadequate relief for sellers who deliver their goods to a buyer prior to receiving full cash settlement. The seller's right to reclaim his goods within ten days after delivery upon discovery that his buyer is insolvent under subsection 2-702(2) in case of a credit sale, and the seller's parallel right to reclaim within ten days of delivery upon dishonor of a check given for payment in a cash sale,⁵² are

50. This nonuniform section reads:

A security interest cannot attach to livestock or to meat or meat products made from such livestock, where (a) the livestock was sold to the debtor by another party, (b) this other party has been paid by draft or check, and (c) the draft or check remains outstanding; *Provided*, That a security interest may attach when the draft or check has been outstanding more than ten days.

Id. § 62A.9-204(6).

51. 416 U.S. 100 (1974). Livestock sellers took checks on delivery of their cattle to a Texas meat packer, who filed a Chapter XI petition before the checks, apparently promptly presented, were paid. Both the bankruptcy trustee and the packer's inventory financier opposed the cattlemen's petition to reclaim. The final disposition on remand to the court of appeals was that the selling cattlemen lost to the inventory financier pursuant to the Texas U.C.C. *In re Samuels & Co.*, 526 F.2d 1238 (5th Cir. 1976), *rev'g en banc* 510 F.2d 139 (5th Cir. 1975).

52. WASH. REV. CODE § 62A.2-702(2) (1979) specifically grants the credit seller 10 days to reclaim after delivery, but no provision expressly creates a parallel right for the cash seller who accepts a check which later bounces. The cash seller's right is presumably granted by § 2-507(2): "Where payment is due and demanded on the delivery to the buyer of goods or documents of title, his right as against the seller to retain or dispose of them is conditional upon his making the payment due." Official Comment 3 to § 2-507(2)

defeated by a good faith purchaser from the buyer.⁵³ Because the definition of "purchase" in subsection 1-201(32) includes taking by "mortgage, . . . lien, . . . or any other voluntary transaction creating an interest in property," the packer's inventory financier, relying on an after-acquired property clause, would defeat the cattleman attempting to reclaim his property on dishonor of the check. New subsection 9-204(6) will prevent the financier from establishing a superior claim if the cattleman moves with diligence to recover his goods upon promptly presenting the check and discovering its dishonor.⁵⁴

The protection afforded the cattleman in subsection 9-204(6) should be extended to all cash sellers of goods who accept a check as conditional payment, and perhaps to credit sellers. As to the former, certainly there is no intent to offer any credit to the buyer, the seller believing the instrument he is receiving will be honored. Consequently, no apparent reason exists for a seller

concludes with the statement: "The provision of this Article for a ten day limit within which the seller may reclaim goods delivered on credit to an insolvent buyer is also applicable here." Section 2-511(3) states in addition that "payment by check is conditional and is defeated as between the parties by dishonor of the check on due presentment."

53. *Id.* § 62A.2-702(3).

54. In *Mahon* the seller's efforts to reclaim were opposed not only by the inventory financier but also by the buyer's bankruptcy trustee. Obviously, the question whether the inventory financier prevails is a matter within the Code; the conflict between the trustee and the reclaiming seller, however, can only be settled under bankruptcy law. The Sixth Circuit Court of Appeals has been the leader in vindicating the rights of the seller who reclaims within § 2-702(2) against the trustee of the buyer. In *In re Mel Golde Shoes, Inc.*, 403 F.2d 658 (6th Cir. 1968), the Sixth Circuit held that the rights of the reclaiming seller were superior to those of the bankruptcy trustee claiming as a lien creditor under § 70(c) of the Bankruptcy Act. In *In re Federal's Inc.*, 553 F.2d 509 (6th Cir. 1977), the court described the seller's § 2-702(2) rights as a "state-created right of ownership," *id.* at 516, and not a statutory lien arising at bankruptcy. The court held the seller immune from the bankruptcy trustee's attack under § 67(c)(1)(A), as well as under § 70(c), of the 1898 Bankruptcy Act. *Id.* Finally, in the Bankruptcy Reform Act of 1978 Congress has resolved the controversy in favor of the seller by inclusion of § 546(c):

(c) The rights and powers of the trustee under sections 544(a), 545, 547, and 549 of this title are subject to any statutory right or common law right of a seller, in the ordinary course of such seller's business, of goods to the debtor to reclaim such goods if the debtor has received such goods while insolvent, but—

(1) such a seller may not reclaim any such goods unless such seller demands in writing reclamation of such goods before ten days after receipt of such goods by the debtor; and

(2) the court may deny reclamation to a seller with such a right of reclamation that has made such a demand only if court—

(A) grants the claim of such a seller priority as an administrative expense; or

(B) secures such claim by a lien.

11 U.S.C.A. § 546(c) (West 1979).

receiving a check to cover himself by reserving a security interest in the goods he is delivering.⁵⁵ As to the latter, an after-acquired property clause should not be allowed to enrich a financier who has not, during the ten-day reclamation period afforded under section 2-702(2), extended new value in reliance upon the debtor's acquisition of the seller's goods. Therefore, at a minimum, when the 1972 amendments are considered, the legislature should amend subsection (6) to read:

A security interest claimed in the debtor's inventory by way of an after-acquired property clause cannot attach to goods sold by another party to the debtor, or to their traceable proceeds, if the debtor has paid the other party by draft, until ten days after delivery of the goods to the debtor, or payment of the draft by the drawee, whichever first occurs.

Such language would offer the cash seller taking a check during the ten days after delivery complete protection from all security interests except one created for new value within the ten-day term.⁵⁶

V. PERFECTION

A. *The Requirement of Perfection*

Once a security interest has attached, it is valid and enforceable against the debtor.⁵⁷ Section 9-201 confirms that a

55. Any such Article 9 interest reserved would, of course, be prior to that of the existing financier, provided the seller followed the requirements of § 9-312(3) relating to purchase money security interests in inventory.

56. Alternatively, if the legislature decided to extend protection to the reclaiming credit seller acting under § 2-702, as well as to the reclaiming cash seller, such could be accomplished by deleting WASH. REV. CODE § 62A.9-204(6) (1979) entirely and by amending *id.* § 62A.2-207(3) to read:

the seller's right to reclaim under subsection (2), as well as the seller's right to reclaim under § 2-507(2) is subject to the rights of a buyer in ordinary course or other good faith purchaser under this Article (Section 2-403) who extends new value to the buyer subsequent to the buyer's receipt of the seller's goods.

(new language in italics).

57. *Id.* § 62A.9-201. A recent case involving §§ 9-201 and 9-203(1) presents the not unusual situation of a real estate broker improperly preparing documents in a sale in which he was acting as agent. The Washington Court of Appeals confirmed the buyer's unencumbered title to the personal property transferred pursuant to the sale of a business on credit when the seller's agent failed to prepare a proper security agreement covering the personal property. *Hecomovich v. Nielsen*, 10 Wash. App. 563, 518 P.2d 1081 (1974). The court, however, awarded the seller damages against the escrow agent based on the "value of the loss of the security interest" caused by its negligence. *Id.* at 573, 518 P.2d at 1088.

security agreement is a contract between the debtor and the secured party enforceable according to its terms upon the debtor's default. This section further provides that a security agreement is valid according to its terms against third parties except as otherwise provided in Article 9. Notwithstanding this language, with few exceptions, in order to afford any meaningful protection against third parties, a security interest must be perfected. In particular, an unperfected security interest is subject to defeat by a creditor who obtains a lien on the collateral by judicial process (the "lien creditor rule")⁵⁸; any conflicting secured creditor who obtains a security interest in the same collateral and perfects, whether before or after the unperfected security interest attaches,⁵⁹ and certain buyers and transferees.⁶⁰ Significantly, under federal bankruptcy law the bankruptcy trustee is granted the powers of a judicial lien creditor as of the date of the debtor's bankruptcy⁶¹ and consequently can use section 9-301 to defeat security interests not perfected at that date.

In the 1962 Text of subsection 9-301(1)(b) an important exception exists to the lien creditor rule: the intervening lien creditor must be without actual knowledge of the unperfected

58. WASH. REV. CODE § 62A.9-301(3) (1979). Section 9-301(3) contains a definition of lien creditor that includes an assignee for the benefit of creditors. Prior to the adoption of the U.C.C., such assignees, who by the voluntary action of an insolvent debtor are liquidators appointed under state law for the benefit of general creditors, had no greater right to the debtor's property against adverse claimants than did the debtor himself. Under the U.C.C., however, the clear intent is that a general assignee shall prevail in the debtor's property over interests unperfected at the time of the assignee's appointment. The U.C.C., however, does *not* contain a definition of assignee for the benefit of creditors. The question arises whether the language of § 9-301(3) was meant to include other liquidators appointed under state law, namely receivers appointed by petition of the debtor's creditors. Professor Shattuck assumes without discussion that such is the case. Shattuck, *Secured Transactions (Other Than Real Estate Mortgages)—A Comparison of Article 9 of the Uniform Commercial Code and the Pre-Code Washington Law*, in COLLECTED ESSAYS ON THE UNIFORM COMMERCIAL CODE IN WASHINGTON 638, 688 (1967). In *Morse Electro Prods. Corp. v. Beneficial Indus. Loan Co.*, 90 Wash. 2d 195, 579 P.2d 1341 (1978), the supreme court had the opportunity to resolve this question but apparently failed to recognize the issue. The court, citing *Western Elec. Co. v. Norway Pac. Constr. & Drydock Co.*, 124 Wash. 49, 213 P. 686 (1923), merely reiterated pre-Code law that "the receiver stands in the shoes of the insolvent." 90 Wash. 2d at 198, 579 P.2d at 1342. Had the court instead determined that a receiver comes within the definition of a lien creditor, the losing claimant (an assignee of the receiver's rights to the fund in issue and an unperfected secured party) may well have prevailed because the court assumed the winning party perfected its security interest subsequent to the date of the receiver's appointment.

59. See WASH. REV. CODE §§ 62A.9-301(a), .9-312(5) (1979).

60. *Id.* § 62A.9-301(1)(c), (d).

61. 11 U.S.C.A. § 544(a) (West 1979) (repealing 11 U.S.C. § 110(c) (1976)).

security interest to prevail. This provision, inconsistent with the pure "race" rules of section 9-312 relating to priority among competing security interests in which knowledge plays no role, injects an element of factual uncertainty into an otherwise predictable priority scheme and was deleted in the 1972 Text.⁶²

The 1972 Text eliminates another troublesome provision of the 1962 Text of section 9-301, the final sentence of subsection 9-301(3). This sentence appears to impute to the trustee of a bankrupt debtor actual knowledge of an unperfected security interest if all lien creditors have such knowledge at the date of bankruptcy. Some commentators have observed that it is extremely doubtful that this provision is valid against the trustee under the Bankruptcy Act.⁶³

New subsection 9-301(4) resolves another question unanswered in the original text—priority between the lien of a levying creditor and a perfected secured party's interest for advances made after the levy on the collateral has been accomplished. Will the levy terminate the secured party's claim to priority in the collateral for the value of any advances subsequent to the levy, or will the initial filing guarantee priority over conflicting creditors for all advances thereafter made? Subsection 9-301(4) of the 1972 Text grants the perfected secured party absolute priority for all advances made during the first forty-five days after a competing levy is made and continued priority thereafter for advances made in ignorance of the lien or pursuant to a preexisting contractual commitment. Priority for the secured party over a later judicial lien creditor has been granted by virtually all judicial decisions under the 1962 Text,⁶⁴ but the need for statutory clarification remains acute as a result of the 1966 Internal Revenue Code amendments⁶⁵ governing priority conflicts between a properly filed federal tax lien and advances under an earlier filed security interest. Under these amendments, an

62. U.C.C. § 9-301(1)(b) (1972 version).

63. *E.g.*, S. RIESENFELD, CREDITORS' REMEDIES AND DEBTORS' PROTECTION 501 (2d ed. 1975). Also, under the Bankruptcy Reform Act of 1978 it is doubtful whether WASH. REV. CODE § 62A.9-301 (3) (final sent.) (1979), is valid against the bankruptcy trustee. *See* 11 U.S.C.A. § 547(b)(4)(B)(ii) (West 1979).

64. *E.g.*, *Friedlander v. Adelphi Mfg. Co.*, 5 U.C.C. REP. SERV. 7 (N.Y. Sup. Ct. 1968). The secured party also prevailed in the absence of a subsequent advance clause, where the advance was made while the debtor was still in debt and there was no change in the collateral. *In re Merriman*, 4 U.C.C. REP. SERV. 234 (S.D. Ohio 1967). Virtually all decisions agree with the *Merriman* result, the only contrary result coming in *Coin-O-Matic v. Rhode Island Hosp. Trust Co.*, 3 U.C.C. REP. SERV. 1112 (R.I. Super. Ct. 1966).

65. Federal Tax Lien Act of 1966, Pub. L. No. 89-719, 80 Stat. 1125 (Current version at I.R.C. § 6323 (b)-(d)).

advance within a forty-five day period after filing of the tax lien will have priority over the tax lien if the advance would enjoy priority under state law over a lien creditor levying on the collateral at the same instant the tax lien is recorded.⁶⁶ Until a definitive state statutory rule is adopted, the threat remains that the federal tax lien may be held to have priority.

B. *The Manner of Perfection*

Perfection is not defined in Article 9, but subsection 9-303(1) states in somewhat circular terms:

A security interest is perfected when it has attached and when all of the applicable steps required for perfection have been taken. Such steps are specified in Sections 9-302, 9-304, 9-305 and 9-306. If such steps are taken before the security interest attaches, it is perfected at the time when it attaches.⁶⁷

The steps referred to are those necessary to give third-party notice. This third-party notice is what turns the security interest from being little more than a contract right into a property right enforceable against most third-party claimants. The Code provides for two methods of notice: creditor possession of the collateral or filing in a public register a financing statement containing prescribed information about the security interest. In certain limited but rather important cases, however, a third party will not have notice because the Code allows for perfection of certain security interests without filing or taking possession.⁶⁸

Part 4 of Article 9 regulates the location of filing, contents of the financing statement, and other particulars surrounding the filing system. Most importantly, section 9-402 states what information the financing statement must contain, and section 9-401 states where it must be filed. The philosophy is one of simplicity, so that a good faith effort on the part of a secured creditor to comply will enhance the likelihood of successfully perfecting his interest. The contents prescribed by the 1962 Text of section 9-401 for the financing statement are names, addresses, and signatures of the debtor and secured party and a description of the collateral covered.⁶⁹ The 1972 Text dropped the requirement of the

66. For discussion of the effect of the 1966 amendments to the I.R.C., see *Texas Oil & Gas Corp. v. United States*, 466 F.2d 1040 (5th Cir. 1972).

67. WASH. REV. CODE § 62A.9-303(1) (1979).

68. See text accompanying notes 79-83 *infra*.

69. In the case of a fixture filing, § 9-402 requires certain additional information

secured party's signature, which served no substantive purpose and posed a trap for the unwary party who accidentally omitted it.

Because security interests are indexed by debtor's name, it is essential that the debtor's name be accurately stated. An incorrect debtor's name will cause a third person searching the record to miss security interests in that particular debtor's property; consequently, filing under an incorrect name will result in lack of perfection and probable loss of the collateral to competing claimants. Under the 1962 Code, however, there is no standard for determining the debtor's "correct" name—should one file under the debtor's legal name or trade name or must one file under both to be perfected?⁷⁰ Subsection 9-402(7) of the 1972

concerning the description and ownership of the real estate where the goods are located so the fixture filing can be properly indexed in the real property records system. The information requirements are not clearly spelled out in the 1962 Text. WASH. REV. CODE § 62A.9-402 (1979). The 1972 Text of § 9-402(5) clarifies precisely what information must be furnished for a fixture filing. For a discussion of fixtures, see text accompanying notes 166-82 *infra*.

70. See, e.g., *Douglas-Guardian Warehouse Corp. v. Esslair Endsley Co.*, 10 U.C.C. REP. SERV. 176 (W.D. Mich. 1971). An unusual problem involving an allegedly misfiled financing statement has been decided under Washington law by the Ninth Circuit. In *Siljeg v. National Bank of Commerce*, 509 F.2d 1009 (9th Cir. 1975), one Washington corporation merged into a second under an agreement that the surviving corporation would amend its articles of incorporation to assume a name identical to the company's premerger name. Although no amendment to the articles was actually filed, as required by Washington law, the Secretary of State issued on June 26, 1967, a certificate confirming the merger and a second certificate stating in part: "I . . . certify that the provisions of the Merger Amendment changes [*sic*] the name of the surviving corporation to Henry House Packing Company, Inc. . . ." 509 F.2d at 1010. The Secretary of State also altered the official records to reflect a name change of the surviving company. In apparent reliance on the above transactions, the defendant bank entered into a security agreement on June 30, 1967, covering inventory and accounts with the surviving firm. The defendant had already prefiled a financing statement under the name of Henry House Packing Company, Inc., as debtor, on June 15.

A proper amendment to the articles of the survivor was filed with the Secretary of State on November 9, 1967, but was back dated to June 26, 1967. *Pacific Nat'l Bank v. Kramer*, 77 Wash. 2d 899, 468 P.2d 436 (1970). The supreme court issued a writ of mandamus to correct the records to show that the legal name of the surviving corporation in the merger was not Henry House Packing Co., Inc., until November 9, 1967. Bankruptcy proceedings were opened on November 27, 1967.

The question before the Ninth Circuit was whether the defendant bank was properly perfected in the collateral. The district court had held as a matter of law that the "true name" of the debtor was as certified by the Secretary of State on June 26 and granted summary judgment for the bank upon the trustee's claim that the interest was not perfected until November 9. The circuit court reversed and remanded for trial on the issue of whether filing in the name of Henry House Packing Co., Inc., was seriously misleading to other creditors. The court rejected a "true name" analysis because then "priority of one creditor over another would turn on a mistake of the Secretary of State. The Uniform Commercial Code is directed toward commercial realities, not corporate technicalities."

Text specifically resolves this problem: filing under the debtor's legal name is both necessary and sufficient; inclusion of trade names does not affect the sufficiency of the financing statement.

The financing statement may describe the collateral by generic name (*i.e.*, "accounts, inventory and chattel paper," or "equipment") because the financing statement is intended merely as notice that a security interest is claimed in collateral of the nature listed. Third parties are expected to ask the named secured party for details of the security interest and the exact collateral it covers. Nevertheless, the financing statement will only effectively perfect the interest in such collateral as is both described in the agreement and listed by type on the financing statement. For example, a financing statement listing only inventory does not perfect a security interest in equipment.

The simplest possible filing system would be a central state-wide index for all financing statements except those covering property in which a real property mortgagee may also obtain an interest.⁷¹ To alert real estate holders, holders of security interests in fixtures, timber, and minerals must file in the county where the real property involved is located. This is the system

509 F.2d at 1012. The court directed the lower court to determine if Henry House was the name by which the surviving corporation was known and thus if there "[w]as information available in the relevant business community which put creditors on notice that they should have searched under the name Henry House Packing Co., Inc." *Id.* at 1013.

The Ninth Circuit's analysis in *Siljeg* is a reasonable and equitable solution to a difficult problem not covered by the 1962 Text of Article 9. Despite the addition of the first sentence of § 9-402(7) to the 1972 Text, Washington's adoption of this provision would not affect the Ninth Circuit's resolution of this problem. *Siljeg* involved a dispute about the precise legal name of the debtor and about the effect of the erroneous certificate issued by the State; the case did not involve an erroneous filing based on a mistaken use of a debtor's trade name instead of his legal name. Comment 7 to the 1972 Text makes clear that the drafters were thinking only in terms of resolving the trade name cases by inclusion of the first sentence of § 9-402(7).

71. No personal property interest in minerals can exist until the minerals have been severed from the ground, as is made clear in WASH. REV. CODE § 62A.2-107(1) (1979). Once at the mine mouth or well head, however, minerals can become collateral for a personal property security interest. Section 9-401(1) of the 1972 Text adds provisions for local filing of interests in extracted minerals and standing timber. No references to either are contained in the 1962 Text. For timber, at least, such was the case because a personal property security interest in standing timber is not recognized under the 1962 Code. Interestingly, there are no rules contained in Article 9 for determining priority between properly filed U.C.C. timber or mineral interests and real estate claimants, as there are in § 9-313 for resolving conflicts between fixture claimants and competing real estate interests. A related section is § 2-107(3), which states that a sales contract for standing timber or minerals to be extracted, when recorded in the real property records, "shall then constitute notice to third parties of the buyer's rights under the contract for sale." The U.C.C. financier's rights, once a financing statement is filed, would presumably be fixed against real estate interests as well.

proposed by the drafters and included in the Code as subsection 9-401(1), alternative one.⁷² Recognizing, however, strong political pressure in some states to preserve the greater degree of local filing which predominated under pre-Code law, the Code drafters also included as alternatives for subsection 9-401(1) two other filing schemes with progressively greater requirements for local filing. In fact, well over one-half of all U.C.C. jurisdictions have opted for alternatives two and three.⁷³

Once a proper financing statement is filed, the filing remains valid for five years,⁷⁴ or until a termination statement is filed, whichever occurs first.⁷⁵ If the secured party wishes to continue the validity of the filing beyond the initial five-year period, he must file a continuation statement before the end of the period.⁷⁶ Failure to do so terminates the perfection of the security interest and subordinates the now unperfected secured party to the claims of all perfected junior liens, whether perfected before or after the lapse of the secured party's perfection.⁷⁷ Refiling after lapse will reperfect the interest, but only from the date of refiling with no relation back.⁷⁸

Automatic perfection—that is perfection without either filing or possession by the creditor or his agent—is permitted very sparingly in Article 9. In only one significant case is automatic perfection granted for other than a short period of time

72. In the province of Ontario, where the basic structure of the Article 9 financing system was adopted in 1970 as the Personal Property Security Act, *ONT. REV. STAT.* ch. 344 (1970), the filing system has been further simplified, as each county has a filing officer to whom all financing statements are directed. This officer has a computer terminal coupled to a central register. The local officer enters each filing directly into the central register and can retrieve all information filed province-wide under the name of a given debtor. Because the filing officer is normally also the local officer in charge of the real property records, filings destined for the real estate records can generally be directed to the same person.

73. As noted earlier, Washington has adopted the second alternative of § 9-401(1). See note 18 *supra*. Adoption of any alternative of the 1972 Text of § 9-401(1) would add clarifying language on fixture filing and the references to local real estate filing of standing timber and mineral interests.

74. *WASH. REV. CODE* § 62A.9-403(2) (1979).

75. *Id.* § 62A.9-404.

76. *Id.* § 62A.9-403(2).

77. See *General Elec. Credit Corp. v. Isaacs*, 90 Wash. 2d 234, 581 P.2d 1032 (1978) (a security interest after lapse is subordinated to a federal tax lien perfected before the security interest lapsed; refiling after a gap does not reestablish the original priorities); *Morse Electro Prods. Corp. v. Beneficial Indus. Loan Co.*, 90 Wash. 2d 195, 579 P.2d 1341 (1978) (a security interest after lapse is subordinated to a second security interest perfected before the first lapsed).

78. *General Elec. Credit Corp. v. Isaacs*, 90 Wash. 2d 234, 581 P.2d 1032 (1978).

before possession or filing is required. That case is the purchase money security interest in consumer goods under subsection 9-302(1)(d).⁷⁹ Automatic perfection is permitted here for two reasons: one, because pre-Code law permitted unrecorded purchase money security interests in consumer goods, and hence the business community is accustomed to the risk of possible unrecorded interests when dealing with a consumer, and two, because the relative cost of filing financing statements in these primarily low dollar-value transactions would be prohibitive.⁸⁰ The purchase money financier may elect to file a financing statement if he wishes, and in fact there is an incentive to do so. An unfiled purchase money security interest in consumer goods is subject to defeat if before it is filed the consumer goods are resold to another consumer who is without actual knowledge of the security interest.⁸¹ This last provision demonstrates that the exception of automatic perfection in purchase money security interests is designed to meet the prior practices and the expectations of the business community.

The other significant cases of automatic perfection are to facilitate transactions in which relatively rapid filing or transfer

79. Washington U.C.C. § 9-302 contains at least two other less significant cases of automatic perfection: (1) a purchase money security interest in farm equipment with a purchase price not exceeding \$2500, WASH. REV. CODE § 62A.9-302(1)(c) (1979); and (2) an assignment of accounts or contract rights which does not "alone or in conjunction with other assignments to the same assignee" constitute a transfer of a "significant part of the outstanding accounts" of the transferor, *id.* § 62A.9-301(1)(e). Adoption of § 9-301 of the 1972 Text would eliminate the farm equipment instance, and adoption of the 1972 Text as a whole would remove the reference to contract rights in the assignment instance because the 1972 text eliminates contract rights as a separate class of collateral. Subsection 9-302(1)(e) nevertheless has generated substantial litigation concerning assignees of accounts who discover belatedly that their assignment constitutes a transaction subject to Article 9 and attempt to invoke this exception when their interests are attacked as unperfected. The scope of this exception to filing has already been litigated in Washington. In *Architectural Woods, Inc. v. State*, 88 Wash. 2d 406, 562 P.2d 248 (1977), the supreme court correctly required the party invoking the exception to establish that the assignment was "casual and isolated" under all of the circumstances of the transaction. *Id.* at 410, 562 P.2d at 250. The court specifically rejected the reasoning of cases from other jurisdictions which compare the dollar amount of the assignment in dispute with the total dollar value of all the debtor's accounts to determine if the assignment is a "significant part" of the debtor's accounts. See *Standard Lumber Co. v. Chamber Frames, Inc.*, 317 F. Supp. 837 (E.D. Ark. 1970).

Because the uncertainty of application of Washington U.C.C. § 9-302(1)(e) is the stuff of which lawsuits are made, no attorney should advise reliance on this exception under any circumstances.

80. J. WHITE & R. SUMMERS, *HANDBOOK OF THE LAW UNDER THE UNIFORM COMMERCIAL CODE* § 23-7, at 799 (1972).

81. WASH. REV. CODE § 62A.9-307(2) (1979).

of possession is expected after the transaction is consummated. Most important among these circumstances are the ten-day initial automatic perfection granted to all purchase money security interests in subsection 9-301(2), the initial automatic ten-day perfection in proceeds on disposition of collateral under subsection 9-306(3), and the initial automatic twenty-one day perfection in instruments and negotiable documents under the conditions contained in subsection 9-304(4).⁸² Finally, under subsection 9-304(5), instruments, negotiable documents, and goods in possession of a bailee other than goods for which a negotiable document is outstanding (primarily goods in a field warehouse) may be released to the debtor for up to twenty-one days for certain specific purposes without loss of perfection. If the documents or goods remain in the debtor's hands for more than twenty-one days, a filing must be made or perfection is lost; because filing is not effective for instruments, possession of instruments must be recovered within twenty-one days or the security interest becomes unperfected.⁸³

For most items of collateral, perfection can be obtained either by the creditor taking possession or by filing a financing statement. The nature of some items of collateral, however, requires that perfection occur by only one or the other method. Accounts and general intangibles are not represented by any particular piece of paper the possession of which confers special rights upon the owner. Consequently, there is no tangible evidence of an account or general intangible of which a creditor can take possession to give third-party notice of his claim. Therefore, perfection as to accounts and general intangibles is possible only by filing.⁸⁴ On the other hand, instruments confer rights on the party in possession which are superior to the claims of other persons, as provided by rules codified in Article 3 for negotiable instruments and Article 8 for investment securities. Allowing the perfection of property rights in such collateral by filing would contradict the free circulation policy of the holder in due course and the bona fide purchaser doctrines.⁸⁵ Therefore, a security

82. None of these provisions is altered from the 1962 Text.

83. WASH. REV. CODE § 62A.9-304(6).

84. *Id.* § 62A.9-302(1).

85. *See, e.g., id.* §§ 62A.3-302, .3-305 (negotiable instruments); *id.* § 62A.8-301 (investment securities).

Section 9-309 confirms the priority of these principles by providing that the rights of a holder in due course of a negotiable instrument and of a bona fide purchaser of an investment security are not affected by the rules of Article 9.

interest in money or instruments may be perfected only through possession,⁸⁶ except in those limited circumstances of short term automatic perfection just mentioned, at the end of which continued perfection rests in each case on the creditor obtaining possession of the collateral.⁸⁷ Security interests in the other items of collateral, namely goods, chattel paper, and negotiable documents, can be perfected either by filing⁸⁸ or by possession.⁸⁹

While a security interest can be perfected in a negotiable document by filing or by possession, one must consider what a document of title represents. Documents, governed by Article 7, constitute receipts issued by a bailee for goods deposited with him. Such documents may be issued by a freight forwarder or by a person in the storage business. In the former case, they are called bills of lading; in the latter, warehouse receipts. Any document can be issued in negotiable or nonnegotiable form.⁹⁰ A nonnegotiable document can be characterized merely as an acknowledgment by the issuer-bailee of his acceptance of the goods and a promise to hold and return the goods to the person in whose name the receipt is issued. Article 9 characterizes a security interest in goods in the possession of a bailee who has not issued a negotiable document as a security interest in the goods themselves.⁹¹ Such a security interest can be perfected by filing as to the goods under subsection 9-304(3) or by obtaining the bailee's acknowledgment that he is in possession of the goods as the secured party's agent, *i.e.*, perfection through possession. The acknowledgment may be through the bailee's issuing of a nonnegotiable receipt in the secured party's name.⁹² Nonnegotiable warehouse receipts are frequently used in financing arrangements called field warehousing⁹³ under which an inventory

86. U.C.C. § 9-304(1) (1972 version).

87. *Id.* § 9-304, Official Comment 1.

88. WASH. REV. CODE § 62A.9-304(1) (1979).

89. *Id.* § 62A.9-305.

90. *Id.* § 62A.7-104.

91. *See id.* § 62A.9-304(3).

92. *Id.*

93. Because no sure method of obtaining a nonpossessory interest in inventory existed in some states, field warehousing was used extensively prior to adoption of the U.C.C. *See generally* 1 G. GILMORE, *supra* note 38, at §§ 6.1-.5. Field warehousing created a possessory security interest in the debtor's inventory through the medium of the field warehousing firm acting as agent for the secured party. Because field warehousing is nothing more than a pledge, it is not treated separately in Article 9, except in § 9-304(3). Even after the advent of the U.C.C. floating lien, field warehousing continues to be used in those situations where direct inventory control by the secured party is considered necessary or desirable. For field warehousing to be a valid security device, however, the

financier actually takes possession of the inventory of the merchant he is financing through the medium of a professional bailee. The bailee sets up storage facilities on the debtor's property, takes possession of the collateral, and issues to the financier nonnegotiable warehouse receipts representing the goods in the bailee-agent's possession. Thus, in substance, there cannot be a security interest in nonnegotiable documents independent of the goods they represent.

In contrast to nonnegotiable documents, negotiable documents in the hands of a holder to whom they have been duly negotiated⁹⁴ give rights in the goods themselves free and clear of the claims of any third party to the goods,⁹⁵ subject only to three situations that are outside the scope of this paper.⁹⁶ This means, first, that a security interest in goods properly perfected by filing, which is created before they have been delivered to a bailee who has issued a negotiable document, is defeated by a third party to whom the document is duly negotiated; second, that a person who perfects a security interest in a negotiable document by filing (as might be the case if the document were proceeds upon the disposition of other collateral) will also be defeated by due negotiation of the document to a second secured party. These principles are reiterated in section 9-309, which states that a holder of a duly negotiated document of title takes priority over an earlier security interest even though it may be perfected.

A security interest in chattel paper can be perfected either by possession under section 9-305 or by filing under subsection 9-304(1). Chattel paper frequently arises as proceeds from the sale of inventory already subject to a security interest. In such event, the chattel paper itself is subject to the inventory financier's security interest, which continues automatically into proceeds under subsection 9-306(3).⁹⁷ What is the legal situation if the debtor fails to deliver the chattel paper to this financier but instead sells or assigns the rights embodied in the chattel paper to a third party, who gives a new value and takes possession of the paper? A conflict then exists between a claimant of a security

collateral must in fact be removed from the debtor's control, if only by segregation under lock and key on the debtor's premises. See *Business Factors, Inc. v. Taylor-Edwards Warehouse & Transfer Co.*, 21 Wash. App. 441, 585 P.2d 825 (1978).

94. See WASH. REV. CODE §§ 62A.1-201(20), .7-501(4) (1979).

95. *Id.* § 62A.7-502.

96. See *id.* §§ 62A.7-205, .7-402, .7-503.

97. As discussed in the text at notes 166-82 *infra*, methods of perfection in proceeds have been substantially altered from the 1962 to the 1972 Text.

interest in the chattel paper by filing and a claimant of a security interest by possession. Section 9-308 determines that the possessory security interest prevails in most cases. Article 9 therefore grants the possessor of chattel paper rights similar to, but not quite as sweeping as, the rights of persons in possession of commercial paper granted in Articles 3, 7, and 8.

The discussion of perfection thus far has omitted one economically significant kind of personal property—automobiles and other vehicles subject to certificate of title statutes. Every state of the United States now has a statute requiring the issuance of a title certificate at the time of any new registration of an automobile.⁹⁸ Under each of these laws, any security interest claimed in the vehicle must be entered on the certificate of title form by the proper state authorities. The Code does not govern the issuance of title certificates nor determine to what vehicles title certificate statutes extend. Subsections 9-302(3)(b) and (4), however, recognize that entry of a lien on a title certificate constitutes perfection for U.C.C. purposes.⁹⁹ Also, title certificates do not issue on vehicles that have not left the dealer's stock. Hence, the Code's perfection requirements govern security interests in vehicles while they remain inventory held for sale.¹⁰⁰ The 1962 Text of section 9-302 does not expressly state that security interests in dealer inventory are subject to the normal filing requirements; the 1972 Text makes the point clear.

VI. SPECIAL PRIORITY PROBLEMS FOR PERFECTED SECURITY INTERESTS

In the following paragraphs a number of special problems concerning perfected security interests will be covered. These include inventory and accounts receivable financing, validity of Code financing in the event of the debtor's bankruptcy, conflict among liens on the same collateral, continuation of perfection in collateral and its proceeds upon disposition of the collateral by the debtor, overlap of personal property and real property law, and interstate movement of collateral or of the debtor.

98. For a list of certificate of title laws, see Meyers, *Multi-State Motor Vehicle Transactions Under the Uniform Commercial Code*, 30 OKLA. L. REV. 834, 890 (1977).

99. Subsections (3) and (4) of § 9-302 were reformulated in the 1972 Text to make the meaning clearer, but no change in substance was made from the 1962 Text.

100. WASH. REV. CODE § 62A.9-302(3) (1979).

A. *Validity of After-Acquired Property Clauses in Bankruptcy*

When the Code was first promulgated, one of the most controversial features of Article 9 was the specific authorization, now contained in subsection 9-204(1) of the 1972 Text, of after-acquired property clauses in inventory and accounts receivable financing. The effect of an after-acquired property clause is simple. The creditor's security interest continues to attach to collateral obtained subsequent to the original attachment of the security interest. Thus, under the Code if a security interest has been perfected by the filing of a financing statement and the debtor obtains new collateral to which the security interest attaches, it is immediately perfected in the new collateral without the necessity of a further filing. In practice, this means that a financier can maintain his security interest as the debtor sells and acquires replacement inventory or as the debtor collects accounts and creates new accounts by further sales.

The controversy surrounding after-acquired property clauses revolved around the trustee's power to avoid preferential transfers under section 60 of the Bankruptcy Act of 1898.¹⁰¹ The proper resolution of this alleged difficulty occupied much of the effort of the country's chief commercial law scholars for more than for a decade.¹⁰² Under the provisions of section 60, the bankruptcy trustee could defeat a security interest perfected in the bankrupt's property within four months preceeding bankruptcy under two conditions: (1) the indebtedness existed before the interest was perfected and (2) the secured creditor had cause to believe the debtor was insolvent at the time his interest became perfected. Since inventory or accounts receivable financing requires careful policing of the debtor and his financial condition, a secured creditor almost always has extensive information concerning his debtor's financial position. Therefore, it was

101. 11 U.S.C. § 96 (1976) (repealed 1978).

102. The Ninth Circuit in *DuBay v. Williams*, 417 F.2d 1277 (9th Cir. 1969), cited a total of 19 law review articles published between 1959 and 1969 on the validity of U.C.C. inventory and accounts receivable financing. *Id.* at 1280 n.2. The *DuBay* court sustained the U.C.C. financing scheme in the face of attack by the debtor's bankruptcy trustee. In the years following, however, still more articles flowed from the pens of the country's most eminent bankruptcy "bulls" and financing experts. See, e.g., Countryman, *Code Security Interests in Bankruptcy*, 75 *COM. L.J.* 269 (1970); Kripke, *Inventory and Receivable Financing Under the Uniform Commercial Code and The Bankruptcy Act*, 87 *BANKING L.J.* 579 (1970).

widely predicted that inventory and accounts receivable financing under U.C.C. after-acquired property clauses would fail because under the superior federal bankruptcy statute, the security interest would be declared invalid on all inventory acquired or accounts receivable created within four months of the debtor's ensuing bankruptcy if no new advance of money was made at the time the debtor received the inventory or created the accounts. The drafters of Article 9 recognized this threat and attempted to avoid the effect of the Bankruptcy Act by including section 9-108, which states that the attachment of a security interest under an after-acquired property clause to collateral newly acquired in the ordinary course of the debtor's business will be deemed to have been for new value and not for an antecedent indebtedness. Clearly, section 9-108 is an attempt to control the meaning of words in a federal statute, and, as such, is ineffective.¹⁰³ Notwithstanding the apparent problem in statutory language, the Code's inventory and accounts receivable financing schemes were upheld in every reported decision, and it was well established prior to the repeal of the Bankruptcy Act of 1898 that this financing technique will withstand the debtor's bankruptcy.¹⁰⁴ The problem solved itself because each court considering the validity of inventory or accounts financing recognized the economic necessity and the popularity of these financing techniques.

Congress has also recognized the need for, and upheld the validity of, U.C.C. inventory and accounts receivable financing in the new Bankruptcy Reform Act. Under subsection 547(c)(5) of the new Act such financing is sustained from the trustee's attack as a preferential transfer to the extent of the least dollar amount of collateral held during the ninety days¹⁰⁵ prior to bankruptcy. Therefore, under the new Act the secured party who carefully polices his collateral to insure that he remains fully secured at all times has nothing to fear from his debtor's bankruptcy.

103. See, e.g., *In re Platt*, 257 F. Supp. 478 (E.D. Pa. 1966).

104. See, e.g., *DuBay v. Williams*, 417 F.2d 1277 (9th Cir. 1969); *Grain Merchants, Inc. v. Union Bank & Savings Co.*, 408 F.2d 209 (7th Cir. 1969); *Rosenberg v. Rudnick*, 262 F. Supp. 635 (D. Mass. 1967). For a discussion on the 1978 Bankruptcy Reform Act's treatment of inventory and accounts receivable financing, see text accompanying note 105 *infra*.

105. The new Bankruptcy Act uses 90 days as the crucial prebankruptcy period in contrast to the 1898 Act's four month period. 11 U.S.C.A. § 547(c)(5)(A) (West 1979).

B. Mechanic's Liens

When an individual takes goods to a workman for repairs and later refuses to pay the bill, absent any agreement between owner and repairman, the repairman by common law or statute¹⁰⁶ has a lien on the goods in his possession for the value of his parts and labor. He may retain possession of the goods as against the owner until his bill is satisfied, and he may eventually sell the goods to realize his claim if he is not paid.¹⁰⁷

A more complex problem arises when the goods are collateral for a security interest perfected *before* they have been delivered to the workman. Can the workman retain the goods as against a secured party with a prior perfected security interest, if the secured creditor demands them after the debtor's default? Pre-Code rules of the various states were in disagreement over the relative priority of the two liens mentioned above. Some states, including Washington, followed the general rule of first in time is first in right, either by provision in their chattel lien statutes¹⁰⁸ or by case law,¹⁰⁹ and permitted the secured party to reclaim the goods from the statutory lienor; other states afforded workmen a super-priority over previously perfected interests, rationalizing that a workman cannot fairly be required to check the chattel mortgage filing index prior to commencing work on articles left for repair.¹¹⁰

In section 9-310 the Code attempts to regulate this problem by adopting as a general rule the super-priority of the mechanic lienor in possession over the previously perfected U.C.C. security interest, unless the statute under which the mechanic claims his lien specifically provides otherwise. The Washington Text of section 9-310 departs radically from the Official 1962 and 1972 Texts¹¹¹ by reversing the rule, so that the mechanic lienor in possession will take priority over the earlier perfected security

106. See, e.g., WASH. REV. CODE § 60.08.010 (1979).

107. See *id.* ch. 60.10.

108. E.g., *id.* § 60.08.030. This provision, which has remained unchanged since 1917, expressly subordinates the general possessory mechanic's lien on chattels to any lien perfected by filing prior to the moment work began.

109. In *Levitch v. Link*, 95 Wash. 639, 164 P. 233 (1917) (decided the same year the general chattel lien statute was amended to give mechanic's liens super-priority over subsequently recorded liens and previously unrecorded liens), the Washington Supreme Court held the livery stable keeper's (agister's) lien, WASH. REV. CODE ch. 60.56 (1979), was subordinate to an earlier perfected mortgage in the absence of statutory language expressly granting priority to the statutory lien.

110. See 2 G. GILMORE, *supra* note 38, at § 33.2.

111. The language of the 1962 Text of § 9-310 remains unchanged in the 1972 Text.

interest only if the lien is statutory and the statute expressly provides for such priority. With this modification, Washington has thus preserved its pre-Code rules subordinating possessor chattel liens to earlier perfected security interests.¹¹² Applying Washington section 9-310 in conjunction with the possessory lien statutes may result unexpectedly in a person receiving nothing despite his efforts to enhance or preserve the value of a secured party's collateral. The fault, however, lies with Washington's pre-Code lien rules. A first step in rectifying this apparent injustice could be taken by the adoption of the Official Text of section 9-310 when the 1972 U.C.C. amendments are considered by the legislature.

Notably, neither the 1972 Text of section 9-310 nor the Washington variation provides guidance for determining priority between a statutory lien granted to a laborer or materialman not in possession and a security interest in the common debtor's property filed prior to the beginning of the statutory lienor's work.¹¹³ Nor does section 9-310 provide any rule for determining priority between a perfected security interest and a statutory lien thereafter arising in favor of a governmental agency for taxes due

112. Only two possessory mechanic's liens are recognized in Washington: the general chattel lien, WASH. REV. CODE ch. 60.08 (1979), and the livery stable keeper's (agister's) lien, *id.* ch. 60.56. Because the former statute contains an express subordination to prior perfected interests, only the agister's lien is affected by the alteration from the Official Text of § 9-310. The Washington Supreme Court has declared the agister's lien subordinate to an earlier perfected interest in the absence of express statutory language granting priority. *Levitch v. Link*, 95 Wash. 639, 164 P. 233 (1917). See notes 109-10 *supra*.

113. A conflict may arise, for example, between an unpaid workman claiming a lien under the general laborers' and materialmen's lien statute, WASH. REV. CODE ch. 60.04 (1979), against a landowner's property for work performed installing fixtures and a security interest in the same fixtures properly perfected through a fixture filing by the supplier. If the words "encumbrances . . . of real estate" in § 9-313 are read to include statutory lienors, then this priority conflict is resolved under § 9-313. Section 9-313 probably should be read, however, as being limited to governing the relative rights of U.C.C. claimants against real property mortgagees and judicial lien creditors, as neither the section nor the official comments mention statutory lienors. Consequently, the answer to the priority conflict between fixture interests and statutory lienors must be found either in the lien statute itself or in common law. In Washington the answer is easy. In 1975 the legislature rewrote the laborers' and materialmen's lien statute, *id.* § 60.04.050, to provide, as in the chattel lien statute, *id.* § 60.08.030, for express subordination of the laborers' and materialmen's lien to prior perfected interests in the land owner's property.

Other conflicts may arise between a U.C.C. financier and claimants under such diverse statutes as the lumbermen's lien, *id.* ch. 60.24, and the restaurant employees' lien, *id.* ch. 60.34. Some Washington nonpossessory statutory liens provide for super-priority of the statutory lien claimant over preexisting perfected liens. See, e.g., *id.* § 60.24.038 (lumbermen's lien). Other nonpossessory statutory liens do not. See, e.g., *id.* § 60.20.020 (nurserymen's lien). No generalization can be made.

or for other sums owing from the debtor.¹¹⁴

C. Buyers of the Collateral

1. In General

Pursuant to sections 9-201 and 9-306(2), a security interest continues in collateral despite its sale, unless one of a number of important exceptions applies. The superior rights of buyers of chattel paper, instruments, and negotiable documents recognized in sections 9-308 and 9-309, and the right of a consumer buyer to take free of an unfiled purchase money security interest in consumer goods under subsection 9-307(2), have already been mentioned.¹¹⁵ Other than the secured party's authorization of a disposition free of his security interest, the only other exception is the important principle that a buyer of inventory sold in the ordinary course of the seller's business¹¹⁶ takes free of any security interest in the inventory created by his seller, even though its existence is known to the buyer.¹¹⁷ The principle is an old one in Anglo-American law¹¹⁸ and made inventory financing not especially attractive until the advent of the U.C.C. But the possibili-

114. I.R.C. § 6323(a) gives priority over a federal tax lien to security interests perfected before the federal tax lien has been filed. By amendments adopted in 1966, § 6323(c) also permits priority over a filed tax lien for a previously filed security interest with respect to advances made to the debtor and in property acquired by the debtor within 45 days after the tax lien has been filed. With respect to any advances made to, or property acquired by, the debtor more than 45 days after the tax lien has been filed, the federal government assumes priority. *Texas Oil & Gas Corp. v. United States*, 466 F.2d 1040 (5th Cir. 1972). For rules on filing United States tax liens, see I.R.C. § 6323(f)(1)-(4) and WASH. REV. CODE ch. 60.68 (1979). See also text accompanying note 66 *supra*.

115. See text accompanying notes 81 & 84-89 *supra*.

116. See WASH. REV. CODE § 62A.1-201(9) (1979).

117. *Id.* § 62A.9-307(1).

118. One pre-Code Washington case allowed a buyer to take free of the interest claimed by the conditional seller to his seller. *Schoenfeld's Standard Furniture Co. v. Stoe*, 175 Wash. 201, 27 P.2d 564 (1933). A more recent Washington case illustrates the extent of U.C.C. protection afforded by § 9-307(1) to the buyer in the ordinary course of business. As a means of perfecting its security interest in a used housetrailer held as stock in trade of its debtor, an inventory financier took physical possession of the title certificate. When the debtor, a mobile home dealer, sold the trailer and defaulted on its obligation to turn the proceeds over to the secured party, the latter repossessed the trailer from the buyers. The repossession violated the rights of the buyers, as buyers in the ordinary course from the debtor, despite the secured party's retention of the certificate. *Williams v. Western Surety Co.*, 6 Wash. App. 300, 492 P.2d 596 (1972). In the course of its opinion the court of appeals emphasized that § 9-307(1) is merely a special case of the more general rule on transfer of title by a merchant who is "entrusted" with possession of goods of the kind in which he deals. *Id.* at 301-03, 492 P.2d at 597-98. See WASH. REV. CODE § 62A.2-403(2)-(3) (1979).

ties for "rolling over" the security interest into subsequently obtained inventory under an after-acquired property clause, coupled with the opportunity to continue perfection in the proceeds of sale, make the impact of subsection 9-307(1) minimal for the diligent inventory financier.

2. *Buyers of Farm Products*

The rule protecting buyers in the ordinary course of business from an interest created by the seller in his inventory is subject to one important and very troublesome exception: a purchase of farm products¹¹⁹ from a farmer will not terminate a security interest created by the farmer unless, as provided in subsection 9-306(2), the financier authorized the sale.¹²⁰ Thus, whenever a farmer sells mortgaged crops or livestock absent express authorization and for any reason fails to remit the proceeds to the financier, the buyer is subject to a successful action for conversion, if he is unable to establish another legally sufficient basis for discharging the security interest.

Two cases in this area have reached the Washington appellate courts. In the first, *Central Washington Production Credit Association v. Baker*,¹²¹ the court of appeals reversed a summary judgment entered on behalf of a livestock financier and remanded for trial on the issue of whether plaintiff financier had either waived the requirement of prior written consent or authorized the sale "by its prior course of conduct" in similar transactions with other debtors. The court stressed that the record showed not only a series of fourteen sales over three years by the

119. Farm products are defined in § 9-109(3). In the context of the following discussion, farm products would be inventory in the absence of § 9-109(3), as they are produced by the farmer for sale in the ordinary course of business.

120. As a consequence, farm financiers' security agreements regularly contain clauses prohibiting sale without prior written authorization. The language contained in the agreement litigated in *Central Wash. Prod. Credit Ass'n v. Baker*, 11 Wash. App. 17, 521 P.2d 226 (1974) read: "[D]ebtor will not permit any of the collateral to be . . . sold, . . . without first having obtained the written consent of the Secured Party." *Id.* at 18, 521 P.2d at 226 (emphasis omitted). To judge from the description of farm financing practices in two widely separated areas of Washington, express authorization for a sale is seldom sought by the farmer in advance, unless he is dealing with a buyer apprised of the rule of § 9-307(1). Such buyers presumably will either demand the farmer produce written authorization or seek it directly from the farm financier. See *Southwest Wash. Prod. Credit Ass'n v. Seattle-First Nat'l Bank*, 19 Wash. App. 397, 577 P.2d 589 (1978), *rev'd*, 92 Wash. 2d 30, 593 P.2d 167 (1979); *Central Wash. Prod. Credit Ass'n v. Baker*, 11 Wash. App. 17, 521 P.2d 226 (1974).

121. 11 Wash. App. 17, 521 P.2d 226 (1974).

particular debtor without prior written or oral consent,¹²² but also a general practice not to enforce the provisions of similar agreements against other farmers.

In the more recent case, *Southwest Washington Production Credit Association v. Seattle-First National Bank*,¹²³ the court of appeals reversed judgment for the plaintiff crop financier and held that the financier's conduct in the *course of performance* of the security agreements constituted a waiver of its security when the collateral was sold by the farmers. The court found that the plaintiff had had frequent contact throughout the year with the farmers involved and was informed of, and acquiesced in, their plans to sell on credit to the particular buyer. Further, the plaintiff had not objected to the sale until the purchaser had become insolvent and failed to remit the agreed purchase price.¹²⁴ From these and other facts, the court in a well reasoned opinion, citing subsection 2-208(3) of the Sales Article,¹²⁵ concluded that plaintiff's course of conduct in administering the security agreements in question constituted overwhelming evidence that a waiver of the provision requiring written authorization prior to sale had occurred.¹²⁶ In a brief opinion, the Washington Supreme Court, however, unanimously reversed and reinstated the trial court's finding that the financier's acquiescence in the sale had been conditioned upon its receipt of full payment.¹²⁷ Nonpayment by the debtors reestablished the security interests in the collateral in the hands of the buyer and defeated the competing claim of

122. The financier objected to only one sale, the one in which proceeds had not been remitted. *Id.* at 19, 521 P.2d at 227.

123. 19 Wash. App. 397, 577 P.2d 589 (1978), *rev'd*, 92 Wash. 2d 30, 593 P.2d 167 (1979).

124. The financier sought to enforce its security interest in crops sold by the farmers on open credit to a food processor that became insolvent before completing payments to the farmers. The principal defendant was the processor's own inventory financier, which claimed a lien on the crops in the processor's hands as after-acquired collateral. *Id.* at 399, 577 P.2d at 590.

125. The court directly applied § 2-208(3) of the Sales Article to find a waiver in a transaction to which Article 2 is *not* technically applicable. While such an argument technically is incorrect, the court could have couched its use of § 2-208 in terms of application "by analogy." For a case discussing whether provisions of Article 2 apply to transactions within Article 9, see *Sherrock v. Commercial Credit Corp.*, 290 A.2d 648 (Del. 1972).

126. The court noted that the financier would have been adequately protected had it required the farmers to retain a purchase money security interest on the sale (and presumably assign it to the financier), or had it placed an express condition reserving its security on the sale. 19 Wash. App. at 402, 577 P.2d at 592.

127. *Southwest Wash. Prod. Credit Ass'n v. Seattle-First Nat'l Bank*, 92 Wash. 2d 30, 593 P.2d 167 (1979).

the buyer's inventory financier. The court held that the trial court's finding was supported by adequate evidence.¹²⁸ Although conceding that the question of waiver is one of fact, the supreme court's reversal of the court of appeals essentially indicates that a buyer who cannot establish written authorization for a sale has little expectation of prevailing in the absence of a showing of affirmative representations, either to himself or to the farmers, that the security interest will be waived.

The *Production Credit* case emphasizes that to insure clear title to all his purchases, the buyer of farm products must be advised of the practical necessity of undertaking a filing search under the name of every one of his farmer-sellers and dealing directly with any financier whom the search uncovers. The buyer can then judge for himself whether the risk of losing a purchase to a financier justifies the cost involved. More significantly, the case raises the question of whether continued special treatment of security interests in farm products, and of farmers as a group, is justified under modern economic conditions.

In the 1962 Washington Text of Article 9, references to farmers and farm products are limited to five substantive provisions:¹²⁹ subsections 9-204(4) and (6), regulating time of attachment of security interests to crops and livestock; subsection 9-302(1)(c), granting automatic perfection of purchase money interests in farm equipment of relatively low value; subsection 9-307(1); and subsection 9-401(1), requiring local filing of interests in farm collateral. All of these special provisions relating to farms and farm products should be eliminated from a revised Washington Text of Article 9.

Two of these provisions, the rules for attachment to crops and automatic perfection for interests in farm equipment, would be deleted by adoption of the 1972 Official Text. A third, non-uniform subsection 9-204(6), added to protect the cash seller of livestock from losing his property to a meat packer's inventory financier in the event a check taken in payment is dishonored, should be extended to all sellers for the compelling reasons previously discussed.¹³⁰

Now that the Code has been in effect for over twelve years, the convenience and simplicity of the new central filing system

128. *Id.* at 34, 593 P.2d at 169.

129. In addition, the definition of farm products is contained in WASH. REV. CODE § 62A.9-109(3) (1979).

130. See text accompanying notes 50-56 *infra*.

for all security interests (other than those intended to be indexed in the local real property records) has become obvious. No need exists for continued local filing of interests in farm collateral. A single central filing eliminates risk to both the financier and searcher in determining either the county of the farmer's residence or the county where crops are located. Both the 1962 and 1972 Codes offer as a preferred alternative for the rules on filing location¹³¹ central filing for *all* interests except those intended to be perfected against competing real estate interests. Tradition should not be sufficient ground for retaining local filing. Unless a compelling reason for continued local filing can be established, the legislature should conform the filing rules to alternative one of subsection 9-401(1) to eliminate this unnecessary distinction.¹³²

The last and most significant farm provision is subsection 9-307(1) itself. The official comments offer no justification for the special treatment extended to buyers of farm products from farmers. Are they somehow different from other inventory sellers? No matter what the case might have been when the farming exception to subsection 9-307(1) was first included in early drafts of the Code, farm operations today are business concerns, whether large or small, and the provision deserves reexamination.¹³³ Subsection 9-307(1) does not protect the farmer because the beneficiaries are the farm lenders, who are sheltered from the normal risks and the normal policing obligations of their inven-

131. See U.C.C. § 9-401(1) (First Alternative) (1972 version).

132. Alternative two of § 9-401(1), adopted in Washington, also calls for local filing of security interests in consumer goods. WASH. REV. CODE § 62A.9-401(1) (1979). Alternative one would require central filing for consumer goods financing as well as farm financing. The same points—ease of access and certainty of proper location—justify central filing for consumer goods.

133. Previous commentators have argued for change in the rule of § 9-307(1) concerning farm products. See, e.g., Dolan, *Section 9-307(1): The U.C.C.'s Obstacle to Agricultural Commerce in the Open Market*, 72 NW. U.L. REV. 706 (1977); Comment, "Farm Products" Under the U.C.C.—Is a Special Classification Desirable?, 47 TEX. L. REV. 309 (1969). But, as explained by Professor Hawkland, the federal government, as a major supplier and guarantor of farm credit, has opposed efforts to remove the farm products rule from the Official Text of the Code, and federal officials have threatened to seek federal legislation giving federally financed farm loans the same priority over farm product purchasers as presently accorded all farm lenders in the Code. A federal rule would clearly prevail over contrary state law where federal loans are concerned but would not affect loans from nonfederal sources. The threats directed by the federal government at the drafters of the Official Text should not dissuade legislatures from enacting on an individual basis the nonuniform amendment eliminating the special advantages accorded the farm financier. See Hawkland, *The Proposed Amendment to Article 9 of the U.C.C.—Part 1: Financing the Farmer*, 76 COM. L.J. 416, 420 (1971).

tory security agreements. It can hardly be maintained that farm lenders, whether commercial entities or federally-financed cooperative associations, are less sophisticated or less able to police the collateral than are other inventory lenders, or that farmers as a class are so much more dishonest borrowers that additional protection is required. Obviously, if there is risk that a farmer may sell the collateral to the detriment of the lender, lending costs—both policing and losses—will rise. But these are costs of doing business and may be shifted forward to the farmer as slightly higher rates and from the farmer forward to the buyer as slightly higher farm prices. Moreover, the commensurate buyer protection arising from repeal of the farm products provision of subsection 9-307(1) should lower costs in an amount equal to the costs of the change in law. The Washington Legislature should amend subsection 9-307(1) to delete all reference to farmers and farm products in order to render inventory financing practices uniform throughout all industries.¹³⁴

D. Competing U.C.C. Financiers—The General Rule

Subject to the rules favoring possessory interests in chattel paper and negotiable documents and to rules granting priority to purchase money security interests under certain conditions, the general rule of priority among conflicting security interests in the same collateral under the 1972 Text is that the first to file a financing statement or to perfect in the collateral will prevail.¹³⁵ This priority rule is based upon a major departure from pre-Code Washington law:¹³⁶ introduction of so-called “pre-filing,” permitting the secured creditor to file a financing statement before the transaction between the parties is completed (*i.e.*, before the security interest has attached).¹³⁷ Thus, it is pos-

134. The suggested amendment of § 9-307(1) would render unnecessary the 1972 amendment to § 9-301(1)(c), which adds the words “or is a buyer of farm products in the ordinary course of business.”

135. U.C.C. § 9-312(5) (1972 version). See generally Jackson & Kronman, *Secured Financing and Priorities Among Creditors*, 88 YALE L.J. 1143 (1979). Of course, two secured creditors can alter the statutory priorities by entering into an agreement between themselves. Section 9-316 explicitly recognizes the validity of a subordination agreement made by anyone entitled to priority in the collateral.

136. In his 1967 analysis of pre-Code Washington law, Professor Shattuck doubted whether a pre-filing under the conditional sales or chattel mortgage statutes would be valid in the face of language requiring filing within ten days after the debtor was put in possession or the advance was made. Shattuck, *supra* note 58, at 691-92.

137. See WASH. REV. CODE § 62A.9-402(1) (1979). For a discussion of attachment, see text accompanying notes 35-47 *supra*.

sible and, in fact, normal practice for the secured party to file a financing statement prior to making his initial advance of credit to the debtor and even prior to signing the definitive security agreement. Because the U.C.C., in further contrast to pre-Code Washington law,¹³⁸ grants no grace period of initial automatic protection *after* attachment for purpose of perfecting any security interest requiring filing or possession (other than the ten days for purchase money security interests and interests claimed in collateral received as proceeds, and the twenty-one days for certain interests in documents and instruments), creditors *must* prefile to avoid any gap between attachment and perfection which might allow another interest to obtain priority.¹³⁹

The first to file or perfect rule under the 1972 Text can be further illustrated by two examples, the second of which will also illustrate a logical defect in the Washington Text. (1) A files on January 2, but first completes his agreement with the debtor and makes an advance on January 10. In the interim, on January 5, B files and makes his advance on the same collateral, thus perfecting prior to A. But A wins as first to file or perfect. This

138. Washington pre-Code law allowed grace periods for filing under the Chattel Mortgage Act, ch. 156, 1929 Wash. Laws 406 (repealed 1965); Conditional Sales Act, ch. 106, 1893 Wash. Laws 253 (repealed 1965) (repeal effective 1967); Accounts Receivable Act, ch. 8, 1947 Wash. Laws 20 (repealed 1965); Trust Receipts Act, ch. 71, 1943 Wash. Laws 134 (repealed 1965); and the bill of sale statute, 1881 TERR. CODE OF WASH. ch. 172, § 2327 (repealed 1965). But the application of the grace period rules in Washington was particularly harsh. Except for the Trust Receipts Act and the bill of sale statute, filing under these statutes after the ten-day grace period had expired was of no effect. See *Clark v. Kilian*, 116 Wash. 532, 199 P. 721 (1921) (chattel mortgages); *Worley v. Metropolitan Motor Car Co.*, 72 Wash. 243, 130 P. 107 (1913) (conditional sales). The language relating to grace periods under the accounts receivable assignment statute was identical but never judicially tested. The Washington court in *Worley* was the only court to conclude under the Uniform Conditional Sales Act that an interest not perfected within the grace period was void.

In addition, the Washington rules as to when the ten-day period began were draconian. Under the conditional sales statute the period ran from the date shown on the conditional sales contract as the date of delivery of the collateral, even though it could be established that the date on the contract was entered in error. *Grunbaum Bros. Furniture Co. v. Humphrey Inv. Corp.*, 141 Wash. 329, 251 P. 567 (1926). No possibility for reform of the contract existed. See *Pacific Fin. Corp. v. Edwards*, 304 F.2d 224 (9th Cir. 1962). Under the express language of the Trust Receipts Act, filing was effective when it was accomplished, if first accomplished after the grace period ran. Ch. 71, 1943 Wash. Laws 134 (repealed 1965). The court similarly construed the Bill of Sale Act in *Umberger v. Berrian*, 195 Wash. 348, 80 P.2d 818 (1938).

139. Unlike the Washington result under pre-Code filing statutes, filing or taking of possession subsequent to the attachment of the security interest merely perfects the interest from the instant the filing or possession is accomplished, protecting the interest against lien creditors or secured parties who subsequently effect liens on the collateral. WASH. REV. CODE § 62A.9-303(1) (1979).

result is logical, even though *A* first perfected on January 10, because from January 2 any other creditor had constructive knowledge of *A*'s claim to an interest through the operation of the filing system. (2) As before, *A* files on January 2. On January 5, *B* makes his advance and perfects his interest by taking possession of the collateral. Under the 1972 Text *A* again wins as first to file or perfect. In both cases, *A*'s priority over *B* will continue for all future advances that he may make while his filing remains effective.¹⁴⁰

In the 1962 Text, however, subsection 9-312(5)(b) contains a special rule applicable only when one or both of the competing interests is a pledge or possessory interest. Illogically, a pledge perfected subsequent to a filing against the same collateral will defeat the previously filed interest if no credit has been advanced by the nonpossessory secured party prior to the perfection of the pledge. Consequently, in example (2), *B* will take priority over *A*. Of what value is the filing system if a filed financing statement does not protect a creditor against *all* Code interests thereafter created in the same preexisting collateral? In apparent response, this deviant provision was eliminated from the 1972 Text.

E. Competing U.C.C. Financiers—Purchase Money Security Interests

Once a debtor has entered into a security agreement extending to after-acquired property, any subsequent acquisition of the same type of collateral will immediately be subject to the security interest. If the secured party has properly filed his financing statement, under the general rule of subsection 9-312(5)(a), even a credit seller thereafter delivering such property to the debtor and retaining a security interest to enforce payment of his purchase price will be subordinate to the earlier interest. Recognizing that credit sellers contribute new value to the debtor's estate in the same amount as the value of the security they claim and therefore do not diminish the assets available to the holder of the earlier interest, the drafters of Article 9, in subsection 9-312(3), provided for a special super-priority for purchase money security interests created under circumstances described above.

The Code differentiates between purchase money interests

140. U.C.C. § 9-312(7) (1972 version).

in inventory and purchase money interests in all other collateral. With respect to the latter, the 1972 Text of subsection 9-312(4) accords the purchase money interest priority in the collateral *and* its identifiable proceeds if perfected before, or within ten days after, the debtor receives possession of the collateral. With respect to inventory purchase money security interests, the Code imposes more stringent conditions and offers a lesser degree of priority over competing interests arising under after-acquired property clauses. The holder of a purchase money interest in inventory must (1) have perfected his interest when the debtor receives possession of the collateral, which means in practice he must file his financing statement before making delivery, *and* (2) as prescribed in subsection 9-312(3)(b), (c), and (d), he must notify holders of conflicting after-acquired property interests. Having met these conditions, the purchase money inventory financier has priority in the inventory itself. Nevertheless, his position is somewhat insecure because his priority in the proceeds of sale is limited by the 1972 Text to cash proceeds only, as defined in subsection 9-306(1).¹⁴¹

Only one reported Washington decision, *Manufacturers Acceptance Corp. v. Penning's Sales, Inc.*,¹⁴² relates to the special priority rules for purchase money interests under subsections 9-312(3) and (4). The narrow holding of the case is that a purchase money security interest in inventory will be subordinated to the after-acquired property clause of an earlier inventory financier unless the purchase money claimant strictly observes the perfection and notification requirements of subsection 9-312(3).¹⁴³

So stated, the holding is erroneous because subsection 9-312(3) is intended to govern priority only between the inventory purchase money interest and a previously *perfected* claimant to the same collateral, whose priority would otherwise be established under subsection 9-312(5)(a), according to which the first to file in the collateral wins. Subsection 9-312(3) states only that an

141. References to priority in *proceeds* of the original collateral for the holder of purchase money interests satisfying § 9-312(3) or (4) first appear in the 1972 Official Text. These provisions were added to aid in resolving the hotly debated issue of priorities in proceeds. Neither subsection of the Washington Code mentions proceeds at all. See text accompanying notes 151-65 *infra*.

142. 5 Wash. App. 501, 487 P.2d 1053 (1971).

143. *Id.* at 508-09, 487 P.2d at 1058. Because, however, the conflict between the competing inventory claimants in that case did not involve rights to proceeds, the decision would not be affected by the 1972 amendments to § 9-313(3) and (4).

inventory purchase money interest has priority over a conflicting interest if all of the conditions of the subsection are met. It does *not* state that the conflicting interest has priority if the requirements are *not met*, as the court's analysis implies.¹⁴⁴ Rather, subsection 9-312(5) governs all cases not within the other subsections of section 9-312, "including cases of purchase money interests which do not qualify for the special priorities set forth in subsections (3) and (4)."¹⁴⁵ Therefore, if no effective financing statement has been filed for either the previously existing security interest or the purchase money interest at the time inventory is delivered to the debtor, subsection 9-312(3) will not afford the purchase money interest priority. Priority, however, will still be accorded the purchase money interest if its holder files a financing statement before the holder of the conflicting interest files.

The facts of the *Penning's Sales* case also raise the question of whether the secured creditor claiming priority in the inventory by virtue of his after-acquired property clause had in fact made an effective filing with respect to the collateral at issue before the inventory purchase money interest was itself filed. The court did not explicitly so hold. If the rationale of the opinion is that such a filing is not necessary on the part of the preexisting secured creditor, the case is incorrectly decided.

In the course of the transactions involved in *Penning's Sales*, the original debtor, a proprietorship under the Penning name, incorporated under the name of Penning's Sales, Inc. The claimant of the after-acquired property interest had entered into a security agreement with the proprietorship and filed a financing statement under the Penning name on July 1, 1967. After the first financier filed, but before the incorporation, a manufacturer made an initial shipment of inventory on credit to the debtor.¹⁴⁶ On March 13, 1968, shortly after receipt of this initial shipment, the incorporation occurred and all subsequent shipments of the inventory under dispute apparently were made to the corporation. On April 4, 1968, the manufacturer obtained a security agreement with the corporation and filed a financing statement covering the inventory. Thereafter, on April 12, 1968, the original financier entered into a new security agreement with the corpo-

144. *Id.* at 509, 487 P.2d at 1058.

145. WASH. REV. CODE § 62A.9-312(5) (1979).

146. The seller originally characterized the relationship as a warehousing arrangement, but the court properly interpreted the transactions as either consignments or credit sales. 5 Wash. App. at 505-06, 487 P.2d at 1056.

ration and filed a financing statement. Presumably, both financing statements were filed in the name of the corporation.

Under these facts, the original financier can prevail only if his filing on July 1, 1967, is effective to perfect an interest in the inventory subsequently acquired by the new corporation. Assuming substitution of the corporation as debtor in the first financier's original security agreement, under the after-acquired property clause the first financier's interest would attach to the inventory supplied to the corporation by the manufacturer. The problem arises that upon the substitution the original financing statement against the proprietorship could not have been found by a search under the corporate debtor's name.¹⁴⁷ The original financing statement, therefore, would certainly appear to have become ineffective, absent the provisions of new subsection 9-402(7), second sentence,¹⁴⁸ and the interest in new collateral acquired by the corporation would have been unperfected until the new April 12 statement was filed under the corporate debtor's name. The opinion, however, records no finding that the

147. Had the new corporation not been substituted into the original security agreement in place of the proprietorship prior to April 4, there would not even have been any attachment of the original party's interest to collateral newly acquired by the corporation.

148. The problems of change of name and change of identity of the debtor have been expressly considered in § 9-402(7) of the 1972 Text. Assuming that a successor debtor, with the approval of the secured party, had been substituted for the original debtor in the security agreement so that the security interest could attach to property thereafter acquired by the successor, under § 9-402(7)(2d sent.), the original secured party would prevail under the facts of *Penning's Sales*. After the original filing in the name of the proprietorship (the original debtor) had become seriously misleading to the creditors of the corporation, the 1972 Text would allow a four-month grace period, during which the original filing would remain effective to perfect the interest in collateral acquired by the successor, even though the earlier filing could not be found by a search under the successor's name. Failure to refile in the name of the successor (the corporation) within the four-month period (which would begin March 13) would result in lapse of the original filing statement and loss of perfection by the first secured party. Filing on April 12, however, would result in continuous perfection and would defeat the April 4th filing by the second inventory claimant.

Section 9-402(7)(2d sent.), provides only one of several situations in which a filing statement is effective even though it might not be found by a search under the debtor's true name. Others are U.C.C. § 9-103(1)(d) and (3)(e) (1972 version) (interstate movement of the collateral or of the debtor's location); *id.* § 9-401(3) (change in the use governing location of filing); *id.* § 9-402(7)(3d sent.) (transfer of collateral from the debtor to third parties after an effective filing has been made); and *id.* § 10-102(2) (transition provision allowing continued perfection without refile of interests perfected under pre-Code law). To maintain the predictability of what third parties must investigate to discover perfected interests, judicial decisions should not expand these exceptions to the general rule that a filing should be discoverable under the debtor's name upon a search in the proper location in the U.C.C. files.

July 1, 1967, filing continued effective, either because it was *not* seriously misleading,¹⁴⁹ or because the manufacturer had actual knowledge of a substitution of the corporate debtor into the financing agreement, which would somehow serve to continue the earlier filing's perfection of the security interest against him.¹⁵⁰ The conclusion is inescapable that the court did not fully appreciate what it was deciding in *Penning's Sales*.

F. Competing U.C.C. Financiers—Perfection and Priority in Proceeds

1. Perfection

A creditor taking a security interest in consumer goods or equipment generally need not concern himself about continuation of his interest in proceeds of the original collateral.¹⁵¹ Such collateral is not bought for resale, and in any event a disposition is not effective to terminate the security interest, unless the creditor agrees to a sale free of his interest under subsection 9-306(2), or unless subsection 9-307(2), consumer's resale to a consumer, applies. With inventory, however, a sale by the debtor to a buyer in the ordinary course of business terminates the financier's interest in the collateral.¹⁵² To afford the secured party

149. What is "seriously misleading" under § 9-402(7) of the 1972 Text is a question of fact, dependent on a determination of whether searching creditors should have found the financing statement. U.C.C. records are generally closed files with no public access. A filing clerk upon payment of a search fee will determine whether filings exist under the precise name furnished by the searching party; it is not the clerk's job to tell the searching party whether there are filings under similar names. Indeed, who can really decide what is a similar name? The only reported decision rendered under Washington law regarding sufficiency of the debtor's name on a financing statement is *Siljeg v. National Bank of Commerce*, 509 F.2d 1009 (9th Cir. 1975), discussed at note 70 *supra*.

150. There is no provision in Article 9 to cover such a case. The closest provision would be WASH. REV. CODE § 62A.9-401(2) (1979), which renders a financing statement filed in the wrong location (centrally, or locally, or in the real property records) effective to perfect the interest reported thereon against anyone who has actual knowledge of the contents of the financing statement. Section 9-401(2) would not apply, however, because the interest reported on the financing statement was claimed in the property of the proprietorship, not the corporation. The inventory involved would never have been property of the proprietorship.

151. Should the collateral be stolen or destroyed, proceeds of insurance obviously become important. A 1972 modification to the Official Text of § 9-306(1) makes clear that insurance proceeds constitute proceeds within the meaning of Article 9, resolving a point that had been decided adversely to the secured creditor in several court proceedings. See, e.g., *Quigley v. Caron*, 247 A.2d 94 (Me. 1968); *Universal C.I.T. Credit Corp. v. Prudential Inv. Corp.*, 101 R.I. 287, 222 A.2d 571 (1966).

152. WASH. REV. CODE § 62A.9-307(1) (1979). As discussed above, under § 9-307(1) a security interest in farm products is not defeated by sale unless the secured creditor

continuous protection, at least until the debtor acquires additional inventory, attachment and perfection of his security interest in the proceeds of sale is essential.

The 1972 Code's regulation of validity and perfection of a security interest in proceeds of the original collateral clarifies and simplifies the provisions of the 1962 Text. The 1972 Text differentiates between "cash" and "noncash" proceeds. Section 9-306(1) defines "money, checks, deposit accounts, and the like" as cash proceeds; everything else is noncash proceeds.

Under both the 1962 and 1972 Texts the security interest continues in (and attaches to) any identifiable proceeds on disposition of the original collateral, whether or not the security agreement so states.¹⁵³ Furthermore, under both the 1962 and 1972 Texts perfection continues automatically in *all* proceeds, regardless of the proceeds character, for ten-days after their receipt by the debtor.¹⁵⁴ Continued perfection after the initial ten days under the 1962 Text depends upon affirmative action by the secured party. Either the original financing statement must expressly claim perfection in proceeds,¹⁵⁵ or the creditor must, within the initial ten-day period after the debtor receives the proceeds, perfect his interest in them either by a new filing against the proceeds or by assuming possession of them. Failure to fulfill one or the other of these requirements causes perfection in the proceeds to lapse.

Under the 1972 Text, however, once the security interest is perfected in the original collateral by a properly filed financing statement, the interest continues automatically perfected beyond the initial ten-day period. No further action by the

assents to a sale free of the security interest, but the farm products financier will be equally as interested in proceeds as the inventory financier if it is not practical to pursue the buyer of the collateral. See text accompanying notes 133-34 *supra*.

153. Well-drafted security agreements will specify that the security interest covers proceeds of the original collateral and, at least in the context of inventory financing, will list by type each kind of proceeds that may conceivably arise.

154. WASH. REV. CODE § 62A.9-306(3) (1979).

155. To accommodate the secured party, the official form for the financing statement under the 1962 Text, Form UCC-1, provides a box to be checked if the secured party claims perfection in proceeds.

Only one reported Washington case has dealt with the claims of a U.C.C. secured party in proceeds. *Ellingsen v. Western Farmers Ass'n*, 12 Wash. App. 423, 529 P.2d 1163 (1974). Although the case was decided on other grounds, interestingly the secured party failed to check the proceeds box. Whether the failure resulted from inadvertence or lack of appreciation of its significance is, of course, impossible to determine; but the continuing automatic perfection in proceeds developed in the 1972 Official Text of § 9-306(3)(A) would seem to comport more closely with the natural expectations of less sophisticated creditors.

secured party is necessary to be perfected in identifiable cash proceeds under subsection 9-306(3)(b) and in those noncash proceeds under subsection 9-306(3)(a) in which an original security interest would be perfected by a filing in the same location.¹⁵⁶ Accounts receivable and chattel paper taken as proceeds of inventory, probably the two most significant kinds of noncash proceeds, would be covered under subsection 9-306(3)(a).¹⁵⁷ Subsection 9-306(3)(a) would also cover trade-ins of used goods taken as down payment on the purchase price of new goods.¹⁵⁸

If continuing perfection in proceeds is not granted automatically under either subsection 9-306(3)(a) or (b), of the 1972 Text, then, as explicitly stated in subsection 9-306(3)(c), perfection in the proceeds will terminate if the interest is not independently perfected by filing or possession prior to the end of the initial ten-day period. This last provision is directed at a troublesome ambiguity in the Washington Text. Under the 1962 Text of subsection 9-306(3) a security interest in an instrument taken by the debtor as proceeds on the sale of original collateral is perfected indefinitely by the original *filing*, that is, by checking the financing statement's proceeds box, despite the clear insistence on possessory interests in instruments stated in Official Comment 1 to section 9-304.¹⁵⁹ Thus, under the 1972 Official Text, continued

156. Although § 9-306(3)(a) and (b) of the 1972 Text generally absolve the financier of the necessity of specifically claiming proceeds on the original financing statement, one situation exists in which such a claim to proceeds must be made: if the secured party wishes to trace his security interest into noncash proceeds that are of a type other than the original collateral and that were acquired by using cash proceeds from the disposition of the original collateral. U.C.C. § 9-306(3)(a) (1972 version). Such a case, for example, would be an inventory financier's claim to equipment acquired through the use of cash proceeds generated by the sale of inventory covered in the security agreement. The secured party would be required to add such language as "equipment claimed as proceeds" to his financing statement.

Although the rule of § 9-306(3)(a) of the 1972 Code, or checking the proceeds box on the financing statement under the 1962 Code, will perfect a security interest in chattel paper or negotiable documents taken as proceeds, a possessory security interest in collateral of this nature may still defeat the perfected proceeds interest. As previously mentioned, a possessory interest in chattel paper may cut off interests claimed in the paper as proceeds under § 9-308. See text accompanying notes 25-26 *supra*. Likewise § 9-309 recognizes the rights of a holder of a negotiable document to whom the document has been duly negotiated; he will cut off the interest of a claimant to the document as collateral or as proceeds. See WASH. REV. CODE §§ 62A.7-501(4), .7-502 (1979).

157. See also U.C.C. § 9-401(1) (1972 version).

158. See *Howarth v. Universal C.I.T. Credit Corp.*, 203 F. Supp. 279 (W.D. Pa. 1962).

159. The third and fourth sentences of Official Comment 1 to § 9-304(1) read as follows:

With respect to instruments subsection (1) [of § 9-304] provides that, except

perfection in instruments taken as proceeds will require the secured party to assume possession within ten days after their receipt by the debtor.¹⁶⁰

2. Priority

The 1962 Text contains no express provision determining priority among conflicting security interests when the collateral in question is proceeds of the original collateral of one or more of the claimants. Conflicting claims in proceeds may occur in either of two principal cases. (1) Creditor A holds a perfected security interest in debtor's inventory and proceeds, and Creditor B has a perfected interest in debtor's accounts. Creditor B's accounts are necessarily proceeds of the sale of creditor A's inventory. (2) Creditor A sells property on credit and retains a purchase money security interest in the collateral, fulfilling the requirements of subsection 9-312(3) or (4), as applicable, to obtain a super-priority in the original collateral over Creditor B, who had previously obtained and properly filed a security interest with an after-acquired property clause in the same type of collateral. Upon disposition of the original collateral, will Creditor A's super-priority under subsection 9-312(3) or (4) continue into proceeds?

for cases of "temporary perfection" covered in subsections (4) and (5), taking possession is the only available method; this provision follows the Uniform Trust Receipts Act. The rule is based on the thought that where the collateral consists of instruments, it is universal practice for the secured party to take possession of them in pledge; any surrender of possession to the debtor is for a short time; therefore it would be unwise to provide the alternative of perfection for a long period by filing which, since it in no way corresponds with commercial practice, would serve no useful purpose.

This Official Comment remains unchanged from the 1962 to the 1972 Texts.

160. Section 9-306(4) defines the extent of the secured party's interest in proceeds in the event of the debtor's bankruptcy, including allowance for limited tracing of cash proceeds into commingled bank accounts, while § 9-306(5) provides for reestablishment of the secured party's original security interest in the original collateral should it be returned to, or repossessed by, the debtor or his financier upon the cancellation of a sales transaction. Minor changes have been made in the 1972 Text of § 9-306(4) for purposes of clarification only; no changes are proposed in § 9-306(5).

The limits of the secured party's right to pursue cash proceeds into commingled accounts upon the debtor's bankruptcy are discussed in *In re Gibson Prods.*, 543 F.2d 652 (9th Cir. 1976). The secured party may assert a perfected interest only in those proceeds that he can actually trace into the commingled accounts. The *Gibson* case, although decided with reference to the Arizona U.C.C., applies equally to Washington law, and, as the court pointed out, the changes in the 1972 Text of § 9-306(4) would affect no change in the secured party's rights in commingled accounts against the bankruptcy trustee. *Id.* at 655. Nor will the adoption of the Bankruptcy Reform Act of 1978 affect the holding in *Gibson*. See 11 U.S.C.A. § 547 (West 1979).

Proper resolution of these two cases, particularly the former, has generated one of the greatest scholarly debates¹⁶¹ about the effects of the 1962 Text. Certainty of result is the essence of secured financing. The practical way to avoid the uncertainty of the first case is for the prospective financier to refuse a loan on inventory or accounts when an earlier interest in either is on file. The general absence of litigation on this first case, both in Washington and elsewhere, indicates that the financing community recognized early the uncertainty under the 1962 Text and acted accordingly.

To settle the first unresolved priority problem, the 1972 Text added subsection 9-312(6).¹⁶² Pursuant to this subsection, the general rule of subsection 9-312(5) is extended to proceeds. Thus, the first financier to file in either inventory or accounts will in fact prevail in the accounts. In particular, an accounts receivable financier need not worry under the 1972 Code that a subsequent inventory claimant could defeat his interest in accounts.¹⁶³

The second situation usually arises when a borrower exhausts the line of credit from its inventory or accounts financier and approaches a supplier to sell on credit against the retention of a purchase money security interest. Regardless of whether the credit purchase and grant of a purchase money interest is a breach of the agreement with the original financier,¹⁶⁴ the question remains whether the purchase money interest's super-priority in the original collateral conferred under subsection 9-312(3) or (4) should extend to proceeds as against the preexisting financier. By appropriate changes in the lan-

161. See, e.g., Henson, "Proceeds" Under the Uniform Commercial Code, 65 COLUM. L. REV. 232 (1965); Weiss, *Original Collateral and Proceeds: A Code Puzzle*, 42 N.Y.U.L. REV. 785 (1967). See also J. WHITE & R. SUMMERS, *supra* note 80, § 25-4, at 909.

Professor Henson, a member of the special Article 9 Review Committee created in 1966, argued that a proceeds interest under the 1962 Text should be considered as initially perfected automatically under § 9-306(3), rather than as a result of the filing of a financing statement with a claim to proceeds. As a result, he argues that U.C.C. § 9-312(5)(a) (1962 version) does not apply, and, therefore, that the inventory financier's interest, arising *earlier in the financing cycle*, should receive priority, even over the interest of a previously filed accounts financier, notwithstanding that perfection of both claimants would occur at the same instant, *i.e.*, the moment when the common debtor first received rights in the proceeds. Henson, *supra*.

162. Subsection 9-312(6) of the 1972 Text reads: "For purposes of subsection (5) a date of filing or perfection as to collateral is also a date of filing or perfection as to proceeds."

163. See Henson, *supra* note 161.

164. A well-drafted security agreement will contain a clause prohibiting the creation of any conflicting interest in any of the collateral claimed by the secured party; violation of this covenant will constitute default and will enable the secured party to seize the collateral or resort to other remedies, but will not invalidate the conflicting interest.

guage of subsection 9-312(3), the 1972 Text expressly limits the super-priority of the purchase money inventory financier in proceeds to *cash* proceeds, so that the financier will be subject to the general rule of subsection 9-312(5), as supplemented by subsection 9-312(6), for noncash proceeds, including accounts. Consequently, the inventory financier will not enjoy priority in the accounts generated by sale of the inventory he financed over either a preexisting, properly perfected financier, or preexisting, properly perfected accounts receivable financier.¹⁶⁵

G. *Perfection in Fixtures—Priority over Conflicting Real Estate Interests*

1. *The Problem*

Goods may become so attached to real estate that they are subject to liens and other interests arising under real property law. Sometimes, as with building materials, they become so integrated into a structure that they lose their identity as personal property. Frequently, as with heavy machinery or appliances, goods may be bolted down or otherwise firmly installed but still removable. Goods in such cases retain their identity as items of personal property while at the same time are subject to real property law. Goods which exhibit these dual characteristics are called "fixtures." Although Article 9 does not precisely define¹⁶⁶ when goods become fixtures (this is left to noncode state law),¹⁶⁷ it authorizes the creation, or continuation, of personal property security interests in goods that are, or will become, fixtures and establishes a set of rules regulating priority in fixtures between conflicting real property and Article 9 personal property interests.

Priority among real estate interests, generally speaking, is measured from the time of recording in an index maintained in each county under the respective laws of each state. To determine whether superior claims to the real estate exist, a prospec-

165. In contrast to its treatment of the purchase money inventory financier, the 1972 Text expressly extends the § 9-312(4) super-priority of purchase money financiers of all other types of collateral to proceeds of all sorts. In effect, however, § 9-312(4) protects very little other than purchase money security interests in equipment. An after-acquired property clause covering consumer goods is essentially prohibited by § 9-204(2), and farm products are normally produced and not purchased.

166. The 1972 Text defines fixtures as goods that have "become so related to particular real estate that an interest in them arises under real estate law." U.C.C. § 9-313(1)(a) (1972 version).

167. WASH. REV. CODE § 62A.9-313(1)(2d sent.) (1979).

tive buyer or mortgagee will consult this index, just as buyers or financiers of personal property will consult the U.C.C. filing indices. To perfect a personal property fixture interest against a claimant of a real estate interest, the Code prescribes a local filing in the office where a mortgage on the same real estate would be filed.¹⁶⁸ This procedure was designed to prevent unfair surprise to claimants of real estate interests. The financing statement for such a filing must include sufficient information concerning the real estate on which the fixtures are or will be located so that the financing statement can be indexed properly to accommodate a real property record search.¹⁶⁹

The priority rules for conflicts between real property and personal property interests in fixtures, as well as the effects of filing or failing to file as a fixture interest, are set forth in section 9-313. As between two personal property or U.C.C. security interests in goods which are fixtures, the rules set out in section 9-312 will continue to govern.

2. *The 1962 Text of Section 9-313*

Under the 1962 Text of section 9-313, any personal property security interest attaching to goods that are or subsequently become fixtures has priority in the goods over all conflicting real property interests in the real estate upon which the goods are or become fixtures, with two exceptions. The first exception, set out

168. *Id.* § 62A.9-401(1)(b). Under the 1972 Text a fixture filing is intended as a *supplemental* means of perfection to insure protection against real estate purchasers and mortgagees. A proper nonfixture filing is sufficient to perfect a U.C.C. interest in goods, whether fixtures or not, against other U.C.C. secured parties and all judicial lien creditors of the debtor. No distinction is made between creditors whose liens attach to the collateral as personal property and creditors whose liens attach to the real property on which the fixtures may be located. The intent of this rule is to prevent attack by the trustee of the debtor in a subsequent bankruptcy from defeating a U.C.C. fixture interest which has been perfected but not fixture filed. U.C.C. § 9-313, Official Comment 3 (1972 version).

Under the 1962 Text, in contrast, the failure to perfect as a fixture, if in fact the goods are fixtures, results in exposure of the secured party to loss of his collateral to the debtor's trustee in bankruptcy pursuant to the interaction of the language of § 9-313(4)(b) of the 1962 Text with § 70(c) of the Bankruptcy Act of 1898 and § 544(a)(1) of the Bankruptcy Reform Act of 1978. See text accompanying note 171 *infra*.

169. The precise information is set forth in § 9-402(5) of the 1972 Text. Although the clear intent of the 1962 Text is that a fixture filing should be indexed in the local jurisdiction, the statute does not expressly state this. Language has been added in the 1972 version of § 9-403(7) directing the local official to file a fixture financing statement (as well as financing statements for timber or mineral interests) as if it were a real estate conveyance; § 9-402(5) of the 1972 Text calls for information to be furnished on the financing statement to enable the local official to accomplish this.

in subsection 9-313(3), recognizes the priority of a competing real estate interest that attaches to the goods as fixtures before the personal property interest attaches, a simple "first in time is first in priority" rule.

The second and much more important exception, subsection 9-313(4), protects the integrity of the real estate recording system by granting priority to certain real estate claimants who obtain their interests after the personal property interest attaches, but before it has been perfected by a fixture filing. Pursuant to the 1962 Text, an attached but unperfected U.C.C. interest in fixtures is defeated by (1) a purchaser for value of an interest in the real estate, (2) a preexisting real estate mortgage to the extent he advances new value after the attachment and before the fixture filing of the personal property security interest, and (3) a creditor obtaining a judicial lien upon the real estate. As with the 1962 Text of subsection 9-301(1), priority in each case is also conditioned upon the real estate claimant having no actual knowledge of the off-record U.C.C. interest.¹⁷⁰

Inclusion of judicial lien creditors among the parties protected by subsection 9-313(4) of the 1962 Text against fixture interests not fixture filed was a serious drafting error. Judicial lien creditors place no reliance on the real estate records nor advance any new value to the debtor when obtaining their liens. Far more significantly, however, inclusion of judicial lien creditors within the protected group of subsection 9-313(4) affords the trustee of the debtor in a subsequent bankruptcy a basis to defeat a nonfixture filed fixture interest by virtue of his status as a judgment lien creditor,¹⁷¹ should it be determined that the goods are fixtures at bankruptcy.¹⁷² Such is the case even if the goods were originally not fixtures and the security interest was originally and properly perfected as a nonfixture interest, and even if the debtor affixed the goods to the real estate without the

170. Reference to actual knowledge is eliminated in the 1972 Text of § 9-313, rendering the statute a "pure race" rather than a "race-notice" statute, consistent with the changes in § 9-301. See text accompanying note 62 *supra*.

171. 11 U.S.C.A. § 544(a) (West 1979). Bankruptcy proceedings filed prior to October 1, 1979, would be subject to the 1898 Bankruptcy Act. Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, § 403, 92 Stat. 2683 (1978). Under the 1898 Act, however, the trustee would still be able to assert judgment lien creditor status. 11 U.S.C. § 110(c) (1976) (repealed 1978).

172. The reverse is also true: fixture filing of what is determined at bankruptcy to be a nonfixture interest renders the security interest subject to defeat. *In re Park Corrugated Box Corp.*, 249 F. Supp. 56 (D.N.J. 1966). This result will continue under the 1972 Text and the new Bankruptcy Reform Act of 1978.

knowledge or against the wishes of the secured party.¹⁷³ As a consequence, a well-advised financier of any collateral that conceivably could become fixtures will file twice under the 1962 Code, once as a nonfixture interest and again as a fixture interest, to insure complete protection in the collateral.¹⁷⁴

3. *The 1972 Text of Section 9-313*

To eliminate these and other difficulties, and to seek greater acceptance of section 9-313 among real estate financing groups,¹⁷⁵ fundamental changes to that section have been made in the 1972 Text. The most significant of these changes are: (1) restatement of the general priority rule of section 9-313 in terms of perfection, rather than attachment, of the personal property interest; (2) definition of the term "fixture filing,"¹⁷⁶ and clarification of its effects; (3) introduction of a degree of conscious parallelism between the priority rules of section 9-313 and those of subsections 9-312(4) and (5); and (4) recognition of a real property analogy to a purchase money security interest, the "construction mortgage,"¹⁷⁷ and guarantee of its priority over conflicting, subsequently recorded personal property purchase money security interests.

173. Although the risk of successful intervention of the bankruptcy trustee against a security interest perfected other than by fixture filing when the goods are later determined to be fixtures is of substantial practical importance, there is a paucity of case law on the subject. In one reported bankruptcy case, involving a U.C.C. fixture claimant who had perfected only by a nonfixture filing and who was seeking priority in the fixtures over a real estate mortgagee after the common debtor's bankruptcy, the U.C.C. claimant prevailed and the trustee did not even intervene, notwithstanding the U.C.C. financier's apparent exposure under § 9-313(4) of the 1962 Code. *In re Chase Laundry & Drycleaning Co.*, 2 Bankr. Ct. Dec. 975 (1976).

174. In a complex transaction some question may arise as to where the financing statement should be filed to perfect the secured party's interest. While there is only one proper location for any transaction (except in some situations in states selecting § 9-401(1), alternative three), multiple copies of the financing statement can routinely be filed to assure the proper location has been covered. There is no penalty for multiple filing, only multiple filing fees. But the penalty for failure to file may include loss of the secured party's collateral.

175. Although adopted in most states, § 9-313 of the 1962 Text was omitted or substantially modified in a significant minority of states, including California.

176. U.C.C. § 9-313(1)(b) (1972 version) states: "[A] 'fixture filing' is the filing in the office where a mortgage on the real estate would be filed or recorded of a financing statement covering goods which are or are to become fixtures and conforming to the requirements of subsection (5) of Section 9-402."

177. *Id.* § 9-313(1)(c) states: "[A] mortgage is a 'construction mortgage' to the extent that it secures an obligation incurred for the construction of an improvement on land including the acquisition cost of the land, if the recorded writing so indicates."

Under section 9-313 of the 1972 Text, the basic rule is that, subject only to two exceptions, an unperfected U.C.C. interest is subordinate to any conflicting real estate claimant (other than the debtor who created the U.C.C. interest).¹⁷⁸ The two exceptions, contained in subsections 9-313(5)(a) and (b), relate to (1) voluntary subordination or relinquishment of his claim to the fixture by the real estate claimant and (2) fixtures which are property of a lessee or other user of the real estate who is entitled by non-Code law to remove them from the real estate as against the real estate claimant. This change in the general rule of section 9-313 alters the entire structure of fixture priorities. The section is no longer biased in favor of the personal property security interest; rather, it now follows the pattern of subsection 9-312(5), that the first interest filed for record generally prevails. This is confirmed by new section 9-313(4)(b): having perfected by fixture filing, a U.C.C. financier has priority in the fixtures over any subsequently recorded real estate interest in the same property.

Section 9-313 also continues, subject to one very important exception, the policy of subsection 9-312(4), protecting a purchase money security interest from claims to the collateral by preexisting creditors of the debtor. Thus, under subsection 9-313(4)(a), a purchase money interest in goods which will become fixtures is protected against a preexisting real estate financier's fixture interest under an after-acquired fixture clause if a fixture filing is accomplished before the goods become fixtures. If the fixture filing also meets the criterion of subsection 9-312(4) that filing be accomplished before, or within ten days after, the debtor acquires possession of the goods, the single fixture filing also gives the purchase money fixture financier priority over preexisting U.C.C. personal property security interests in the same goods. The exception to subsection 9-313(4)(a), fixture purchase money priority, is in favor of a prior recorded construction mortgage under subsection 9-313(6). The purpose of this provision is to recognize that a construction mortgage is itself in the nature of a purchase money interest, and that advances made by the construction mortgagee may be intended to fund the purchase of the same items being sought on credit from the prospective U.C.C. purchase money financier. The practical effect of the construction mortgage priority is, of course, to force the prospective U.C.C.

178. *Id.* § 9-313(7).

purchase money fixture financier to contact construction mortgagees of record and to obtain either a subordination agreement covering the fixtures he plans to finance or a direct commitment from the mortgagee to pay for the fixture prior to installation.

Section 9-313 of the 1972 Text also contains provisions to protect a U.C.C. fixture interest against competing real estate claims in two instances in which perfection has been achieved other than by fixture filing.¹⁷⁹ Both instances recognize the imprecise nature of the legal rules determining what sort of attachment to real property renders personal property a fixture, as well as the lack of control which a financier has over such attachment. The first instance is provided in subsection 9-313(4)(c), governing readily removable office or factory machines and replacement¹⁸⁰ home appliances that are consumer goods. If the security interest has been perfected under the Code prior to the goods becoming fixtures, priority of the U.C.C. interest is guaranteed. The practical problem, of course, is what the words "readily removable" mean. Clearly, a cautious U.C.C. equipment or consumer goods financier may still decide to file his interest twice to avoid controversy under the 1972 Text about the meaning of "readily removable." By doing so, he is fully protected, whether his collateral becomes fixtures or not.

The second instance deals with the problem of creditors with conflicting judicial liens on the real property to which a fixture is attached. Reversing the rule of subsection 9-313(4) of the 1962 Text, new subsection 9-313(4)(d) states that a personal property security interest in fixtures perfected by any method proper under Article 9 will prevail over a subsequently obtained judicial lien on the real estate. The purpose is, of course, to protect the security interest which has been perfected by a proper nonfixture filing, but not by a fixture filing, from being defeated by the debtor's trustee in bankruptcy, if the debtor should affix the goods to his land. Subsection 9-313(4) of the 1972 Text effectively forecloses the trustee's power under the Bankruptcy Act of 1898 to defeat a U.C.C. fixture interest that has been perfected

179. In practice, perfection will usually have been accomplished by a central or local filing as equipment or consumer goods or automatically in the case of a purchase money interest in consumer goods.

180. Replacement home appliances are specified because originally installed consumer appliances frequently will be covered under a construction mortgage.

either by a fixture filing or by a proper nonfixture filing.¹⁸¹

Unfortunately, the enactment of the Bankruptcy Reform Act of 1978 may reopen the way for the trustee to defeat a U.C.C. fixture interest which has not been fixture filed prior to the debtor's bankruptcy. Under subsection 544(a)(3) of the Bankruptcy Reform Act, the trustee is granted for the first time a power to avoid any transaction that may be defeated by a bona fide purchaser of the debtor's real estate at the moment of bankruptcy. Probably intended to supplement the trustee's powers to cut off unrecorded deeds, mortgages, and other equitable interests in states where the real estate recording act does not benefit a judicial lien creditor,¹⁸² the new provision clearly applies under

181. Under the Bankruptcy Act of 1898, there also exists the possibility of a trustee's challenge, even under the provisions of the 1972 Text, to a perfected but nonfixture-filed fixture interest as a voidable preference under § 60(a) and (b). 11 U.S.C. § 96(a), (b) (1976). Because no reported cases under § 9-313 have advanced such an argument, it is uncertain whether this attack might have been successful. Under § 60(a)(2), an interest in real property may be defeated by the trustee if it may be defeated by a bona fide purchaser, and a fixture interest not filed as a fixture filing is vulnerable to a purchaser under § 9-313(7). Of course, the trustee would also have the burden of proof that the secured party had reasonable cause to believe the debtor was insolvent. *Id.*

The avenue of attack against the perfected but nonfixture-filed interest as a preferential transfer has been specifically cut off by § 547(e)(1)(A) and (B) of the Bankruptcy Reform Act of 1978, which provides that an interest in fixtures cannot be defeated by the trustee once it has been perfected against a lien creditor. 11 U.S.C.A. § 547(e)(1)(A), (B) (West 1979). The rule of § 9-313(4)(d), therefore, would suffice to protect the perfected but nonfixture-filed fixture interest against the claim that it is a preference under the new act.

182. The general common law rule is that a judicial lien creditor, unlike bona fide purchasers or mortgagees, is not protected by state real property recording acts against latent defects affecting his debtor's title to land, unless the legislature has extended the recording statute to cover judicial lien creditors. Therefore, absent such protection, the judicial lien creditor is subject to all unrecorded instruments and off-record equities that would be superior to the debtor's own interest in the land. Likewise the bankruptcy trustee, using his power as a judicial lienor under § 70(c) of the Bankruptcy Act of 1898, cannot defeat these interests in bankruptcy proceedings applying the law of states, such as Washington, which do not include judicial lien creditors among the parties protected by the recording act. *See* WASH. REV. CODE § 65.08.070 (1979); *Fales Co. v. Seiple Co.*, 171 Wash. 630, 19 P.2d 118 (1933) (receiver in bankruptcy, as neither a bona fide purchaser nor a mortgagee, cannot defeat unrecorded deed). The trustee's only attack on an unrecorded instrument under the Bankruptcy Act of 1898 would be as a preference under § 60, which requires proof of the knowledge of the debtor's insolvency on the part of the owner of the off-record interest. 11 U.S.C. § 96(b) (1976) (repealed 1978). The language of § 544(a)(3) of the new act can thus be explained as merely an extension of the trustee's powers previously available under § 70(c) to permit the trustee to avoid off-record interests in states such as Washington. It has the unfortunate effect, however, of voiding properly perfected, but nonfixture-filed, U.C.C. fixture interests as well, as as pointed out in the text of this article. A change in § 544(a)(3) to conform with § 547(a)(1)(A) and (B) can be expected as one of the initial technical amendments to the Bankruptcy Reform Act of 1978.

the rule of subsection 9-313(7) to perfected but nonfixture-filed U.C.C. fixture interests as well. The inclusion of such a power without an exception for U.C.C. fixture interests, in the face of other newly enacted language in subsection 547(e)(1)(A) and (B) of the Bankruptcy Reform Act specifically protecting a properly perfected but nonfixture-filed fixture interest from attack as a preferential transfer, seems strange indeed and well may be a legislative error. But until such time as subsection 544(a)(3) is amended, a secured party can obtain complete protection for an interest in goods that may become fixtures only by a dual filing.

VII. MULTISTATE PROBLEMS

A. *Choice of Law in General*

The preceding discussion presumes that each transaction has occurred entirely within a single jurisdiction. The U.C.C., however, is state law, and, by the very fact that its subject matter is more or less moveable, many transactions relate to more than one state. Rather than leave resolution of the applicable law in situations involving contact with more than one jurisdiction to the common law of conflicts, the Code contains a general choice of law provision,¹⁸³ and special provisions in Article 9 relating to security interests in multistate situations. These latter provisions are contained in section 9-103 of the 1972 Text, and in section 9-103, in conjunction with section 9-102, in the 1962 Text.

Although there are substantial differences between the Article 9 choice of law provisions adopted in Washington and those present in the 1972 Text, the core common to both relates to two essential matters: (1) determining the jurisdiction according to the laws of which the initial perfection or nonperfection of a security interest will be measured, and (2) determining the effect on perfection should the location of the collateral that determined initial perfection shift into a new jurisdiction. Because perfection or nonperfection bears upon the rights of third parties, these two questions require answers that can be obtained with certainty by persons who are not parties to the security agreement. Fixed rules are required to lend predictability; they tell the parties where to file and others where to look.

The principal differences between the 1962 and 1972 Texts

183. WASH. REV. CODE § 62A.1-105 (1979).

in the multistate transaction, or choice of law, rules relate to the scope of the special Article 9 choice of law rules in relation to the applicability of the general rule of section 1-105. The 1972 Article 9 choice of law rules are restricted solely to the previously mentioned questions of perfection, matters relating to protection of third-party interests. All other choice of law questions (*i.e.*, questions arising out of the agreement) are subsumed under the general rule of section 1-105, which allows the parties to choose the applicable law, and in the absence of choice, directs the court to apply a modified "significant contacts" analysis to determine the appropriate law.¹⁸⁴

The 1962 provisions, by contrast, significantly curtail the applicability of the general choice of law rule of section 1-105. Subsection 9-102(1) of the 1962 Text contains the statement, deleted in the 1972 Text, that "this Article applies so far as concerns any personal property and fixtures within the jurisdiction of this state. . . ." Although uncertainty surrounds the meaning of this provision,¹⁸⁵ it is generally accepted as a mandatory choice of law rule requiring application of forum law when that is the location of the collateral.¹⁸⁶ In addition, the multistate rules in the 1962 Text of section 9-103 apply to questions of validity, as well as of perfection, of the security interest.¹⁸⁷ Under the U.C.C., validity is an undefined concept the scope of which is open to question. The word can be interpreted narrowly to mean only formal requisites or broadly to include non-Code substantive law. Regardless of the term's interpretation, it deals with

184. Subsection (1) of § 1-105 reads:

Except as provided hereafter in this section, when a transaction bears a reasonable relation to this state and also to another state or nation the parties may agree that the law either of this state or of such other state or nation shall govern their rights and duties. Failing such agreement this Title applies to transactions bearing an appropriate relation to this state.

Id. § 62A.1-105(1). Subsection (2) provides for the applicability of special conflicts rules, such as §§ 9-102 and 9-103 of the 1962 Text, and § 9-103 of the 1972 Text, to supersede the general rule of § 1-105(1).

185. For a recent overview of the difficulties in interpreting the choice of law rules of §§ 9-102 and 9-103 of the 1962 Text, see Juenger, *Nonpossessory Security Interests in American Conflicts Law*, 26 AM. J. COMP. L. (SUPP.) 145, 156-61 (1978).

186. Official Comment 3 to the 1962 Text of § 9-102 provides in part:

In general this Article adopts the position, implicit in prior law, that the law of the state where the collateral is located should be the governing law, without regard to possible contacts in other jurisdictions. . . . This "narrow" approach, appropriate in the field of security transactions, should be contrasted with the broad approach stated in Section 1-105 with reference to the applicability of the Act as a whole.

187. WASH. REV. CODE § 62A.9-103(2) (1979).

matters between the parties, and its inclusion within section 9-103 impinges on the parties' freedom to contract on choice of law where no substantial countervailing third-party interest is served.

B. Perfection in Multistate Transactions

Section 9-103 prescribes, in effect, that the law of the jurisdiction where the collateral is located at the moment when perfection is claimed to have occurred will govern whether the interest is or is not perfected. The drafters of Article 9 realized, however, that no single rule is able adequately to fix the location of all kinds of collateral. Accordingly, section 9-103 of the 1972 Text divides collateral into five mutually exclusive categories for the purpose of determining applicable law in multijurisdictional transactions. Of these, two do not warrant separate treatment in an introductory survey;¹⁸⁸ the other three categories, (1) documents, instruments, and "ordinary goods,"¹⁸⁹ (2) goods covered by a certificate of title on which liens must be recorded,¹⁹⁰ and (3) accounts, general intangibles, and "mobile goods,"¹⁹¹ require elaboration. For purposes of determining the place for perfection, the location of collateral in each of these three classes can be generalized as (1) the situs of the collateral, (2) the place of issue of the certificate of title, and (3) the domicile of the debtor, respectively.

The categories of section 9-103 of the 1972 Text represent only one major modification from those in the 1962 Text. The 1972 Text prescribes only one location rule for all intangible collateral;¹⁹² in contrast, accounts, together with contract rights, form a category separate from general intangibles and mobile goods under the 1962 Text. The location of accounts and contract rights under the earlier text is defined as the jurisdiction

188. These categories are (1) chattel paper under § 9-103(4); and (2) minerals and related accounts under § 9-103(5). The multistate perfection rules for documents, instruments, and ordinary goods apply to possessory interests in chattel paper while the rules for accounts apply to nonpossessory interests in chattel paper. Minerals are not goods until removed from the earth. Security interests attaching at the mine mouth can be perfected only in the jurisdiction where the mine mouth is located. Neither chattel paper nor minerals are separately treated in the 1962 Code; therefore, they fall into the residual category of § 9-103(3) in the 1962 Text.

189. U.C.C. § 9-103(1) (1972 version).

190. *Id.* § 9-103(2).

191. *Id.* § 9-103(3).

192. *Id.*

where the office containing the debtor's books is located. Because under the 1962 Text a contract right may mature into a general intangible, by prescribing different rules for determining the location of, and hence the place to perfect interests in, contract rights and general intangibles, the authors of the 1962 Code committed a drafting blunder¹⁹³ that the 1972 Text remedies.

Except for the deletion of references to validity and the consolidation of all intangible property into one class, the changes in section 9-103 represent primarily an effort to present a more complete and more intelligible statement of rules already contained in, or derived by the courts from, the 1962 Text.¹⁹⁴ The most conspicuous 1972 Text additions are explicit language in subsections 9-103(2) and (3) establishing rules for continuing perfection of existing interests when the location of intangible collateral or collateral subject to a title certificate is moved from jurisdiction to jurisdiction. Also, subsection 9-103(3) of the 1962 Text relating to ordinary goods, documents, and instruments has been rewritten to clarify the rules for initial perfection and for continuing perfection of existing interests when the collateral changes location.

With but one exception, perfection of a security interest in ordinary goods,¹⁹⁵ documents, and instruments¹⁹⁶ is governed by the law of the jurisdiction that is the situs of the collateral at the moment "the last event occurs on which is based the assertion that the security interest is perfected or unperfected."¹⁹⁷ The law

193. A perfected interest in contract rights may be converted into an unperfected security interest in general intangibles if the debtor's chief place of business is located in a state other than that in which his records concerning the contract rights are kept, unless the secured party also files a financing statement in general intangibles in the state of the debtor's chief place of business before the debtor completes performance on the contract from which the rights arise. See text accompanying note 31 *supra*.

194. See, e.g., *Associates Realty Credit Ltd. v. Brune*, 89 Wash. 2d 6, 568 P.2d 787 (1977) (interpreting WASH. REV. CODE § 62A.9-103(3) (1979)); *Morris v. Seattle-First Nat'l Bank*, 10 Wash. App. 129, 516 P.2d 1055 (1973) (interpreting WASH. REV. CODE § 62A.9-103(3), (4) (1979)).

195. Ordinary goods are defined by exclusion as the residuum of goods which are neither mobile nor covered by a certificate of title. U.C.C. § 9-103(1)(a) (1972 version).

196. The same rule also applies to a possessory security interest in chattel paper. *Id.* § 9-103(4) (1972 version); see note 188 *supra*.

197. U.C.C. § 9-103(1)(b) (1972 version). Perfection requires that all steps for attachment, *id.* § 9-203(1), have occurred and that filing or taking possession, if required, has been accomplished. *Id.* § 9-303. Should a secured party prefile in the debtor's goods in state A while they are located in that state, but the goods are removed to state B before the creditor makes his initial advance of value, then the last event determining perfection would occur while the goods are in state B. In such a case the filing in state A would not perfect an interest in the collateral.

of this jurisdiction continues to govern perfection until the collateral is removed from the jurisdiction. If collateral subject to a perfected security interest is moved into another U.C.C. jurisdiction, the second jurisdiction will accord the security interest automatic perfection in the collateral for four months or such shorter period as perfection continues in the first jurisdiction while the collateral remains in the second jurisdiction.¹⁹⁸ Perfection in the second jurisdiction will lapse at the end of this period of initial automatic perfection unless the secured party perfects his interest in the second jurisdiction according to its laws.¹⁹⁹ If he does so, perfection in the second jurisdiction continues thereafter without interruption.²⁰⁰ In the case of a nonpossessory security interest, this means, of course, filing a proper financing statement in the second jurisdiction or repossessing the collateral, unless the security interest is a purchase money interest in consumer goods perfected without filing. In this last case, perfection continues beyond the initial four-month period without further creditor action.²⁰¹

The exception to the rule of subsection 9-103(1)(b) is the case of an interstate credit sale, in which a purchase money financier understands at the time of sale that the goods immediately will be moved to another jurisdiction. In this case, perfection and priority of the security interest will be measured by the law of the jurisdiction of intended destination for the first thirty days after the security interest attaches and thereafter, if the goods arrive in that jurisdiction within the thirty days.²⁰² The

198. *Id.* § 9-103(1)(d). Perfection in the first jurisdiction might expire before the goods have been present four months in the second. For example, filing remains valid for only five years unless a continuation statement is filed. *Id.* § 9-403(2).

199. *Id.* § 9-103(1)(d)(i).

200. *Id.* § 9-103(1)(d)(ii).

201. Of course, unless perfected by filing in the second jurisdiction, a purchase money security interest in consumer goods is defeated by a consumer buying without actual knowledge of the interest. *Id.* § 9-307(2). A previous filing in the first jurisdiction will protect against a consumer buyer in the second jurisdiction for only four months. *Id.* § 9-103(1)(d)(iii).

202. While 30 days may be a reasonable period for the normal transit of goods nationwide, the rule of § 9-103(1)(c) (and the corresponding rule of § 9-103(3) of the 1962 Text) speaks of 30 days from the date of attachment of the interest, not from the date of seller's shipment.

A purchase money interest will attach as soon as the conditions of § 9-203(1) are met; thus a purchase money interest may attach before the goods are shipped, particularly if the purchase money financier is a third party. *See id.* § 9-107. The contract among the parties may call for the advance of the purchase price directly to the seller prior to shipment, and the buyer-debtor will acquire property rights in the goods sufficient for the fulfillment of § 9-203(1)(c) as soon as the goods are identified to the sales

effect of this provision is that a purchase money financier will be accorded the super-priorities of subsections 9-312(3) or (4) and 9-313(4)(a), as applicable, at the place of destination (assuming it is a U.C.C. jurisdiction) if he follows the requisites of those sections, including timely filing at the destination.²⁰³ Filing elsewhere will not perfect the security interest if, in fact, the goods arrive within the thirty-day span after the attachment of the purchase money interest.

Accounts, general intangibles, and mobile goods²⁰⁴ under the 1972 Text are deemed located in the jurisdiction where the debtor has his place of business,²⁰⁵ if he has one, or his residence, if he does not,²⁰⁶ and it is this law which governs perfection.²⁰⁷ In the event of a change in the debtor's location to another U.C.C. jurisdiction, perfection in the new jurisdiction will continue automatically for four months on the basis of the earlier perfection in the first jurisdiction. But this perfection, under subsection 9-103(3)(e), will lapse if filing has not occurred in the second jurisdiction prior to the expiration of the four months.²⁰⁸

contract. *Id.* § 2-501(1). Thus, delays in transit or the attachment of the interest before shipment may cause the 30-day period to be exceeded. If such is the case, § 9-103(1)(c) no longer applies, and perfection will be measured by the general rule of § 9-103(1)(b), the location of the goods when the last act in the attempted perfection occurs—most likely the jurisdiction in which the seller is located. Therefore, if there is doubt as to whether the goods will arrive at the destination within the allowed time of § 9-103(c), the financier should file in the seller's jurisdiction, as well as in the buyer's jurisdiction, to perfect under § 9-103(b).

203. Perfection at the destination, if § 9-103(1)(c) applies, will presumably also grant automatic perfection similar to that under § 9-103(1)(d) in each of the U.C.C. jurisdictions through which the goods pass during the 30 days on their way to the destination, although the statute is silent on this point.

204. Mobile goods are defined as goods that are not subject to certificate of title laws of a type normally used in more than one jurisdiction. A nonexhaustive list of examples given by the statute itself in § 9-103(3)(a) includes vehicles, construction and farm machinery, and shipping containers, if the goods are used as equipment, *see* U.C.C. § 9-109 (1972 version), or as inventory for lease, *see id.* § 9-103(3)(a). In contrast, an inventory of such items held for *sale* will be ordinary goods, perfected where they are located under § 9-103(1). Clearly, borderline cases exist as to whether goods are mobile or ordinary and may call for perfection by filing in more than one jurisdiction to prevent loss of the security interest.

205. If the debtor has more than one place of business, § 9-103(3)(d) deems his chief executive office as the place of business. Under the 1962 Text the location of intangibles is referred to as "the chief place of business." WASH. REV. CODE § 62A.9-103(2) (1979). Collectively, all of these locations relate to a domicile rule as the location for intangibles. Section 9-103(3)(c) contains rules, as does § 9-103(2) and (5) of the 1962 Text, for perfecting a security interest in intangibles if the debtor is a foreign domiciliary.

206. U.C.C. § 9-103(3)(d) (1972 version).

207. *Id.* § 9-103(3)(b).

208. *Id.* § 9-103(3)(e). This provision remedies the omission of rules for change of the

Mention has already been made of perfection of liens in goods (primarily automobiles, other highway vehicles, mobile homes, and boats) subject to certificate of title laws.²⁰⁹ Subsections 9-302(3) and (4) of the 1972 Text recognize that perfection by entry of the lien on the certificate of title in accordance with the applicable title statute is both necessary and sufficient for perfection of the lien under the Code, unless the collateral is in a dealer's inventory for sale.²¹⁰

Subsection 9-103(2) governs the interstate movement of goods subject to certificate of title statutes. The basic rules incorporated into the 1972 Text are simple. When goods subject to an outstanding certificate of title are moved into a U.C.C. jurisdiction, a lien entered on the certificate of title from the first jurisdiction remains perfected at least until a new certificate of title is issued in the second jurisdiction. If the lien is entered on the second jurisdiction's certificate of title, perfection of the security interest continues without interruption in the second state. If, on the other hand, the debtor procures (whether by fraud or by accident) a "clean" certificate of title not showing the lien, perfection of the security interest from the first jurisdiction nonetheless continues in the second jurisdiction until four months have elapsed after the goods entered the second jurisdiction.²¹¹

If goods subject to a properly perfected security interest in a jurisdiction in which no certificate of title is outstanding (as would be the case for automobiles registered before a certificate of title statute was enacted and in which a lien would be perfected by filing under the Code)²¹² are moved by the debtor into a second jurisdiction where a certificate of title not showing the lien is procured, perfection continues in the second jurisdiction for four months.²¹³

debtor's location in the case of intangible collateral and mobile goods in § 9-103(1) and (2) of the 1962 Text and clarifies that a grace period of automatic perfection will be accorded in the new jurisdiction. As in the case of goods subject to a title certificate, it is possible to infer from the language of § 9-103 of the 1962 Text that no grace period is permitted, with the consequence that a change in location without an immediate filing in the new jurisdiction will result in lapse of perfection.

209. See text accompanying notes 98-100 *supra*.

210. U.C.C. § 9-302(3)(b) (1972 version).

211. *Id.* § 9-103(2)(b). If the new certificate is procured more than four months after the goods entered the second jurisdiction, the perfection of the security interest from the first jurisdiction obviously lapses immediately on the issuance of the clean certificate.

212. *Id.* § 9-302(1)(d).

213. *Id.* § 9-103(2)(c).

Simple as they may seem, these two rules resolve issues repeatedly litigated under the 1962 Text of subsections 9-103(3) and (4). In two Washington cases the courts have adopted the majority position, which also corresponds with the resolution in the 1972 Text. In the first case, *Morris v. Seattle-First National Bank*,²¹⁴ decided by the court of appeals without reference to the 1972 Text, a certificate of title procured in Washington after the automobile involved had left Texas failed to show a lien that was entered on the face of the Texas title certificate. Upon repossession by an agent of the Texas secured party within four months after the car left Texas, a professional auto buyer, GM Auto Sales, was held to be subject to the lien of the Texas financier pursuant to subsection 9-103(3) of the 1962 Text.

In the later case, *Associates Realty Credit Ltd. v. Brune*,²¹⁵ a mobile home not subject to title certificate laws in British Columbia was subject to a properly perfected security interest. The mobile home was moved to Washington where a title certificate not showing the British Columbia lien was procured. The clean certificate was used by the owners to obtain a secured loan from a professional lender, which had its lien properly entered on the certificate. Within four months of the mobile home's arrival in Washington, the Canadian creditor located the mobile home and sued to foreclose its mortgage, claiming priority over the Washington lender. In holding for the Canadian secured party, the supreme court interpreted subsection 9-103(4) of the 1962 Text, governing perfection of liens on title certificate property, as subject to the provisions of subsection 9-103(3) of the 1962 Text, which grants a four-month automatic perfection in Washington for liens perfected elsewhere. Significantly, the Washington court referred to the provisions of subsection 9-103(2) of the 1972 Text as a basis for its interpretation.²¹⁶

The rules of subsection 9-103(2) of the 1972 Text, codifying *Morris* and *Brune*, are only two of a number of instances in

214. 10 Wash. App. 129, 516 P.2d 1055 (1973). The court explained how the debtor was able to launder title through the medium of a New York title certificate issued under a law not requiring liens to be recorded on the face of the certificate. As previously mentioned, by 1978 every state had enacted laws requiring entry of liens on the face of any newly issued title on an automobile. See note 98 *supra*.

215. 89 Wash. 2d 6, 568 P.2d 787 (1977).

216. *Id.* at 13 n.3, 568 P.2d at 791 n.3. The Washington Supreme Court has taken judicial notice of 1972 Text clarifications of imperfections in the 1962 Text on one other occasion. See *General Elec. Credit Corp. v. Isaacs*, 90 Wash. 2d 234, 243 n.5, 581 P.2d 1032, 1037 n.5 (1978). See also U.C.C. § 11-108 (1972 version).

which parties dealing with the debtor are required under the 1962 and 1972 Texts to bear the risk²¹⁷ of perfected, but not readily discoverable,²¹⁸ liens on the collateral. Financiers and dealers should understand the rules governing possible existence of such liens on the property in which they trade and either investigate or assume the risk in the transactions they undertake. The drafters of the 1972 amendments, however, did not believe that non-professional buyers of used cars and trucks can fairly be held to anticipate interests not on the face of the certificate, much the same as consumer buyers are not expected to investigate for unfiled interests in goods they purchase. Thus, the provisions of subsection 9-103(2) of the 1972 Text are subject to an exception in favor of a "non-professional buyer"²¹⁹ who pays value in reliance on a clean certificate issued notwithstanding the existence of a perfected lien from another jurisdiction. Pursuant to subsection 9-103(2)(d), purchase by such a buyer terminates the unlisted lien, notwithstanding that its four-month period of automatic perfection has not ended.²²⁰

VIII. DEFAULT AND ENFORCEMENT

A. *Defining Default*

Because Article 9 does not define default, the secured party's attorney must carefully set forth in the security agree-

217. Other examples, already provided for in the 1962 Text and carried forward, include the temporary automatic perfection granted on change of the collateral's location under other provisions of § 9-103; the automatic temporary perfection in instruments and negotiable documents under § 9-304(4) and (5); and the automatic perfection of purchase money security interests in consumer goods under § 9-302(1)(d). Additionally, § 9-402(7) of the 1972 Text provides for temporary automatic perfection after a debtor's name change and continuing perfection upon transfer of collateral by a debtor to a third party, and § 10-102(2) provides for post-U.C.C. perfection of perfected pre-Code interests. See note 148 *supra*.

218. "Not readily discoverable" means undiscoverable by a record search under the current name of the person known to be the owner of the property in question in the jurisdiction where either the debtor or the goods are located.

219. The term "non-professional buyer" is broader than the term "consumer," and the provision of § 9-103(2)(d) is broader than a consumer protection statute. Nevertheless, it is analogous to § 9-307(2), which grants priority to a consumer buyer over an unfiled purchase money consumer goods interest, presumably because of the average consumer's unfamiliarity with the expectations of the business community.

220. Decisions under § 9-103(3) and (4) of the 1962 Text, relating to continuing automatic perfection of a lien not shown on the face of a new title certificate, have both upheld and rejected continued perfection. See *Associates Realty Credit Ltd. v. Brune*, 98 Wash. 2d 6, 568 P.2d 757 (1977); *Norris v. Seattle-First Nat'l Bank*, 10 Wash. App. 129, 516 P.2d 1055 (1973).

ment the debtor's obligations.²²¹ Resort to "boilerplate" clauses is unwise; the attorney must prepare a definition of default for inclusion in the agreement which is appropriate to the particular transaction. Section 1-208 of the Code expressly permits the use of an "acceleration clause" empowering the secured party to demand immediate repayment of his advance if he "in good faith believes that the prospect of payment or performance is impaired." Language to this effect should always be included.²²² If the advance is not repaid at once, acceleration will place the debtor in default and allow the secured party to collect the whole balance, not just the unpaid installment.

B. 1972 Amendments to Part Five

Part 5 of Article 9²²³ governs both the secured party's rights after default in collecting the balance and the debtor's rights, both before and after default, against overreaching.²²⁴ Changes in

221. Prompt payment is not the only important consideration; other obligations creditors routinely require are that the collateral be kept clear of conflicting liens, that the collateral and records concerning it be kept available for inspection, and that the collateral be insured and maintained in good repair. Breach of any of these obligations would constitute default.

222. Because of variation in the Washington Text of § 1-208 from the Official Text, acceleration clauses should only be used cautiously. Pre-Code Washington law recognized the validity of such acceleration clauses; the Washington rule was that the creditor must have "reasonable cause to deem [himself] insecure," before exercising his rights. *Jacobson v. McClanahan*, 43 Wash. 2d 751, 754, 264 P.2d 253, 255 (1953). The Washington Text omits the second sentence of the Official Text of § 1-208, which places on the debtor the burden of proving the secured party is not acting in good faith. Consequently, the burden of proving a good faith belief in diminished prospects of repayment rests on the accelerating creditor. See *Article One—General Provisions*, in *COLLECTED ESSAYS ON THE UNIFORM COMMERCIAL CODE IN WASHINGTON* 20 (1967).

223. WASH. REV. CODE §§ 62A.9-501 to .9-507 (1979).

224. Washington has enacted a second paragraph to § 9-501(1). *Id.* § 62A.9-501(1); see text accompanying notes 226-38 *infra*. This paragraph prohibits a deficiency judgment after repossession of the collateral in cases of purchase money security interests in consumer goods. Also, § 9-501(3) prohibits waiver of specific debtor's rights granted by Part 5, including the right to any surplus on collection of intangible collateral under § 9-502 or disposition of tangible collateral under § 9-504, and the right to damages for creditor misconduct under § 9-507(1). In addition, § 9-501(3), in conjunction with §§ 9-504, 9-505, and 9-506, forbids the waiver prior to default of the debtor's right to notice of sale or other disposition under § 9-504(3), the creditor's intention to retain the collateral under § 9-505(2), the right to require disposition of the collateral if he believes sale will produce a surplus under § 9-505, and the right to redeem under § 9-506.

Sections 9-504(3) and 9-505(2) are amended by the 1972 Text expressly to authorize the debtor's post-default waiver of the right to notice of sale and to notice of strict foreclosure. Validity of post-default waiver under the 1962 Text is denied by court decision in some states. See, e.g., *Hall v. Owen County State Bank*, — Ind. App. —, 370 N.E.2d 918 (1977).

Part 5 from the present Washington Text to the 1972 Official Text are minimal. Other than technical amendments to section 9-502, subsections 9-501(3), and 9-504(1) and (2), only subsections 9-504(3) and 9-505(2) would be affected. Under the 1962 Text a creditor in possession of the collateral after default must send notification to the debtor of sale under subsection 9-504(3) or of his intention to retain the collateral under subsection 9-505(2). Also, except in the case of consumer goods, such notice must be sent 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 interest in the collateral."²²⁵ Compliance with this provision requires a U.C.C. record search. To eliminate this expense, as well as to foreclose the possibility that an off-record interest might exist of which the secured party allegedly had knowledge, the 1972 Text requires that notice be sent only to such other secured creditors as have given the secured party timely notice of their interests in the collateral. The basis for the changes is that junior secured creditors will only be interested in the fate of the collateral if they anticipate that a surplus over the senior secured party's claim would be realized on sale. In practice, this does not often happen, but if it appears that it may, junior parties are assumed to be aware of the possibility. The new provision merely requires their affirmative action to safeguard their interests. Both subsections 9-504(3) and 9-505(2) have also been modified explicitly to provide that the debtor may waive *after default* his rights to notice of sale and to object to the secured party's retention of the collateral.

C. *Cumulation of and Limitations on Remedies*

The interests of debtor and creditor collide most sharply in Part 5 of Article 9. It is hardly surprising, therefore, that nearly half of all reported Washington Article 9 cases during the first twelve years of the Code dealt with allegations of creditor violation of the provisions of Part 5. A review of the provisions of Part 5 in light of cases interpreting the Washington Code is appropriate because of the significance of the provisions to a creditor faced with enforcing his interest after default.

The only nonuniform language in Part 5 of the Washington Text is the second paragraph of subsection 9-501(1), reading as

225. WASH. REV. CODE § 62A.9-504(3) (1979).

follows:

Notwithstanding any other provision of this Code, in the case of a purchase money security interest in consumer goods taken or retained by the seller of such collateral to secure all or part of its price, the debtor shall not be liable for any deficiency after the secured party has disposed of such collateral under RCW 62A.9-504 or has retained such collateral in satisfaction of the debt under subsection (2) of RCW 62A.9-505.²²⁶

Two technical problems in the drafting are immediately obvious: (1) the statute does not indicate at what point in time the goods must be consumer goods for the rule to apply, and (2) the statute refers only to a purchase money interest "taken or retained by the seller," despite section 9-107's extension of the concept of purchase money financing to include a person "who by making advances or incurring an obligation gives value to enable the debtor to acquire rights in or the use of collateral" The first problem was resolved by the Washington Supreme Court in *Commercial Credit Equipment Corp. v. Carter*,²²⁷ in which the court held that the initial use, or intended use as communicated to the seller, controls the classifications of the goods for purposes of subsection 9-501(1), notwithstanding a subsequent change in use.²²⁸

The second problem has not been litigated; in both cases in which interpretation of the second paragraph of subsection 9-501(1) has been required, the security interest appears to have been retained by the seller and thereafter assigned to a professional financier.²²⁹ Under pre-Code law a conditional sale could only be created by agreement between the vendor and vendee;²³⁰ a third-party financier advancing the purchase price would have received a chattel mortgage. Presumably, the drafters did not intentionally create a dichotomy of treatment between the two

226. *Id.* § 62A.9-501(1).

227. 83 Wash. 2d 136, 516 P.2d 767 (1973).

228. *Id.* at 139, 516 P.2d at 769. The buyer acquired a \$24,000 airplane for his private use, and when he was unable to make the payments, he began, with the approval of the secured party, to rent the plane in an effort to make sufficient money to meet his obligation. By the time it was repossessed, the number of hours the plane had been flown in a rental capacity exceeded those flown in a private, or personal use, capacity. The court also rejected the proposition, advanced by the trial court, that consumer goods should be restricted to nonluxury items.

229. In *Carter*, this fact is stated explicitly; in *Lew v. Goodfellow Chrysler-Plymouth, Inc.*, 6 Wash. App. 266, 492 P.2d 258 (1971), it is implied in the court's description of the financing arrangements.

230. Ch. 106, 1893 Wash. Laws 253 (repealed 1965).

types of purchase money interests provided for in the Code, and it would appear that the provision should be amended by deleting the language "taken or retained by the seller of such collateral to secure all or part of its price" at the time the 1972 amendments are considered, so that the provision would read:

Notwithstanding any other provision of this Code, in the case of a purchase money security interest in consumer goods, the debtor shall not be liable for any deficiency after the secured party has disposed of such collateral under RCW 62A.9-504 or has retained such collateral in satisfaction of the debt under subsection (2) of RCW 62A.9-505.

A third and more significant question of the second paragraph of subsection 9-501(1) is whether the legislature intended the provision to prohibit recovery from a consumer debtor of any amount in excess of the value of the collateral or merely to deny a deficiency judgment only in those cases in which the creditor undertakes to repossess first. The Washington Court of Appeals addressed this question in *Lew v. Goodfellow Chrysler-Plymouth, Inc.*,²³¹ one of the earliest Washington Code cases. Mr. Lew's new car disappeared from the dealer's service lot while in the dealer's custody and was found abandoned several months later by the police. Lew refused to accept return of his damaged car, despite a tender of the amount alleged by the dealer to represent his costs and also refused to make further payments under the sales and security agreement which he had signed. In a multiparty suit the trial court entered judgment on behalf of the secured creditor for the deficiency remaining after foreclosure and sheriff's sale of the car.²³² As held by the trial court, the creditor's refusal to accept possession of the car prior to initiating its foreclosure action on the lien removed its subsequent deficiency action from the bar of section 9-501(1). The court of appeals cited with approval the analysis of Professors Shattuck and Cosway²³³ that a deficiency judgment is *not* prohibited by subsection 9-501(1) if the creditor immediately resorts to suit and eschews repossession.

Clearly, the court's interpretation of the effect of the

231. 6 Wash. App. 226, 492 P.2d 258 (1971).

232. From the appellate opinion it appears that Lew was in fact insulated from liability for the unpaid balance by a judgment over against Goodfellow as the negligent party in the theft. *Id.* at 228-29, 492 P.2d at 260.

233. *Id.* at 231, 492 P.2d at 262 (quoting 8 WASH. PRACTICE § 9:1270(5), at 210 (1967)).

nonuniform second paragraph of subsection 9-501(1) is correct. As the Washington Comments²³⁴ to section 9-501 point out, the second paragraph is a continuation, in the case of consumer purchases only, of prior Washington practice under the conditional sales statute,²³⁵ which forced the seller to elect either to repossess or to sue for the balance due on the contract.²³⁶ Under prior Washington law, the seller, upon electing to sue, could enforce his judgment by levy on any property of the debtor, including the property sold.²³⁷ The only change from prior law, therefore, would appear to be that the purchase money financier, by bringing suit, does not lose his original priority in the collateral created by the security interest lien.²³⁸ This change is relevant, however, only with respect to his priority in the collateral against intervening lien creditors of the debtor, including a trustee in bankruptcy, and does not affect the debtor-secured party relationship.

In addition, section 5.103 of the Uniform Consumer Credit Code (U.C.C.C.),²³⁹ not adopted in Washington, but in force in at least eleven states, restricts a purchase money financier of consumer goods with a cash price of \$1750 or less²⁴⁰ to a similar election to repossess or to sue on the contract. The section explicitly prohibits the creditor from attempting in any way to realize his judgment out of the collateral that was the subject of the sale.²⁴¹ In their comments the drafters state that "the rights of the creditor and consumer are controlled by Part 5 (Default) of U.C.C. Article 9, *except to the extent that such rights are changed by this Act.*"²⁴² Based on the specific prohibition of resort to the collateral in U.C.C.C. subsection 5.103(7), the

234. WASH. REV. CODE ANN. tit. 62A (1976) contains Washington comments prepared as an aid to Washington practice.

235. Ch. 106, 1893 Wash. Laws 253 (repealed 1965).

236. See, e.g., Washington Co-op. Chick Ass'n v. Jacobs, 42 Wash. 2d 460, 256 P.2d 294 (1953).

237. Standard Fin. Co. v. Townsend, 1 Wash. 2d 274, 276, 95 P.2d 786, 788 (1939).

238. Section 9-501(5) provides that a levy on the collateral after the secured party reduces his claim to judgment shall relate back to the date of the security interest's original perfection. Under prior law, the effect of a conditional seller suing to enforce the contract was to make the sale absolute, thus terminating his originally retained rights in the collateral, as well as his priority over other creditors who might levy on the collateral before the seller could do so.

239. UNIFORM CONSUMER CREDIT CODE § 5.103 (1974 version).

240. One thousand dollars or less in the 1968 Official Text of the U.C.C.C. *Id.* (1968 version).

241. *Id.* § 5.103(7) (1974 version).

242. *Id.* § 5.103, Official Comment 1 (emphasis added).

Washington Court of Appeals correctly interpreted subsection 9-501(1) to permit the creditor to foreclose on the collateral after judgment. But, even though a secured party holding a purchase money interest in consumer goods may foreclose on the collateral after suing on the contract, the secured party must still determine whether the possibility of collecting a deficiency judgment against the consumer outweighs the risk of total loss or further depreciation in value of the collateral should he fail to repossess immediately on default.

Except as limited in the case of a purchase money security interest in consumer goods, subsection 9-501(1) expressly provides that the secured party's remedies are cumulative, as the Washington Supreme Court has twice confirmed. In the earlier case the supreme court affirmed a court of appeals decision²⁴³ that a secured party may repossess his collateral and at the same time initiate suit for deficiency, in contrast to Washington pre-Code conditional sale and chattel mortgage law.²⁴⁴ The court also upheld the secured party's right to cancel a planned sale under section 9-504 and proceed instead to foreclosure and sheriff's sale.²⁴⁵ In the second case the supreme court upheld the right of a seller of corporate stock, upon default in the purchase agreement, to a deficiency judgment following a public sale of the stock pledged to secure the buyer's performance.²⁴⁶

D. Secured Party Self-Help

Two sections, 9-502 and 9-503, specifically authorize the secured party's resort to collateral without obtaining prior judg-

243. Peoples Nat'l Bank v. Peterson, 7 Wash. App. 196, 498 P.2d 884, *aff'd*, 82 Wash. 2d 822, 514 P.2d 159 (1973).

244. The election of remedies under the Conditional Sales Act has been mentioned. See text accompanying note 236 *supra*. Under the chattel mortgage statute the mortgagee had no alternative but to foreclose. Roche Fruit & Produce Co. v. Vaught, 143 Wash. 601, 255 P. 953 (1927).

245. The court of appeals observed that the creditor can change his method of realization as long as no injury, such as further depreciation to the property, befalls the debtor. 7 Wash. App. at 199 n.2, 498 P.2d at 886 n.2. The supreme court specifically pointed to the debtor's right to object to the secured party's method of realizing on the collateral granted in § 9-507(1)(1st sent.), noting that no such objection was made prior to trial. 82 Wash. 2d at 831, 514 P.2d at 165.

246. Foster v. Knutson, 84 Wash. 2d 538, 527 P.2d 1108 (1974). In a third and more recent case in which the issue of cumulative remedies was not specifically raised, the supreme court nevertheless upheld the secured party's right to repossess some of the collateral and, even prior to sale, bring an action for deficiency and judicial foreclosure on collateral that had not been seized. Borg-Warner Accept. Corp. v. Scott, 86 Wash. 2d 276, 543 P.2d 638 (1975).

ment against the debtor. Pursuant to section 9-502, on default the secured party may collect the proceeds of intangible collateral directly from the account debtors and apply them in satisfaction of the defaulted obligation;²⁴⁷ under section 9-503, the secured party has an immediate right to take possession of tangible collateral, "if such can be done without breach of the peace."²⁴⁸ No Washington appellate cases have discussed section 9-502, but section 9-503, perhaps predictably, is at the eye of the hurricane. Three major issues involving section 9-503 have been litigated: (1) the constitutional validity of self-help repossession prior to judgment, (2) the effect of third-party interests on the secured party's right of repossession, and (3) the meaning of breach of the peace.

In *Faircloth v. Old National Bank of Washington*,²⁴⁹ and again two months later in *Borg-Warner Acceptance Corp. v. Scott*,²⁵⁰ the Washington Supreme Court unanimously joined the large number of state and federal courts upholding the constitutionality of section 9-503 against allegations that the legislative sanction of self-help repossession in section 9-503 constitutes state interference in the debtor's property without due process of law.²⁵¹

247. Agreements for purchase of, or for lending against, intangibles must carefully detail whether the transaction is a sale or a loan, as well as whether the debtor is liable for a deficiency or entitled to a surplus. Specification of these terms is important not only to determine the parties' rights on default under § 9-502, but also to answer other questions involving the agreement. For example, the court of appeals has held that the discount on a sale of accounts, as opposed to the interest on borrowing against accounts, is not subject to the Washington usury statutes. *Schmitt v. Matthews*, 12 Wash. App. 654, 531 P.2d 309 (1975). In addition, because § 9-502 merely requires the creditor to proceed with his collections "in a commercially reasonable manner," standards for collection should also be set out in the agreement to minimize the possibility of later disagreement.

248. WASH. REV. CODE § 62A.9-503 (1979).

249. 86 Wash. 2d 1, 541 P.2d 362 (1975).

250. 86 Wash. 2d 276, 543 P.2d 638 (1975).

251. See, e.g., *Adams v. Southern Cal. First Nat'l Bank*, 492 F.2d 324 (9th Cir. 1973), cert. denied, 419 U.S. 1006 (1974). Numerous additional citations to cases and law review articles are given by the supreme court in the course of the *Faircloth* and *Scott* decisions. The arguments to invalidate § 9-503 are well known. See *Fuentes v. Shevin*, 407 U.S. 67 (1972); *Sniadach v. Family Fin. Co.*, 395 U.S. 337 (1969) (prejudgment seizure of the property of defendant in a lawsuit may occur only after judicial inquiry into the probable likelihood that the plaintiff will prevail on the merits). The recovery of possession by a secured party has been held to be a private remedy, sanctioned either by contract or by common law, and not, therefore, a matter of state action. Cf. *Flagg Bros. v. Brooks*, 436 U.S. 149 (1978) (upheld against a due process attack § 7-210, which allows a sale, without a prior court hearing, under a warehouseman's lien for storage charges). In a later decision sustaining nonjudicial mortgage foreclosure, the Washington Supreme Court cited its *Faircloth* decision with approval. *Kennebec, Inc. v. Bank of the*

Although section 9-503 itself is silent, the common law clearly establishes the right of repossession only against the debtor and creditors whose claims in the collateral are subordinate to those of the party repossessing.²⁵² As the court of appeals recently held in *Barnett v. Everett Trust & Savings Bank*,²⁵³ interference with rights to possession and sale belonging to a creditor senior to the party repossessing constitutes conversion of the senior creditor's interest in the property. The junior creditor repossessed restaurant equipment upon default under a security agreement entered into with the purchasers of the restaurant under a pre-Code conditional sale. The conditional sellers, whose interest had been property recorded under pre-Code law and whose rights were preserved by virtue of that filing without the need for refiling pursuant to subsection 10-102(2), had declared a default and foreclosed in superior court at approximately the same time the bank repossessed.²⁵⁴ Relying on Washington pre-Code law, the court upheld judgment for the conditional sellers against the junior secured party in an amount equal to the loss in value suffered by the collateral upon its removal by the junior party from the restaurant premises. That the senior lien arose under prior law is incidental to the thrust of the decision: rights of junior lien holders to repossess will be terminated by the senior secured party's declaration of default.²⁵⁵

West, 88 Wash. 2d 718, 721, 565 P.2d 812, 814 (1977). The court of appeals has also rejected a debtor's attack on § 9-503. *Mount Vernon Dodge, Inc. v. Seattle-First Nat'l Bank*, 18 Wash. App. 569, 570 P.2d 702 (1977).

252. Section 9-504 implicitly recognizes that the right of repossession belongs only to the senior lien on the collateral by its references in subsections (1) and (4) to the rights (or lack thereof) of creditors junior to the selling creditor and by its omission of reference to rights of creditors senior to the selling creditor.

253. 13 Wash. App. 332, 534 P.2d 836 (1975).

254. The bank's repossession in the face of the perfected earlier interest can be accounted for by the fact that perfection of the prior interest was by filing with the county auditor under the former Conditional Sales Act (originally enacted ch. 106, 1893 Wash. Laws 253) (repealed 1965) (repeal effective 1967). The bank officials and their legal counsel apparently failed to consider the possible existence of a valid pre-Code interest not shown in a U.C.C. record check. The circumstances of this case emphasize the need to determine whether any valid interests not revealed by a check of the U.C.C. filings may exist. Other circumstances are out-of-state perfection preserved under § 9-103 and those circumstances covered in § 9-402(7) of the 1972 Text. See notes 148 & 217 *supra*. Although the U.C.C. has been in effect in Washington since July 1, 1967, and the possibility of pre-Code interests therefore diminishes with time, § 10-102(2) preserves the perfection of pre-Code interests indefinitely; further, the provision for perfecting pre-Code conditional sales contracts by local filing provides for no termination of perfection for a properly filed conditional sale contract until full payment has been made. See ch. 106, § 2, 1893 Wash. Laws 253 (repealed 1965).

255. *Cf. Murdock v. Blake*, 26 Utah 2d 22, 484 P.2d 164 (1971) (judicial creditor's

Neither section 9-503 nor any other provision of the Code contains a definition of breach of the peace. Pre-Code Washington conditional sales cases, however, recognized necessary limits on the seller's right of repossession. When supplemented by numerous cases from other jurisdictions,²⁵⁶ these Washington cases make it clear that a creditor may not use force²⁵⁷ or intimidation²⁵⁸ to recover collateral over the objections of a debtor who is at the scene. The rule is also clear that a secured party may not enter a locked dwelling.²⁵⁹ Nevertheless, he may take without permission a locked car or other object left outside on the debtor's premises.²⁶⁰ Case law clearly extends less protection to the debtor against a secured party's unauthorized invasion of business premises, but the extent of the secured party's power to recover collateral from a business debtor is uncertain.²⁶¹

levy upon, and sale of, judgment debtor's interest in property subject to U.C.C. security interest held to be conversion of secured party's rights in the property).

256. For an annotation of cases discussing breach of peace in the context of creditor repossession, see Annot., 99 A.L.R.2d 358 (1965).

257. In the often-cited case, *Burgin v. Universal Credit Co.*, 2 Wash. 2d 364, 98 P.2d 291 (1940), the Washington Supreme Court approved a jury instruction which read in part:

[I]f the buyer is in personal possession of the [collateral] and protests against such repossession and attempts to obstruct the seller in doing so, then under such circumstances, it becomes the duty of the seller to proceed no further in such attempted repossession and to resort to legal process to enforce his right of repossession given him by the contract. Under such contract the seller is not entitled to use force to repossess [the collateral], and if he does, and in so doing, inflicts personal injuries upon the purchaser or party in lawful possession of the same, he is liable in damages for such injuries.

Id. at 373, 98 P.2d at 295.

258. In *Stone Mach. Co. v. Kessler*, 1 Wash. App. 750, 463 P.2d 651 (1970), a seller repossessed in Oregon a bulldozer sold in Washington. Since the buyer had previously told the seller that he would not allow a repossession without judicial process, the seller had the local Oregon sheriff, uniformed and armed, accompany him to where the defendant was working with the machine. The sheriff ordered the defendant to permit the repossession, although he admitted he had no legal papers. The defendant stood aside, testifying later that he did not resist because he did not believe he could disregard the sheriff's order.

The court of appeals upheld a judgment for the debtor based on conversion. Although the propriety of the repossession was decided under Oregon law, OR. REV. STAT. § 79.5030 (1977), nothing indicates the result would have been different under Washington law. The court cited *Burgin* and other Washington cases to support the debtor's right to resist nonjudicial repossession.

259. Cases abound from other jurisdictions holding entry into a house or locked garage to be a breach of the peace. See, e.g., *Girard v. Anderson*, 219 Iowa 142, 257 N.W. 400 (1934).

260. See, e.g., *Gregory v. First Nat'l Bank*, 241 Or. 397, 406 P.2d 156 (1965); *Pioneer Fin. & Thrift Corp. v. Adams*, 426 S.W.2d 317 (Tex. Civ. App. 1968).

261. See, e.g., *Borg-Warner Accept. Corp. v. Scott*, 86 Wash. 2d 276, 543 P.2d 638

The most recent U.C.C. case decided by the Washington Supreme Court involving a disputed repossession is *Borg-Warner Acceptance Corp. v. Scott*.²⁶² In *Scott*, two agents for the creditor recovered equipment by diverting the debtor's attention while another two rolled the collateral out of his business premises and into a waiting truck. Holding that the debtor had failed to prove any damages as a result of the repossession,²⁶³ the court failed to rule whether the repossession was a breach of the peace. Under the facts stated by the supreme court, however, one can, based on factors present in cases from other jurisdictions, predict that the supreme court would have upheld the trial court's ruling that the repossession was lawful. The entry was made during business hours into the service area of a car repair shop and the goods were removed without objection from the debtor or third parties.²⁶⁴ Moreover, to avoid confrontation, the creditor's agents left as soon as challenged.

If the secured party cannot peaceably repossess the collateral, then his only resort in enforcing the security interest is to the courts, either in foreclosure on the lien or in suit on the underlying debt.²⁶⁵ Should he choose to do so, he can obtain a judgment for the entire sum due him and have immediate execution, not only on the collateral, but also, if the collateral is insufficient to cover the judgment, on so much of the rest of the debtor's property as is necessary to cover the deficiency. The debtor's refusal to relinquish the collateral peaceably does not affect the secured party's property rights in the collateral, and in

(1975). Compare *Cherno v. Bank of Babylon*, 54 Misc. 2d 277, 282 N.Y.S.2d 114 (Sup. Ct. 1967), *aff'd*, 29 A.D.2d 767, 288 N.Y.S.2d 862 (1968) (creditor entry into locked business premises using landlord's key and with his permission not a breach of peace) with *Gulf Oil Corp. v. Smithey*, 426 S.W.2d 262 (Tex. Civ. App. 1968) (unauthorized entry into locked gas station by picking the lock held a breach of the peace).

262. 86 Wash. 2d 276, 543 P.2d 638 (1975).

263. *Id.* at 279, 543 P.2d at 641. The debtor did not assert commission of a tort on his person or conversion of his equity in the property. *Cf. Stone Mach. Co. v. Kessler*, 1 Wash. App. 750, 463 P.2d 651 (1970) (upholding award to debtor of damages measured by the difference between debtor's total payments and fair market value of collateral). In fact, the court found he made no attempt to show any equity existed. 86 Wash. 2d at 280, 543 P.2d at 641. Rather, the injury alleged was for loss of the collateral's use from the date of repossession to trial. While intimating that an action for loss of use might lie in favor of a defaulting debtor, the court dismissed the debtor's claim on the basis that he had not attempted to show any damages as a result of the loss of possession. *Id.* at 281, 543 P.2d at 642.

264. Other cases have permitted entry into open private premises. *See, e.g., Marine Midland Bank-Cent. v. Cote*, 351 So. 2d 750 (Fla. Dist. Ct. App. 1977) (open carport); *Kroeger v. Ogsden*, 429 P.2d 781 (Okla. 1967) (open airplane hangar at public airport).

265. *See* WASH. REV. CODE § 62A.9-501(5) (1979).

measuring the secured party's rights against third-party claimants to the collateral, the lien on execution relates back to the original date of perfection of the security interest.²⁶⁶

E. Satisfaction by Sale or Otherwise

The secured party who has succeeded in repossessing his collateral may elect, except in one instance,²⁶⁷ either to dispose of the collateral under section 9-504 or to retain it in full satisfaction of the debtor's obligations under section 9-505(2) (so-called "strict foreclosure"). If the secured party elects to dispose of the collateral by sale or otherwise,²⁶⁸ the proceeds are used to satisfy the amount due the secured party, as well as the party's costs of sale and reasonable attorney's fees if provided for in the agreement.²⁶⁹ If the proceeds are greater than the amount due the secured party plus costs and recoverable attorney's fees, the excess either will be made available to holders of subordinate interests in the collateral, if there are any who have notified the secured party of their claims, or will be returned to the debtor.²⁷⁰ If the proceeds are less than the amount due, however, the secured party is entitled to sue the debtor for the deficiency under subsection 9-504(2) and to execute on the debtor's other property after obtaining judgment. A good faith purchaser will take the collateral free of all rights of the debtor, of the secured party, and of any lien creditors whose claims are subordinate to the secured party,²⁷¹ a provision necessary to insure that a fair price for the collateral can be achieved. Junior secured parties must realize their claims either out of the remaining proceeds of sale or out of the debtor's other property.

266. *Id.*

267. This instance, provided for in § 9-505(1), arises when a consumer has paid more than 60% of an indebtedness secured by consumer goods. In such a case the secured party must sell the collateral unless the debtor renounces his rights after default. Section 9-507(1)(3d sent.) provides for the award of minimum statutory damages should a secured party fail to comply with the sale requirement of § 9-505(1) and the debtor's actual damages do not exceed the statutory minimum.

268. Section 9-504(1) states that the secured party in possession of the collateral after default may "sell, lease or otherwise dispose" of the collateral. In *Grant County Tractor Co. v. Nuss*, 6 Wash. App. 866, 496 P.2d 966 (1972), the court of appeals held that a judicial determination of the value of collateral constituted a disposition for purposes of entry of a deficiency judgment, even if the creditor had not yet sold the property at the moment judgment was entered. *Id.* at 870, 496 P.2d at 969. Because disposition normally will be by sale, this article will refer to the disposition as a sale.

269. WASH. REV. CODE § 62A.9-504(1)(a)-(b) (1979).

270. *Id.* § 62A.9-504(1)(c)-(2).

271. *Id.* § 62A.9-504(4)(a)-(b).

The Code does not prescribe how collateral must be sold. For the protection of the debtor and the assurance of a fair price,²⁷² however, subsection 9-504(3) establishes as a minimum standard applicable to any disposition of collateral, by sale or otherwise, that "every aspect of the disposition including the method, manner, time, place and terms be commercially reasonable."²⁷³ But the secured party may decide, consistent with this standard, whether to sell by public sale (auction),²⁷⁴ by private negotiated sale,²⁷⁵ or to make some other disposition of the collat-

272. A "fair" price, not a term of art in the Code, would be a price realized on a sale or other disposition, all aspects of which are commercially reasonable, where the debtor and other parties entitled to notice have been properly notified. Section 9-507(2)(1st sent.), recognizing that a price obtained by a disposition that conforms to the requirements of § 9-504(3) nevertheless may be lower than the best price that might have been obtained, insulates the secured party from liability in such an event.

273. *Id.* § 62A.9-504(3). To reduce disputes over the issue of commercial reasonableness, the Code in § 9-507(2) establishes several benchmarks of conduct that, if met, establish a sale as commercially reasonable: (1) sale in a customary manner in a recognized market, (2) sale at the market price, or (3) sale "in conformity with reasonable commercial practices among dealers in [that] type of property." Of course, these rules apply only to sales of collateral having an established market and market price, such as investment securities and automobiles; the rules offer little help to secured parties seeking to sell most varieties of used goods for which no large and established market exists. In case of doubt, however, § 9-507(2)(4th sent.) offers the creditor one certain refuge from attack: disposition approved by a court proceeding or by a bona fide creditors' committee is conclusively presumed to be commercially reasonable.

274. In *Foster v. Knutson*, 84 Wash. 2d 538, 527 P.2d 1108 (1974), the supreme court has further defined what standards must be met for a public sale to be commercially reasonable when no recognized market for the collateral exists:

The sale is valid where notice of 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 of bidders. . . . [The secured party] is required to use his best efforts to sell the collateral for the highest price and to have a reasonable regard for the debtor's interests.

Id. at 549, 527 P.2d at 1114-15.

275. In *Mount Vernon Dodge, Inc. v. Seattle-First Nat'l Bank*, 18 Wash. App. 569, 570 P.2d 702 (1977), the court of appeals rejected a contention that *Foster v. Knutson*, 84 Wash. 2d 538, 527 P.2d 1108 (1974), must be read to bar private sales under the Code. The collateral in *Mt. Vernon Dodge* was new and used cars, which the court observed are "customarily sold in a recognized market and are the subject of widely distributed standard price quotations." 18 Wash. App. at 586, 570 P.2d at 712. The court, noting that a lender does not have to establish itself as a retail dealer to make a commercially reasonable

eral. In addition to a general standard of commercial reasonableness, subsection 9-504(3) specifically requires the secured party to give reasonable notice²⁷⁶ to the debtor and junior creditors who have notified him of an interest in the collateral of the time after which a private sale will be held or the time and place of a public sale.

If the creditor violates the requirements of subsection 9-504(3), subsection 9-507(1) gives the debtor specific legal rights both before and after the sale. If the debtor believes that the secured party is not proceeding properly before a sale has taken place, under subsection 9-507(1) the debtor has the right to seek a court order to restrain the creditor's improprieties or to supervise the sale. In the only Washington case discussing the debtor's right to seek court intervention to correct creditor misconduct prior to sale, both the court of appeals and the supreme court pointed to the debtor's *failure* to object under subsection 9-507(1) during the ten-month pendency of a foreclosure and deficiency action as evidence that the objections raised at trial and on appeal were not well taken.²⁷⁷

If a sale has taken place, the debtor and any junior creditor entitled to receive notice of sale have a right to recover "any loss caused by a failure [of the secured party] to comply with the provisions of [Part 5]."²⁷⁸ Two Washington Court of Appeals cases²⁷⁹ have dealt with creditors' sales in which the notice requirements of subsection 9-504(3) were not met. Both cases held that failure to give the debtor proper notice of sale will not

sale, also approved sales of the collateral to car dealers in the wholesale market and return of the collateral to the factory for credit. *Id.* at 587, 570 P.2d at 712. This last issue has been debated in the literature but seldom decided. See J. WHITE & R. SUMMERS, *supra* note 80, § 26-11, at 990. See also U.C.C. § 9-507, Official Comment 2 (1972 version).

276. The requirement of notice to the debtor of an impending sale cannot be waived prior to default, WASH. REV. CODE § 62A.9-501(3) (1979), but the secured creditor may define in the security agreement when notice must be sent to the debtor. If this time period is consistent with what has been upheld by case law as reasonable, litigation regarding sufficiency of notice may be avoided. No Washington case treating the reasonableness of the notice has been reported; in other jurisdictions cases have upheld notice posted between 8 and 10 days prior to sale. *Associate Discount Corp. v. Forcier*, 5 U.C.C. REP. SERV. 294 (N.Y. Sup. Ct. 1968) (10 days notice); *Atlas Constr. Co. v. Dravo-Doyle Co.*, 3 U.C.C. REP. SERV. 124 (Pa. Ct. C.P. 1965) (8 days notice).

277. *Peoples Nat'l Bank v. Peterson*, 7 Wash. App. 196, 199, 498 P.2d 884, 886 (1972), *aff'd*, 82 Wash. 2d 822, 514 P.2d 159 (1973).

278. WASH. REV. CODE § 62A.9-507(1)(1st sent.) (1979).

279. *Commercial Credit Corp. v. Wollgast*, 11 Wash. App. 117, 521 P.2d 1191, *pet. rev. denied*, 84 Wash. 2d 1004 (1974); *Grant County Tractor Co. v. Nuss*, 6 Wash. App. 866, 496 P.2d 966 (1972).

bar a deficiency judgment but will permit the debtor to recover the loss resulting from his lack of notice under subsection 9-507(1).²⁸⁰ In neither case were any damages awarded, however, because no losses were established.

In the earlier case, *Grant County Tractor Co. v. Nuss*,²⁸¹ the court of appeals reversed an order of the trial court denying a deficiency because of lack of notice prior to sale with directions for entry of a judgment in the amount of the deficiency established at trial. The opinion does not clearly state whether the defendant debtor counterclaimed for damages as a result of lack of notice of sale or whether he prayed only for denial of the deficiency. In any event, no damages resulting from the lack of notice were established at trial, all parties apparently proceeding on the premise that the sale was commercially reasonable and brought the highest price possible. The court of appeals, therefore, did not reach the question of who has the burden of proof on the issue of damages in the event of sale without proper notice. The court also appeared to rest its decision, at least in part, on a finding that the debtor, who voluntarily returned the collateral and gave the secured party written notice of rescission of the underlying sale, might have waived his right to notice of sale.²⁸²

In the second case, *Commercial Credit Corp. v. Wollgast*,²⁸³ the debtor voluntarily relinquished possession to the secured

280. As the court noted in *Grant County Tractor Co. v. Nuss*, 6 Wash. App. 866, 496 P.2d 966 (1972), there are two divergent lines of judicial authority, one denying a deficiency judgment as sanction for improper secured-party conduct in § 9-504(3), and the other permitting a deficiency judgment, subject to the debtor's counterclaim for damages, under § 9-507(1). *Id.* at 869, 496 P.2d at 968-69. Representative cases in the line of authority denying a deficiency are *Skeels v. Universal C.I.T. Credit Corp.*, 222 F. Supp. 696 (W.D. Pa. 1963), *modified on other grounds*, 335 F.2d 846 (3d Cir. 1964), and *Braswell v. American Nat'l Bank*, 117 Ga. App. 699, 161 S.E.2d 420 (1968).

281. 6 Wash. App. 866, 496 P.2d 966 (1972).

282. *Id.* at 870, 496 P.2d at 969. The court cited *Nelson v. Monarch Inv. Plan, Inc.*, 452 S.W.2d 375 (Ky. Ct. App. 1970), as authority for this proposition. The 1962 Text of § 9-504(3) does not expressly authorize even a post-default waiver of notice of sale, and there is a split of authority as to whether a post-default waiver is effective to release the secured party from its obligation to give notice of sale. For an excellent discussion of the issues, see *Hall v. Owen County State Bank*, — Ind. App. —, —, 370 N.E.2d 918, 924 (1977), holding that such a waiver is not permitted under the 1962 Text. The 1972 Text of § 9-504(3) permits the debtor, after default, to sign a statement "renouncing . . . his right to notification of sale." In any event, receipt of the debtor's written rescission or, more properly, revocation of acceptance under § 2-608 of an underlying sales agreement should not be the basis for advice not to send written notice of sale to the debtor in conformity with § 9-504(3), in the absence of a specific renunciation of the right to notice of sale.

283. 11 Wash. App. 117, 521 P.2d 1191, *pet. rev. denied*, 84 Wash. 2d 1004 (1974).

party for the apparent purpose of effectuating a sale. Several months after the repossession and about two months prior to the sale, the secured party sent to the debtor notice that the collateral was subject to sale if the debtor did not contact the secured party. The notice failed to include, however, the date after which a private sale would be held. After acknowledging that insufficient notice does not bar a deficiency, the court of appeals specifically declined to follow those cases from other jurisdictions²⁸⁴ creating a presumption that the collateral was worth at least the amount remaining due and imposing upon the secured party a burden of establishing that the debtor was not prejudiced by not having had an opportunity to participate in the sale. Instead, the court concluded that the debtor had not shown any loss by the lack of notice of sale.²⁸⁵

Although the collateral was sold for \$300, while the amount due at the time was approximately \$1800 and the debtor in his counterclaim asserted a retail value of over \$3000, the court of appeals upheld the trial court's finding that all aspects of the sale were commercially reasonable. The creditor introduced evidence to show that it had sold to the highest of three bidders and produced its employees' repossession reports as evidence of the collateral's deteriorated condition. The creditor also established facts tending to show the debtor abused the collateral while it was in his possession. The debtor, on the other hand, did not establish that he had been denied an opportunity to bid on the collateral as a result of lack of notice, and the court suggested that the debtor might in any case have waived his right to notice by his voluntary surrender of the collateral with the understanding that the creditor would sell it.²⁸⁶

Based on the *Nuss* and *Wollgast* decisions, and in the absence of any contrary indication from the supreme court, it appears that if only the notice of sale is deficient and the secured party can produce evidence to establish the sale was otherwise commercially reasonable, then the burden is shifted to the debtor to show that lack of notice of sale caused him any loss. Absent proof of such loss, Washington courts will award the secured party a judgment for the full deficiency.

284. *E.g.*, *Norton v. National Bank of Commerce*, 240 Ark. 143, 398 S.W.2d 538 (1966).

285. 11 Wash. App. at 124, 521 P.2d at 1196.

286. *Id.* The court cited *Nelson v. Monarch Inv. Plan, Inc.*, 452 S.W.2d 375 (Ky. Ct. App. 1970), and *Grant County Tractor Co. v. Nuss*, 6 Wash. App. 866, 496 P.2d 966 (1972), as authority for its conclusion.

Neither the court of appeals nor the supreme court, however, has confronted a case in which not only was the notice of sale inadequate but also the sale itself did not meet standards of commercial reasonableness. In the absence of any such precedent, a federal district court in Washington has recently held that Washington law would create a rebuttable presumption that the collateral was actually worth the full amount due when the unreasonable sale took place.²⁸⁷ The decision amounts, in effect, to the denial of a deficiency judgment unless the secured party can establish that the true value of the collateral (as contrasted with the sale price) was actually less than the amount due at the time of default. To the extent that he can carry this burden, a deficiency judgment remains available despite the unreasonable disposition. In view of the court of appeals refusal in the *Nuss* and *Wollgast* decisions to recognize denial of a deficiency judgment as a sanction available under the Code for creditor misconduct, the federal court's prediction of Washington law is sound.

If the secured party elects strict foreclosure, he must notify the debtor and, under the 1972 Text, those junior secured parties who have notified him of an interest in the collateral.²⁸⁸ If the secured party receives no objection within the time allowed by the statute,²⁸⁹ he may retain the collateral in full satisfaction of the debtor's obligations under the security agreement. Strict foreclosure also means that the rights of the debtor and all junior secured parties to any excess in value of the collateral over the value due are extinguished and that the secured party is free to deal with the collateral as he wishes, either holding it for his own use or selling it and keeping the proceeds. Obviously, an election to exercise strict foreclosure will usually be made only when the secured party either believes the collateral is worth more than the outstanding debt or feels that further pursuit of the debtor by seeking deficiency judgment would be fruitless. Similarly, an objection to strict foreclosure will ordinarily be raised only when the debtor or a junior secured party believes that the collateral

287. *United States v. Cawley*, 464 F. Supp. 189 (E.D. Wash. 1979). The Small Business Administration (SBA), having paid off the original lender on default of an SBA-guaranteed loan, sued the debtor and the personal guarantors. The SBA's agent, without affording any notice to the debtor, disposed of the collateral without advertisement and with very little effort to find potential buyers. The court determined that pursuant to the Ninth Circuit's holding in *United States v. MacKenzie*, 510 F.2d 39 (9th Cir. 1975), state law should apply to the SBA's suit against the debtor and the personal guarantors.

288. U.C.C. § 9-505(2) (1972 version).

289. Thirty days under the 1962 Text, WASH. REV. CODE § 62A.9-505(2) (1979); 21 days under the 1972 Text, U.C.C. § 9-505(2) (1972 version).

would realize at a sale an excess over the secured party's claim on sale.

Until sale, or until the secured party's election of strict foreclosure has become effective, the debtor has the right to redeem the collateral by tendering the amount of any money then due and performing any other obligations in default.²⁹⁰ The statute further requires that to redeem, the debtor must pay the secured party's expenses on default, including, if provided for in the agreement, attorney's fees. If the debtor does redeem, the security interest is restored and continues in the collateral to secure any unmatured obligations, or the collateral is released of the security interest and returned to the debtor if the obligations have been paid in full. The right to redeem is extinguished by sale or by the secured party's effective election to retain the collateral in strict foreclosure.

IX. CONCLUSION

The advantages to Washington in adopting the 1972 Text of the Uniform Commercial Code are obvious: the statutory resolution of issues inadequately treated under existing law and, equally important, the harmonization of Washington Law with that of its neighbor and commercially significant states. Examples of existing inadequacies the 1972 Text resolves include the proceeds problem (section 9-306, perfection, and section 9-312, priorities); regulation of fixture interests and the interface between real and personal property law (section 9-313); change of name or identity of the debtor (unregulated in the 1962 Text, section 9-402(7) of the 1972 Text); and multistate transactions (section 9-103). Rather than leave the resolution of these and other uncertainties to the haphazard and after-the-fact solutions of litigation, it is far better to afford the planner of commercial transactions the predictability a statutory resolution offers.

By demonstrating the advantages of the 1972 Text, as modified by the several proposed nonuniform amendments intended to deal with Washington problems, the author hopes that the legal community, particularly the Washington Bar Association, will actively support and advocate the adoption of the 1972 Text of the Uniform Commercial Code by the Washington Legislature at its next regular session.

290. WASH. REV. CODE § 62A.9-506 (1979).