Priorities in Accounts: The Crazy Quilt of Current Law and a Proposal for Reform

Dan T. Coenen

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Priorities in Accounts: The Crazy Quilt of Current Law and a Proposal for Reform

Dan T. Coenen*

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## PRIORITIES IN ACCOUNTS

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## I. INTRODUCTION

Moe Promisee has a right under a contract to receive monetary payments from Mae Promisor. Moe assigns his right first to Faye and then to Clay. Whom must Mae pay, Faye or Clay?

For more than a century, judges have struggled with successive assignments to different persons of the same contract right. These cases, which typically involve rights to monetary payments called “accounts,” have generated subtleties of doctrine and disagreements among courts. Today, as a general rule, the Uniform Commercial Code controls these cases. Ambiguities, however, lurk in the Code. Cryptic common-law doctrines also continue to govern many successive-assignment problems. As a result, the law of successive-assignment priorities remains fraught with complexity and confusion.

Against this backdrop it is surprising that no comprehensive treatment of this subject exists in the modern legal literature. Professor Corbin devoted a section of his treatise to disputes among competing assignees. His treatment is outdated, however, because it was pub-

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1. See, for example, Elliot Axelrod, Successive Assignments—Conflicting Priorities, 14 U. Dayton L. Rev. 295, 295 (1989).
2. See, for example, Grant Gilmore, Security Interests in Personal Property § 25.6 at 670-71 (Little, Brown, 1965); David Coleman, Note, Priority of Successive Assignments in Illinois, 1963 U. Ill. L. Forum 261, 261 (stating that “a great diversity of law has developed in American jurisdictions with regard to the test for priority”).
3. See Restatement (Second) of Contracts § 342 cmt. c (1979) (stating that “[t]he subject is now largely governed by the Uniform Commercial Code”).
4. See, for example, notes 118-327 and accompanying text.
5. See notes 36-47, 334-49 and accompanying text.
lished prior to the promulgation of the U.C.C. Professor Farnsworth and other contemporary treatise writers also have touched on this subject, but their analyses lack depth. The contemporary law review literature helps even less: it contains nothing approaching a focused and comprehensive treatment of the priority problems arising from multiple assignments.

This Article intends to fill this gap in the legal literature. It explores in detail the modern law governing successive account transfers. It then considers broader jurisprudential and economic issues raised by these cases and proposes a new framework for assessing successive-assignment problems.

Part II sketches the commercial realities of account transfers. Part III outlines the evolution of the legal principles that govern priorities in

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7. The Supplement to the Corbin treatise itself recognizes, and indeed emphasizes, this fact: Since this chapter was written the use of assignments of contract rights as security for financing a wide variety of commercial activities has greatly expanded. A concomitant proliferation of special rules regarding creation and perfection of the security interest and priority between competing security interests has made this branch of the law a subject in its own right, beyond the scope of this treatise. The reader is referred to the literature on secured commercial transactions with particular reference to Article Nine of the Uniform Commercial Code.

Id. § 876 at 244 n.30 (West, Supp. 1992).

8. See E. Allan Farnsworth, Farnsworth on Contracts § 11.9 at 118-25 (Little, Brown, 1990); John D. Calamari and Joseph M. Perillo, The Law of Contracts § 18-21 at 751-53 (West, 3d ed. 1987); John E. Murray, Jr., Murray on Contracts § 142 at 829-32 (Michie, 3d ed. 1990). Leading commentators on the U.C.C. have discussed important facets of the problem, but have not provided a comprehensive analysis. See, for example, Ronald A. Anderson, 8 Anderson on the Uniform Commercial Code §§ 9-106:5 to 9-106:13 at 565-70 (Lawyer’s Cooperative, 3d ed. 1985 & Supp. 1991) (addressing definitions of accounts and contracts rights, but not specifically addressing the special priority problems caused by multiple transfers of a single account); Barkley Clark, The Law of Secured Transactions Under the Uniform Commercial Code ¶ 1.08[6] at 1-94 to 1-98, ¶ 2.07[6] at 2-58 to 2-61, ¶ 3.03[4] at 3-28 to 3-29 (Warren, Gorham & Lamont, 2d ed. 1988) (discussing transactions involving accounts that are not subject to Article Nine pursuant to Section 9-104(f) and problems raised by Sections 9-301(1)(d) and 9-302(1)(e)); Peter F. Coogan, et al., Secured Transactions under the Uniform Commercial Code § 3.08 at 3-45 to 3-68 (Matthew Bender, 1992) (in Bender’s Uniform Commercial Code Service, Vols. 1-1D) (discussing U.C.C. Sections 9-104(f) and 9-302(1)(e)); William B. Davenport and Daniel R. Murray, Secured Transactions §§ 7.02(b), (c), (e)(2), (e)(3) at 308-11, 313-16 (ALL-ABA, 1978) (setting forth an example of competing security interests in the same account and addressing proceeds priority problem under the 1962 and 1972 versions of the U.C.C.); William D. Hawkland, Richard A. Lord, and Charles C. Lewis, 9 Uniform Commercial Code Series ¶ 9-312:06 at 255-65 (Clark Boardman Callaghan, 1991) (addressing priority among conflicting security interests generally, but not in the specific context of accounts); Ray D. Henson, Handbook on Secured Transactions Under the Uniform Commercial Code §§ 5-6, 5-7 at 146-55 (West, 2d ed. 1979) (discussing some priority problems arising from the assignment of accounts and contract rights); James J. White and Robert S. Summers, Uniform Commercial Code ¶ 22-10 at 1000-02 (West, 3d ed. 1988) (Student Edition) (discussing impact of Section 9-302(1)(e) on filing requirements as to accounts).

9. The only recent treatment dwells on the common-law rules, notwithstanding the U.C.C.’s dramatic statutory reordering of this field of law. See generally Axelrod, 14 U. Dayton L. Rev. 295 (cited in note 1).
successively-assigned contract rights. Part IV then lays out the present-day law of successive-account assignments. In particular, Part IV seeks to impose a structure on this disjointed body of doctrine by describing it in terms of a general rule subject to exceptions. The general rule is that the first assignee to file a U.C.C. financing statement takes priority. The exceptions to this rule, as we shall see, are numerous and complex.

In examining these exceptions, Part IV explores important interpretive issues under U.C.C. Sections 9-104, 9-301(1)(d), 9-302(1)(e), and 9-312, as well as the proper framing of non-Code law in the many cases to which it continues to apply. Part V steps away from these discrete issues and looks at account priorities with a broader focus. It posits that a unifying theme in this field is judicial protection of the "nonprofessional" assignee at the expense of banks and other "professional" financers. Part V defends this orientation as consistent with efficiency and fairness, but also criticizes courts for often pursuing these values in the teeth of clear statutory text.

Responding to difficulties highlighted in earlier sections of the Article—as well as the U.C.C. Permanent Editorial Board's recent initiation of a major reevaluation of Article Nine—Part VI offers a program for reform. That program would amend Article Nine to cover all assignments of contractual rights to any form of monetary payment. In addition, it recommends simplifying and clarifying those Code provisions that govern account assignments. Finally, the program proposed here calls for rewriting the Code's perfection and priority rules to legitimize judicial efforts to protect nonprofessional recipients of limited account assignments. Part VI suggests that adopting these reforms would produce a sound, intelligible, and genuinely uniform body of law to cover the problems created by successive assignments.

II. TRANSACTIONS IN ACCOUNTS

A. Defining the Term "Account"

Assignable rights take many forms. The holder of a contract to buy Sunnybrook Farms has a right that may be transferred to others.\textsuperscript{10} The promisee who has contracted to have a pyramid constructed or an oil well drilled has a transferrable right as well.\textsuperscript{11} The most marketable form of contract right, however, is the right to receive a payment of

\textsuperscript{10} See Corbin, \textit{Corbin on Contracts} § 864 at 430 (cited in note 6) (noting that the right of a purchasing party is assignable).

\textsuperscript{11} See id. § 864 at 429.
money. Such a right typically is referred to as an "account," unless embodied in a promissory note or similar writing, or in so-called "chattel paper." The U.C.C. defines an "account" as "any right to payment for goods sold or leased or for services rendered, which is not evidenced by an instrument or chattel paper, whether or not it has been earned by performance." As we shall see, this legal definition of the term "account" is not coextensive with the businessperson's definition. It identifies well enough for now, however, the basic type of contractual right that this Article concerns.

B. Account Transactions

Rights to future payments have present value. As a result, holders of accounts long have sold these rights for cash or assigned them as security for credit. The earliest transfers of accounts were small, individualized transactions. By the twentieth century, however, dealing in accounts had become big business.

The first form of systematic trading in accounts, often called "factoring," involved purchasing a business's receivables outright. The

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12. A business's receivables are an attractive form of collateral for loans because realizing their value does not require repossession and resale; rather, the secured lender can collect the account proceeds directly from the account debtor under U.C.C. Section 9-502(1). See, for example, Coogan, et al., Secured Transactions § 4B.10 at 4B-51 (cited in note 8); Special Project, The Priority Rules of Article Nine, 62 Cornell L. Rev. 834, 880 n.203 (1977).


14. The U.C.C. refers to such documents as "instruments." Section 9-105(1)(i) defines an "instrument" as "a negotiable instrument . . . , or a certificated security . . . or any other writing which evidences a right to the payment of money and is not itself a security agreement or lease and is of a type which is in ordinary course of business transferred by delivery with any necessary indorsement or assignment." U.C.C. § 9-105(1)(i) (1980) (cross references omitted).

15. U.C.C. Section 9-106(1)(b) defines "chattel paper" as "a writing or writings which evidence both a monetary obligation and a security interest in or a lease of specific goods." It goes on to provide that "[w]hen a transaction is evidenced both by such a security agreement or a lease and by an instrument or a series of instruments, the group of writings taken together constitutes chattel paper."

Distinctive priority rules exist for instruments and chattel paper. See, for example, id. § 9-308. Thus, the treatment of priorities for those specialized forms of contracts rights is beyond the scope of this Article.

16. Id. § 9-106.

17. See notes 506-17 and accompanying text.


19. According to one commentator:

Factoring, which traces its history to the growth of the woolen industry in England beginning in the late 14th century, involved the outright purchase of accounts receivable at a discount by a factor without recourse to the assignor for inability of the account debtor to pay. In most instances, the factor notified the account debtor of the assignment by an appropriate legend on the original invoice and collected the account in its own name. Morton M. Scult, Accounts Receivable Financing: Operational Patterns Under the Uniform Com-
emergence of factoring as a form of commercial activity illustrates the recognition of a new variety of value-maximizing exchange.\textsuperscript{20} The account-purchasing factor made money on the spread between the face value of the receivable and the discounted cash price the factor paid for it.\textsuperscript{21} In turn, the cash paid for the account provided the account seller with capital needed to fund current business operations.\textsuperscript{22} As the factoring industry matured, more specialized forms of factoring arrangements emerged. For example, a factor buys “without recourse” when it is required to absorb losses that arise from unpaid accounts.\textsuperscript{23} A factor buys “with recourse” when the assignor must buy back an account if the account debtor defaults.\textsuperscript{24} Under a “notification” arrangement, the account debtor is told of the account transfer and remits payment directly to the factor-assignee.\textsuperscript{25} Under a “non-notification” arrangement, the account debtor continues to pay the assignor, who passes along any payments received to the factor.\textsuperscript{26} All these forms of factoring, as well

\textit{mercial Code}, 11 Ariz. L. Rev. 1, 2 (1969) (footnotes omitted). The term “factoring” today is used in a number of different ways. See, for example, R.E. O’Leary, Accounts Receivable as Security, 29 Mo. L. Rev. 486, 487-88 (1964). In this article the term is used to describe the outright purchasing of accounts. The term “discounting” also is sometimes used for this purpose. Id. at 487.


\textsuperscript{21} See Clark, \textit{The Law of Secured Transactions} ¶ 1.04 at 1-24 (cited in note 8) (noting payment risk and payment delay as two factors determining discount price at which factor purchases accounts).

\textsuperscript{22} See Coogan, et al., \textit{Secured Transactions} § 15.01 at 15-3 (cited in note 8) (noting that businesses “will often turn to a professional financer to convert receivables into cash for current needs”); \textit{Daly v. Shrimplin}, 610 P.2d 397, 398 (Wyo. 1980) (stating that business that supplied water to drilling sites “sold accounts receivable at a discount to secure operating cash”). Notably, the development of factoring also created efficiencies by facilitating the specialization of labor. See Scult, 11 Ariz. L. Rev. at 2 (cited in note 19) (noting that factoring permits the assignor “to dispense with credit and accounts receivable departments”). See generally Comment, \textit{Multistate Accounts Receivable Financing: Conflicts in Context}, 67 Yale L. J. 402, 402-03 (1958) (discussing advantages of factoring).

\textsuperscript{23} See, for example, Clark, \textit{The Law of Secured Transactions} ¶ 10.04(2) at 10-43 (cited in note 8).

\textsuperscript{24} See, for example, Gilmore, \textit{Security Interests in Personal Property} § 5.2 at 132 (cited in note 2). See also U.C.C. § 9-502 cmt. 4 (stating that “there may be a true sale of accounts . . . although recourse exists”).

\textsuperscript{25} See, for example, Clark, \textit{The Law of Secured Transactions} ¶ 1.04 at 1-24 (describing notification-based factoring).

\textsuperscript{26} Gilmore, \textit{Security Interests in Personal Property} § 25.6 at 671 (noting, among other things, that “non-notification accounts receivable financing . . . during the first half of this century, came to rival notification financing in volume and importance”). The drafters of the U.C.C. noted the distinction between notification and non-notification factoring in the Official Comments: “Under the non-notification system of accounts financing, the seller-assignor, despite the assignment, bills and collects from the account debtor; under notification financing the account debtor makes payment to the assignee, but the bills may be prepared and sent out by either assignor or assignee.” U.C.C. § 9-103 cmt. 5(a). See also id. § 9-502 cmts. 1 & 2 (describing various forms of account assignments).
as others, remain in place today. 27

Account assignments result not only from factoring, but also from another common commercial practice known as "accounts receivable fi-

nancing." 28 Unlike the factor, the accounts receivable financer does not purchase the assignor's accounts outright; rather, the financer takes a collateral assignment of those accounts and then lends money against them. 29 Many secured transactions arise in this way. A local bank, for example, may agree to lend funds to a general contractor secured by its right under a construction contract to as-yet unearned progress pay-

ments. 30 A financial institution may provide funds to a sales firm or manufacturer, taking as security a floating lien on the borrower's ever-

shifting corpus of accounts. 31 Or a lender may provide its customer with a line of credit against which the customer may borrow so long as its assigned account pool remains at a stipulated level. 32 The common ele-

ment of these and like transactions is that an institutional financer lends money against accounts, rather than buying those accounts directly. 33

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27. For an illustration of a specialized form of notification-and-recourse-based factoring, see In re Amco Products, Inc., 17 Bankr. 758 (Bankr. W.D. Mo. 1982), rev'd, 50 Bankr. 723 (W.D. Mo. 1983). The bank, acting as factor, required a reserve account to be kept by the customer from which the bank could directly collect otherwise uncollectible portions of any assigned rights to payment; the customer had to maintain the account at no less than five percent of the balance of outstanding amounts due. Id. at 759. For another illustrative account transfer arrangement, see Major's Furniture Mart, Inc. v. Castle Credit Corp., 602 F.2d 538, 540 (3d Cir. 1979) (describing recourse arrangement under which factor paid assignor face amount of each account less 15% "discount" and less another 10% to produce a reserve fund for chargeback of bad accounts).

28. See, for example, Scult, 11 Ariz. L. Rev. at 1-2 (cited in note 19).


30. See E. George Rudolph, Financing on Construction Contracts Under the Uniform Com-

mercial Code, 5 B.C. Indus. & Comm. L. Rev. 245, 246 (1963) (stating that "[b]uilding contractors commonly assign future payments under their contracts as security for working capital loans"). Numerous cases involving this form of financing are discussed in notes 420-46 and accompanying text. For a discussion of the specialized federal-law problems presented by assignments of rights to payment for work on federal government projects, see Clark, The Law of Secured Transactions ¶ 11.06 at 11-31 to 11-36 (cited in note 8).


32. See, for example, Lehigh Press, Inc. v. National Bank of Ga., 389 S.E.2d 376, 377 (Ga. Ct. App. 1989) (describing line of credit agreement under which assignor "could borrow . . . an amount equal to 80 percent of [its] eligible receivables up to $250,000").

33. On the values and attractiveness of accounts receivable financing, see O'Leary, 29 Mo. L. Rev. at 489 (cited in note 19). For another good discussion of factoring and accounts receivable financing, see Scult, 11 Ariz. L. Rev. at 1-4 (cited in note 19).
Account transfers also occur outside the contexts of commercial factoring and institutional accounts receivable financing. A borrower may pay off a debt owed a family member by transferring some right to future payment to that person.\footnote{34} A small merchant may sell a single receivable to raise quick cash for business operations.\footnote{35} A corporation may assign accounts as part of a sale of assets or upon its liquidation.\footnote{36} Given this array of transactions in accounts, it is not surprising that claims by more than one assignee to the same account often arise. The law has responded to resulting priority problems in three distinct stages: (1) the development of common-law rules; (2) the ensuing enactment of accounts receivable statutes, beginning in the 1940s; and (3) the later promulgation of the U.C.C. with its extensive, but incomplete, treatment of account assignments.

III. The Development of the Law of Successive Account-Holder Priorities

A. The Common-Law Response

As with other contract law problems, issues of account-assignee priority were initially the business of the common-law courts. The courts in this country dealt with these conflicts by spinning out no fewer than three different rules. The “New York Rule” insisted that “[f]irst in time is first in right.”\footnote{37} Under this rule, priority went to the first assignee, even if that meant the second assignee had to disgorge payments already received.\footnote{38} The “English Rule,” adopted in states such as California and Pennsylvania, gave priority to the first value-giving assignee to notify the account debtor of the assignment.\footnote{39} Under this rule, “second in time” meant “first in right” so long as the second assignee provided the initial notification without knowledge or reason to know of an earlier transfer.\footnote{40} Finally, the authors of the Restatement of Contracts,
tracking the law of Massachusetts, adopted the delightfully denominated "four horsemen rule." That rule gave priority to the first assignee except when the second assignee, without knowledge or notice of the first assignment, (1) received payment, (2) obtained a judgment against the account debtor, (3) made a novation with the account debtor, or (4) received a writing customarily accepted as a symbol of the assigned right.

This three-way traffic in American law was not, it turned out, complex enough for American courts. Some courts generated "completely confusing decisions." Others shifted positions. Still others adopted rules that differed from any of the three main approaches. In all jurisdictions, complicating principles of equity overlaid the applicable common-law rule. So stood the law in 1943, when the Supreme Court...
handed down its decision in *Corn Exchange National Bank & Trust Co. v. Klauder*.

### B. The Accounts Receivable Statutes

In *Klauder*, the Court held that an account assignment unaccompanied by notice to the account debtor was a preference voidable by the bankruptcy trustee in states that followed the English rule. The Court's reasoning in the case was hardly exotic, for it simply put the bankruptcy trustee—as required by then-existing bankruptcy law—in the shoes of a diligent good faith purchaser of the account. For two practical reasons, however, the decision sent shock waves through the commercial finance industry. First, the taking of account assignments on a non-notification basis became entirely unworkable in all English rule states. Second, factors and lenders feared that, even in non-English rule states, courts would read *Klauder* broadly to favor the bankruptcy trustee over assignees who in good faith had given fair value for their interests in the debtor's accounts. This concern, as it turned out, proved well-founded.

In response to resulting cries of alarm, legislatures in most states
enacted "accounts receivable statutes." The purpose of these statutes was to provide an airtight mechanism by which the factor or accounts receivable financer could lock in a position superior to the ever-lurking bankruptcy trustee.

How did the assignee achieve this perfected status? Some states enacted validation statutes, by which perfection occurred automatically; in other words, the legislature simply codified the New York first-in-time rule. In other states, the legislature put in place a public recordation system and granted perfection and priority to the first assignee to file a notice of its interest. At least one state adopted a bookmarking statute, under which the assignee clinched priority by physically noting its interest on the assignor's account ledgers. By 1952, more than forty states had enacted some form of accounts receivable statute. However, the ensuing enactment of Arti-

because it was still possible for a bona fide purchaser to have gained priority by, for example, collecting the debt.

55. See Gilmore, Security Interests in Personal Property § 8.6 at 272 (stating that Klauder "move[d] the state legislatures into action with unprecedented speed"); In re Panama Airways, Inc., 4 U.C.C. Rep. Serv. (Callaghan) 424, 429 (S.D. Fla. 1967) (quoting Gilmore, Security Interests in Personal Property § 8.6). Congress later amended the Bankruptcy Act to overturn the result of Klauder. Even so, the accounts receivable statutes stayed on the books. See, for example, O'Leary, 29 Mo. L. Rev. at 488-89 (cited in note 19).

56. See Panama Airways, 4 U.C.C. Rep. Serv. at 429 (finding that the accounts receivable statute was "intended to cover and protect the widely prevalent commercial practice of non-notification financing through assignment of accounts receivable, which had been previously threatened by attack in the bankruptcy courts under [Klauder]"); Gilmore, Security Interests in Personal Property § 8.7 at 278-79 (stating that purpose of statutes was to supply an "indefeasible status" and "impregnable position" to assignee). See also Coleman, 1963 U. Ill L. Forum at 268 (cited in note 2) (stating that accounts receivable statute passed so that "assignee would be secure against conflicting interests").

57. Gilmore, Security Interests in Personal Property § 8.7 at 274. The Illinois experience is illustrative:

In 1943 the Illinois legislature responded [to Klauder] by passage of the accounts receivable statute, thereby defining when and how accounts receivable could be perfected so that an assignee would be secure against conflicting interests in accounts assigned to him. Known as a validation statute, it adopted the rule that notification was unnecessary in the field of accounts receivable financing, and declared that a written assignment of an account receivable would be valid as against all creditors and subsequent assignees "at the time such assignment was or is made."

Coleman, 1963 U. Ill L. Forum at 268 (footnotes omitted).

58. See Gilmore, Security Interests in Personal Property § 8.7 at 275.

59. U.C.C. § 9-302 cmt. 5 (indicating that one state—North Dakota—had enacted a bookmarking statute). See also Kupfer and Livingston, 32 Va. L. Rev. at 933 & n.60 (cited in note 43) (indicating that Georgia and Pennsylvania, at least initially, passed bookmarking statutes).

60. U.C.C. § 9-302 cmt. 5. See also Gilmore, Security Interests in Personal Property § 8.7 at 276 n.5 (asserting: "By 1958 there were 15 validation statutes and 23 filing statutes. One state (North Dakota) had a 'bookmarking' statute. . . .") (citing Comment, 67 Yale L. J. at 410 nn.32, 33 (cited in note 22)); Parnsworth, Parnsworth on Contracts § 11.9 at 122-23 n.29 (cited in note 8). For a valuable collection and discussion of the various account receivable statutes (particularly the many variations among such statutes), see Comment, 67 Yale L. J. at 410-17 (cited in note 22).
C. The U.C.C.'s Treatment of Accounts

Article Nine of the U.C.C. was a project of monumental proportions compared to the accounts receivable statutes. The drafters of Article Nine sought to integrate the treatment of all security transfers of personal property, including goods, fixtures, quasi-intangible property like notes and documents of title, and all forms of intangible property, including accounts. In keeping with this aim, Article Nine recognized a single, unitary form of collateral transfer known as the "security interest." The Code then established a comprehensive set of rules governing these security interests. Those rules specify how to create, perfect, and enforce a security interest, as well as how to determine priorities among competing claimants of property subject to a security interest. As a rule, the creation (or, to use the Code's terminology, "attachment") of a security interest requires the debtor to execute a "security agreement" describing the transferred property. In general, the Code requires an additional step—usually public filing of a financing statement—to perfect the security interest. In conformance with the purpose of Article Nine, these rules apply only, as a general matter, to transactions in which property is taken as collateral for a debt.

The Code's drafters, however, decided that the account should occupy a place of distinction in Article Nine. In particular, they ex-

61. See U.C.C. § 9-102(1); Gilmore, Security Interests in Personal Property § 8.6 at 271 (noting that accounts receivable statutes have been repealed with enactment of the Code).
63. U.C.C. § 1-201(37). See Coogan, et al., Secured Transactions § 2.01 at 2-5 to 2-6 (cited in note 8) (stating that "Article 9 substituted the generic security interest" for a multiplicity of pre-Code security devices).
64. See U.C.C. §§ 9-203, 9-204.
65. See id. §§ 9-302 to 9-306, 9-401 to 9-408.
66. See id. §§ 9-501 to 9-507.
67. See id. §§ 9-201, 9-301, 9-307 to 9-315.
68. Id. § 9-203.
69. See id. § 9-203(1)(a).
70. See id. §§ 9-401, 9-402. See generally Coogan and Gordon, 76 Harv. L. Rev. at 1541, 1544 (cited in note 31) (stating that perfection in the "bankruptcy sense" means that "the parties have taken all necessary steps to protect against attack by a subsequent lien creditor," and thus, under federal bankruptcy law, the bankruptcy trustee).
71. See U.C.C. § 9-102(1)(a).
72. The Code's drafters also put chattel paper in a place of distinction in Article Nine and, in many ways, treated accounts and chattel paper in similar fashion. See, for example, id. (regarding treatment of absolute transfers of accounts and chattel paper as security interests). In many respects, however, the Code distinguishes between accounts and chattel paper. See, for example, id. § 9-305 (regarding possessory perfection). See generally id. § 9-102 cmt. 5 (itemizing U.C.C. provisions dealing specifically with both accounts and chattel paper). For this reason, this Article con-
tended Article Nine’s rules of attachment, perfection, and priorities not only to collateral transfers, but also to outright sales of accounts.73 The drafters took this step for a number of reasons. First, they saw the distinction between account sales and account security transfers as murky in many cases.74 Second, the Code’s drafters recognized that unrecorded sales of the wholly intangible interest in accounts, no less than collateral transfers of such property, would generate “the type of secret interest which the law abhors.”75 Third, the Code’s treatment of accounts tracked the accounts receivable statutes, which generally did not distinguish between account sales and security transfers.76

cerns itself solely with accounts.

73. Id. § 9-102(1)(b). See, for example, In re Cripps, 31 Bankr. 541, 543 (Bankr. W.D. Okla. 1983) (collecting case-law authority on application of U.C.C. to outright account sales); Coogan and Gordon, 76 Harv. L. Rev. at 1541 (cited in note 31) (stating that “as a practical matter, all buyers of accounts . . . are secured parties, even though the transaction is not one ordinarily thought of as a secured transaction”). To accomplish this result, the Code drafters defined the term “security interest” to include (in addition to collateral transfers of all other forms of personal property) “any interest of a buyer of accounts,” U.C.C. § 1-201(37) (emphasis added), and stated in Section 9-102(1)(b) that Article Nine applied to “any sale of accounts.”

74. U.C.C. § 9-102 cmt. 2. See, for example, Valley Bank of Nev. v. City of Henderson, 528 F. Supp. 907, 911 (D. Nev. 1981) (noting the difficulty of determining whether an assignment is meant as a security interest or an outright purchase); K.A.O.P. Co. v. Midway Nat'l Bank, 372 N.W.2d 774, 777 (Minn. Ct. App. 1985) (stating that “Article 9 of the Uniform Commercial Code applies to both security interests in accounts and to outright sales of accounts because of the difficulty in distinguishing between a security transfer and a sale”); Coogan, et al., Secured Transactions § 3.08[1][a] at 3-45 (cited in note 8).

The difficulty of drawing this distinction derives in large measure from the existence of hybrid factoring arrangements, under which the factor has a significant, but not total, right of recourse against the assignor upon default by the account debtor. Professor Gilmore deemed even the outright-purchasing nonrecourse factor a “financier, a ‘banker,’ a lender of money against security” because it “is a supplier of working capital, not a joint venturer in a business enterprise.” Gilmore, Security Interests in Personal Property § 5.1 at 128-29 n.3 (cited in note 2). For similar views, see Bramble Transp., Inc. v. Sam Senter Sales, Inc., 294 A.2d 97, 101 (Del. Super. Ct. 1971) (citing Delaware Study Comment to Section 9-102 as noting that inclusion of outright sales “fully recognizes the commercial practice, frequently followed by manufacturers, merchandisers, and other businessmen of deriving working capital from such assets in order to finance various phases of their business”), aff’d, 294 A.2d 104 (Del. 1972); Rudolph, 5 B.C. Indust. & Comm. L. Rev. at 245 n.3 (cited in note 30) (noting that whether an assignment is outright or for security “is only a technical distinction since either form may be used to finance on future payments”); Karen C. Jensen, Comment, Assignment of Accounts and Contract Rights—Exploring the Scope of Article Nine and Applying the 9-302(1)(e) Filing Exemption, 1977 Utah L. Rev. 331, 332-33. See also Henson, Handbook on Secured Transactions § 5-6 at 146-47 (cited in note 8).


76. See U.C.C. § 9-302 cmt. 5; Gilmore, Security Interests in Personal Property § 8.7 at 275 (cited in note 2) (stating that “the statutes were typically very broad: transfers which were sales or
The framers of Article Nine, however, did not follow accounts receivable statutes that required filing to perfect each and every account assignment. The drafters concluded that these statutes were tripping up some account assignees who never would have thought of filing and did not remotely resemble professional factors and account financers. For this reason, the drafters decided to bestow perfection on some account assignments regardless of filing and to exclude other account transfers from the Code altogether. This decision has complicated greatly present-day priority rules applicable to successive-account-assignment problems. In particular, it has meant that a complex mix of Code and non-Code law governs these disputes.

IV. Present-Day Priority Rules

Lawyers and judges who confront account-priority problems must deal with a welter of complexities: the need to decide whether or not the priority conflict falls within the Code; the nonuniformity, sparseness, and indeterminacy of non-Code law; the possible impact of the Code on the formulation of non-Code rules; and the presence of knotty interpretive problems within the Code itself. The framework set forth in this Part of the Article seeks to help courts and lawyers steer their way through these booby traps. Most basically, it does so by suggesting that the law of successive-assignment priorities is best understood in terms of a general rule marked by various exceptions. We turn first to the general rule.

A. The General Rule: The First to File Wins

The Code defines the term “security interest” to cover not only assignments of collateral interests in accounts, but also most outright account sales. It follows that U.C.C. Section 9-312, which fixes priorities among conflicting security interests, governs most priority disputes between account assignees. The general rule of Section 9-312 is set forth in subsection (5)(a):

outright assignments were included as well as transfers for security”); id. § 10.5 at 308.
77. See Gilmore, Security Transactions in Personal Property § 8.7 at 276.
78. Id.
79. See U.C.C. § 9-302(1)(e), (g).
80. See id. § 9-104(f).
81. See notes 210-327 and accompanying text.
82. See notes 36-47 and accompanying text.
83. See notes 334-49 and accompanying text.
84. See, for example, notes 351-402 and accompanying text.
85. U.C.C. § 1-201(37).
86. See note 2.
Conflicting security interests rank according to priority in time of filing or perfection. Priority dates from the time a filing is first made covering the collateral or the time the security interest is first perfected, whichever is earlier, provided that there is no period thereafter when there is neither filing nor perfection.\footnote{87}

Section 9-312(5)(a) speaks of both filing and perfection because the holders of security interests often can perfect their interests in ways other than filing; in particular, most security interests in goods are perfectible by taking possession.\footnote{88} The Code makes clear, however, that a secured party may not perfect by way of possession the distinctively intangible interest in accounts.\footnote{89} Thus, with only two exceptions that concern automatic, rather than possessory, perfection,\footnote{90} security interests in accounts covered by the Code are perfectible \textit{only by filing}.\footnote{91} This fact permits translation of Section 9-312(5)(a)'s first-to-perfect-or-file directive into an even simpler general rule for accounts: Priority belongs to the first filer.\footnote{92}

Application of this general principle poses no serious problem in most cases. A complication arises, however, when the first of the two assignments is an absolute, rather than collateral, transfer. In such a case the question arises whether the first-to-file principle of Section 9-

\footnotesize

\begin{itemize}
\item 87. U.C.C. § 9-312(5)(a). See Scult, 11 Ariz. L. Rev. at 25 (cited in note 19) (stating that "where no special rule exists to cover a particular situation, the general rules stated in section 9-312(5) apply").
\item 88. See U.C.C. § 9-305.
\item 89. See id. §§ 9-302(1), 9-305 cmt. 1; Cripps, 31 Bankr. at 543-44 (quoting White and Summers, \textit{Uniform Commercial Code}) (stating that "[e]ven if the creditor collects ledger cards, journals, computer print-outs, sales slips and any other items believed to represent receivables he will not by those acts perfect a security interest in accounts"). But see Feldman v. Philadelphia Nat'l Bank, 408 F. Supp. 24, 38 (E.D. Pa. 1976) (suggesting, erroneously, that assignee's possession of written assignment document perfects that assignee's interest in account); \textit{In re Epps}, 25 Bankr. 115, 117 (Bankr. N.D. Tex. 1982) (suggesting that possession of contractual right to renewal commissions was obtained upon notice to account debtor and account debtor's issuance of written recognition of assignment).
\item 90. See U.C.C. §§ 9-302(1)(e), (g).
\item 91. Id. § 9-302 cmt. 5; id. § 9-305 cmt. 1 (stating that "security interest in accounts . . . may under this Article be perfected only by filing"). See, for example, Scult, 11 Ariz. L. Rev. at 11 (cited in note 19); Gilmore, \textit{Security Interests in Personal Property} § 25.8 at 674-75 n.2 (cited in note 2).
\end{itemize}
312 or the rights-in-the-collateral principle of Section 9-203 controls. The problem is highlighted by hypothetical Case A:

Case A. On January 1, Mike Mechanic repairs the car of Obie Obligor, who has agreed to pay Mike $1000 for his work on April 1. On February 1, Mike sells without recourse at a substantial discount all his accounts receivable, including the Obie Obligor account, to First Assignee Factoring, Inc. On March 1, Second Assignee Bank lends Mike $50,000 and secures from him a floating lien covering all accounts, including the account owed by Obie Obligor. The Bank files its U.C.C. financing statement later that day. First Assignee Factoring files its financing statement thereafter. When Mike defaults, who has a prior right to payment from Obie, First Assignee Factoring or Second Assignee Bank?

Under an orthodox first-to-file analysis, Second Assignee Bank, as the first filer, takes priority over First Assignee Factoring. This is true even though First Assignee Factoring was, true to its name, the first assignee. Indeed, Second Assignee Bank would prevail even if it took its assignment with knowledge of the earlier assignment to First Assignee Factoring, and even if First Assignee Factoring first gave notice to Obie of the assignment to it. These results differ radically from those dictated by pre-Code common-law principles. They are, however, proper under Section 9-312’s pure race rule.

But wait. First Assignee Factoring might argue that it wins due to the absolute character of the assignment it received, notwithstanding

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93. See notes 84-91 and accompanying text.
95. See, for example, *K.A.O.P. Co.*, 372 N.W.2d at 778; Coogan, et al., *Secured Transactions* § 15.10(b) at 15-50 (cited in note 8); O’Leary, 29 Mo. L. Rev. at 496 (cited in note 19); Clark, *The Law of Secured Transactions* ¶ 3.08(1)(b) at 3-82 & n.289 (cited in note 9) (noting, but properly criticizing, cases holding that first filer loses if filing made with knowledge of prior unperfected security interest); Coogan and Gordon, 65 Harv. L. Rev. at 1523-54 (cited in note 31) (stating that, under Section 9-312(b)’s first-to-file rule, a “first filer’s knowledge that there exists an earlier created security interest which has been perfected through a later filing is also irrelevant”).
96. See *M.D. Hodges Enters., Inc. v. First Ga. Bank*, 256 S.E.2d 350 (Ga. 1979) (applying first-to-file rule to grant priority to second assignee that gave second notice to account debtor of assignment).
97. See notes 36-47 and accompanying text. See also Rudolph, 5 B.C. Indust. & Comm. L. Rev. at 255 (cited in note 30) (stating that “[i]f the first assignee has perfected his assignment by filing and has priority under the provisions of the Code, then he will apparently be able to recover amounts already collected by the junior assignee,” and noting that the Massachusetts rule is changed by this result). See generally Coleman, 1963 U. Ill. L. Forum at 268-69 (cited in note 2).
Second Assignee Bank’s earlier filing and the pure race principle of Section 9-312. After all, the common law views an absolute assignment as divesting the assignor of all its rights in an account in much the same way a handoff rids a quarterback of the pigskin. One must have rights in the collateral to create an enforceable security interest. It follows, according to this argument, that Second Assignee Bank could not receive a security interest at all in the Obie Obligor account on March 1, much less an interest entitled to priority under Section 9-312. As a result, the argument goes, First Assignee Factoring should win.

Given the text, structure and history of the Code, courts should reject this argument. The suggested interpretation would in effect exempt outright buyers of accounts from the filing requirement. Section 9-302, however, specifies only two particular instances in which absolute assignments are automatically perfected. That section thus teaches that no automatic perfection rule—or functional equivalent thereof—exists for absolute assignments. The proposed interpretation also would make the Code, with respect to absolute assignments, a validation-type statute that carries forward the New York first-in-time

99. See Charles L. Knapp and Nathan M. Crystal, Problems in Contract Law 1133 (Little, Brown, 2d ed. 1987); Farnsworth, Farnsworth on Contracts 11.10 at 126-27 (cited in note 8); Corbin, Corbin on Contracts § 902 at 614 (cited in note 6) (stating that “[a]n assignment of a contract right is operative to extinguish the right of the assignor,” and that “[t]o produce this effect, it is not necessary that notice shall be given to the obligor”).

100. U.C.C. § 9-203(1)(c).

101. Compare Septembertide Publishing, B.V. v. Stein & Day, Inc., 884 F.2d 675, 681-82 (2d Cir. 1989). In that case, the court broadly stated that funds owed by a subpublisher to a publisher that were previously transferred to the author “could not be assigned thereafter [to the publisher’s professional financer] because an assignor cannot assign that which it no longer owns or controls.” Id. In giving priority to the author over the professional financer, however, the court also broadly relied on its determination that author was a third-party beneficiary of an agreement under which the subpublisher was bound to make payments to publisher. Id. at 682.

102. In an earlier draft of this Article, this sentence read: “Given the text, structure, and history of the Code, we should expect to hear this argument only from drunken sailors.” I substituted the sentence in the text only after Professor McDonnell—who is hardly a drunken sailor, but instead is one of the nation’s leading authorities on Article Nine—indicated that the rights-in-the-collateral argument at least is plausible when the assignor has made an absolute assignment of an account to the first assignee without retaining any collection responsibilities or acceding to any recourse or chargeback arrangement. For the reasons set forth immediately below, I find this position unpersuasive. In considering this issue, however, one must distinguish Case A from one in which the first assignee receives an absolute assignment and the account debtor also makes an enforceable agreement that it will pay account proceeds directly to the assignee. In such a case, the rights-in-the-collateral argument is far stronger because the assignee holds not only an Article Nine security interest, but also has a novation or third-party beneficiary arrangement that independently negates any continuing payment right claimable by the assignor. Even in this situation, it is not clear under existing authorities that the assignor loses transferable rights in the previously transferred account. See generally notes 416-21.

103. See generally U.C.C. § 9-302.

104. See id. at § 9-302(1)(e) (regarding nonsignificant-part assignments); id. § 9-302(1)(g) (regarding assignments for the benefit of creditors).
The history of the Code makes clear, however, that Article Nine was designed to displace accounts receivable statutes of the validation variety with a notice-by-recording system. The Code's description of the absolute transfer of accounts as a "security interest" further suggests that the assignor does not part with all transferable rights in accounts even following an absolute assignment. The cases, not surprisingly, also point in this direction.

Finally, the proposed trumping of the Section 9-312 first-to-file principle by the Section 9-203 rights-in-the-collateral principle would undermine two policies at the core of Article Nine's treatment of accounts. First, this interpretation would require courts to distinguish between account sales and account security transfers. This is the very line, however, that the drafters sought to avoid drawing by subjecting both types of assignments to the Code. Second, the proposed interpretation wars with the Code's overriding purpose of defeating secured parties who rely on secret interests, for the unrecorded absolute assignment is no less hidden from view than the unrecorded collateral transfer. Indeed, a competing absolute assignment poses an even greater danger to a later assignee than a competing collateral assignment inasmuch as payment of the collateralized debt ordinarily extinguishes the

105. See notes 55-56 and accompanying text.
106. See U.C.C. § 9-302 cmt. 5.
107. U.C.C. § 1-201 (37). See In re Liles and Raymond, 24 Bankr. 627, 629 (Bankr. M.D. Tenn. 1982) (stating that "[b]y definition, . . . an outright purchaser of contract rights has a security interest in the contract rights which he obtains"); Jensen, 1977 Utah L. Rev. at 333 n.18 (cited in note 74) (stating that Sections 9-102(b)(1) and 1-201(37) ensure that "any provision in the code which is applicable to the usual security interests will also be applicable to interests created by sales").
108. See, for example, United States v. Trigg, 465 F.2d 1264, 1268 (8th Cir. 1972); In re Cowthorn, 33 Bankr. 119, 120 (M.D. Tenn. 1983) (rejecting argument that "an assignment is an irrevocable transfer under Tennessee law" so that assigned account "cannot be considered property of the debtor's estate"); Cripps, 31 Bankr. at 544 (rejecting argument that absolute assignee of accounts defeats later lien creditor because of title passage, and stating that "[t]itle, for purposes of defining rights of parties, is of little relative consequence under the U.C.C."); Nevada Rock & Sand Co. v. United States, 376 F. Supp. 161, 172 (D. Nev. 1974); In re Uvesco, Inc., 13 U.C.C. Rep. Serv. (Callaghan) 957, 958 (S.D. Fla. 1973) (noting, and rejecting, assignee's claim to priority over bankruptcy trustee on ground "that there was an actual transfer or conveyance of a portion of the commission and that title passed"); City of Vermillion v. Stan Houston Equipment Co., 341 F. Supp. 707, 711 (D. S.D. 1972) (rejecting argument that "from the date of the assignment the Contractor had no property interest upon which the I.R.S. could attach a lien"). See generally Clark, The Law of Secured Transactions ¶ 3.08[1][c] at 3-86 (cited in note 9) (noting that "[t]he first-to-file-or-perfect rule also governs priorities between an assignee of accounts receivable and a factor"); U.C.C. § 9-102 cmt. 2 (stating that account buyer "is treated as a secured party, and his interest as a security interest"). But compare Coogan, et al., Secured Transactions ¶ 3.08[1][a] at 3-45 (cited in note 8) (suggesting that "a true sale of the accounts will move the assets out of the 'property of the estate' of the seller and beyond the reach of the seller's trustee in bankruptcy").
109. See note 73 and accompanying text.
110. See note 74 and accompanying text.
competing collateral assignment. For all these reasons, there can be no doubt about Case A. Second Assignee Bank wins under the first-to-file rule of Section 9-312.

We start, then, with a general rule governing successive-assignment priorities: The first assignee to file wins. Having identified this general rule, we turn to its many exceptions.

B. The Section 9-302(1)(e) Nonsignificant-Part Exception

The Code itself establishes the first exception to the first-to-file principle. That exception arises out of Section 9-302(1)(e), and its application is illustrated by Case B:

CASE B. On Day 1, Adele Accountdebtor buys Horatio the Hog from Arthur Assignor for $450 with payment due on Day 5. At that time, Arthur has twenty hog-sale accounts. On Day 2, Arthur sells this single right to payment from Adele to a neighbor, Alfee Assignee I. On Day 3, Arthur sells the same account to Artee Assignee II, another neighbor, who files a U.C.C. financing statement later that day. Both Assignee I and Assignee II, who have never taken an

111. See generally Gilmore, Security Interests in Personal Property § 7.12 at 249 (cited in note 2) (stating that “[a] borrower’s other creditors are entitled to know what his true situation is; a requirement of public notice for perfection of security interests seems to be a wise accompaniment to the recognition of the effectiveness of security transfers of contract rights, particularly of those to arise in the future”).

112. See George W. Ulrich Lumber Co. v. Hall Plastering, Inc., 477 F. Supp. 1060, 1065 (W.D. Mo. 1979) (holding that “whether the transaction was an assignment of the contract right as collateral for the loan or whether the contract right was sold will not affect the priority of those claims”). As one commentator has stated, Thus the Code is drafted carefully so as to point out that both forms of accounts receivable financing (sale or loan) are within Article 9. But once it is decided that a transaction of this nature is in Article 9, the Code makes no attempt to distinguish between these two forms of accounts receivable financing. Rather the sections of Article 9 are, with one exception, applied equally to both forms[,] the sale of accounts being treated the same as the assignment of accounts to secure a loan.

Michael R. Ford, Note, Commercial Transactions: Is a Transfer of Accounts to Satisfy Pre-existing Debt an Article 9 Transaction?, 22 Okla. L. Rev. 423, 424 (1969). See also Clark, The Law of Secured Transactions ¶ 10.04[2] at 10-43 (stating that “[f]rom the Article 9 viewpoint, the most important concern for the factor is not to forget to file the financing statement”); U.C.C. § 9-301 cmt. 4 (indicating that priorities for secured parties not dealt with in Section 9-301 “are covered in Section 9-312”).

account assignment before, demand payment from Accountdebtor on Day 5. Who brings home the bacon, Assignee I or Assignee II?

If the first-to-file rule applies to this case, Assignee II prevails because Assignee I has not filed at all. The first-to-file rule, however, does not control Case B because of Section 9-302(1)(e). That section provides that a financing statement need not be filed to perfect “an assignment of 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.” Did Assignor transfer a significant part of his accounts to Assignee I? Surely not. It follows that Assignee I’s security interest was automatically perfected upon its attachment. Because Section 9-312 dictates that “security interests rank according to priority in time of filing or perfection,” Assignee I, whose security interest was perfected when it attached on Day 2, defeats Assignee II, whose interest was obtained and perfected thereafter.

1. Some Background on Section 9-302(1)(e)

Three basic points about Section 9-302(1)(e) should be made up front. First, the courts have left no doubt that the burden of proving the applicability of Section 9-302(1)(e) is on the nonfiling claimant who seeks the shelter of that provision. Only one decision looks the other

114. Subsection (1)(g) of Section 9-302 exempts from the filing requirement assignments of accounts for the benefit of creditors. The theory behind this exemption is that such transfers are not financing transactions. U.C.C. § 9-302 cmt. 5. Regardless of filing, such assignments are unlikely to go unnoticed by most would-be subsequent account transferees who investigate the assignor and its business. If the reported cases are any guide, Section 9-302(1)(g) presents neither account claimants nor the courts with any serious difficulties.

115. See, for example, notes 149 and 159 and accompanying text.

116. See, for example, White & Summers, Uniform Commercial Code § 22-7 at 991 (cited in note 8).

117. U.C.C. § 9-312(5)(a) (emphasis added). See notes 86-87 and accompanying text.


way, and that case (not surprisingly, as we shall see) involved a nonprofessional account assignee.\textsuperscript{120}

Second, the prevailing view is that Section 9-302(1)(e) provides for automatic perfection of both absolute and collateral assignments.\textsuperscript{121} The section’s applicability to collateral assignments may seem odd in light of a statutory purpose to perfect “casual or isolated assignments” that “no one would think of filing.”\textsuperscript{122} After all, under a statutory scheme that requires filing to perfect almost all collateral transfers, it seems strange to say that “no one would think of filing” with regard to a collateral transfer of an account. One could write a long footnote in a law review article about why the Code drafters might have applied Section 9-302(1)(e) to collateral assignments.\textsuperscript{123} The key point, however, is that the section’s language is clear as a bell.\textsuperscript{124}

Third, some courts have advocated reading a clear and precise standard into Section 9-302(1)(e) so that transferees can readily determine upon receiving the assignment whether or not they need to file in light of the exemption.\textsuperscript{125} That approach is not proper, however, because the purpose of Section 9-302(1)(e) is to safeguard “assignments holds a properly perfected security interest in collateral and what it alleges are its proceeds has the burden of proof on that issue”). For cases placing a similar burden on secured creditors who assert a right to proceeds under Section 9-306(4), see In re Gibson Products of Arizona, 543 F.2d 652, 657 (9th Cir. 1976); In re Conklin’s, Inc., 14 Bankr. 318, 330 (Bankr. S.C. 1981); In re Guaranteed Muffler Supply Co., 1 Bankr. 324, 330 (Bankr. N.D. Ga. 1979).


121. See, for example, In re Crabtree Constr. Co., 87 Bankr. 212, 213 (Bankr. S.D. Fla. 1988) (stating that “[t]he debtor’s argument that the form of the document created a security interest and not an absolute assignment does not preclude the applicability of the statutory exception”); In re Fort Dodge Roofing Co., 50 Bankr. 666, 669-70 (Bankr. N.D. Iowa 1985) (implying that although the specific assignment was not an absolute transfer, such a transfer could fall within the Section 9-302(1)(e) exception).

122. U.C.C. § 9-302 cmt. 5.

123. For example, the drafters of the Code may have found the line between security and absolute transfers as likely to be blurred in applying Section 9-302(1)(e) as in applying other sections of the Code. See note 73 and accompanying text. The drafters may have reasoned that, because most insignificant-part account transfers would be insignificant, the cost of filing even for security transfers would not be justified. Finally, the drafters may have concluded that any estate-preservation purpose of Section 9-302(1)(e), see note 135 and accompanying text, applied no less to security transfers than to absolute ones.

124. The key interpretive question is whether the term “assignment,” as used in Section 9-302(1)(e), includes both collateral and absolute assignments. Common usage leaves no doubt that the answer to this question is yes. If any doubt exists about this issue, however, it is removed by other Code sections and Comments, which make it clear that the term “assignment” applies to both types of account transfers. See, for example, U.C.C. § 9-102(2) (noting that security interests may be created by “assignment”) and cmt.2 (discussing “assignments of accounts . . . as security for an obligation”).

125. For example, In re Boughner, 8 U.C.C. Rep. Serv. (Callaghan) 144, 150 (Bankr. W.D. Mich. 1970) (advocating interpretation of (1)(e) “making it possible for secured parties and attorneys to determine with reasonable certainty whether an assignment must be filed to perfect”).
which no one would think of filing." Persons who would not think of filing do not need a clear rule to tell them whether or not to file.

2. The Purposes Underlying the Nonsignificant-Part Standard

So how do courts decide whether a particular assignment involves a significant part of the assignor's accounts? This question is difficult to answer, largely because mystery surrounds the Code drafters' selection of the significant-part standard. In promulgating U.C.C. § 9-302(1)(e), the drafters sought to protect the "casual or isolated assignment." How the drafters thought the "significant part" rubric would serve to achieve that goal, however, is unclear. Perhaps they anticipated that this standard would provide a workable rule of thumb for distinguishing assignments to sophisticated assignees designed to generate working capital (for which filing ought to be required) from assignments to "little persons" who happened to get involved in assignment transactions without reason to know of technical filing rules (for which filing ought not be required).

If the drafters intended such a rule-of-thumb approach, however, they picked a peculiar rule. The most unsophisticated account transferee, after all, may well take a limited one-shot assignment that involves all or most of a small-time assignor's contractual rights to payment. Conversely, the highly sophisticated transferee sometimes will take an assignment of a large account that constitutes only a small fraction of a major corporate assignor's receivables portfolio. For these reasons, one cannot readily explain the significant-part standard as a rule of thumb designed to distinguish formal and recurring assign-

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126. See notes 77-80 and accompanying text.
127. See White and Summers, Uniform Commercial Code § 22-10 at 1003 (cited in note 8) (stating that "certainty in planning should have little relevance in construing this provision").
128. See, for example, Boughner, 8 U.C.C. Rep. Serv. at 150 (stating that "[i]n spite of the general clarity of the UCC and its great improvement over former statutes, I find subsection (e) to be anything but pellucid.").
129. See note 155 and accompanying text.
130. See, for example, Jensen, 1977 Utah L. Rev. at 342 (cited in note 74). The commentator says that consideration of this issue requires juxtaposing statutory language and the drafters' stated intent. Id. The comments state fairly clearly that Section 9-302(1)(e)’s purpose is "to protect an assignee that does not regularly take assignments. This purpose seems to have little relation to the criterion of whether the assignment was of an insignificant portion of the assignor's total accounts.". Id.
131. See notes 77-80 and accompanying text. In keeping with this theory, commercial factors and account financers may often have continuing, or at least substantial, arrangements with the assignor. Assignments to such ongoing financers thus would normally concern "alone or in conjunction with other assignments to the same assignee ... a significant part of the outstanding accounts of the assignor." U.C.C. § 9-302(1)(e).
132. See, for example, Architectural Woods, 552 P.2d at 248-49.
133. See, for example, In re Bindl, 13 Bankr. 148, 149 (Bankr. W.D. Wis. 1981).
ments from casual or isolated ones.

Another possible explanation for the significant-part litmus is that the drafters sought to achieve efficiency by sheltering trivial account transfers from the filing requirement. From this perspective, the purpose of Section 9-302(1)(e) is similar to that of Section 9-302(1)(d), which automatically—and thus cost-effectively—perfects purchase money security interests in consumer goods, which are usually small-ticket items. The “not a significant part” standard, however, seems an ill-fitting formula for pursuing this objective. If the drafters had meant to perfect automatically only account transfers that are negligible or small in the absolute sense, they could have done so in so many words. They would not have chosen the explicitly relative standard suggested by the term “significant part.”

A more plausible explanation for the drafters’ choice of this legal rubric may be that the drafters of Section 9-302(1)(e) sought to protect the nonfiling assignee only if doing so would not unduly bleed the assignor’s estate. On this view, the drafters wrote the section to ensure that the bulk of any assignor’s intangible property remained subject to claims of general creditors and later account transferees unless claimed by an assignee who had provided full public notice. In other words, the Code’s drafters may have decided to cut a break to assignees who understandably failed to file, but only if doing so did not encumber a significant part of the assignor’s account property to the disadvantage of other creditors.

In the end, any search for the purpose underlying the significant-part formulation faces the difficulty that the drafters seem to have given the matter less thought than they should have. Courts thus have little choice but to muddle through Section 9-302(1)(e) cases as best they can, with only limited guidance.

3. The Judicially Crafted Section 9-302(1)(e) Tests

The confusion surrounding the drafters’ choice of the significant-part standard is best evidenced by the actual application of that standard by the courts. Befuddled judges have developed no fewer than five

134. See id. at 150.
135. Compare U.C.C. § 2-201(1) (extending Statute of Frauds rule only to sales of goods at a price of $500 or more).
136. See Jensen, 1977 Utah L. Rev. at 342 (cited in note 74) (stating that “[t]he requirement that the assignment be of an insignificant part of the assignor’s accounts limits impingement on the rights of other creditors who may not have had notice of the assignment if it was not filed” and that “[i]t assures a significant part of the assignor’s accounts or contract rights will be available for satisfaction of their claims”). A case seemingly sensitive to this notion is Liles and Raymond, 24 Bankr. at 650 (citing fact that accounts assigned “represented a major portion of the debtor’s gross income” and were necessary to success of Chapter 11 reorganization).
separate tests for adjudging the applicability of Section 9-302(1)(e). Some courts use the percentage test, which focuses on the proportion of the assignor's total accounts transferred to the assignee. Other courts apply one of three separate variations of the "casual or isolated" standard, which emanates from the admonition of the Official Comment accompanying Section 9-302(1)(e). Still other courts adopt what might be called the "osterizer" approach. These tribunals seem to reject any strict version of either the percentage test or the casual-or-isolated test and throw into the analytical blender a number of considerations before declaring whether the significant-part exemption applies.

a. The Percentage Test

Under the percentage test, the court determines what percentage of the assignor's accounts the transfer represents and then declares whether that percentage is significant. Although this approach seems simple enough, its application has spawned analytical problems. First, in fixing the operative percentage of accounts transferred, some courts have focused on the volume of the assignor's accounts at the time of the litigation. This approach is wrong because it is necessarily at the time of attachment that automatic perfection either does or does not occur under Section 9-302.

137. See notes 140-53 and accompanying text.
138. See note 154 and accompanying text.
139. See notes 154-81 and accompanying text.
140. See notes 182-92 and accompanying text.
141. See generally White and Summers, Uniform Commercial Code § 22-10 at 1002 (cited in note 8).
142. See, for example, Drapery Design Center, 86 Bankr. at 124 (focusing on unpaid accounts at time of decision in making "significant part" analysis); In re Arctic Air Conditioning, Inc., 35 Bankr 107, 109 n.3 (Bankr. E.D. Tenn. 1983) (considering debtor's "receivables on the date of bankruptcy"). See also White and Summers, Uniform Commercial Code § 22-10 at 1002.
143. See, for example, B. Hollis Knight Co., 605 F.2d at 397, 400 (8th Cir. 1979) (stating that "[t]he determination of whether an assignment constitutes a significant part of the assignor's outstanding accounts must be made on the basis of the facts available at the time of the assignment"); Consolidated Film Indus. v. United States, 403 F. Supp. 1279, 1283 (D. Utah 1975) (stating that Section 9-302(1)(e) "requires reference to the amount of contract rights owned by [assignor] at the time of the assignment"), rev'd on other grounds, 547 F.2d 533 (10th Cir. 1977). Analysis is complicated in those cases in which an assignor makes a continuing assignment of accounts extending into the future, such as by giving a lender a floating lien in some subset of the assignor's accounts. See Gilmore, Security Interests in Personal Property § 19.6 at 337 (cited in note 2) (suggesting that section's applicability depends on whether "assignment, together with others which may be made to [the assignee] in the future, will . . . result in the 'transfer [of] a significant part'"). See also B. Hollis Knight Co., 605 F.2d at 401 n.2 (noting that the Code "requires a court to examine the total of all assignments to the secured party whether or not they took place in a single transaction"). In these cases, the rule most consistent with the notion of automatic perfection would focus on the dollar value of accounts held and transferred as of the date each separate account comes into existence, at which time, under U.C.C. Section 9-203, the security interest in that account.

144. See generally White and Summers, Uniform Commercial Code § 22-10 at 1002 (cited in note 8).
Second, judges have had to wrestle with how to calculate the percentage of accounts transferred by the assignor. Some courts, for example, have questioned whether they should include uncollectible accounts in computing the total amount of the debtor's outstanding accounts.\textsuperscript{144} Again, the proper approach is to focus on collectibility at the time of assignment rather than the time of litigation, for any automatic perfection would occur at the time of attachment.\textsuperscript{145} Considerations of certainty and convenience further counsel that courts should presume accounts to be collectible as of the time of assignment unless the non-Section 9-302(1)(e) claimant proves otherwise. If proof of uncollectibility is offered, however, courts should measure the total body of the assignor's accounts based on their actual discounted value.\textsuperscript{146} This approach not only comports with commercial reality, but also best conforms to the estate-preservation policy that seems to underlie, at least in part, the significant-part standard.\textsuperscript{147}

actually attaches. Such an approach would present complex and artificial computational difficulties. Courts thus are likely to analyze such cases by focusing more generally on the dollar value of accounts held and transferred over a continuing period. See, for example, \textit{Bindl}, 13 Bankr. at 150. The focus, however, should not be on the assignor's account holdings as of the time of litigation, but rather on the overall picture of the assignor's account holdings at or about the time the assignment(s) in issue took place.

Arguably, attention in all cases should focus on the account picture at the time of litigation, particularly in light of the anti-estate-bleeding justification offered above for the Section 9-302(1)(e) filing exception. See note 136 and accompanying text. However, thinking of a secured interest holder's perfected status as being in suspended animation pending future and unknowable events outside the control of the secured creditor seems too exotic. That notion, one might suppose, seemed too exotic to the drafters of the Code as well.

144. See, for example, \textit{B. Hollis Knight Co.}, 605 F. 2d at 400, 402.

145. See \textit{Crabtree Constr. Co.}, 87 Bankr. at 213 (stating that “collectibility later determined by the parties is not relevant”); \textit{In re Sun Air Int'l, Inc.}, 24 Bankr. 135, 137 (Bankr. S.D. Fla. 1982) (emphasizing lack of direct evidence of which accounts would have been considered collectible at the time of the assignment, and finding that the fact that “debtor's office manager testified and identified which accounts were actually paid, as best she could remember,” does not count in figuring what part was transferred).

146. In applying Section 9-302(1)(e), courts must recognize “qualitative differences in accounts receivable” so that accounts known to be uncollectible are not counted as part of debtor's outstanding accounts. See \textit{B. Hollis Knight Co.}, 605 F. 2d at 402 (noting that “reasoning is similar when there are significant limitations on . . . collectibility” so that courts should “discount [the] value” in determining total amount of outstanding accounts). See also \textit{Sun Air Int'l}, 24 Bankr. at 137 (suggesting willingness to take this approach although bankruptcy trustee “cites no authority for that interpretation”).

147. See note 136 and accompanying text. The cases have presented other interesting percentage calculation issues. For example, in \textit{In re Tri-County Materials, Inc.}, 114 Bankr. 160 (C.D. Ill. 1990) Tri-County made a contract with Ladd to supply Ladd with sand and gravel for payments amounting to some $250,000. 114 Bankr. at 161. To fulfill this contract, Tri-County leased equipment from KMB and assigned to the lessor, KMB, partial payment rights from Ladd to secure Tri-County's own payment obligations under the lease. The assignment permitted KMB to request that the Ladd Construction Company . . . make any and all payments to [Tri-County] by including on said check payment the name of [KMB] who shall have said check negotiated and endorsed by [Tri-County] and said check shall be deposited in [KMB's] ac-
The most basic difficulty in applying the percentage test lies not in
count with [Tri-County’s] endorsement, at which time [KMB] shall issue a check to [Tri-
County] for the difference between the amount of the check issued and the rental payment
owed to [KMB].
Id. at 164-65 (quoting the Lease Agreement).
On these facts, the court concluded:

It is thus clear that the assignment was not of the entire Ladd account but only of that
portion of the account necessary to cover the balance due to KMB. At the time the parties
entered into the Agreement, the total rental amount was estimated at $30,000; the actual
figure turned out to be $30,484. The ratio of the amount assigned to the total account, even
assuming that the Ladd contract was the only account, is approximately 12%.
Id. at 165.
This way of computing the part of the assignor’s accounts that have been transferred seems
sensible because it reflects commercial reality. The assignee, in everyone’s understanding, was to
get, at most, $30,484 in value out of the assignment. In these circumstances, it would be artificial
to conclude—as the lower court had done—that the entire $250,000 account (constituting 100% of
the debtor’s accounts) had been assigned.
A.2d 230 (R.I. 1972). There, a plumbing subcontractor gave a security interest to one of its suppli-
ers, named National, in “all monies now due or which will be due as retainer” from the general
contractor. 292 A.2d at 232. The amount of the retainage, apparently at all relevant times, was
slightly over $20,000. The subcontractor previously had granted a security interest in the same
retainage account to the SBA, which held a priority position as to that collateral. Id. In giving the
benefit of the Section 9-302(1)(e) exemption to the supplier to the exclusion of a receiver repre-
senting the subcontractor’s general creditors, the court reasoned in part: “Once the S.B.A.’s secur-
ity interest in the retainage was satisfied, approximately $10,000 was available to National. Such
an amount, in our opinion, bearing in mind the purpose of [Section 9-302(1)(e)], does not consti-
tute a significant part of Elhatton’s receivables.” Id. at 234-35. Although brief, the court’s reason-
seems to be that the part of the subcontractor’s accounts transferred to National was $10,000,
rather than the full $20,000 account; thus the subcontractor transferred at most 50%, rather than
100%, of its then-outstanding accounts to National. If this was the court’s understanding, it seems
wrong; otherwise, a claimant’s ability to claim the Section 9-302(1)(e) exception would turn on the
fortuity that there existed a prior competing claim to a portion of the assigned account. It was
certainly possible at the time of the assignment that the SBA loan would be paid off, so that the
entire account collateral would become available to satisfy National’s claim. Even though the sub-
contractor had previously given the SBA a security interest in the retainage, it retained rights in
the full $20,000 retainer to transfer to other secured parties, and in fact did transfer to National
“all monies now due or which will be due as retainer.” Id. at 232 (emphasis added). Under these
circumstances it is artificial to say that the subcontractor assigned to National only $10,000 in
accounts, thus constituting only 50% of the subcontractor’s outstanding accounts. Rather, the
proper conclusion is that the subcontractor assigned to National (albeit as a partially subordinate
security interest) $20,000 in accounts, which constituted 100% of the subcontractor’s receivables.
Yet another percentage-computation problem was presented by In re Rankin, 102 Bankr. 439
(Bankr. W.D. Pa. 1989). There, the collateral assignee argued that the court should count only a
small portion of the total amount of the assigned account because the assignor also had transferred
to the creditor substantial realty collateral that would satisfy most of the debt without resort to
the account collateral. The court properly rejected this argument because “the assignment, by its
plain language, assigned all of the account. The entire account was available to the Bank in the
event its other collateral proved to be insufficient.” Id. at 442. The existence of the realty collateral
did not affect the amount of the account collateral the assignor assigned. The assignee might have
first resorted to the realty collateral or the account collateral. Even if it first resorted to the realty
collateral that collateral may have turned out to be unavailable due to any number of reasons
(including, for example, the existence of a prior competing claim to the realty or a defect in its
transfer). Therefore, the assignor did—as a practical matter as well as a conceptual mat-
computing the percentage of accounts transferred, but in determining whether this percentage rises to the level of being “significant.” Courts have provided only garbled guidance on this critical point. The safest generalization is that some courts think that sixteen percent of one’s accounts is not a significant part, although even that statement must be qualified. The reality is that the courts have failed to demarcate any clear line between the significant and nonsignificant part of a debtor’s accounts. This failure may explain why few courts, if any, have embraced a pure percentage test.

transfer all of its account to the assignee. Thus all of the account properly was taken into consideration in applying Section 9-302(1)(e).

148. See note 141 and accompanying text.

149. See, for example, Tri-County Materials, 114 Bankr. at 165 (stating that 12% “is surely on the ‘insignificant’ side”); Rankin, 102 Bankr. at 442 (stating that when debtor transfers to a bank the “only account of substance,” filing is required); Drapery Design Center, 96 Bankr. at 124 (finding that $30,039 constitutes significant part of $62,647); In re First City Mortgage Co., 69 Bankr. 765, 768 (Bankr. N.D. Tex. 1986) (stating that the transfer to a bank of a “substantial portion, if not all of the Debtor’s accounts... in conjunction with an existing debtor/creditor relationship” is not within the Section 9-302(1)(e) exemption); AM Int’l, 46 Bankr. at 571 (finding that assignment of 75% of 50%—that is, 37.5%—of assignor’s receivables is a significant part); Arctic Air Conditioning, 35 Bankr. at 109 n.3 (stating that Section 9-302(1)(e) exemption not afforded to wife of corporation’s president who loaned corporation $10,000 and received back assignment of $10,000 in contract rights, when corporation had about $15,000 in unpaid accounts on date of bankruptcy); In re Barrington, 34 Bankr. 55, 57 (Bankr. M.D. Fla. 1983) (stating that there is no “overwhelming consensus as to what figure represents a cutoff”); Liles and Raymond, 24 Bankr. at 630 (holding Section 9-302(1)(e) exemption inapplicable because “debtor assigned a substantial portion of its future contract rights in milk proceeds to FmHA”); Bindl, 13 Bankr. at 150 (refusing to find assignment of $7,159 out of $170,400 to professional assignee insignificant); In re B. Hollis Knight Co., 461 F. Supp. 1213, 1214 (E.D. Ark. 1967) (describing “25% to 50%” as “clearly a significant part of the outstanding accounts” and stating that 14% does not constitute a significant part under percentage test), rev’d on other grounds, 605 F.2d 397 (8th Cir. 1979); In re Munro Builders, Inc., 20 U.C.C. Rep. Serv. at 741-42 (finding assignment of 40% of contract rights to bank constitutes a significant part); In re Consolidated Steel Corp., 11 U.C.C. Rep. Serv. (Calleghan) 406, 411 (M.D. Fla. 1972) (holding subcontractor’s assignment of $5,838 account to supplier not a significant part of assignor’s $116,000 in then-existing payment rights); Lehigh Press, 389 S.E.2d at 379 (holding that 57% is a significant part).

150. The leading case is Standard Lumber Co. v. Chamber Frames, Inc., 317 F. Supp. 837, 840 (E.D. Ark. 1970) (holding that assignment of 16% made to supplier of goods was not a significant part). See also Tri-County Materials, 114 Bankr. at 165 (finding that 12% was “insignificant”); Crabtree Constr. Co., 87 Bankr. at 213 (finding that 14% was not significant): Sun Air Int’l, 24 Bankr. at 137 (same); B. Hollis Knight Co., 461 F. Supp. at 1214 (same).

151. For example, in Bindl the court explicitly refused to find 16% “the bottom limit of a significant part.” 13 Bankr. at 150. In B. Hollis Knight Co., the Eighth Circuit explained that Standard Lumber was “not inconsistent with” the Eighth Circuit’s own decision not to apply the Section 9-302(1)(e) filing to an account transfer constituting 14% of the assignor’s accounts. 605 F.2d at 401. The court observed: “In Standard, the secured party, Standard Lumber Company, did not regularly take assignments from its suppliers. There was no question that the assignment was an isolated one and, thus, there was no reason for the District Court to consider the issue.” Id. See also note 164 and accompanying text (noting focus of some courts on absolute value of transferred account).

152. See, for example, Architectural Woods, 562 P.2d at 249 (stating that “the percentage...
This is as it should be. If the drafters had preferred a mechanical percentage approach, they could have themselves declared that an assignment of up to ten, twenty, or thirty percent of the assignor's accounts did not require filing. By opting instead for the more pliable significant-part test, the drafters required something more. In particular, courts undertaking the significant-part inquiry should also consider the absolute value of the accounts assigned. To track the language of the Comment, one might well think of filing as to a $100,000 account even though it constitutes only ten percent of the assignor's receivables. One might well, however, not think of filing as to an assignment of a $100 account even though it constitutes twenty-five percent of the assignor's outstanding receivables.

Taking account of the absolute value of the assignment in this way meshes with the language of the Code. The $100,000 assignment involves a significant part of the assignor's accounts for the very reason that $100,000 would be seen as significant by the assignor, the assignee, and any normal human being. The same cannot be said of the $100 assignment, even though it concerns a larger percentage of the assignor's accounts. In short, a focus on the absolute value of the assigned accounts, as well as the percentage of accounts transferred, comports with both the Comment's focus on casual or isolated assignments and the provision's size-tied text. In light of these considerations, a number of courts have deemed the absolute size of the transferred account a proper consideration in determining the applicability of the filing exemption.

Particularly interesting is Professors White's and Summers's flip-flop in their position on the percentage test. In the first edition of their treatise, these commentators advocated adoption of the percentage test. White and Summers, Uniform Commercial Code § 23-9 at 808-09 (West, 1st ed. 1972). In their later editions, Professors White and Summers concluded that certainty in this field had proven to be a "will o' the wisp." As a result, they urged abandonment of the percentage test. White and Summers, Uniform Commercial Code § 22-10 at 1002-03 (cited in note 8).

153. See note 125 and accompanying text.

154. See, for example, Consolidated Film Indus., 547 F.2d at 537 (considering "the size of the transaction"); In re Hostetler, 49 Bankr. 737, 739 (Bankr. W.D. Pa. 1986) (citing absolute amount); In re Bindl, 13 Bankr. at 150 (stating: "I am not compelled by the suggestion that 16 percent represents the bottom limit of a significant part of accounts assigned. Farm Loan Service has been assigned accounts in the amount of $7,159.44; Federal Land Bank, $89,700.00; Equico, $113,758.68; and FHA, $25,000. None of those sums are on their face insignificant."); Miller, 406 F. Supp. at 477 (holding that transfer of account constituting about 20% of $4,439,300 in accounts was a significant part, "especially in view of the high absolute value of the transaction at issue"); Architectural Woods, 562 P.2d at 249 (noting that "cases may find the dollar amount to be significant without regard to the percentage"). See generally Page, 53 Wash. L. Rev. at 519 n.47 (cited in note 113); Coogan, et al., Secured Transactions § 10.53[8] at 1087; George W. Ultch Lumber Co., 477 F. Supp. at 1069.

For cases that are insensitive to this analysis, see Crabtree Constr. Co., 87 Bankr. at 213 (hold-
b. The Casual-or-Isolated-Assignment Test

Flustered by the cloudiness of the significant-part standard and the mechanical quality of the percentage test, many courts have looked to the Official Comment for guidance in applying Section 9-302(1)(e). The relevant language of the Comment states:

The purpose of the subsection (1)(e) exemption is to save from ex post facto invalidation casual or isolated assignments: some accounts receivable statutes were so broadly drafted that all assignments, whatever their character or purpose, fell within their filing provisions. Under such statutes many assignments which no one would think of filing might have been subject to invalidation. The paragraph (1)(e) exemption goes to that type of assignment. Any person who regularly takes assignments of any debtor's accounts should file.\textsuperscript{155}

Courts often have said that "the case law has developed two tests under Section 9-302(1)(e): the percentage test and the casual or isolated test."\textsuperscript{156} In fact, courts have extracted three different tests, in addition to the percentage test, out of the Comment's reference to casual or isolated transfers. Some courts apply the filing exemption if, without more, they find that the account transfer is casual or isolated.\textsuperscript{157} Others apply the exemption only if the assignment both qualifies as casual or isolated and passes the percentage test or some kindred standard.\textsuperscript{158} Filing that security assignment of 14% of assignor's accounts, worth $173,144, to secure debt of $93,000 is within Section 9-302(1)(e) filing exception;\textsuperscript{159}\textsuperscript{160}\textsuperscript{161}\textsuperscript{162} Fort Dodge Roofing Co., 50 Bankr. at 670 (applying Section 9-302(1)(e) exception to protect nonprofessional assignee, although transferred account worth $52,000, because assignment concerned only 6.2% of assignor's total receivables); In re K & G Health Care Indus., Inc., 28 U.C.C. Rep. Serv. (Callaghan) 837, 838-39 (Bankr. S.D. Fla. 1979) (finding that assignment to bank of $75,000 account by company that generated about $330,000 in accounts per month was "not significant").

\textsuperscript{155} U.C.C. § 9-302 cmt. 5.
\textsuperscript{156} B. Hollis Knight Co., 605 F.2d at 400-01 (suggesting that two tests have emerged as aids in interpreting the significant part standard: the "casual or isolated" test and the "percentage" test); Tri-County Materials, 114 Bankr. at 164. In accord, Fort Dodge Roofing Co., 50 Bankr. at 669 (stating that "courts have utilized two basic tests to determine whether filing a financing statement is necessary to perfect a security interest in accounts receivable"); Consolidated Film Indus., 403 F. Supp. at 1283 (stating that "[t]here have been two differing approaches or tests utilized by courts under § 9-302(1)(e)"").

\textsuperscript{157} Padgett, 49 Bankr. at 215; In re Himlie Properties, Inc., 36 Bankr. 32, 34 n.5 (Bankr. W.D. Wash. 1983); Barrington, 34 Bankr. at 57; Architectural Woods, 562 P.2d at 250; Sherburne Corp. v. Carter, 340 A.2d 82, 85-86 (Vt. 1975); Abramson, 440 S.W.2d at 328-29.

\textsuperscript{158} B. Hollis Knight Co., 605 F.2d at 401 (concluding that Section 9-302(1)(e) requires application of both percentage and "casual and isolated" tests). The court in Tri-County Materials found support for requiring both tests to be met in the language of the Code and its comments:

The totality of circumstances surrounding the transaction determines whether an assignment was casual or isolated. . .

\textsuperscript{\ldots} The statutory language specifically requires that the assignment be an insignificant part of the outstanding account. . . A showing of a casual or isolated assignment of a significant part of outstanding accounts would not be entitled to the exemption given this clear statutory requirement. . . [G]iven the comments to the UCC regarding the purpose of this exemption, in a case involving the transfer of an insignificant part of outstanding accounts to a
Finally, one court has declared that the filing exemption applies if either the percentage test or the casual-or-isolated test is met.\textsuperscript{159}

All three variations on the casual-or-isolated theme require identification of the earmarks of the casual or isolated transfer. Courts adopting the casual-or-isolated standard uniformly have agreed that the professional character of the account assignee and the regularity with which the assignee receives account assignments are the guiding criteria for applying the Section 9-302(1)(e) filing exemption.\textsuperscript{160} Beyond this, however, there is much disagreement. Many courts, for example, have taken the position that the assignee’s status as a commercial financing institution \textit{ipso facto} disqualifies it from receiving a casual or isolated assignment.\textsuperscript{161} Other courts have taken a different stance. Some of these

\textsuperscript{159} Wood, 67 Bankr. at 323 (stating that “[t]his Court supports the position of the Bankruptcy Court which utilized both the percentage test and the casual and isolated transaction test in applying U.C.C. Section 9-302(1)(e). However, the assignee need only satisfy one test to fall within the exemption from filing.”). As indicated above, the foundation of all these variations of the casual-or-isolated test lies in the Comment to Section 9-302(1)(e). Some courts, however, have sought to bolster the case for applying the casual-or-isolated test—and in particular to do so to the exclusion of the percentage test—with additional policy arguments. In Barrington, the court advocated adoption of the casual-or-isolated test in part because, under it, commercial lenders “cannot avoid filing respecting a substantial security interest by extending the payment schedule, causing monthly payments to fall below the point of ‘significance.’” 34 Bankr. at 58. To believe that banks would manipulate loan transactions in this manner simply to avoid the easy and certain step of filing a U.C.C. financing statement is speculative and, indeed, farfetched. A number of courts have argued that the casual-or-isolated test will create greater certainty for creditors and courts than the competing percentage test. See, for example, id. at 67 (stating that the casual-or-isolated test provides “greater certainty”). The casual-or-isolated test, however, creates enough of its own problems that certainty in its application is not a persuasive reason for its adoption. See, for example, Sun Bank, 466 So. 2d at 1093 (stating that the casual-or-isolated test does not seem any more certain than the percentage test); Page, 53 Wash. L. Rev. at 517 (cited in note 113); Jensen, 1977 Utah L. Rev. at 344 (cited in note 74) (stating that “[t]his test excludes from the filing exemption, banks or professional lenders, regardless how small the assigned account”); George W. Ulch Lumber Co., 477 F. Supp. at 1069 (barring bank from claiming Section 9-302(1)(e) exemption because of its involvement in commercial financing, and stating “whether Bank regularly takes assignments of contract rights, as distinguished from other collateral security, is not decisive”). See also Tri-County Materials, 114 Bankr. at 164 (stating that “[t]he totality of circumstances . . . determines whether an assignment was casual or isolated,” but also stating flatly that “a creditor whose regular business is financing . . .
courts have indicated that an assignment to a bank may qualify as casual or isolated if the bank shows it has not taken other account assignments in the past. Other courts have signaled that, while a financial institution that takes a security assignment always must file, the Section 9-302(1)(e) exclusion might remain available for an outright account purchase.

Tracking the Code Comment, most courts have found that assignments—whether to financial institutions or to others—fail to meet the casual-or-isolated description as long as the assignee regularly takes account assignments. Again, however, some courts deem this factor dis-

should not fall within [the] exemption); Consolidated Film Indus., 403 F. Supp. at 1285 (finding it important that assignee “was not a regular commercial financer”); H. & Val J. Rothschild, Inc., 242 N.W.2d at 847 (citing as critical that “Rothschild [the assignee] has extensive experience in commercial finance”).

162. See, for example, B. Hollis Knight Co., 605 F.2d at 402; Valley Bank of Nev., 528 F. Supp. at 914; In re First Gen. Contractors, Inc., 12 U.C.C. Rep. Serv. 782, 783 (S.D. Fla. 1971) (suggesting that Code filing requirement does not apply even to commercial financing transactions so long as the lender is “not following a regular practice of financing accounts”). Assuming the appropriateness of the casual-or-isolated test, the distinction between banks that do and do not regularly take assignments of accounts receivable is strained and should be rejected. The reason is that the test seeks, in the end, to protect “assignments which no one would think of filing.” This description simply does not fit a bank that takes a security interest in an account. That is true regardless of whether or not the bank regularly takes account assignments. The inappropriateness of the assignment-taking-bank/non-assignment-taking-bank distinction is well illustrated by the leading case supporting this distinction, B. Hollis Knight Co. In that case, the court remanded for a finding on whether the particular bank-assignee regularly took account assignments, 605 F.2d at 402-03. Whether the bank did or not, however, the bank clearly was not the type of transferee that deserved the protection afforded transferees of accounts no one would think of filing. The bank in fact had filed a U.C.C. financing statement in an effort to perfect its interest in the transferred account. The bank sought to fall back on the Section 9-302(1)(e) exception only because it erred in completing the U.C.C. form, and thus had not properly filed. Id. at 399.

163. See Valley Bank of Nev., 528 F. Supp. at 914 (stating that “[t]his section is applicable only when an outright sale of an account occurs, or the security interest is granted to an assignee who is not regularly engaged in financing activities”); K.A.O.P. Co., 372 N.W.2d at 777 (questioning “whether the filing exemption in [Section 9-302(1)(e)] applies to the bank absent an outright assignment of [the assignor’s] right to the fees.”).

164. See U.C.C. § 9-302 cmt. 5. For examples of cases so holding, see B. Hollis Knight Co., 605 F.2d at 401 (suggesting that the rationale of the casual-or-isolated test is to “require a secured creditor to file if he regularly takes assignments of a debtor’s accounts, but [not to require filing] if this was not a usual practice”); Tri-County Materials, 114 Bankr. at 165 (stating that it is important that the assignee “was not in the business of accepting contract assignments,” among other factors); Wood, 67 Bankr. at 324 (stating that “the authorities are clear that where the assignee is regularly engaged in commercial financing and routinely accepts assignments of accounts, perfection by way of filing under the U.C.C. is required regardless of the actual amount of the accounts assigned”); Padgett, 49 Bankr. at 215 (stating that “[t]he Comment . . . advises that ‘[a]ny person who regularly takes assignments of any debtor’s accounts should file.’ . . . In this case, [assignee] took a series of assignments over a period of time, not just an isolated one. Therefore, the Court finds that [assignee] is an unperfected party as it did not file. . . .”); Fort Dodge Roofing Co., 50 Bankr. at 670 (granting assignee-supplier that had only once before accepted an assignment of accounts protection under Section 9-302(1)(e)); Barrington, 34 Bankr. at 57 (quoting Section 9-302 cmt. 5); K.A.O.P. Co., 372 N.W.2d at 777 (stating that the “exemption . . . is applicable ‘only when
positive, while others call it a significant consideration. All these cases, however, draw a fundamental distinction between what might be described as “professional” and “nonprofessional” account assignees. As a practical matter, only the nonprofessional may claim to have received a casual or isolated assignment. A similar claim by a bank or other professional financier is almost certainly destined to fail.

... assignee ... is not regularly engaged in financing activities’); George W. Ultech Lumber Co., 477 F. Supp. at 1067-8 & n.7 (noting that “Gilmore ... emphasized regularity” and finding this “the principal factor in determining whether to apply the exemption”); Abramson, 340 S.W.2d at 329 (finding Section 9-302(1)(e) exemption satisfied, without any reference to percentage of accounts sold, because discount sale of $8,331.73 in accounts to bindery company was casual or isolated and “there is no evidence that Bindery [the assignee] ‘regularly takes assignments of any debtor’s account,’ to quote the language used in the commentary”).

Courts that emphasize the regularity factor rely on the Comment’s admonition: “Any person who regularly takes assignments of any debtor’s accounts should file.” U.C.C. § 9-302(1)(e) cmt. 5. The assumption seems to be that the sentence’s reference to “any debtor” means any debtor in the world, so that regular past account transactions with anyone necessarily removes the assignee from under the protective casual-or-isolated umbrella. Another possible reading of the Comment, however, is that the reference to “any debtor” denotes any particular debtor, so that filing is advisable by assignees who have taken past assignments of the particular assignor’s accounts. After all, those assignees might expect to be receiving “a significant part of the outstanding accounts of the assignor.” U.C.C. § 9-302(1)(e) (emphasis added).

165. See, for example, M.D. Hodges Enters., 256 S.E.2d at 352 (stating that Section 9-302(1)(e) “indicates that the exception from filing for the isolated or casual assignment of accounts is not available to ‘any person who regularly takes assignments of any debtor’s accounts,’” and that “[a] bank which regularly loans money and accepts accounts as security must file”). See also the cases collected in note 173.

166. See Architectural Woods, 562 P.2d at 250 (stating that the fact that the “[p]rintiff was a wholesaler of wood products [and] ... was not in the business of commercial financing or obtaining assignments. ... [w]as a significant factor in determining the casual and isolated nature of the assignment”). See also B. Hollis Knight Co., 605 F.2d at 401 (finding that the casual-or-isolated test “requires a court to examine the circumstances surrounding the transaction, including the status of the assignee”); City of Vermillion, 341 F. Supp. at 712.

167. See, for example, Drapery Design Center, 86 Bankr. at 124 (emphasizing that the Credit Union was a financial institution); Fort Dodge Roofing Co., 50 Bankr. at 669-70 (illustrating broad application of Section 9-302(1)(e) to protect non-financial institution); Brent Explorations, 31 Bankr. at 748 (stating that “the legislative history, as revealed by the official comments indicates an intent to protect an insignificant and ignorant assignee”); K.A.O.P. Co., 372 N.W.2d at 778 (stating that “the bank took this pledge of collateral in the ordinary course of financing”); Page, 53 Wash. L. Rev. at 514 (cited in note 113) (stating that “[t]he casual and isolated test relies on an examination of the circumstances surrounding the assignment and on the assignee’s financing experience. An isolated assignment, made to a nonprofessional buyer of accounts, is exempt from the filing requirements under this third test.”).

168. Apparently only three reported cases exist in which a financial institution successfully invoked the Section 9-302(1)(e) automatic-perfection rule: K & G Health Care Indus., 28 U.C.C. Rep. Serv. at 839-40; In re Hostetler, 49 Bankr. at 739; and Effective Commun. West, Inc. v. Board of Cooperative Educ. Servs., 446 N.Y.S.2d 684 (N.Y. App. Div. 1981). The K & G Health Care court, for example, found that the assignment to the bank “was an isolated transaction, the subject assignment and accompanying note and security agreement being Barnett Bank’s only loan transaction with K & G during the period of time in question.” 28 U.C.C. Rep. Serv. at 839. Of course, questions may arise as to whether a particular assignee qualifies as a professional. See, for example, Wood, 67 Bankr. at 324 (stating that “[t]his Court is unable to find any authority which
At least if one accepts the basic soundness of the Code filing system, judicial focus on the professional character of the account assignee in applying Section 9-302(1)(e) comports with sound policy. Financial institutions that regularly take account assignments should file U.C.C. financing statements. Those statements provide useful information that may avoid wasteful, and even catastrophic, reliance by third parties.\footnote{169} Filing by financial institutions, moreover, produces few transaction costs because their employees know of the U.C.C. filing system and routinely use it.\footnote{170} Indeed, several institutions will find it cost-effective to file as to all account transfers, rather than to make case-specific and uncertain determinations whether particular transfers involve a significant part of a debtor's accounts.\footnote{171} Put another way, when a financial institution seeks to use the Section 9-302(1)(e) exemption, it is simply seeking relief from its own mistake.\footnote{172} Courts should hardly encourage filing errors, however, and this is especially true with financial institutions that profit greatly through their own use of the U.C.C. filing system.\footnote{173} In sum, the judge-made distinction between professional and nonprofessional claimants of the Section 9-302(1)(e) exemption makes good economic sense.

The central goal of interpreting statutes, however, is not to make good economic sense. Rather it is to give a fair and proper meaning to the language of the statute.\footnote{174} This is not to say that economic considerations are unimportant in construing the Code. In fact, because the

characterizes attorneys as a group which are ineligible to engage in casual and isolated assignments of accounts under U.C.C. 9-302(1)(e)\footnote{169}. See generally Special Project, 62 Cornell L. Rev. at 839 (cited in note 12).

\footnote{170} See Clark, The Law of Secured Transactions § 1.04 at 1-26 (cited in note 8) (stating that “[i]t is a simple matter for the assignee to file a financing statement and thus warn the world”); Douglas G. Baird and Thomas H. Jackson, Possession and Ownership: An Examination of the Scope of Article 9, 35 Stan. L. Rev. 175, 186 (1983) (noting that “[t]he cost of making an Article 9 filing is quite small”).

\footnote{171} See Gilmore, Security Interests in Personal Property § 19.6 at 538 (cited in note 2) (stating that “[a]ll right-minded assignees will . . . file”).

\footnote{172} See id. Gilmore notes that Section 9-302(1)(e) “is carefully drafted so that no assignee, engaged in a regular course of financing, will ever be tempted to rely on it in order to avoid a filing which ought to be made.” Id. For examples of cases in which the professional assignee specifically undertook to file a proper financing statement, but then failed to do so, see K.A.O.P. Co., 372 N.W.2d at 775 (noting that “[a]lthough Midway National Bank [assignee] prepared a financing statement, neither the bank nor Engelston [another assignee] ever filed a financing statement with the Secretary of State's office”); City of Vermillion, 341 F. Supp. at 709, 712. See also note 162 (discussing B. Hollis Knight).

\footnote{173} See K.A.O.P. Co., 372 N.W.2d at 777 (stating that “[t]his exemption was 'never intended to provide an escape hatch for negligent institutional financiers'”) (quoting Valley Bank, 528 F. Supp. at 914); Sun Bank, 466 So. 2d at 1092 (inquiring whether “assignee was sufficiently removed from commercial financing circles as to be excused from being unaware of any necessity to file”).

\footnote{174} See generally notes 572-73 and accompanying text.
Code is a commercial statute designed to govern practical business arrangements, we may assume that the Code's drafters preferred commercially sensible results.\textsuperscript{176} In construing the Code, however, this interpretive norm cannot take primacy over clear statutory text. Consider, in this vein, the following variation on Case B:

**Case C.** All the facts of Case B remain the same except that, on Day 2, Arthur Assignor transfers the single $450 Horatio the Hog account to the First Assignee Bank, rather than Alfee Assignee I, the neighboring farmer. Now who takes priority: First Assignee Bank or the second assignee and first filer, Artee Assignee II?

Given our discussion of Case B, any normal English-speaking person would answer this question in favor of the Bank. The inquiry mandated by Section 9-302(1)(e) is whether the assignment involves a significant part of the assignor's accounts. If a $450 account, constituting five percent of Arthur Assignor's receivables, is not a significant part of his accounts when transferred to Assignee I, how can it be a significant part of his accounts simply because it is transferred to someone else? To say that whether an assignment involves a significant part of the outstanding accounts of the assignor depends on the identity of the assignee makes no sense. Either an account is a significant part of the assignor's accounts or it isn't, and that should be true whether the assignee is First Assignee Bank, Dagwood Bumstead, or the Man in the Moon.

To be sure, courts should give Code provisions a purposive interpretation that is sensitive to the Code Comments.\textsuperscript{176} The Code Comments, however, “do not approach the weight of legislation; if the statutory provisions adopted by the legislature contradict or fail to support the Comments, the Comments must be rejected.”\textsuperscript{177}

Does the critical professional-nonprofessional distinction distilled

\textsuperscript{175} The distinctive difficulty of amending the Code, because of its uniform character, may justify greater judicial tinkering than might he applied to other statutes in order to avert demonstrably bad results.

\textsuperscript{176} See note 579 and accompanying text.

\textsuperscript{177} Robert H. Skilton, Some Comments on the Comments to the Uniform Commercial Code, 1966 Wis. L. Rev. 597, 604. (quoting John Honnold, Cases and Materials on the Law of Sales and Sales Financing at 19 (2d ed. 1962). Such broad pronouncements about the relationship between Code text and Code Comments have tended to oversimplify matters—especially in a time when the Permanent Editorial Board is constantly revising the Comments “on the run,” in much the same manner that an administrative agency makes shifting policy decisions through the promulgation of rules pursuant to delegated authority. The Permanent Editorial Board, however, is not an administrative agency. Moreover, even administrative agencies can only promulgate rules that comport with statutory mandates. The Comments cannot and do not permit courts to do whatever they wish in interpreting the Code. The text of the Code continues to impose important limits.
by courts from the Comment’s reference to casual or isolated transfers depart too much from the statutory text? An affirmative answer to this question finds strong support in the preceding discussion of how the normal English-speaking person would read Section 9-302(1)(e). The same conclusion draws support from two additional considerations.

First, if one takes the casual-or-isolated test to its logical stopping point, the Section 9-302(1)(e) filing exemption applies even when an assignor makes a small and single transfer to a nonprofessional assignee of the only accounts it ever has had. It shatters the eardrum, however, to hear that an assignment does not involve a significant part of a debtor’s outstanding accounts when in fact it transfers all the debtor’s receivables. The Comments are helpful aids, but not when used to tear up the statutory text; and this reading of Section 9-302(1)(e) rips the word “part” right out of Code.

Second, there exists strong evidence that courts that have read the professional-nonprofessional distinction into Section 9-302(1)(e) have pushed the Code’s text beyond the breaking point. In particular, at least three courts have applied the casual-and-isolated test to excuse

178. See text following note 174. This analysis gains support from Professor McDonnell, who long has championed purposive interpretation of the Code. See note 579. In his commentary on the subject, Professor McDonnell finds a contradiction between the text of Section 9-302(1)(e) and the Comment to it. Coogan, et al., Secured Transactions § 3.08[5][b] at 3-63 (cited in note 8) (chapter by Professor McDonnell; compare note 166). He goes on to note that “courts have manipulated [the section] . . . to protect unsophisticated, non-merchant financers.” Id. § 3.08[5][a] at 3-62 (emphasis added).

179. See Architectural Woods, 562 P.2d at 248-50 (applying casual-or-isolated standard to find Section 9-302(1)(e) satisfied although wood-supplier assignee received $144,953 in accounts and there was no indication that the assignor had any other accounts when assignments were made); E. Turgeon Constr. Co., 292 A.2d at 234-35 (holding that $10,000 assignment was not a significant part, but failed to engage in inquiry whether assignor had additional receivables).

180. See Page, 53 Wash. L. Rev. at 522 (cited in note 113) (describing this outcome as “startling”). A number of courts have thus rejected this result. See, for example, B. Hollis Knight Co., 605 F.2d at 401 (stating that “[t]he language of the section would not permit an assignee to escape the filing requirement if he received a large proportion of an assignor’s accounts whether or not the transaction was an isolated one”); Consolidated Film Indus., 547 F.2d at 537 (stating that “we have to conclude that from all appearances this [account] constituted most if not all of the accounts or rights of the assignor. If that is true, and there is no evidence from appellee to the contrary, it would make no difference that it may be an isolated transaction.”); Uvesco, 13 U.C.C. Rep. Serv. at 959 (suggesting that if debtor were transferring its “only contract right,” that would amount to a “significant part of the debtor’s outstanding contract rights”). Of course any interpretation of Section 9-302(1)(e) based on the estate-preservation purpose also would preclude such extreme applications of the casual-or-isolated test. See note 136 and accompanying text.

181. Courts have found that Comment-based interpretations in other settings push Code text too far. See, for example, In re Bel Air Carpets, Inc., 452 F.2d 1210, 1212 (9th Cir. 1971) (refusing to follow the language of the Comment to U.C.C. Section 2-702(2) over the clear language of the Code itself); Frericks v. General Motors Corp., 363 A.2d 460, 464 (Md. Ct. App. 1976) (relying on the “clear language” of U.C.C. 2-607 over the contradictory language of the accompanying Comment); Wright v. Bank of Cal., 81 Cal. Rptr. 11, 14 (Cal. Ct. App. 1969) (deciding that “[t]he plain language of [Section 3-408] cannot be varied by reference to the comments”).
the filing requirement, even while expressly recognizing that the account transfer at issue involved a significant part of the assignor's accounts. These courts did not even pretend to rely on statutory purpose as an aid in interpreting the Code's text; rather, they unashamedly substituted for the statutory standard a different standard derived exclusively from the Comment.

Often there is room for debate about whether statutory language is sufficiently ambiguous in a particular respect to bear a proffered construction. This group of cases indicates, however, that courts adopting a strong professional-nonprofessional distinction under the casual-or-isolated test are ignoring the Code's text rather than interpreting it. The term "significant part," albeit ambiguous, is not so ambiguous as to support the fundamental distinction between professional and nonprofessional assignees drawn by courts applying the casual-or-isolated test. Accordingly, courts should abandon this approach.

c. The Osterizer Test

Some courts have eschewed strict versions of either the casual-or-isolated test or the percentage standard and, at least on the surface, opted for a more open-ended appraisal of the applicability of Section 9-302(1)(e). The distinctive mark of these osterizer cases is that the courts, in applying the filing exemption, mention factors in addition to the percentage of transferred accounts and the regularity with which the assignee receives account assignments. Some courts, as we have

182. See George W. Ultch Lumber Co., 477 F. Supp. at 1068 (noting that Architectural Woods and First General Contractors both applied Section 9-302(1)(e) "in spite of findings that the assignments constituted a significant part"); First Gen. Contractors, Inc., 12 U.C.C. Rep. Serv. at 763 (exempting account transfer from filing because it was "a casual and isolated transaction" even while stating explicitly that the "assignment in question did involve a 'significant part' of the outstanding accounts" of the assignor).

183. See, for example, Brent Explorations, 31 Bankr. at 748 (citing casual and isolated nature of assignment as a "factor some courts consider"); Consolidated Film Indus., 403 F. Supp. at 1285 (stating that courts should first look at "the size of the assigned contract vis-à-vis the remaining contract rights of the assignor," and if that is not dispositive, the court should consider "other relevant factors").

184. Also properly placed in this category are cases in which the court blends the critical considerations underlying both the percentage and casual-or-isolated test. An example is Drapery Design Center, in which the court reasoned:

The Credit Union stands on no better footing than does Rigdon. Its underlying course of dealing regarding the Debtor's assigned accounts was neither casual nor isolated. Its claim of $176,109.76 relates to assigned notes and accounts receivable assigned by the Debtor to satisfy six (6) loans made by the Credit Union. The Credit Union's business is that of a financial institution. Further, the aggregate amount of the assignments as stated above constitutes a significant portion of the Debtor's outstanding accounts. Its transactions with the Debtor were multiple. Therefore, the Credit Union, likewise, has failed to successfully demonstrate that it meets the filing exception. . . .

86 Bankr. at 124. See also Brent Explorations, 31 Bankr. at 747-48.
seen, cite the absolute size of the transferred account.\textsuperscript{185} Other courts have noted additional factors as well.

These factors fall into four basic categories. First, some courts have noted the degree of formality with which the account transfer was made.\textsuperscript{186} Reliance on this factor apparently reflects a sensitivity to the Comment's reference to safeguarding casual account transfers.\textsuperscript{187} Second, a few courts have noted the reality, or heightened risk, of adverse reliance on a failure to file in the particular case.\textsuperscript{188} The thought behind this approach seems to be that a stricter insistence on filing is justified when a greater danger from failing to file exists. Third, there are decisions that—with some textual justification—consider the significance, or potential significance, of the account transfer in light of considerations other than the percentage of accounts transferred and the assignment's absolute size.\textsuperscript{189} Finally, some courts explore whether a special justification exists for filing or failing to file a financing statement in the individual case.\textsuperscript{190} These courts, in declining to apply the filing exemp-

\textsuperscript{185} See note 154 and accompanying text.
\textsuperscript{186} See \textit{Tri-County Materials}, 114 Bankr. at 165 (denying assignee Section 9-302(1)(e) exemption where, among other things, assignment was accomplished by a formal written agreement and notice was given to the account debtor); \textit{K.A.O.P. Co.}, 372 N.W.2d at 777 (noting the use of standard U.C.C. forms in effecting the transfer and finding Section 9-302(1)(e) inapplicable). Contrast \textit{Wood}, 67 Bankr. at 324 (finding Section 9-302(1)(e) protection appropriate where the transaction was between two individuals with a personal relationship).
\textsuperscript{187} See note 154 and accompanying text.
\textsuperscript{188} See, for example, \textit{Bindl}, 13 Bankr. at 150 (including in list of reasons why exemption did not apply the common presence of subsequent transferees of milk proceeds checks with consequent risk of adverse reliance unless filing is required). Contrast \textit{K.A.O.P. Co.}, 372 N.W.2d at 778 (granting a second assignee priority even though it “may have originally believed that another party had priority” because of the importance of policy behind filing requirement).
\textsuperscript{189} \textit{AM Int'l}, 46 Bankr. at 871 (finding Section 9-302(1)(e) inapplicable in part because transfer of accounts as part of “financing the purchases of AMI equipment was essential to TDS’ operations”); \textit{Brent Explorations}, 31 Bankr. at 747 (citing assignor’s inability to pay its bills due to the assignment as one factor that cuts in favor of filing); \textit{Bindl}, 13 Bankr. at 150 (stating that “[t]he multiplicity of assignees and the continuing nature of the assignments augur for the completeness of notice”); \textit{K.A.O.P. Co.}, 372 N.W.2d at 777 (looking to the unliquidated nature of the transferred account in denying Section 9-302(1)(e) protection because of corresponding inability to compare it with all other outstanding accounts). Contrast \textit{Hostetter}, 49 Bankr. at 739 (granting Section 9-302(1)(e) protection because the assignments in question constituted only a small portion of the assignor’s obligation to the assignee); \textit{K & G Health Care Indus.}, 28 U.C.C. Rep. Serv. at 839 (finding the security interest perfected without filing because “the subject assignment and accompanying note and security agreement [was the assignee’s] only loan transaction with [assignor]”).
\textsuperscript{190} See \textit{Brent Explorations}, 31 Bankr. at 748 (stating that assignee “knew it should have recorded the assignment” because it was “a large supplier of pipe [with] sufficient business acumen to file liens”); \textit{K.A.O.P. Co.}, 372 N.W.2d at 777 (questioning applicability of Section 9-302(1)(e) where transferee reserved only a security interest in the accounts rather than receiving an absolute assignment, and noting the transferee’s failure to file an already prepared financing statement); \textit{H. & Val J. Rothschild, Inc.}, 242 N.W.2d at 847 (noting the assignee’s familiarity with mortgage filing requirements in refusing to excuse the failure to file security interest). Contrast \textit{Fort Dodge Roof-
tion, have emphasized the particular assignee’s familiarity with the filing system and consequent assumption of the risk in failing to use it.\textsuperscript{191}

Those courts that take the osterizer approach do not typically focus on any of these factors. Rather, they deem the professional or nonprofessional character of the assignee to be most important in applying Section 9-302(1)(e).\textsuperscript{192} As we have seen, however, the statutory text does not bear this interpretive approach.\textsuperscript{193}

4. A Better Approach to Section 9-302(1)(e)

So how should courts interpret Section 9-302(1)(e)? In general terms, courts should construe the section in keeping with its underlying aims, but only so far as its language permits. Judges undertaking this effort are not likely to find perfect peace of mind. Nevertheless, they might avoid some psychic wear and tear by following these suggestions:

First, courts should reject out of hand the extreme antitextual interpretations of Section 9-302(1)(e) that bar all financial institutions from ever invoking the filing exemption,\textsuperscript{194} and permit nonprofessional assignees to claim the exemption even when they receive all the assignor’s accounts.\textsuperscript{195} These rules do too much violence to the language of the Code, even if they are sensible as a matter of abstract policy.

Second, in divining whether an assignment involves a significant part of the assignor’s accounts, courts should not focus on whether the assignee is a professional financier.\textsuperscript{196} Critics of this position will argue that the drafters of the U.C.C. included Section 9-302(1)(e) in the Code to protect the nonprofessional account transferee.\textsuperscript{197} The drafters did so, however, by forging a rule that does not focus on the professional or nonprofessional status of the transferee. Moreover, they did so in a set-

\textsuperscript{191} See note 190.
\textsuperscript{192} See, for example, \textit{Fort Dodge Roofing Co.}, 50 Bankr. at 669 (noting that two years passed between assignee’s taking of assignments in excusing the failure to file second assignment under Section 9-302(1)(e)); \textit{Consolidated Film Indus.}, 403 F. Supp. at 1284 (stating that the assignee “apparently was given information that its assignment was not a significant portion of [assignor’s] contract rights, and it may have [reasonably] relied on that information in not filing a financing statement”).
\textsuperscript{193} See notes 174-82 and accompanying text.
\textsuperscript{194} See note 161 and accompanying text.
\textsuperscript{195} See notes 178-80 and accompanying text.
\textsuperscript{196} See notes 174-82 and accompanying text.
\textsuperscript{197} See, for example, \textit{Bindl}, 13 Bankr. at 150 (explaining that “as suggested by the official comment to the UCC, in isolated or casual assignments filing is an undue burden on the unsophisticated transferee”). See also notes 77-80 and accompanying text.
tung where sound reasons can be marshalled for preferring a rule that rejects any such distinction.\textsuperscript{198}

The proper judicial response to this state of affairs is not to rewrite the statute to distinguish between nonprofessional and professional assignees. Rather, judges should give the Section 9-302(1)(e) exemption an ample scope in all cases to ensure that nonprofessionals who claim the exemption are not prejudiced by the Code's incidental extension of the exemption to institutional financers.\textsuperscript{199} In short, courts should apply Section 9-302(1)(e) in all cases on the premise that the claimant is a family farmer or other small businessperson. Otherwise, courts will make precedent that, if applied in principled fashion, later will leave deserving nonprofessionals out in the cold.\textsuperscript{200}

Third, courts that cannot resist differentiating between the “little person” assignee and the expert financial institution should not accomplish this result by warping the language of Section 9-302(1)(e). Instead they should, in an intellectually honest and straightforward manner, fashion supplementary non-Code law under Section 1-103 to avoid harsh and unfair results in cases that genuinely threaten the nonprofessional assignee’s interests.\textsuperscript{201} A nonprofessional assignee might actually rely on the lack of any filed financing statement in taking an account assignment. If a lending bank later pops up and claims a prior position based on Section 9-302(1)(e), courts might apply the doctrine of equitable estoppel to subordinate the bank. Whether such an application of

\textsuperscript{198} The drafters may have foreseen inordinate difficulties for courts called on to distinguish between professionals and nonprofessionals. See note 605 and accompanying text. The drafters may have reasoned that all or most assignments to professionals would involve a substantial part of the debtor’s accounts, so that the section would have little practical bearing on professionals even if made applicable to them. See note 131 and accompanying text. Perhaps the drafters anticipated that professional assignees would file as to small account transfers regardless of whether Section 9-302(1)(e) applied to them, thus further limiting the real-world impact of the section on such assignees. See notes 170-71 and accompanying text. Whatever their reason, the drafters drew up a rule that, though concededly designed in large part to protect nonprofessionals, draws no line at all between professional and nonprofessional transferees.

\textsuperscript{199} By way of analogy, a major purpose of a three-year statute of limitations is to protect persons prejudiced by delay in initiating actions. The existence of this purpose, however, does not mean that persons who are not prejudiced by delay cannot invoke the statute or are subject to a less generous interpretation of the term “three years.” Rather, the statute is enforced according to its terms.

\textsuperscript{200} The practical difficulties in taking this leap are twofold. First, a court looking at an individual case is not likely to have sympathy for a Section 9-302(1)(e) claimant that is a bank or commercial factor. Second, even the court that looks beyond the individual case will be tempted to read less generously an exemption applicable to both professionals and nonprofessionals, than one applicable only to nonprofessionals. By recognizing these impulses, courts should be better able to overcome them.

\textsuperscript{201} See Clark, The Law of Secured Transactions ¶ 1.01[1][d] at 1-5 (cited in note 8) (stating that “courts . . . rely heavily on § 1-103 to fill in the gaps deliberately or accidentally left in Article 9”). Section 1-103 is set forth in substantial part in the text accompanying note 406.
equitable estoppel is displaced by the particular provisions of Sections 9-302(1)(e) and 9-512, and is thus impermissible under Section 1-103, is debatable. But there is room to argue that courts may equitably subordinate the distinctively culpable professional assignee whose lack of diligence has induced detrimental reliance.

Finally, courts applying the Section 9-302(1)(e) exemption should focus—in conformance with the section's "significant part" language—on the portion of accounts transferred and the absolute size of the assignment. Inescapably such line-drawing involves difficult judgments. In general, however, courts should apply a sliding scale under which the tolerable percentage of accounts transferred rises as the absolute size of the assignment decreases. It is not surprising that a number of cases illustrate a proper application of this approach.

On a more general level, courts need to reflect on the proper philosophy to bring to close cases under Section 9-302(1)(e). There is reason to advocate resolving close cases in favor of filing, given "[t]he desirability of providing public notice of interests in such ephemeral property, and the ease with which [assignees] can file." The better view, however, is just the opposite. Because Section 9-302(1)(e) sets forth a rule of lenity designed to protect nonprofessionals who take limited and out-of-the-ordinary account assignments, courts should construe the statute liberally in all cases to ensure that they achieve this aim.

5. The Interplay of Section 9-302(1)(e) and the First-To-File Rule

Section 9-302(1)(e) establishes a principle of perfection and not of priorities. Even when applicable, Section 9-302(1)(e) does not always...
operate in such a way as to provide an exception to the first-to-file rule. This point is illustrated by Case D:

Case D. On Day 1, Adele Accountdebtor buys Horatio the Hog from Arthur Assignor for $450, with payment due on Day 5. As of Day 1, Alfee Assignee I already holds a floating lien that covers all accounts of Arthur Assignor and has a U.C.C. financing statement on file as to that security interest. On Day 2, Arthur Assignor transfers his right to payment for Horatio—one of his twenty hog accounts—to Artee Assignee II. Assignee I and Assignee II both demand payment on Day 5.

In this case Assignee I is not covered by Section 9-302(1)(e) because he has taken all of Arthur's hog accounts on a continuing basis. Assignee II, however, has not obtained a significant part of Arthur's accounts and so can claim the benefit of Section 9-302(1)(e). Does this mean that Assignor II takes priority? Quite the contrary.

The reason why is that Section 9-302(1)(e) serves only to perfect Assignee II's security interest automatically; it does not give Assignee II priority. Instead, Section 9-312(5)(a) fixes priorities, and it does so on the basis of time of filing or perfection.²⁰⁸ Because Assignee I filed before Assignee II's security interest was automatically perfected by 9-302(1)(e), Assignee I wins Case D.

Even the otherwise meticulous Professor Farnsworth stumbles on this point. He correctly notes that “Article 9 exempts from its ‘first-to-file’ rule ‘an assignment of 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.’” Then he adds: “Such an assignment, although within the scope of Article 9, is apparently entitled to priority if it was made before the competing assignment.”²⁰⁹ That, however, is often not the case because filing may predate the assignment. Assume, for example, that on Day 1 Big Bank has on file a financing statement covering all the assignor's accounts. On Day 2, Max makes a nonsignificant-part assignment of Account No. 219 to Zelma. On Day 3, Max enters into a security agreement that assigns Account No. 219 to Big Bank. On these facts, Big Bank takes priority even though the assignment to Zelma was “made before the competing assignment.” This is the proper result because, although Section 9-302(1)(e) excuses Zelma from the Article Nine filing rules, it does not excuse her from the Article Nine priority rules. Under those

²⁰⁸. U.C.C. § 9-312(5)(a). See id. § 9-312(5)(a) cmt. 4; White and Summers, Uniform Commercial Code § 24-4 at 1131.

²⁰⁹. Farnsworth, Farnsworth on Contracts § 11.9 at 123 (cited in note 8) (emphasis added).
priority rules Big Bank wins because it filed before the automatically perfected assignment to Zelma occurred. The bottom line is that, although Section 9-302(1)(e) creates an exception to the general rule of first-to-file priority, the applicability of Section 9-302(1)(e) to an assignee’s interest does not mean that the competing first filer will always lose. Rather, because of its interaction with Section 9-312(5), Section 9-302(1)(e) provides an exception to the general first-to-file rule only if the first-filed financing statement covering the competing interest is recorded after the Section 9-302(1)(e) account transfer is automatically perfected.

C. The Section 9-104(f) Exclusion

When the Code’s drafters extended Article Nine’s coverage to account sales, they could have provided a complete set of rules for deciding all priority disputes arising from successive assignments. The drafters, however, were not so ambitious. Viewing their overriding purpose as the regulation of security devices, the drafters exempted from the Code certain account transfers “which, by their nature, have nothing to do with commercial financing transactions.” The result was Section 9-104(f), which provides that Article Nine “does not apply” to

a sale of accounts or chattel paper as part of a sale of the business out of which they arose, or an assignment of accounts or chattel paper which is for the purpose of collection only, or a transfer of a right to payment under a contract to an assignee who is also to do the performance under the contract or a transfer of a single account to an assignee in whole or partial satisfaction of a preexisting indebtedness;...

This section does not exclude specified accounts from Article Nine. Rather, it excludes specified transactions in accounts. The result is that one transfer of an account may fall within Article Nine, while another transfer of the identical account may fall outside the Article. Such situations present prickly priority problems, particularly for the first-filing financer who carefully has jumped through every Article Nine hoop.

Before turning to Section 9-104(f)’s effect on priorities, however, it is
necessary to explore the types of account transactions Section 9-104(f) excludes from the Code.

1. Professor Gilmore’s “Financing Nature” Approach

Professor Gilmore asserted that Section 9-104(f)’s listing of account transfers set forth merely an illustrative collection of examples. Thus, according to Gilmore, courts should view the list as nonexclusive and use the section to remove from Article Nine all nonfinancing sales. This interpretation merits attention because Gilmore, the Reporter for the Article Nine project, “is the horse’s mouth.” Moreover, although some courts have rejected Gilmore’s position, others have cottoned to his view. This latter tendency is unfortunate, because Professor Gilmore’s reading of Section 9-104(f) is nothing less than outrageous.

Gilmore’s interpretation flatly contradicts the statutory text. On its face, Section 9-102 extends the Code to all account sales and transfers for security. Moreover, neither Section 9-104(f) nor any other Code

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216. Gilmore, Security Interests in Personal Property § 10.5 at 309.
217. Clark, The Law of Secured Transactions ¶ 1.01[2][c] at 1-7 (cited in note 8). See also Homer Kripke, Suggestions for Clarifying Article 9: Intangibles, Proceeds, and Priorities, 41 N.Y.U. L. Rev. 687, 690 (1966) (stating that “[i]t is all but impossible to discuss ambiguous areas in the present article 9 without finding that Mr. Coogan and Professor Gilmore, like Kilroy, have been there before”).
218. See, for example, Sun Air Int’l, 24 Bankr. at 137 (rejecting theory that Code is inapplicable to any transaction “not intended as a financing arrangement” because Code “was not intended to be applied only to transactions intended for security”); Sun Bank, 466 So. 2d at 1092 (refusing to recognize general exemption from Code for nonfinancing transactions); John Deere Co. v. Neal, 544 S.W.2d 514, 516 (Tex. Civ. App. 1976) (stating “[t]hat such comprehensive exclusion was not the intent of the draftsman seems apparent”). See also Cripps, 31 Bankr. at 542-44 (refusing to apply Section 9-104 even though parties stipulate that sale of accounts from one individual to another “was not a commercial financing transaction”); Consolidated Film Indus., 403 F. Supp. at 1282 (rejecting generalized nonfinancing transaction exemption).
219. For example, in Panama Airways, Inc., the court construed an account receivable statute, which broadly required filing as to assignment of “an existing or future right to the payment of money,” not to cover transactions “where there is no accounts receivable factoring or financing in the ordinary commercial sense.” 4 U.C.C. Rep. Serv. at 428-30. It also noted that the problem “remains with us even under the Uniform Commercial Code,” id. at 431, and quoted Gilmore’s illustrative-list interpretation of Section 9-104(f) to support judicial exclusion of nonfinancing transactions, id. See also First Gen. Contractors, 12 U.C.C. Rep. at 764 (reaffirming Panama Airways as reaching proper result under Code and citing Gilmore with approval); Cripps, 31 Bankr. at 544 (discussing “financing nature” approach used in In re Hurricane Elkhorn Coal Corp. II, 19 Bankr. 609 (Bankr. W.D. Ky. 1982)).
220. Professor Gilmore himself recognizes this fact. Gilmore, Security Interests in Personal Property § 10.5 at 309 (noting that “final draft starts by covering all ‘sales’”). In accord, Board of Trustees of the Vacation Trust Carpenters Local No. 1780 v. Durable Developers, Inc., 724 P.2d 736, 745 (Nev. 1986) (hereinafter “Vacation Trust”) (stating that “[a]ccording to the drafter’s comments to this section, every assignment of an account receivable, whether intended for security or not, is included within the scope of Article Nine unless expressly excluded by some other
provision contain language supporting a generalized exemption for nonfinancing assignments. Rather, Section 9-104(f) enumerates four, and only four, specific categories of excluded account transactions. The point is driven home by the Comment to Section 9-104, which teaches that only “certain transfers . . . which, by their nature, have nothing to do with commercial financing transactions” are excluded from the Article.

The Code’s drafters knew how to craft illustrative lists when they so desired, and they did not write such a list into Section 9-104(f).

Professor Gilmore’s position also is untenable in light of the history of the Code. Early drafts of the Code did endorse Gilmore’s view. The 1952 version applied the Code only “to any financing sale of accounts,” while the Code’s 1950 incarnation exempted from the filing requirement “an assignment of accounts . . . not for the purpose of financing.” By 1956, however, the Code’s drafters had scrapped the financing-sale litmus because it was too “undefined.” Instead, they

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221. See Sun Bank, 468 So. 2d at 1092 (stating that “the specific language of section 9-104(f) does not appear to allow for additional ad hoc exemptions and such an approach would subject the priority and filing rules established by Article 9 to increasing uncertainty”) (footnote omitted); John Deere Co., 544 S.W.2d at 516 (stating that “[t]he scope of Chapter 9 has been generally defined by Section 9.102, and specifically limited by Section 9.104. There is no apparent reason to give an expansive reading to the enumerated limitations”).

222. U.C.C. § 9-104 cmt. 6 (emphasis added).

223. See, for example, id. § 9-102(2) & cmt. 1.

224. See generally Coogan, et al., Secured Transactions § 3.08[1][b] at 3-46 (cited in note 8); Gilmore, Security Interests in Personal Property § 10.5 at 309 (cited in note 2); Jensen, 1977 Utah L. Rev. at 333 (cited in note 74).


226. U.C.C. § 9-303(f) (1950). In a curious passage, the Comments to Section 9-102 of the 1952 Code stated: “Subsection 1(b) brings under this Article all ‘financing’ sales of accounts, chattel paper and contract rights, whether made for security or not. The kinds of sales meant to be excluded by the qualification ‘financing’ are identified in Section 9-104(f).” U.C.C. § 9-102 cmt. 3 (1952). As Professor McDonnell suggests, the Comment “shows that these provisions were intended to work in tandem.” Coogan, et al., Secured Transactions § 3.08[1][b] at 3-47 (cited in note 8). The Comment, however, does not reveal how Sections 9-102 and 9-104(f) were to interact under the 1952 draft. The point is now academic because the drafters in 1956 opted to remove the pliable financing qualification from Section 9-102 altogether and let Section 9-104(f) alone define those categories of accounts not covered by Article Nine.

227. American Law Institute, 1956 Recommendations of the Editorial Board for the Uniform Commercial Code at 14, 254 (1957). Even Professor Gilmore acknowledged that “[t]he undefined (and perhaps undefinable) phrase ‘financing sale’ was evidently felt to be too vague.” Gilmore, Security Interests in Personal Property § 10.5 at 309 (cited in note 2). Subsequent struggling with what is and what is not a financing sale confirms the validity of this concern. See, for example, Sun Air Int’l, 24 Bankr. at 137 (characterizing present and absolute assignment of account for agreement to provide legal services as “a financing arrangement for the payment of attorneys fees”); John Deere Co., 544 S.W.2d at 516 (stating that a tractor retailer’s sale of chattel paper to large wholesaler for cash cannot be said to have nothing to do with commercial financing”); Ford, 22 Okla. L. Rev. at 438, 439 (cited in note 112) (arguing that leading cases supporting the illustrative-list interpretation in fact involved financing transactions properly covered by
sculpted Article Nine to cover “all sales” of accounts “except as otherwise excluded.” The drafters of Article Nine thus initially embraced, but later repudiated, the very standard Professor Gilmore would apply. They did so, moreover, because the listed categories of account transfers set forth in Section 9-104(f) “satisfactorily specify types of transactions in accounts . . . not subject to the Article.”

Any doubt about the inappropriateness of Professor Gilmore’s interpretation was removed by the 1972 Code Amendments, which added to Section 9-104(f) its fourth excluded category of accounts: the single account transfer made to satisfy a preexisting debt. The revisors added this category to validate earlier decisions that had found such transfers outside Article Nine even though they are not listed in Section 9-104(f). If the Code’s revisors had agreed with Professor Gilmore’s reading of Section 9-104(f), however, they would not have had to amend the section to vindicate those holdings. More important, once the Board decided to amend Section 9-104(f), it did not rewrite the section to reach all nonfinancing assignments. Rather, it added to the section only a single and specific category of account transactions. In sum, the drafters of the Code consistently have refused to give courts carte blanche to exclude account transfers on the nebulous ground that they do not involve a financing sale.

Even so, there continue to be rumblings that Professor Gilmore had things right. The Court of Appeals for the District of Columbia, for example, recently endorsed Gilmore’s approach to Section 9-104(f), as have other tribunals. Moreover, although Professor McDonnell seems in the end to reject the financing-sale interpretation of Section 9-104(f), his treatment of that interpretation overstates its credibility. In particular, following his discussion of Spurlin v. Sloan and Lyon v.

Code); Jensen, 1977 Utah L. Rev. at 335 n.27 (cited in note 74) (same).
229. Id. at 14 (emphasis added).
230. See U.C.C. § 9-104 cnt. 8 (citing the Lyon and Spurlin decisions discussed in notes 287-90 and accompanying text).
231. In accord, Consolidated Film Indus., 403 F. Supp. at 1282 (rejecting view that 1972 Amendment simply clarified the preexisting meaning of Section 9-104(f); rather, the amendment “was in fact necessary to effect” results of earlier preexisting-debt-satisfication cases).
232. See notes 224-31 and accompanying text.
234. See note 219 and accompanying text.
235. See Coogan, et al., Secured Transactions § 3.08[4][a] at 3-55 (cited in note 8) (stating that “[b]y narrowly confining the statutory exemption to the facts of the Spurlin case, the revisers effectively rejected language which would exclude a range of nonfinancing transfers from the Article”); id. § 3.08[2] at 3-51 (criticizing “continuing judicial unwillingness to accept the drafters’ attempt to draw bright lines as to which assignment of accounts will and will not be included in the scope of Article 9”); id. § 3.08[3][c] at 3-54 to 3-55.
Ty-Wood Corp.," Professor McDonnell suggests that "Professor Gilmore's position [has been] buttressed by the reference to the Lyon case in the [1972] comment to Section 9-104." His reasoning is as follows:

[In 1972] a new sentence was added to the comment stating "this paragraph excludes from the article such transactions as that involved in" Lyon and Spurlin. Since Spurlin clearly involved a transfer of a single account in partial satisfaction of an existing indebtedness, the new comment is unexceptional with respect to that case. But the characterization of the Lyon transfer as an absolute conveyance in satisfaction of debt, as has been seen, is very questionable. Nor can Lyon be fitted within any of the other express exemptions of Section 9-104(f). The real ground for that decision appears to be the non-professional character of the lender. It is difficult to square the new wording of Comment 6 with the position that Section 9-104 exhausts the types of absolute assignments excluded from Article 9.

The key to this analysis is that Professor McDonnell describes the Lyon court’s finding that the account transfer in that case was an absolute conveyance as "very questionable." From this premise, Professor McDonnell reasons that the Code drafters may well have intended to extend the Section 9-104(f) exclusion to broadly protect nonprofessionals, whether or not they take an account transfer in satisfaction of an obligation. In Lyon itself, however, the appeals court embraced and emphasized the trial court’s finding of fact that the account transfer was not for purposes of security, but was an absolute conveyance in payment of a preexisting debt. Accordingly, the best reading of the 1972 Comment is that the new exclusion in Section 9-104(f) applies only when such a finding is made. Of course, the Comment’s reference to Lyon might be read to throw interpretive light on Section 9-104(f)’s new preexisting-indebtedness exclusion, including by suggesting that security as well as absolute transfers meet the "in satisfaction" requirement. In no way, however, does the Comment’s brief reference to Lyon support a wideranging antitextual exemption for all nonfinancing account transfers.

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238. Coogan, et al., Secured Transactions § 3.08][3][c] at 3-54 (cited in note 8).
239. Id. § 3.08[3][a] at 3-52.
240. Lyon, 239 A.2d at 821.
241. See notes 238-236 and accompanying text.
242. In accord, White and Summers, Uniform Commercial Code § 22-10 at 1001 (cited in note 8) (stating that "we believe that all sales or assignments of accounts except for those specifically excluded under 9-104(f) are governed by Article Nine."); Clark, The Law of Secured Transactions § 1.04 at 1-26 (cited in note 8) (stating that "although Comment 6 to § 9-104 suggests that the courts might create ad hoc exemptions based on this [non-financing-transactions] standard, the proper result is not to "open up this Pandora's box"). See also Editors' Note, Goldstein v. Madison Nat'l Bank, 3 U.C.C. Rep. Serv. 2d (Callaghan) 280, 281 (D.C. Cir. 1986) (stating that "[w]hile the amendment achieves the same result as [Spurlin and Lyon], it does not adopt the reasoning behind the decisions").
We turn now to examining the four categories of account transactions the drafters did exclude from Code coverage in Section 9-104(f).

2. The Sale-of-a-Business Exclusion

The first type of account transfer excluded from Code coverage is the “sale of accounts . . . as part of a sale of the business out of which they arose.” This exclusion fits comfortably with Section 9-104(f)’s overarching aim of excluding specified nonfinancing transfers from Article Nine. The sellers of business assets typically are not seeking current operative funds; instead, they are removing any need for working capital by disposing of their operations.

Even so, why should the business purchaser not be required to comply with the Code’s attachment and perfection requirements with respect to the transfer of accounts? Following the notion of Professor Gilmore, it is difficult to say that the transfer of accounts pursuant to the sale of a business is not the type of transaction that no one “would have thought of filing.” The sale of a business is always a significant transaction, and the parties to such a transaction are almost always represented by counsel. Such a sale requires the execution of formal documents and often involves a number of public filings. Indeed, counsel for the buyer of the business should, and often will, check the U.C.C. files to discover any existing encumbrances against property—including account property—being transferred as part of the sale. It is ironic that the business buyer, who thus profits from the U.C.C. filing system, should not have to use that same system to warn potential future transferees of the account purchases the buyer has made.

On the other hand, one can construct an efficiency argument to support the sale-of-a-business exclusion. The seller of a business no longer has that business. No person would be so foolish as to purchase accounts from someone who is not conducting business operations. Thus, the argument goes; it is a needless and wasteful exercise to require the business buyer to provide warning via the U.C.C. files to protect possible future purchasers of the business’s seller’s accounts.

This rationale for the sale-of-a-business exemption is not persua-

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243. U.C.C. § 9-104(f).
244. In accord, Coogan, et al., Secured Transactions § 3.08[4][d] at 3-61 (cited in note 8).
245. See Ford, 22 Okla. L. Rev. at 426 (cited in note 112) (suggesting that the earmark of a financing transaction is whether “the assignment enabled [the assignee] to obtain or retain money advanced by another to aid his business”); Jensen, 1977 Utah L. Rev. at 335 n.27 (cited in note 74) (same). The seller of a business may use sale proceeds to provide working capital for another business. Such a transaction, however, travels far from any ordinary factoring-type transaction.
246. See note 78 and accompanying text.
sive. For example, a business may be sold in stages, or a business seller may have another business, or set up a new business, that provides "cover" for reselling already-assigned accounts. Particularly given the significance of business-sale transactions, and the low cost of filing, one can make a strong case against this Code exemption. Nonetheless, the sale-of-a-business exclusion stands large as life in Section 9-104(f).247

3. The For-Collection-Purposes-Only Exclusion

The second Section 9-104(f) exclusion applies to "an assignment of accounts . . . which is for the purpose of collection only." Any non-recourse notification-based account sale to an institutional factor is for collection purposes in the sense that the parties envision that the assignee will process and bear the risk as to all account payments.248 Such assignments, however, are not for collection purposes only, and clearly are subject to Article Nine.249 Even so, some courts have used the for-collection-purposes-only exclusion to protect creditors who have taken notification-based assignments to facilitate payment of the assignor's debt.250 These cases are off the beam, however, because the purpose of the exclusion was to protect the "assignment of an account to a collection agency or to an attorney for simple collection of a deadbeat account."251


248. See notes 23-26 and accompanying text.

249. See White and Summers, Uniform Commercial Code § 21-9 at 956 (cited in note 8) (suggesting that Article Nine requires filing by factors who "buy accounts outright and without recourse"); Gilmore, Security Interests in Personal Property § 10.5 at 308 (cited in note 2) (noting that the factoring operation in which "the assignee buys receivables without recourse against the assignor" is closely related to straight accounts receivable financing). See also District of Columbia v. Thomas Funding Corp., 15 U.C.C. Rep. Serv. 2d (Callaghan) 242, 246 (D.C. Ct. App. 1991) (stating that factoring arrangement is "a frequently used means of commercial financing that the drafters of the Uniform Commercial Code clearly contemplated would fall within the scope of Article 9").

250. See, for example, Feldman, 408 F. Supp. at 38 (finding lessor's assignment of rents to lender that provided funds with which lessor purchased aircraft was made "to facilitate direct payment of the loan by means of the rent payments" and thus "was for collection purposes only," and suggesting that Lyon was a for-collection-purposes-only case); United States v. Mercury Motor Express, Inc., 294 F. Supp. 919 (S.D. Ga. 1968) (conclusory opinion deeming collection-purposes exclusion applicable to assignment made with view toward account proceeds being paid directly to assignee to satisfy assignor's debt).

251. Ford, 22 Okla. L. Rev. at 426 (cited in note 112). In accord, In re Cauhorn, 33 Bankr. 119, 120 (M.D. Tenn. 1983) (stating that "the phrase 'for the purpose of collection only' must necessarily apply only to assignments of a non-commercial nature, such as the assignment of a debt to a collection agency for the sole purpose of obtaining collection of the debt"); Brent Explo-
So what assignments do fall within this category of excluded account transactions? Consider Case E.

CASE E. Sam Seller, Inc. holds sixteen long-overdue invoices unpaid by Betsy Buyer Co. Sam assigns all these accounts to Curly's Collection Agency. In return, Curly's agrees it will promptly remit to Sam one-half of all collections it receives from Betsy.

This assignment is for collection purposes only in the most literal sense: Sam's sole reason for transferring the accounts is to facilitate their collection. Looking to the purpose of 9-104(f), the assignment is not a financing transaction—at least in the ordinary discounting sense—because Sam's transfer does not transform his right to future payment into any present operating capital. Rather Sam has received only an executory agreement entitling Sam to realize at most a portion of amounts Sam already is owed and to do so only in the event that collections in fact occur. Case E thus provides the paradigmatic example of the assignment for collection purposes only.

What of Case F?

CASE F. As in case E, Sam holds sixteen overdue accounts pay-
ble by Betsy. Now, however, Sam assigns the accounts to Curly’s for $1000 in cash. Curly’s is to keep all amounts it collects from Betsy.

Is this transfer for collection purposes only? There is room to argue that it is not. Some might even say that, from Sam’s perspective, the assignment in Case F is not for collection purposes at all; rather, its purpose is to produce immediate cash. This fact marks the Case F transfer as more like a financing transaction than the assignment involved in Case E. Indeed, the transaction in Case F may be said to differ from the ordinary account sale only in the respect that the sold accounts are overdue. If the Code’s drafters meant to exclude from Article Nine all sales of overdue accounts, however, they could have done so with far more direct and explicit language than Section 9-104(f) employs.

To these considerations might be added the observation that no great injustice will follow from applying the Code to account transfers like the one in Case F. The typical buyer of overdue accounts is a professional collection agency or lawyer, and ought to know of the U.C.C. filing system. In addition, because such transferees ordinarily will take only the limited portion of the assignor’s accounts that are in default, those transferees often can invoke the Section 9-302(1)(e) exemption even if not saved from their folly in failing to file by Section 9-104(f).

On balance, however, courts should find that Case F falls within

254. See Coogan, et al., Secured Transactions § 3.08(4)(c) at 3-61 (cited in note 8) (stating that “cases would seem to establish that a transfer is for collection only when the assignor does not receive anything of value other than the collection activities themselves”).

255. See In re Worden, 63 Bankr. 721, 724 (Bankr. D.S.D. 1988) (stating that “contrary to the facts in the instant case, a ‘collection only’ assignment does not involve an advance of money”); Swiden Appliance & Furniture, Inc. v. National Bank of S.D., 357 N.W.2d 271, 275 (S.D. 1984) (holding that the Section 9-104(f) “exclusion for contracts or chattel paper sold or assigned for the purpose of collection only” did not apply since the sale of the retail installment sales contracts was not “for the purpose of collection only,” but also involved the bank’s advance of money to the seller’); Daly, 610 P.2d at 401 (recognizing that “a ‘collection only’ assignment does not involve an advance of money. Rather, the money is paid only if the collection is made.”). See also Franchise Tax Bd. v. Credit Managers Ass’n., 142 Cal. Rptr. 777, 780 (Cal. Ct. App. 1977).

256. See Ford, 22 Okla. L. Rev. at 426 (cited in note 112) (stating that “[t]he basic reason for this exclusion is that an account which is assigned solely for the purpose of being collected and in no manner related to the obtaining of capital for a business is not a financial transaction and, therefore, does not belong in Article 9”). See generally note 245 and accompanying text.

257. Rather, a broad application of the “for collection purposes only” exclusion, such as to Case E, arguably threatens to cause injustice by jeopardizing the positions of later transferees. This is so because a business might sell overdue accounts to a collection agency and then sell them again to an unsuspecting transferee unable to secure notice of the prior transfer from the U.C.C. files. The uncollectability of the accounts may cause the cash-short position that induces the assignor to engage in such nefarious behavior.

258. See note 251 and accompanying text.

259. See notes 113-210 and accompanying text.
the Section 9-104(f) exclusion. This is so because, just as in Case E, the assignment in Case F involves a transfer of overdue accounts, made because they are overdue, to a professional collection agency. To say that the transaction does not involve commercial financing is plausible in these circumstances. Indeed, the account sale in Case F resembles an outright assignment of a damages claim (such as an action in tort) more than a traditional factoring transaction. No less important, this interpretation avoids affording more protection to the assignee who merely undertakes collection efforts (Case E) than the assignee who both works at collection and enriches the assignor’s estate by paying for the opportunity to do so (Case F). Nor does this analysis of Case F require the unsatisfying conclusion that Section 9-104(f) places all overdue-account transfers outside the Code. For example, even tardy account debtors often pay their bills in due time without the need for special collection efforts; thus the sale of such accounts as part of a larger account sale to a factor would hardly qualify as being for collection purposes only.

There is reason to believe that Professor Clark would exclude Case F from the Code, and the case law does not foreclose that result. Although the question is close, the better view is that the Section 9-104(f) exclusion applies to cash purchases of overdue accounts by a buyer specifically planning to undertake affirmative collection efforts.

4. Assignments and Delegations

The third Section 9-104(f) exemption covers the “transfer of a right to payment under a contract to an assignee who is also to do perform-

261. Contrast id. § 9-104(k) (excluding even security transfers of tort claims from Article Nine).
262. See text following note 266.
263. See Clark, The Law of Secured Transactions § 1.08[6][b] at 1-96 (cited in note 8) (indicating that “if the transfer of accounts is to a collection agency or other third party after default . . . the transaction is clearly excluded”).
264. Thus, Daly differs from Case E because in Daly “there was no indication that the accounts were past due.” Coogan, et al., Secured Transactions § 3.08[4][c] at 3-60 (cited in note 8). In re Worden is distinguishable because it involved not an account sale, but an assignment designed to “secure advances loaned by a bank.” Coogan, et al., Secured Transactions § 3.08[4][c] at 3-60 (cited in note 8). The best case authority for not applying the Section 9-104(f) exclusion to Case E is probably Franchise Tax Bd. v. Credit Managers Ass’n., 142 Cal. Rptr. 777 (Cal. Ct. App. 1977). There a debtor assigned its accounts for the benefit of its creditors in return for their agreement to delay enforcement of the debtor’s obligations to them. Contrary to the analysis in the text, the court refused to apply the for-collection-purposes-only exemption on the ground that the debtor had received a present consideration—in the form of the enforcement moratorium—in return for the account transfer. Id. at 780. Even so, the Credit Managers case is readily distinguishable from Case E. Because the transaction in that case involved a restructuring of debt, the transfer of accounts was part of a financing transaction. Of no less importance, the accounts transferred in Credit Managers were not overdue at all.
This language embraces the delegatee-assignee—that is, the person who both assumes duties and obtains rights under the contract held by the assignor. A strong argument exists for excluding these transactions from the Code because the delegatee-assignee may not think of the transaction as involving an “account” at all. As a functional matter, being a delegatee-assignee differs little from being hired to do a job in the first place, and the businessperson understandably may fail to recognize that a legal difference exists that requires the filing of a U.C.C. financing statement. Such assignments, moreover, travel far from ordinary assignments pursuant to factoring or accounts financing arrangements. In particular, the principal benefit to the assignor from such transfers is not the receipt of funds, but the assignee’s assumption of the assignor’s contractual duties. Thus it is unlikely that such transfers will involve any meaningful financing of the assignor’s operations even in the loose sense of transforming a right to future payments into significant current cash. Finally, the assignee-delegatee has a special claim to realize the value of the assigned account because the delegatee’s own work earns the right to payment of that account.

The core of the performance-as-well-as-payment exclusion is plain enough. The builder who assumes both the right to payment, as well as the duty to perform, under another’s construction contract falls outside
Article Nine. On the other hand, the exemption does not reach the bank that takes an assignment of a contractual right to a consulting fee payable to the bank’s own consultant even though the bank is to perform under the contract in the sense that it is obligated to pay the fee. In such a case, the bank is not the delegatee of the assignor’s duty to render consulting services and therefore has not undertaken the relevant performance for purposes of 9-104(f).

More complex cases will generate more difficult issues. For example, in Petron Trading Co. v. Hydrocarbon Trading & Transport Co. the assignor was a supplier obligated to deliver fuel to the State of New York. The supplier-assignor subcontracted with the assignee, who agreed to deliver some of the fuel, and took a security interest in the assignor’s right to payment from the state to secure the supplier’s obligation to pay. On these facts, the court refused to apply the Section 9-104(f) exclusion to protect the assignee. The court reasoned that the assignor “did not extricate itself from its contract with the State” because it “retained rights to petition for price adjustments” and “continued to prepare invoices.” This analysis is unpersuasive. Delegators seldom are extricated from the underlying transaction; at least, they remain responsible for performance in the event of the delegatee’s

269. See Coogan, et al., Security Interests in Personal Property § 3.08(4)(b)(ii) at 3-56 (cited in note 8) (citing assignment-delegation by the building contractor as the prototype case under this Code rule).
270. Autrey, 673 P.2d at 449-50.
271. See In re Hengalo Enters., Inc., 51 Bankr. 54 (Bankr. S.D. Fla. 1985) (finding Section 9-104(f) payment-and-performance exemption inapplicable to collateral transfer of franchise agreements entitling assignor to operate car dealership; apparent reasoning of court is that such contracts do not involve a right to payment but instead provide only a means for generating income by way of car sales to third parties); Charter First Mortgage, 56 Bankr. at 846 (deeming “questionable” the position that a receiver is an assignee within the meaning of the performance-and-payment exemption). A division of authority exists on whether a general contractor’s assignment to a surety company, as part of a performance bond, of rights to payment from the project owner, contingent on the contractor’s default, is excluded from Article Nine by Section 9-104(f)’s payment-and-performance language. A number of cases say that it is. See, for example, In re V. Pangori & Sons, Inc., 53 Bankr. 711, 717 (Bankr. E.D. Mich. 1985) (collecting cases); City of Vermillion, 341 F. Supp. at 711. Other courts, and Professor Gilmore, say that it is not. See Gilmore, Security Interests in Personal Property § 10.5 at 309 (cited in note 2); In re Kuhn Constr. Co., 11 Bankr. 746, 749 (Bankr. S.D. W. Va. 1981). See generally Robert A. Hillman, Julian B. McDonnell, and Steven H. Nickles, Common Law and Equity Under the Uniform Commercial Code § 24.01[2][a][i] at 24-11 n.35 (Warren, Gorham & Lamont, 1985). The debate has little if any practical significance, however, given the courts’ uniform protection of construction sureties through the equitable subrogation doctrine. See notes 422-48 and accompanying text.
273. Id. at 1159.
274. See Farnsworth, Farnsworth on Contracts § 11.10 at 131 (cited in note 8) (noting that delegations are more often upheld “if the delegating party is to remain in the business and supervise the performance”).
Also unenlightening was the court's observation that the transaction was "somewhat akin to a commercial financing transaction, in that it afforded [the supplier-assignor] a means of obtaining the oil it needed to make the deliveries it contracted to make." The same point applies in any delegation case. The assumption of construction obligations by an assignee building contractor, for example, affords the delegator-assignor the means of obtaining the goods and services that it has contracted to deliver to the owner. The Section 9-104(f) exclusion, however, clearly covers such a transfer.

If the arrangement in Petron Trading properly falls outside Section 9-104(f), it is because the assignee did not take an outright assignment of amounts owed by the state, but instead took only a traditional collateral interest in the accounts to secure the supplier-assignor's obligation. In keeping with Section 9-104(f)'s underlying purpose, to say that the assignment had "nothing to do with commercial financing transactions" is difficult. Indeed, the assignee in Petron Trading is hardly different from a supplier that engages in the most orthodox form of secured financing by selling on an open-account basis while taking as collateral some portion of the buyer's assets. In addition, there is reason to believe the drafters envisioned that Section 9-104(f) would exclude only account sales—and not security transfers—from the reach of Article Nine. Thus, even Professor Gilmore, who advocated the most expansive interpretation of the provision in other respects, indicated that Section 9-104(f) was designed to exempt only nonfinancing sales from Article Nine.

Even so, the better view is that the subcontractor-assignee in Petron Trading—and similarly situated subcontractors—should enjoy the benefit of the Section 9-104(f) exemption. These subcontractors, particularly construction subcontractors, will often be small businesses. In other contexts, courts have stretched the Code's text to afford protection of such businesses when they fail to file financing statements.

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275. See id. § 11.10 at 126.
276. 663 F. Supp. at 1159.
277. See note 269 and accompanying text.
278. U.C.C. § 9-104 cmt. 6.
279. See notes 215-42 and accompanying text.
280. Gilmore, Security Interests in Personal Property § 10.5 at 309 (cited in note 2) (stating that "the Article was meant to apply to 'sales' of intangibles in institutionalized financing transactions (such as factoring); the three types of transfers which are specifically excluded are merely examples of 'non-financing' sales"). See also Valley Bank of Nev., 528 F. Supp. at 913 (stating that Section 9-104(f) "removes certain transactions from the scope of Article Nine," but that "[a]ll the transactions removed, however, are outright transfers of accounts.")
281. See notes 414-21 and accompanying text.
cases like Petron Trading, however, courts need not stretch the Code's language at all. This is so because in that case the assignee did receive "a transfer of a right to payment under a contract" and was "also to do the performance under the contract." Indeed, Section 9-104(f)'s use of the broad term "transfer" supports the conclusion that the subcontractor's fate should not hinge on whether it took its interest in the account by way of sale or security transfer.282

This is all the more true because an underlying premise of Article Nine is that courts, in general, should afford the same treatment to both absolute and collateral assignments of accounts.283 Moreover, it makes particularly good sense to apply that principle in this context. In many cases involving subcontractor-assignees, for example, the parties' working (if not formal) understanding will be that the delegator-assignor's obligation to the subcontractor is payable immediately upon the delegator-assignor's receipt of payments from the account debtor.284

In such situations, the difference between a security assignment and an absolute assignment of the owner's obligation is of little practical importance because in either event the parties anticipate a prompt turnover of funds upon their receipt by the assignor. To draw a distinction based on the technical description of the assignment in the contract thus elevates form over substance in derogation of basic Code policy.285

In sum, Petron Trading should not be followed.286 Rather courts should apply the performance-as-well-as-payment exemption liberally to protect those whose efforts generate account collections others thereafter seek to snatch from their grasp.

5. The Satisfaction-of-a-Preexisting-Indebtedness Exclusion

The final Section 9-104(f) exemption applies to "a transfer of a single account to an assignee in whole or partial satisfaction of a preexisting indebtedness." This language, the Comments tell us, was added to validate the results reached in the infamous Spurlin and Lyon cases.287

282. In the Petron Trading case itself the court recognized that "transfer" is a broad term. 663 F. Supp. at 1161.

283. See notes 72-75 and accompanying text.

284. See Rudolph, 5 B.C. Indus. & Comm. L. Rev. at 258 (cited in note 30) (stating that "the contractor will ordinarily pay subcontractors and material suppliers on the same basis on which he is being paid by the owner").

285. See U.C.C. § 9-101 cmt. (stating that "[t]he scheme of the Article is to make distinctions, where distinctions are necessary, along functional rather than formal lines").

286. Contrast In re Consolidated Steel Corp., 11 U.C.C. Rep. Serv. 408 (M.D. Fla. 1972) (finding no need to address claim of performance-and-payment exemption where subcontractor's supplier secured agreement from general contractor and subcontractor that checks should be drawn jointly to supplier and subcontractor).

287. U.C.C. § 9-104 cmt. 6 (citing Spurlin and Lyon). For other early cases embracing the approach of Spurlin and Lyon, see Cohen v. Casillo, 364 A.2d 858, 861 (Conn. Ct. App. 1976)
In *Spurlin*, a contractor assigned rights to payment generated by work on a project to a partner in the venture to settle partnership accounts. The case is infamous because of the court's monumental fumbling with the statutory text in finding that the parties had not created an Article Nine security interest at all.\textsuperscript{288} *Lyon* is infamous for two reasons. First, with every textual reason not to do so, the Court in *Lyon* followed *Spurlin*’s lead and held that the Code did not apply to account transfers made “in payment of a preexisting debt.”\textsuperscript{289} Second, the court found that the assignments in that case constituted payment rather than security, despite the assignee’s own admission that they were “taken as ‘security.’”\textsuperscript{290} Although these cases were hardly analytical masterpieces, the drafters seemed to like the principle for which they stood. Accordingly, in 1972 they grafted the new “satisfaction of a preexisting indebtedness” category of account transfers onto Section 9-104(f).\textsuperscript{291}

This preexisting-debt exception to Article Nine is not easy to explain or justify. This exclusion conflicts with the statutory purpose of exempting from Code requirements only those account transfers that “have nothing to do with commercial financing transactions.”\textsuperscript{292} The reason for transferring accounts to meet preexisting debt obligations, after all, typically is to stave off the creditor’s cash-depleting collection efforts. In effect such transfers entail debt extensions, through which the assignor is able to augment current operating capital by averting immediate cash outflows.

In addition, it seems strange to give preferential treatment to this particular class of account transferees. The recipient of an account transfer that extinguishes a preexisting debt merely surrenders a claim that would have been costly to enforce and might have proven uncol-

\footnotesize{\textsuperscript{288} Lyon, 239 A.2d at 820-21.


\textsuperscript{290} See *Spurlin*, 454 S.W.2d 354, 357 (Ky. Ct. App. 1970) (citing *Spurlin* with approval).

\textsuperscript{291} See *U.C.C.* § 9-104(f) & cmt. 6.

\textsuperscript{292} Id. See Ford, 22 Okla L. Rev. at 426 (cited in note 112) (stating: “The real question the court should be considering is whether this assignment is one which serves a valid financing purpose. Has the assignment enabled the retailer to obtain or retain money advanced by another to aid his business? If it has, it is a financial transaction and belongs within Article 9.”). See generally notes 245 and 256 and accompanying text.
lectible altogether. In contrast, the outright buyer of accounts parts with cold cash that flows directly into the assignor's estate. It seems odd in these circumstances to favor the former transferee over the latter. That, however, is precisely the effect of the 1972 amendment to Section 9-104(f).

In some respects, the added language is clear. The assignee must have received only "a single account" if she wants to get outside the Code ballpark; three (or even two) accounts and you're in.293 Moreover, "preexisting debt" means "preexisting debt"; simultaneity in creating the debt and making the assignment knocks the transaction out of Section 9-104(f).294

Can financial institution lenders take advantage of the satisfaction-of-a-preexisting-debt exemption? Not according to the court in Bank of Cave Spring v. Gold Kist, Inc.295 This decision is wrong. As with Section 9-302(1)(e), not a kernel of statutory language justifies distinguishing between professional and nonprofessional lenders in applying the preexisting-debt exclusion.296 Either an assignment is "in whole or partial satisfaction of a preexisting indebtedness" or it isn't; the business address of the assignee holding the indebtedness should have nothing to do with this inquiry. As a practical matter, however, it will count with some courts.297

293. See, for example, Vacation Trust, 724 P.2d at 745 (stating that exception is inapplicable if assignor transfers more than one account to assignee).
294. For example, the court in Cripps stated:
   "The facts in Sloan are clearly distinguishable from the case at bar. Sloan dealt with the assignment of monies owed in satisfaction of a preexisting debt. We are dealing in the instant case with a sale of accounts for value received. 31 Bankr. at 544. See also York, 412 F. Supp. at 823 (holding preexisting indebtedness exclusion unavailable because assignment was made "to secure the loan simultaneously advanced"); Clark, The Law of Secured Transactions ¶ 1.04 at 1-25 (cited in note 8) (stating that "[i]f the transaction involves the sale of a single account for new value rather than in satisfaction of an antecedent debt, the buyer loses in the seller's bankruptcy if he has not filed a financing statement")."
31 Bankr. at 544. See also York, 412 F. Supp. at 823 (holding preexisting indebtedness exclusion unavailable because assignment was made "to secure the loan simultaneously advanced"); Clark, The Law of Secured Transactions ¶ 1.04 at 1-25 (cited in note 8) (stating that "[i]f the transaction involves the sale of a single account for new value rather than in satisfaction of an antecedent debt, the buyer loses in the seller's bankruptcy if he has not filed a financing statement").

In Vacation Trust, the court confronted a case in which the assignor transferred a single $250,000 account, but designated only $129,000 of it to satisfy a preexisting debt, with the remaining $121,000 to secure future advances. 724 P.2d at 739. The court concluded that the entire assignment fell outside the Code because of the preexisting-debt exclusion (although it subordinated the assignee's claim to at least a portion of the $121,000 account proceeds on other grounds). Id. at 745-46. The court's reasoning was that the assignee received only one assignment and that this assignment was taken (to the tune of $129,000) in satisfaction of a preexisting debt. Id.

The Vacation Trust court's reasoning seems simultaneously too technical and too metaphysical. The practical financial fact was that only $129,000 of the assignor's corpus of accounts was transferred in satisfaction of a preexisting debt. One wonders whether the court would have reached the same result (which, as a matter of logic and principle, it would seem bound to do) if the preexisting portion of the assignor's debt had been $1000 or $1.29.
296. See notes 174-82 and accompanying text.
297. See Sherburne Corp., 340 A.2d at 86 (distinguishing Lyon in bank-assignee case on ground that "the assignment in Lyon was between relatives"); Valley Bank of Nev., 528 F. Supp.
The trickiest problem presented by Section 9-104(f) is determining whether the account transfer is in “satisfaction” of a preexisting debt. One interpretive difficulty is suggested by Case G.

Case G. On Day 1, Freddy Friend knocks on Molly McDelinquent’s door and complains that she still owes him a $5,000 debt. Molly explains that she soon will receive payment on the one and only account she holds and dashes off a note that reads: “I assign to Freddy Friend, as security for my $5,000 debt to him, the account now owed me by Barney Beefbuyer, payable later this month.” On Day 2, Second Assignee Bank obtains, and perfects by filing, a security interest in all of Molly’s accounts as part of a loan transaction. Molly thereafter defaults on her debts, and Barney Beefbuyer wants to know whether to pay Freddy or Second Assignee Bank.

On these facts, Freddy did not achieve automatic perfection under Section 9-302(1)(e) because Molly transferred to him all her then-outstanding accounts. It follows that, if the Code covers that assignment, Freddy will lose under the first-to-file rule of 9-312(5). Freddy’s only chance is to jump outside the Code through the escape hatch of Section 9-104(f).

Freddy’s argument is that he received “a transfer of a single account . . . in whole or partial satisfaction of a preexisting indebtedness.” One can imagine the response of counsel for Second Assignee Bank. She will say, almost verbatim: “Come on, Freddy. You didn’t get any ‘satisfaction’ of that debt. You only got some security for it.” The Bank’s counsel will note that the Code language relied on by Freddy was designed to codify Spurlin and Lyon, and that the courts in both those cases deemed critical the difference between absolute and security assignments. The Bank’s attorney will go on to cite authority that suggests that all the Section 9-104(f) exclusions apply only to absolute transfers. If the Bank’s counsel is really on her toes, she also will observe that the Code itself, in another context, differentiates between “security for” and “total or partial satisfaction of” a preexisting claim. The inference thus is strong that the drafters of Section 9-
104(f) saw providing “security” and providing “satisfaction” as different colored horses, and that Freddy is trying to ride the wrong one into the regions of non-Code law.\footnote{205}

Perhaps, however, things are not so simple. One fly in the ointment is Lyon. As we have seen already, some analysts assert that the assignments at issue in Lyon were made solely as security.\footnote{206} Thus, because the 1972 Code Comment says that the transactions involved in Spurlin and Lyon fall outside the Code, one might infer that the 1972 exclusion covers security transfers.\footnote{207} In a similar vein, when the satisfaction-of-a-preexisting-indebtedness exclusion was put forward in the Permanent Editorial Board’s Final Report, the following proposed new Comment accompanied it: “[T]his paragraph excludes from the Article such transactions as that involved in In re Panama Airways, Inc. . . . , where an unliquidated single receivable from a customer was transferred to the supplier to secure the related debts.”\footnote{208}

Do these spicy morsels of legislative history establish that a transfer of a single account as security for a preexisting debt is in whole or partial satisfaction of that debt within the meaning of Section 9-104(f)? To the contrary. With respect to Lyon, the safer assumption is that the drafters of the 1972 Code Comment accepted the Lyon court’s own characterization of the assignments at issue in that case.\footnote{209} The court in Lyon ruled that the account transfers involved therein were “not for security,” and emphasized that the Code covers security assignments.\footnote{210} Lyon thus undermines, rather than supports, the view that the security transfer involved in Case G falls outside Article Nine.\footnote{211}

Freddy’s interpretive effort also gets no help from the drafters’ loose talk about Panama Airways because the proposed 1971 Comment that discussed that case never became the Official 1972 Comment. Indeed, the Official 1972 Comment dropped all mention of Panama Airways and of transfers “to secure . . . debts.” The deletion of this

\footnote{205. See First City Mortgage Co., 69 Bankr. at 768 (holding that transfer of accounts to bank to secure loan clearly not excluded by Section 9-104(f)); Valley Bank of Nev., 528 F. Supp. at 913 (refusing to follow Spurlin and Lyon in part because “assignments involved here were never intended to be outright transfers, but, rather, were intended to provide Valley Bank [the assignee] with collateral to secure its loan’’); Cohen, 364 A.2d at 861-82 (same).

206. See note 239 and accompanying text. See also Coogan, et al., Secured Transactions \S 3.08[2] at 3-49 (cited in note 8).

207. See Coogan, et al., Secured Transactions \S 3.08[3][a] at 3-52.


209. See notes 239-41 and accompanying text.

210. See Lyon, 239 A.2d at 820-21.

211. See, for example, Cohen, 364 A.2d at 861-82 (emphasizing distinction in Lyon rule between assignment “to satisfy a preexisting debt” and assignment “intended for security”).}
language, coupled with the Official Comment's approbation of only *Spurlin* and *Lyon*, sends a strong signal that the satisfaction-of-a-pre-existing-indebtedness exclusion does not embrace traditional security transfers. For all these reasons, courts properly have recognized that this aspect of Section 9-104(f) does not remove collateral assignments from the perfection and priority rules of Article Nine.\(^312\)

Of course, it remains necessary to explore what distinguishes a security assignment from a satisfaction assignment. The key interpretive issue is presented by Case H.

**Case H.** The facts are the same as in Case G except the paper signed by Molly McDelinquent reads: "I hereby absolutely and unconditionally assign to Freddy Friend, in payment of my $5,000 debt to him, the account now owed by Barney Beefbuyer, payable later this month. If Barney Beefbuyer fails to pay this account, however, *I shall remain fully liable for my debt.*"

The argument is strong that Case H, like Case G, involves a security transfer not excluded from the Code by Section 9-104(f). This is so because the account assignment, although absolute, does not satisfy Molly's debt in the ordinary sense: it does not discharge Molly's duty of performance.\(^313\)

Freddy will argue, nonetheless, that Molly's assignment in Case E involved no less a satisfaction of a debt than did the assignments in *Spurlin* and *Lyon*, which the drafters of the 1972 amendment sought to exclude from Code coverage. Freddy will point to the actual language of the assignments in the *Lyon* case, which gave no indication that they served to discharge the assignor's underlying debts.\(^314\) Freddy also will note the failure of the courts in both *Spurlin* and *Lyon* to state that the assignments did effect such a discharge.\(^315\) He will emphasize even more those courts' overriding focus on the proposition that the assignments were absolute and unqualified, and not on the proposition that the assignments effected a discharge.\(^316\)

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\(^312\) See note 305.

\(^313\) See *Ballentine's Law Dictionary* 1139 (3d ed. 1969) (defining "satisfaction" as "[t]he discharge of an obligation"). See also *Geeslin v. Blackhawk Heating & Plumbing Co.*, 398 N.E.2d 1176, 1181 (Ill. Ct. App. 1979) (stating that "assignment was made to pay a debt, not to secure one" because assignment discharged the debt and provided full satisfaction).

\(^314\) *Lyon*, 239 A.2d at 821.

\(^315\) No such indication appears in *Lyon*. One student author asserts that the assignee in *Spurlin* "did not have recourse to [the assignor] if the account was not paid." *Ford*, 22 Okla. L. Rev. at 428 (cited in note 112). The opinion in the case, however, nowhere states that such an agreement was in place. The payments pursuant to the assignment—and not the assignor's action simply in assigning his rights—were necessary to "settle his accounts" under the parties' agreement. *Spurlin*, 368 S.W.2d at 315.

\(^316\) *Lyon*, 239 A.3d at 821 (stating that "the absolute and unqualified language of the as-
There is, on the other hand, a basis to argue that the Lyon and Spurlin courts viewed the transactions in those cases as involving satisfaction of the antecedent debts in the pure sense of providing a discharge. In particular, both courts referred to the assignments as being in "payment" of the preexisting debts, and the term "payment" often is used as a synonym for "satisfaction" or "discharge." Of no less importance, both courts reasoned that the assignments at issue did not involve collateral-type Article Nine security interests. It is hard to say, however, that those assignments did anything more than "secure payment" of an underlying "obligation" if the obligation persisted even after the assignment was made.

Freddy's life also is complicated by Panama Airways, which involved precisely the type of "you may collect from my account debtor but I'm not discharged" assignment presented in Case H. As already noted, the authors of the 1971 proposed Comment described the transaction in Panama Airways as a security transfer, and the authors of the 1972 Comments chose not to cite this case as a proper example of the satisfaction-of-a-preexisting-debt exclusion. This legislative history, the bank will argue, cuts against applying that exclusion to the transfer to Freddy in Case H. Finally, the Bank will say that the preexisting-indebtedness exclusion is so questionable in the first place that it
should be construed narrowly so as not to extend to Case H.\textsuperscript{325}

The authorities point in both directions on the question presented by Case H.\textsuperscript{326} On balance, however, Freddy should win on the ground that absolute assignments made as the primary (albeit not exclusive) source of payment of preexisting loans fall within the preexisting-indebtedness exclusion of Section 9-104(f). This result will shock some Article Nine purists, who surely will view Case H as involving a security transfer that functionally involves no satisfaction of the underlying debt at all. The term “satisfaction,” however, is not self-defining; it permits a distinction between account transfers designed to provide the primary source of payment (despite the presence of an additional conditional right to proceed against the assignor if the accounts prove uncollectible) and transfers of accounts as pure collateral (because they are subject to collection only if and when the debtor defaults on payment obligations). The adoption of this distinction, however dubious as a matter of policy, is simply the fairer reading of the critical Spurlin and Lyon cases, both of which focused not on whether the preexisting obligation persisted, but on whether the assignment was absolute and unconditional in character.\textsuperscript{327}

325. See note 292 and accompanying text.

326. Compare Goldstein, 807 F.2d at 1074 (suggesting that the key inquiry is “whether the assignment by [assignor] was an absolute assignment”); Valley Bank of Nev., 528 F. Supp. at 913 n.8; Feldman, 408 F. Supp. at 38 (suggesting that assignment of account “to facilitate direct payment” is “exempt from the provisions of Article Nine”) (citing Lyon); Consolidated Film Indus., 403 F. Supp. at 1282 (stating that the “assignment of a contract right in consequence of a past-due obligation . . . is within the spirit of the § 9-104(f) exceptions”); Vacation Trust, 724 P.2d at 745-46; with Rankin, 102 Bankr. at 445; Fort Dodge Roofing Co., 50 Bankr. at 698 (stating “After the assignment was made, Stetson did not adjust its books to decrease the amount owed to it by Fort Dodge Roofing and in fact claimed that after the transfer was made, Fort Dodge Roofing was still indebted to it in the amount of $170,000. . . . Therefore, the Court concludes that even though Stetson acted as the owner of the account, the transfer was in reality merely a transfer of a security interest in the accounts rather than an outright transfer of the ownership to Stetson”); Miller, 406 F. Supp. at 477 n.25 (stating “The defendant’s contention may be correct that assignments which are meant to effect payment in themselves and not merely to provide security are not controlled by the UCC. . . . Nevertheless, there is no evidence to show that the assignment alleged here was so intended. To the contrary, it stretches credibility to assert that AIBC’s debt to the New York Bank on the first loan was extinguished on May 3 by virtue of the contract right assignment; had the defendant not received repayment on November 2, it seems at least as likely that it would have sought payment from AIBC on its promissory note as from the Swiss Bank on the assignment.”); E. Turgeon Constr. Co., 292 A.2d at 234 (refusing to apply Spurlin principle because assignee failed to “show that once the assignment had been made, it had reduced the balance due,” and concluding that “[t]his failure . . . shows that [the assignee] regarded the retainage as security and not payment”).

327. See notes 314-16 and accompanying text.
6. Section 9-104(f) and Successive-Assignment Priority Problems

The determination that Section 9-104(f) applies to an account assignment merely sets the stage for resolving the parties' priority dispute. Section 9-104(f), after all, is not a priority provision; it is a scope provision that excludes certain types of transactions from Article Nine altogether. The Code's basic priority rule for conflicting account transfers is the first-to-file rule of Section 9-312. That rule obviously does not apply to a priority dispute between two account assignees who are both excluded from the Code by Section 9-104(f). Moreover, non-Code common law generally governs those cases that have "one leg inside... and one leg out" of the Code. We shall soon see that Code priority rules continue to govern unusual cases involving Section 9-104(f). Let us begin, however, by looking to the ordinary case, which the common law controls.


When Section 9-104(f) pushes the priority dispute outside Article Nine, how should the court fix the non-Code rule that controls the case? One response is to say that the court should simply scout pre-Code common law to find whether the state follows the New York, Eng-

328. See, for example, Charter First Mortgage, 56 Bankr. at 846 (suggesting that, even if transferee has been assigned an account excluded by the performance-and-payment rule of Section 9-104(f), "[t]hat section does not wipe out the [previously perfected] security interest a creditor, for financing purposes, as here, might have already taken in the contract"). Of course, the applicability of Section 9-104(f) to an account transfer may also have an important impact outside the priorities context. Paul, 343 A.2d at 626 (refusing to apply Section 9-318(4), which invalidates prohibition on account assignments, to accounts excluded from Article Nine by Section 9-104).


330. See notes 85-92 and accompanying text.

331. See Zubrow, 68 Minn. L. Rev. at 908-11 (cited in note 75).

332. See, for example, Coogan, et al., Secured Transactions § 3.08[1][c] at 3-48 (cited in note 8) (noting that Section 9-104(f) excludes those accounts from Code rules of "attachment, priority and default as well as perfection"); Parnsworth, Parnsworth on Contracts § 11.9 at 129 (cited in note 8) (stating that "an assignment of an account that is excluded...is left to the conflicting common law rules on priority"); Consolidated Film Indus., 403 F. Supp. at 1281 (stating that assignee "claims that [its interest] does not constitute a security interest, and that, consequently, common law priority rules govern"); Gilmore, Security Interests in Personal Property § 8.7 at 277 n.15 (cited in note 2) (stating that with respect to accounts receivable statutes, "[m]ost courts assumed that a claim or chose not within the statute continued to be governed by the pre-statutory common law...[which] would seem to have been the only possible conclusion"). Compare American East India Corp., 400 F. Supp. at 162-65 (finding it "a difficult question of interpretation which we need not resolve" whether common law governs a priority dispute between an "Article Nine secured party" and a "section 9-104(f) performing assignee, but observing that there is a "reasonable argument" that the common law governs).

333. See notes 351-404 and accompanying text.
lish, or Massachusetts four-horseman rule. Some courts have done just that. This approach, however, fails to recognize that the Code, to use a now-popular metaphor, has “change[d] the space” in which non-Code law is to be found.

334. See generally notes 37-47 and accompanying text. A good discussion of the common-law authorities appears in Corbin, Corbin on Contracts § 902 at 614-20 (cited in note 6), including the accompanying supplementary materials. The West Key Number under which these cases are collected is Assignments #88.


336. Laurence H. Tribe, The Curvature of Constitutional Space: What Lawyers Can Learn From Modern Physics, 103 Harv. L. Rev. 1, 4 (1989) (emphasis omitted). The Code’s existence can shape the nature and scope of common-law rules. See, for example, Farnsworth, Farnsworth on Contracts § 11.2 at 67 (cited in note 8) (noting that even when Code provisions exclude account transactions from Code coverage “it can be expected to have an impact by analogy”); Clark, The Law of Secured Transactions ¶ 1.08[12] at 1-126 (cited in note 8) (same); Axelrod, 14 U. Dayton L. Rev. at 300 (cited in note 1) (noting Florida court’s reliance in part on Code’s notice-filing system in opting for first-to-notify English rule as most proper common-law rule). An interesting example of the influence of the Code on non-Code law is provided by American East India Corp. In that case, B filed a financing statement perfecting a floating lien covering all of A’s after-acquired accounts; A then contracted with D to deliver goods to D for money and then assigned A’s rights and delegated A’s duties under that contract to C. 400 F. Supp. at 148-54. The court assumed that New York common law governed the priority dispute between B, as an Article Nine security interest holder, and C, as a Section 9-104(f) performance-and-payment transferee. Id. at 155 n.7. The court also accepted C’s argument that pre-Code New York common law would have treated the interest assignment to C as legal (because the A-D contract existed at the time of the assignment to C) and the assignment to B as equitable (because the A-D contract did not yet exist at the time of the assignment to B). Id. at 163. The court further assumed that, under pre-Code common law, B’s legal interest would defeat A’s earlier claim. Id. at 163-64. Following the teaching of Section 9-204 and its accompanying Official Comment, however, the court found that B’s security interest in after-acquired accounts was “not merely an ‘equitable’ interest” in light of the enactment of the Code. Id. at 164. Therefore, in a Code world, the assignments to both B and C were legal, so that B took priority under the New York first-in-time rule. Id. at 165.

An important question concerning the interaction of Code and non-Code law is whether a Section 9-104(f) assignee should take priority if that assignee is the first filer of a U.C.C. financing statement. The Code exempts the Section 9-104(f) assignee from filing, and no provision of the Code awards the Section 9-104(f) assignee priority when that assignee is the first filer. Under some applications of the common-law rules, the later-filing Article Nine secured party might take priority. For example, in an English rule jurisdiction if, notwithstanding the Section 9-104(f) claimant’s first filing, the Article Nine secured party first informed the account debtor of that later assignment, the second-filing secured party takes priority. The better view is that the first-filing Section 9-104(f) transferee should always take priority over the second-filing Article Nine secured party. After all, the Article Nine secured party should be expected to check the U.C.C. files. The Section 9-104(f) assignee’s filing, albeit gratuitous, provides the type of notice that properly should avert the second transfer altogether. In sum, a rule favoring the first-filing claimant under Section 9-104(f) best adapts the common law to the practical realities of a Code-dominated commercial world. See Comment, U.C.C. Section 9-301(1) and Accounts, Contract Rights and Chattel Paper: The Non-Existential Priorities?, 41 Wash. L. Rev. 895, 905 (1966) (stating that “[t]he more reasonable analysis . . . is that section 9-104(f) was not intended to deny priorities that might otherwise
Prior to the Code, for example, New York gave priority to the first assignee under any and all circumstances. The underlying rationale for this rule was that by "the first assignment the assignor had divested himself of all it had, so that nothing remained for it to transfer by a second assignment." As we have seen already, the Code repudiates this vision of the universe by routinely permitting the assignee of an already-transferred account to prevail so long as that claimant files first. In addition, the first-assignee rule may have persisted in New York in part because it best served the interests of the commercial factoring and accounts financing industries centered in that state. Today, however, the Code and its filing rules govern virtually all assignments to commercial financers, so that any such reason for applying the New York rule even in New York has disappeared. In such an environment, should New York courts mechanically favor the first assignee in a priority dispute governed by non-Code law? Of course not.

In a similar vein, prior to the Code many states followed the English practice of awarding priority to the first account assignee that provided notice to the account debtor. The theory behind this rule was that prospective assignees could and would check with account debtors to learn of prior assignments so as to avoid giving value for already-transferred accounts. Today, however, the Code requires assignees of most accounts to give notice via the U.C.C. filing system, so that prospective account transferees protect themselves not by contacting each of the assignor's account debtors, but by checking the Article Nine

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337. See notes 37-38 and accompanying text.
338. Farnsworth, Farnsworth on Contracts § 11.9 at 121 (cited in note 8).
339. See notes 91-112 and accompanying text.
340. See Gilmore, Security Interests in Personal Property § 25.6 at 671 (cited in note 2) (noting that the New York rule guaranteed "a happy life" for assignees who could be sure no prior assignments had occurred).
341. See notes 61-80 and accompanying text.
342. See New York Law Revision Commission, Communication and Study Relating to Assignments of Accounts Receivable 8 (1946) (reprinted in New York Law Revision Commission, 1946 Report Recommendations and Studies 351, 356 (Williams, 1946)). The Commission indicated a preference for retaining the first-in-time rule and expressed concern that a notice requirement would impose hardship on assignors by giving "an erroneous and unfavorable impression of the assignor's financial position." Id. It also noted that "[i]n the future, when the practice of borrowing upon the security of accounts receivable has become more widespread and the tendency to regard it as an indication of financial difficulty has been overcome, the Commission may resume study of the topic." Id.
343. For a discussion of the English rule, see notes 39-40 and accompanying text.
344. See Axelrod, 14 U. Dayton L. Rev. at 297 (cited in note 1); Corbin, Corbin on Contracts § 901 at 608 (cited in note 6) (stating that "[i]f . . . the owner has notice of the assignment, any subsequent assignee can avoid loss by making inquiry of the owner").
345. See notes 91-111 and accompanying text.
records. As a result, the policies that once supported the English rule carry limited force in the modern setting.\(^{346}\)

This analysis suggests that, in a Code-dominated world, the Restatement's four-horsemen rule seems preferable to either the New York or English approaches. That rule generally grants priority to the first assignee. There is some sense in this approach because a first assignee, unlike subsequent ones, cannot even possibly discover any competing assignment. At the same time, the four-horsemen rule smooths the roughest edges of the New York rule by granting priority to the second assignee who has invested the energy necessary to reduce the account to judgment or reached that heightened level of expectancy induced by securing a novation or payment.\(^{347}\)

Of course, courts that now labor in the fields of Code-era common law need not follow any of these three rules. There may be good reason to forge a new and improved common-law principle to govern the narrowed and distinctive set of common-law priority conflicts generated by Section 9-104(f). One candidate for a better approach would be to afford more protection to nonprofessional, than professional, account assignees. The specifics of, and reasons for, such a rule will be developed in short order.\(^{348}\) For now, suffice it to say that such an approach would track the recurring instinct of the courts.\(^{349}\)

Whatever common-law priority rule covers Section 9-104(f) accounts, that rule will produce departures from the first-to-file principle that generally governs successive-assignment cases.\(^{350}\) In some Section 9-104(f) cases the first filer will prevail. The first filer, however, will win not because she was the first filer, but because she fits into some other

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346. Prior to promulgation of the Code, some businesses opposed the first-to-notify rule on the ground that "account debtors would interpret [an] assignment as an indication of financial weakness." Scult, 11 Ariz. L. Rev. at 3 n.15 (cited in note 19); In accord, Coleman, 1963 U. Ill. L. Forum at 266 n.35 (cited in note 2). This justification—whether or not sensible in the first place—has no application in the modern commercial setting. Today, account assignments are widespread, are typically filed under the U.C.C., and are recognized as an orthodox and acceptable manner of generating current funds. The traditional objection to the first-to-notify rule thus no longer pertains.

347. See notes 41-43 and accompanying text. See, for example, Restatement (Second) of Contracts, § 342 cmt. e (1979) (explaining four-horsemen rule as reflecting "the interest of the security of transaction"); Corbin, Corbin on Contracts § 902 at 618 (cited in note 6) (citing heightened claim of second assignee to "money that he has innocently collected by the exercise of diligence and effort"); Richard E. Speidel, "Stakeholder" Payments Under Federal Construction Contracts: Payment Bond Surety vs. Assignee, 47 Va. L. Rev. 640, 653 (1961) (citing possibility that "assignee . . . has relied upon the finality of payments actually received" in arguing against construction surety's claim to contract proceeds already paid out to a financier assignee of the general contractor by the project owner).

348. See notes 601-30 and accompanying text.

349. See notes 548-52 and accompanying text.

350. See notes 85-92 and accompanying text.
legal pigeonhole—such as by being the first assignee, or the first assignee to inform the account debtor of the assignment, or the first assignee to reduce the assignment to judgment. Because Section 9-104(f) subjects many account priority disputes to resolution under the common law, it creates a large, but indeterminate, exception to the Code's general first-to-file rule.

We turn now to exploring some important ways in which the Code shapes the exception to the first-to-file rule applicable to Section 9-104(f) accounts.

b. The Direct Impact of the Code on Section 9-104(f) Priority Disputes

The foregoing discussion suggests that the Code should help shape common-law priority rules applicable to Section 9-104(f) account transfers by forcing a reassessment of the underlying justifications for traditional common-law approaches. It may be that the Code also directly dictates rules that control at least some priority conflicts concerning Section 9-104(f) accounts. One set of disputes that the Code may continue to govern is illustrated by Case I.

CASE I. On January 1, Harold Housepainter transfers six overdue accounts, which constitute seventy-five percent of Harold’s then-existing account holdings, to Alice Attorney. Alice and Harold agree that Alice will use her best efforts to effect collections and pay to Harold sixty percent of all collections made on the accounts. On January 10, Harold gives Second Assignee Bank a security interest in all his accounts, including those overdue accounts already assigned to Alice, as collateral for a $5000 loan. The bank immediately files a U.C.C. financing statement and informs all of Harold’s account debtors of this assignment. Although Alice has initiated work on the collection actions by January 10, she has neither filed a U.C.C. financing statement nor notified any account debtor. If the jurisdiction in which these events occur follows the English first-notice-to-the-obligor rule, does Alice or the Bank have priority to the overdue accounts?

At first blush, the answer to this problem seems obvious. Because Alice received a Section 9-104(f) assignment (for collection purposes only), the Code does not govern her priority dispute with the Bank. The applicable common-law rule in this jurisdiction is that the first notifier wins, and in this case the Bank provided the first notice. As a

351. See notes 248-64 and accompanying text.
352. See note 332 and accompanying text.
result, the Bank takes priority under non-Code law.\textsuperscript{353}

But wait. Even though the Code does not apply to Alice’s assignment,\textsuperscript{354} she will advance a syllogistic argument for priority under the Code itself. The argument goes like this:

\textit{Major premise:} Alice would have defeated the Bank if she promptly had filed an Article Nine financing statement on January 1. This is so, Alice will argue, because, although Alice’s transfer was not technically governed by the Code at all, it would be anomalous to give priority to a second transferee and second filer just because its interest in the accounts was subject to the Code.\textsuperscript{355}

\textit{Minor Premise:} The purpose of Section 9-104(f) is to ensure that persons who come within that provision are not prejudiced by not filing.\textsuperscript{356}

\textit{Conclusion:} Alice should win even though she failed to file; otherwise she would be prejudiced by not filing in derogation of the purpose of Section 9-104(f).

The plausibility of Alice’s syllogism negates the suggestion that the Code is out of the picture in determining all priority disputes involving Section 9-104(f) assignments. Indeed, if Alice’s argument is accepted, the Code—via Section 9-104(f)—precludes application of the English rule and mandates priority for every assignee who receives a Section 9-104(f) transfer before a competing transferee records a financing statement.

Is Alice’s interpretation of Section 9-104(f) proper? It is not. There is no indication that the section’s drafters had cases like Case I in mind or meant the section to establish a rule of successive-assignment priorities. Rather, the sole pronouncement of Section 9-104(f) is that the Code “does not apply” to the assignments enumerated in that section.\textsuperscript{357} The practical effect of Alice’s syllogism is to treat Section 9-104(f) transfers as automatically filed and thus automatically perfected. The Code’s drafters, however, provided for automatic perfection of account transfers in Section 9-302(1)(e) and (g) and not in Section 9-
104(f). As we have seen, there is good reason to scrap the English rule in crafting the modern common law of successive assignments. These considerations establish, however, that Section 9-104(f) does not mandate that result.

There is another important way in which the Code might settle priority disputes that involve Section 9-104(f). Consider Case J:

**CASE J.** On January 1, The Bobo Bush and Bamboo Shoppe, Ltd. assigned all its accounts to First Assignee Bank as security for a loan. By February 1, some of the accounts had become overdue. As a result, on February 1, Bobo transferred the overdue accounts to Cueball Collection Agency, which knew nothing of the prior assignment, in return for Cueball’s promise to use its best efforts to collect the accounts and remit fifty percent of all collections to Bobo. On March 1, the Bank filed its financing statement. In a jurisdiction that follows the New York first-in-time rule, who has priority to the overdue accounts, Cueball Collection Agency or First Assignee Bank?

A court might well assume that Article Nine is irrelevant to this problem under the one-leg-in-and-one-leg-out rule generally applicable to Section 9-104(f) assignments. Following this analysis, the bank wins Case J because it was the first assignee in a New York rule jurisdiction. Relying on “Alice’s syllogism,” Cueball will argue that Section 9-104(f) grants it priority by way of an attributed first filing on February 1. As we have seen, however, courts should reject this argument. Even so, Cueball may not be out of luck, for an alternative analysis under the Code may well protect its interest. Behold U.C.C. Section 9-301(1)(d):

[A]n unperfected security interest is subordinate to the rights of, . . . in the case of accounts and general intangibles, a person who is not a secured party and who is a transferee to the extent that he gives value without knowledge of the security interest and before it is perfected.

By its terms Section 9-301(1)(d) fits Case J. First Assignee Bank held an unperfected security interest in accounts, and before the bank perfected by filing on March 1, Cueball Collection Agency gave value for

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358. See notes 113-14 and accompanying text. To the extent that the drafters of Section 9-104 had priority disputes in mind, they may have planned nothing more than to ensure that the Section 9-104(f) transferee was protected against the bankruptcy trustee.
359. See notes 343-46 and accompanying text.
360. U.C.C. § 9-104(f).
361. See note 332 and accompanying text.
362. See notes 37-38 and accompanying text.
363. See notes 357-59 and accompanying text.
364. U.C.C. § 9-301(1)(d).
the same accounts without knowledge of the security interest. Finally, under Code Sections 1-201(37), 9-105, and 9-104(f), Cueball Collection Agency is not a secured party. In other words, Cueball's interest takes priority under Section 9-301(1)(d) of Article Nine because its interest is not subject to Article Nine due to Section 9-104(f).

First Assignee Bank will not roll over when Cueball advances this contention. The Bank will declare it nonsensical that Section 9-301(1)(f) states a priority rule governing an account transfer to which Article Nine does not apply. The only sensible interpretation of Section 9-301(1)(f), First Assignee Bank will continue, is that it protects transferees other than those excluded altogether from Code coverage by Section 9-104. There is, however, a profound difficulty with this argument. No person other than the transferee described in Section 9-104(f) could, in the case of accounts, be a transferee who gives value and yet not be a secured party. The Code, after all, treats all outright and collateral transferees of accounts as secured parties with the sole exception of those transferees covered by Section 9-104. In other words, under First Assignee Bank’s interpretation of Section 9-301(1)(d), that section cannot protect any account transferee notwithstanding the section’s express coverage of account transferees.

365. See id. § 1-201(44)(d) (defining “value”).
366. Id. § 9-301(1)(d). See also id. § 1-201(25) (defining “knowledge”).
367. See id. § 9-105(m). See also id. § 9-102(1)(b).
368. See id. § 1-201(37).
369. See id. § 9-104(f) (identifying account transfers, including those “for collection purposes only,” to which Article Nine does not apply). Contrast O’Leary, 29 Mo. L. Rev. at 496 (cited in note 19) (suggesting that Section 9-301 creates exception to first-to-file rule). See generally Comment, 41 Wash. L. Rev. at 898 (cited in note 336).
370. See Goldstein, 807 F.2d at 1073 (stating that “Section 104(f) of Article 9 excludes certain transactions from Article 9’s scope. If the transaction at issue is excluded, it would be odd indeed for Article 9’s choice of law provision to apply.”). Comment, 41 Wash. L. Rev. at 898 (finding it probable that Section 9-301 does not work “in favor of ‘9-104(f) buyers’ ” because the Code provides “that no provision of article 9 applies to transactions described in section 9-104(f)”). The Bank will further observe that when the Code’s drafters did want Code priority rules to apply to transactions otherwise excluded from the Code by Section 9-104, they provided for that result. See U.C.C. § 9-104(f), (g).
371. The same interpretive problem is presented with respect to Section 9-301(1)(c)”s treatment of chattel paper. See Comment, 41 Wash. L. Rev. at 896.
372. To tamper a bit with the observations in Comment, 41 Wash. L. Rev. at 902: “Since any sale of [accounts] creates a security interest in the buyer, except as provided in section 9-104(f); the very language of subsection [(1)(d)] of this section prohibits its operation in favor of buyers of [accounts] except buyers whose interests arise in sales described in section 9-104(f).”
373. See notes 220-23 and accompanying text.
374. One possible response to this argument is that the lien creditor is a transferee of accounts who is not a secured party within the meaning of Section 9-301(1)(d). This interpretation, however, presents too many problems to be taken seriously. First, U.C.C. Section 9-301(1)(b) deals specifically with the protection of lien creditors; to read Section 9-301(1)(d) as defining the rights
Can Section 9-301(1)(d) be construed to give some significance to the word “accounts” without dictating a priority rule for Section 9-104(f) assignments? Professor Clark says yes. In his view, the drafters meant for Section 9-301(1)(d) to protect outright buyers of accounts, as opposed to persons who take account assignments as collateral. After all, Section 9-301 otherwise protects just such buyers of goods, instruments, documents, and general intangibles in subsection 1(d) and its companion provision, 1(c). Thus, according to Professor Clark, buyers of accounts are not secured parties under Section 9-301(1)(d) and, accordingly, merit priority under that section over any collateral transferee that has not yet perfected its interest as of the time of the purchase.

The problem with Professor Clark's interpretation is that it flatly contradicts the Code's definitional edict that the term “secured party” includes any “person to whom accounts . . . have been sold.” It also contradicts the Code's reiteration of this definitional point in at least two additional Code sections and five Code Comments. Finally, Professor Clark's interpretation contradicts the policy behind this defi-

of lien creditors would thus be anomalous and indeed inconsistent with Section 9-301(1)(b). Second, to say that a lien creditor gives value for purposes of Section 9-301(1)(d) is imprecise; the definition of giving value envisions a consensual exchange, see U.C.C. § 1-201(44), and the lien creditor does not secure its interest by way of such an exchange. Finally, the Official Comment makes clear that subsection 1(d) is designed to “deal with purchasers,” U.C.C. § 9-301 cmt. 4, and a lien creditor does not fit this description because such a transferee does not obtain its interest by way of a “voluntary transaction,” id. § 1-201(32). In accord, Mazer v. Williams Bros. Co., 337 A.2d 559, 562-63 (Pa. 1975).

Section 9-301(1)(d) cannot be read to protect lien creditors. Nor can it be read to protect such transferees of accounts as the beneficiaries of constructive trusts, for they are not purchasers who give value either. If the section protects any transferees of accounts at all, it must protect some subset of those persons who buy accounts or take them as security for a debt. One subset of such transferees is the class of Section 9-104(f) transferees.

375. Clark, The Law of Secured Transactions ¶ 3.03[4] at 3-28 to 3-29 (cited in note 8). In accord is Petron Trading Co., 663 F. Supp. at 1160-62. See also Coogan, et al., Secured Transactions ¶ 7B.03[6][b] at 7B-26 (cited in note 8) (indicating, without analysis of Section 9-301(1)(d)’s “not a secured party” interpretation, that if first-filing buyer of accounts “was aware of [earlier] unperfected interest it takes subject to it under Section 9-301(1)(d)”).

376. See also Cohen, 364 A.2d at 861 (suggesting that Section 9-301 affords priority to account transferee over earlier, but unperfected, transferee).

377. In particular, Section 9-301(1)(c) specifically undertakes to protect the buyer. See also Gilmore, Security Interests in Personal Property ¶ 12.6 at 384 (cited in note 2).


379. U.C.C. § 9-105(m).

380. See id. §§ 1-201(37), 9-105(1)(b).

381. Id. §§ 1-201 cmt. 37, 9-102 cmt., 9-104 cmt. 6, 9-105 cmt. 2, 9-302 cmt. 5. See also id. § 9-502 cmt. 2. As stated in Comment, 41 Wash. L. Rev. at 903 (cited in note 336): “Reading together sections 9-105(1)(i), 1-201(37), and 9-105(1)(b)[,] one concludes that the Code generally provides that buyers of accounts and contract rights are secured parties and, therefore, that their rights are not determined by reference to section 9-301(1)(d).”
nitional postulate: that "the distinction between a security transfer and a sale" of accounts is sufficiently "blurred" so that no effort should be made to divide these transfers into two different categories. Professor Clark's construction of Section 9-301(1)(d) is not indefensible. It should, however, be greeted with a healthy dose of skepticism.

On a more practical level, Professor Clark's interpretation of Section 9-301(1)(d) provides no help to First Assignee Bank in its efforts to win Case J. Cueball Collection Agency, after all, was not a collateral transferee of Bobo. Rather, because it took an absolute assignment of accounts, Cueball is in the very class of assignees Professor Clark would protect under Section 9-301(1)(d), and is entitled to priority due to First Assignee Bank's unperfected status at the time Cueball purchased the accounts. As a result, the Bank must find an interpretation of Section 9-301(1)(d) that protects neither Section 9-104(f) account transferees nor outright account purchasers. The only possibility is to argue that the section does not protect any account assignees at all.

In support of this interpretation, the Bank can point out that Section 9-301(1)(d) applies "in the case of accounts and general intangibles." Thus, interpreting Section 9-301(1)(d) not to protect account transferees does not render Section 9-301(1)(d) meaningless, for outright buyers of general intangibles can still claim the section's protections. The Bank will add that the Code's drafters tacked Section 9-301(1)(d) onto the Code late in the drafting process so as to extend the good-faith purchaser protection already afforded to nonsecured-party buyers of goods to deserving nonsecured-party buyers of intangibles. The Bank will say that, under these circumstances, it is not surprising that Section 9-301(1)(d) refers to both general in-

382 U.C.C. § 9-102 cmt. 2. See note 74 and accompanying text. See also Coogan and Gordon, 76 Harv. L. Rev. at 1532 & n.14 (cited in note 31) (noting that Article Nine, with only the one exception set forth in Sections 9-502(2) and 9-504(2), "does not distinguish between loans secured by... accounts... and sales of those items") (emphasis original); Henson, Handbook on Secured Transactions § 3-11 at 42 (cited in note 8) (stating that "[t]he only time when a difference between a sale and a security transfer of account is really material is on default").

383 It is possible that the Code's drafters simply goofed in their choice of language so that Professor Clark's position best captures their actual intent. Professor Clark can rely on that portion of Section 9-105(1) that provides that its definition of secured party applies "unless the context otherwise requires," U.C.C. § 9-105(1) (emphasis added). The context of Section 9-301, he might say, otherwise does require treating account buyers as secured parties, secured party status, particularly in light of the generalized focus on property buyers of various forms in subsections 9-301(c) and (d).

384 See notes 390-92 and accompanying text.

385 For more on the meaning of the term "general intangibles," see notes 502-25 and accompanying text.

386 Contrast note 509 and accompanying text.

387 See U.C.C. § 9-301 cmt. 4.
tangibles and accounts even though (as it turns out) no account transferees can claim the section's benefits.\textsuperscript{388}

We have, then, three possible views of Section 9-301(1)(d): (1) that the section protects those account assignees described in Section 9-104(f) even though that provision says that Article Nine does not apply to those assignees; (2) that the section protects the outright assignee by not treating him as a secured party even though the Code defines the term "secured party" to include the outright assignee; and (3) that the section protects no assignees of accounts, but only assignees of general intangibles, even though the section says that it applies "in the case of accounts or general intangibles."\textsuperscript{389} Which of these troublesome interpretations is the most tolerable?

The second view, advocated by Professor Clark, should be the first to go. Adoption of his construction requires the conclusion that the Code's framers committed a drafting error properly corrected by judicial interpretation.\textsuperscript{390} While such an approach may be proper in some situations, it seems inappropriate when other plausible interpretations are available. Moreover, this slip-of-the-pen theory is weakened by the drafters' well-evidenced recognition in other contexts that their own definition of the term "secured party" covers account buyers.\textsuperscript{391} Courts should accept at face value Section 9-301(1)(d)'s declaration that it protects only the transferee who is "not a secured party."\textsuperscript{392}

Of the remaining two interpretations, the better is the first one: Section 9-301(1)(d) protects Section 9-104(f) account transferees against unperfected secured creditors. It is conceivable that the drafters of the Code did not specifically contemplate that Section 9-301(1)(d) would operate in this manner. There is no strong evidence that the drafters had some other intent, however, and this approach—unlike the

\textsuperscript{388} See Comment, 41 Wash. L. Rev. at 896 (cited in note 336) (suggesting that this is a plausible interpretation).

\textsuperscript{389} A fourth possible interpretation is that Section 9-301(1)(d) protects all account buyers, whether in category 1 (i.e., excluded from the Code by Section 9-104(f)) or category 2 (i.e., included in the Code by Section 9-102(1)(b)). This construction, however, combines the interpretive difficulties of both interpretation #1 and interpretation #2.

\textsuperscript{390} See note 379 and accompanying text.

\textsuperscript{391} See notes 380-81 and accompanying text.

\textsuperscript{392} See notes 378-84 and accompanying text. See also U.C.C. § 9-301 cmt. 4 (stating that "[p]aragraphs (1)(c) and (1)(d) deal with purchasers (other than secured parties)"). Professor Clark's interpretation also is objectionable because it produces the anomalous result that the second transferee, who is the second to file, defeats the first transferee and first filer, so long as the first filing postdates the second assignment. This result is inconsistent with the drafters' plan to subject account transferees to the Code-filing rules. It also contradicts Section 9-312's declaration that it determines priorities among "conflicting security interests." U.C.C. § 9-312(5). Finally, this result is troubling because Section 9-301 reaffirms the protection afforded "persons entitled to priority under Section 9-312." U.C.C. § 9-301(1)(a).
removing alternative—does give significance to Section 9-301(1)(d)’s specific reference to “accounts.”

393. No less important, this interpretation comports with the underlying purpose of Section 9-301(1)(d). That purpose is to subordinate secured parties who delay in perfecting their interests to persons who, in the interim, give value for the property subject to the interest.

394. Section 9-104(f) transferees—including those who take an account transfer in satisfaction of a preexisting debt—do just that.

395. Finally, while it may seem odd to apply an Article Nine priority rule to a property transfer when Article Nine says it does not apply to such transfers, in reality it is not so odd at all. For example, it is fair to say that Article Nine does not apply to sales of goods, instruments, or general intangibles. In a number of sections, however, Article Nine deals with such transactions in fixing priority rules for Article Nine security interests. Nothing more than this type of incidental application of Article Nine is involved in applying Section 9-301(1)(d) to priority disputes involving accounts uncovered by the Code due to Section 9-104(f).

The bottom line is that Sections 9-104(f) and 9-301(1)(d) create a statutory exception to the first-to-file rule applicable to account transfers to which the Code otherwise does not apply. Under that exception, the bona fide Section 9-104(f) account purchaser takes priority over an earlier Article Nine assignee, so long as the Section 9-104(f) transferee receives her assignment before the competing claimant files.

A decision that Section 9-301(1)(d) applies to Section 9-104(f) accounts raises several additional interpretive difficulties. What if, for example, a court runs into Case K instead of Case J?

CASE K. The facts of Case J are unchanged except that Cueball Collection Agency had knowledge of the earlier, unperfected security interest held by First Assignee Bank when Cueball took its for-
collection-purposes-only assignment prior to First Assignee Bank's filing.

The question posed by Case K is simple enough. We just concluded that Cueball should win Case J under Section 9-301(1)(d) because Cueball took its for-collection-purposes-only assignment without knowledge of the earlier security interest. Does it follow that Cueball should lose Case K under Section 9-301(1)(d) because in that case it had such knowledge?

There is a temptation to say no. As our earlier discussion shows, Section 9-301(1)(d) is hardly a highlight in the history of Code drafting. While courts grudgingly might feel bound to give its direct command some meaning, they also might be reluctant to read its negative implication to create a binding rule. The better view is that courts should apply Section 9-301(1)(d) to penalize the knowing Cueball no less than they apply the section to protect the non-knowing Cueball. Courts called on to interpret analogous Code provisions have adhered to similar negative implications. This implication-based construction of Section 9-301(1)(d) is also sensible and fair, for there is little reason to favor the Section 9-104(f) account transferee who takes the Section 9-104(f) assignment with actual knowledge that a prior assignee already has taken an assignment of the same accounts.

From the conclusion that a Section 9-104(f) account assignee loses to a prior unperfected security interest if she had knowledge of it at the time of the assignment, it follows a fortiori that knowledge of a prior perfected security interest is also fatal to the Section 9-104(f) transferee’s claim. Section 9-301(1)(d) does not command this result, even (at least directly) by negative implication. A contrary result would be anomalous and untenable, however, given our analysis of Case K.

In sum, Section 9-301(1)(d) dictates successive assignment priority rules—that may well defeat the first filer—for some cases involving Sec-

400. See notes 364-99 and accompanying text. See also Petron Trading Co., 663 F. Supp. at 1160-81 (struggling with interpretation of Section 9-301(1)(d)).
401. Contrast American East India Corp., 400 F. Supp. at 162 & n.18 (noting, but not addressing apparent negative-implication argument that Section 9-104(f) account transferee is subordinate to previously perfected security interest under Section 9-301(1)(d)).
403. See, for example, Special Project, 62 Cornell L. Rev. at 944 (cited in note 12) (stating that, under Section 9-301(1)(c), “knowledge that a security interest exists is sufficient by itself to subordinate the buyer”).
404. Knowledge is irrelevant in fixing priorities between conflicting security interest holders. See note 95 and accompanying text. That rule, however, is designed to ensure early and prompt filings. Since the Section 9-104(f) transferee is not required to file at all, Code policy favoring a pure-race rule has little application. Each of the three traditional common-law rules would subordinate a second transferee who takes with actual knowledge of a prior assignment. See notes 37-43 and accompanying text.
tation 9-104(f) account transfers. Those rules, however, cover only two limited types of cases: (1) cases in which the Section 9-104(f) transferee takes the assignment without knowledge of an earlier, but unperfected, security interest (which the Section 9-104(f) transferee wins) and (2) cases in which the Section 9-104(f) transferee takes the assignment with actual knowledge of the prior security interest (which the Section 9-104(f) transferee loses). In all other cases, court-fashioned common-law principles will dictate the contours of the Section 9-104(f) exception to the first-to-file rule.

D. Exceptions Arising Under Section 1-103

Professors White and Summers describe Section 1-103 as "probably the most important single provision in the Code." That section states: "Unless displaced by the particular provisions of this Act, the principles of law and equity . . . shall supplement its provisions." In successive-assignment cases, Section 1-103 causes departures from the first-to-file rule in two basic ways. First, non-Code law may provide a defense to the first filer's claim of priority based on that party's conduct. For example, Section 1-103 carries into the Code the doctrines of estoppel and fraud. Thus, a first filer may forfeit priority if it misleads the second filer (or even a nonfiler) into giving value on the understanding that the first filer claims no interest. Other principles of law and equity may operate in similar fashion to generate a defense to the first filer's claim.

A second important set of exceptions to the first-to-file rule arises when—regardless of the first filer's actions—the second filer (or nonfiler) holds a claim to the account property other than or in addition to an Article Nine security interest. These cases usually involve

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405. White and Summers, Uniform Commercial Code § 5 at 19 (cited in note 8).
406. U.C.C. § 1-103.
407. Id.
408. See, for example, Petron Trading Co., 633 F. Supp. at 1163; AM Int'l, 46 Bankr. at 573 (stating that "[e]ven if CUB's consent does not amount to a contractual subordination agreement under the U.C.C., there are equitable reasons why AMI's interest in the payments is superior to CUB's"); Restatement (Second) of Contracts § 342 cmt. e (1979) (recognizing that first-filing assignee may be defeated by subsequent assignee if "there is an estoppel"). See generally Special Project, 62 Cornell L. Rev. at 857-58 (cited in note 12).
409. See, for example, Liles & Raymond, 24 Bankr. at 630 n.5 (holding that consensual discharge of perfected security interest results in subordination). For an extensive treatment of common-law-based exceptions to the first-to-file rule, including exceptions based on estoppel and fraud, see Hillman, et al., Common Law and Equity §§ 24.01 to 24.05 at 24-1 to 24-76 (cited in note 271).
410. See, for example, Consolidated Steel Corp., 11 U.C.C. Rep. Serv. at 410 (finding it unnecessary to reach claimant's arguments that it is "the third party beneficiary of the contract between the debtor and Wagoner and that its interest as a third party beneficiary is superior to
claims to payments owed for construction work made by a first-filing secured financier of a building contractor.\textsuperscript{411} We turn first to those cases that involve competing claims of suppliers or subcontractors, and then to those cases that concern the competing claims of construction sureties.

1. Suppliers and Subcontractors

Non-Code law sometimes protects the nonprofessional claimant of accounts against a first-filing financial institution assignee.\textsuperscript{412} One set of beneficiaries of these judicial rulings are suppliers and subcontractors on construction projects.\textsuperscript{413} Some courts have protected these claimants with favorable readings of non-Code statutory lien law.\textsuperscript{414} Other courts have favored subcontractors or suppliers on the theory that they hold the [assigned] claim of the debtor to the amount due on the contract price’); \textit{Jacobs v. Northeastern Corp.}, 206 A.2d 49, 55 (Pa. 1965) (stating that “[r]ights of subrogation, although growing out of a contractual setting and oftentimes articulated by the contract, do not depend for their existence on a grant in the contract, but are created by law to avoid injustice” and that “[i]nsubrogation rights are not ‘security interests’ within the meaning of Article 9”).

\textsuperscript{411} These cases arise because “[c]onstruction contracts customarily permit the owner to withhold a certain percentage of each progress payment, usually ten percent, until the contractor has completed the project to the owner’s satisfaction. This retainage is withheld to discourage abandonment by the contractor.” Ronald P. Friedberg, \textit{Note, Construction Sureties: Don’t Put All Your Eggs in the Equitable Subrogation Basket}, 41 Case W. Res. L. Rev. 305, 308 (1990). See, for example, \textit{Transamerica Ins. Co. v. Barnett Bank}, 540 So. 2d 113, 115 (Fla. 1989), in which the court stated that “[t]he first [term] is a contractual provision under which the owner retains a percentage of the progress payments for the purpose of curing or mitigating subsequent contractor default. The retainage is paid to the contractor upon satisfactory performance and/or payment, but neither the contractor nor its assignees or creditors have any claim on the funds until the contractor performs.”

\textsuperscript{412} The Code makes clear that non-Code law governs “a lien given by statute or other rule of law for services or materials.” U.C.C. § 9-104(c).

\textsuperscript{413} See generally Coogan, et al., \textit{Secured Transactions} § 4B.10[2] at 4B-54 (cited in note 8) (stating that “the secured lender will lose to the subcontractors [and] materialmen . . . to the extent progress payments or retainage is needed to cure the contractor’s breaches”).

\textsuperscript{414} For example, \textit{National Bank of Detroit v. Eames & Brown, Inc.}, 242 N.W.2d 412 (Mich. 1976) (giving priority to subcontractors and suppliers with statutory lien against monies payable to general contractor over bank, which did not provide funds for project giving rise to liens but nonetheless held a properly perfected floating security interest covering general contractor’s accounts); \textit{Panhandle Bank & Trust Co. v. Graybar Electric Co.}, 492 S.W.2d 76 (Tex. Civ. App. 1973) (relying on statutory and equitable grounds for according subcontractor’s materialman priority over bank); \textit{Caristo Constr. Corp. v. Diner’s Fin. Corp.}, 236 N.E.2d 461 (N.Y. Ct. App. 1968) (finding that, because construction funds were by statute a trust fund for payment of subcontractor and supplier, assignment of funds was subordinate). See also \textit{Southern Agency Co. v. LaSalle Cas. Co.}, 393 F.2d 907 (8th Cir. 1968) (holding assignee’s claim to insurance premium receivables unenforceable due to statute under which receivables constituted trust fund for insurance company). See generally Henson, \textit{Handbook on Secured Transactions} § 3-14 at 53 n.68 (cited in note 8) (noting that bank assignee’s interest in assigned funds may be subject to statutory liens in some states); Scult, 11 Ariz. L. Rev. at 10 n.54 (cited in note 19); Rudolph, 5 B.C. Indus. & Comm. L. Rev. at 257 (cited in note 30) (discussing New York and California statutes, which “illustrate a strong tendency to give labor and material suppliers a preferred position”).
an "equitable lien" against sums owed by the project owner or are beneficiaries of a "construction trust fund."\footnote{415}

Another important way in which courts favor suppliers and subcontractors over the first-filing financial institution is by invoking longstanding principles now codified in Sections 9-203 and 9-318 of the Code. An illustrative case is \textit{Himes v. Cameron County Construction Corp.},\footnote{416} which concerned a priority battle over construction-contract retainages between a general contractor's unpaid suppliers and its financing bank. The suppliers based their claim on the contract between the owner and the general contractor, which permitted the owner to withhold payments otherwise due the general contractor to satisfy claims for labor and materials. The bank relied on its perfected security interest, which covered "all moneys that are now or may hereafter become due and payable"\footnote{417} to the general contractor. The court ruled that priority went to the suppliers on the ground that the bank's security interest never attached to the retainages. The court reasoned that attachment of a security interest requires that the debtor—in this case, the general contractor—have "rights in the collateral."\footnote{418} On the facts, however, the general contractor never obtained rights in the retainages because the contract specifically permitted the owner to withhold the retainages from the contractor when suppliers remained unpaid.\footnote{419} A number of courts have used the same or similar reasoning to afford pri-

\footnote{415. See \textit{Chattanooga Brick \\& Tile}, 18 U.C.C. Rep. Serv. at 1066 (giving priority to equitable lien on retainage held by supplier over filed Article Nine security interest); \textit{United Parcel Serv., Inc. v. Weben Indus., Inc.}, 784 F.2d 1005 (5th Cir. 1986) (applying Georgia law and collecting numerous construction trust fund cases), rev'd 610 F. Supp. 13 (N.D. Tex. 1985) (refusing to recognize constructive trust held by subcontractor and thus giving priority to funds retained by owner to contractor's perfected accounts financer); \textit{In re Inca Materials, Inc.}, 880 F.2d 1307 (11th Cir. 1989) (following \textit{United Parcel Serv.}).

For cases recognizing the equitable claim of laborers and suppliers to retainages unpaid to a defaulting general contractor, see Rudolph \textit{5 B.C. Indus. \\& Comm. L. Rev.} at 249 \\& nn.12, 15 (cited in note 30); Speidel, \textit{47 Va. L. Rev.} at 646-47 \\& nn.19-21 (cited in note 347) (noting recognition in cases of "the equitable right of materialmen and suppliers to priority" over the general contractor's assignees of contract proceeds owed by the project owner). See also Hillman, et al., \textit{Common Law and Equity} § 24.05[2] at 24-75 to 24-76 (cited in note 271) (noting continuing applicability of equitable lien doctrine in unusual cases to give priority to otherwise subordinate secured party). But see \textit{Cherokee Carpet Mills, Inc. v. Worthen Bank and Trust}, 561 S.W.2d 310, 313 (Ark. 1978) (stating that "partial payment to a contractor by an owner is not held in trust for subcontractors, materialmen, mechanics or employees").


\footnote{417. Id. at 1095 (quoting the assignment).

\footnote{418. Id. at 1095-96.

\footnote{419. Id. at 1097.}
ority to nonprofessional account claimants. Less sympathetic claimants, although invoking like legal theories, have met with less success.

2. The Construction Surety

Perhaps the most important exception to the first-to-file rule that arises under U.C.C. Section 1-103 operates to protect the construction surety. This recurring problem is illustrated by Case L.

Case L. First Assignee Bank gives Calamity Construction Company a $100,000 loan to finance Calamity's construction of an office building for Otto Owner. As security for the loan, Calamity grants

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420. See First Commercial Corp. v. First Nat'l Bancorporation, Inc., 572 F. Supp. 1430 (D. Colo. 1983); Heinrichsdorf v. Raat, 655 F.2d 860 (Colo. Ct. App. 1982); Weld Colorado Bank v. E & E Constr., Inc., 653 F.2d 758 (Colo. Ct. App. 1982). See also Mid-Atlantic Supply, Inc. v. Three Rivers Aluminum Co., 790 F.2d 1121 (4th Cir. 1986) (holding that Bank's security interest in debtor's accounts did not reach a check which was made to debtor and his supplier because debtor only held the check in trust for supplier); In re Sherman, 627 F.2d 594 (2d Cir. 1980) (holding that insurance company's right to retain renewal commissions to satisfy past advances not a security interest in contract rights); Duly, 610 P.2d at 402 (applying Section 9-318(1) equivalent in Wyoming Code to defeat assignee's claims against account debtor where account debtor and assignor had agreed that account debtor could deduct amount payable to subcontractor on earlier job from payments due under assigned contract). Contrast Septembertide Publishing, in which an author made a contract with hardcover publisher, which in turn contracted with softcover publisher. 884 F.2d at 676-77. The softcover publisher agreed to pay the hardcover publisher royalties, and the agreement between the hardcover publisher and the author required the hardcover publisher to pay two-thirds of such royalties to the author. Id. at 677. The court gave priority as to two-thirds of royalties owed to the hardcover publisher by the softcover publisher to the author, notwithstanding the bank's first-filed floating security interest covering all of the hardcover publisher's accounts. The court, relying in part on Sections 9-203 and 9-318, reasoned that the author was the third-party beneficiary of the agreement between the hardcover publisher and the softcover publisher, and that "[o]nce vested, the author's third-party rights could not be assigned without its consent." Id. at 679-82. But compare Clark, The Law of Secured Transactions ¶ 2.04 at 2-39 to 2-40 (cited in note 8) (stating that "case law strongly suggests that secured creditors are having little difficulty with the requirement that the debtor have rights in the collateral," and citing "the broad notion of rights in the collateral under Article 9"); Notably, the result in Himes seems to be one that would have been proper under pre-Code law. See Corbin, Corbin on Contracts § 893 at 588 (cited in note 6) (stating that "the power may be reserved [by the account debtor] to discharge the obligation by payment to a third party" and that "[t]he right of the assignee is subject to such a power"); id. § 901 at 611 n.50 (citing additional cases) and 613 (collecting numerous cases in which surety who satisfies laborers' and suppliers' claims defeats, on subrogation theory, competing claim of general contractor assignee).

421. See MNC Commercial Corp. v. Joseph T. Ryerson & Son, Inc., 882 F.2d 615, 619 (2d Cir. 1989) (finding a contractual right of set-off held by steel corporation, though exempt from filing requirement, unprotected from subordination under Code priority rules); AMCO Prods., Inc., 17 Bankr. at 764-65 (rejecting bank's argument that bankrupt's estate does not include reserve account that bank had contractual right to draw against to cover shortfalls in collections on obligation assigned by customer to bank where in fact such shortfalls existed).

422 Professor Clark collects some 20 reported decisions concerning this type of priority dispute. See Clark, The Law of Secured Transactions ¶ 11.04[3]-[5] at 11-17 to 11-28 (cited in note 8). The problem was common under pre-Code law. See Corbin, Corbin on Contracts § 901 at 608-14 (cited in note 6).
First Assignee Bank a security interest in all its rights to payment under its contract with Otto. Thereafter, pursuant to its contract with Owner, Calamity secures both a performance and a payment bond from Second Assignee Surety, Inc. The bonds obligate the surety to finish performance and to pay off all subcontractors, laborers, and suppliers if the contractor defaults. Pursuant to the bonds, Calamity assigns to the surety all its payment rights under the Otto-Calamity contract to cover any expenses the surety might incur in completing the project. After finishing half of the office building, Calamity defaults on the construction contract. Second Assignee Surety finishes the work pursuant to its bond. First Assignee Bank has filed a U.C.C. financing statement, but Second Assignee Surety has not. On these facts, is the bank or the surety entitled to the now-earned progress payments and retainages that Otto Owner has refused to pay Calamity due to its breach of contract?

Because both First Assignee Bank and Second Assignee Surety took security interests in the same account, First Assignee Bank will claim priority as the first assignee to file under Section 9-312(5)(a). The first-to-file rule, however, does not control this case. Rather, courts have been all but unanimous in declaring that the first-filing bank is subordinate to the second-filing or nonfiling surety. Their reasoning is that, wholly apart from its consensual security interest, the surety has a prior right to amounts unpaid by the owner under the doctrine of equitable subrogation. In particular, because the owner had a right to retain unearned contract payments vis-à-vis the contractor's bank upon the contractor's default, so does the surety that steps into the shoes of the owner upon finishing the project.

423. See notes 85-92 and accompanying text.
424. See, for example, Canter v. Schlager, 267 N.E.2d 492 (Mass. 1971) (giving the surety priority; collecting many earlier cases). See generally Henson, Handbook on Secured Transactions § 5-7 at 153-55 (cited in note 8); Clark, The Law of Secured Transactions ¶ 1.07 at S1-14 (Cum. Supp. No. 2 1992) (noting that "the courts simply love sureties in these cases"); White and Summers, Uniform Commercial Code § 21-6 at 948 (cited in note 8); Coogan, et al., Secured Transactions § 4B.10(3) at 4B-88 (cited in note 8) (stating that "surety has priority"); Hillman, et al., Common Law and Equity ¶ 24.01[2][a][i] at 24-9 (cited in note 271) (stating that "courts agree almost unanimously that the [s]urety should prevail").
425. For example, Rudolph, 5 B.C. Indus. & Comm. L. Rev. at 248 (cited in note 30) suggesting that, at least on private project, subrogation is to rights of owner even when surety pays off suppliers and subcontractors under payment bond. See also id. at 251-54 (discussing progress payment of differing judicial treatment of surety subrogation claims to retained percentages versus unreleased progress payments); Friedberg, 41 Case W. Res. L. Rev. at 315 (cited in note 411) (stating that "the doctrine of equitable subrogation, as applied in nearly every jurisdiction, grants payment and performance bond sureties a superior claim to undisbursed contract funds over the lender with a perfected security interest in such funds."). See generally Corbin, Corbin on Contracts § 901 at 609-10 (cited in note 6); Speidel, 47 Va. L. Rev. at 645-48 (cited in note 347).
426. For illustrative discussions of the surety-lender priority problem, see, in addition to
Some observers have criticized this analysis as formalistic and insensitive to pertinent policy considerations. They have a point. Passing references to "subrogation" and "shoes" hardly provide a satisfying analysis of this recurring conundrum in account priority law. Close analysis, however, shows that the courts have picked the right rule for the construction-surety cases.

On the formal side, the Code's legislative history establishes that the Code itself does not protect the first-filing bank. Section 9-312(7) of the 1952 revision of the Code broadly favored lending banks over construction sureties. The Code's drafters, however, excised that provision from their finished product. In doing so, they explained that "existing law" under which "the surety's rights come first" should "not be disturbed." One might respond that this analysis does not apply to


427. See, for example, Friedberg, 41 Case Wes. Res. L. Rev. at 326 (cited in note 411); John Harrison, Note, Secured Transactions: Who Is Entitled to Assigned Construction Progress Payments Made to Assignee Bank After Contractor's Default?, 32 Okla. L. Rev. 287, 291 (1979). See also Corbin, Corbin on Contracts § 902 at 307 (Supp. 1982) (citing "the superior results of preferring the Uniform Commercial Code secured party to the common law surety interest"); Rudolph, 5 B.C. Indus. & Comm. L. Rev. at 257 (stating that "whether the position of a surety, a professional risk taker, should be fully equated to that of labor and material claimants is open to question"); Hillman, et al., Common Law and Equity § 24.01[2][a][ii] at 24-13 to 24-14 (citing "appealing policy argument" that subjecting sureties to first-to-file rule would generate greater certainty and solve bankers' "problem of lack of notice of suretyship arrangements").

428. Courts may favor sureties because they fear that subordinating sureties would also jeopardize the position of project owners. If state law dictates that a surety stands in the shoes of a project owner, and the contractor's lender takes priority over the surety, then why shouldn't the contractor's lender take priority over the owner too? Steering clear of this result makes eminently good sense. See, for example, Corbin, Corbin on Contracts § 902 at 617 (cited in note 6) (stating that "[w]hatever rule is adopted as to preference between successive assignees, care must be taken to protect the obligor"). Any justification for subordinating sureties based on their insurer-like loss-spreading capacity, see note 425, does not apply to lender-owner priority disputes. Moreover, requiring Code filings of all owners who keep retainages would needlessly generate massive transaction costs because lenders know that owners routinely hold back retainages. In any event, the owner's right not to pay out unearned retainages to the contractor's assignee seems clearly established by U.C.C. § 9-318(1)(a).

429. See, for example, Transamerica Ins. Co., 540 So. 2d at 116.


432. Id. See, for example, Rudolph, 5 B.C. Indus. & Comm. L. Rev. at 256 (cited in note 30) (stating that "[w]hen the draftsmen eliminated the 1952 provision favoring assignees they apparently intended that the Code should thereafter be neutral in these disputes between assignee banks and sureties").
PRIORITIES IN ACCOUNTS

Case L because the surety in Case L did not simply stand on its common-law rights; he obtained an Article Nine security interest.433 This argument is feckless, however, for the plain reason that the surety that does more to safeguard its legal rights—by specifically securing a consensual, in addition to a nonconsensual, interest—should not as a result receive less legal protection.434

A determination that the Code does not control the surety-bank priority dispute does not mean that the surety must win under applicable non-Code law. Courts fashioning common-law doctrine could opt for a priority rule that favors the contractor’s lender.435 To do so, however, would not make good economic sense.

Assume no surety is in the picture. The bank then will make its lending decision (as to whether to lend, how much to lend, and at what rate to lend) with full knowledge that it may never realize its account collateral because the owner will not make payments if the contractor breaches.436 Assume now that the project owner requires a surety bond, but that the surety will not issue a bond unless it knows it will get the benefit of retainages withheld by the owner upon the surety’s completion of the project.437 Under a rule favoring the first-filing lender over the nonfiling surety, the surety can obtain this result only by filing a financing statement and obtaining a subordination agreement from the contractor’s lender.

Will the lender provide this agreement? For two reasons, it normally should. First, without such an agreement, the entire transaction, including the loan agreement the bank wishes to effect, will not go forward.438 Second and more important, the bank’s subordination of its interest to the surety does not worsen the bank’s position.439 The bank is giving up nothing more than its interest in monies that the owner, upon the contractor’s default, would hold back from the bank any-

433. See Hillman, et al., Common Law and Equity ¶ 24.01[2][a][ii] at 24-12 & n.43 (cited in note 271) (developing this argument and noting that the cases reject it).
434. In accord is Clark, The Law of Secured Transactions ¶ 1.07[2] at 1-62 (cited in note 8). Clark states that “it makes no difference that the contractor executed a legal assignment . . . [because] the surety’s primary reliance is still on its equitable right of subrogation,” but notes, however, that the “surety is asking for trouble when it acts as though Article 9 applies and then fails to play according to its rules”. Id.
435. See, for example, Rudolph, 5 B.C. Indus. & Comm. L. Rev. at 250 (cited in note 30).
436. See U.C.C. § 9-318.
437. This is hardly an exotic assumption if, as has been said, “[t]he premium that the surety charges reflects its expectation of reaching the retainage.” Clark, The Law of Secured Transactions ¶ 1.07[1] at 1-61.
438. See Henson, Handbook on Secured Transactions § 5-6 at 152 (cited in note 8).
439. See Speidel, 47 Va. L. Rev. at 653 (cited in note 347) (stating that “[c]laims of the [owner] and the . . . surety pose similar threats to [the lender’s] security.”).
way. It is sensible in these circumstances simply for courts to give the surety priority without insisting that it incur the needless transaction costs involved in scouring the U.C.C. files, securing subordination agreements, and filing U.C.C. financing statements.

The soundness of this result is confirmed by a host of additional considerations. For example, “thousands of bonds are constantly being written all over the country,” thus, the cost of requiring sureties to comply with the Code would be enormous in the aggregate. In addition, the notice value of U.C.C. filings by construction sureties is minimal; lenders know that sureties are a probable feature of a construction project and can confirm the use or nonuse of a surety bond through a

440. See, for example, First Nat'l Bank of Minot v. MacDonald Constr. Co., 137 N.W.2d 667 (N.D. 1965) (recognizing prime contractor’s right to withhold payments upon subcontractor’s default). See Hillman, et al., Common Law and Equity ¶ 24.01[2][a][iii] at 24-14 (cited in note 271) (holding that by defaulting, contractor forfeited retainage to the bank); Coogan, et al., Secured Transactions § 4B.10[2] at 4B-54 (cited in note 8) (noting rule that “contractor has rights in only those payments actually due under the contract so that secured lender will lose to . . . the owner to the extent progress payments or retainages is needed to cure the contractor’s breaches”). Lending banks might prefer to have a surety on the scene, both to help police the contractor and to minimize mop-up costs (by way of a professional surety’s, rather than a nonprofessional owner’s, handling of the project following a contractor’s default). See Coogan, et al., The Law of Secured Transactions § 4B.10[3] at 4B-58 (recognizing lender’s potential right to surpluses upon job completion by surety).

441. See Thomas H. Jackson and Anthony T. Kronman, Secured Financing and Priority Among Creditors, 88 Yale L. J. 1143, 1154, 1180 (1979) (asserting, with respect to another Code priority rule, “[t]he justification for the rule, then, is that it does what parties would do for themselves in its absence, and thereby achieves a savings in transaction costs”; also recognizing that obtaining subordination agreements is costly). See also In re J.V. Gleason Co., 452 F.2d 1219, 1224 (8th Cir. 1971) (stating that to require filing “where no legitimate purpose is served is a waste of time and energy”); Frances A. Rauer, Note, Conflicts Between Set-Offs and Article 9 Security Interests, 39 Stan. L. Rev. 235, 236 (1986) (noting that “minimizing the total costs of credit” constitutes “a major policy objective of the law of secured transactions”). At least one observer has suggested that it is wise to adopt a rule that requires sureties to “achieve priority through a subordination agreement.” Friedberg, 41 Case W. Res. L. Rev. at 321-22 n.111 (cited in note 411). The argument is that this method forces “the surety and the lender to define their respective rights” and thus reduces the likelihood of an expensive dispute. Id. However, to seek to avoid an “expensive dispute” by adopting a rule that requires staggering front-end transaction costs in the form of constant file searching and negotiation of subordination agreements hardly makes sense. The way to avoid these disputes is simply to make the governing priority rule both efficient and clear. The existing rule that consistently favors sureties serves this end well.

442. Henson, Handbook on Secured Transactions § 5-6 at 151 (cited in note 8).

443. See Baird and Jackson, 35 Stan. L. Rev. at 185-86 & n.38 (cited in note 170) (noting potential significance of costs involved in filing and checking files).
routine check of project documents. Finally, both lenders and sureties are used to the universally recognized pro-surety rule and have structured rates and practices upon it. A departure from the rule at this time would disrupt reliance interests and thwart the Code’s goal of interstate uniformity.

Considerations of fairness, as well as efficiency, favor the existing surety-favoring rule. A contrary rule would improve the lender’s financial position—by making available to it funds otherwise unreachable from the owner—solely because of the fortuity that a surety bond was secured. It also seems unfair to favor the bank in these cases because the surety’s own work is what matures the owner’s duty to pay the funds from which the bank seeks to exclude the surety.

In the end, these reasons are less important than the actions of the courts. Moreover, the drumbeat of the cases is steady and clear: performing sureties may rest assured of priority over lenders with security interests in a contractor’s accounts.

E. Additional Exceptions to the First-To-File Rule

The foregoing discussion—focusing on U.C.C. Sections 9-302(1)(e), 9-104(f), and 1-103—highlights the most often invoked account-related exceptions to the general first-to-file rule. In many cases, however, the first filer will take a backseat to a competing account assignee under Code rules that generally apply to all types of secured parties. The creditor who first files a flawless financing statement, for example, nonetheless may forfeit priority if it later makes a subordination agreement, terminates its financing statement, or lets the financing statement lapse. The first proper filer also will lose if she had “knowl-

445. See generally Baird and Jackson, 35 Stan. L. Rev. at 190-91 (recognizing that one “situation in which the informational value of a filing requirement would be insignificant is where there is widespread knowledge that the possessor of an asset is not the owner”).

446. See note 424 and accompanying text.

447. *Transamerica Ins. Co.*, 540 So. 2d at 117 (stating that favoring banks over sureties “would frustrate uniformity and create conflict in the application of U.C.C.”).

448. See *Munsey Trust Co.*, 332 U.S. at 240 (1947) (recognizing “the peculiarly equitable claim of those responsible for the physical completion of building contracts”); Grant Gilmore, *The Assignee of Contract Rights and His Precarious Security*, 74 Yale L. J. 217, 245 (1964) (stating that sureties are favored because they make advances that “enable the assignor to complete the performance of the contract”).

449. U.C.C. § 9-316. See, for example, *AM Int’l*, 46 Bankr. at 571-73 (holding that first filing assignee loses priority to later assignee because of subordination agreement, and noting that “a subordination ‘agreement’ can be inferred from words of the parties, course of dealing, surrounding circumstances and the like”).

450. See U.C.C. § 9-404.

451. See id. § 9-403(2). Most financing statements will lapse if not renewed within five years of filing. “Upon lapse the security interest becomes unperfected unless perfected without filing.” Id. See generally Special Project, 62 Cornell L. Rev. at 853-54 (cited in note 12) (discussing circum-
edge of the contents" of an earlier, but improperly filed, financing statement. And the first filer as to a particular account may find itself out of luck if a second filer claims the same account through a debtor different than the first filer's transferor.

Five other matters, distinctive to account assignments, merit more extended attention: (1) the special problems posed by purchase-money security interests in accounts; (2) the proper treatment of account proceeds of inventory collateral; (3) the distinctive rules applicable to priority disputes involving proceeds of accounts; (4) exceptions to the first-to-file rule arising out of the Code's limited definition of the term "account"; and (5) the removal of Code coverage by account-related scope provisions other than Section 9-104(f).

1. Purchase-Money Security Interests in Accounts

Some secured creditors are more equal than others. The Code offers a "super-priority," even against first filers, to any creditor who obtains a purchase-money security interest ("PMSI"). A secured

stance under which perfection lapses). A security interest in accounts can lapse with respect to account proceeds unless perfection is properly maintained. See Clark, The Law of Secured Transactions § 10.01[2][b] at S10-2 (Supp. 1990) (cited in note 8).


453. The leading case on this subject, with respect to accounts, is Bank of the West v. Commercial Credit Fin. Seres., 852 F.2d 1162 (9th Cir. 1988). A useful discussion of the case appears in Clark, The Law of Secured Transactions § 2.11[1][b][iii] at 52-22 to 52-24 (Cum. Supp. No. 1 1992). Detailed discussions of the dual debtor problem appear in Coogan, et al., Secured Transactions § 7B.03 at 7B-20 to 7B-28, and Clark, The Law of Secured Transactions § 3.06[4] at 3-91 to 3-92. For a recent statement from the Permanent Editorial Board on this issue, see Permanent Editorial Board Commentary on the Uniform Commercial Code, PEB Commentary 6: Section 9-301(1) (1990) (indicating that the first-to-file rule should not necessarily protect the creditor who takes a security interest through an original debtor's transferee). See also Special Project, 62 Cornell L. Rev. at 860-63 (cited in note 12) (suggesting that the first filer's loss of priority in these circumstances can be explained by viewing Section 9-312 as fixing priority rules only for competing security interests that were created by a single debtor). Another interesting departure from the strict first-to-file rule, applicable to transferees of certain foreign assignors, is established by U.C.C. Section 9-103(3)(c). That section provides: If the debtor is located outside the United States in a jurisdiction that does not provide for Article Nine-type filing, the financing statement may be filed in the state where the debtor has its major U.S. executive office; in the alternative, perfection against a foreign assignor may always be accomplished by notification of the account debtor. Of course, "account debtor notification is ineffective as a means of perfection in all other situations." Clark, The Law of Secured Transactions § 10.04(3)(b) at 10-45 n.156 (cited in note 9). See note 95 and accompanying text.

454. U.C.C. Section 9-104(f) describes the principal forms of account transfers to which Article Nine does not apply. For a discussion of these exceptions, see notes 211-327 and accompanying text.

455. U.C.C. §§ 9-312(3), (4). For a detailed general study of the purchase-money security
creditor takes a PMSI if that creditor provides the money the debtor uses to purchase the property subject to the security interest. When Zinc, Inc. sells restaurant furniture under a conditional sales contract, for example, it takes a PMSI in the furniture because the seller’s extension of credit on the purchase price has directly facilitated the sale. In like fashion, Lava Lou Lender’s security interest in a Dimension Pinball Machine is of the purchase-money ilk if Lava Lou has lent to the Dimension Machine buyer the funds the borrower spent to acquire that treasure.

As lenders with PMSIs in goods, Zinc, Inc. and Lava Lou Lender may sidestep the general first-to-file rule under U.C.C. Sections 9-312(3) and 9-312(4). The Code speaks with a delphic voice, however, to the question whether the PMSI exception to the first-to-file rule extends to security interests in accounts. In particular, after Section 9-312(3) sets out the PMSI rules for security interests in inventory, Section 9-312(4) goes on to explain:

A purchase money security interest in collateral other than inventory has priority over a conflicting security interest in the same collateral or its proceeds if the purchase money security interest is perfected at the time the debtor receives possession of the collateral or within ten days thereafter.

The argument is straightforward that this rule does not afford any protection to the PMSI in accounts. Under the express terms of Section 9-312(4), the PMSI can take priority only if it “is perfected at the time the debtor receives possession or within ten days thereafter.” In the usual sense, however, a debtor cannot take possession of accounts because they constitute purely intangible property. Thus, the argument goes, Section 9-312(4) provides no exception to the first-to-file rule when the collateral are accounts.

interest, see Coogan, et al., Secured Transactions § 7B.01 at 7B-3 to 7B-8 (cited in note 8) (chapter by Professor McDonnell).


459. U.C.C. § 9-312(4).

460. See notes 88-91 and accompanying text (noting assignees’ inability to perfect account interests under U.C.C. Section 9-305 because accounts are not susceptible to possession). See also Arctic Air Conditioning, 35 Bankr. at 109 (stating that “since defendant could not have physically possessed the contract rights, a written agreement was necessary to create a security interest” under U.C.C. Section 9-203); Scult, 11 Ariz. L. Rev. at 4-5 (cited in note 19) (stating that “[a]lthough accounts, contract rights and general intangibles are not capable of ‘possession’ by a secured party within the meaning of the Code, a security interest in such collateral is enforceable only if the debtor has signed a written security agreement”).

461. Professor McDonnell skirts this problem in his otherwise helpful discussion of PMSIs in...
All things considered, courts should reject this analysis and afford otherwise qualifying account transferees PMSI priority under Section 9-312(4). The text of Section 9-312(4) leans in this direction by suggesting on its face that it applies without exception to "collateral other than inventory." Of no less importance, the Official Comments state flatly that "[s]ubsection (4) states a general rule applicable to all types of collateral except inventory." Nor is there any apparent policy reason for treating PMSIs in accounts or other nonpossessible intangible property less hospitably than other forms of PMSIs. A basic purpose of affording PMSI priority is to avert monopolization of credit by the holder of a security interest that broadly covers the debtor's after-acquired property. In addition, the PMSI rule achieves this result without prejudicing the preexisting floating-lien financer because the purchase-money interest extends only to new collateral that is added to the debtor's estate as a direct and traceable consequence of the purchase-money financing. These policies for favoring purchase-accounts. He states that a purchase-money financer of accounts should take priority over an earlier-filed floating lienholder "if it files within the applicable period of grace." Coogan, et al., Secured Transactions § 7B.12[2] at 7B-69 (cited in note 8). He does not explain, however, when or how that grace period—which is tied to the taking of possession—begins to run.

See Coogan, et al., Secured Transactions § 7B.12[2] at 7B-69 (concluding that the purchase-money financer of accounts should be able to obtain priority under Section 9-312(4) because "[a]ccounts are 'other collateral' within the terms of that section"); Clark, The Law of Secured Transactions § 3.09[2][b] at 3-97 (cited in note 8) (stating that Section 9-312(4) "contemplates a purchase money security interest in collateral other than inventory, and is not limited to tangible collateral").

U.C.C. § 9-312 cmt. 3 (emphasis added).

See, for example, Coogan, et al., Secured Transactions § 7B.05 at 7B-32 to 7B-33 (citing "avoidance-of-stranglehold" philosophy of purchase-money provisions); Robert Braucher and Robert Riegert, Introduction to Commercial Transactions at 464 (Foundation, 1977); Special Project, 62 Cornell L. Rev. at 870-71 (cited in note 12) (recognizing that "the purchase money exception facilitates commerce and reduces the potential unfairness created by monopolization of credit").

See, for example, First Interstate Bank v. IRS, 930 F.2d 1521, 1525 (10th Cir. 1991) (holding that "such an interest takes priority over any pre-existing lien on the theory that because the lender has augmented the capital assets of the borrower, previous creditors are not prejudiced"); Clark, The Law of Secured Transactions ¶ 10.06[2] at 10-52 (stating that "[t]his superpriority is frequently not a bad thing for the general financer, since value is added to the debtor's stock by the secondary financing"); Coogan, et al., Secured Transactions § 7B.05 at 7B-35 (stating that "[t]o allow the floating lienor to prevail as to assets which the debtor acquired through the new value provided by the purchase money credits arguably would give a windfall to the floating lienor"); Jackson and Kronman, 88 Yale L. J. at 1178-77 (cited in note 441) (stating that "[i]f the appreciation in the debtor's estate resulting from [the purchase-money lender's] loan can be linked to the debtor's acquisition of distinct items of property, the debtor can grant [that lender] purchase money priority without occasioning a de facto demotion of the [earlier floating lienholder's] security interest"). The purchase-money priority rule may eliminate needless transaction costs by automatically prioritizing the purchase-money interest. Viewed from the time of a first-filed floating lien transaction, this may be the case because the parties otherwise would have to negotiate, with some difficulty, a cost-of-credit reduction to offset the floating lienor's situational monopoly. Id. at 1172-73. On this view, the "purchase-money provision in Article 9 merely
money creditors apply no less forcefully when the borrower buys non-
possessory intangibles than when the borrower buys restaurant furni-
ture or Dimension Pinball Machines. 466

Any interpretation that extends Section 9-312(4) to nonpossessory
intangibles necessitates a somewhat awkward inquiry into when a trans-
feree of accounts takes possession of them. To say that the assignee
takes possession for purposes of Section 9-312(4) on the date the trans-
feree of the intangibles takes place, however, is not farfetched. 467 That
others have reached the same conclusion—either explicitly 468 or implicit-
ly 468—is not surprising.

Application of Section 9-312(4) to account transfers raises tricky
questions about whether particular interests in accounts qualify as PMS-
IIs. Consider, for example, Case M.

466. The acquisition of certain forms of intangible property—such as patents, copyrights,
trade secrets or other forms of intellectual property—may be especially important to the operation
and growth of the debtor's business. Professor McDonnell suggests that there is another policy
reason for favoring the secured lender who finances the purchase of accounts over an earlier-filed
floating lienholder. In his view, the floating lienholder is adequately protected by its interest in
accounts generated by the debtor's own sales or services, which are "all that a receivables finance
normallty expects or needs." Coogan, et al., Secured Transactions § 7B.12[2] at 7B-69 (cited in
note 8). This assumption is inappropriate, however, when the floating lienholder has bargained for
a security agreement that by its terms covers accounts either generated or purchased by the
debtor. Unless the security agreement is written in this way, no priority question will exist at all.

467. Section 9-103(5) of the 1962 Code provides some support for this proposition by recog-
nizing the possibility that accounts "are within the jurisdiction of [a] state" even when the as-
signor's records concerning them are located elsewhere. See generally Special Project, 62 Cornell L.
Rev. at 884 & n.230 (cited in note 12) (stating that meaning of the term "possession" varies in
different contexts).

that when a bank finances the acquisition of one company by another, possession of the acquired
company's accounts receivable and other intangibles occurs when the deal is closed).

469. See MBank Alamo, 886 F.2d at 1452-54 (acknowledging possibility of obtaining
purchase-money priority in accounts, although denying such priority on facts); Northwestern Nat'l
Bank SW v. Lectro Sys., Inc., 262 N.W.2d 678 (Minn. 1977) (implying that appellant who had
security interest in accounts would have been entitled to purchase-money priority if it had pro-
vided funds for the purchase of those accounts); In re Woodworks Contemporary Furniture, Inc.,
44 Bankr. 971 (Bankr. W.D. Wis. 1984) (agreeing with holding and reasoning of Lectro Sys.);
Case M. Bungling Bank agrees to lend a general contractor sufficient funds to facilitate the general contractor’s pursuit of a particular construction contract. In light of this commitment, the contractor is able to bid on the job and obtain the contract. The general contractor then transfers its payment rights under the contract to the Bungling Bank as collateral for its loan. Does Bungling Bank have a PMSI in the construction-contract account?

The bank will argue that it does because “by making advances or incurring an obligation [it gave] value to enable the debtor to acquire rights in” the account. The interest taken by the bank, however, is not a PMSI in the ordinary sense because the borrower has not used the loan proceeds to make a purchase at all. It is also doubtful that the no-skin-off-your-back policy behind the purchase-money priority provisions applies in this setting. This is so because the contractor’s payment rights are not purchased solely with the money lent by that bank; rather, they are purchased principally with the contractor’s work in performing the contract. It is precisely that work, however, that the floating lienholder is counting on to generate additional accounts to collateralize its own earlier commitments. Finally, giving PMSI status to persons who facilitate the creation of accounts—in addition to persons who facilitate their outright purchase—will create hair-raising characterization problems. For all these reasons, the better result is to restrict the PMSI in accounts to the lender who in fact finances an account purchase.

470. U.C.C. § 9-107(b).
471. See Lectro Sys., 262 N.W.2d at 680 (finding no PMSI in accounts, the court reasons that “[t]his is not a case in which funds were advanced for the purchase of a receivable”); Woodworks Contemporary Furniture, 44 Bankr. at 973 (quoting Lectro Sys. with approval); White and Summers, Uniform Commercial Code § 24-5 at 1139 n.4 (cited in note 8); Gilmore, Security Interests in Personal Property § 29.2 at 781 (cited in note 2); Coogan, et al., Secured Transactions § 7B.04[2] at 7B-31 (noting that the “purchase money creditor enables the acquisition of the collateral rather than . . . their production or generation in the debtor enterprise”) (cited in note 8); Clark, The Law of Secured Transactions ¶ 3.06[2][b] at 3-97 (distinguishing case in which “funds were used to perform an existing contract” from one in which funds are used “to purchase rights under the contract”) (cited in note 8).
472. Contrast note 465 and accompanying text.
473. Compare Lectro Sys., Inc., 262 N.W.2d at 680 (rejecting bank’s argument that loan to subcontractor that enabled subcontractor to finish contract and thus earn right to payment was a purchase-money transaction), with Friedberg, 41 Case W. Res. L. Rev. at 321-22 n.111 (cited in note 411) (arguing that construction-surety’s contingent interest in assigned project payments is a PMSI). See also White and Summers, Uniform Commercial Code § 24-5 at 1139 n.4 (expressing concern about “mak[ing] any loan a purchase money loan if it enabled the debtor to conduct his business and generate profit”).
474. See Coogan, et al., Secured Transactions § 7B.12[3] at 7B-70 (concluding that a bank that makes a loan to enable a contractor to finish a project, and thus generate account debt, does not have a PMSI; otherwise “the different standing of purchase money and operational financing
2. Security Interests in Accounts as Proceeds of Inventory

One of the most talked-about problems in the history of Article Nine concerns the position of the accounts financer vis-à-vis an inventory financer who claims accounts as proceeds. Following promulgation of the Code, controversy raged over whether a later-filing creditor with a PMSI in inventory could claim account proceeds to the exclusion of an earlier-filing direct transferee of the same account. The Code was ambiguous on this point, and some commentators advocated awarding priority to the later-filing inventory financer in derogation of the general first-to-file rule.

The 1972 Amendments mooted this debate. Under those amendments, the special protection afforded by Section 9-312(3) to the PMSI in inventory extends only to “cash proceeds received on or before delivery of the inventory to a buyer.” It follows that no exception to the ordinary first-to-file rule protects the inventory financer whose proceeds are accounts.

will collapse”); Clark, The Law of Secured Transactions ¶ 3.09[2][a] at 3-96 (same); Henson, Handbook on Secured Transactions § 5-5 at 89 (cited in note 8) (suggesting that PMSI in accounts arises “where Bank B advances funds to Financer C to enable C to purchase the accounts of A”); Gilmore, Security Interests in Personal Property § 29.2 at 780 (cited in note 2) (suggesting that the PMSIs in accounts would be only of “academic” interest). See generally note 469 (collecting cases). Notably, the problem identified here lurked in MBank Alamo, 886 F.2d at 1451-54. In that case, a manufacturer agreed to sell X-ray machines on credit to a distributor on the condition that the distributor would assign back to the manufacturer all accounts generated by its resale of the X-ray machines. Id. at 1450. The manufacturer thereafter argued it had a PMSI as to those accounts, entitled to priority over two earlier-filed accounts financers, because its commitments had “enable[d] the debtor to acquire” the accounts. Id. at 1451 (quoting U.C.C. § 9-107(2)). The court rejected this argument on the ground that the manufacturer looked too much like a proceeds-claiming inventory financer (whom the Code clearly subordinates to an accounts receivable financer by way of U.C.C. Section 9-312(3), see notes 475-78 and accompanying text). Id. at 1452-53. As Professor McDonnell has noted, the court more properly could have rejected the claim of priority on the ground that the manufacturer failed to qualify as a PMSI holder. As he puts it: “[The manufacturer’s] commitments did not enable [the distributor] to ‘acquire’ the accounts within the meaning of Section 9-107(b). The commitment allowed [the distributor] to generate the accounts. . . [However, the] accounts arose in the business of [the distributor] as part of its normal business operations rather than being purchased.” Coogan, et al., Secured Transactions § 7B.12[4][c] at 7B-73 (emphasis added).

475. See, for example, Final Report, § 9-312 at 113-14 (cited in note 308) (describing the problem as “one of the most widely discussed questions under the 1962 Code”). Commentary on this subject was extensive. See, for example, Gilmore, Security Interests in Personal Property § 25.8 at 674 n.1; Coogan and Gordon, 76 Harv. L. Rev. at 1559-64 (cited in note 31); Scult, 11 Ariz. L. Rev. at 26-30 (cited in note 19) (collecting earlier literature).

476. The principal exponent of this position was Professor Henson. See, for example, Henson, Handbook on Secured Transactions § 6-5 at 213 (cited in note 8).

477. See U.C.C. § 9-312(3) (emphasis added). See also id. § 9-312(3) cmt. 3.

478. See id. § 9-312 cmts. 3, 8. In accord, for example, Coogan, et al., Secured Transactions § 15.10[3][b] at 15-67; id. § 7B.11[1] at 7B-66. As stated in the Permanent Editorial Board’s Final Report: The Committee believes that where a financing statement as to accounts financing is filed
Notwithstanding the 1972 Amendments, some departures from the first-to-file rule will continue to result from the interaction of the Code's proceeds and PMSI rules. One reason why is that the cash-proceeds limitation of Section 9-312(3) applies only to the PMSI in inventory.\(^{479}\) Consider, in this regard, Case N:

Case N. Snuffleupagus properly files a floating lien covering all of Cookie Monster's accounts. Thereafter Oscar sells a steamroller to Cookie Monster on credit, retaining a PMSI. Oscar files his financing statement covering his security interest before Cookie Monster takes delivery of the steamroller. For a time, Cookie Monster uses the steamroller in his business, but then sells it to Prairie Dawn, who promises to pay Cookie Monster $10,000 in one year in a writing that is neither an instrument nor chattel paper. Cookie Monster thereafter defaults on his obligations to Snuffleupagus and Oscar, who both lay claim to the Prairie Dawn account.

Oscar, although he is the second filer, takes priority on these facts. The reason why is that the steamroller was not inventory, but equipment.\(^{480}\) Oscar properly perfected his PMSI in that equipment under Section 9-312(4), and that interest carries over to the collateral's proceeds, including accounts.\(^{481}\) For Oscar, the would-be Grouch, Article Nine has chased the clouds away. His second-filed security interest gives him a first-priority position with respect to the Prairie Dawn account.\(^{482}\)

Notwithstanding the limits imposed by Section 9-312(3), even a secured creditor who lays claim to account proceeds of inventory may, in a proper case, defeat a perfected direct account assignee. If an inventory financer files before any filing by the account transferee, the inventory financer takes priority even though her financing statement does not mention accounts at all. This result arises because the inventory financer is not relying on the special protection provided by the PMSI

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\(^{479}\) See note 477 and accompanying text.

\(^{480}\) U.C.C. § 9-109(2).

\(^{481}\) See id. § 9-312 cmt. 3 (stating that PMSI continues in proceeds of non-inventory collateral); Coogan, et al., *Secured Transactions* § 7B.11[3] at 7B-67 (emphasizing that "Section 9-312(4) does not limit the 'flow through' of the priority to cash proceeds of the acquired asset").

\(^{482}\) In accord, for example, Special Project, 62 Cornell L. Rev. at 880 (cited in note 12) (noting that "section 9-312(4) extends purchase-money priority to account proceeds arising from [sales of] noninventory").
rule of Section 9-312(3), but instead on the general protection afforded by Section 9-312(5). This protection is available to the inventory financer because other Code provisions broadly extend the first-to-file principle to proceeds of collateralized property. One can quibble about whether these provisions in effect create an exception to the first-to-file rule. However, the fact that they do cause the first filer to take a subordinate position with respect to the accounts themselves is clear.

3. Security Interests in Checks or Cash as Proceeds of Accounts

In many cases, priority as to a transferred account has significance only if that priority extends to the account's proceeds. Consider, for example, Case O.

Case O. Fan and Stan both pay for assignments from Ann of an account payable to her by Jan. Fan files first. Stan, however, receives payment on the account, without notice of Fan's competing interest, by way of a check drawn by Jan. Can Fan, because she has priority as to the account, recover from Stan the check, its proceeds, or an equivalent amount?

According to a recent pronouncement of the Permanent Editorial Board, Fan is out of luck even though she was the first to file. The Board's reasoning is that Stan took the check as a holder in due course; thus, under Section 9-309, he has "priority over an earlier security interest even though perfected."
The appropriateness of this application of Section 9-309, which gives priority to the check recipient even though his receipt of the check is wholly derivative of his interest in an account that is subordinate to the interest of another, is hardly self-evident. At least one court rejected the position now espoused by the Permanent Editorial Board,481 and distinguished commentators—writing prior to issuance of the Board’s declaration—approved the result in that case.482

Even so, the broad language of Section 9-309 strongly supports the Permanent Editorial Board’s position. So does the longstanding policy—now embodied in Article Three of the Code—that favors finality and assuredness in taking negotiable paper.483 Because the Board’s approach to Case 0 is more than reasonable, it should be followed by the courts in the interest of achieving and maintaining uniformity.

A different problem arises if Stan receives payment by way of cash instead of by check. Again, the Permanent Editorial Board would preclude any recovery by Fan from Stan under these circumstances.484 The Board’s reasoning on this question, however, differs significantly from its analysis of Case 0. In addressing the cash-proceeds issue, the Board states that “resort must be had to the principles of law and equity” made applicable to Code problems by Section 1-103.485 It goes on to explain: “[I]f [Stan] gave value for the assignment (as [he] must have, see § 9-203(1)(b)) and obtained the payment in good faith and without secure priority under Section 9-308, and when a first filer’s proceeds interest in a check or its proceeds might lapse under Section 9-306 are all beyond the scope of this Article. In accord, Allstate Fin. Corp. v. Financorp, Inc., 934 F.2d 55 (4th Cir. 1991).

491. Bank of the West v. Commercial Credit Fin. Serv., Inc., 855 F. Supp. at 807, 819-20 (N.D. Cal. 1997). The Bank of the West case involved the unsuccessful assertion of priority under Section 9-309 by a second-filing factor who had bought accounts without recourse and then had taken the checks as payments on those accounts.

492. See Clark, The Law of Secured Transactions ¶ 3.08[1][c] at 3-85 to 3-86 (cited in note 8) (stating that “the decision seems correct,” including inapplicability of Section 9-308, because second-filing “factor had no interest in the checks except as proceeds of the accounts”); Hillman, et al., Common Law and Equity ¶ 25.02[5][c] at §25-25 (Cum. Supp. 1991) (cited in note 271) (reasoning that case was correctly decided because the junior account holder’s “liability was based on conversion of the accounts rather than the proceeds of the accounts”).

To the extent that the latter authority approved Bank of the West solely on the ground that the junior account holder received checks directly from the account debtor rather than proceeds passed through to it following collections by the assignor, that analysis is questionable for two reasons. First, the factual recitation by the court in Bank of the West indicates that some of the check payments received by the junior assignee came from the assignor, rather than directly from the account debtor. 852 F.2d at 1164-65. Second, whether collections come from the account debtor or through the assignor seems to make no difference as a matter of Code language or Code policy. Most important, in either case, the junior assignee who takes a check in good faith qualifies as a holder in due course.

493. See Allstate Fin. Corp., 934 F.2d at 59-60.
494. PEB Commentary 7 at 34-35 (cited in note 488).
495. Id. at 34.
knowledge or reason to know of the prior assignment, then [Stan] may retain the payment. See Restatement, Second, Contracts, § 342(b).

The key difficulty with this analysis is that it unjustifiably assumes that all states abide by the four-horsemen rule of Restatement Section 324(b), which entitles an innocent second-in-time assignee to retain account collections. While the Permanent Editorial Board might properly claim authority to engage in ongoing interpretation of the Code itself, claiming authority to declare uniform principles of non-Code common law is a far different matter. Even so, as the Board suggests, there is good cause for courts to interpret the common law so that Stan keeps the cash. Otherwise, given the preceding analysis of Case O under Section 9-309, "cash would be rendered less negotiable than a check."

In short, the gravitational pull of the Code on the common law is distinctively powerful in this setting, for otherwise an anomaly will arise. The resulting common-law rule—which subordinates the first filer if the competing account transferee has innocently collected money proceeds—highlights the many uncertainties that face even the most properly perfected first-filing account assignee.


Departures from the Code's first-to-file rule also result from the Code's specialized definition of the term "account." Consider Case P.

Case P. On January 1, Fern Factoring, Inc. takes an outright assignment of all of Saul Dramaseller's existing rights to payment. Those rights are (1) Saul's payment rights for six past deliveries of videocassettes, and (2) Saul's entitlements to payment for seven transfers of staging rights as to a recently copyrighted play. On February 1, Saul assigns these thirteen payment rights to Second Assignee Bank as collateral for a $100,000 loan. Second Assignee Bank files its financing statement on February 1, and Fern Factoring files on February 2. Who has priority as to these receivables?

Article Nine governs this priority dispute to the extent it concerns...
the payment rights generated by the videocassette sales. Those sales
gave rise to accounts because Section 9-106 defines the term “account”
to reach “any right to payment for goods sold.”502 Both Fern Factoring
(as a buyer of those accounts)503 and Second Assignee Bank (as a collateral
transferee of those accounts),504 therefore, hold Article Nine security
interests. Article Nine’s first-to-file rule controls, and Second
Assignee Bank prevails.505

The same analysis, however, does not apply to the seven assigned
entitlements to payment arising from Saul’s transfer of the staging
rights. The reason why is that those entitlements are not “rights to pay-
ment for goods sold or leased or for services rendered.”506 Thus, they
are not accounts, but general intangibles, for purposes of the U.C.C.507
Second Assignee Bank’s collateral interest in the staging-right pay-
ments is a security interest under Article Nine, because one can take an
orthodox security interest in general intangibles.508 Article Nine, how-
ever, does not cover the sale of general intangibles, so that Saul’s trans-
fer of the staging-right payments to Fern Factoring falls outside Article
Nine.509 Non-Code law, therefore, controls the Fern Factoring/First As-

502. U.C.C. § 9-106 (emphasis added). The Code definition of the term “account” is set forth
at note 15 and accompanying text.
503. See U.C.C. § 9-102(1)(b).
504. See id. § 9-102(1)(a).
505. See notes 88-112 and accompanying text.
507. See Coogan, et al., Secured Transactions § 3.08[5][b] at 3-64 (cited in note 8) (noting
that rights to payment for the right to show a film would be considered a general intangible under
“‘general intangibles’ may include, in addition to non-monetary rights, rights to payments which
are not accounts”).
508. See U.C.C. § 9-102(1)(a); id. § 9-106 cmt. (explaining that Code extends to collateral
transfers of general intangibles, which “are used or may become customarily used as commercial
security”); Joseph Kanner Hat Co., 482 F.2d at 940 (stating that right to be reimbursed for mov-
ing expenses is a general intangible, which Article Nine governs because there was an intent to
secure); Himlie Properties, 36 Bankr. at 34-35 (holding that security transfer of general intangibles
was covered by Code).
509. See, for example, Joseph Kanner Hat Co., 482 F.2d at 939 n.5; Morrison, 28 U.C.C. Rep.
Serv. at 174-75 (holding assignment of royalty payments from recording company not within Arti-
cle Nine). See generally Coogan, et al., Secured Transactions 15.02 at 15-9 to 15-10; Gilmore,
Security Interests in Personal Property § 10.5 at 308 (cited in note 2).

A danger exists that courts will fail to navigate safely through these tricky Code provisions. In
Vinzant, the court flatly stated: “Assignments of rights to payments under contracts are subject to
the filing provisions of the U.C.C. unless the assignment falls within the provisions of [9-104(f)].”
108 Bankr. at 757. This statement is inaccurate. The Code does not apply to all “[a]ssignments of
rights to payments under contracts.” As the preceding citations show, the Code does not apply to
absolute assignments of contractual rights to payment that constitute general intangibles. The
right to payment involved in Vinzant itself—namely rights to payments under annuity con-
tracts—were general intangibles. Nonetheless, the court correctly applied Article Nine’s filing
rules in the case because the assignments of the annuity contracts were collateral assignments
rather than absolute transfers. Id. at 754.
signee Bank priority dispute over the staging-right payments because that dispute has one foot in and one foot outside the Code.\(^{510}\) Under non-Code law, Fern Factoring may well have a prior claim to these payment rights even though it was the second filer. In particular, Fern Factoring will take the prize if the transfer occurred in a jurisdiction that follows the New York first-in-time rule.\(^{511}\)

As Case P illustrates, some contract rights that the business person may think of as accounts are not accounts for purposes of Article Nine.\(^{512}\) "Examples of such rights are the right to payment of a loan not evidenced by an instrument or chattel paper; a right to receive partial refund of purchase prices paid by reason of retroactive volume discounts; rights to receive payment under licenses of patents and copyrights, exhibition contracts, etc."\(^{513}\) Other contractual monetary payment rights that are not accounts include the right to payment given in exchange for trade secrets or for the purchase of realty,\(^{514}\) a capital reserve account of an agricultural cooperative member,\(^{515}\) the right to royalties under a contract transferring rights to reproduce and distribute recordings,\(^{516}\) and perhaps the right to payment under a non-competition agreement.\(^{517}\)

\(^{510}\) See, for example, \textit{Morrison}, 28 U.C.C. Rep. Serv. at 174-75; \textit{Farnsworth, Farnsworth on Contracts} § 11.9 at 123 (cited in note 8) (stating that "an assignment of... a contract right other than an account is left to the conflicting common law rules on priority"). See generally note 392 and accompanying text.

\(^{511}\) See notes 37-38 and accompanying text.

\(^{512}\) See, for example, \textit{Coogan, et al., Secured Transactions} § 15.02 at 15-8 to 15-9; id. § 21.02[1][a] at 21-75 (cited in note 9) (stating that "the financer would tend to include [as an account] any claim to payment of money arising out of the rendering of services or sales of any assets (whether or not those assets are good) if payment is no longer conditional upon further performance by the entity upon whose balance sheet the item appears") (footnotes omitted); \textit{Coogan and Gordon, 76 Harv. L. Rev.} at 1631 (cited in note 31) (stating that "to a businessman, his accountant or his financer, the term 'receivables' describes unconditional rights to payment of money").

\(^{513}\) U.C.C. § 9-106 cmt. See also id. § 9-102 cmt. 2 (stating that obligation "to repay money lent" that is not an instrument or chattel paper is a general intangible).

\(^{514}\) See \textit{Coogan, et al., Secured Transactions} § 15.02 at 15-9; \textit{Clark, The Law of Secured Transactions} ¶ 1.08[10][a][i] at 1-114 to 1-117 (cited in note 8) (discussing real estate cases). For cases holding assignments of a land vendor's rights to receive payments to be general intangibles, see \textit{In re D. J. Maltese, Inc.}, 42 Bankr. 689 (Bankr. E.D. Mich. 1984); \textit{In re S.O.A.W. Enters., Inc.}, 32 Bankr. 279 (Bankr. W.D. Tex. 1983) (holding that assignments of numerous contracts for the sale of real estate were not accounts or chattel paper, but general intangibles, representing a flow of payments from the vendees of the real estate); \textit{In re Southworth,} 22 Bankr. 376 (Bankr. D. Kan. 1982).


\(^{517}\) The key question in this regard is whether money paid for the promise not to compete is
Other commentators have wondered why the Code distinguishes between payment rights earned by the transfer of goods or services and payment rights earned by the transfer of intangibles or other forms of given in exchange for services. Probably it is not. The promisor under such an agreement does not undertake to perform "services" in the ordinary sense; rather she promises not to undertake specified work. Even more important, the legislative materials suggest that the Code's definition of the term "accounts" targets traditional accounts, or "the ordinary commercial account receivable." U.C.C. § 9-106 cmt. The right to money payments under a one-shot noncompete agreement hardly seems to fit this description. Contrast Worden, 63 Bankr. at 724 (raising issue of whether noncompetition agreement gives rise to account). For a questionable ruling, see Padgett, 49 Bankr. at 214-15. There the court confronted a "two-for-one" contract, under which a seller of soybeans obtained as consideration a right to receive, at the buyer's election at a future date, either twice the amount of delivered soybeans or the cash equivalent. id. at 213. The court concluded that this contract right constituted an "account", even though the buyer could perform by delivering either money or goods. Id. at 214-15. See Dynair Electronics, Inc. v. Video Cable, Inc., 127 Cal. Rptr. 268, 273 (Cal. Ct. App. 1976) (stating that "[r]eference to section 9106, and especially to the UCC Comment under that section, removes any doubt the former section was intended to define the terms 'account' and 'contract right' in terms of a right to payment of money"). For some other cases finding contractual rights to money payments not to be accounts, see, for example, Joseph Kanner Hat Co., 482 F.2d at 940 (holding right to be reimbursed for moving expenses not an account); Vinzant, 108 Bankr. at 757 (holding payment rights under annuity contracts not an account). See also Personal Constr. Co. v. Miller & Miller Auctioneers, Inc., 532 F.2d 186 (10th Cir. 1975) (holding money owed a construction company by auctioneer who sold construction company's equipment not an account); In re Cooper, 2 Bankr. 188 (Bankr. S.D. Tex. 1980) (holding promoter's right to payment from agent who sold concert tickets for promoter not an account); Jeness, 1977 Utah L. Rev. at 355 n.29 (cited in note 74) (noting that royalty payment for film contract in Consolidated Film Indus. would constitute general intangibles). For general discussions of general intangibles, see Clark, The Law of Secured Transactions at 1-16 to 1-21 (cited in note 8); Coogan, et al., Secured Transactions § 15.05 at 15-19 to 15-22 (cited in note 8); Henson, Handbook on Secured Transactions § 5.11 at 167-68; White and Summers, Uniform Commercial Code § 21-9 at 955 (cited in note 8).

One important definitional point concerns whether amounts payable to a contractor or subcontractor constitute an account or a general intangible. There was some uncertainty about this matter under the accounts receivable statutes. Compare Costello v. Bank of Am. Nat'l Trust & Sav. Ass'n, 246 F.2d 807 (9th Cir. 1957) (construing bookmarking accounts receivable statute not to cover payment rights under construction contract), with Honolulu Constr. & Draying Co. v. Terrace Developers, Ltd., 395 F.2d 691 (Haw. 1964) (construing accounts receivable statute to cover assignment of payment rights under construction contract).

Homer Kripke also questioned the status of such payment rights following enactment of the Code. Kripke, 4 N.Y.U. L. Rev. at 691-92 (cited in note 217). The Code, however, seems clear on this point, and the courts have concluded uniformly that the contractor, for Article Nine purposes, is a holder of an account. See, for example, AM Int'l, 46 Bankr. at 571 (stating that "[c]ases have held that where a subcontractor assigns to a supplier its right to payment under a contract, that assignment creates a security interest"); Mississippi Bank v. Nickles & Wells Constr. Co., 491 So. 2d 1056 (Miss. 1982) (holding that right to payment under construction contract constitutes an account); Sherburne Corp. v. Carter, 340 A.2d at 85-86 (finding that right to payment under construction contract constitutes "account" under Article Nine that is not excluded by Section 9-104). See also Gilmore, Security Interests in Personal Property § 12.5 at 380-83 (cited in note 2); Clark, The Law of Secured Transactions ¶ 11.01 at 11-2 (cited in note 8) (finding that "[t]he term also includes service contracts such as real estate construction contracts, which are frequently subject to Article 9 financing"); Kuhn Constr. Co., 11 Bankr. at 749 (stating that "were the contractor to assign these same rights to an entity other than a surety, such as a financier, Article 9 would apply"); In re Munro Builders, Inc., 20 U.C.C. Rep. Serv. at 740-41.
performance. Indeed, proposals have been made—even by some of the Code’s original drafters—\(^5\) to jettison this distinction and apply the Code to all forms of contractual payment rights.\(^6\) In forging the 1972 Amendments, however, the Permanent Editorial Board rejected these proposals.\(^7\) It reasoned that “too many standard forms of agreement use the term ‘accounts’ and reflect [the] intention of the parties to include only traditional accounts arising from the sale of goods or services.”\(^8\)

Redefining the term “accounts” for purposes of the perfection and priority rules, however, could not and would not change any intention of the parties expressed in consensual security agreements.\(^9\) Moreover, the Board’s reasoning ignores the fact that the Code already defines the term “accounts” to include many forms of payment rights that are not traditional accounts in the sense of being routinely carried on a seller’s or service-provider’s account ledgers.\(^10\) For better or worse, however, the law remains unchanged. The consequence is that the common-law rules still apply to many priority problems involving successive assignments of contractual rights to the payment of money.\(^11\)

What principles should govern these priority problems? For reasons already given, courts need not feel bound to follow some dusty pre-Code formula in deciding these cases. Rather, in a commercial world revolutionized by the U.C.C., courts should look to the common law with a more creative eye.\(^12\)

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518. See Coogan, et al., Secured Transactions § 5A.9 at 5A-47 (cited in note 8) (recognizing that “some financing patterns for general intangibles for the payment of money seem to be so similar to those for accounts as to argue in favor of bringing absolute assignments within the article”); Coogan and Gordon, 76 Harv. L. Rev. 1537-38 (cited in note 31); Kripke, 4 N.Y.U. L. Rev. at 693-700 (cited in note 217).
521. Id. at 217.
522. See U.C.C. § 9-203. See generally White and Summers, Uniform Commercial Code § 22-4 at 881 (cited in note 8). Contrast Coogan, et al., Secured Transactions § 15.05 at 15-21 (noting that, in light of the thin line between accounts and many general intangibles, “[i]t is difficult to imagine a receivables financing situation in which the financer would not be advised to include some claim to general intangibles”).
523. A large sum payable under a major construction contract is illustrative.
524. See Sun Bank, 466 So. 2d at 1090 (noting that trial court’s application of common-law first-to-notify-debtor rule was based on conclusion that assigned payment right was not an account within the Code). See also Gilmore, Security Interests in Personal Property § 8.7 at 277 (cited in note 2) (noting that, under the account receivable statutes, “[s]ince many types of intangibles were expressly excluded from the statutory coverage, there was left a common law area which co-existed, so to say, with the statutory area”).
525. See notes 348-49 and accompanying text.
5. Section 9-104 Exceptions Apart from Section 9-104(f)

As we have seen, Section 9-104(f) excludes important categories of money-payment rights from the coverage of Article Nine.\(^\text{526}\) So, too, do five other provisions of Section 9-104.

Section 9-104(d) makes Article Nine inapplicable to “a transfer of a claim for wages, salary or other compensation of an employee.”\(^\text{527}\) Section 9-104(c) excludes accounts assigned by a governmental unit.\(^\text{528}\) Section 9-104(g) excludes “a transfer of an interest in or claim in or under any policy of insurance, except as provided with respect to proceeds . . . and priorities in proceeds.”\(^\text{529}\) Section 9-104(j) removes from Code coverage rents from a lease of real estate.\(^\text{530}\) And Section 9-104(l) excludes any deposit account in a bank or other financial institution.\(^\text{531}\)

One surprising effect of these provisions is to place outside Article Nine even priority disputes between claimants who have received direct collateral transfers of the exempted-from-the-Code account property. For example, when a debtor grants a collateral interest in the debtor’s bank account to two different lenders, it certainly “smells” like an Arti-

\(^{526}\) See notes 211-237 and accompanying text.

\(^{527}\) This provision is designed to focus state-by-state attention on the important social problems posed by employee assignments, including whether such compensation rights should be assignable at all. The courts have encountered few interpretive problems with the section. They have made clear, however, that the section covers only traditional employees and not independent contractors. See, for example, Rankin, 102 Bankr. at 443 (stating that “it is clear that the debtor operated as an independent contractor, in business for himself. His earnings were not wages, salary or other compensation of an employee exempted from Article 9 by § 9104(4)’); K.A.O.P. Co., 372 N.W.2d at 776 (trial judge’s ruling that payment for legal services were not wages subject to 9-104(d) exclusion not challenged on appeal); Perry v. Freeman, 293 S.E.2d 381 (Ga. Ct. App. 1982) (holding that payment to independent contractor not excluded by Section 9-104(d) exclusion of compensation of employee). For a discussion of the wage-assignment exemption, see Clark, *The Law of Secured Transactions* ¶ 1.08(4) at 1-93 to 1-94.

\(^{528}\) U.C.C. § 9-104(3). See Clark, *The Law of Secured Transactions* ¶ 1.08(5) at 1-94 (cited in note 8) (noting that “If a rural water district borrowed funds and assigned as security future water receipts to be paid by customers, the transaction would be exempt,” but arguing that “the flat exemption does not seem justified”).

\(^{529}\) U.C.C. § 9-104(g). For an extensive discussion of the insurance-related exemption, see Clark, *The Law of Secured Transactions* ¶ 1.08(7) at 1-98 to 1-106.

\(^{530}\) U.C.C. § 9-104(j). For a discussion of the rental-payment exemption, see Clark, *The Law of Secured Transactions* ¶ 1.08(10)[b] at 1-120 to 1-122.

\(^{531}\) U.C.C. § 9-104(l). Section 9-105(1)(e) of the Code defines “deposit account” as “a demand, time, savings, passbook or like account maintained with a bank, savings and loan association, credit union or like organization, other than an account evidenced by a certificate of deposit.” For a comprehensive treatment of the law governing assignments of deposit accounts, see Zubrow, 68 Minn. L. Rev. at 99 (cited in note 75). See also Peter F. Coogan, Homer Kripke, and Fredric Weiss, *The Outer Fringes of Article 9: Subordination Agreements, Security Interests in Money and Deposits, Negative Pledge Clauses, and Participation Agreements*, 79 Harv. L. Rev. 229, 261-63 (1965).
The most common priority battle involving deposit accounts pits a financial institution exercising a common-law set-off right against an Article Nine secured party who lays claim to the deposit account as proceeds of inventory, equipment, or accounts. Much has been written on this subject, and it will not be repeated here. The theme of these cases, however, is significant for our purposes: courts almost always subordinate the professional financer, and are willing to bend the Code's text to achieve that result.

532. See AMCO Prods., Inc., 17 Bankr. at 761 (holding Code priority rules not applicable to security transfer of reserve account because it constitutes deposit account); Zubrow, 68 Minn. L. Rev. at 971-74 (discussing application of common-law priority rules to bank deposits).

533. See Clark, The Law of Secured Transactions ¶ 3.11 at 3-128 (describing this as "[a] classic priority clash that has been the subject of intense litigation").


535. See Clark, The Law of Secured Transactions ¶ 3.11 at 3-128 (stating that "the courts almost always give priority to the Article 9 claimant, whether the matter is resolved under Article 9 or by fashioning a common law priority rule"); White and Summers, Uniform Commercial Code § 21-8 at 954-55 (cited in note 8); Rauer, 39 Stan. L. Rev. at 248 (cited in note 441) (stating that ")regardless of the rationale used, bank set-offs typically lose when the third party claims a perfected security interest in the proceeds"). See, for example, City of Vermillion, 341 F. Supp. at 711-12 (holding that secured creditor takes priority over bank exercising set-off right).

536. Particularly heavy-handed are those cases that say that Section 9-104(i) exempts set-off rights only from Code perfection rules, but not from Code priority rules. See White and Summers, Uniform Commercial Code § 21-8 at 954-55 (collecting cases). The logical implication of this position is that the Code's priority rules apply to all transfers to which the Code "does not apply" by reason of Section 9-104. The consequence of this reasoning is that persons who receive Section 9-104 transfers should routinely lose priority disputes with Code transfers (in particular under U.C.C. Section 9-201, see Continental American Life Ins. Co. v. Griffin, 306 S.E.2d 285 (Ga. 1983)), notwithstanding the fact that Section 9-104 is designed to safeguard such transferees from the technical requirements of Article Nine. The better reasoned authorities reject this distinction between perfection and priority. See, for example, State Bank of Rose Creek v. First State Bank, 520 N.W.2d 723, 725-26 (Minn. 1982) (relying heavily on Coogan treatise). See generally Clark, The Law of Secured Transactions ¶ 3.11 at 3-128 to 3-131.
V. A Jurisprudential and Policy Appraisal of the Judicial Treatment of Account Priorities

Richard Posner has said that the American judge “rarely starts his inquiry with the words of the statute, and often, if the truth be told, he does not look at the words at all.” There could be little better evidence for this proposition than the manner in which judges have treated the U.C.C.’s provisions concerning accounts. Courts have all but ignored Section 9-302(1)(e)’s “significant part” language. In word and deed, many courts have endorsed Professor Gilmore’s antitextual “illustrative list” reading of Section 9-104(f). Courts also have neglected other statutory commands in untangling account-priority issues.

Why? At the most basic level, these decisions reflect the intensely substantive character of much American judging. As Professors Atiyah and Summers have documented, “[m]any American judges have a very non-formal or substantive conception of what counts as a true rule.” These judges are likely to see a statutory rule “as no more than a mere ‘guide,’” and may well “go behind it to determine its meaning almost without limits.” By and large, Atiyah and Summers avoid normative evaluation of highly substantive reasoning. Judgments about such reasoning are inescapable, however, if judicial action is to be critiqued at all.

Any such critique requires at least three steps. First, one must identify the particular substantive reason relied on by the court—the relevant “moral, political, economic or social consideration” that has

538. See notes 174-81 and accompanying text.
539. See note 218 and accompanying text.
540. See, for example, notes 535-36 and accompanying text (discussing bank deposit setoffs).
542. Id. For another illustration of this phenomenon in the Article Nine area, see David Gray Carlson, Rationality, Accident, and Priority Under Article 9 of the Uniform Commercial Code, 71 Minn. L. Rev. 207, 210 (1986) (stating that “although law professors are practically unanimous in believing that Article 9 condones a race priority wherein knowledgeable lenders can defeat prior unknowable lenders, some judges have not been as placid”). Contrast David M. Phillips, The Commercial Culpability Scale, 92 Yale L. J. 228, 290 (1982) (noting that results inconsistent with widely shared norms of behavior “may presage judicial hostility to the strict application of the Code”).
543. See, for example, Atiyah and Summers, Form and Substance at 420 (cited in note 541). At the same time, Professors Atiyah and Summers signal a concern about judicial excesses in substantive reasoning: “[O]ne of our principal purposes is to rehabilitate formal legal reasoning, because we are convinced that formal reasons are central to law, and that their proper analysis is one of the most neglected topics in the history of modern legal theory.” Id. at 7.
544. See id. at 419-20.
spurred the court to action. Second, one must evaluate whether that substantive reason is sound. Third, one must decide whether that reason, even if sound, is one the court legitimately may invoke in the face of countervailing formal reasons generated by statutory text, precedent, and the like. A careful pursuit of each of these three inquiries suggests that the courts have veered off course in refining and applying the Code's account-priority rules.

A. Protection of Nonprofessional Assignees as a Substantive Reason in Account-Priority Cases

The central substantive aim running through the account-priority decisions is clear enough. It is to give special protection to the nonprofessional account transferee, while imposing the strictest of requirements on professional assignees like banks and other financial institutions. Courts have invoked this professional-nonprofessional distinction explicitly in cases involving the Section 9-302(1)(e) significant part standard. As Professor McDonnell has shown, the same orientation explains the courts' erratic application of Section 9-104(f). A disfavor of the professional lender also dovetails with the judicial proclivity to subordinate financial institutions that assert set-off rights, or that find themselves competing with subcontractors or suppliers for retainages held back from general contractors by project owners. This overriding tendency to favor the nonprofessional and to disfavor the professional surfaces even in decisions that seem at first
B. The Normative Soundness of the Professional-Nonprofessional Distinction

To many, heightened protection of the “little person” nonprofessional is on its face a proper, and indeed powerful, desideratum. For others, however, articulating a more detailed and context-specific defense of this approach is necessary. At least with respect to priority disputes concerning limited account transfers, such a defense can be mounted. Stating that defense is helped by looking at the account transfer from three different angles: first, from the point in time the transaction is initiated; second, from the point in time that the court must untangle problems that the account transfer has created; and third, from a broader instrumentalist perspective of facilitating efficient transactions.

View One: Viewed from the front end of the transaction, the distinction between professionals and nonprofessionals reflects differences in the relative abilities of these two groups of assignees to protect their own interests. Professionals should and do know about U.C.C. filing rules; nonprofessionals, understandably, often do not. That the filing

552. A good example is provided by American East India Corp., in which the court found that a commercial financer had priority over an import-export company, the nonprofessional financer, as to an account. 400 F. Supp. at 162-65. The court nonetheless went on to conclude that amounts paid representing the import-export company’s performance on the contract were not Article Nine proceeds and, therefore, were not covered by the commercial financer’s security interest. Id. at 165-68. Accordingly, the account debtor’s payment to the commercial financer was improper.

Using a theory of conversion, however, the court awarded to the commercial financer the amount in excess of that which was attributable to performance by the nonprofessional financer. The nonprofessional financer thus was entitled to reimbursement of its performance expenses. Id. at 168-69. The bottom line was that the nonprofessional financer—although “second in time” in every respect—was given virtually all the account proceeds. See also Sun Air Int’l, 24 Bankr. at 137 (protecting nonfinancial institution assignee by applying Section 9-302(1)(e) even though court properly holds Section 9-104(f) inapplicable to account transfer).

553. See, for example, Lake River Corp. v. Carborundum Co., 769 F.2d 1284, 1289 (7th Cir. 1985) (Judge Posner) (noting that “substantial corporation” is “well able to avoid improvident commitments”).

554. Wholly apart from the filing rule, professional account lenders and factors are better positioned to evaluate the circumstances and trustworthiness of account transferors through use of such mechanisms as credit reporting agencies and to call on lawyers or other business specialists to obtain subordination agreements. See Jackson and Kronman, 88 Yale L. J. at 1159 & n.89 (cited in note 441) (suggesting appropriateness of fixing priority rules based on “the comparative advantage [some] creditors enjoy in obtaining and assessing information about the debtor’s behavior”); Rauer, 39 Stan. L. Rev. at 250 (cited in note 441) (stating that because “[b]anks are large institutions” they can “fairly easily” conduct such activities as “negotiat[ing] subordination agreements” and “look[ing] for other collateral”).
rule (unlike, for example, the rule of duress or fraud) imposes a purely formal requirement for perfecting a transaction is significant.\textsuperscript{555} Furthermore, the formality required by a filing rule is not natural;\textsuperscript{556} it is instead what might be called a technical requirement, akin to the rule that a promise is enforceable only if memorialized in a sealed writing.

Whenever a legal system imposes such technical requirements, it necessarily favors professionals because they, by reason of the very fact that they are professionals, are better able to learn of, assimilate, and comply with such rules. Put another way, the adoption of technical requirements—like the U.C.C. filing requirement—alters legal baseline rules in favor of professional players. Recognition of a principle that mitigates the rigor of a technical requirement for nonprofessionals thus provides a sort of compensating tradeoff to nonprofessionals for adopting the technical legal requirement in the first place.\textsuperscript{557}

View Two: An approach to perfection and priorities that favors nonprofessional assignees over professional assignees also is justifiable when viewed from the back end of the transaction. At bottom, perfection and priority rules dictate who should bear a risk of loss.\textsuperscript{558} Indeed, the basic first-to-file rule is defensible on risk-allocation grounds because the initial transferee can best avert loss by promptly notifying other prospective secured parties of the earlier transfer. Thus, a failure to provide such notice—including by a nonprofessional—may be said to justify subordination of the transferee whose failure to provide such warning presumptively results in the loss caused by multiple transfers.

Significant reasons exist, however, for saying that professional account transferees are generally better loss bearers than are nonprofessional assignees. The first reason is elementary: the uncollectibility of an account is more likely to produce serious harm to the nonprofessional assignee than the professional. To a family farmer or business proprietorship, the failure to collect a transferred account—even a small one—may be catastrophic. A similar result is not likely for the

\textsuperscript{555} See generally Lon L. Fuller, Consideration and Form, 41 Colum. L. Rev. 799 (1941) (discussing the rationales behind legal formalities).

\textsuperscript{556} See id. at 815.

\textsuperscript{557} Another argument for special treatment of nonprofessionals is that “[f]ailure by the first secured party to file notice of his security interest can be interpreted as a per se category of conduct intended to cause others to rely to detriment upon the debtor's assets.” Phillips, 92 Yale L. J. at 250 (cited in note 542). When a secured party is unaware of the filing system, however, attributing such an intention-based culpability to that person is difficult. See id. Reliance on this sort of rationale “must be made cautiously,” lest incentives for careless conduct by nonprofessionals be created. See id. at 265-66 n.141. But if operative rules restrict professionals' exposure to nonprofessional non-filers to limited account transfers, it seems improbable that the incentives for careless conduct will be increased too much.

\textsuperscript{558} See id. at 228 (characterizing priority rules as determining who must suffer the loss after a failed transaction).
properly capitalized financial institution. Professionals also may be better loss bearers because generally they will value the proceeds of account collections less highly than "little person" nonprofessionals. This theory of a wealth-tied relativity of value is extremely controversial. To some observers, however, it may help explain the professional-nonprofessional distinction drawn by courts in account assignment cases.

A less controversial, and more powerful, justification for this distinction lies in the professional financier's superior practical ability to spread the risk of account-collection losses. Institutional financers engage in many transactions over extended periods of time with a wide variety of customers. They thus can adjust rates and prices to cushion against account-collection risks in a way that the painting subcontractor or other small businessperson cannot. This economic reality provides an appealing reason for saying that professional financers are generally better loss bearers than amateur account transferees.

View Three: Finally, judicial favoritism of nonprofessional account assignees may reflect a broader instrumentalist perspective focusing on economic efficiency. This is the case because applying the usual perfection rules to nonprofessional account transferees may well drive such transferees from the market altogether. If amateurs come to know or sense that they cannot safely purchase accounts unless they hire lawyers to file U.C.C. financing statements, they simply will not buy accounts. The resulting constriction of the class of potential account purchasers will, in turn, reduce competition for the purchase of these assets and thus frustrate wealth-maximizing transactions. This is especially true because banking and factoring institutions may have little interest in limited, one-shot transactions except at highly discounted prices. Subjecting nonprofessional account transferees to the ordinary

559. This assertion may be even more apt when an unanticipated loss of a value already being counted on is at stake.
560. Contrast Phillips, 92 Yale L. J. at 268-69 (cited in note 542) (noting that juries may "allocate loss according to the relative wealth of the contesting parties").
561. Id. at 265 n.141 (noting that "[f]actors such as size, wealth, and expertise might allow one commercial party to pool risk better than another and therefore dictate allocation of risk to that party, regardless of the other's negligence").
562. See Rauer, 39 Stan. L. Rev. at 250 (cited in note 441) (arguing that bank relying on set-off rights should normally lose "[b]ecause the bank can bear the burdens of risk and monitoring more cheaply").
563. See Architectural Woods, 562 P.2d at 250 (stating that "the casual assignee may not . . . take the time and resources to investigate outside sources of information").
565. See Daly, 610 P.2d at 402 & n.5; Abramson, 440 S.W.2d at 327 (noting assignor's inability to sell to professional factors "because of the small size of the accounts").
U.C.C. rules threatens to dry up an already limited pool of transferees for the small, nonrecurring account assignment.\footnote{Contrast Coogan, et al., \textit{Secured Transactions} § 7B.01[3][b] at 7B-7 (cited in note 8) (noting that automatic perfection rule for purchase-money financers of consumer goods results in part from fact “that consumer creditors do not typically search the record before lending”). One objection to this argument rests on the proposition that affording special protection to nonprofessionals imposes economic costs. Economic losses—in terms of both lost claims to security and heightened dispute-resolution costs—will result from the presence of multiple, conflicting assignments generated by the nonprofessional’s authorized failure to file. Also, the professional market for limited assignments may contract once professionals interested in such transactions recognize the risk of subordination to valid, unfiled assignments. If professionals have only a limited interest in limited assignments, however, these costs should be minimal. In addition, if some professionals wish to pursue this business, they should be able to fix rates in such a way as to cover these risks without having to flee the market altogether. The economic calculus in this area is complex. For the reasons set forth in the text, however, considerations of economic efficiency may weigh at least as much for as against special protection of nonprofessional account assignees.}

Arguably, all these arguments for favoring nonprofessional account assignees are unpersuasive because they prove too much. The U.C.C. filing rules generally impose technical requirements on all parties who take security interests and put the risk of loss on all secured parties who fail to file or otherwise perfect those interests. Article Nine usually does not give special treatment to nonprofessional secured parties. Why then should the law afford special treatment to nonprofessional secured parties who take account transfers?

One possible response to this question is that account assignees should not receive special treatment. This conclusion does not suggest that nonprofessional account transferees should be treated the same as professional assignees as a normative matter. Rather, it suggests that all nonprofessionals should receive an added measure of protection under Article Nine.

The more fundamental point, however, is that significant reasons do exist for structuring the law to be more protective of nonprofessional account transferees than other nonprofessional secured parties. At least three considerations indicate why.

The first consideration flows from Article Nine’s coverage of both collateral and outright assignees of accounts.\footnote{See notes 73-76 and accompanying text.} Outright transferees of accounts may well liken themselves more to buyers of property, who...
ordinarily need not concern themselves with filing rules, than to orthodox collateral-taking secured parties, who certainly should be so concerned. Given that many nonprofessional account transferees may view themselves as buyers, rather than as financers, giving them a break in establishing filing requirements seems proper because they understandably will not focus on using the Article Nine filing system at all. This thought led the original drafters of Article Nine to conclude that there was a class of transactions, which “no one would think of filing,” that properly should be excluded from the Code’s filing requirement.\textsuperscript{8}

Second, there exists a sort of perfection trap for the nonprofessional account transferee that does not exist for collateral transferees of other forms of property. This is so because the nonprofessional account transferee might well assume that his interest is as protected as it can be once he, without incident, provides notice of the assignment to the account debtor. Nonprofessional collateral transferees of other forms of property cannot be tricked in this way, for there is no account debtor to advise of the property transfer. Non-account transferees thus may more properly be expected to discover and use another way of telling the world of their interest—namely, the U.C.C. filing system.\textsuperscript{9}

Finally, from the perspective of creditors competing with the nonprofessional secured party, an important difference exists between accounts and other forms of property. This is so because of the built-in and distinctive precariousness of account collateral.\textsuperscript{7} For example, a party with a possessory security interest in a harvester would be shocked to find that security interest subordinated to an unfiled security interest held by a nonprofessional. Even fully perfected assignees of account collateral know, however, that their interests are readily subject to divestment or diminishment in any number of ways. In particular, the account debtor may assert against that assignee any defense and many set-offs that are available against the assignor, even though the assignee lacks any knowledge of such defenses or set-offs.\textsuperscript{571} To subject

\begin{footnotes}
\textsuperscript{568} See U.C.C. § 9-302 cmt. 5.

\textsuperscript{569} Secured parties who take instruments or chattel paper could fall into this trap. It seems more likely, however, that nonprofessional transferees of such collateral will naturally protect their interests by taking possession of the documentary collateral. See U.C.C. § 9-305. This mode of perfection is not available to the account transferee. See notes 88-91 and accompanying text.

\textsuperscript{570} As numerous commentators have documented, a floating lienholder may find that contract-based payment rights prove uncollectible for a host of reasons. Clark, \textit{The Law of Secured Transactions} ¶ 11.01 at 11-3 (cited in note 8) (calling such collateral “precarious”); Corbin, \textit{Corbin on Contracts} § 395 at 591 (cited in note 6); Henson, \textit{Handbook on Secured Transactions} § 3-14 at 52 (cited in note 8); Coogan and Gordon, 76 Harv. L. Rev. at 1568 (cited in note 31) (noting that accounts financers traditionally have followed the pattern of operating “a little bit scared”); Zubrow, 68 Minn. L. Rev. at 916 (cited in note 75) (discussing the risk of fraud by the debtor); Gilmore, 74 Yale L. J. at 227-60 (cited in note 448).

\textsuperscript{571} U.C.C. § 318(1)(a), (b). For a discussion of this subject, see Gilmore, \textit{Security Interests}
professional transferees of accounts to the additional risk of subordi-
nation to a competing nonprofessional assignee thus is qualitatively differ-
ent from creating a similar risk for transferees of other types of
property. Imposing such a risk on a first-filing professional account as-
signee does interfere with that person's contracted-for expectancy.
Given the many qualifications that already crowd that interest, how-
ever, it does so in only a limited way.

C. The Propriety of Using the Professional-Nonprofessional
Distinction in Account-Priority Cases

All these considerations support, as an abstract matter, the judicial
instinct evidenced in the account-priority cases. As a substantive mat-
ter, distinguishing between the professional and nonprofessional as-
signee makes sense. Legal analysis, however, does not begin and end
with substantive reasoning. Courts also must heed formal rea-
sons—most importantly, reasons generated by the texts of operative
statutes. "[I]t must be stressed that the very concept of a formal rea-
son . . . entails that there are some circumstances in which coun-
tervailing reasons of substance cannot be used." Whether the text of a
statute overrides countervailing substantive reasons depends, in the
end, on the text's clarity or ambiguity. Does there inhere in Sections
9-302(1)(e) and 9-104(f) the sort of ambiguity that justifies the strong
professional-nonprofessional distinction courts have overlaid on those
provisions? Enough has been said already to explain why the proper
answer is no. Three additional observations might be offered, how-
ever, to suggest why strained efforts to find ambiguities in those provi-
sions is a particularly misbegotten venture.

First, Sections 9-302(1)(e) and 9-104(f) are part of a Code carefully
forged by experts to deal comprehensively with the subject of commer-
cial law. This is not to say that the Code is free of unclarity. It is to

in Personal Property §§ 41.1 to 41.11 at 1077-1126 (cited in note 2).
572. See note 547 and accompanying text.
573. See Atiyah and Summers, Form and Substance at 10 (cited in note 541) (emphasis orig-
nal in part and added in part). "The statute is not just one additional reason to be taken account
of by the judge, a reason which may tip the scales in one direction or be overridden by contrary
substantive arguments. The statute shuts out contrary arguments." Id. at 8.
574. See, for example, Western Union Tel. Co. v. F.C.C., 665 F.2d 1126, 1137 & n.21 (D.C.
Cir. 1987) (stating that a statute's plain meaning should be given priority in its construction”).
575. See, for example, notes 174-82, 215-42 and accompanying text.
576. See U.C.C. § 9-101 cmt.; Clark, The Law of Secured Transactions ¶ 1.01 at 1-3 (cited in
note 8) (proclaiming that the UCC is perhaps the most carefully drafted statute in history”). One
may or may not like the set of rules embodied in this comprehensive Code. Professor Carlson, for
example, finds that Article Nine establishes "a set of priorities that awards a bounty to experts for
locating and punishing amateur lenders." Carlson, 71 Minn. L. Rev. at 210 (cited in note 542). See
also id. at 209 (stating that "[b]ecause the experts heavily lobbied the drafters and the amateurs
say, however, that these Code provisions differ fundamentally from, for example, the Sherman Antitrust Act or the Fourteenth Amendment's Due Process Clause. Courts called on to apply the U.C.C. should not shrink from invoking policy to resolve genuine ambiguities. They should not be out, however, to find ambiguities behind every rock and bush.

Second, applying unrestricted notions of ambiguity to the Code threatens the Code's foundational objective of bringing simplicity and uniformity to commercial law. Again, courts certainly should see to it that Article Nine is "liberally construed and applied to promote its underlying purposes and polices." At some point, however, the Code's text must limit judicial discretion to pursue policy objectives, lest we end up with as many constructions of Code provisions as there are courts. Constraining purposive interpretation in this way not only enhances certainty and interstate uniformity; it advances more fundamental jurisprudential aims such as producing intelligibility in law and increasing the probability that similarly situated persons will be similarly treated.

Finally, the Code's framers knew how to write statutes that distinguish between professionals and nonprofessionals when they saw fit to do so. Many sections of Article Two draw this very line by making results turn on whether the contracting party is or is not a merchant.

578. See U.C.C. § 9-102. See, for example, Jensen, 1977 Utah L. Rev. at 341-42 (cited in note 74) (recognizing that "[t]here are special incentives for favoring the clarity and uniformity of statutory standards over the flexibility of judicially created standards in the area of defining the scope of Article Nine").
580. See Atiyah and Summers, Form and Substance at 26-27 (cited in note 541) (stating that "interpretive formality . . . tends to lead to more predictability").
581. Professors Atiyah and Summers cite these aims—as well as "freedom from official arbitrariness in the administration of the law"—as "more or less obvious justifications" for adhering to formal reasons. Id. at 24. They point out that adherence to formal reasons has the salutary effect of "controlling and limiting agendas" in the legal process, id. at 25, holding down dispute-resolution costs, minimizing the risk of error, and providing for "repose . . . in human affairs." Id. at 25-26. They also emphasize that "laws which can be identified solely by reference to their source or origin are in general easier to discover," id. at 26, and "make the law more certain and predictable," id. at 27.
582. The term "merchant" is defined in Section 2-104(1) as "a person who deals in goods of the kind or otherwise by his occupation holds himself out as having knowledge or skill peculiar to the practices or goods involved in the transaction or to whom such knowledge or skill may be attributed by his employment of an agent or broker or other intermediary who by his occupation holds himself out as having such knowledge or skill." Many Article Two provisions draw important
The Code’s drafters recognized no such distinction, however, in Sections 9-302(1)(e) and 9-104(f).

Questions of ambiguity are matters of degree. They are also, as this discussion suggests, matters of context. There are good reasons why courts applying the Code’s account provisions should respect the ordinary meaning of the words those provisions employ. Courts interpreting Sections 9-302(1)(e) and 9-104(f) have failed to heed this counsel.

VI. A Program for Reform

So what should be done to help along the law of account-assignment priorities? As we have seen, explicit statutory commands bar the courts, in most cases, from applying the sensible distinction between professional and nonprofessional assignees developed and defended in Part IV.583 To be sure, courts retain some freedom to draw this distinction in fashioning common-law rules.584 Manipulating the common law in a Code-dominated field, however, can do little to produce a sound and coherent body of law. The only real path to progress lies in the direction of statutory reform.

The opportunity for reform, as it turns out, is singularly ripe at the present moment. The Permanent Editorial Board recently formed a Study Committee “charged with recommending whether Article 9 and related provisions of the UCC are in need of revision.”585 That committee has just begun its work.586 Based on the analysis set forth in the preceding parts of this Article, my own recommendation is that that committee should propose significant revisions to Article Nine’s treatment of accounts. The most sensible program of reform would entail five key steps.

A. Step One: Extending the Code to All Contractual Payment Rights

As a first step, the revisors of Article Nine should modify the existing Code definition of “account” to include all contractual rights to all money payments. The Permanent Editorial Board declined to make this move in 1972 on the ground that parties had come to use the term...
“account” in security agreements in the technical and narrow sense that that term is used in Section 9-106.\textsuperscript{587} Thus, the Board concluded, a re-definition of the term could produce unpleasant surprises for those assignors who had assumed that they had transferred only traditional accounts when they used the term “account” in their security agreements.\textsuperscript{588} The easy answer to this problem—if it is a problem at all\textsuperscript{589}—is simply to choose a statutory term other than “accounts” to cover the newly expanded category of Code-covered contractual rights. The term “payment rights,” for example, would provide a suitable substitute.

Fine-tuning the Code’s definitional provisions to subject to Code rules all collateral and absolute transfers of contract-based payment rights would have three happy effects. First, it would eliminate the arbitrary results produced by defining the term “account” to cover only payment rights generated by transfers of goods and services.\textsuperscript{590} Second, a shift from the narrow term “account” to the broader concept of “payment rights” would eliminate irksome linedrawing problems that exist under the Code’s present language.\textsuperscript{591} Third, and most important, this definitional shift would set the stage for a desirable result: the comprehensive treatment within the Code of all priority conflicts involving all assignments of all commercially significant contract rights.\textsuperscript{592}

B. Step Two: Undoing the Section 9-104(f) Exclusions

In addition to expanding the Code category now called “accounts,” Article Nine’s revisors should reject the notion—now reflected in Section 9-104(f)—that many categories of account transfers should be excluded from the Code altogether. Instead, the committee should welcome the chance to extend Article Nine’s coverage to virtually all payment-right transactions.\textsuperscript{593} This shift in approach is sensible based

\textsuperscript{587} See notes 518-21 and accompanying text.
\textsuperscript{588} See id.
\textsuperscript{589} See notes 522-23 and accompanying text.
\textsuperscript{590} See notes 502-19 and accompanying text. The restricted character of the existing definition of the term “accounts” causes odd results, not only under the Code’s priority rules, but also in regard to the Code’s treatment of defenses available against the assignee of a contract right. See Coogan and Gordon, 78 Harv. L. Rev. at 1538 (cited in note 31) (noting defect in “the exclusion of receivables which are general intangibles from . . . 9-318”); Gilmore, Security Interests in Personal Property § 12.8 at 392 (cited in note 2) (stating that “[i]t is not clear why § 9-319(4) was not made applicable to all intangible claims”).
\textsuperscript{591} See, for example, note 517 and accompanying text.
\textsuperscript{592} But compare note 636.
\textsuperscript{593} There is perhaps good reason to continue to exclude wage assignments from Article Nine. See U.C.C. § 9-104 cmt. 4 (noting that such assignments “present important social problems whose solution should be a matter of local regulation”). Why governmental assignments or assignments of insurance proceeds or rental payments for realty should be excluded from Code coverage
on both the internal logic of the Code and broader considerations of policy. From a purely intra-Code perspective, Article Nine’s drafters undertook to deal comprehensively with those account transfers connected with commercial financing transactions.594 By adopting Section 9-104(f), however, the drafters undercut their own efforts because priority disputes fall outside the Code whenever they pit an institutional factor or account financer against a Section 9-104(f) transferee.595 To deal fully with “financing” assignments within the Code, no choice exists but to deal with “nonfinancing” assignments as well.

The revisors of Article Nine should also scrap the Section 9-104(f) exclusions because of broader policy considerations. The subject of account priorities has confused judges for a hundred years.596 Section 9-104(f) as prior analysis shows, continues to breed such confusion by injecting much complexity and nonuniformity into this field of law.597 No good reason exists why this should be so. No fundamental and divisive policy concerns justify differing treatment on a state-by-state basis of the account transfers enumerated in Section 9-104(f).598 Nor is the number of Section 9-104(f) cases so small as to be insignificant. The very existence of the Code, with its already substantial coverage of accounts, provides a golden opportunity to the revisors of Article Nine to deal in a genuinely comprehensive manner with all perfection and priority issues presented by contractual payment-right transfers.599

is less clear. See notes 528-30 and accompanying text. The proper treatment of deposit accounts presents a distinctive problem because of the recurring conflict between a security interest in a bank account and the depository bank’s right of set-off under state law. See notes 531-36 and accompanying text. Professor Zubrow has treated the subject of deposit-account transfers at great length. Her key conclusions are that (1) deposit-account assignments, at least of the collateral variety, should be included in Article Nine, Zubrow, 68 Minn. L. Rev. at 901; and (2) bank set-off rights should be treated like normal security interests that must be filed to secure perfection, id. at 907-08. I agree with the former conclusion. I am doubtful of the latter. Persons who lend money against deposit account collateral should be aware of the universal risk of the bank’s exercising set-off rights. For this reason and others, to require all banks to go through the motion of filing financing statements to make set-off rights as to all bank depositors operable vis-à-vis third parties seems to be a low-need and high-cost approach. See Clark, The Law of Secured Transactions ¶ 1.08[9] at 1-107 (cited in note 8) (stating that absent Section 9-104(f) exclusion of set-offs, “a blizzard of financing statements might be required”). Beyond this, I leave to others the task of developing sound priority rules in this area. See generally note 534 (collecting authorities).

595. See note 332 and accompanying text.
596. See notes 1-2 and accompanying text.
597. See notes 211-327 and accompanying text. Because some transfers of an account are covered by Article Nine while others are not, the Code carries forward a problem it sought to solve: resolution of priority problems “in the no-man’s land between the various security devices.” Gilmore, Security Interests in Personal Property at 655 (cited in note 2) (Introductory Note).
598. Contrast note 527 (discussing wage assignments); Zubrow, 68 Minn. L. Rev. at 911 (cited in note 75) (describing differential treatment of deposit accounts among states as “unwarranted”).
599. See generally Jackson and Kronman, 88 Yale L. J. at 1144 (cited in note 441) (recognizing that the “comprehensive and systematic treatment of priority questions” represented a “dis-
This is especially true because the legal setting of today differs greatly from the setting that prevailed when the Code was adopted. Because the Code has so long been in place, lawyers and businesspersons recognize that the Code governs most account transactions. As a result, there is far less reason to exclude large groups of account assignments wholesale from the rules of Article Nine. The revisors of Article Nine should not lose sight of the Code’s central and enduring purposes: to “simplify, clarify and modernize the law governing commercial transactions,” and “to make uniform the law among the various jurisdictions.” The revisors could do much to advance these objectives if they simply repealed Section 9-104(f) and put in place a uniform body of statutes governing all transfers of all contractual payment rights.

C. Step Three: Codifying the Professional-Nonprofessional Distinction

Once the revisors of Article Nine decide to formulate a new set of rules for contractual payment rights, they then must decide what those new rules will be. A good starting point would be to retain, as the general rule, the first-to-file principle of Section 9-312(5)(a). That rule has operated without dire effects for many years, builds on the investment long since made in the Code filing system, and continues to carry the advantages of straightforwardness and simplicity. In addressing the proper limits of this general rule, however, courts should not look to existing Code approaches, but instead to the evident judicial instinct to distinguish between professional and nonprofessional account transferees. To this end, the revisors should junk the unsuccessful significant part test of Section 9-302(1)(e), as well as the grab bag of assignments excluded from the Code by Section 9-104(f). In place of these excised sections, the revisors should identify a single set of payment-right transfers deserving of an exemption from the Code’s ordinary perfection and priority rules.

A suitable description of such transfers might well be as simple as this: “The assignment of payment rights to a nonprofessional transferee.” Properly construed, this nonprofessional assignee formulation

600. U.C.C. § 1-102(2)(a), (c). One commentator states: “The approach toward uniformity is one of the important advantages of the Code. The confusion of five separate sets of rules with many subvariations . . . seemed to impose a permanent burden on financing across state lines.” Craig, 42 B.U. L. Rev. at 207 (cited in note 92).
602. See notes 547-52 and accompanying text.
would serve to render the statute's protection inapplicable to three types of persons: (1) the financial institution; (2) the person who acts like a financial institution by regularly receiving account assignments; and (3) the person who takes an assignment so substantial in absolute size that that assignee is not fairly viewed as a nonprofessional.

A textual litmus that turns on whether an account transfer is to a nonprofessional assignee will raise difficult questions of application in some cases. That, however, is hardly catastrophic. First, uneven and undesirable results under this new standard will be mitigated by appropriate purposive interpretation by the courts. For example, courts confronting close cases can consider the specific assignee's ability to avoid, absorb, and spread account-collection losses in deciding whether the assignee qualifies as a nonprofessional. Second, some level of open-endedness is unavoidable, and indeed desirable, in framing any legal rule of this sort. The purpose of affording protective treatment to some, but not other, account transferees is to avoid otherwise harsh results for those assignees least able to protect their interests through compliance with technical legal requirements, and to absorb the effects.

603. See Coogan, et al., Secured Transactions § 3.08[8][b] at 3-65 (cited in note 8) (stating that “[i]f the assignee regularly takes assignment of accounts, it is not burdensome to require it to file”); Jensen, 1977 Utah L. Rev. at 343 (cited in note 74) (noting that “those assignees who regularly take assignments . . . have greater opportunity and motivation to investigate the coverage of Article Nine”). For an example of a case in which a nonfinancial institution acts like one, see In re Drapery Design Center, Inc., 86 Bankr at 124 (finding that nine assignments to individual lender over four months to secure at least $30,039 were neither casual nor isolated where lender made loans against assignor’s accounts “during the course of an unspecified number of years”).

604. Gilmore, Security Interests in Personal Property § 19.6 at 538 (cited in note 2) (citing “beneficent purpose of protecting assignees who are both insignificant and ignorant”). It might be proper to add a rule that states any transfers over a specified dollar amount—for example, $30,000—cannot qualify for this special protection. This limitation might be criticized as too rigid and arbitrary, but Article Nine establishes any number of rigid rules of a similar numeric character. For example, U.C.C. § 9-301(2) (requiring party with PMSI to file within 10 days of taking possession to defeat intervening lien creditors); id. § 9-312(4) (establishing similar 10-day rule for defeating earlier-filed non-PMSI). Such a rule might add a desirable level of certainty in applying this prong of the professional test.

605. An illustrative case is In re First Gen. Contractors, Inc., 12 U.C.C. Rep. Serv. (Callaghan) 762 (Bankr. S.D. Fla. 1971). There no filing was required for the transfer of a $25,000 account to secure a $25,000 loan made for “general operating purposes” to the borrower, a dry wall contractor, by Adobe Brick and Supply Company. The court concluded that the assignment was “casual and isolated,” so that no filing was required. It seems a bit of a stretch to say, however, that an assignment of a $25,000 account as collateral for a loan made for general operations qualifies as “casual.” A no less plausible description of the transaction is that a non-bank acted like a bank and then claimed—successfully—that it did not have to play by the same rules.

606. See note 579 and accompanying text.

607. See notes 553-62 and accompanying text.

608. See Baird and Jackson, 35 Stan. L. Rev. at 184-86 n.35 (cited in note 170) (stating that “[t]here is likely . . . to be a residual level of imprecision that cannot be cost-effectively removed”).
of account-collection losses. Achieving this largely rightness-based and backward-looking objective requires—as in many other contexts—a flexible legal tool. Holmes said that “[t]he life of the law has not been logic: it has been experience.” Experience, in the form of judicial treatment of the Code’s existing account provisions, teaches that something like the assignment-to-a-nonprofessional standard provides the proper rule for excluding accounts from ordinary Article Nine filing requirements. So, too, do those considerations of logic, collected in Part V, that support the distinction between professional and nonprofessional assignees. A statutory standard based on the professional or nonprofessional character of the assignee at the least should prove sounder than tests that focus on such dubious concerns as whether the assignment involves a significant part of the assignor’s accounts, was given in satisfaction of a preexisting debt, or otherwise falls within the welter of Section 9-104 exclusions.

Perhaps most important, the test proposed here carries the badge of intellectual honesty. There may be pragmatic reasons for leaving the existing Code provisions, like sleeping dogs, where they lie. Institutional financiers, for example, might balk at any statutory pronouncement that expressly discriminates in favor of nonprofessionals. Article Nine “populists,” on the other hand, may be willing to finesse the issue by continuing to count on courts to give nonprofessionals special protection by twisting the existing language of the Code. A respect for the rule of law demands more than this. Important rules ought not to sneak into the Code through judicial manipulation of the text and the inertia of those charged with overseeing the operation of Article Nine. A need exists for an honest assessment whether the professional-nonprofessional distinction has a proper role to play in fixing account priorities. If it does, Article Nine’s revisors ought to recognize that distinction

609. Atiyah and Summers, *Form and Substance* at 6 (cited in note 541).
610. See, for example, U.C.C. § 1-203 (stating rule of good faith); id. § 2-302 (stating rule of unconscionability). See also Ford, 22 Okla. L. Rev. at 481 (cited in note 112).
612. See notes 128-36 and accompanying text.
613. See notes 292-93 and accompanying text.
614. See notes 593-99 and accompanying text.
615. Contrast Zubrow, 68 Minn. L. Rev. at 921-22 (cited in note 75) (suggesting that the financial institutions’ self-interested lobbying efforts resulted in exclusion from Code of deposit account assignments and set-off rights).
616. See notes 572-82 and accompanying text.
617. See, for example, *McIntosh v. Murphy*, 469 P.2d 177, 181 (Haw. 1970) (straightforwardly acknowledging that reliance-based exception to Statute of Frauds “is to be preferred over having the trial court hew over backwards to take the contract out of the Statute of Frauds”).
explicitly, in a straightforward standard that courts can consistently apply.

D. Step Four: Forging Special Rules for Special Transferees

If the revisors choose to give special treatment to assignments to nonprofessionals, they then must decide what that special treatment will be. Three basic possibilities exist. First, nonprofessionals might be excused from filing, but required instead to perfect their interests by notifying the account debtor. Second, nonprofessionals might be afforded automatic perfection. Third, nonprofessionals might be afforded not only automatic perfection, but also automatic priority. On balance, the best choice is a general rule of automatic perfection, perhaps coupled with a rule of automatic priority for a very narrow class of the most-deserving nonprofessional assignees.

1. Notice-to-the-Debtor Perfection Versus Automatic Perfection

Should Article Nine provide that the nonprofessional assignee must notify the account debtor of the assignment to secure a perfected position? Reason exists to say that it should. Most important, such a rule would advance a basic goal of Article Nine's filing rules, even while excusing nonprofessionals from the technical and burdensome filing requirement. It would generate, at low cost, the dispersal of information about the assignee's otherwise undiscoverable interest to an identifiable source (namely, the account debtor) who could be readily consulted by later would-be transferees seeking to avoid reliance on the debtor's already-encumbered property. Additionally, such a rule probably would pose no major practical problems for nonprofessional assignees because they often will inform account debtors of their assignments anyway. Article Nine already provides strong incentives to provide such notice clearly and early on.

The very naturalness of providing such notice, however, also generates an argument against notice-to-the-account-debtor perfection. If such notice is likely to occur in any event, little need exists to mandate

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618. See Restatement (Second) of Contracts § 342 cmt. b (1979) (stating that "[t]he English rule has consequences similar to that of a system of public filing, except that the obligor acts as the filing office").

619. See also id. (noting that English rule is "somewhat more convenient where a single obligor is involved . . . than in cases of multiple obligors, as where a business concern assigns its accounts receivable").

620. See U.C.C. § 9-318(1)(b) (stating that "[u]nless 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 . . . any other defense or claim of the account debtor against the assignor which accrues before the account debtor receives notification of the assignment").
that it occur to protect third-party interests. This is especially true because conditioning a nonprofessional assignee's perfection on notice to the account debtor would engender difficulties of proof at odds with the Code's goals of creating simplicity and certainty in these transactions. Did the assignee actually give notice? To whom? At what time? In the proper manner? As to what account? As to all these matters, what does the account debtor have to say?

The inevitable uncertainty surrounding these questions will produce doubts about the security of the nonprofessional assignee's position, which are not easily reconciled with a decision to show special solicitude to the nonprofessional assignee in the first place. The nonprofessional assignee might minimize such uncertainty by providing a "bulletproof" form of notice, such as a professionally prepared declaration delivered by registered mail. To expect such deliberate and formal action, however, is little different from requiring perfection by filing. In the end, insufficient reason exists to impose on nonprofessional assignees one formal perfection requirement (notice) in place of another formal perfection requirement (filing). Rather, in keeping with the current Code's basic approach, the revisors should treat the interests of nonprofessional account transferees as automatically perfected. Affording automatic perfection to qualifying nonprofessionals will serve the critical purpose of protecting the small-scale assignee, who understandably fails to file, from the trustee in bankruptcy and subsequent lien creditors. It also will protect deserving nonprofessionals against the claims of later-filing professional assignees, without unduly hampering the practical ability of professional financers to buy or lend against accounts.

621. See id. § 9-302(1)(e).
622. See Page, 53 Wash. L. Rev. at 516 (cited in note 113) (noting that Gilmore viewed Section 9-302(1)(e) as basically "a line of defense in bankruptcy").
623. See notes 626-27 and accompanying text. In effect a rule of automatic perfection gives the professional filer one-half the benefit normally accorded the first filer by Article Nine. Although the professional first filer cannot "be confident [it] will prevail over earlier claimants," it can "determine the risks that [it] faces from subsequent property claimants," Baird and Jackson, 35 Stan. L. Rev. at 194 (cited in note 170) (emphasis added in part, original in part), which would be none at all. The professional account assignee may attack this "half-a-loaf" result for treating nonprofessionals too generously and departing dramatically from the ordinary priority principles embodied in Article Nine. It is, however, not much of a departure at all, since Section 9-302(1)(e) already embodies an automatic perfection rule that exposes the professional financer to exactly the same sort of risk the proposed standard creates.

In addition, the Code already affords a sort of super-priority to the first-filing professional assignee of accounts. Such transferees enjoy a distinctive protection against most competing security interest holders who claim accounts as proceeds. See notes 473-76 and accompanying text. Unlike holders of security interests covering all other forms of property, the holder of a perfected security interest in accounts faces no risk of divestment by a later good faith purchaser for value. Compare U.C.C. § 9-307 with § 9-309. Those who get special benefits from the law may more fairly
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2. Automatic Perfection Versus Automatic Priority

Affording automatic perfection to the nonprofessional who takes an account assignment will not protect such assignees if an institutional transferee already has recorded its interest. Such a previous filing frequently will exist because institutional financers often secure floating liens that cover all of an assignor's after-acquired payment rights. The risk of subordinating the automatically perfected nonprofessional's interest to such a competing claimant is troubling because the timing of that claimant's filing may be seen as a mere fortuity. Why on Earth should a nonprofessional who takes an assignment on Day 2 have priority over the bank that files on Day 3, but not the bank that files on Day 1? Because a basic purpose of singling out the nonprofessional is to excuse her from having to deal with the U.C.C. files, whether the nonprofessional could have discovered the professional assignee's previous filing if she had checked those files should not matter. As we already have seen, the case for special protection of the nonprofessional rests in part on the professional financer's superior capacity to bear and spread account collection losses. The professional's superiority in these respects, however, does not hinge at all on whether that professional's filing predated or postdated the assignment to a competing nonprofessional assignee.

Does it follow that the nonprofessional recipient of a limited account transfer should receive not only automatic perfection, but also automatic priority? On balance, probably not. Most important, a rule of automatic priority would clash with the Code's basic goal of removing the need for post-filing policing by a secured party who complies with Article Nine formalities. A rule of automatic perfection forces a professional financer to bear the risk that an account transferred to it already has been transferred to a nonprofessional prior to professional's filing. The professional financer, however, can fairly guard against this

be asked to bear special burdens. So it is with professional account assignees who might complain of an automatic perfection rule for nonprofessionals.

624. See note 31 and accompanying text.
625. See notes 558-62 and accompanying text.
626. See, for example, H. and Val J. Rothschild, Inc., 242 N.W.2d at 848 (stating that "Article 9 establishes a system of notice filing whereby a creditor by proper filing of a financing statement can rely upon his prior secured position as contained in a written security agreement"); Rauer, 39 Stan. L. Rev. at 245 (cited in note 441) (stating that "first-in-time principle . . . helps to fix the level of risk" and "relieves the creditor who is first in time of the burden of monitoring the debtor after extending credit"); In re Howell Enters., Inc., 105 Bankr. 495, 499 (Bankr. E.D. Ark. 1989) (subordinating constructive trust to floating lien, and stating that "[t]here are overriding policy reasons for insulating a secured creditor's lien rights in after-acquired property from attack by unrecorded claims similar to the claims asserted here"); U.C.C. § 9-312 cmt. 5 (emphasizing importance of removing need for later checking by first-filing secured party); Robert E. Scott, A Relational Theory of Secured Financing, 86 Colum. L. Rev. 901, 953-56 (1986).
risk before giving value, even outside the U.C.C. filing system, by checking with account debtors, by securing an affidavit from the assignor, and by examining, through credit agencies and others, the assignor’s character and veracity. In pre-Code days, this same risk of earlier unrecorded assignments was routinely put on professional financers—particularly those located in New York—by way of the strict first-in-time rule. Thus, a rule of automatic perfection for nonprofessionals puts an added, but limited, burden on professional account assignees.

A rule of automatic priority has far different and far graver effects. First, such a rule greatly increases the first-filing professional assignee’s risk of subordination. Under an automatic-priority rule, the professional assignee runs that risk against not only a pre-filing transferee, but also any nonprofessional assignee who takes an assignment at any time at all. This risk may mean that, as a practical matter, the professional financer that holds accounts as security will see herself as having no security at all. Such a perception could seriously deter much socially useful accounts financing, particularly by way of the future-oriented floating lien.

A rule of automatic priority also would greatly increase the debtor-monitoring costs of the professional financer. In effect, the professional assignee battling an automatic perfection rule must assure himself only at the time of the professional’s own filing that no prior transfers have occurred. A professional facing a rule of automatic priority, however, must monitor the assignor’s affairs continuously following his filing to ensure that his security remains sound. Insisting on ceaseless monitoring seems inefficient. More important, the burden simply might discourage valuable account transactions too much.

A rule of automatic priority carries with it the added risk that shady assignors will re-use accounts already subject to an honestly obtained and recorded security interest. This danger could be reduced by adoption of a rule that strips away priority whenever the nonprofessional takes an assignment with knowledge of the earlier-filed transaction. Knowledge, however, often is hard to prove, and a rule focusing on the transferee’s knowledge in large numbers of cases would diminish the salutary certainty provided by the first-to-perfect-or-file principle. Finally, the post-filing nonprofessional transferee—as opposed to the pre-filing transferee—at least could have discovered the earlier filing in the Article Nine files. Particulary for this reason, there exists a basis in fairness for preferring an automatic-perfection to an automatic-priority rule.

627. See notes 37-38 and accompanying text.
In light of all these considerations, the Code’s revisors should, as a general matter, afford to nonprofessionals only automatic perfection and not automatic priority. The policies supporting special treatment of nonprofessionals, however, may justify supplementing the rule of automatic perfection in one limited way: by adopting a rule of automatic priority for the nonprofessional assignee of a genuinely limited account assignment over a professional assignee who received an assignment that included a substantially greater dollar volume of additional collected or collectible accounts. To render this added protection less manipulable and more readily administered, the Code’s drafters also should specify that the nonprofessional can claim it only if the value of the accounts transferred to the nonprofessional is less than a stipulated amount—for example, $5000.

To afford this added protection to the genuinely limited assignment is defensible in light of the policies set forth above. First, the proposed rule would protect only the smallest of the small-time nonprofessional account transferees. In addition, it would subordinate only those professional assignees particularly well-positioned to absorb and spread the account collection loss, because of the necessarily small size of the lost account and the professional transferee’s continuing ability to realize other substantially greater accounts transferred by the same assignor. Finally, such a rule is not likely to unduly discourage or complicate professional factoring or accounts receivable financing. Rather, the continuing assurance that the large-scale professional assignee will, in all cases, remain able to collect the large majority of the customer’s transferred accounts—and be exposed, at most, to a risk of some $5000—should suffice to protect the professional assignee’s interests without forcing major changes in its business practices. Because the professional is a professional, it should be able to spread this limited, added risk through a modest adjustment of account prices or loan rates.

Undoubtedly, a rule of automatic perfection, supplemented by this narrow rule of automatic priority, will draw criticism from professionals and nonprofessionals alike. All priority systems, however, require some sort of compromise. 628 The compromise proposed here gives much to the professional financer; indeed, in many cases the professional financer should fare better under this set of rules than under existing Code-based law. 629 This compromise also gives broad benefits to nonprofessionals. Most important, it protects all nonprofessional transfer-

628. Baird and Jackson, 35 Stan. L. Rev. at 177 (cited in note 170) (noting that, with respect to rules allocating loss between innocent first and second filers, “some sort of compromise is inevitable”).

629. See, for example, note 154.
ees in those cases in which they seem to need protection most: bankruptcy cases. This is so because automatic perfection standing alone suffices to protect the claim of the qualifying nonprofessional against the bankruptcy trustee.620

There is much room for debate about the best perfection and priority rules for account transactions. All in all, however, much can be said for a rule that affords automatic perfection to nonprofessional assignees, coupled with a narrow rule of automatic priority reserved for the most appealing nonprofessional-assignee cases. Reflecting the policies operating in this field, this approach seems to steer a sensible middle course between the competing interests of professional and nonprofessional account assignees.

E. Step Five: Clearing Away the Underbrush of the Code's Account Priority Rules

At the very least, the revisors of Article Nine should clear away the excrescences of account-priority law built into the Code by Sections 9-312(4) and 9-301(1)(d). With respect to Section 9-312(4), the committee should clarify that secured parties can take PMSIs in payment rights when funds are provided for the purchase of those rights in the ordinary purchase-money sense.631 With respect to Section 9-301(1)(d), the committee should consider and decide expressly whether that section protects outright-buyer account transferees, Section 9-104(f) account transferees, or no account transferees at all.632

If the revisors follow the other recommendations set forth here, the proper way to deal with the Section 9-301(1)(d) problem is to remove any reference to accounts (or, to use the proposed nomenclature, "payment rights") in that section. As explained above, the best reading of Section 9-301(1)(d) is that it protects those account transferees, and only those account transferees, described in Section 9-104(f).633 Under the first two proposals set forth above, however, Section 9-104(f) would

630. See note 70.

631. An interesting and difficult question is whether the qualifying nonprofessional assignee should get the protections of the four-horsmen rule, see notes 41-43 and accompanying text, in addition to automatic perfection. Should a nonprofessional's security interest that would otherwise be subordinate to the security interest of an earlier filed floating lien nonetheless take priority if, for example, the nonprofessional collects the account in good faith? The answer to this question, in many cases, will be determined by the principles discussed in notes 488-501 and accompanying text.

632. See generally Comment, 41 Wash. L. Rev. at 905 (cited in note 336) (commenting that "Sections 9-301(1)(c) and (1)(d) of the Uniform Commercial Code are awkwardly, if not incomprehensively, drafted; they and companion section 9-104(f) appear to be in need of clarification, if not extensive revision").

633. See notes 364-99 and accompanying text.
not continue to exist. As suggested in the third proposal, there would continue to be value in protecting many of the nonprofessional account transferees now covered by Section 9-104(f). Those transferees, however, should receive ample protection, apart from Section 9-301(1)(d), under the fourth proposal’s newfangled rules of automatic perfection and limited automatic priority.

Any effort to implement these five proposals may require some clean-up work in addition to polishing away the rough edges of Sections 9-312(4) and 9-301(1)(d). That task, however, should not prove too difficult. A key advantage of the proposals made here is that they are, in their totality, straightforward and uncluttered. All payment rights are covered by the Code. These rights are divided into only two groups. Assignments to nonprofessionals get the benefit of automatic perfection, as well as the narrow and well-defined automatic priority described above. All other assignments of payment rights are subject to the Code’s ordinary prescriptions regarding perfection and priorities, including the first-to-file rule of Section 9-312(5). No obscure provisions exist and no extensive common-law rules overlay the Code.

The proposed statutory framework will generate tough questions, particularly regarding whether a given non-financial-institution assignee that takes a given assignment qualifies as a nonprofessional. At the same time, the proposed framework will prove less cumbersome and more intelligible than the existing crazy quilt of Code and non-Code rules that govern account priority conflicts. The Code seeks to clarify and simplify commercial law for the working businessperson and practicing lawyer. Judged by these critical criteria, the scheme proposed herein reflects a vast improvement over existing law, while advancing the felt need to protect deserving nonprofessional account transferees.

VII. Conclusion

For more than one hundred years, the law of account priorities has bred confusion and uncertainty. It is time for a change. Building on the professional-nonprofessional distinction recognized in the case law, the revisors of Article Nine should move to simplify and clarify the rules that govern these disputes. In the meantime, this Article seeks to offer

634. For example, the Code’s revisors would have to be mindful of possible priority conflicts between two nonprofessional assignees. Under the proposal made here—which simply affords nonprofessionals automatic perfection—such conflicts would be resolved in effect by the first-in-time New York rule.

635. This is true only if the term “payment rights” is defined not to include wages. See note 590 and accompanying text.

636. See notes 603-05 and accompanying text.

637. See note 578 and accompanying text.
aid to lawyers and judges forced to claw their way through the clutter of modern-day account-priority law.