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Article 9: Secured Transactions; Sales of Accounts, Contract Rights and Chattel Paper

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be held only to the duty of due diligence and good faith as the "greater" duty owed by the issuer certainly cannot be considered as one of its "rights and privileges."

It is clearly not "at once apparent," as the court stated, that the obligations of the transfer agent and the issuer "must be the same." A more precise drafting of Section 8-406(1) would have removed this possible ambiguity from its meaning.

T.H.T.

ARTICLE 9: SECURED TRANSACTIONS; SALES OF ACCOUNTS, CONTRACT RIGHTS AND CHATTEL PAPER

SECTION 9-102. Policy and Scope of Article

- (1) Except as otherwise provided in Section 9-103 on multiple state transactions and in Section 9-104 on excluded transactions, this Article applies so far as concerns any personal property and fixtures within the jurisdiction of this state
 - (a) to any transaction (regardless of its form) which is intended to create a security interest in personal property or fixtures including goods, documents, instruments, general intangibles, chattel paper, accounts or contract rights; and also

ANNOTATION

†BRUCE LINCOLN-MERCURY, INC. v. UNIVERSAL C.I.T. CREDIT CORP.
325 F.2d 2 (3d Cir. 1963)

The plaintiff automobile dealership and the defendant credit corporation entered into an agreement for the wholesale financing of new cars. The terms required the credit corporation to pay the invoice price to the manufacturer upon the dealer's receipt of new cars, and upon the sale of the cars, the dealer to pay the credit corporation the sum paid to the manufacturer plus interest. Plaintiff later borrowed ten-thousand dollars from the defendant as a capital loan to be repaid in a year for which it pledged shares of its corporation as collateral. The relationship between the parties had already become strained when a local officer of defendant called for a meeting at a crowded restaurant and boisterously demanded immediate payment of the balance of the note. The plaintiff paid the entire amount the next morning and notified the defendant that their business relationship was terminated. Plaintiff sought wholesale financing from another company, which eventually was denied plaintiff. Some time after the termination of business between the parties when the new model cars were introduced, the manufacturer erroneously billed defendant for five cars delivered to plaintiff which defendant's home office mistakenly paid. The plaintiff accepted the cars believing they were financed by its new creditor although the invoices on the cars indicated that

† Based on 1953 Code.

they were paid by defendant. The defendant's local office sent a billing which included a trust receipt to plaintiff who denied ever receiving it. The local officer of defendant went to the plaintiff's show-room, was paid for two cars that the plaintiff had already sold, prohibited sale to customers on the premises and proceeded then and there to auction the remaining three cars for which it had mistakenly paid the manufacturer. Subsequently, the plaintiff sold its dealership.

Plaintiff brought an action against the defendant for inducing prospective customers and financing agencies not to deal with it, based on the premature calling of the note in public and the unorthodox car selling incident. The plaintiff was granted compensatory and punitive damages.

On appeal, the court reversed, holding that the plaintiff failed to establish any tortious interference with its business since it did not show a pecuniary loss of any prospective economic advantage. This holding was supported by the fact that under Section 2-204 there was no contract for financing the five automobiles between the parties, and the plaintiff was mistakenly in possession of the cars. The court further pointed out that the transaction lacked the necessary intent under Section 9-102 to become a secured transaction.

COMMENT

Although there was objective conduct by the defendant indicating an intent to enter into an agreement, the requisite intent to form the financing contract as required by Section 2-204 or to make a secured transaction under Section 9-102 was lacking.

T.H.T.

SECTION 9-302. When Filing Is Required to Perfect Security Interest; Security Interests to Which Filing Provisions of This Article Do Not Apply

(2) If a secured party assigns a perfected security interest, no filing under this Article is required in order to continue the perfected status of the security interest against creditors of and transferees from the original debtor.

CASES ANNOTATED UNDER OTHER SECTIONS

FRENCH LUMBER CO. v. COMMERCIAL REALTY & FIN. CO.

— Mass. —, 195 N.E.2d 507 (1964)

See the Annotation to Section 9-312, *infra*.

SECTION 9-311. Alienability of Debtor's Rights: Judicial Process

The debtor's rights in collateral may be voluntarily or involuntarily transferred (by way of sale, creation of a security interest, attachment, levy, garnishment or other judicial process) notwithstanding a provision in the security agreement prohibiting any transfer or making the transfer constitute a default.

CASES ANNOTATED UNDER OTHER SECTIONS

FRENCH LUMBER CO. v. COMMERCIAL REALTY & FIN. CO.

— Mass. —, 195 N.E.2d 507 (1964)

See the Annotation to Section 9-312, *infra*.

SECTION 9-312. Priorities Among Conflicting Security Interests in the Same Collateral

(5) In all cases not governed by other rules stated in this section (including cases of purchase money security interests which do not qualify for the special priorities set forth in subsections (3) and (4) of this section), priority between conflicting security interests in the same collateral shall be determined as follows:

(a) in the order of filing if both are perfected by filing, regardless of which security interest attached first under Section 9-204(1) and whether it attached before or after filing;

ANNOTATION

FRENCH LUMBER CO. v. COMMERCIAL REALTY & FIN. CO.

— Mass. —, 195 N.E.2d 507 (1964)

French purchased an auto and financed it through Ware. In return, French gave Ware a security interest in the auto which was properly perfected. Later, French gave a security interest in its remaining equity in the auto to Commercial as collateral for funds advanced to French. This security interest was also properly perfected. French failed to make payments under its agreement with Ware and, under threat of repossession, after Ware repossessed the car, arranged to refinance the car with Associates for \$5,022. As collateral, Associates received a security interest in the car from French and in turn paid Ware \$4,256, French's debt to Ware. Ware, after receiving the money, sent Associates the security agreement and cancelled note of French.

When French defaulted in its payments to Associates after paying \$1,297.50, Associates repossessed the car and auctioned it. This action was brought in equity to determine the ownership of the proceeds of the auction as between Commercial and Associates. The lower court held that Associates, although negligent in not receiving an assignment from Ware, was not aware of Commercial's interest in the auto. Had Associates received an assignment from Ware, Associates would have succeeded to Ware's priority. The court held that by the doctrine of subrogation Associates had priority over Commercial to the amount of \$3200 (the total amount received for the auto at the auction) since Associates' negligence did not alter Commercial's previous position.

Upon appeal, the court affirmed, stating that Section 9-312(5)(a) provides that the order of filing determines the order of priorities among secured parties with conflicting interests in the same collateral. Under this section Commercial would prevail over Associates, unless Associates acquired Ware's security interest and priority either by assignment, as provided by Section

UNIFORM COMMERCIAL CODE ANNOTATIONS

9-302(2), or by subrogation. The court held that Associates prevailed over Commercial by subrogation because the Code did not supersede the equitable doctrine of subrogation by virtue of Section 1-103. The court further held that Associates was not limited in its recovery by the original sum owed Ware less any payments by French to Associates.

COMMENT

The court correctly determined that the Code did not supersede the doctrine of subrogation. Section 1-103 provides that principles of law and equity, unless displaced by the Code, remain in effect.

The Code specifically permits a debtor to transfer his remaining interest in collateral given a creditor, as was done in the principal case. Section 9-311 allows this even if the contract between the debtor and creditor prohibits such a transfer by the debtor. The Code provides in Section 9-312(5)(a) that, among creditors with conflicting security interests in the same collateral, the order of priority is determined by the order of filing. Under Section 9-302(2), an assignee of a creditor who has a security interest acquires the creditor's priority over other creditors.

In the principal case, there may be some merit to the argument that Associates could not employ subrogation because (1) it could have succeeded to Ware's priority by receiving an assignment from Ware as permitted by Section 9-302(2) but failed to do so, and (2) Associates attempted to preserve its rights under the Code by filing its security interest but failed. In essence, Associates had an adequate remedy at law but lost it through its own negligence.

Aside from the application of the doctrine of subrogation, theoretically the problem could have been solved without going outside the scope of the Code. If the security interest of Commercial was solely in the debtor's equity in the chattel, then Associate's security interest in the chattel was in that which remained above the debtor's equity in the chattel. If such an interpretation were utilized, Section 9-312 would not have been applicable since the security interest was in the same *chattel* as opposed to being in the same *collateral*. The solution of the court properly avoided this theoretical analization and was the most cogent.

Assuming that the doctrine of subrogation applies in the principal case, the court's holding in awarding damages gives greater rights in the collateral to a party who becomes subrogated than those of the original creditor. Commercial received a security interest in French's remaining equity in the auto. As payments were made by French to Associates, Commercial's interest in the auto should have increased. Subrogation is an equitable doctrine and should not be employed if it will extinguish all rights held by a holder of a second security interest in the same collateral who had complied in all respects with the Code.

R.W.D.

SECTION 9-318. Defenses Against Assignee; Modification of Contract After Notification of Assignment; Term Prohibiting Assignment Ineffective; Identification and Proof of Assignment

(1) Unless an account debtor has made an enforceable agreement not to assert defenses or claims arising out of a sale as provided in Section 9-206 the rights of an assignee are subject to

- (a) all the terms of the contract between the account debtor and assignor and any defense or claim arising therefrom; and
- (b) any other defense or claim of the account debtor against the assignor which accrues before the account debtor receives notification of the assignment.

(3) The account debtor is authorized to pay the assignor until the account debtor receives notification that the account has been assigned and that payment is to be made to the assignee. A notification which does not reasonably identify the rights assigned is ineffective. If requested by the account debtor, the assignee must seasonably furnish reasonable proof that the assignment has been made and unless he does so the account debtor may pay the assignor.

ANNOTATION

FALL RIVER TRUST CO. v. BROWDY, INC.

— Mass. —, 195 N.E.2d 63 (1964)

The plaintiff bank advanced \$7,596.93 to Watuppa Finishing Corp., a dyeing and finishing company, in exchange for assignments of accounts receivable from the defendant, which had submitted goods for finishing. The bank notified defendant of the assignments, but payment was later refused. Defendant claimed that Watuppa owed it for goods delivered and not returned an amount at least equivalent to that which the bank was demanding. The plaintiff brought an action to recover on the assigned accounts and the defendant sought a set-off.

At the trial the only facts to be considered by the court were set out by an auditor's report, which found that Watuppa had received from the defendant goods valued at \$42,393.10 which had not been returned and that Watuppa owed the defendant at least the \$7,596.93 advanced by the bank.

On appeal, the court reversed, holding that Section 9-318(1) was controlling, and the auditor's report did not state facts sufficient to issue a final judgment. Whether the defendant's goods were delivered to the assignor under the contract assigned and the time which defendant's claim arose had to be determined in order to be able to apply the defenses available to an account debtor against an assignee under this section.

COMMENT

Under Section 9-318(1) the assignee of accounts takes subject to only those claims of the account debtor against the assignor which are based upon the same contract out of which the accounts arose, and those which accrue

before the account debtor received notification of the assignment from the assignee. Proper application of this section would allow an assignee to take free from defenses if the account debtor's claim against the assignor arose *independently* from the assigned accounts-contract and *after* the account debtor received notification of the assignment from the assignee.

T.H.T.

SECTION 9-504. Secured Parties Right to Dispose of Collateral After Default: Effect of Disposition

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

CASES ANNOTATED UNDER OTHER SECTIONS

SKEELS v. UNIVERSAL C.I.T. CREDIT CORP.
222 F. Supp. 696 (W.D. Penn. 1963)

For a complete discussion and analysis of this case, see note *infra* p. 831.