



MEMORANDUM

To: Ed Smith, Chair, Joint Review Committee
From: Professor Stephen L. Sepinuck, ABA Advisor to Joint Review Committee
Date: December 10, 2008
Re: Issues For Consideration by the Committee

Acknowledging that the Joint Review Committee will need approval to go beyond its stated charge, I ask the Committee consider whether any or all of the following issues merit seeking such permission.

Technical Issues

1. Clarify whether an instrument which is part of chattel paper still an instrument. There was a comment to this effect under old § 9-104 but there is nothing similar in revised § 9-102.
2. Fix the definition of “good faith” in § 9-102(a)(43) along the lines of § 8-101(a)(10). Section 9-102 comment 19 tries to accomplish by statute should be done in the statute: make the heightened standard of good faith applicable to the Article 1 duty of good faith in an Article 9 transaction. This is important for: (i) the states that have not yet enacted revised Article 1; and (ii) those which have enacted revised Article 1 but chosen to retain the old, purely subjective standard of good faith,
3. Remove the limitation in § 9-102(a)(64)(D), (E) to the value of the original collateral. There is often no way to ascertain the value of the collateral before it was damaged or destroyed. It can be impossible to value it after it was damaged or destroyed. Moreover, if the insurance covers replacement value, all of that should be proceeds. it would be better to phrase the limitation as something like “arising from or payable as a result of damage to or destruction of the collateral.”
4. The last sentence of § 9-621 comment 2 indicates that a lienor with the right to notification of a proposed acceptance of collateral who does not received it has a cause of action against the secured party conducting the acceptance. This comment is correct if the notification was not sent, but is not accurate if the proposal was properly sent and simply not received.

5. Clarify whether/when a secured party must notify the debtor before foreclosing on an account debtor's collateral:

Account Debtor borrows from Dealer, and grants Dealer a security interest in specific goods. Dealer assigns the chattel paper to Creditor with recourse. In seeking to collect from Account Debtor, Creditor repossesses the goods and is preparing to dispose of them. Must Creditor give notification of the disposition to Dealer?

If the chattel paper was used as collateral for a loan (not sold without recourse), Dealer qualifies as an "obligor" under 9-102(a)(59) because Dealer either owes performance of Account Debtor's obligation or "is otherwise accountable in whole or in part for payment or performance of the obligation." Moreover, Dealer is likely to be a secondary obligor because Dealer probably has a right of recourse against Account Debtor. See § 9-102(a)(71)(B); Restatement (Third) of Suretyship and Guaranty § 1 & comment c. As a result, Creditor must generally give notification to Debtor of almost any planned disposition of Account Debtor's collateral. I suspect that this would be a surprise to most SPs and arguably inconsistent with the thrust of § 9-607(a).

6. Clarify whether a creditor can acquire an attached security interest in a motor vehicle (that is held as consumer goods or equipment, not inventory) through possession pursuant to an oral agreement. Presumably, a creditor could under 9-203(b)(3)(B). However, that provision refers to "possession of the secured party under section 9-313." It is unclear what that reference to 9-313 is intended to do. It could be a reference to 9-313(c), which indicates when a secured party has possession through an agent. Yet presumably the secured party could possess on its own accord, and nothing in 9-313 provides when or how that happens. Thus, such an interpretation would be an incomplete description of when a secured party has possession. Alternatively, the reference to 9-313 could be to 9-313(b), which covers goods covered by a certificate of title statute and indicates that compliance with the COT statute is generally the only way to perfect. However, that seems to confuse attachment with perfection and we can perceive no obvious reason why a COT statute should trump the normal rules on attachment. It would also seem to contradict the thrust of 9-203 comment 5. Finally, it could be reference to § 9-313(a), but that just does not seem to be a definition of possession.

Policy Questions

7. Provide for temporary continuity of perfection for a copyright that becomes registered. This may run up against federal law, but it should nevertheless be attempted. Under current law, the financing of debtors who acquire or generate copyrightable works (publishers and software developers) is problematic because even though a security interest will attach to after-acquired copyrights, perfection will be lost immediately upon federal registration and even if a federal filing is promptly made, the security interest remains vulnerable to preference attach for 90 days.

8. Should the suggestion in § 9-331 comment 5 that failure to search is a lack of good faith be revisited, particularly in light of *In re Jersey Tractor Trailer Training, Inc.*, 2008 WL 2783342 (D.N.J. 2008) (holding that a purchaser of accounts who searched under an incorrect name of the debtor and therefore failed to discover a proper filing by a previous secured party could not qualify as a holder in due course; the purchaser should have searched under the debtor's correct name and roots of that name)?
9. Consider revising § 9-607(c). That rule limits a secured party's duty to collect from account debtors in a commercially reasonable manner to situations in which the secured party has some right of recourse against the debtor or secondary obligor. In short, it imposes this duty in connection with loans secured by receivables rather than to pure sales of receivables. That limitation makes sense so long as the duty relates to only how the receivable is settled or compromised. *See* § 9-607 comment 9. However, the duty of commercial reasonableness probably encompasses more. For example, it should be interpreted as prohibiting the secured party from collecting in ways that injure the debtor's business reputation. Thus, harassment of account debtors or actions that violate the Fair Debt Collection Practices Act – regardless of whether it constitutes a tort – is and should be – commercially unreasonable. This type of behavior should be prohibited even when the receivables have been sold.
10. Does a subordination agreement follow the secured loan when it is sold?