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Tennessee Law and the Secured Transactions Article of the Uniform Commercial Code

*Charles Hampton White**

On July 1, 1964, the Uniform Commercial Code became effective in Tennessee. The author here explains the provisions of the Code dealing with secured transactions and compares these provisions with the former Tennessee law of secured transactions.

From the admission of Tennessee as a state in 1796, until midnight of June 30, 1964, there has never been any uniform, integrated set of laws or body of laws regulating the lending of money secured by personal property as collateral in this jurisdiction.[1] As the population and economy of the state have grown, new commercial practices have arisen and incident thereto, new types of financing schemes.

Some of the types of security transactions now used in Tennessee date back hundreds of years, even to the days of the common law of England.[2] Other types of loans secured by interests in personal property are of comparatively recent origin and stem from the ac-

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1. The 1962 Official Draft of the Uniform Commercial Code was enacted by the 83d General Assembly of Tennessee as chapter 81 of the Public Acts of 1963. It became effective July 1, 1964. Article 9 of the Uniform Commercial Code is codified as TENN. CODE ANN. §§ 47-9-101 to 47-9-507 (repl. vol. 1964). Tennessee thus became one of the twenty-eight states to enact the Uniform Commercial Code; the other states having so enacted it are:

State	*Effective Date*	*State*	*Effective Date*
Alaska	January 1, 1963	Montana	January 1, 1965
Arkansas	January 1, 1962	Nebraska	September 1, 1965
California	January 1, 1965	New Hampshire	July 1, 1961
Conneeticut	October 1, 1961	New Jersey	January 1, 1963
Georgia	April 1, 1963	New Mexico	January 1, 1962
Illinois	July 1, 1962	New York	September 27, 1964
Indiana	July 1, 1964	Ohio	July 1, 1962
Kentucky	July 1, 1960	Oklahoma	January 1, 1963
Maine	December 31, 1964	Oregon	September 1, 1963
Maryland	February 1, 1964	Pennsylvania	July 1, 1954
Massachusetts	October 1, 1958	Rhode Island	January 2, 1962
Michigan	January 1, 1964	West Virginia	January 1, 1954
Missouri	July 1, 1964	Wisconsin	July 1, 1965
		Wyoming	January 1, 1962

2. See Gilmore & Axelrod, *Chattel Security: I*, 57 YALE L.J. 517 (1948); Gilmore, *Chattel Security: II*, 57 YALE L.J. 761 (1948); Glenn, *The Chattel Mortgage as a Statutory Security*, 25 VA. L. REV. 316 (1939); Glenn, *The Conditional Sale at Common Law and as a Statutory Security*, 25 VA. L. REV. 559 (1939); Glenn, *The Pledge as a Security Device*, 24 VA. L. REV. 355 (1938); Note, 22 TENN. L. REV. 848 (1953).

tivities of the American Law Institute and the National Conference of Commissioners on Uniform State Laws.[3]

As Tennessee, along with the rest of the nation, shifted from the agrarian to the urban and industrial society, new types of commercial transactions came into use. The "pump priming" legislation of the gloomy days of the early 30's and the advent of the New Deal, coupled with the terrific inflationary boom during the two decades following World War II, have produced a national commercial society founded primarily upon credit. It is with this question of credit secured by interests of whatever nature in personal property as collateral, and how to lessen the risk of loss to the lender or secured party upon default of the borrower, that article 9 of the Uniform Commercial Code seeks to deal.

Historically, in Tennessee, loans secured by some form or type of pledge, assignment, transfer, mortgage, lien, or other security concept in or upon the property of a debtor have been classified into two groupings:[4]

> (a) Those in which the debtor seeks to borrow money and use items of personal property which he currently owns or intends to acquire as collateral; and
> (b) Those in which the debtor is in fact the purchaser and is "borrowing" the purchase money for a new item of consumer goods or equipment or inventory from a seller-lender and permitting or suffering the seller-lender to retain title to the chattel or personal property until the full purchase price is paid.

Although Tennessee has made great industrial and commercial progress since the end of World War II, large scale mercantile financing, such as on assignments of accounts receivable or inventory financing of the field warehousing variety, has not generally been conducted here; thus, the absence of a factor's lien statute[5] or the comparatively recent enactment of assignment of accounts receivable validation statute[6] has not seriously affected the existing financial

3. *E.g.*, TENN. CODE ANN. § 47-1001 (1956).

4. See Coogan, *Article 9 of the Uniform Commercial Code: Priorities Among Secured Creditors and the "Floating Lien,"* 72 HARV. L. REV. 838 (1959); Everett, *Securing Security*, 16 LAW & CONTEMP. PROB. 49 (1951); Gilmore, *The Secured Transactions Article of the Uniform Commercial Code*, 16 LAW & CONTEMP. PROB. 27 (1951).

5. Chapter 11 of title 47 of the Tennessee Code Annotated, entitled "Factors and Agents," could in no wise be considered a factor's lien statute such as N.Y. PERSONAL PROP. LAW § 45. For an excellent discussion of the historical development of the "factor's lien statute," see Skilton, *The Factor's Lien on Merchandise*, 1955 WIS. L. REV. 355, 609.

6. Chapter 114 of the Public Acts of 1959, entitled "Assignment of Accounts Receivable," was a hybrid of the validation and notice type of statute enacted by many states following the decision of the Supreme Court of the United States in Corn Exchange Nat'l Bank & Trust Co. v. Clauder, 318 U.S. 434 (1943). See generally, Dunham, *Inventory and Accounts Receivable Financing*, 62 HARV. L. REV. 588 (1949).

fabric nor created many serious problems under the existing statutory framework in Tennessee.

Under the present checkerwork pattern of Tennessee personal property security laws, if John Doe needs an additional one-thousand dollars in his business and assigns a portion of his accounts receivable; or if ABC Candy Company needs additional working capital and executes a chattel mortgage upon all of its present and future equipment; if Richard Roe must have one-hundred dollars until pay day and pledges his wife's diamond solitaire, all of these hypothetical situations involve two basic propositions:

(a) A loan of money; and
(b) A transfer, surrender, or assignment of existing or owned personal property by the debtor to the lender, pursuant to a pledge or mortgage to secure the credit risk involved.

Likewise, if John Doe seeks to buy a new television set from Ajax Appliance Company he normally executes a conditional sales or "title retained" contract; if Offset Printing Company, Ltd., seeks to purchase a new four-color rotary press for its printing plant, it is also likely to execute a conditional sales contract; if Sun Valley Motors, Inc., seeks to purchase a new supply of automobiles to increase its stock in trade, it will probably execute a trust receipt arrangement with the Equitable National Bank; all of these three hypothetical situations involve the same basic propositions as before: a purchase of new goods, whether inventory, equipment, or consumer goods, and a purchase money mortgage or an installment sale with a lien or title to the goods being retained by the seller-lender to secure the payment of the purchase price. All of these transactions involve credit, collateral, and risk of loss upon default, and turn, in part, upon the concept of title.

Why should Tennessee business men and Tennessee lawyers be forced to resort to such formal niceties as exist between a chattel mortgage on the one hand and a conditional sales contract on the other, and the disastrous consequences of selection of the wrong form for the wrong transaction, when in essence each of these situations represent the same basic factual and legal confrontation?[7]

Article 9 of the Uniform Commercial Code involves the most complicated and intricate of the myriad of new concepts incorporated into the Uniform Commercial Code. Due to the complexity of some of its sections and the extremely far-reaching questions posed therein, it is not possible in one article to present, analyze, and interpret, if

7. Birnbaum, *Article 9—A Restatement and Revision of Chattel Security,* 1952 WIS. L. REV. 349; Gilmore, *The Secured Transactions Article of the Uniform Commercial Code,* 16 LAW & CONTEMP. PROB. 27 (1951); Gilmore & Axelrod, *Chattel Security: I,* 57 YALE L.J. 517 (1948); Gilmore, *Chattel Security: II,* 57 YALE L.J. 761 (1948).

in fact interpretation at this time is possible, all of the many sections of article 9. Instead, an attempt will be made here to discuss the most basic provisions of article 9 and where possible to correlate those provisions with the existing laws of Tennessee. In many of the areas covered by article 9 there are no prior Tennessee decisions, since not all of the legislation which article 9 supplants or supersedes has been enacted here which the more influential commercial states have had in force for some period of time.

I. BACKGROUND AND SCOPE OF ARTICLE 9

By 1940, our economy was on the rise; lend-lease shipments to Britain boosted industrial output; expansion of our commercial society was necessary; credit was desperately needed throughout the nation. Yet, an overhaul of the varied assortment of security laws existing throughout the nation was also badly needed. The National Conference of Commissioners on Uniform State Laws and the American Law Institute began to study the overall problems presented. By 1952, a draft of the Uniform Commercial Code was ready for study and in 1954 was enacted in Pennsylvania.[8]

Article 9, entitled "Secured Transactions; Sales of Accounts, Contract Rights and Chattel Paper," is the draftsman's answer to the factor's lien acts, the Uniform Trust Receipts Act, the Uniform Conditional Sales Act, the various chattel mortgage acts, and each of the other various statutory enactments on security interests in personal property.[9] "Primarily, article 9 rationalizes and harmonizes concepts that were already in existence, but without functionally defined scope, and without unification."[10]

Section 9-102 sets forth the scope of article 9:

> (1) Except as otherwise provided . . . this Article applies so far as concerns any personal property and fixtures within the jurisdiction of this State
>
> (a) to any transaction (regardless of its form) which is intended to create a security interest in personal property or fixtures including goods, documents, instruments, general intangibles, chattel paper, accounts or contract rights; and also
>
> (b) to any sale of accounts, contract rights or chattel paper.
>
> (2) This Article applies to security interests created by contract including pledge, assignment, chattel mortgage, chattel trust, trust deed, factor's lien, equipment trust, conditional sales, trust receipt, other lien or title retention contract and lease or consignment intended as security. This Article does not apply to statutory liens except as provided in Section 9-310.

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8. See note 1 *supra*.

9. SPIVACK, SECURED TRANSACTIONS 1 (1963).

10. Kripke, *Article 9: Secured Transactions Under the Uniform Commercial Code in Pennsylvania*, 15 U. PITT. L. REV. 602 (1954).

Article 9 has thus swept away the cobwebs of title theories versus lien theories under the various chattel mortgage and conditional sales acts; the exciting and at times fascinating ideas of springing titles under the Uniform Trust Receipts Act; the questions of notice under accounts receivable financing statutes; and replaces them all with new concepts which apply equally to all transactions, regardless of form or purpose, but with some consideration given to the identity of the parties and their purpose in entering the transaction.[11]

To accomplish an updating of commercial law to correspond with modern commercial practices, to harmonize into one basic framework all aspects of the varied world of personal property security, article 9 utilizes new concepts, creates new terminology and definitions,[12] overrules the United States Supreme Court,[13] and probably attempts to govern a field which Congress has already preempted.[14]

II. The Security Interest and the Security Agreement

What each lender desires is some type of interest in the collateral of his debtor as security for his loan. Heretofore these interests have been called "retained titles," "liens," "equitable liens," among others. The Uniform Commercial Code creates as the one interest a secured party can obtain in personal property as collateral "the security interest" which section 1-201(37) defines as:

> "Security interest" means an interest in personal property or fixtures which secures payment or performance of an obligation. The retention or reservation of title by a seller of goods notwithstanding shipment or delivery to the buyer (Section 2-401) is limited in effect to a reservation of a "security interest." The term also includes any interest of a buyer of accounts,

11. Kripke, *Article 9: Secured Transactions Under Uniform Commercial Code in Pennsylvania*, 15 U. Pitt. L. Rev. 602 (1954); Spivack, *In Re Article 9*, 28 Temp. L.Q. 603, 605 (1955).

12. Spivack, Secured Transactions 17 (1963); Birnbaum, *Article 9—A Restatement and Revision of Chattel Security*, 1952 Wis. L. Rev. 349.

13. Tenn. Code Ann. § 47-9-205 (repl. vol. 1964).

14. Some sections of the Uniform Commercial Code, *e.g.*, Tenn. Code Ann. §§ 47-9-108, -9-205, -9-306 (repl. vol. 1964), by drastically changing existing commercial law, raise perplexing questions under the Bankruptcy Act and present some serious federal-state questions on how far state law will be controlling in resolution of questions involving the status of a secured party's claim to collateral in event of bankruptcy of the debtor. Moore v. Bay, 284 U.S. 4 (1931); *Cf.* International Shoe Co. v. Pinkus, 278 U.S. 261 (1929).

On the question of the interrelationship and the problem of preemption between the Bankruptcy Act and state laws on personal property security, see generally, Countryman, *The Secured Transactions Article of the Commercial Code and Section 60 of the Bankruptcy Act*, 16 Law & Contemp. Prob. 76 (1951); Hill, *The Erie Doctrine in Bankruptcy*, 66 Harv. L. Rev. 1013 (1953); Kennedy, *The Trustee in Bankruptcy Under the Uniform Commercial Code: Some Problems Suggested by Articles 2 and 9*, 14 Rutgers L. Rev. 518 (1960); Levy, *Effect of the Uniform Commercial Code upon Bankruptcy Law and Procedure*, 60 Com. L.J. 9 (1955).

chattel paper, or contract rights which is subject to Article 9. The special property interest of a buyer of goods on identification of such goods to a contract for sale under Section 2-401 is not a "security interest," but a buyer may also acquire a "security interest" by complying with Article 9. Unless a lease or consignment is intended as security, reservation of title thereunder is not a "security interest" but a consignment is in any event subject to the provisions on consignment sales (section 2-326). Whether a lease is intended as security is to be determined by the facts of each case; however, (a) the inclusion of an option to purchase does not of itself make the lease one intended for security, and (b) an agreement that upon compliance with the terms of the lease the lessee shall become or has the option to become the owner of the property for no additional consideration or for a nominal consideration does make the lease one intended for security.

It will be immediately observed that this definition includes the interests of a buyer of accounts, chattel paper, or contract rights on the basis that his interest is more closely akin to those of the secured lender-seller and, therefore, should be treated and governed by the same rules and concepts.

Since the "security interest" is intended to apply to all transactions, regardless of form, and supplants all previously existing security devices,[15] with certain minor exceptions,[16] the creation and existence of a "security interest" depends upon the execution or making of a security agreement. Section 9-105(1)(h) states that a "security agreement" means an agreement which creates or provides for a "security interest," and such agreement may rest in parol in the instance of possessory security interests, provided certain requirements are met.[17]

Of course, a security agreement creating a security interest would be a "mere sounding brass or tinkling cymbal" were it not supported by some type of consideration. The lender cannot have a security interest, pursuant to a security agreement, in any personal property

15. TENN. CODE ANN. § 47-9-102 (repl. vol. 1964).

16. TENN. CODE ANN. § 47-9-104 (repl. vol. 1964), excludes certain types of liens or other security interests from the coverage of the provisions of article 9. Among the exclusions are:

(a) A security interest subject to any statute of the United States;
(b) a landlord's lieu;
(c) certain liens given by statute for services or materials;
(d) assignments of wages;
(e) railroad equipment trusts;
(f) sale of accounts in connection with a sale of a business with a business;
(g) any claim under a policy of life insurance;
(h) rights reduced to judgment or available by setoff;
(i) interest in land; and
(j) transfers of tort claims, bank accounts, credit union interests, etc.

17. TENN. CODE ANN. §§ 47-9-203, -9-305 (repl. vol. 1964).

of the debtor as collateral for the security interest until he has loaned the debtor some money or has given to him "value."[18]

"Value" is one of the Uniform Commercial Code's new concepts and is defined by section 1-201(44) as:

> "Value." Except as otherwise provided with respect to negotiable instruments and bank collections (Sections 3-303, 4-208 and 4-209) a person gives "value" for rights if he acquires them
> (a) in return for a binding commitment to extend credit for the extension of immediately available credit whether or not drawn upon and whether or not a charge-back is provided for in the event of difficulties in collection; or
> (b) as security for or in total or partial satisfaction of a pre-existing claim; or
> (c) by accepting delivery pursuant to a pre-existing contract for purchase; or
> (d) generally, in return for any consideration sufficient to support a simple contract.

"Value" as thus defined, makes some radical departures from the existing law respecting secured transactions. Specifically is this true when this definition is considered alongside the provisions of section 9-108 which unequivocally state that after-acquired collateral is not to be considered as security for antecedent debt. The problems this concept of value raises are numerous, particularly in view of its obvious collision with section 60 of the Bankruptcy Act,[19] as well as the decisions in Tennessee which have dealt with mortgages involving personal property containing after-acquired property clauses.[20] "Value" thus defined, and section 9-108 also sharply conflict with the additional new concept of article 9 of the "purchase money security interest." These conflicts will more sharply appear when considered in section V of this article.

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18. SPIVACK, SECURED TRANSACTIONS 34 (1963).

19. Official comment 1 of Uniform Commercial Code § 9-108 seeks to avoid the preference problem under the Bankruptcy Act § 60, 64 Stat. 24 (1950), 11 U.S.C. § 96 (1958), by establishing two tests which must be met in order to qualify under § 9-108: (a) The secured party must have originally given new value at the inception of the secured transaction; and (b) the after-acquired property must come in either the ordinary course of the debtor's business or as an acquisition which is made under a contract of purchase entered into within a reasonable time after the giving of new value and pursuant to the security agreement.

Query: Whether these two limitations can save a secured party against a trustee in bankruptcy in a plenary suit brought under section 60(b) of the Bankruptcy Act?

20. *Compare* Phelps, Dodge & Palmer Co. v. Murray, 2 Tenn. Ch. 746 (1877), holding that a chattel mortgage of subsequently acquired goods or property having no connection with collateral *in esse* at the date of the execution of the chattel mortgage is void as to subsequent purchasers or attaching creditors, *with* Judge v. Jones, 99 Tenn. 20, 42 S.W. 4 (1897), which holds that a chattel mortgage may effectively and validly attach to property not in existence at the date of execution and such property may become original security for the original debt the chattel mortgage secures.

The draftsmen of article 9 were aware that the broad definitions of the security interest, coupled with the expansive provisions of section 9-204(3) dealing with after-acquired property, and section 9-204(5) dealing with future advances, might make a seller of consumer goods, equipment, or inventory extremely reluctant to sell such items to a debtor under an installment sale, or deferred time purchase type of contract, where the seller-lender was aware, through notices filed in the office of the Secretary of State, that the debtor had tied up all of his assets with one or more lenders under a "floating lien." In such a case, if it were not possible for the debtor to obtain new equipment from a dealer in equipment, his business could easily become stiffled.

Recognizing the need for some type of protection for the seller of equipment, inventory, or new consumer goods in general to secure the unpaid purchase price, and being aware of the historical priority which the law has accorded purchase money transactions,[21] section 9-107 creates a purchase money security interest which, as will be seen, stands on a higher and different footing from the "security interest" as defined in section 1-201(37). Section 9-107 defines the "purchase money security interest" as:

> A security interest is a "purchase money security interest" to the extent that it is
> (a) taken or retained by the seller of the collateral to secure all or part of its price; or
> (b) taken by a person who by making advances or incurring an obligation gives value to enable the debtor to acquire rights in or the use of collateral if such value is in fact so used.

Thus, despite all of the discussion concerning the "floating lien," a seller of consumer goods, equipment, farm equipment, or inventory under the provisions of article 9 can be as fully protected in so far as his purchase money security interest in the goods is concerned as he was prior to the enactment of the Uniform Commercial Code.

The traditional security agreement forms arose to meet the credit needs of particular types of debtors. The man purchasing a lawnmower had little in common with the manufacturer seeking new capital or new equipment for his plant. A farmer seeking funds with which to tide over a drought had little in common with the appliance dealer seeking new funds with which to purchase additional inventory. Article 9 recognizes that there are different classes of debtors, and although it does not define them in different terms, it recognizes their differing interests by classifying the most frequently used col-

21. See Gilmore, *The Purchase Money Priority*, 76 Harv. L. Rev. 1333 (1963).

lateral, "goods," into four categories which recognize the different types of debtors and the differing types of transactions they are likely to enter.[22] Section 9-109 classifies "goods" as follows:

> Goods are
> (1) "consumer goods" if they are used or bought for use primarily for personal, family or household purposes;
> (2) "equipment" if they are used or bought for use primarily in business . . . or if the goods are not included in the definitions of inventory, farm products or consumer goods;
> (3) "farm products" if they are crops or livestock used or produced in farming operations or if they are products of crops or livestock in their unmanufactured states . . . . If goods are farm products they are neither equipment nor inventory;
> (4) "inventory" if they are held by a person who holds them for sale or lease or to be furnished under contracts of service or if he has so furnished them, or if they are raw materials, work in process or materials used or consumed in a business. Inventory of a person is not be be classified as his equipment.

These classifications are important in many instances: in determining rights of a person who buys from a debtor goods held subject to a security interest,[23] in certain priority disputes,[24] in determining when and where to file notices of the security interest,[25] and in rights and remedies upon default.[26]

Modern commercial financing involves not only tangible personal property, or "goods" as set forth above, but also accounts, chattel paper, and general intangibles which are frequently the collateral on many types of substantial commercial loans involving acquisition of inventory or supplies and new working capital. The Uniform Commercial Code recognizes that commercial loans, secured by collateral in the form of documents, chattel paper, accounts receivable, and other intangibles, have assumed a major status in the credit structure of this state, as well as the more influential commercial states of the nation. In keeping with this effort to harmonize and integrate the various forms and devices used to effect security interests in personal property, including intangibles, it is necessary for the Code to use some new definitions for the new concepts it introduces into this phase of secured transactions. Yet as this type of collateral presents some problems which have not generally been encountered in Ten-

22. SPIVACK, SECURED TRANSACTIONS 42 (1963); Everett, *Securing Security*, 16 LAW & CONTEMP. PROB. 49 (1951).

23. TENN CODE ANN. § 47-9-307 (repl. vol. 1964).

24. TENN. CODE ANN. § 47-9-312 (repl. vol. 1964).

25. TENN. CODE ANN. § 47-9-401 (repl. vol. 1964).

26. TENN. CODE ANN. § 47-9-501 (repl. vol. 1964).

nessee and have been adequately treated elsewhere,[27] they will not be further discussed in this article.

III. ATTACHMENT OF THE SECURITY INTEREST IN THE COLLATERAL AND RIGHTS OF THE PARTIES THEREIN

A. *Formalities*

Assuming that the lender seeking security and the debtor have reached an agreement providing for a security interest in debtor's property, which is not otherwise unlawful under some other statute of this state, and that the security agreement has been reduced to writing and contains a description of the collateral, the security interest of the secured party attaches:

(a) When the security agreement states that it attaches.
(b) When value is given.
(c) When the debtor has rights in the collateral.

The security interest attaches as soon as the last of the three above events has occurred, unless the agreement explicitly postpones the time of attaching.[28]

Since section 9-204(3) provides that after-acquired property, whenever acquired, may also become subject to the security interest, the seeds of the much-discussed "floating lien" are planted.[29] Read together, section 9-204(1) and (3) suggest that the security interest created in the original collateral and in the after-acquired property stand on an equal footing. Official comment 2, section 9-204, suggests this result; but various writers have suggested that this security interest may be severable or standing on different levels, especially if there have been other creditors whose rights have intervened between the date of the original security agreement and the acquisition of the new collateral and the attachment thereto of the security

27. See, *e.g.*, Coogan, *Intangibles as Collateral Under the Uniform Commercial Code*, 77 HARV. L. REV. 997 (1964); Coogan & Gordon, *The Effect of the Uniform Commercial Code Upon Receivables Financing—Some Answers and Some Unresolved Problems*, 76 HARV. L. REV. 1529 (1963); Kupfer, *Accounts Receivable, Trust Receipt, and Related Types of Financing Under Article 9 of the Uniform Commercial Code*, 27 TEMP. L.Q. 278 (1953); Note, 27 TEMP. L.Q. 91 (1953).

28. TENN. CODE ANN. § 47-9-204 (repl. vol. 1964).

29. The term "floating lien" is nowhere used in the text of the Uniform Commercial Code. Official comment 3, Uniform Commercial Code § 9-204, alludes to the concept of a "floating lien" when it says: "This article accepts the principle of a 'continuing general lien' which is stated in Section 45 of the New York Personal Property Law and other similar statutes applicable to 'factor's liens'."

The phrase "floating lien" was greatly discussed in the hearings conducted by the New York Law Revision Commission. See 2 N.Y. LAW REV. COMM'N REPORT 67-71 (1954).

interest pursuant to the after-acquired property clause.[30] Actually, section 9-204(1) and (3), together represent the theory of a continuing general lien contained in the various factor's lien laws of the more important commercial states, such as New York. This is a significant and radical departure from the existing law in this state and of many other states as well.[31] It has been severely criticized by some authorities as permitting the unscrupulous lender to force the debtor to encumber all of his assets, present and after-acquired, as security for a present loan; others believe that such a transaction is intended and in fact desired by the modern businessman of today.[32] Whatever the view taken, this section is the vanguard of the controversy, if such actually exists, concerning the "floating lien." It is significant in this connection that article 9 does not in any of its many sections contain any clause condemning or striking down a security agreement as "unconscionable" as comparable to section 2-302 of the sales article.[33] Yet section 1-203 of the Code imposes and incorporates into every contract or duty within the Uniform Commercial Code the obligation of good faith in performance and enforcement. Perhaps this is a recognition by the draftsmen that most of the parties to security agreements are sui juris, normally business men who are capable of hard bargaining in their own behalf.

In accordance with article 2 and the provisions of the sales article, article 9 also abolishes the concept of title.[34] This is necessary if there is to be but one form of "security interest" and one "security agreement." The official comment to section 9-202 suggests that in situations in which interests of third parties may be involved, such as a trustee in bankruptcy or a lien creditor, the status of title to the collateral will be determined according to "other rules of law or the

30. *Compare* Coogan, *A Suggested Analytical Approach to Article 9 of the Uniform Commercial Code*, 63 COLUM. L. REV. 1 (1963), suggesting that the security interests may be severable and exist independently of each other, *with* Gordon, *The Security Interest in Inventory Under Article 9 of the Uniform Commercial Code and the Preference Problem*, 62 COLUM. L. REV. 49 (1962), in which it is suggested that the security interest may attach to inventory as an "entity" by which there would be only one transfer by the debtor to the secured party; thus no problem under TENN. CODE ANN. § 47-9-108 (repl. vol. 1964), and thus, no preference problem. See Manchester Nat'l Bank v. Roche, 186 F.2d 827, 831 (1st Cir. 1951), for a scholarly discussion of the "entity" theory of inventory under a factor's lien act providing for a continuing general lien.

31. See note 5 *supra*.

32. *Compare* 2 N.Y. LAW REV. COMM'N REPORT 1079 (1954), *with* Coogan, *Article 9 of the Uniform Commercial Code: Priorities Among Secured Creditors and the "Floating Lien,"* 72 HARV. L. REV. 838, 876 (1959). See generally, SPIVACK, SECURED TRANSACTIONS 9 (1963); 2 N.Y. LAW REV. COMM'N REPORT 1011 (1954).

33. While "unconscionable provisions" are not condemned in article 9, it is evident that the draftsmen sought to afford some greater degree of protection to certain types of debtors, *e.g.*, consumers. TENN. CODE ANN. §§ 47-9-504, -9-505 (repl. vol. 1964).

34. TENN. CODE ANN. § 47-9-202 (repl. vol. 1964).

agreement of the parties . . . ."[35] It is submitted that section 9-202, abolishing the concept of title, while perhaps desirable in determining risks of loss and other corollary questions which frequently arise under a contract of sale, is an open invitation to litigation under article 9. In the event of bankruptcy of the debtor, to what items of property does his trustee in bankruptcy take title under section 70 of the Bankruptcy Act?[36] Clearly, the concept of title is vital in this area and section 9-202 leaves many questions unanswered.

The formalities required by section 9-203 for a security agreement are quite simple: the debtor must sign a security agreement which contains a description of the collateral; or, the collateral must be in the possession of the secured party at the time of making the agreement.[37] Thus, incorporated into article 9 is its own unique provisions respecting the Statute of Frauds in so far as secured transactions are concerned. Unless the secured party is in possession of the collateral by means of a pledge, or other type of possessory security interest at the time the security agreement is made, the security will not be enforceable against the debtor unless it is in writing and signed by him.[38] In this connection, it is worthy to note that article 9, in most instances, has codified the common law of the pledge as it exists in Tennessee. Thus, since it represents no serious change from the existing law respecting pledges, only occasional references will be made to pledges or other possessory types of security interests herein.[39]

B. *Proceeds*

To the secured party whose collateral is either inventory, which will obviously be depleted as sales in the ordinary course of business are made by the debtor, or accounts receivable, which will diminish as the account debtors remit their payments to the creditor, the concept of "proceeds" becomes crucial. If the security interest extends

35. UNIFORM COMMERCIAL CODE § 9-202, official comment.

36. 30 Stat. 565 (1898), as amended, 11 U.S.C. § 110 (1958). "The trustee in bankruptcy gets the title to all property which has been transferred by the bankrupt in fraud of creditors, or which prior to the petition he could by any means have transferred, or which might have been levied upon and sold under judicial process against him." Moore v. Bay, 284 U.S. 4, 5 (1931).

37. TENN. CODE ANN. § 47-9-203(1)(9)(b) (repl. vol. 1964). It should be observed that § 47-9-203 subjects the validity of the security agreement to contrary provisions of other statutes which will prevail in the event of conflict. Thus, TENN. CODE ANN. § 45-2101 (1956), entitled "Lenders of Money," TENN. CODE ANN. § 45-2001 (1956), entitled "Industrial Loan and Thrift Companies," TENN. CODE ANN. § 45-1801 (1956), entitled "Credit Unions," TENN. CODE ANN. § 45-2201 (1956), entitled "Pawn Brokers," and TENN. CODE ANN. § 47-1901 (Supp. 1963), entitled "Retail Installment Sales," must be consulted in determining the validity of any security agreement, written or oral, pursuant to § 47-9-203.

38. Coogan, *A Suggested Analytical Approach to Article 9 of the Uniform Commercial Code*, 63 COLUM. L. REV. 1, 17 (1963); Note, 22 TENN. L. REV. 776 (1953).

39. *Ibid.*

only to the collateral, and unless it is replaced by substitutions, it withers away, leaving the secured party secured but with no collateral as security. Of course, the problem of proceeds has other aspects as well. Recognizing that a secured party would not advance money on the type of collateral mentioned unless something is done to protect his interest in the "proceeds," section 9-203, by including "proceeds" within the definition of the word "collateral," makes it possible for the security interest to shift from the first tier collateral, the inventory or accounts receivable, to the second tier collateral, the "proceeds" which stands as the substitute for the original collateral. Thus, another step has been taken toward the creation of the "floating lien" problem. Such a security interest was possible under section 10 of the Uniform Trust Receipts Act, with some reservations;[40] however, it could not be accomplished under a conditional sales contract or a chattel mortgage agreement.

C. *After-Acquired Property*

There has been some confusion among the decisions in Tennessee regarding the validity of mortgages of personal property which contain after-acquired property clauses: one case suggests that a valid mortgage may be made of property not in existence at the date of the execution of the mortgage; another suggests that a mortgage of subsequently acquired property having no connection with the property actually in existence at the date of execution of the mortgage is void as against subsequent purchasers or attaching creditors.[41] Section 9-204 resolves any confusion on this subject and accepts the principle of a "continuing general lien" on all of the property of the debtor.

> It rejects the doctrine—of which the judicial attitude toward after-acquired property interest was one expression—that there is reason to invalidate as a matter of law what has been variously called the floating charge, the free-handed mortgage and the lien on a shifting stock. This Article validates a security interest in the debtor's existing and future assets, even though . . . the debtor has liberty to use or dispose of collateral without being required to account for proceeds or substitute new collateral.[42]

Of course, a security agreement cannot create nor can a security interest exist in any type of collateral unless the debtor has rights therein; however, section 9-204(1)(3) permits the debtor to grant to a secured party, not only a security interest in the goods which the debtor has *in esse* at the time of execution of the agreement, but also

40. See Note, 66 YALE L.J. 922 (1957).
41. See note 19, *supra*.
42. UNIFORM COMMERCIAL CODE § 9-204, official comment 3.

a security interest in such goods as he may acquire thereafter. The security agreement may provide not only for present advances by the secured party, but may obligate him to make future advances as well.

These provisions involving after-acquired property and future advances may not be so drastic as might first appear. The security agreement may well provide for a future advance on the strength of existing collateral; it may also provide for future advances to be secured by future or after-acquired collateral. The secured party will receive no additional security interest in any after-acquired goods under an obligation to make future advances, unless the future advance is actually made. Viewed within this framework it is not so shocking for the debtor to grant a security interest in after-acquired goods where the secured party may also be obligated to make future advances as the goods are acquired.[43]

The inter-relation between the two concepts of after-acquired property and future advances presents an interesting question. For the purposes of perfection,[44] the security interest in the after-acquired property relates back to the date of the original perfection of the original security agreement by the filing of the financing statement. Yet, does the secured party have one single unified interest in all of the debtor's property, both that which was in existence at the date of the attachment of the security interest originally and that subsequently acquired by virtue of the after-acquired property clause? Or does the security interest split into more than one, existing simultaneously under the same security agreement?[45] What effect, if any, would the appearance of a lien creditor, such as a trustee in bankruptcy, make in the interim?

The after-acquired property clause of a security agreement is limited in scope by section 9-204(4)(a)(b) to crops which become such less than a year after execution of the agreement and consumer goods, unless the consumer acquires rights in such goods within ten days after the giving of value. Otherwise, in the commercial or business world the Uniform Commercial Code places no restrictions on the use of the after-acquired property clause among persons who are sui juris.

43. *Ibid.*

44. See seetion IV *infra.*

45. *Compare* Gordon, *The Security Interest in Inventory Under Article 9 of the Uniform Commercial Code and the Preference Problem,* 62 Colum. L. Rev. 49 (1962), in which the "entity" theory of inventory collateral is elaborately discussed, *with* Coogan, *A Suggested Analytical Approaeh to Article 9 of the Uniform Commercial Code,* 63 Colum. L. Rev. 1, 14 (1963), in which the suggestion is made that Uniform Commercial Code § 9-204, in effect creates not one security interest, but a series of security interests which arise from time to time.

D. *Retention or Commingling of Proceeds*

Thirty years ago the mention of the doctrine of *Benedict v. Ratner*,[46] was sufficient to make factors tremble. It was almost as frightening to them as "kiting" was to bankers. Many courts in various states were swayed by the eloquence and reasoning of Mr. Justice Brandeis and blindly followed the implication of this decision, perhaps without recognition of the fact that it was merely a decision of the Supreme Court of the United States on a question of the law of the State of New York.[47] Simply stated, *Benedict v. Ratner*, held, that a debtor who has and exercises unfettered dominion or control over collateral, in effect, voids the security interest of the secured party. Mr. Justice Brandeis spoke of the disdain with which the law looks upon the secret lien and its general prejudice against covert security devices. Factors and other lenders, financing on the strength of inventory or accounts receivable as their collateral and fearing with justification the extension of this doctrine, ingenuously devised expensive schemes, such as field warehousing, to enable the debtor to obtain possession and yet maintain his security interest.[48] Such schemes greatly increased the cost of obtaining money to a debtor; proved extremely cumbersome in practice; and often diminished the debtor's standing in his commercial community. Section 9-205 expressly overrules, in effect, the decision in *Benedict v. Ratner*, as well as a series of decisions in Tennessee,[49] and states:

> A security interest is not invalid or fraudulent against creditors by reason of liberty in the debtor to use, commingle or dispose of all or part of the collateral (including returned or repossessed goods) or to collect or compromise accounts, contract rights or chattel paper, or to accept the return of goods or make repossessions, or to use, commingle or dispose of proceeds, or by reason of the failure of the secured party to require the debtor to account for proceeds or replace collateral. This section does not relax the requirements of possession where perfection of a security interest depends upon possession of the collateral by the secured party or by a bailee.

Section 9-205 not only presents interesting questions under the law of the State of Tennessee by expressly overruling a series of local decisions, but presents some interesting federal questions in the application of the provisions of the Bankruptcy Act. It would seem that in

46. 268 U.S. 353 (1925).

47. See 4 COLLIER, BANKRUPTCY § 70 (14th rev. ed. 1959).

48. SPIVACK, SECURED TRANSACTIONS 16 (1963).

49. Morgan Bros. v. Dayton Co. & Iron Co., 134 Tenn. 228, 184 S.W. 1010 (1916); Bank of Cookeville v. Brier, 95 Tenn. 331, 32 S.W. 205 (1895); Bank of Rome v. Haselton, 83 Tenn. 216 (1885); R. W. McCrasly & Co. v. Hasslock, 63 Tenn. 1 (1874); Tenn. Nat'l Bank v. Ebbert & Co., 56 Tenn. 153 (1872); *but see* Hickman v. Perrin, 46 Tenn. 135 (1868); Cunningham v. G. F. C. Corp., 35 Tenn. App. 237, 244 S.W.2d 181 (W.S. 1951).

bankruptcy cases, wherein the provisions of section 9-205 were drawn in question regarding retention of possession, returned merchandise,[50] or commingling of proceeds, the provisions of the Bankruptcy Act and the decisions thereunder will prevail over contrary provisions, such as section 9-205 of the Uniform Commercial Code.[51] Could cash proceeds commingled by the debtor within ten days after bankruptcy be attacked by a trustee as a statutory lien, vulnerable under the provisions of section 67(c) of the Bankruptcy Act?[52] Or could the reattachment of the security interest, pursuant to section 9-205, on returned goods be attacked by the trustee as a preferential transfer voidable under section 60 of the Bankruptcy Act?[53] These are but two of several questions which have been raised regarding the interrelationship between section 9-205 and the various provisions of the Bankruptcy Act.[54]

IV. PERFECTION OF THE SECURITY INTEREST

Not only does a secured party want his money to be paid in accordance with the terms of the security agreement; he wants to be certain that in the event of a debtor's default, such as an equity receivership or a voluntary or involuntary bankruptcy, his security interest in the collateral will withstand, not only the competing claims of other creditors, but the attacks which might well be launched by the debtor's trustee in bankruptcy. The answer to this problem, in part, depends upon whether the secured party has "perfected" his security interest in the collateral.

Although none of the sections of article 9 define the words "perfect," "perfected," or "perfection," section 9-303 states that a "security interest is perfected when it has attached and when all of the applicable steps required for perfection have been taken." According to section 9-303, official comment 1, a security interest is "perfected" when the secured party has taken whatever steps are necessary to give him such an interest.[55]

50. *E.g.*, Lee v. State Bank & Trust Co., 38 F.2d 45 (2d Cir. 1930), *cert. denied*, 285 U.S. 547 (1932); Kennedy, *The Trustee in Bankruptcy Under the Uniform Commercial Code: Some Problems Suggested by Articles 2 and 9*, 14 RUTGERS L. REV. 518, 534 (1960).

51. Globe Bank v. Martin, 236 U.S. 288, 298 (1915); Moore v. Bay, 284 U.S. 4, 5 (1931), wherein it was held that in case of conflict, the Bankruptcy Act is "superior to all state laws."

52. See Kennedy, *supra* note 50, at 532.

53. *Id.* at 543.

54. See generally, Friedman, *The Bankruptcy Preference Challenge to After-Acquired Property Clauses Under the Code*, 108 U. PA. L. REV. 194 (1959); Gordon, *The Security Interest in Inventory Under Article 9 of the Uniform Commercial Code and Preference Problem*, 62 COLUM. L. REV. 49 (1962); Kennedy, *supra*, note 50.

55. "Perfection, as used in Article 9, in effect means the greatest bundle of rights with respect to personal property which it is possible for a party to obtain under the law of secured transactions." SPIVACK, SECURED TRANSACTIONS 33 (1963).

The word "perfected," although used by the draftsmen to describe the highest or optimum status for a secured party to enjoy, seems poorly chosen.[56] It was an attempt to correlate this phase of the state law on security in personal property with the Bankruptcy Act and its use of the word "perfected" in section 60. It is submitted that "perfected" as used throughout article 9 and "perfected" as used in the Bankruptcy Act are not coextensive in scope and tend to confuse and muddle an already complex conceptual area of the law.[57]

In determining the manner and means of "perfection," article 9 generally follows the theories of notice filing as required by the Uniform Trust Receipts Act and the accounts receivable validation statutes, rather than the limited individual instrument type of filing specified by the various chattel mortgage or conditional sales registration or recording acts.[58]

Scction 9-301 outlines the categories of persons who prevail over "unperfected" security interest as follows:

> (1) Except as otherwise provided in subsection (2), an unperfected security interest is subordinate to the rights of
> (a) persons entitled to priority under Section 9-312;
> (b) a person who becomes a lien creditor without knowledge of the security interest and before it is perfected;
> (c) in the case of goods, instruments, documents, and chattel paper, a person who is not a secured party and who is a transferee in bulk or other buyer not in ordinary course of business to the extent that he gives value and receives delivery of the collateral without knowledge of the security interest and before it is perfected;
> (d) in the case of accounts, contract rights, 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.

Section 9-301 does not attempt to assert that a secured party hold-

56. Coogan, *A Suggested Analytical Approach to Article 9 of the Uniform Commercial Code*, 63 COLUM. L. REV. 1, 25 (1963).

57. "Under the Code the word 'perfccted' has been given (probably unintentionally) a meaning differing from that of the Bankruptcy Act. The combined effect of Sections 9-204 and 9-303 is that a security interest is perfected upon the happening of whatever is the last of the three steps required under Section 9-204 to cause the security interest to attach and the one step required to provide (or in rare cases excuse) public notice under the appropriate section refcrred to in Section 9-303. Since the filed financing statement may be something far short of the security agreement, a Code interest could technically be 'perfected' at a time when it had not yet been made enforceable by compliance with the special statute of frauds provision of Section 9-203(1); thus, a security interest perfected in the Code sense would not necessarily be perfected in the bankruptcy sense. Obviously, if it is not enforceable against the debtor or 'third parties', the security interest would not be enforceable against the trustee or other lien creditors." *Id.* at 26.

58. UNIFORM COMMERCIAL CODE § 9-302, official comments 1, 5.

ing a "perfected" security interest surpasses the rights of all parties in the collateral. Indeed, it is doubtful that it could do so.[59]

Section 9-301 contains a definition of "lien creditor" which is in keeping with the concepts of the Uniform Trust Receipts Act, except that it is enlarged to include the secured party's most resourceful and dangerous potential enemy, the trustee in bankruptcy.

Mechanically, "perfection" under article 9 is relatively simple. It can be accomplished in two ways: "Perfection" by possession and "perfection" by filing.[60] To determine which of the two methods must be used, the secured party and his attorney must consider a number of factors:

(a) The nature and type of the collateral.
(b) The use to which the collateral will be put. (The same collateral can be consumer goods in the hands of one debtor and equipment if owned by another).
(c) The relationship between the debtor and the secured party.

A. *Perfection by Possession*

This is by far the simplest and most effective system of perfection of a security interest for the secured party, as he has in his hands at all times, with the minor exceptions noted, the collateral which insures or secures the repayment of his loan.[61] No other party can complain of "secret liens" or "unfettered dominion" by the debtor. Of course, this is in the realm of the pledge and the bailment where the bailee acknowledges that he holds the goods for the secured party and not for the debtor. Article 9 makes no basic change in the laws of Tennessee in regard to the perfection of a pledge; a written se-

59. This is of course obvious when consideration is given to the problem of perfecting a security interest against the trustee in bankruptcy whose status, powers, and duties are not limited by the classifications of the Uniform Commercial Code. See Moore v. Bay, 284 U.S. 4 (1931).

If a security interest is perfected within four months after bankruptcy and the security interest was given in order to secure an antecedent debt, the trustee in bankruptcy of the debtor may attack the transaction as a voidable preference under section 60 of the Bankruptcy Act, assuming that the trustee can establish the other elements of voidable preference. Further, if the security interest is vulnerable to a single creditor, regardless of the size of his claim, the secured party in a contest with the trustee in bankruptcy will probably lose his secured status and become an unsecured creditor of the bankrupt. Moore v. Bay, 284 U.S. 4 (1931). The result is the same if a hypothetical creditor could have attached the collateral in the hands of the debtor. Constance v. Harvey, 215 F.2d 571 (2d Cir. 1954).

60. TENN. CODE ANN. § 47-9-302 (repl. vol. 1964).

61. TENN. CODE ANN. § 47-9-304(4)(5) (repl. vol. 1964), permits a security interest to be perfected in instruments and documents for a short period of time even though the secured party may not have filed a financing statement and the collateral is in the debtor's possession. For a more complete discussion of this question, see generally SPIVACK, SECURED TRANSACTIONS 78 (1963); UNIFORM COMMERCIAL CODE § 9-304, official comment 4.

curity agreement is not even required to perfect a security interest by means of a pledge.[62] Naturally, the pledge is an ideal type of security transaction where John Doe seeks to pawn his watch for ten dollars, or where Richard Roe seeks to borrow ten-thousand dollars and gives two-hundred shares of General Motors common stock or a negotiable instrument as collateral security for the payment of the loan. On the other hand, it would be cumbersome as a security device in the purchase of an auxiliary diesel electric generator or a fleet of sixteen new diesel tractor-trailer trucks. In the modern world of commercial credit, it is normally unpracticable or impossible to use the possessory type of perfection; the debtors must have inventory, equipment, and accounts receivable if they are to remain in business and repay the loan which the security agreement and the security interest secure.

It is, however, sometimes necessary for the secured party, having a possessory "perfected" security interest in certain types of collateral, to surrender his collateral to the debtor for a limited purpose and time. Such is true where the collateral is a negotiable warehouse receipt or bill of lading. Section 9-304, subparagraphs (4) and (5), permits a secured party to deliver or redeliver to the debtor instruments or goods for the purpose of "ultimate sale or exchange or of presentation, collection, renewal, or registration of transfer" for a period of twenty-one days without loss of his perfected status. This is really not a significant change from the Uniform Trust Receipts Act[63] and conforms with section 60(a)(7) of the Bankruptcy Act.[64] This redelivery, of course, represents somewhat of a serious risk to a secured party in the event that the documents are negotiable.[65] However, if he has perfected his seeurity interest and the security agreement so provides, his security interest can attach to the proceeds derived from the exchange, sale, or transfer of the instruments or goods. Further, without a negotiable warehouse receipt, a merchant debtor cannot obtain his inventory without which he cannot sell finished goods, the profits from which are used to pay the secured party's loan.

Except as may otherwise be provided by section 9-304(4) and

62. *Compare* TENN. CODE ANN. § 47-9-302, -9-305 (repl. vol. 1964), *with* Barfield v. Cole, 36 Tenn. 465 (1857), holding that a pledge may be created without a written contract, and if there be a written pledge agreement no registration thereof is required.

63. TENN. CODE ANN. § 47-1001 (1956).

64. 64 Stat. 25 (1950), 11 U.S.C. § 96 (1958).

65. *Compare* UNIFORM COMMERCIAL CODE § 9-304, official comment 4, *with* In re Alday Motor Co., 50 F.2d 288 (6th Cir. 1930), which held that the pledgee lost his lien and became an unsecured creditor of the pledgor when the pledgee surrendered the property to the pledgor so that the pledgor could pass title to a third party who promised to discharge the obligation.

(5), a "security interest" perfected by possession is perfected the moment the secured party obtains delivery of the collateral.

B. *Perfection by Filing*

Since there are basically two types of security interests, possessory and nonpossessory, and since the Code provides that a possessory type of security interest may be perfected by possession, article 9 requires that in the majority of other types of secured transactions, with certain exceptions,[66] the perfection of the secured party's security interest be accomplished by filing.[67]

Historically, in Tennessee "filing," "recording," and "registering" have in general referred to the filing or recording of a chattel mortgage, chattel deed of trust, deed of trust, mechanic's liens, or other type of instrument which gives claim and notice to the world of a specific lien or a claim against a specific item of property, real or personal.

In 1937, with the enactment of the Uniform Trust Receipts Act,[68] the concept of "notice filing" was introduced into Tennessee and has subsequently been reaffirmed by the enactment of chapter 114 of the Public Acts of 1959, codified as sections 47-1801 to 47-1814 of the Tennessee Code Annotated, providing a system for the validation of assignments of accounts receivable in Tennessee. Thus, the notice filing provisions of article 9 are not entirely new and are in conformity with the two most recent statutory provisions in this area.

Section 9-302 states that filing of a financing statement is necessary to perfect the security interest in all cases except:

> (a) a security interest in collateral in possession of the secured party under Section 9-305;
> (b) a security interest temporarily perfected in instruments or documents without delivery under Section 9-304 or in proceeds for a 10 day period under Section 9-306;
> (c) a purchase money security interest in farm equipment having a purchase price not in excess of $2,500; but filing is required for a fixture under Section 9-313 or for a motor vehicle required to be licensed;
> (d) a purchase money security interest in consumer goods . . .
> (e) an assignment of accounts or contract rights which does not alone or in conjunction with other assignments to the same assignee transfer a significant part of the outstanding accounts or contract rights of the assignor;

66. TENN. CODE ANN. § 47-9-302(3) (repl. vol. 1964), exempts security interest property which is subject to a statute of the United States requiring national registration. The result was the same under prior Tennessee law by virtue of chapter 3 of title 59, entitled "Certificates of Title," codified as TENN. CODE ANN. § 59-301 to -330, on motor vehicles.

67. TENN. CODE ANN. § 47-9-302 (repl. vol. 1964).

68. TENN. CODE ANN. § 47-1001 (1956).

(f) a security interest of a collecting bank . . . or arising under the Article on Sales . . . or covered in subsection (3) of this section.

The document which must be filed in order to perfect the security interest is called the "financing statement" which section 9-402 requires to be signed by both the debtor and the secured party, giving the addresses of both and a statement indicating the types or describing the collateral. The other aspects of the financing statement will be covered in a subsequent section of this article.[69]

The financing statement simply gives notice to the world of the existence of or the intention to enter a financing arrangement between the debtor and the secured party, and contains little if any more information than do the present notices filed under the Uniform Trust Receipts Act or the accounts receivable validation statute. This type of filing has many advantages over the present system in use in Tennessee: it will last for five years;[70] it can be used to cover many different lending transactions;[71] it can cover both after-acquired and presently existing collateral;[72] it can cover proceeds; and it can cover constantly shifting collateral, such as inventory or accounts receivable. Thus the financing statement is really the document or instrument from which the whole concept of the "floating lien" is derived.

C. *Proceeds*

Where a secured party has obtained a security interest in collateral which is the subject of sale by the debtor to a buyer in the ordinary course of business, the secured party is naturally concerned with the continued existence of his security interest. Once the collateral is sold, the secured party has no security interest in the collateral as such;[73] however, section 9-306 provides that the security agreement and financing statement may state that a perfected security interest continues, following the transfer of collateral, into the proceeds derived from the sale of the collateral. However, where a debtor wrongfully or dishonestly transfers the collateral, the secured party might prefer to file the proceeds rather than attempt to recover the collateral. Section 9-306 permits the secured party to do this provided the proceeds have not been so commingled by the debtor as to be unidentifiable.

69. See Section VI, *infra.*

70. TENN. CODE ANN. § 47-9-403(2) (repl. vol. 1964).

71. Coogan, *Article 9 of the Uniform Commercial Code: Priorities Among Secured Creditors and the "Floating Lien,"* 72 HARV. L. REV. 838, 855 (1959).

72. TENN. CODE ANN. §§ 47-9-108, -9-203, -9-204 (repl. vol. 1964); UNIFORM COMMERCIAL CODE § 9-402, official comment.

73. TENN. CODE ANN. § 47-9-307 (repl. vol. 1964).

Section 9-306(1) defines "proceeds" as

> (1) "Proceeds" includes whatever is received when collateral or proceeds is sold, exchanged, collected or otherwise disposed of. The term also includes the account arising when the right to payment is earned under a contract right. Money, checks and the like are "cash proceeds." All other proceeds are "non-cash proceeds."

If the security agreement and the financing statement did not specify a security interest in "proceeds," the secured party is not left without a remedy or in an unsecured status by the unauthorized transfer of the collateral by the debtor to a buyer in the ordinary course of business. Section 9-306(3) permits the secured party to file a financing statement claiming a security interest in the proceeds within a period of ten days after the receipt by the debtor of the proceeds. Also, section 9-306(3) provides that the security interest in the proceeds is continuously perfected without any further action on the part of the secured party, provided that the original financing statement covering the original collateral also covered proceeds of the sale or disposition of the collateral.

Section 9-306(4)'s treatment of "proceeds" presents some interesting questions in the field of bankruptcy. This provision grants to a secured party with a perfected security interest in proceeds a security interest in identifiable non-cash proceeds; in identifiable cash proceeds in the form of money which is not commingled with other money or deposited in a bank account prior to the insolvency proceedings; in identifiable cash proceeds in the form of undeposited checks; and in all cash and bank accounts of the debtor, if other cash proceeds have been commingled or deposited in the bank account, provided that the secured party's interest is limited to the amount of cash proceeds received by the debtor within ten days preceding the filing of insolvency proceedings, diminished by any right of setoff of the debtor.[74] Section 9-205 which purports to overrule the doctrine of *Benedict v. Ratner*[75] is of some assistance in removing some of the bankruptcy obstacles here. However, the problem of identification remains and may prove to be an insurmountable obstacle to the secured party seeking to assert his security interest against the debtor's trustee in bankruptcy seeking to exercise his rights under section 70 of the Bankruptcy Act. In addition, it is questionable if proceeds are so commingled as to become unidentifiable whether the secured party

74. Tenn. Code Ann. § 47-9-306(4) (repl. vol. 1964). This is in accord with § 10 of the Uniform Trust Receipts Act. Prior Tennessee decisions are basically in accord with § 47-9-306(4). See generally, In re Harpeth Motors, Inc., 135 F. Supp. 863 (M.D. Tenn. 1955); Commerce Union Bank v. Alexander, 44 Tenn. App. 104, 312 S.W.2d 611 (M.S. 1957).

75. See Gordon, *supra* note 45.

would have any claim which he could establish to them in preference to or senior to another secured party claiming a similar security interest in the same proceeds.[76]

Section 9-306 in its treatment of returned goods as "proceeds" presents additional bankruptcy problems. This is especially true in view of the abolition of the concept of title by section 2-401 of the Sales Article and section 9-202 of article 9. Although sections 9-202 and 9-306, when read together, may not present such a basic change in the law of states having factor's lien statutes which have adjusted their commercial financial practices to the continuing general lien theory, the inclusion of this provision in the law of Tennessee may create several new problems in addition to the already apparent conflicts with the several bankruptcy cases on the rights of secured parties in returned goods as proceeds.[77]

D. *Buyers in the Ordinary Course of Business*

A merchant debtor who sells at wholesale or retail from an inventory or stock of goods in trade, depends upon his sales to his customers to produce income from which he is to repay his loan to the secured party. Unless buyers in the ordinary course of business from such merchant debtors can be assured of receiving clear titles to the chattels so purchased, the likelihood of merchant debtors' being able to operate profitably and thus repay their loans is jeopardized. Section 9-307, reflecting the draftsmen's recognition of the many problems which have developed in the past in connection with transfers by purchase or otherwise of collateral by a merchant debtor, accords the buyer in the ordinary course of business, other than a person buying farm products from a person engaged in farming operations, a free and clear title to the chattel and cuts off any claim which the secured party might otherwise have in the collateral. In addition, a buyer of consumer goods for his own use as a consumer, or a buyer of farm equipment having an original purchase price of less than five-hundred dollars takes his purchase free of the security interest of a secured party, even though this interest is perfected, unless prior to the purchase, the secured party has filed a financing statement covering such goods. Essentially, this is not a significant change from the present law in Tennessee under the provisions of the Uniform Trust

76. For a thorough analysis of the bankruptcy problems presented by § 9-306(4) of the Uniform Commercial Code, see Kennedy, *The Trustee in Bankruptcy Under the Uniform Commercial Code: Some Problems Suggested By Articles 2 and 9*, 14 RUTGERS L. REV. 518, 531 (1960).

77. *E.g.*, Lee v. State Bank & Trust Co., 38 F.2d 45 (2d Cir. 1930), *cert. denied*, 285 U.S. 547 (1932). See, Kennedy, *supra note* 76, at 534.

Receipts Act.[78] An automobile dealer since 1937 has certainly been able to pass clear title to the buyer in the ordinary course of business, free from any interest of the "entruster" or the financing agency which held the technical title to the collateral.[79] Thus, section 9-307 is not a significant change in this respect in the area of the law of personal property security.

E. *Purchasers of Instruments and Documents*

Negotiable instruments, by their very nature and definition, stand on a different footing and enjoy a different status from inventory, equipment, consumer goods, or other commonly used items of collateral. They are negotiable; they often pass and are used in lieu of money. Section 9-309, therefore, provides that a holder in due course of a negotiable instrument or a holder to whom a negotiable instrument has been duly negotiated, or a bona fide purchaser of such instrument, takes priority over an earlier security interest of any secured party, even though perfected. Again, this is in keeping with the general concept of the law of negotiable instruments and the provisions of article 3 (commercial paper) of the Uniform Commercial Code which favor the free negotiability of such instruments and documents.[80]

F. *The Secured Party Versus the Artisan*

Many troublesome questions have been presented to Tennessee courts involving competing claims between holders of security interests in automobiles or other similar items of personal property and artisans who from time to time have repaired or serviced the vehicles, the effect of which placed the collateral in an operating or serviccable condition, or, as in some cases, actually improved its value as security. Notice was the determining factor in some decisions;[81] others seemed to have been determined strictly on the basis of the concept of title to the collateral.[82]

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78. *In re* Harpeth Motors, Inc., 135 F. Supp. 863 (M.D. Tenn. 1955); J. B. Wilder & Co. v. Wilson, 84 Tenn. 548 (1886); Hoskins & Co. v. Carroll, 15 Tenn. 505 (1835); Hurt v. Reeves, 6 Tenn. 49 (1818).

79. TENN. CODE ANN. § 47-1010 (1956).

80. See generally, Coogan, *supra* note 71, at 870.

81. Diamond Service Station v. Broadway Motor Co., 158 Tenn. 258, 12 S.W.2d 705 (1929), held that the lien given to the artisan by the former §§ 64-1901 to -1914 of the Tennessee Code Annotated did not have priority over the lien of the conditional seller nnder a conditional sales contract where the seller had no knowledge of the transaction between the conditional vendee and the artisan and the collateral was not enhanced in value. *But cf.* Gem Motor Co. v. Securities Inv. Co., 16 Tenn. App. 608, 65 S.W.2d 590 (M.S. 1933).

82. *E.g.*, Nelson-Collins-Nash, Inc. v. Associates Discount Corp., 193 Tenn. 696, 249 S.W.2d 902 (1951).

Section 9-310 of the Uniform Commercial Code seeks to resolve these questions, and will undoubtedly change or overrule some of the existing decisions in Tennessee in this area. This section provides that when a person, such as an automobile mechanic, in the ordinary course of his business, furnishes services or material with respect to goods subject to a security interest, a lien upon the goods in the possession of such artisan or repairman, given by statute such as provided in section 64-1901 of the Tennessee Code Annotated, prevails over a perfected security interest of a secured party, unless the lien is statutory and the statute expressly provides otherwise.[83]

V. Secured Party Versus Secured Party Versus Trustee in Bankruptcy: The Priority Problem

Perhaps no other section of the Uniform Commercial Code has evoked such an outburst of legal journalism as the priority rules of article 9. This is primarily due to the novelty of the approach: A statute seeks to set forth, within the finite limits of human reason and experience, a complete set of rules to determine which secured party wins and which loses in the event of a clash between them in the same collateral. Nothing of this nature has existed before in Tennessee, although rules similar in content and almost as broad in scope have existed in other states prior to the adoption of the Uniform Commercial Code.[84] In the absence of a uniform and integrated law on security in personal property, such a system of priority rules would hardly have been possible in Tennessee.

Section 9-312 contains the basic priority rules, either in index or definition form. Since treatment of all of the situations covered by article 9 is beyond the scope of this article, only those major rules or more important priority rules will be treated here. The unique priority rules involving accounts receivable, chattel paper, and general intangibles have been elaborately treated elsewhere.[85] Since "goods" are the type of collateral which the Tennessee secured party and his attorney will most likely enconnter in priority situations, the discussion of the priority rules herein will be primarily directed to-

83. Such will resolve the inconsistencies in this area as represented by McGhee v. Edwards, 87 Tenn. 506, 11 S.W. 316 (1889), and Adams v. Stone Bros., 6 Tenn. Civ. App. (6 Higgins) 224 (M.S. 1915).

84. "This section [9-312] is mostly in accord with New York law, although it would effect some changes as to certain present security devices." 3 N.Y. Law Rev. Report 2061 (1955).

85. See, *e.g.*, Coogan and Gordon, *The Effect of the Uniform Commercial Code Upon Receivables Financing—Some Answers and Some Unresolved Problems*, 76 Harv. L. Rev. 1529 (1963); Coogan, *Intangibles as Collateral Under the Uniform Commercial Code*, 77 Harv. L. Rev. 997 (1964); Kupfer, *Accounts Receivable, Trust Receipt and Related Types of Financing Under Article 9 of the Uniform Commercial Code*, 27 Temp. L.Q. 278 (1953); and Note, 27 Temp. L.Q. 91 (1953).

ward competing security interests in "goods" as defined by article 9.

Basically, Section 9-312(2),(3),(4), and (5), establishes four rules of priority:

(a) Certain perfeeted security interests in crops take priority over other perfected security interests in crops;
(b) Purchase money security interests in inventory collateral prevail over other perfected security interest in such collateral under certain circumstances;
(c) Purchase money security interests in non-inventory collateral prevail over certain other perfected security interests in non-inventory collateral under certain circumstances;
(d) Where non-purchase money, non-possessory perfected security interests clash,
    (1) the first security interest filed prevails; or,
    (2) the first security interest perfected prevails, unless both are perfected by filing; or,
    (3) priority is determined in the order the security interests attach so long as neither is perfected.

Article 9 uses the words "perfect," "perfected," and "perfection," on the one hand, and the words "priority" and "priorities" on the other, thus creating some confusion. It has been suggested that article 9 should be interpreted so that the words "perfect," "perfected," and "perfection" relate to steps generally to protect a security interest against attack by a trustee in bankruptcy of the debtor. All other questions regarding rights of various competing secured parties, including questions as to who is prior in time or in right, subordination, etc., should be considered under the general heading of "priority" or "priorities."[86]

Section 9-301(1)(b), suggests that the only instance in which an unperfected security interest should prevail would be in a contest against a lien creditor as therein defined, with knowledge of the unperfected security interest, while a perfected security interest would be valid whether or not such subsequent lien creditor had knowledge of its existence. This presentation and definition may cause some difficulties in interpreting and construing these portions of the Uniform Commercial Code alongside the pertinent provisions of the Bankruptcy Act.

A. *Priorities Between Perfected Security Interests in Crops*

Section 9-312(2) gives priority to a new value security interest in crops based on a current crop production loan as opposed to an earlier perfected security interest in the crop which secured an obligation due more than six months before the crop became a growing

86. Coogan, *A Suggested Analytical Approach to Article 9 of the Uniform Commercial Code*, 63 COLUM. L. REV. 1, 25 (1963).

crop. Priority of the subsequent perfected security interest is not dependent upon knowledge of the subsequent lender. This is somewhat of a change from existing law in this state.[87]

B. *The Purchase-Money Priority*

Section 9-312(3) and (4) creates a purchase-money priority in the event of conflicting claims between secured parties, primarily in inventory and equipment type financing situations. These rules provide a superior status for the secured party who has sold to the debtor inventory or equipment or has loaned to him funds with which to acquire the inventory or equipment as against the competing claims of a prior secured party claiming an interest under an after-acquired property clause of a prior perfected security interest. Section 9-312(3) confers the purchase-money priority on the inventory financier, provided certain conditions are met, and section 9-312(4) does likewise for the equipment seller or financier.

In order to gain the coveted priority status afforded by section 9-312(3), an inventory financier must satisfy the following requirements:

> (a) He must perfect his security interest before the debtor obtains possession of the collateral; and,
> (b) He must notify a secured party whose security interest is known to him, as well as any person who, prior to the date of the purchase money secured party's filing of his financing statement, has filed a financing statement claiming the same inventory of his intention to acquire purchase-money security interest in the inventory, describing the inventory by item or type.

On the other hand, the equipment-type purchase-money secured party has only to perfect his security interest within ten days following delivery to or acquisition by the debtor of the collateral. No requirement is placed upon the equipment-type purchase-money secured party to notify any one; there is no secured party whose interest could have priority to that of the purchase-money secured party in the equipment-type financing situation. Various commentators have sought to explain the difference in treatment, particularly regarding the notice required and the period of grace for filing, between the equipment-type purchase-money secured party and the inventory-type purchase-money secured party, along the following lines:

> Inventory financing is likely to consist of repeat transactions involving a substantial amount of money, and the financier, whether operating on a general lien or purchase-money basis, is not likely to be an amateur. Thus, it is not unreasonable to require that he comply with a certain number of

87. See Polk v. Foster, 66 Tenn. 98 (1874).

formalities. The requirement that filing be done before the debtor receives possession of the collateral, without a provision for a grace period, will protect any other financier who cheeks the records from making an advance against goods already subject to a purchase-money security interest.[88]

On the other hand, in the equipment-type purchase-money transaction, non-professionals normally conduct the sale of this type of collateral. It is often necessary that the debtor obtain immediate possession of the collateral in order to meet the pressing needs of his business. Thus, the ten day grace period and elimination of any notification to any prior secured party seems not to be unreasonable. Further, equipment purchases are not likely to be so numerous as the inventory-type financing arrangements.

C. *Purchase-Money Security Interests in Consumer Goods*

Due to the relaxation of filing requirements for financing statements on consumer goods set forth in section 9-302 and the limitations placed upon after-acquired property clauses pertaining to consumer goods in section 9-204(4)(b), the problems of priority in consumer goods are considerably lessened. However, priority problems can exist in the field of consumer goods and are essentially of the same type as those which will exist in the field of inventory and equipment-type financing, and the purchase-money financier of consumer goods must bear the risk of the first-to-file rule or obtain a special priority under section 9-312(4).[89]

The purchase-money priority contained in section 9-312(3) and (4) stems from the traditional preferred position accorded by the law to the lender supplying either the capital with which to acquire new goods or equipment or to the seller of such goods on a deferred payment basis. This preferred status was partially incorporated into the Uniform Trust Receipts Act by giving the entruster priority status over other claimants of the debtor. Thus, the inclusion of the purchase-money priority concept into article 9 of the Uniform Commercial Code seems appropriate and in accordance with the historical precedents which the law has established in this area of finance.[90]

D. *Priorities Among Non-Purchase Money, Non-Possessory Perfected Security Interests*

Herein lies the great difficulty with the priority rules as set forth in article 9. The "first-to-file rule," the "first-to-perfect rule," and the

88. Coogan, *supra* note 71, at 863.
89. *Id.* at 864.
90. In Tennessee the title of a vendor retained by a written contract, althought unregistered, is superior to any right acquired by a purchaser for value and without notice. Knoxville Outfitting Co. v. Knoxville Fireproof Storage Co., 160 Tenn. 203, 22 S.W.2d 354 (1929); Shaw v. Webb, 131 Tenn. 173, 174 S.W. 273 (1914).

"first-to-attach rule" all arise from the basic recognition of the existence of fraudulent, stupid, or dishonest debtors or secured parties whose diligence leaves much to be desired. These rules also stem, in part, from the Code's concept of notice filing of very broad financing statements. The "first-to-file rule," as set forth in section 9-312(5)(a), is the personal property equivalent of the "race" type recording statute on which first year law students had teething troubles as they endeavored to distinguish this type from the other three types of recording acts in use in the United States. In order to obtain priority, a secured party, who has otherwise perfected his security interest, must be the first to file his financing statement if he is to gain priority over other secured parties, even though their security interests may have attached prior in time to his. For example, if *A* files a financing statement on March 1, 1964, pursuant to an agreement with the debtor to make an advance on June 1, and *B*, another lender, loans ten-thousand dollars to the debtor on April 1, 1964, and immediately thereafter files his financing statement fearing a possible conflict as to his interest in the collateral, *A* clearly prevails over *B* by virtue of his prior filing. The priority accorded to the first secured party to file seems not to depend upon the time of making of the advance, the date of the execution of the security agreement, the knowledge of the existence of a competing security interest, or the identity of another secured party. Of course, the "first-to-file rule" poses many potential problems, especially when considered with the period of validation and effectiveness of a financing statement.[91]

Also, due to the purchase-money priority rule also contained in section 9-312, the secured party who was first to file cannot always be certain that his filing will afford him priority in the event of a conflict with a subsequent purchase-money secured party.

E. *The "First-to-Perfect Rule"*

Section 9-312(5)(b) provides that if one or more of the competing security interests has been perfected by a method other than filing, priority is accorded to the first secured party to perfect his security interest, regardless of the date of the security interest or the date of filing. This is due to the definition and concept of "perfection" as used by article 9.[92] If the parties have reached an agreement; if the debtor has acquired rights in collateral; if value has been given, either in the form of a loan or an installment sale of goods or a commitment for either; and public notice has been given or is excused,

91. For examples of other problems which can easily arise under Uniform Commercial Code § 9-312(5), see official comment 4 to that section and Coogan, *supra* note 71, at 857.

92. See note 55 *supra*.

the security interest has then been perfected. Whichever competing secured party has perfected his security interest first is the winner in this situation. The "first-to-perfect rule" is most likely to occur in the event of a conflict between the holder of a possessory security interest who is excused from obtaining a written security agreement or the requirements of notice filing and a non-possessory type security interest whose perfection depends upon filing to acquire the necessary public notice; the pledge versus the chattel mortgage type of transaction. In such a case, if the pledge were perfected in advance of the execution of the chattel mortgage type security interest, even though both comply in all respects with the requirements of article 9 as regards perfection, the pledgee will clearly prevail over the chattel mortgage type secured party.[93]

There are many other priority rules set forth in article 9 dealing with temporary perfection of security interests in instruments and documents;[94] rules regarding priority in accounts and chattel paper;[95] and special rules concerning priorities among conflicting interests in commingled or processed goods,[96] in accessions,[97] and in fixtures.[98] There have been many exhaustive studies made of the minute aspects of the application of the priority rules as regards certain specific types of such collateral, and further reference to them will not be made herein.[99]

F. *The "Floating Lien"*

Nowhere in the Code are the words "floating lien" used in the official text; it is alluded to from time to time in the official comments.[100] The use of this term was aparently first made in connection with the study conducted by the New York Law Revision Commission on the Uniform Commercial Code.[101] The concept of the "floating lien" has

93. For examples of other problems which might arise under Uniform Commercial Code § 9-312(5)(b), see official comment 4 to the section.
94. Tenn. Code Ann. §§ 47-9-304, -9-309 (repl. vol. 1964).
95. Tenn. Code Ann. § 47-9-308 (repl. vol. 1964).
96. Tenn. Code Ann. § 47-9-315 (repl. vol. 1964).
97. Tenn. Code Ann. § 47-9-314 (repl. vol. 1964).
98. Tenn. Code Ann. § 47-9-313 (repl. vol. 1964).
99. *E.g.*, Coogan, *Security Interests in Fixtures Under the Uniform Commercial Code*, 75 Harv. L. Rev. 1319 (1962); Coogan and Clovis, *Uniform Commercial Code and Real Estate Law: Problems for Both the Real Estate Lawyer and the Chattel Security Lawyer*, 38 Ind. L.J. 535 (1963); Googan and Gordon, *The Effect of the Uniform Commercial Code Upon Receivables Financing–Some Answers and Some Unresolved Problems*, 76 Harv. L. Rev. 1529, 1551 (1963); Gordon, *The Security Interest in Inventory Under Article 9 of the Uniform Commercial Code and the Preference Problem*, 62 Colum. L. Rev. 49 (1962); Kripke, *Fixtures Under the Uniform Commercial Code*, 64 Colum. L. Rev. 44 (1964).
100. *E.g.*, Uniform Commercial Code § 9-204, official comment 3; Uniform Commercial Code § 9-205, official comment 1.
101. 2 N.Y. Law Rev. Comm'n Report 1079 (1954).

been one of the major reasons for criticism of article 9 and, in turn, of the entire Uniform Commercial Code.

The "floating lien" is thought to be made possible by the aggregation and interrelationship of the following sections of article 9:

> Section 9-108 permitting a secured party to obtain a security interest in after-acquired collateral which is not considered as being given, transferred or surrendered for an antecedent debt;
> section 9-204(3) permitting a security agreement to contain an after-acquired property clause;
> section 9-204(5) permitting a security agreement to contain obligations regarding future advances or commitments to make future advances or to give other value;
> section 9-306 creating a security interest in proceeds;
> section 9-205 permitting the debtor to use or dispose of collateral without accounting to the secured party or to freely commingle the collateral with other collateral without destroying the validity of the security agreement, thereby overruling the doctrine of *Benedict v. Ratner* and the applicable decisions of this state.

The merits and demerits of the "floating lien" have been elsewhere discussed at length.[102] Until the validity and meaning of section 9-108 is interpreted by a bankruptcy court, until a diligent trustee in bankruptcy, exercising the "strong arm" provisions under section 70 of the Bankruptcy Act, challenges the debtor's right to commingle proceeds as permitted by sections 9-305 and 9-306, until a bankruptcy court reconciles or interprets the concepts of "perfection" as used in article 9, and in section 60 of the Bankruptcy Act it will not be possible, in the writer's opinion, to determine with accuracy whether the "floating lien" is a valid, legal security device, or is a concept which has existed primarily in the minds of legal scholars.

VI. FILING

Part 4 of article 9, commencing with section 9-401, sets forth the necessary procedures for filing security agreements or financing statements in order to perfect those security interests which article 9 determines must be perfected by filing. Section 9-401 gives the place or locality in which certain types of financing statements covering particular types of collateral must be filed; section 9-402 sets forth

102. "Opponents of the floating lien have argued that it allows the financier who first contacts the borrower to monopolize that borrower's business and makes relatively improbable the situation where numerous financiers are simultaneously extending the same kind of inventory credit to the same merchant. A related point is also made that the floating lien makes broad security interests so easy to get that greedy financiers will take more security than they really need, thus tying too many of the merchant's assets and handicapping him in his future operations." 2 N.Y. LAW REV. COMM'N REPORT 1079 (1954); see also Coogan, *supra* note 71.

the formal requisites of the financing statement. These two sections represent significant departures from existing law in Tennessee.

The legal niceties of affidavits, acknowledgements, seals, and various other archaic formalities are dispensed with and

> (1) A financing statement is sufficient if it is signed by the debtor and the secured party, gives an address of the secured party from which information concerning the security interest may be obtained, gives a mailing address of the debtor and contains a statement indicating the types, or describing the items, of collateral. A financing statement may be filed before a security agreement is made or a security interest otherwise attaches.

If they choose, the parties may file the actual security agreement, rather than a financing statement, in the chattel mortgage or conditional sale type of situation. Yet, article 9 in its adoption of the notice filing theory has greatly simplified the perfection security of interests by filing, using a method heretofore reserved to inventory and accounts-receivable financing systems.[103]

At present in Tennessee there is no limitation on the period of effectiveness of a recorded chattel mortgage.[104] Prior to June 30, 1964, conditional sales contracts were not required to be recorded to retain their perfected status.[105] Under the Uniform Commercial Code a financing statement is effective for a period of five years and thereafter for a period of sixty days, during which a continuation statement may be filed.[106]

No provision of the present uncoordinated personal property security laws of Tennessee affords to a debtor the right to obtain from a lender or secured party a statement of the charges due or the amount paid on the indebtedness which a security interest secures. This is often the source of much debate and litigation in the courts of general sessions in particular. This will no longer be necessary. Section 9-404 affords to the debtor the right to demand and compel a secured party to furnish a termination statement on demand. Such a termination statement may be used by a debtor and a preferred secured lender to avoid priority problems under the "first-to-file

103. Until the enactment of the Uniform Commercial Code the "notice filing" concept existed only in Tennessee in the trust receipt (inventory type financing situation), TENN. CODE ANN. § 47-1001 (1956), and the area of validation of assignments of accounts receivable, TENN. CODE ANN. § 47-1801 (1956).

104. Note, *The Uniform Commercial Code—The Effect of Its Adoption in Tennessee, Article Nine—Secured Transactions,* 22 TENN. L. REV. 776, 848 (1953).

105. Tatum v. Jameson, 21 Tenn. 298 (1841); Bradshaw v. Thomas, 15 Tenn. 497 (1835); *but see* Byrd v. Wilcox, 67 Tenn. 65 (1874) (holding registration necessary where a lien is retained as security for payment of the purchase price). *Cf.* Free Service Tire Co. v. Manufacturer's Acceptance Corp., 38 Tenn. App. 647, 277 S.W.2d 897 (E.S. 1955).

106. TENN. CODE ANN. § 47-9-403(2) (repl. vol. 1964).

rule."[107] In this context, it should be pointed out that section 9-208 allows the debtor the right to obtain at least once in every six months a statement of his account or a list from the secured party of the collateral which the secured party holds to insure payment of the indebtedness. A termination statement secured pursuant to section 9-404, together with a statement of account as provided under section 9-208, if coupled with a subordination agreement permitted by section 9-316, could combine to resolve many of the priority problems which competing secured parties might encounter as described in the previous section.[108] Neither the right to obtain a termination statement nor the right to obtain a statement of account existed at common law or by statute in Tennessee prior to the enactment of article 9; it is submitted that both are desirable and should prove beneficial to society in general.

VII. Remedies on Default

All of the intricate and theoretical niceties of article 9 depend upon and are, in fact, designed to deal with one catastrophe: the default of the debtor in payment of the indebtedness or performance of the obligation which the security agreement is intended to secure. In fact, the remedies available on default are the only distinctions which set apart a secured and an unsecured creditor. Were it not that the secured party with a perfected security interest in four-hundred shares of DuPont stock could confidently expect to realize at least a portion of his advance from the liquidation of the collateral, his position is no better than that of the Aid Finance Company holding an unsecured promissory note upon the voluntary bankruptcy of the debtor.

In this area, as in the many other arenas of commercial jousting, the Uniform Commercial Code takes as its standards or ground rules "commercial reasonableness."[109] Actually, these ideas are probably what both parties to the transaction visualize from its inception. The normal business debtor is not seeking a court ordered foreclosure with its attendant costs if a smaller deficiency upon resale will be realized by a private sale or eliminated entirely by an acceptance of the collateral as satisfaction for the indebtedness or obligation.

The remedies on default are set forth in part 5 of article 9 and collect in one area the various alternative courses of action available to a secured party faced with default and prescribe the steps which he must take. In keeping with its policy of "commercial reasonable-

107. Coogan, *supra* note 71, at 860.
108. *Ibid.*
109. Tenn. Code Ann. §§ 47-9-501(3), -9-504, -9-507(2) (repl. vol. 1964); Spivack, Secured Transactions 133 (1963); Dennon, *Liquidation of Collateral for Defaulted Loans in General and Under the Uniform Commercial Code,* 18 Bus. Law. 1087 (1963).

ness," the secured party is given cumulative remedies by which to seek to realize on his security and minimize any loss. This appears to be a change in Tennessee chattel security law.[110]

A. *Right to Possession*

This is certainly the most important remedy available to a secured party holding a non-possessory security interest in tangible collateral. Once it is exercised, the secured party is placed in the same relative status, in general, as the pledgee upon default.[111]

Section 9-503 permits the secured party to take possession of the collateral;[112] direct the debtor to assemble the collateral at a reasonably convenient place; or to render the collateral useless or unusable if removal from the debtor's premises be impractical.[113]

These provisions are actually not as new as they might appear on first examination. It is not unusual in some types of financing to require the debtor to collect or assemble the collateral, and certainly, the parties can so provide in their security agreement.[114]

The provisions of section 9-503 permitting a secured party to render collateral on the debtor's property useless or inoperative raises a host of problems and are new to Tennessee law.

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110. Prior to the Uniform Commercial Code, a chattel mortgagee, upon default, had three remedies in Tennessee:

(a) An action for foreclosure;

(b) an action on the note or for the debt; and

(c) replevin.

If he chose replevin he waived his other remedies. Lawrence v. Bridleman, 11 Tenn. 496 (1832).

The conditional seller, upon default, was afforded two remedies under the provisions of TENN. CODE ANN. § 47-1301 (1956):

(a) He could retake possession, or

(b) He could have judgment for the remaining unpaid balance; he could not pursue both remedies.

Friedman v. Georgia Showcase Co., 27 Tenn. App. 754, 183 S.W.2d 9 (E.S. 1944).

The pledgee could sell the collateral upon reasonable notice or he could file a bill in equity for sale and to foreclose the equity of redemption. Arrendale v. Samuel D. Morgan & Co., 37 Tenn. App. 703 (1857).

111. SPIVACK, SECURED TRANSACTIONS 134 (1963); UNIFORM COMMERCIAL CODE § 9-501, official comments 2, 3. Upon taking possession, however, a secured party incurs some additional duties to the debtor in so far as regards the protection and care of the collateral. TENN. CODE ANN. § 47-9-207 (repl. vol. 1964).

112. This appears to be in accordance with present Tennessee law. Third Nat'l Bank v. Olive, 198 Tenn. 687, 281 S.W.2d 675 (1954) (chattel mortgage); Murray v. Federal Motor Truck Sales Corp., 160 Tenn. 140, 22 S.W.2d 227 (1929) (conditional sales); Saxon v. Champion Shoe Mach. Co., 7 Tenn. App. 603 (W.S. 1928).

Although the concept of title has been for all practical purposes abolished by Uniform Commercial Code sections 2-401, 9-202, repossession by replevin will not be a problem nnder the Uniform Commercial Code, since replevin tests only right to possession in Tennessee and proof of title is not necessary. Young v. Harris-Cortner, 152 Tenn. 34, 268 S.W. 1120 (1924).

113. TENN. CODE ANN. § 47-9-503 (repl. vol. 1964).

114. Comment, 39 MARQ. L. REV. 246, 255 (1956).

On this question official comment to section 9-503 provides, in part:

> The authorization to render equipment unusable or to dispose of collateral without removal would not justify unreasonable action by the secured party, since under Section 9-504(3), all his actions in connection with disposition must be taken in a "commercially reasonable manner."[115]

It is submitted that such a policy declaration falls far short of solving many problems, among which are the following:

(1) What action may the debtor take after default if he does not desire to have the property remain on his premises?

(2) May the secured party be forced by the debtor to remove the property after it has been unusable for a reasonable time and no sale consummated?[116]

B. *The Secured Party's Collection Rights*

Section 9-502 recognizes the increasing importance of assignment of accounts receivable and chattel paper as financing devices, as it permits the secured party to collect accounts following default. Prior to section 9-502 there were no uniform statutory provisions in Tennessee or elsewhere on this subject.[117]

However, section 9-502 attempts to place the secured party holding a non-possessory security interest in accounts, chattel paper, or general intangibles in the same relative position as the holder of a non-possessory security interest in tangible collateral; it allows the secured party to notify the account debtor to make payment directly to and to take control of any proceeds of such collateral to which the secured party is entitled under section 9-306.[118]

Section 9-502 thus permits a secured party to notify, following default, an account debtor of the assignment when the security agreement as originally executed contemplated a "non-notification" type of agreement.

Where the secured party has a security interest in accounts, contract rights, or chattel paper, which he acquired by purchase, section 9-502 permits him to retain any surplus realized on the collection of the accounts unless the security agreement provides to the contrary. This contemplates a financing arrangement between businessmen and they are thus left free to contract as they may wish, subject to the

115. UNIFORM COMMERCIAL CODE § 9-503, official comment.

116. For a further discussion of these and other related questions, see, Comment, *supra* note 114.

117. UNIFORM COMMERCIAL CODE § 9-502, official comment.

118. SPIVACK, SECURED TRANSACTIONS 135 (1963). This is in keeping with the theory of equality of remedies given to the buyer and seller under the sales article. *Compare* TENN. CODE ANN. § 47-2-702 (repl. vol. 1964) (seller's remedies), *with* TENN. CODE ANN. § 47-2-711 (repl. vol. 1964) (buyer's remedies).

provisions of the other articles of the Uniform Commercial Code.[119] Neither section 9-201(37) nor section 9-502 give any standards to determine when the underlying transaction between the secured party and the debtor is a sale within the language of these two sections.[120]

C. *Notice and Disposition of Collateral*

The provisions of section 9-504 on notice after repossession and disposition of the collateral, in general, are in accordance with present Tennessee law, except that until now, no Tennessee court has been required to consciously apply the doctrine of "commercial reasonableness" to the problem of notice or disposition of collateral.[121]

The flexibility created by section 9-504 will perhaps avoid such harsh results which are possible at present by technical variances or irregularities on resale in Tennessee.[122]

The notice provisions of section 9-504(3) provide that the secured party, following repossession, must give the debtor reasonable notice of either a private or public sale unless the collateral is perishable or threatens to speedily decline in value.[123]

The most significant change, aside from the injection of the concept of "commercial reasonableness" made by section 9-504 in present Tennessee law, concerns the timing and type of resale following repossession. The Uniform Trust Receipts Act required the secured party following repossession to give the debtor at least five days notice prior to a public or private sale, either of which it approved;[124] Tennessee Code Annotated, section 47-1302 governing sales after repossession of conditionally sold goods, required a public sale at least ten days following the repossession. Section 9-504, in general, thus adopts the theory of the Uniform Trust Receipts Act and permits great latitude on resale. Furthermore, section 9-504 also protects the purchaser at resale after repossession in keeping with the other

119. UNIFORM COMMERCIAL CODE § 9-502, official comment 4.

120. *Ibid.*

121. UNIFORM COMMERCIAL CODE § 9-504, official comment 1.

122. The conditional seller, upon regaining possession, cannot hold the property as his own, but must expose it for sale as required by TENN. CODE ANN. § 47-1302 (1956). Cowan v. Singer Mfg. Co., 92 Tenn. 376, 21 S.W. 663 (1893). The conditional seller's or chattel mortgagee's action will be closely scrutinized in sale after repossession and he will not be permitted to obtain a profit from his position. Bill Jones Auto Co. v. H. E. Carr & Co., 4 Tenn. App. 443 (M.S. 1926). *But see,* Sweeney v. Mergenthaler Linotype Co., 8 Tenn. Civ. App. (8 Higgins) 244 (W.D. 1918), where a mortgagee after repossession was excused from resale where it was shown that a sale would be futile.

123. This is in accord with present Tennessee law. Ham Const. Co. v. Dempster Bros., Inc., 36 Tenn. App. 356, 255 S.W.2d 712 (E.S. 1952); *but see* Quick v. Woodard Motor Co., 23 Tenn. App. 254, 130 S.W.2d 147 (M.S. 1938).

124. TENN. CODE ANN. § 47-1007 (1956).

ideas and concepts of the draftsmen of the Code to sweep away the formal niceties of the preexisting law.[125]

D. *Disposition of Consumer Goods*

The theory of compulsory disposition at public sale of conditionally sold articles in Tennessee, upon repossession, required by Tennessee Code Annotated, section 47-1302 is carried forward into the Uniform Commercial Code by section 9-505 which requires, in the case of consumer goods, a sale, either public or private, in accordance with section 9-504, with certain reservations,[126] if the consumer has paid sixty per cent of the price or sixty per cent of the loan. Experience, however, has also shown that sometime parties are better off if the secured party retains the collateral, following repossession, in full satisfaction of the underlying obligation.[127] Section 9-505 permits either of these alternatives subject to a right to redeem by the debtor of the collateral, following repossession and before resale,[128] and sanctions imposed upon the secured party for his failure to comply with the provisions of this part.[129] It is thus submitted that section 9-505 presents no striking departure from existing Tennessee law in this area.[130]

VIII. Conclusion

The Uniform Commercial Code in its treatment of personal property security represents a sincere and conscious effort on the part of its draftsmen, authors and sponsors to update and modernize commercial law so as to be able to keep abreast of today's space-age economy. It is submitted that once a familiarity with the new terms, concepts, and theories is acquired, the average practitioner should not encounter any serious difficulty operating under the Uniform Commercial Code and will, in all probability, discover that in most instances the ideas are the same, although perhaps a little hard to recognize at first examination.

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125. Compare Tenn. Code Ann. § 47-2-706(6) (repl. vol. 1964).

126. The waiver provisions of Tenn. Code Ann. § 47-9-505(1) (repl. vol. 1964), are in accord with former Tennessee Law. Massillon Engine & Thresher Co. v. Wilkes, 82 S.W. 316 (Tenn. 1904); Commerce Union Bank v. Jackson, 21 Tenn. App. 412, 111 S.W.2d 870 (M.S. 1937); Gillenwaters v. Chapman Drug Co., 2 Tenn. App. 8 (E.S. 1925).

127. Uniform Commercial Code § 9-505, official comment 1.

128. Tenn. Code Ann. § 47-9-506 (repl. vol. 1964).

129. Tenn. Code Ann. § 47-9-507 (repl. vol. 1964).

130. See Comment, *supra* note 114, at 261.