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# Money, Money Everywhere but not a Drop to Secure: A Proposal for Amending the Perfection Rules for Security Interests in Money and Deposit Accounts

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# MONEY, MONEY EVERYWHERE BUT NOT A DROP TO SECURE: A PROPOSAL FOR AMENDING THE PERFECTION RULES FOR SECURITY INTERESTS IN MONEY AND DEPOSIT ACCOUNTS

BRIAN M. MCCALL\*

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“Radix enim omnium malorum est cupiditas quam quidam appetentes erraverunt a fide et inseruerunt se doloribus multis.”<sup>1</sup>

## I. INTRODUCTION

Although all creditors desire money to repay loans they have made, securing repayment with a lien on debtors' other money is not easy. Article 9 of the Uniform Commercial Code,<sup>2</sup> along with the rest of the UCC, has developed particular rules governing transactions in money that differ from transactions in goods and other personal property that are used as a medium of exchange. The drafters of Article 9 created a system that requires the artificial sorting of monetary value into different categories, depending on its form at any given moment. Physical currency,<sup>3</sup> instruments,<sup>4</sup> investment property,<sup>5</sup> and deposit accounts<sup>6</sup> all have different perfection rules.

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1. 1 *Timothy* 6:10 (Latin Vulgate). “For the desire of money is the root of all evils; which some coveting have erred from the faith, and have entangled themselves in many sorrows.” 1 *Timothy* 6:10 (Douay-Rheims, Challoner revision).

2. U.C.C. art. 9 (2007). Unless otherwise indicated, all references to “Article 9” are to the 2007 Official Text of the UCC, Article 9, entitled “Secured Transactions.”

3. Physical currency authorized by a governmental body, such as notes and coins, would fall under the definition of “money” in the UCC. See U.C.C. § 1-201(24) (1999).

4. Article 9 defines an “instrument” as  
a negotiable instrument or any other writing that evidences a right to the payment of a monetary obligation, is not itself a security agreement or lease, and is of a type that in ordinary course of business is transferred by delivery with any necessary indorsement [sic] or assignment. The term does not include (i) investment property, (ii) letters of credit, or (iii) writings that evidence a right to payment arising out of the use of a credit or charge card or information contained on or for use with the card.

U.C.C. § 9-102(a)(47) (2007). An example of an instrument would be a check. The definition, however, is drafted quite broadly, as evidenced by the second sentence. Specific items that the drafters do not wish to include in the term have been carved out. “Negotiable instruments” are a subset of instruments defined as

an unconditional promise or order to pay a *fixed amount of money*, with or without interest or other charges described in the promise or order, if it: (1) is payable to bearer or to order at the time it is issued or first comes into possession of a holder; (2) is payable on demand or at a definite time; and (3) does not state any other undertaking or instruction by the person promising or ordering payment to do any act in addition to the payment of money . . . .

This article argues that a secured party should be permitted to perfect a security interest<sup>7</sup> in all monetary value of a debtor, regardless of its form, by filing a financing statement. To accomplish this revision, two changes are necessary: (1) the rule that a security interest in physical currency may be perfected only by possession<sup>8</sup> must be abolished, and (2) a secured party should be able to perfect a security interest in deposit accounts of a debtor by either filing or control.

In support of this argument, Part II will briefly examine the nature and definition of money and the history of the treatment of money in parts of the UCC other than Article 9, particularly Article 2. Part III will examine the history of the treatment of money in Article 9 itself. Parts IV and V will examine various arguments in favor of and against the proposed change and, in particular, will examine the case for consistency, first with goods and second with the payment system in general—that is, among all the varying forms generally accepted as payment. Part VI will examine how the proposed change would advance two distinct roles of secured creditors, one as an asset-based lender and one as an investor in a going concern. Part VI also will touch upon fixed and floating charges, the two different types of security interests under English law, and compare them to Article 9. Finally, Part VII will summarize why Article 9 should be amended to eliminate the unique, inconsistent, discriminatory, and inefficient treatment of money.

Before proceeding, two underlying assumptions of this article must be stated. First, a system of secured credit with a significant priority in bankruptcy is economically efficient and likely to continue to exist for the foreseeable future. Second, the cost of obtaining secured credit generally will be less than the cost of obtaining unsecured credit. As a corollary, an increase in the amount of available collateral will result in a decrease in the cost of secured credit in at least some cases. Each of these assumptions is subject to debate, but they will nevertheless be used as a starting point for this article.

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U.C.C. § 3-104(a) (1999) (emphasis added). To paraphrase, then, an instrument may be an order or promise to pay money.

5. “Investment property” is “a security, whether certificated or uncertificated, security entitlement, securities account, commodity contract, or commodity account.” U.C.C. § 9-102(a)(49) (2007).

6. A “deposit account” is “a demand, time, savings, passbook, or similar account maintained with a bank . . . not includ[ing] investment property or accounts evidenced by an instrument.” *Id.* § 9-102(a)(29).

7. A “security interest” is “an interest in personal property or fixtures which secures payment or performance of an obligation.” U.C.C. § 1-201(37) (1999).

8. U.C.C. § 9-312(b)(3) (2007).

## II. THE NATURE AND DEFINITION OF MONEY

*A. Finding a Definition and Category for Money*

What is money? This is somewhat like asking, "What is love?" Most people profess to know what money is but would have a hard time defining it. The UCC defines "money" as "a medium of exchange currently authorized or adopted by a domestic or foreign government[, . . . includ[ing] a monetary unit of account established by an intergovernmental organization or by agreement between two or more nations."<sup>9</sup> This definition is interesting not only for what it contains but also for what it omits.

When defining "money" or the related term "cash," courts usually begin by referring to physical objects: coins, notes, or *specie*.<sup>10</sup> The UCC does not similarly limit the definition of money to physical items, though they appear to be included in the definition.<sup>11</sup> What else is meant to be captured by the definition in that case? The average layperson might think of funds in a bank account. In common parlance, people refer to bank accounts as "their money." Legally, this is inaccurate. Unless referring to physical currency placed in a safe deposit box, bank accounts are nothing more than a chose in action, a legal right to sue the bank to force it to pay the customer the amount of money represented by the bank account using the bank's unencumbered assets.<sup>12</sup>

Some courts have held that when people use the term "money," they intend to refer to bank accounts.<sup>13</sup> These cases, however, do not actually define "money" to include bank deposits. Rather, the cases reflect a court's attempt to ascertain the real intention of a party that used the word "money" in a will, bequest, or contract, which requires a court to look at "money" not in its technical, legal sense but in a more general, colloquial sense.<sup>14</sup> These cases demonstrate an important dichotomy between the commercial system and the legal system. In ordinary commerce, people use the term "money" to refer to all media of exchange or items representing monetary value, such as bank accounts, credit card payments, checks, notes, and coins. Yet the legal system,

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9. U.C.C. § 1-201(24) (1999).

10. See, e.g., *Lane v. Railey*, 133 S.W.2d 74, 79 (Ky. Ct. App. 1939); *Matthews v. Matthews-Baker (In re Estate of Matthews)*, 702 N.W.2d 821, 826 (Neb. Ct. App. 2005). "Specie" is defined as "coined money; coin." AMERICAN HERITAGE DICTIONARY 1730 (3d ed. 1992).

11. § 1-201(24).

12. See *Citizens Bank of Md. v. Strumpf*, 516 U.S. 16, 21 (1995); 1-9 Banking L. (MB) § 9.03 (Feb. 2005); Joseph H. Sommer, *Where Is a Bank Account?*, 57 MD. L. REV. 1, 7-10 (1998); see also *Libyan Arab Foreign Bank v. Bankers Trust Co.*, (1989) 3 All E.R. 252, 268 (Q.B.) (stating the identical rule under British law).

13. See, e.g., *Lane*, 133 S.W.2d at 81 (discussing the holding in *Mut. Life Ins. Co. of N.Y. v. Spohn*, 186 S.W. 633, 633-34 (Ky. Ct. App. 1916)).

14. See, e.g., *Lane*, 133 S.W.2d at 79; *Estate of Matthews*, 702 N.W.2d at 826.

and in particular the UCC, limits this definition to that which is “authorized” by a government.<sup>15</sup> This UCC definition potentially reduces the list to merely notes and coins. These cases acknowledge the dichotomy between ordinary commercial use and legal definitions by interpreting laypersons’ use of the term “money” as it is understood in everyday speech, as opposed to its legal definition.<sup>16</sup>

A key to understanding the UCC’s definition of money is the phrase “authorized or adopted by a domestic or foreign government.”<sup>17</sup> This phrase reflects the state theory of money, which can be summarized as follows: Money is whatever the appropriate government says it is.<sup>18</sup> This theory sheds light on the UCC’s definition. Under present law, the definition is limited to notes and coins; these physical items are the only things currently authorized or approved as “money.”<sup>19</sup> The definition is drafted in such a way, however, as to permit other, nonphysical concepts or transactions to be treated as money if “authorized or approved” by a government.<sup>20</sup>

This fiat (i.e., state-dictated) definition of money is not very helpful for purposes of the UCC and particularly of Article 9 because of the categorization technique used throughout the UCC. In order to apply the rules in the UCC and determine their legal effects, terms must not only be defined but must be ascribed to one of the categories devised by the Code, such as “goods,” “instruments,” or “general intangibles.”<sup>21</sup> Money could be categorized either as a good or as some form of intangible right. Money in the form of coins

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15. § 1-201(24).

16. See *Lane*, 133 S.W.2d at 79; *Estate of Matthews*, 702 N.W.2d at 826.

17. § 1-201(24).

18. See generally CHARLES PROCTOR, MANN ON THE LEGAL ASPECT OF MONEY 15-23 (6th ed. 2005) (describing the state theory of money in greater detail).

19. See § 1-201(24). See generally PROCTOR, *supra* note 18, at 15-23 (discussing government-authorized physical currencies in various states).

20. § 1-201(24). In theory, a bank account could become money if so authorized by a government. There is at least one precedent for money that did not exist in any physical form. During the process of European Monetary Union, the Euro was adopted as the currency of the European Member States. Prior to the introduction of Euro notes and coins, the national currencies of the member states remained in circulation and were simply redefined as a subdivision of the Euro (as if no U.S. dollars, only pennies, were in circulation). Although people could hold accounts (such as bank accounts and capital accounts in corporations) in Euros, they were not legally money but rather choses in action. Because Euros did not themselves have physical form, one could dispute whether Euros legally “existed” as money. Presidency Conclusions, Madrid European Council (Annex 1 paras. 8-9, 14) (Dec. 15-16, 1995); Sommer, *supra* note 12, at 7-10.

21. For example, it is necessary to know whether a document is an “instrument,” a “letter of credit,” or a “document” to determine whether the rules of Article 3, 5, or 7 apply to a specific transfer of such. Unless an item constitutes “goods,” Article 2 does not apply. For Article 9 purposes, different methods of perfection, and in some cases priority rules, are permitted or required depending on whether the collateral is categorized as “goods,” “instruments,” “accounts,” or “investment property.”

containing precious metals of intrinsic value could be goods.<sup>22</sup> Despite the disapproval of some commentators, particularly with respect to foreign exchange trading,<sup>23</sup> the courts appear to support the understanding of money—especially coins—as tangible personal property or goods. Thus, they have subjected transactions in money to the same rules as apply to other goods.<sup>24</sup>

With the advent of paper notes, money in the form of bank or government notes came to be seen as a chose in action, an intangible right to receive the amount of gold or other precious metal represented by the note.<sup>25</sup> On the other hand, this right later came to be seen as an instrument instead of a chose in action because the right was represented by a written promise, which was the note itself.<sup>26</sup> This description places money in the category of an instrument.<sup>27</sup>

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22. The 2000 version of the UCC defines “goods” as “all things (including specially manufactured goods) which are movable at the time of identification to the contract for sale other than the money in which the price is to be paid, investment securities (Article 8) and things in action.” U.C.C. § 2-105(1) (2000). Further, “[g]oods is intended to cover . . . money . . . being treated as a commodity but not . . . [as] the medium of payment.” *Id.* at cmt. 1. Thus, unless the money is that in which the price is to be paid, coins and notes could be seen as a “thing” that is “movable.” If, however, money is a chose in action, it would be excluded from the definition.

23. See, e.g., Thomas C. Baxter, Jr. & James H. Freis, Jr., *Resolving Funds Transfer Disputes Related to Currency Exchange Transactions: What Law Governs?*, 1995 COM. L. ANN. 297, 305-07; Stephen C. Veltri, *Should Foreign Exchange Be “Foreign” to Article Two of the Uniform Commercial Code?*, 27 CORNELL INT’L L.J. 343, 345-51 (1994); Michael Latham Manire, Note, *Foreign Exchange Sales and the Law of Contracts: A Case for Analogy to the Uniform Commercial Code*, 35 VAND. L. REV. 1173, 1188 (1982).

24. See, e.g., *United States v. Bryser*, 954 F.2d 79, 85 (2d Cir. 1992) (theft of money was theft of “goods” for purposes of 18 U.S.C. § 659); *Cordner v. United States*, 671 F.2d 367, 368 (9th Cir. 1982) (coins withdrawn from circulation and having numismatic value were property); *Levin v. Dare*, 203 B.R. 137, 146 (Bankr. S.D. Ind. 1996) (currency constitutes “tangible personal property” within meaning of Indiana exemption statute); *Villegas v. Transamerica Fin. Servs., Inc.*, 708 P.2d 781, 783 (Ariz. Ct. App. 1985) (money is a “good” or “commodity” within meaning of Arizona Consumer Fraud Act); *Exotic Coins, Inc. v. Beacom*, 699 P.2d 930, 935 (Colo. 1985) (en banc) (Colorado could regulate sellers of coins, as coins were regulated not as currency but as collectors’ items); *DeBiase v. Commercial Union Ins. Co. of N.Y.*, 278 N.Y.S.2d 145, 149 (N.Y. Civ. Ct.) (rare coins owned by coin collector are personal effects, not “money” within meaning of insurance policy), *aff’d*, 286 N.Y.S.2d 502, 502 (N.Y. App. Term 1967); *Thorne & Wilson, Inc. v. Utah State Tax Comm’n*, 681 P.2d 1237, 1238-39 (Utah 1984) (dealer in coins was selling “tangible personal property” in commodity transactions within meaning of state sales tax law); *Scotchman’s Coin Shop, Inc. v. Dir. of Revenue State of Mo.*, No. RS-81-0644, 1982 WL 12021, at \*4 (Mo. Admin. Hearing Comm’n Nov. 30, 1982) (money treated as a commodity is a good for purposes of Missouri sales tax laws). But see *United States v. Investors Diversified Servs., Inc.*, 102 F. Supp. 645, 647 (D. Minn. 1951) (loan of money is not lease, sale, or contract for sale of goods or commodities for purposes of the Clayton Act); *Riverside Nat’l Bank v. Lewis*, 603 S.W.2d 169, 174 (Tex. 1980) (money is not a “good” or “tangible chattel” within the meaning of Texas’s Deceptive Trade Practices Act).

25. See PROCTOR, *supra* note 18, at 25.

26. See *id.*

The difficulty today, considering that all governments have abandoned gold or other *specie* as a backing of their currency, is that modern-day coins contain no metals of intrinsic value and paper notes no longer represent the promise to pay any *specie*.<sup>28</sup> Thus, despite how most people act on a daily basis, the dollar bills in people's pockets are no longer goods, instruments, or even choses in action because they contain nothing of inherent value and do not represent the right to receive anything. Nevertheless, this history of the nature of money, as either goods or an instrument, continues to affect the categorization and treatment of money in the UCC.

*B. The Treatment of Money in Article 2: Sometimes Goods, Sometimes Not*

Article 2 of the UCC defines "goods" as "all things that are moveable at the time of identification to a contract for sale."<sup>29</sup> Many commentators and several courts have interpreted this definition to require that contracts for the sale of money be considered contracts for the sale of goods covered by Article 2—and often contracts for the sale of commodities, as with foreign currency and items no longer valid as legal tender.<sup>30</sup> This definition of "goods" excludes the money in which the sale price is to be paid. This exclusion does not affect this author's characterization of the nature of money. The exclusion merely serves to limit the scope of Article 2 by preventing all contracts from falling under Article 2 simply for involving the payment of money.<sup>31</sup> The drafters likely felt this exclusion was important because the definition of goods otherwise would necessarily include money.

Perhaps the inclusion of money within the concept of goods is a residual effect of the era when money actually was a physical object of intrinsic value. Earlier versions of Article 2 were unclear as to whether foreign exchange

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27. See U.C.C. § 9-102(a)(47) (2007); see also PROCTOR, *supra* note 18, at 17 (noting that "[b]anknotes in the modern sense were not always distinguishable from other negotiable instruments," are "promissory notes within the meaning of section 83 of the Bills of Exchange Act 1882" (the UK's equivalent to Article 3 of the UCC), but at the same time are more than a negotiable instrument).

28. In fact, under United States law, a dollar bill represents the right to demand the payment of another dollar bill. See 12 U.S.C. § 411 (2000) (mandating that Federal reserve notes "shall be redeemed in lawful money on demand"); 31 U.S.C. § 5103 (2000) (making Federal reserve notes lawful money); see also PROCTOR, *supra* note 18, at 63 (describing all currencies as "fiduciary money" with purchasing power unrelated to their intrinsic value).

29. U.C.C. § 2-103(1)(k) (2007); see U.C.C. § 2-105(1) (2000).

30. See *Koreag, Controle et Revision S.A. v. Refco F/X Assocs., Inc.* (In re *Koreag, Controle et Revision S.A.*), 961 F.2d 341, 355 (2d Cir. 1992); *Vishipco Line v. Chase Manhattan Bank, N.A.*, 754 F.2d 452, 455 (2d Cir. 1985); *Compania Sud-Americana de Vapores, S.A. v. IBJ Schroder Bank & Trust Co.*, 785 F. Supp. 411, 431 n.19 (S.D.N.Y. 1992); U.C.C. § 2-103 cmt. 7 (2007); U.C.C. § 2-105 cmt. 1 (2000); 9 SAMUEL WILLISTON & RICHARD A. LORD, A TREATISE ON THE LAW OF CONTRACTS § 26.14 (4th ed. 1999).

31. For example, Article 2 was not intended to cover an employment contract, even though the employer agrees to pay money in exchange for services.



transactions, which cannot be settled in physical form by actual delivery of money, were included. Many courts held that foreign exchange transactions constituted sales of goods governed by Article 2, but these courts did not analyze whether delivery was made in the form of money or a chose in action, such as a payment to a bank account.<sup>32</sup> Some commentators advocated the efficiency and benefits of this broad reading and recommended that Article 2 be revised to place all foreign exchange transactions clearly within its scope.<sup>33</sup>

Despite such commentary, the 2007 text of Article 2 distinguishes between foreign exchange transactions that are settled in physical form and those that are settled by payment to a bank account.<sup>34</sup> Foreign exchange transactions that are settled in physical form are included within Article 2's definition of "goods," but those settled by payment to a bank account are excluded.<sup>35</sup> In fact, transactions that are settled in physical form do not even fall under the subject matter of the term "foreign exchange transaction" as defined in the 2007 version of Article 2.<sup>36</sup> Rather, a "foreign exchange transaction" requires both parties to deliver the object of the transaction "through funds transfer, book entry accounting, or other form of payment order, or other agreed means to transfer a credit balance";<sup>37</sup> this transaction is not considered an exchange of goods.<sup>38</sup> Thus, under the 2007 version, money in the form of physical currencies, notes, and coins fall under Article 2's definition of "goods" when the subject of a contract,<sup>39</sup> but the sale of money in the form of bank transfers does not.<sup>40</sup> As a result, the 2007 version of Article 2 brings the treatment of

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32. See, e.g., *Koreag*, 961 F.2d at 355; *Intershoe, Inc. v. Bankers Trust Co.*, 571 N.E.2d 641, 644 (N.Y. 1991); see also *Saboundjian v. Bank Audi (USA)*, 556 N.Y.S.2d 258, 261-62 (N.Y. App. Div. 1990) (finding Article 2 of the UCC "instructive" when calculating damages in a case involving foreign currency trading). But see *United Equities Co. v. First Nat'l City Bank*, 383 N.Y.S.2d 6, 11-12 (N.Y. App. Div. 1976) (applying various provisions of Article 2 of the UCC despite it being "unlikely that the parties anticipated at the time of making the contract that there would be a physical delivery" of the foreign currency and treating deposits to a bank account as an adequate delivery method under Article 2), *aff'd*, 363 N.E.2d 1385 (N.Y. 1977).

33. See, e.g., Raj Bhala, *A Pragmatic Strategy for the Scope of Sales Law, the Statute of Frauds, and the Global Currency Bazaar*, 72 DENV. U. L. REV. 1, 3-5 (1995).

34. As of the writing of this article, no jurisdiction has adopted the 2007 version of Article 2; these changes exist only in the theoretical world, not in the law of any jurisdiction.

35. U.C.C. § 2-103(1)(i), (k) (2007) (defining foreign exchange transactions as nonphysical transactions and excluding them from the definition of "goods").

36. *Id.*

37. § 2-103(1)(i).

38. § 2-103(1)(k).

39. This reasoning suggests that foreign exchange transactions settled in physical form would be goods subject to the 2007 version of Article 2. Under the 2000 version, though, which is still in force in all jurisdictions, the result is uncertain. Article 2 might exclude all foreign exchange transactions, include them all, or only include those settled in physical form.

40. U.C.C. § 2-103(i) (2007). In one sense, the new definition of "foreign exchange transactions" settles this issue, but there are still some interesting ambiguities in the language. The first sentence of the definition of foreign exchange transactions uses the phrase "in which

money in line with Article 9 in applying different rules to transactions in monetary value when such value is represented in a tangible form, as opposed to an intangible form.<sup>41</sup>

### III. TREATMENT OF MONEY AND DEPOSIT ACCOUNTS IN ARTICLE 9

#### A. *The Original Version of Article 9: Open Issues*

The categorization of money in the context of Article 9 has had an even less straightforward history than under Article 2. As originally drafted, Article 9 contained no explicit definition placing “money” within one of its categories of personal property.<sup>42</sup> This left three possibilities: (1) money is personal property covered by the scope of Article 9 but is not “goods,” which would make filing a financing statement the only permissible method of perfecting a security interest in money; (2) money is covered by Article 9 and constitutes “goods,” which would mean a security interest may be perfected either by filing or by possession; or (3) money is not covered by Article 9, which would mean common law governs the perfection of security interests in money.

In the 1967 case of *In re Midas Coin Co.*,<sup>43</sup> the court grappled with this issue and decided that when money was being used as a commodity, it would

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*delivery is to be through*” one of the listed nonphysical payment methods. *Id.* (emphasis added).

The last sentence, describing transactions that are excluded from the definition (and therefore included in Article 2), uses the phrase, “in which one or both of the parties is *obligated* to make physical delivery . . . of banknotes, coins, or other form of legal tender or specie.” *Id.* (emphasis added). The definition does not explain clearly how to categorize a foreign exchange contract that provides for either physical delivery or an alternate form of settlement. If the receiving party can make the election for physical settlement, the payor appears obligated. If, however, the payor can make the election, one could argue there is no actual obligation to deliver physical currency. Furthermore, even where there is a contractual requirement of physical settlement, standard practice is to settle virtually no commercial foreign exchange transactions by physical delivery. If “delivery is [in fact] to be through” nonphysical form despite a technical obligation to deliver physical currency, is such a contract included in the definition of “foreign exchange transaction” and thus excluded from Article 2? The official commentary gives no indication. Finally, it is curious that the drafters used the phrase “bank notes, coins, or other form of legal tender or specie” instead of the defined term “money” in the exclusion clause. The definition of money is broad enough to encompass a situation where a government authorizes a nonphysical form of money (that is, a currency that exists wholly without notes and coins). Would a foreign exchange transaction in such nonphysical currency be excluded from the definition of “foreign exchange transaction” if a party were obligated to physically deliver legal tender, albeit a legal tender that exists wholly in the form of a book entry account or credit? The definition leaves this issue open.

41. § 2-103(1)(i), (k).

42. U.C.C. art. 9 (1962).

43. 264 F. Supp. 193 (E.D. Mo. 1967).

be considered goods.<sup>44</sup> Therefore, money as a commodity was covered by Article 9 and a bank's possession of the money perfected its security interest.<sup>45</sup> The decision makes sense and appears to be a reasonable interpretation of the UCC as in effect at that time.<sup>46</sup> The court had concluded that given the broad scope of Article 9, which covers security interests in all personal property other than two specifically designated items, money must be included in the scope of Article 9.<sup>47</sup>

The court had read the scope provision to require all personal property covered by Article 9 to be included in one of the categories enumerated in section 9-102, as then enacted.<sup>48</sup> The only two possibilities contained in the enumerated list into which money could fall were "general intangibles" or "goods."<sup>49</sup> The court concluded that because money was tangible and because the Article 9 definition of "goods" referred to money and general intangibles as separate items, money was not a general intangible.<sup>50</sup> The court found that despite the explicit exclusion of "money" from the Article 9 definition of "goods,"<sup>51</sup> the drafter's intent was to allow perfection by possession, in accord with the common law.<sup>52</sup> The court relied heavily on the fact that Article 2 treated money as "goods" when it was the subject matter of a sales transaction—that is, when money was treated as a commodity.<sup>53</sup> The court also found that Articles 9 and 2 should be read consistently. In other words, if money was subject to the rules governing *sales* of goods, money should also be subject to the same rules as goods when perfecting a security interest.

Many courts have since concluded that holding a bank's possession of money to be insufficient to perfect a security interest would contradict common

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44. 264 F. Supp. at 197.

45. *Id.* at 197-98.

46. *Id.* at 195. The UCC defined "goods" as "all things which are moveable . . . but does not include money, documents, instruments, accounts, chattel paper, general intangibles, contract rights and other things in action." *Id.* (quoting U.C.C. § 9-105 (1962)). "Money" was further defined as "a medium of exchange" adopted by a government as "currency." *Id.*

47. *Id.* at 195-96.

48. *Id.* at 198. The court read the words "including goods, documents, instruments, general intangibles, chattel paper, accounts or contract rights" to serve as a limiting function (i.e., only items in those categories were personal property subject to Article 9). The court thus reasoned that "money" must fall in one of the enumerated categories. *Id.* at 198-99. In the course of amending this provision that now appears in section 9-109 of the 2007 version of the UCC, this list of types of personal property has been omitted. U.C.C. § 9-109 (2007). However, "[n]o change in meaning is intended." § 9-109 cmt. 2. In any event, even if not required to fall into one of the formerly enumerated categories to come within the scope of Article 9, an item of personal property must match one of the terms in sections 9-308 through 9-316 for the UCC to supply the correct perfection method.

49. *In re Midas*, 264 F. Supp. at 199.

50. *Id.* at 198-99.

51. *Id.* at 195 (quoting U.C.C. § 9-105(1)(f) (1962)).

52. *Id.* at 196 (quoting § 9-105 cmt. 1).

53. *Id.*

sense and the policy behind Article 9 of promoting public notice of valid security interests.<sup>54</sup> Finally, it also would contradict the notion that creditors of a debtor who had surrendered possession of money should be on notice that the debtor has transferred some property right in the money to a third party.

*B. The 1972 Revisions and the Inadvertent Omission*

As the *In re Midas* court showed, it was possible to treat money as “goods” for which perfection could be achieved either by filing or possession.<sup>55</sup> In 1972, perhaps reacting to this decision, section 9-304(1) was amended to require possession as the only valid method for perfecting a security interest in money.<sup>56</sup> This change foreclosed the possibility of perfecting a security interest in money by filing. The official reason given in the Appendix for this change was the following: “The change in subsection (1) corrects an inadvertent omission in the 1962 Text, and makes clear that a security interest in money cannot be perfected by filing.”<sup>57</sup> Even if the omission of money from the mandatory possession rule truly had been inadvertent, the explanation in the Appendix did not detail the reasons for excluding money from the filing regime.

An official comment to section 9-304 goes on to state that “[f]or similar reasons [to those for excluding instruments], filing is not permitted as to money.”<sup>58</sup> These reasons attempt to give a two-part rationale for requiring possession for perfection of security interests in instruments: The rule (1) follows the Uniform Trust Receipts Act (UTRA) and (2) corresponds to commercial practice.<sup>59</sup> Even if these reasons applied to money, they provide poor justification.

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54. *Octagon Gas Sys., Inc. v. Rimmer*, 995 F.2d 948, 957 (10th Cir. 1993); *Hong Kong & Shanghai Banking Corp. v. HFH USA Corp.*, 805 F. Supp. 133, 140 n.3 (W.D.N.Y. 1992); *North v. Desert Hills Bank (In re North)*, 310 B.R. 152, 159 (Bankr. D. Ariz. 2004); *In re Atl. Computer Sys., Inc.*, 135 B.R. 463, 466 (Bankr. S.D.N.Y. 1992); *Newton v. First Am. Nat'l Bank (In re Webb)*, 106 B.R. 517, 521 (Bankr. E.D. Tenn. 1989); *In re Vt. Knitting Co.*, 98 B.R. 184, 189 (Bankr. D. Vt. 1989); *Brams Ltd. v. Elf Enters., Inc.*, 573 N.W.2d 139, 143 (Neb. 1998); *Chase Manhattan Bank v. State (In re Chase Manhattan Bank)*, 357 N.E.2d 366, 368 (N.Y. 1976).

55. *See supra* Part II.A.

56. U.C.C. § 9-304(1) (1972).

57. *Id.* at app.

58. *Id.* at cmt. 1.

59. *Id.* Specifically, the comment states:

With respect to instruments subsection (1) provides that, except for the cases of “temporary perfection” covered in subsections (4) and (5), taking possession is the only available method; this provision follows the Uniform Trust Receipts Act. The rule is based on the thought that where the collateral consists of instruments, it is universal practice for the secured party to take possession of them in pledge; any surrender of possession to the debtor is for a short time; therefore it would be unwise to provide the alternative of perfection for a long period by filing which, since it in no way corresponds with

As to the first reason, the definition of “goods” in the UTRA explicitly excluded money.<sup>60</sup> The UTRA, unlike Article 9, was drafted to serve a narrow set of transactions.<sup>61</sup> Both in the scope of property covered by the UTRA<sup>62</sup> and in the limitation on its applicability to certain enumerated transactions,<sup>63</sup> the UTRA was narrowly delineated. The reason for these restrictions lay in the UTRA’s purpose, which was to simplify and standardize the law relating to a specific subset of financing transactions, primarily the importation of foreign goods for resale.<sup>64</sup>

The drafters of Article 9, on the other hand, set themselves a much broader scope both in terms of the types of property and the transactions to be covered.<sup>65</sup> Article 9 “provide[d] a comprehensive scheme” that regulated security interests in all types of personal property with limited, specific exceptions.<sup>66</sup> The enumerated purposes for covered transactions of the UTRA have disappeared from Article 9. The exclusion of money from the definition of “goods” in the UTRA was necessary to achieve its more limited scope, but because Article 9 was intended broadly to regulate security interests in money and many other items,<sup>67</sup> its definition of “goods” served a different purpose. That purpose was to identify the correct method of perfection of such interests. Thus, the UTRA’s exclusion of money from the definition of goods is not an adequate rationale for the exclusion of money from the definition of goods or the filing regime of Article 9.

The comment’s second rationale, that the rule corresponded to commercial practice,<sup>68</sup> also does not provide a solid justification. First, the comment does not discuss the rationale for extending the possession-only perfection rule to money.<sup>69</sup> It only discusses the rule as to instruments and then assumes that the same commercial practice exists for both money and instruments.<sup>70</sup> Second, commercial practice is not necessarily proof of the best or most efficient rule

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commercial practice, would serve no useful purpose.

For similar reasons, filing is not permitted as to money. *Id.*

60. Unif. Trust Receipts Act § 1 (1957) (“‘Goods’ means any chattels personal other than: money, things in action, or things so affixed to land as to become a part thereof.”).

61. *Id.* at commissioners’ prefatory note.

62. “Trust receipts” are defined as security interests in goods, documents, and instruments. *Id.* § 2(1)(a).

63. *See id.* § 2(3) (requiring that possession of the subject property by the trustee be for one of three stated purposes: resale or exchange of goods, documents, or instruments; manufacture of goods or documents for sale or shipping; or delivery, presentation, collection, or renewal of instruments.)

64. *See id.* at commissioners’ prefatory note.

65. U.C.C. § 9-101 cmt. 1 (2007); *id.* § 9-109; *see also* U.C.C. § 1-201(37) (1999) (defining “security interest” broadly).

66. U.C.C. § 9-101 cmt. 1 (2007); *id.* § 9-109; *accord* U.C.C. § 1-201(37) (1999).

67. *See* U.C.C. § 9-304 (1972).

68. *Id.* at cmt. 1.

69. *Id.*

70. *Id.*

because commercial practice had been formed by the legal regime governing security interests.<sup>71</sup> Because the law had mandated that the only method for perfecting a security interest in money was possession, it was necessarily true that secured parties' commercial practice would be either to perfect by possession or not to perfect where possession was impractical or impossible.<sup>72</sup> A commercial practice designed to conform with an existing legal rule is unconvincing as support for the restatement of that rule.

Prior to the initial adoption of Article 9, the UTRA was intended to cover only certain types of collateral, not including money. Thus, a secured party in a transaction involving money had been required to perfect under the common law rule, which required possession. The original version of Article 9 had been unclear as to the proper treatment of money, as demonstrated by *In re Midas*. Since the 1972 amendments to Article 9, it has become clear that money constitutes its own category of personal property distinct from goods and, as under the common law, possession is the only permissible method for perfecting a security interest in it. The general evolution of Article 9 in other respects, though, has been to move away from common law pledges, both by including more types of property in the scope of Article 9<sup>73</sup> and by expanding the use of filing.<sup>74</sup> Though the rule as to the perfection of security interests in money has been clarified, there has never been a thoughtful analysis of why money should be excluded from this general trend of permitting perfection by filing.

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71. See Laura Bartell, *The Lease of Money in Bankruptcy: Time for Consistency?*, 16 BANKR. DEV. J. 267, 319 (2000) (stating that "just because these expectations are shaped by the legal regime governing them, it makes no sense to justify the legal regime by the intent of the parties. Nor is it likely, in this 'chicken-or-the-egg' scenario, that the intent of the parties is really driving the legal characterization"); see also PERMANENT EDITORIAL BD. FOR THE UNIF. COM. CODE, PEB STUDY GROUP UNIFORM COMMERCIAL CODE ARTICLE 9 REPORT section 18.A (1992) [hereinafter PEB STUDY GROUP REPORT] (stating in its discussion of instruments, "That rationale is somewhat circular. It is not surprising that commercial practice is to take possession when that step is the only means of achieving perfection.").

72. If, however, both filing and possession were clearly permissible methods, incidents of secured parties choosing possession over filing could indicate that they found possession to serve an important purpose not achieved by mere filing, such as protecting their security interests against third-party good faith transferees.

73. See, e.g., U.C.C. § 9-101 cmt. 4(a) (2007); *id.* § 9-109; see also *id.* § 9-102 (defining the types of property discussed in Article 9). This is further evidenced by the inclusion of deposit accounts, payment intangibles, health care insurance receivables, nonpossessory statutory agricultural liens, supporting obligations, and property securing rights to payment and commercial tort claims. See *id.* § 9-109.

74. See *id.* § 9-312(a) (including instruments and investment property within the types of collateral for which filing can be effective).

*C. The History of Deposit Accounts*

The history of deposit accounts is simpler than that of money. Prior to the adoption of the 1999 version, Article 9 excluded transactions in deposit accounts from its scope.<sup>75</sup> As with money, scant justification was given for the exclusion. Comment 7 states:

Rights under life insurance and other policies, and deposit accounts, are often put up as collateral. Such transactions are often quite special, do not fit easily under a general commercial statute and are adequately covered by existing law. Paragraphs (g) and (l) make appropriate exclusions, but provision is made for coverage of deposit accounts and certain insurance money as proceeds.<sup>76</sup>

Despite acknowledging that bank accounts are often used as collateral, the comment concludes that bank accounts should be excluded because they are often quite "special" and "do not fit easily under a general commercial statute."<sup>77</sup> The comment provides no explanation of how deposit accounts are special or why this particular chose in action cannot fit as easily under a general commercial statute as can a payment intangible not originating from a bank.

Deposit accounts were not completely excluded, however, because the definition of deposit accounts did not cover "an account evidenced by a certificate of deposit."<sup>78</sup> Again, there is no explanation of why the issuing of a certificate of deposit to represent the deposit account makes the transaction less "special" or more capable of easily fitting "under a general commercial statute."<sup>79</sup> The claim that existing law adequately covered the area is also difficult to defend.<sup>80</sup>

The anomaly of the exclusion of certain bank accounts appeared evident to the Permanent Editorial Board (PEB) Study Group on Article 9. They originally proposed including deposit accounts within Article 9's scope and within the filing regime.<sup>81</sup> Two of the questions that emerged through the

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75. U.C.C. § 9-104(l) (1972).

76. *Id.* § 9-104 cmt. 7.

77. *Id.*

78. *Id.* § 9-105(1)(e).

79. *Id.* § 9-104 cmt. 7.

80. See William F. Kroener III & Stephen L. Sepinuck, *Report of the Subcommittee on the Use of Deposit Accounts as Original Collateral* 3 (Article 9 Study Comm. Permanent Editorial Bd. for Unif. Com. Code, Working Document No. M6-44, 1992) [hereinafter *Report of Subcommittee*] ("[N]on-Code law does not adequately cover security interests in deposit accounts. In most jurisdictions and for most deposit accounts, the law provides no certain method to create a security interest in a deposit account and it is difficult to predict whether any specific attempt to create one will be enforced.").

81. See PEB STUDY GROUP REPORT, *supra* note 71, at section 18.A; *Report of Subcommittee*, *supra* note 80, at 4. The subcommittee originally proposed a two-tiered structure that would require filing for secured parties who were not the deposit bank; perfection would

drafting process were: (1) whether consumer deposit accounts should be included and (2) whether filing should be permitted.<sup>82</sup> These debates were resolved in the 1999 UCC revisions.

*D. The 1999 Revisions and the Treatment of Instruments and Deposit Accounts*

One of the self-described “important change[s]” in the 1999 revisions of Article 9 was a rule allowing perfection by filing with respect to a security interest in instruments.<sup>83</sup> The rule includes several special priority rules and protections for certain transferees.<sup>84</sup> The comments to the section effecting this change describe the rationale:

Under subsection (a), a security interest in instruments may be perfected by filing. This rule represents an important change from former Article 9, under which the secured party’s taking possession of an instrument was the only method of achieving long-term perfection. The rule is likely to be particularly useful in transactions involving a large number of notes that a debtor uses as collateral but continues to collect from the makers.<sup>85</sup>

Again, no detailed explanation for the rule change has been provided, other than the fact that it will benefit some transactions where large numbers of instruments are used as collateral.<sup>86</sup>

The rationale that filing could be of use for some transactions involving a large number of instruments raises a question: Why is there not a similar rationale for situations in which a debtor has a large amount of money he desires to use as collateral?<sup>87</sup> The only explanation for the exclusion of money from the filing regime was a cross-reference to the reason for excluding instruments,<sup>88</sup> which of course are no longer excluded. Consequently, there remains no explanation of the reason for requiring possession for perfecting a security interest in money.

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then be automatic upon attachment for the deposit bank. *See Report of Subcommittee, supra* note 80, at 22-27.

82. *See Report of Subcommittee, supra* note 80, at 22-27.

83. U.C.C. § 9-312 cmt. 2 (2007).

84. *Id.* § 9-312.

85. *Id.* at cmt. 2.

86. *See id.*

87. It might not be immediately apparent why a debtor with a large amount of money would need a loan. Many businesses will require the use of large amounts of cash in the operation of their business and thus cannot use that money as cash available for making purchases or paying off loans. Examples include businesses that use money as the products they sell (such as currency exchange operators, coin dealers, and check cashers) and businesses like multiple-location retailers that need money to complete retail transactions.

88. U.C.C. § 9-304 cmt. 1 (1972).



Furthermore, the 1999 revisions addressed the issue of consumer deposit accounts. The drafters excluded consumer accounts from the revised text of Article 9<sup>89</sup> and nonconsumer accounts from the filing regime.<sup>90</sup> The first compromise involved issues of the intersection of Article 9 and consumer protection law, which falls outside the scope of the current discussion. The second compromise significantly reduced the effect of including non-consumer deposit accounts within Article 9.

#### IV. A CASE FOR PERMITTING FILING

Reasons in favor of the changes proposed by this author can be categorized as follows: (1) promoting consistency within the UCC, particularly because current inconsistency results in unnecessary discrimination against certain types of debtors and transactions, (2) promoting the policy of fair and public notice of interests in property, and (3) simplifying the treatment of proceeds of collateral. This Part explores each of these benefits before turning in the next Part to an examination of possible objections.

##### *A. Consistency and Elimination of Unnecessary Discrimination*

Two notions of consistency are relevant to the argument for filing. First, for purposes of formalism and logic, the UCC should treat money in a consistent manner throughout. If, in its essence, money is like other goods, it should be treated like goods not only for the purposes of Article 2 but for the purposes of Article 9 as well. In other words, unless there is some specific reason relating to the nature of secured transactions that justifies varied treatment, money should be viewed the same way for every purpose of the UCC.

The second notion of consistency arises from the interrelation of the classes of personal property contained in the payment system (e.g., money, instruments, deposit accounts, and investment property). These items appear to have great similarities, which would warrant similar treatment.<sup>91</sup> As value moves through the payment system, it should be treated consistently whenever possible, regardless of its form.<sup>92</sup> Because an obligation to pay a \$100 check, a bank account with a balance of \$100, or a \$100 bill all represent an identical value that differs only in form, they are treated as fungible by commercial actors. A distinction among these types seems arbitrary and can create arbitrary

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89. U.C.C. § 9-109(d)(13) (2007) (unchanged from the 1999 revision). Idaho, Illinois, Louisiana, Mississippi and Oklahoma have declined to include the exclusion of consumer deposit accounts.

90. *Id.* § 9-312(b)(1) (unchanged from the 1999 revision).

91. See discussion *infra* Part IV.A.2.

92. See discussion *infra* Part IV.A.2.

results and behavior. These arbitrary results discriminate against certain types of debtors and transactions.<sup>93</sup>

### 1. Consistency with the Definitions of “Money” and “Goods”

The law, especially Article 2, generally has treated money as goods.<sup>94</sup> Under the version of Article 2 currently in force in most jurisdictions, the sale of money is usually treated as the sale of goods.<sup>95</sup> The proposed 2007 version of Article 2 attempts to distinguish the sale of money<sup>96</sup> in nontangible form, such as electronic transfer, and exclude it from Article 2. Some commentators have argued that all transactions where money is the subject should be made explicitly subject to Article 2 as the sale of goods.<sup>97</sup> For now, this remains only a possible interpretation of Article 2 as currently adopted.

The *In re Midas* court looked to the treatment of money in Article 2 and determined that money is considered goods when treated as a commodity.<sup>98</sup> Sales of physical currency are subject to the same legal regime as the sale of goods.<sup>99</sup> This is important in light of Article 9 because when Article 9 speaks of “money,” it also is referring to money in physical form as opposed to other intangible forms.<sup>100</sup> It is illogical that when a coin dealer sells coins, the coins are goods subject to Article 2, but if the coin dealer wants to obtain a loan secured by the coins, they would no longer constitute goods.

Further, Article 9 is inconsistent with the definition of “money” in Article 1, which does not require money to exist in any tangible form.<sup>101</sup> Any medium of exchange authorized by a government, even a medium that is wholly electronic or intangible, would qualify as money.<sup>102</sup> As currently drafted, one cannot perfect a security interest in intangible money because there is nothing to “possess.” Thus, the definition of “money” for purposes of the rest of the UCC is inconsistent with the perfection rule of Article 9. Allowing perfection by either filing or possession would accommodate both physical and intangible money.

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93. See discussion *infra* Part IV.A.1.

94. See discussion *supra* Part II.

95. See discussion *supra* Part II.B.

96. Here the term “money” is being used in a nontechnical, generic sense, not as defined in the UCC.

97. See, e.g., Bhala, *supra* note 33, at 3-5.

98. See *supra* Part III.A.

99. See *supra* Part II.B.

100. See U.C.C. § 9-312 (2007). This is because the other “forms” of money are covered by other classes of collateral with their own perfection rules. Because section 9-312 requires possession of money to accomplish perfection, it assumes that money is always represented by something tangible which can be possessed.

101. See U.C.C. § 1-201(24) (1999).

102. See discussion *supra* Part II.A.

One approach to achieving consistency throughout the UCC would be to adopt a use test, as in *In re Midas*.<sup>103</sup> When money is used as an object of a transaction, it would be treated as goods, but when money is used as a medium of exchange, it would not. Under this approach, filing would be permitted when money is treated like inventory by the debtor (i.e. a coin dealer or a currency exchange operator). Yet the use test likely would be difficult to administer. For example, a currency exchange operator hands across an English pound, which is inventory, in exchange for a dollar bill, which might be reused as inventory later. Is the dollar bill considered inventory or a medium of exchange?

An over-inclusive rule would be simpler to administer, such as a rule where money is always treated like goods. If consistency can be found with the other categories of property, it may be reasonable to ignore the distinction drawn between physical and nonphysical money in the 2007 revision of Article 2 and treat all money in a consistent manner by allowing filing.<sup>104</sup> The main reason for exclusion of money from the definition of goods in Article 2 is to avoid the extension of Article 2 to all contracts where money is paid in exchange for the promises or performance of the contracting party.<sup>105</sup> Such a concern does not apply to Article 9, so a different rule—consistent with the remaining UCC provisions—may be justifiable.

The current inconsistent treatment of money and goods discriminates against debtors who maintain large amounts of cash. These debtors fall into two categories: (1) those who deal in money and (2) service-based businesses that tend to receive many payments in cash. The first category includes coin dealers, currency exchange operators, check cashing businesses, and ATM owners. The inventory of these businesses consists of money. Because money is not a “good” as defined by Article 9, their inventory is not treated like inventory of other debtors. The second disadvantaged group includes such businesses as theme parks, taxi and bus companies, Laundromats, dry cleaners, vending machine and videogame operators, and beauty salons. Cash received by these businesses as payments for services is different from cash proceeds arising from the sale of goods because a security interest can be perfected in the goods before the goods are sold. This puts service-based businesses at a disadvantage to those that primarily sell goods.<sup>106</sup>

For both categories of businesses, money often represents a significant, in some cases the most significant, asset in their working capital. The nature of a business may require that cash be maintained in large quantities as opposed to converting it to other forms of value, such as bank accounts or instruments. The existing regime discriminates against such debtors by effectively precluding them from using these assets as collateral because the secured party’s security interest will remain unperfected. As a result, these businesses

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103. 264 F. Supp. 193, 199 (E.D. Mo. 1967).

104. See discussion *infra* Part IV.A.2.

105. See discussion *supra* Part II.B.

106. See discussion *infra* Part V.A.

must contend with a significantly reduced borrowing base for obtaining secured credit. There does not appear to be a good policy rationale for subjecting these categories of businesses to a reduced borrowing base and therefore to paying more for both secured and unsecured credit.

## 2. Consistency Among the Various Forms of Money

Liquid financial value (i.e., media of exchange regardless of whether they are authorized by a government) takes several forms in the existing payment system: physical cash, instruments, deposit accounts, investment property, and receivables from credit card payments. Despite the fact that financial value flows freely and rapidly among these various forms, and despite the fact that most participants in the payment system treat these forms as essentially fungible, Article 9 creates three distinct perfection regimes: (1) possession, (2) control,<sup>107</sup> and (3) filing.<sup>108</sup> The availability of each of these regimes is a function of what form the financial value exists in at the moment of perfection.

Filing should be available as a permissible method at all times, regardless of the form of the financial value. The possession regime for money has already been discussed. The following section discusses the rules for the other forms of monetary value and argues for the addition of filing as an option for both money and deposit accounts.

### a. Instruments and Credit Card Payments

In addition to the precedent for considering money as goods, there is also precedent for treating money like instruments.<sup>109</sup> When money in the form of paper notes formerly represented the right to receive *specie*, the similarity to an instrument was especially pronounced.<sup>110</sup> Even in the modern world of fiat currency, the law often treats money and instruments in a similar manner.

The law of property provides an example. A person who acquires personal property from another acquires only the interests that his transferor had. One who acquires property from a thief or a converter does not acquire good title to the property.<sup>111</sup> This principle does not apply, however, if the property in

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107. U.C.C. §§ 9-104, 9-106 (2007).

108. See U.C.C. art. 9 (2007).

109. See discussion *supra* Part III.

110. See U.C.C. § 3-104 (1999). A negotiable instrument is “an unconditional promise or order to pay a fixed amount of money” to the bearer on demand and does not require any other undertaking by either party. *Id.* So, too, does a note backed by *specie* represent the unconditional promise of the issuer, usually the sovereign, to pay a stated amount of *specie* to the bearer of the note either on demand or at times prescribed by statute. PROCTOR, *supra* note 18, at 25.

111. RESTATEMENT (SECOND) OF TORTS § 229 (1965) (“One who receives possession of a chattel from another with the intent to acquire for himself or for a third person a proprietary interest in the chattel which the other has not the power to transfer is subject to liability for

question is either money or instruments.<sup>112</sup> Though there are subtle distinctions between the treatment of money and instruments,<sup>113</sup> the general policy and principles are the same. Those who acquire possession of either money or instruments and are not acting in bad faith should obtain good title.<sup>114</sup> In the case of a particular type of instrument, one in bearer form, the similarity to money is even clearer.<sup>115</sup> The like treatment of instruments and money is not surprising. Notwithstanding the different legal characterizations,<sup>116</sup> commercial

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conversion to a third person then entitled to the immediate possession of the chattel.”); RAY ANDREWS BROWN & WALTER B. RAUSHENBUSH, *THE LAW OF PERSONAL PROPERTY* § 9.3 (3d ed. 1975).

112. See *Fed. Ins. Co. v. Banco de Ponce*, 751 F.2d 38, 41 (1st Cir. 1984) (negotiable instruments are subject to exceptions to classical conversion); *Burtch v. Hydraquip, Inc. (In re Mushroom Transp. Co.)*, 227 B.R. 244, 258 (Bankr. E.D. Pa. 1998) (cause of action for money had and received fails when the recipient is unaware the money was unlawfully procured) (quoting *Solomon v. Gibson*, 615 A.2d 367, 369 (Pa. Super. Ct. 1992)); *Hinkle v. Cornwell Quality Tool Co.*, 532 N.E.2d 772, 777 (Ohio Ct. App. 1987) (“a bona fide purchaser of a bank note, or a holder in due course, cannot be held liable for conversion”); *Story v. Palmer*, 284 S.W. 331, 332 (Tex. Civ. App. 1926) (money is not subject to conversion because title passes by delivery); U.C.C. § 3-306 (1999) (holder in due course takes an instrument free of claims of prior holders); BROWN & RAUSHENBUSH, *supra* note 111, at § 9.5. The most striking example of the commonality of treatment of money and instruments is the case of *Miller v. Race*, (1758) 97 Eng. Rep. 398 (K.B.), which is often cited as authority for the rule that a transferee of money takes good title regardless of defects in title of prior owners, notwithstanding the fact that this case did not involve money but rather a bank note. *Id.* at 398-99; see also James Steven Rogers, *The New Old Law of Electronic Money*, 58 SMU L. REV. 1253, 1256 (2005) (discussing *Miller*). These bank notes were not legal tender at the time and thus fit the modern definition of a negotiable instrument.

113. Compare U.C.C. § 9-330(d) (2007) (in the case of an instrument, the possessor must be a “purchaser” who “gives value and takes possession of the instrument in good faith”) with § 9-332(a) (in the case of money, the person need only be a “transferee” who has not acted “in collusion with the debtor”).

114. *Id.* §§ 9-330(d), 9-332(a). Compare the similarity of the rules in section 9-330(d) governing the rights of good faith purchasers of instruments, in which a security interest is perfected by filing, with the rights under section 9-332(a) of good faith transferees of money when a security interest in the money as “proceeds” has been perfected under section 9-315(c). Although there are some distinctions, the general treatment is the same. In the case of instruments, the purchaser must be unaware that the “purchase violates the rights of the secured party” but need not be unaware of the existence of the perfected security interest. *Id.* § 9-330(d) cmt. 7. A transferee of money, however, has an easier standard to meet: He need only not be “in collusion with the debtor in violating the rights of the third party.” *Id.* § 9-332(b); see *id.* § 9-332 cmt. 4. The difference between the rules for instruments and money is merely a difference in degree of the stringent nature of the test of a “good” as opposed to “bad actor.”

115. See *id.* § 1-201(20) (implying that anyone in possession of a negotiable instrument in bearer form can enforce it).

116. See U.C.C. § 9-102(a)(47) (2007); U.C.C. § 1-201(24) (1999). Money is technically a medium of exchange authorized or approved by a government, U.C.C. § 1-201(20) (1999), while instruments such as checks are orders to pay money to a named person or a designated recipient, U.C.C. § 9-102(a)(47) (2007).

participants generally treat money and checks (i.e., instruments) as equivalent alternatives within the payment system.<sup>117</sup>

Another payment alternative, generally accepted along with checks and money, is a credit card payment. Once the credit card is accepted as payment, the merchant is left with a “payment intangible” owed from the credit card issuer (albeit one that is collected through the sponsoring network and the merchant’s bank).<sup>118</sup> Participants in the economy generally view money, checks, and credit card use as “payment” or a medium of exchange.<sup>119</sup> The only reason that checks and credit card payments do not fall into the UCC’s definition of “money” is that they are not “authorized or adopted” by a government.<sup>120</sup> In other words, in normal commercial situations, participants in the payment system treat instruments, credit cards, and money as fungible or interchangeable.<sup>121</sup> Just as in the law of property, this similarity in function and essence supports a legal rule: Transfer to a good actor generally transfers good title. Similarly, in the law of secured transactions, these items of collateral are often treated as interchangeable and should be subject to the same perfection rules to the greatest extent possible.<sup>122</sup>

Instead, checks and receivables from credit card issuers are both eligible for perfection by filing,<sup>123</sup> but payment in cash is not. Different perfection rules as to these forms of payment create arbitrary results. For example, a retail department store that receives more of its customer payments in the form of checks and credit cards than in the form of cash is able to grant a perfected

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117. Only when a problem occurs in the system, such as when a check is dishonored due to insufficient funds, do participants become aware of the differences. On a day-to-day basis, when the system is functioning, the legal distinctions among these forms are undetectable.

118. See U.C.C. § 9-102(a)(61) (2007) (defining “payment intangible” as “a general intangible under which the account debtor’s princip[le] obligation is a monetary obligation”); 2 BARKLEY CLARK & BARBARA CLARK, *THE LAW OF BANK DEPOSITS, COLLECTIONS, AND CREDIT CARDS* ¶ 15.02 (2004).

119. For example, the Bankruptcy Code defines “cash collateral” as “cash, negotiable instruments, documents of title, securities, deposit accounts, or other cash equivalents,” which demonstrates the perception of money as analogous to these other forms. 11 U.S.C. § 363(a) (2000); see, e.g., BROWN & RAUSHENBUSH, *supra* note 111, at § 9.5 (referring to “money and . . . negotiable commercial paper such as promissory notes, bills of exchange and bank checks” as “the media in which payment is made”); cf. Sommer, *supra* note 12, at 18 (stating that “checks are different money than coins, although one employing the same unit of account,” and that “money is what a payment system does”).

120. U.C.C. § 1-201(20) (1999).

121. The legal distinctions among these items are apparent when a check is returned for insufficient funds or a credit card issuer becomes insolvent. Despite awareness of such theoretical possibilities, the payment systems function routinely without much conscious attention to them.

122. For example, it would not be possible to perfect a security interest in an intangible payment right, such as a credit card receivable, by possession, because there is no tangible object to possess.

123. See U.C.C. §§ 9-310 to -312 (2007).

security interest directly in those payment forms, without having to rely on proceeds tracing rules, when the secured party simply files a financing statement. In contrast, a Laundromat or videogame operator that receives virtually all of its customer payments in the form of money cannot grant a perfected security interest in these payments.<sup>124</sup> Basing a perfection rule merely on the distinction in the form of payment the debtor receives is arbitrary and unnecessary because these forms of payment are treated by most commercial actors as fungible.

One might object that the legal differences among these forms of payment justify different perfection rules that address differences between money and other forms of collateral. While the essence of money as a medium of exchange—and the related needs for certainty of ownership and finality of payment—may require special rules,<sup>125</sup> those rules need not affect the method of perfection. Only the priority of different interests should be affected. In fact, these rules already exist in relation to instruments,<sup>126</sup> funds in a bank account,<sup>127</sup> and even money itself<sup>128</sup> when it is in the form of proceeds of other collateral.<sup>129</sup>

In the case of instruments, the drafters of the 1999 revisions rightly recognized that to maintain negotiability, permissive filing should not frustrate the normal expectations of transferees of negotiable instruments. First, an Article 9 filing should not defeat the integrity of the Article 3 rules or the rights

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124. *See id.* §§ 9-312 to -313. In theory, the Laundromat owner could agree to deliver all cash received to the possession of the secured party each day or several times a day in order to grant a perfected security interest, or the owner could agree to place cash overnight at the close of business each day in a bank account subject to the secured party's control. Both of these solutions are exceedingly awkward to implement and leave the secured party unperfected for varying periods of time.

125. *See id.* § 9-332 cmt. 3.

126. *See id.* §§ 9-330(d) to -331.

127. *See id.* § 9-332(b).

128. *See id.* § 9-332(a). Although this rule already exists, it requires some technical amendment. A "transferee" of money is entitled to the benefit of this priority rule. There is no definition of "transferee" in Article 9 or Article 1. The drafters must have assumed a "transfer" of money involved the transfer of possession. Whereas Article 3 provides that a transfer of an instrument occurs "when it is delivered," there is no comparable definition of transfer of money. *Id.* § 3-203. One might interpret section 9-332 to mean that a transferee of money who did not take possession would take priority over a secured party in possession of the money in issue, which seems anomalous. This problem is dealt with adequately with respect to instruments because a purchaser desiring to defeat prior security interests in the instrument must take possession of the instrument. *See id.* § 9-330(d). Such a requirement should be added to section 9-332, as well.

129. If investment property is considered a form of payment, its treatment is consistent with instruments and deposit accounts in that a secured party relying solely on filing can have its interest defeated by a party taking possession, delivery, or control of the investment property. *See id.* § 9-328.

of holders in due course.<sup>130</sup> Furthermore, because instruments serve as a medium of exchange in commerce and negotiability of those instruments depends on transferees' ability to take good title, the permissive filing regime includes special rules protecting these reasonable expectations of market participants.<sup>131</sup> The goals underlying these priority rules for instruments are in harmony with the goals of smooth operation of the payment system and finality of completed payment transactions. It would be impractical for every person accepting an endorsed check to search the public filing records applicable to each prior holder of the check.<sup>132</sup> Therefore, once an instrument is transferred, there must be clear rules to determine the finality of that transfer.

These principles are equally applicable to transfers in money as a medium of exchange.<sup>133</sup> Thus, permitting filing for perfection of security interests in money need not disregard the special role of money as a medium of exchange. The same priority rules qualifying the effect of permissive filing for instruments could easily be applied to good faith transferees of money. In fact, no new rule needs to be written; UCC section 9-332(a) already includes such a rule.<sup>134</sup> Therefore, a permissive filing rule would allow a debtor who receives payments from clients in cash to use that cash in the same way as a debtor who receives payments in checks. The debtor could add it to his or her borrowing base by granting a security interest in those payments through filing but continue to use the money in its business.

Discrimination among different forms of payment accepted in the payment system and against businesses that accept cash rather than other forms of payment is an arbitrary rule. One may reach the same conclusion by stepping back one level in the payment system. Some businesses operate on a cash-only basis, while others will accept a promise or obligation to pay as an intermediate step. The promise or obligation to pay can take several forms: an instrument such as a promissory note, a payment intangible, an account, or chattel paper.

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130. See *id.* § 9-331(a).

131. See *id.* § 9-330(d) ("Except as otherwise provided in Section 9-331(a), a purchaser of an instrument has priority over a security interest in the instrument perfected by a method other than possession if the purchaser gives value and takes possession of the instrument in good faith and without knowledge that the purchase violates the rights of the secured party."); see also *id.* § 9-330 cmt. 7 ("a purchaser who takes even with knowledge of the security interest qualifies for priority under subsection (d) if it takes without knowledge that the purchase violates the rights of the holder of the security interest").

132. See PEB STUDY GROUP REPORT, *supra* note 71, at § 18.B ("Because instruments are normally transferred by delivery, those taking a delivery should not be required (on pain of subordination) to search the public records.").

133. See PEB STUDY GROUP REPORT, *supra* note 71, at § 15.F (discussing the rules of negotiability and finality relating to cash proceeds of collateral).

134. "A transferee of money takes the money free of a security interest unless the transferee acts in collusion with the debtor in violation of the rights of the secured party." U.C.C. § 9-332(a) (2007). This rule is necessary under current law since secured parties can obtain a nonpossessory security interest in money in the form of identifiable cash proceeds. See *id.* § 9-315(d); discussion *infra* Part IV.C.



Security interests in all of these may be perfected by filing.<sup>135</sup> Therefore, failing to permit perfection by filing treats cash-only businesses differently from businesses that accept other forms of payment prior to receiving payments in cash. No policy reason supports such a distinction.

As it happens, this analysis demonstrates the one way a secured party currently can perfect a security interest by filing with respect to money received from a debtor's customers. Prior to tendering the money, the customer can promise to pay that money so as to create an account or payment intangible. A secured party can then file a financing statement covering the account or payment intangible plus proceeds, leaving the secured party with a perfected security interest in the money as proceeds.<sup>136</sup> Again, there appears to be no rationale for distinguishing between these two processes of payment.

#### b. Deposit Accounts and Investment Property

Deposit accounts and investment property both represent forms in which monetary value can be stored and sometimes invested for gain. The definition of "investment property" broadly encompasses items ranging from stock certificates to shares in money-market accounts.<sup>137</sup> As a result, many types of investment property become almost indistinguishable from deposit accounts. For example, a short-term money market account with check-writing ability appears almost indistinguishable from a deposit account.<sup>138</sup> Furthermore, deposit accounts are not limited to accounts held with state or federally chartered banks, but instead may be held with any entity "engaged in the business of banking."<sup>139</sup> Deposit accounts and accounts constituting investment property can both be used for origination and receipt of payments within the payment system. Businesses routinely make and receive transfers of bank credits that are regulated by UCC Article 4A.<sup>140</sup> Corporate transactions also may use investment property, particularly cash equivalents such as treasury bonds, money market shares, or commercial paper, as a form of payment. Such transactions are regulated by Article 8 of the UCC.

Despite the similarity between deposit accounts and many forms of investment property, the perfection rules vary. A secured party may not perfect an interest in a deposit account by filing.<sup>141</sup> Yet the definition of "deposit account" excludes an account represented by an instrument, such as a

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135. See U.C.C. § 9-310 (2007); *id.* § 9-312.

136. See *id.* § 9-315.

137. See *id.* § 9-102(a)(49).

138. As some investment property may be indistinguishable from a deposit account in substance, courts have turned to using phrases like "investment" and "shares" to distinguish an account as investment property. See, e.g., *In re Quackenbush*, 339 B.R. 845, 854 (Bankr. S.D.N.Y. 2006).

139. U.C.C. § 9-102(a)(8) (2007).

140. U.C.C. art. 4A (2007).

141. *Id.* § 9-312(b)(1).

certificate of deposit, which can be perfected by filing.<sup>142</sup> On the other hand, the UCC permits filing as to all investment property.<sup>143</sup> Thus, when a business converts cash into a financial asset, its ability to grant a secured lender a perfected security interest by filing will be determined solely by whether the form of investment chosen is a certificate of deposit, uncertificated deposit account, or investment property.

As with instruments, the rules governing investment property recognize the need for alternative perfection methods in order to achieve other policy goals. In the case of certificated investment property, which is analogous to an instrument or a certificate of deposit, the rules provide for perfection by delivery with any necessary endorsement or registration.<sup>144</sup> In the case of a securities entitlement, which is analogous to a deposit account because it is a chose in action representing a right to underlying financial assets, the rules permit perfection by control.<sup>145</sup>

The perfection and priority rules for deposit accounts and securities entitlements are almost identical, with the exception that the rules permit filing for securities entitlements but not deposit accounts.<sup>146</sup> A party that perfects by control takes priority over a secured party that perfects by another method, such as filing in the case of investment property.<sup>147</sup> Absent agreement to the contrary, the institution that maintains the deposit account or securities entitlement takes priority over a party that perfected by either filing or control.<sup>148</sup> This hierarchy can be explained in terms of reliance. For example, a party who is relying on a specific piece of investment property and therefore goes to the trouble of obtaining a control agreement with the securities intermediary should take priority over a party relying on the general pool of securities entitlements without distinction. Similarly, a party relying on a particular instrument can obtain priority by taking possession of it, whereas a party relying on the general pool of instruments need only file.

The same rationale can be applied to deposit accounts. If a secured party makes a credit decision based on priority with respect to a particular account, such as a term deposit account as to which the debtor cannot make an early withdrawal of funds, the party should be able to maintain priority by taking control. On the other hand, a secured party not relying on a precise account but

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142. *Id.* § 9-102(a)(29).

143. *Id.* § 9-312(a).

144. *Id.* § 8-106(a) to (b); *id.* § 9-314.

145. *Id.* § 8-106(d) to (e); *id.* § 9-314.

146. Compare *id.* § 9-104 and *id.* § 9-327 with *id.* § 8-106(d) to (e) and *id.* § 9-328(1) to (3).

147. *Id.* § 9-328(1). In the case of a deposit account, there is no way to perfect other than control. Therefore, the effect of section 9-327(a) is unclear, aside from demonstrating that a perfected security interest takes priority over an unperfected security interest in a deposit account.

148. *Id.* § 9-327(3) to (4); *id.* § 9-328(3).

merely wanting to give the debtor credit in its borrowing base for the value held across all of its deposit accounts should be able to perfect by filing.

Further, filing would avoid a particular problem inherent in the method of perfecting by control. The current system does not provide assurances to a secured party who takes control that the security interest in a particular bank account will achieve the original goal of the secured party. A debtor can easily open additional deposit accounts, over which the secured party does not have control, and direct funds to those accounts, thereby diverting them from the intended security package. The secured party can require the debtor to agree contractually not to do so, but the damage will have been done by the time the debtor files a petition in bankruptcy. The secured party is left not with a security interest in the funds contained in the bank account but a contractual breach of contract claim against the now-bankrupt debtor. Filing would avoid this problem because the secured party could take a security interest in all of the debtor's existing and after-acquired deposit accounts.

An objection that filing would impede the functioning of the banking system and the finality of payment should be dismissed. When permitting perfection in a deposit account by control, the drafters of the UCC recognized the need for a special priority rule to preserve the functioning of the payment system.<sup>149</sup> Once payment is correctly made out of a deposit account, the transferee (as long as not acting in collusion with the debtor) is entitled to retain the funds free of any security interest that was in those funds while in the deposit account.<sup>150</sup> The same policy reasons exist with respect to perfection by filing, so these rules would serve the same function.<sup>151</sup>

### 3. The Argument for Consistency

Article 9's treatment of money is not only inconsistent with Article 1's definition of money,<sup>152</sup> which does not require a tangible form to exist, but it also treats money differently from other goods<sup>153</sup> with respect to which filing is sufficient to perfect.<sup>154</sup> The existing regime creates arbitrary distinctions within the payment system and treats monetary value differently solely based on the

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149. *See id.* § 9-332(b).

150. *Id.*

151. *See, e.g., id.* § 9-332 cmt. 3 ("Broad protection for transferees helps to ensure that security interests in deposit accounts do not impair the free flow of funds . . . . Rules concerning recovery of payments traditionally placed a high value on finality. The opportunity to upset a completed transaction, or even to place a completed transaction in jeopardy by bringing suit against the transferees of funds, should be severely limited. Although the giving of value usually is a prerequisite for receiving the ability to take free from third party claims, where payments are concerned the law is even more protective.")

152. U.C.C. § 1-201(20) (1999).

153. U.C.C. § 9-102(a)(44) (2007) (excluding money from the definition of "goods").

154. *Id.* § 9-310.

form in which it exists at a given time.<sup>155</sup> The rule also distinguishes unnecessarily between businesses that will accept promises of payment and those that require direct payment. When money is used like goods in a debtor's business, such as the inventory of a coin dealer, money changer, or check-cashing business, the perfection rule differs even though the currency is treated the same way as nonmonetary forms of inventory. The result is more costly secured or unsecured credit for the debtors whose inventory consists largely of cash.

Likewise, a debtor's customers can make payments either in the form of physical currency or in nonphysical form, such as payments directly to a bank account, by credit card, or by check. Even though debtors treat all received payments the same regardless of their form, Article 9 treats the various forms differently. Businesses that receive more payments in cash face a distinct cost disadvantage in obtaining credit when compared to businesses that receive customer funds in forms as to which security interests can be perfected by filing. Article 9 offers no justification for such a distinction in treatment.

One might object that money in physical form deserves such differing treatment due to its negotiability. The same argument could apply to negotiable instruments, though, but Article 9 accommodates their negotiability by allowing filing while providing that perfection by possession takes priority.<sup>156</sup> Thus, even though a secured party cannot be certain that its claim will not be defeated by a subsequent good-faith transferee, the secured creditor does retain its rights against the trustee in bankruptcy. The same rules could solve the problem of the negotiability of money.

Given the interchangeability of money, instruments, credit card payments, and bank deposits, no good justification for treating money differently can be found. Allowing perfection of a security interest in money by filing will preserve an approach consistent with the various interchangeable forms within the payment system and put debtors with large inventories of money in the same position as debtors with large inventories of other goods.

#### *B. Supporting the Policy Goals of the UCC: Notice Filing*

One of the stated goals of Article 9 is to promote simplicity and certainty in commercial transactions, a goal that is supported by encouragement of notice filing.<sup>157</sup> Part of this policy involves discouraging the existence of hidden or

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155. *See id.* § 9-312.

156. *See, e.g.*, §§ 9-330 to -331.

157. *See, e.g.*, *Chi. Dist. Council of Carpenters Pension Fund v. Tessio Constr. Corp.*, No. 02 C 4987, 2003 WL 21312664, at \*5 (N.D. Ill. June 4, 2003) ("More importantly, the certainty provided to businesses by the UCC enables commercial enterprises to analyze risk and make business decisions with a certain degree of predictability. The [c]ourt is not inclined to abandon this well-established system of relative reliability created by the UCC, simply because it might work a hardship . . ."); *Yamaha Motor Corp., U.S.A. v. Tri-City Motors & Sports, Inc.*, 429 N.W.2d 871, 878 (Mich. Ct. App. 1988) (stating "the underlying goal of Article 9" as "to

secret liens—property interests whose existence cannot be determined in a reasonable manner.<sup>158</sup> Yet the current version of Article 9 recognizes that filing may not always be a practical method of providing notice in the context of commercial payments.

The practical effect of the special priority rules for instruments is that a secured party who perfects by filing obtains a limited priority that in general is only valid against the trustee in bankruptcy.<sup>159</sup> This effect may be the prime benefit sought by the lending party.<sup>160</sup> Such division between the general unsecured creditor, the creditor with a limited priority based on filing, and the one who takes possession of instruments (or as proposed herein, takes possession of cash or control of deposit accounts) is logical.

Average creditors probably do not undertake a detailed examination of the cash possessed by the debtor or held in the debtor's bank accounts when evaluating the debtor's credit position. Rather, they likely assume that some or all of such monies are the proceeds of other collateral. In other words, trade creditors likely will not simply assume based on the fact of possession of cash in hand or in bank accounts that the funds are unencumbered and unsecured credit may safely be extended. Due to the very ease with which instruments can be negotiated or funds spent, the ability to create a nonpossessory lien in the instruments or cash is unlikely to be troubling to unsecured creditors.

Average unsecured creditors are unlikely to need to search the public records, as they are not relying on the presence of cash in making their credit decisions. For creditors who do wish to rely on cash or bank accounts being unencumbered in a particular instance, though, public filing exists. Finally, transferees taking possession of the instrument or cash would likely rely on possession as indication of ownership. The priority rules for instruments (and,

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provide a simple and unified structure within which the immense variety of present-day secured financing transactions can go forward with less cost and greater certainty," and that the UCC "accomplishes the goal, at least in part, by adopting the practice of 'notice filing'" (quoting Mich. Comp. Laws § 19.9101, § 440.9101)); see also *In re Midas Coin Co.*, 264 F. Supp. 193, 198 (E.D. Mo. 1967); Timothy G. Hayes, Note, *Secured Creditors Holding Lien Creditors Hostage: Have a Little Faith in Revised Article 9*, 81 IND. L.J. 733, 748 (2006).

158. See *Lindquist v. Dorholt (In re Dorholt, Inc.)*, 224 F.3d 871, 873 (8th Cir. 2000); *Clark v. Valley Fed. Sav. & Loan (In re Reliance Equities, Inc.)*, 966 F.2d 1338, 1341 (10th Cir. 1992); *Iowa Oil Co. v. Citgo Petroleum Corp. (In re Iowa Oil Co.)*, No. C04-1002-LRR, 2004 WL 2326377, at \*5 (N.D. Iowa Sept. 30, 2004); *Morris v. Intrust Bank, N.A. (In re Anderson)*, 351 B.R. 752, 756 (Bankr. D. Kan. 2006); *In re JII Liquidating, Inc.*, 344 B.R. 875, 886 (Bankr. N.D. Ill. 2006); *TWA, Inc. v. U.S. Dep't of Agric. (In re TWA Inc. Post Confirmation Estate)*, 312 B.R. 759, 762 (Bankr. D. Del. 2004); *Swope v. Wash. Mut. Home Loans, Inc. (In re Johnston)*, 333 B.R. 724, 733 (Bankr. W.D. Pa. 2005); *Escrow Connection v. Haas*, 235 Cal. Rptr. 200, 202 (Cal. Ct. App. 1987); *Union Fed. Sav. Bank v. INB Banking Co. Sw.*, 582 N.E.2d 426, 432 (Ind. Ct. App. 1991); *Bank Am. Commercial v. Okla. Natural Gas Co. (In re N-REN Corp.)*, 773 P.2d 1269, 1271-72 (Okla. 1989); *Trapp v. Jackels*, No. 49490-2-I, 2002 WL 31558027, at \*4 (Wash. Ct. App. Nov. 18, 2002).

159. See PEB STUDY GROUP REPORT, *supra* note 71, at § 18.A.

160. See *id.*

as proposed, for cash and deposit accounts) would thus reflect commercial reality. Potential transferees of funds, who actually rely on possession by a debtor, can continue to do so, but those who do not, such as the trustee in bankruptcy and general unsecured creditors, will be unharmed by the potential presence of a filed security interest covering the cash and deposit accounts.

The policy of encouraging notice raises a converse issue under the current section 9-312, which requires possession of money to perfect a security interest.<sup>161</sup> Because people generally equate possession of money with ownership, a perfection rule that undermines this principle creates misperceptions. Specifically, the existing perfection rule creates the possibility of misleading creditors of a secured party. If a secured party takes possession of money, there is no public record to put creditors on notice that the money in its possession is not its property.<sup>162</sup> Permissive filing, on the other hand, would provide adequate notice to the creditors of both the debtor and the secured party. The creditors of a debtor, if they wish to rely on the debtor's possession of cash, would need only check the public filings. Creditors of the secured party would not run the risk of mistakenly believing the cash to be the secured party's own money because the cash would physically remain with the debtor.<sup>163</sup>

Because the notion that possession indicates ownership is so fundamental to the nature of money, a more consistent rule would be to require public notice such as filing when possession would be misleading. Therefore, public filing by debtors should be required when their possession obscures the fact that some of their rights have been alienated to a secured party. This would be more clear and consistent than a rule that provides for a debtor's hidden ownership right in cash merely possessed by a secured party. This proposed rule would better provide notice to all parties because it would encourage a public record for nonpossessory interests in money.

Likewise, the current system provides no public notice of perfected security interests in deposit accounts. Creditors who want to obtain such information must first obtain the identity of the debtor's banks (another fact not a matter of public record) and then contact the individual banks to inquire as to the existence of a control agreement. Under Article 9, the deposit bank has no obligation to reply to such an inquiry from a party with whom it has no relationship.<sup>164</sup> In fact, responding to such an inquiry might violate obligations

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161. U.C.C. § 9-312 (2007).

162. See Bartell, *supra* note 71, at 309 ("A third party, even one with no knowledge of the debtor's interest, who extends credit to the creditor in reliance on his possession of debtor's money, can get no claim to the funds because, in this situation, ownership does not follow possession.").

163. Admittedly, this theoretical risk may be low in practice because it is unclear how many secured parties actually take possession of money.

164. Some commentators on the Subcommittee's proposals feared that if filing were not permitted, banks would become the gatekeepers of information about security interests created in deposit accounts, which would put an undue burden on banks. See, e.g., PEB STUDY GROUP

of privacy and confidentiality owed by the bank to its customer. Permitting filing of security interests in deposit accounts would promote the goal of public notice by taking this information out of private hands and making it a matter of public record.

*C. Simplifying the Problem of Proceeds*

The existing rules associated with identifiable cash proceeds can effectively provide a creditor with a perfected security interest in the money and deposit accounts constituting payments from the debtor's customers so long as the creditor has perfected an original security interest in the debtor's inventory.<sup>165</sup> One difficult issue that has plagued the drafting and practical application of Article 9, though, has been the problem of cash proceeds of collateral. A security interest in money can only be perfected by filing when that money represents "identifiable" cash proceeds of collateral.<sup>166</sup>

Thus, when a debtor enters bankruptcy or a secured party enforces a debt, litigation can arise over whether the money in the debtor's possession or deposit accounts belonging to the debtor constitutes identifiable cash proceeds. Such litigation would center on two main questions: (1) of what the money are proceeds, and (2) whether the specific money can be "identified" as these proceeds. Courts must determine whether particular amounts of money are proceeds and how to identify them as such.<sup>167</sup> These types of cases are factually intensive and are costly and time-consuming to litigate.

Further, as the case of *In re S. & J. Holding Corp.*<sup>168</sup> illustrates, the rule contained in section 9-315(d)(2) assists only a specific set of secured parties—those who lend to debtors that sell the collateral.<sup>169</sup> A secured party who lends to a debtor that charges for use of the collateral, or a secured party who lends to a debtor that provides only services, cannot obtain a perfected security interest in customers' payments without surrendering possession of money or control of all deposit accounts where funds might be held.<sup>170</sup> Even if collateral is sold for cash proceeds, the matter is not over; the proceeds must be "identifiable."<sup>171</sup>

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REPORT, *supra* note 71, at 411 (memorandum of Cecilia Absher and Richard Siegel of Davis Polk & Wardwell). Their concerns do not seem to have come to pass, simply because most people recognize the futility of attempting such an inquiry.

165. U.C.C. § 9-315 (2007).

166. *Id.*

167. *Id.*

168. 42 B.R. 249 (Bankr. S.D. Fla. 1984).

169. *Id.* at 250-51 (applying section 9-306 and holding that money received by the bankrupt from clients' use of video equipment did not constitute proceeds from the sale or disposition of the collateral but from use of the collateral and therefore the only way to perfect a security interest in the money was by possession).

170. See 2 BARKLEY CLARK & BARBARA CLARK, THE LAW OF SECURED TRANSACTIONS UNDER THE UNIFORM COMMERCIAL CODE ¶ 7.02 (2003).

171. U.C.C. § 9-315(d)(2) (2007).

Debtors who cannot assure a secured party that the payments they receive will fall into the definition of “identifiable” cash proceeds from the sale or disposition of collateral<sup>172</sup> are at a distinct disadvantage in obtaining secured credit.

The PEB Study Group recognized that due to these difficult issues, the benefits of revised section 9-315<sup>173</sup> are limited.<sup>174</sup> A secured party is better off classifying personal property as original collateral, rather than having to rely on tracing rules to show that the property constitutes proceeds of other collateral. Due to the amendments to Article 9, which allow a creditor to perfect an original security interest in bank deposits by control and in instruments by filing, the creditor can claim such an interest in after-acquired collateral in the form of customers’ payments to the debtor so long as the customers do not pay in cash and the debtor does not divert funds to a different bank account.<sup>175</sup>

The disparity in treatment for differing forms of payment is unjustified. The proposed rule change would improve efficiency by reducing the number of *ex post facto* disputes over money and bank accounts in the debtor’s possession. Secured parties could simply take an original security interest in all money and deposit accounts of the debtor *ex ante*, perfect the interest by filing, and avoid costly litigation over characterization and identification of the money as proceeds.<sup>176</sup> Admittedly, not all disputes over tracing proceeds would be eliminated. For example, a secured party with a first-priority security interest in a piece of equipment would want to trace cash proceeds upon disposition thereof to maintain priority over another secured party with a perfected security interest in money of the debtor. Still, the changes would eliminate at least some disputes between secured and unsecured parties.

#### *D. Better Monitoring of the Use of Cash in Bankruptcy*

The significant benefit that a debtor receives by allowing perfection by filing for money is that the debtor would be entitled to use the money in its business instead of surrendering possession to the secured party. This benefit would come with a corresponding restriction following a petition in bankruptcy. Where operation of the business of the debtor has been authorized in a case filed under Chapter 7, 11, 12, or 13 of the Bankruptcy Code, the trustee (or debtor-in-possession) is generally free to use the estate’s assets in the

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172. *Id.* § 9-315.

173. This was formerly section 9-306.

174. See PEB STUDY GROUP REPORT, *supra* note 71, at § 15.A cmt. 1(d) (“When compared with the use of expansive coverage of after-acquired collateral in security agreements and financing statements, the benefits to secured parties of classifying collateral as proceeds are relatively small.”).

175. U.C.C. § 9-312 (2007).

176. See PEB STUDY GROUP REPORT, *supra* note 71, at § 15.A cmt. 1(d) (Dec. 1, 1992) (identifying this practical benefit as flowing from the changes made with respect to instruments and deposit accounts).



ordinary course of business.<sup>177</sup> One of the most significant exceptions is that without the applicable secured party's consent or a court determination, the debtor may not use cash collateral.<sup>178</sup>

Under current law, a single party likely will not have a security interest in all cash and bank accounts of a debtor. There are more likely to be a number of parties with multiple and potentially conflicting interests in portions of the debtor's cash. If a secured party could obtain a perfected security interest in all cash and deposit accounts of a debtor, that party could monitor the trustee's or debtor-in-possession's proposed use of the money and bank account funds, which would be consumed in use, regardless of whether such use were in the ordinary course of business or otherwise. All creditors could gain an advantage from such a situation because it would produce a single party with the ability and incentive to monitor the trustee's or debtor-in-possession's use of the cash from a creditor's perspective and with the standing to require the court's approval of the proposed uses.<sup>179</sup> For those debtors whose bankruptcy is primarily attributable to poor management, such oversight has the potential of improving returns for all creditors, including unsecured creditors.<sup>180</sup> Admittedly, it may be difficult to prove that this benefit would arise in all or even most bankruptcies, but it appears plausible in at least some cases.

#### V. ANSWERING OBJECTIONS

Keeping in mind the benefits discussed above, including consistency, notice, elimination of discriminatory treatment, cheaper credit, and reduced litigation, the following section will address some potential objections to the proposed rule change.

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177. 11 U.S.C. § 363(c)(1) (2000) (“[U]nless the court orders otherwise, the trustee may enter into transactions, including the sale or lease of property of the estate, in the ordinary course of business, without notice or a hearing, and may use property of the estate in the ordinary course of business without notice or a hearing.”).

178. *Id.* § 363(c)(2) (“The trustee may not use, sell, or lease cash collateral under paragraph (1) of this subsection unless—(A) each entity that has an interest in such cash collateral consents; or (B) the court, after notice and a hearing, authorizes such use, sale, or lease in accordance with the provisions of this section.”).

179. Admittedly, though § 363(c)(2) would afford an opportunity for all secured parties with an interest in the cash collateral to participate, there would be at least one party involved with an interest in the overall cash pool. In certain cases, creditors with only a limited interest might rely on the monitoring by the secured creditor with the overall interest. Unlike a creditor with an interest in only part of a debtor's cash, a holder of a security interest in the overall pool would not have the incentive to favor use of some cash over other cash.

180. See Rizwaan Jameel Mokal, *The Floating Charge—An Elegy* 6-14 (bepress Legal Series, Working Paper No. 1380, 2006), available at <http://law.bepress.com/expresso/eps/1380>.

*A. Filing Would Not Benefit Unsecured Creditors*

One might object that the position of unsecured creditors has been passed over too quickly in the preceding analysis. It could be argued that the current perfection rules for money and deposit accounts help preserve some assets unencumbered for the unsecured creditors. One side effect of the current rule is that the practical difficulties associated with perfecting a security interest in money used in the debtor's business and with obtaining control over all deposit accounts effectively cause portions of working capital to be reserved for distribution to the unsecured creditors.

First, assuming for the moment the desirability of reserving some assets for distribution to unsecured creditors, the perfection rules are an inefficient way to achieve this. Such a goal is better suited to the Bankruptcy Code. Further, the current rule does not always have this effect because cash and deposit accounts may constitute identifiable cash proceeds of collateral. If the original security interest in the cash-producing collateral was properly perfected and the cash proceeds can be traced to that collateral, the cash or deposit account will be reserved for the appropriate secured party<sup>181</sup> to the exclusion of unsecured parties.

In addition, the current rule discriminates between creditors of businesses that require large pools of cash and those that do not. It benefits the unsecured creditors of the former but not the latter. There is no reason why only an unsecured creditor lending to the former type of debtor should be entitled to a pool of unsecured assets. If some amount of the assets of a bankrupt debtor should be reserved for unsecured creditors as a policy matter, it should be done directly and for the benefit of all unsecured creditors.<sup>182</sup>

*B. Filing Would Benefit Only Certain Debtors*

A potential objection to the proposed changes is that they would only benefit specific classes of debtors: those who use money as inventory and service businesses that do not sell inventory. These debtors represent a respectable portion of all secured credit, though, so the rules ought to accommodate them. In addition, such accommodation has precedent; other changes in the UCC have been implemented that affect only a specific class of debtors. For example, the change to the perfection rule for instruments only affects those that deal in a large volume of instruments.<sup>183</sup> Because the costs of the rule changes would be small, there is no sensible rationale for discriminating against debtors that would benefit from the changes.

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181. See U.C.C. § 9-315(d)(2) (2007).

182. In the United Kingdom, for example, current insolvency law reserves a prescribed part of a company's net property which is subject to floating charges (after paying off fixed charge holders) for the benefit of all unsecured creditors. See Enterprise Act, 2002, c. 40, § 252 (Eng.). Efficiency and fairness might justify such a rule but are a subject for another article.

183. See U.C.C. § 9-312 cmt. 2 (2007).

*C. Money Is Unique*

Because money and its ability to move freely from hand to hand are such important parts of our economic system, one may argue that perfection should occur by more rigorous means than mere filing. Economic actors may also complain that they should not bear the transaction costs of checking public records. Nevertheless, allowing perfection by filing need not violate the policy goals of free transferability and finality of payment since they can be preserved by a priority rule such as that contained in section 9-332. This change is admittedly of limited benefit to secured parties, effectively only giving them priority over the trustee in bankruptcy, and would entail some minor transaction costs. The benefits to at least some debtors, though—as described above—are substantial.

*D. Possession Nearly Always Equates to Ownership*

Possession of money nearly always represents ownership of money.<sup>184</sup> One might argue that permissive filing would undermine this legal principal by creating situations in which parties could have an interest in money without possessing it. On the contrary, the current rule requiring possession actually undermines this principle even more because a secured party takes possession without taking ownership.<sup>185</sup> In fact, the existing system violates the principle without providing any means of notifying third parties of the violation.<sup>186</sup> Filing would provide notice of the limitation on the debtor's ownership of its cash.

*E. Money is a Different Medium of Exchange*

The unique nature of money as a medium of exchange might also cause reluctance to subsume it in the filing regime. Instruments such as checks function in that role in our modern economy, though, and in fact are often viewed as interchangeable with cash. These instruments' effectiveness as a medium of exchange has not been reduced by the ease with which secured parties can take a perfected security interest in them.<sup>187</sup> Permitting filing with respect to some media of exchange but not others is arbitrary.

*F. Money is Fungible and Easily Commingled*

As cases concerning cash proceeds demonstrate, money is a fungible item that can be commingled with other money. Thus, one might argue that it will be difficult to identify the specific money in which a secured party has taken a

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184. See Bartell, *supra* note 71, at 305.

185. See § 9-312(b)(3).

186. See *id.*

187. *Id.* § 9-312(a).

security interest, which will lead to litigation. In fact, this situation is unlikely to arise because that very characteristic will make a secured party reluctant to take a security interest in only specified money of the debtor. More likely, a secured party will wish to perfect a security interest in all money of the debtor. In the rare instances where a secured party and debtor might wish to limit the security interest to specific money,<sup>188</sup> physical currency is actually easier to distinguish than other commodities because cash and deposit accounts have unique serial numbers or other identifying marks.<sup>189</sup>

In addition, the law has a long history of developed rules to deal with commingled tangible property that is fungible. In general, all those with a property interest in commingled items have a pro rata ownership interest in the mass of items.<sup>190</sup> Article 9 has its own version of this general principal, which states that a security interest can attach and be perfected in goods that are commingled with other goods.<sup>191</sup> If the security interest is perfected before the goods are commingled, it takes priority over a security interest that is perfected after commingling.<sup>192</sup> If more than one perfected security interest exists prior to commingling, the secured parties hold their interests pro rata.<sup>193</sup> If parties can cope with perfecting by filing when their security interests are in such fungible goods as grain, oil, and gas, which bear no individual serial marks, they should be able to cope with perfection by filing with respect to money.

## VI. THE DUAL NATURE OF SECURED LENDERS

The preceding discussion has treated all secured lenders as essentially the same. In fact, there are two types of secured creditors, accommodated under English law by the devices of fixed and floating charges. Article 9 does not explicitly create this distinction, although some of its provisions bear

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188. One example would be a coin dealer wishing to pledge particular coins in his inventory.

189. See, e.g., *Langella v. United States*, No. 95-2322, 1995 WL 732755, at \*2 (2d Cir. Dec. 8, 1995); *United States v. Simon*, No. 94-10372, 1995 WL 306829, at \*1 n.1 (9th Cir. May 18, 1995); *United States v. Ritchie*, 35 F.3d 1477, 1479 (10th Cir. 1994).

190. See, e.g., *Basin Elec. Power Coop. v. ANR W. Coal Dev. Co.*, 105 F.3d 417, 423 (8th Cir. 1997); *Arnold v. Producers' Fruit Co.*, 61 P. 283, 285 (Cal. 1900); U.C.C. § 7-207(b) (2007) ("If . . . fungible goods are commingled, the goods are owned in common by the persons entitled thereto and the warehouse is severally liable to each owner for the owner's share. If, because of overissue, a mass of fungible goods is insufficient to meet all the receipts the warehouse has issued against it, the persons entitled include all holders [of] overissued receipts . . ."); see also *id.* § 8-503(b) ("An entitlement holder's property interest with respect to a particular financial asset under subsection (a) is a pro rata property interest in all interests in that financial asset held by the securities intermediary, without regard to the time the entitlement holder acquired the security entitlement or the time the securities intermediary acquired the interest in that financial asset.").

191. *Id.* § 9-336.

192. *Id.* § 9-336(f)(1).

193. *Id.* § 9-336(f)(2).

similarities to these English forms. A change in the perfection rule for security interests in money, based more solidly on the English system, would be a positive step toward creating a scheme that fully recognizes and accommodates both types of secured lenders.

#### *A. Fixed and Floating Charges Under English Law*

Under English law, a fixed charge is a security interest over specifically and unambiguously identified assets in which the secured party has created a direct property interest. The debtor has limited control over the secured assets and generally may not dispose of them without the secured party's consent.<sup>194</sup> In contrast, a floating charge generally meets three criteria: (1) the security is over a class of present and future assets, rather than a specifically identified asset, (2) the assets generally are revolving (i.e., changing or circulating), and (3) prior to a specific event, such as a declaration of default, the debtor may deal with and dispose of the assets in the class without the secured party's consent.<sup>195</sup> Although there are exceptions, fixed charges are generally taken over individual assets such as real property, fixtures, and equipment,<sup>196</sup> whereas floating charges are generally taken over pools of assets such as receivables, inventory, and raw materials.<sup>197</sup> In fact, a floating charge usually includes the pool of assets comprising the debtor's entire business.<sup>198</sup>

The distinction between fixed and floating charges leads to differing results in priority, control, and remedies. Fixed charge holders obtain a higher priority than floating charge holders or even statutorily preferred creditors. Floating charge holders, on the other hand, rank behind both fixed charge holders—even those subsequently granted—and statutorily preferred creditors.<sup>199</sup> As to control, a debtor attempting to establish a fixed charge must surrender a certain

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194. *Agnew v. Comm'r of Inland Revenue*, [2001] UKPC 28, [26] [2001] 3 W.L.R. 454 (appeal taken from C.A.N.Z.); PALMERS COMPANY LAW FROM SWEET AND MAXWELL § 13.109 (2006); Stephen Atherton & Rizwaan Jameel Mokal, *Charges over Chattels—Issues in the Fixed/Floating Jurisprudence* 3-4 (bepress Legal Series, Working Paper No. 1380, 2006), available at <http://law.bepress.com/expresso/eps/1371>.

195. *Nat'l Westminster Bank plc v. Spectrum Plus Ltd.*, [2005] UKHL 41, [96], [101]; *In re Cosslet (Contractors) Ltd.*, [1998] Ch. 495, 510 (C.A.) (floating charge is "on a fluctuating body of assets which remain under the management and control of the chargor"); *In re Yorkshire Woolcombers Ass'n, Ltd.*, [1903] 2 Ch. 284, 295 (C.A.).

196. PALMERS COMPANY LAW, *supra* note 194, at § 13.109.

197. VANESSA FINCH, *CORPORATE INSOLVENCY LAW: PERSPECTIVES AND PRINCIPLES* 80 (2002).

198. *Id.*

199. Enterprise Act, 2002, c. 40 § 252 (Eng.); Insolvency Act, 1986, c. 45 § 176 (Eng.); Mokal, *supra* note 182, at 2. In fact, as to priority, a portion of the funds recovered from the assets subject to the floating charge are reserved for payments to unsecured creditors. See Enterprise Act § 252. As discussed above, such an approach may make more sense under the UCC than the theory that unsecured creditors should be able to share in cash, which the debtor is effectively unable to charge under the current version of Article 9.

amount of control over the asset and its disposition, but a debtor granting a floating charge is free to deal with the assets in the pool. Therefore, if a debtor disposes of an asset subject to a fixed charge, the secured party's property right in the charged asset automatically continues in the substituted asset.<sup>200</sup> In the case of a floating charge, assets leaving the pool are transferred free of a security interest as the debtor remains free to dispose of particular assets. Proceeds of a floating charge are not traced; instead, as new assets enter the relevant pools (either inventory or receivables), they are subject to the charge as original collateral without any need to trace their source.

Finally, a holder of a fixed charge can exercise a more direct self-help remedy, such as appointing a receiver to sell the particular asset for cash, while a floating charge holder can appoint an administrator to conduct an insolvency proceeding and liquidate or reorganize the debtor's business.<sup>201</sup> Because a floating charge allows a creditor to create security over all the debtor's assets, the creditor also can invest in the entirety of the debtor's business as a going concern.<sup>202</sup> Rather than disposing of specific assets to satisfy the secured party's claim, the creditor can sell them as a going concern.<sup>203</sup>

A secured party can take either type of charge in money and deposit accounts, but obtaining a fixed charge is practically more difficult. The secured party must deprive the debtor of most control over the money, which most likely means taking possession. In *National Westminster Bank plc v. Spectrum Plus Ltd.*, the House of Lords established that secured parties must exercise significant restrictions over a debtor's use of a deposit account in order to create a fixed charge therein.<sup>204</sup> This is similar to the current Article 9 regime, requiring possession of money and control of deposit accounts. Unlike Article 9, though, English law allows a secured party to take a floating charge over the revolving pool of money and deposit accounts held by a debtor without having to take possession or control of them.<sup>205</sup>

The difference between fixed and floating charges comes from the difference between two types of lenders. In the former, a lender is investing in

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200. See, e.g., *Foskett v. McKeown*, [2001] 1 A.C. 102, 127 (H.L.).

201. See generally Caroline McDermott, *Overview of the Effects of the New Administration Procedure*, FIN. & CREDIT L. 6.5(1) (2004) (discussing the administration procedures introduced by the Enterprise Act).

202. FINCH, *supra* note 197, at 80.

203. Mokal, *supra* note 180, at 10 (noting the potential synergistic benefits of "mopping up" all assets into a single unit that could be sold or transferred as a unit to new management).

204. [2005] UKHL 41, [54]-[61]. Although *Spectrum* primarily involved the issue of whether the secured creditor had created a fixed charge over book debts (known in America as receivables), the Lords considered whether a fixed charge had been created over the bank account into which the receivables were paid. Lord Hope of Craighead discussed the level of control needed over the bank accounts to create a fixed charge, stating, "[t]he uncollected book debts were to be held exclusively for the benefit of the bank. But everything then depended on the nature of the account with the bank into which the proceeds were to [be] paid under the arrangement described in clause 5 of the debenture." *Id.* at [55].

205. See FINCH, *supra* note 197, at 80.

and basing its credit decision on a debtor's specific assets and wishes to exercise priority claims, control, and monitoring rights over those specific assets. This type of lender will be referred to as an "asset lender." Although an asset lender will certainly have some concern with the overall health of the debtor's business, the primary economic interest of an asset lender is in the continuing value of the specific collateral relative to the amount of credit extended.

The holder of a floating charge over all assets of the debtor can be understood as investing in the business of the debtor. This type of lender will be referred to as a "debt investor." Although the liquidation value of particular assets is likely to be considered, the debt investor primarily bases credit decisions on the present and potential collective value of the pool of assets comprising the business as a going concern. In this sense, a potential debt investor is similar to an equity investor, who may consider the enterprise's valuable assets but whose primary interest is the actual and potential value of the whole enterprise.

#### *B. Asset Lenders and Debt Investors Under Article 9*

Article 9 provides rules for both asset lenders and debt investors. Article 9 clearly was drafted to accommodate asset lenders who can obtain a security interest in a specific asset so long as the asset is adequately described in the security agreement.<sup>206</sup> If the collateral consists of "tangible negotiable documents, goods, instruments, money, . . . tangible chattel paper[, or] . . . certificated securities," the secured party can enhance its control over the specific asset by perfecting its security interest through possession.<sup>207</sup> Taking possession of specific types of collateral will also enhance an asset lender's priority position.<sup>208</sup> Article 9 even contains a special priority-enhancing rule benefiting a specific type of asset lender, the purchase-money lender.<sup>209</sup>

As to a debt investor, Article 9 is less straightforward. The Article could have been drafted to provide for a security interest much like a floating charge over all assets of a debtor. The drafters did take at least one step in that direction; a financing statement is effective under the UCC as to description of collateral if it refers to "all assets or all personal property" of the debtor.<sup>210</sup> Problematically, a security agreement is not similarly effective if it contains either such a statement or a similarly generic all-encompassing form.<sup>211</sup> This

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206. U.C.C. § 9-203(b)(3)(A) (2007); *id.* § 9-108 (requiring that a description "reasonably identify" the target property).

207. *Id.* § 9-313(a).

208. *See id.* § 9-330; *see also id.* § 9-328 (granting priority to parties with control over the investment property); § 9-329 (providing priority to secured parties with control of letter-of-credit rights).

209. *Id.* § 9-324.

210. *Id.* § 9-504(2).

211. *See id.* § 9-108(c).

rule regarding security agreements undermines the liberality of Article 9's other provisions and hampers debt investors' ability to create the necessary security interests.

Even more important to debt investors are the exclusions from Article 9's scope. These exclusions are both explicit<sup>212</sup> and indirect through the technical requirements for attachment and perfection. Although the trend in Article 9's development has been to increase its scope with respect to types of property, the following items are still explicitly outside its application: (1) collateral as to which security interests are regulated by another state's, federal, or foreign law,<sup>213</sup> (2) most insurance policies,<sup>214</sup> (3) most judgments,<sup>215</sup> (4) noncommercial tort claims,<sup>216</sup> (5) real property,<sup>217</sup> and (6) consumer deposit accounts.<sup>218</sup>

Some of these categories are not completely problematic. For instance, if another law, such as a certificate-of-title statute, provides a feasible method for achieving the appropriate security interest, the secured party should be able to reach a desirable result. Compliance with both systems may burden the debt investor with some additional transaction costs, but they should be manageable, particularly for repeat parties in the market. Such piecing together of liens on both real and personal property already occurs under American real estate law and Article 9.<sup>219</sup>

Still, a subset of property remains excluded from the security package of a debt investor. This could lead to one of two conclusions: (1) these items should be included in the scope of Article 9 or (2) the policy reasons for their exclusion outweigh their typical contribution to the value of the going concern. A detailed discussion of this argument with respect to all of these categories is beyond the scope of this article, but it seems reasonable to conclude preliminarily that the remaining assets do not appear to be necessary to most business enterprises.<sup>220</sup>

The types of collateral that are indirectly excluded from the scope of Article 9, including money and deposit accounts, also affect debt investors. Although technically within Article 9's scope, the requirement of possession to perfect effectively excludes money from the security package of most secured parties. A debtor's need to retain possession of money indicates that money is a

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212. *Id.* § 9-109(c) to (d).

213. *Id.* § 9-109(c).

214. *Id.* § 9-109(d)(8).

215. *Id.* § 9-109(d)(9).

216. *Id.* § 9-109(d)(12).

217. *Id.* § 9-109(d)(11).

218. *Id.* § 9-109(d)(13). Although there are other provisions to this section, they relate to the exclusion of transactions rather than types of collateral.

219. *See id.* § 9-604 (providing that a single security agreement can provide for security interests in real and personal property and for coordination of enforcement against both).

220. The one exception may be insurance proceeds, but these are only necessary to businesses that have actually suffered an insurable loss, which is not likely to include most debtors.



necessary part of the going concern of the business. In other words, the money is essential to the continued operation of the business. Though the debt investor may obtain control of as many bank accounts as the debtor will allow, the investor's security is only as good as the debtor's commitment not to open new bank accounts and transfer controlled funds into them. Thus, an asset lender structuring a specific transaction that involves a blocked or specific account may be able to rely on the perfected security interest in that controlled account, but a debt investor cannot be similarly certain that all funds held in the debtor's bank accounts are a valid part of the debtor's borrowing base. The debt investor who wants to invest in a going concern, which means creating a security package that would allow a transfer of all assets to a new owner or manager, is hindered by this effective exclusion.<sup>221</sup>

Because Article 9 effectively excludes money from a debtor's borrowing base, a debt investor cannot make a priority investment in all the debtor's assets. More importantly, a debt investor cannot make a priority investment in the money used in the business or held in bank accounts since money is essential for a business to continue as a going concern. Thus, excluding money from Article 9 undermines the debt investor's ability to base its investment price on all assets of a business.

### *C. Benefits of Accommodating Debt Investors*

The argument for accommodating debt investors in Article 9 assumes that facilitating this type of lender is desirable. There appear to be several benefits to such a view. First, as with the floating charge in England, a creditor with a security interest in all assets of the debtor assumes the role of a main creditor,<sup>222</sup> whose monitoring takes in the whole business of a debtor rather than focusing on individual assets.<sup>223</sup> A single creditor with this global interest may prove to be an efficient monitoring participant, which can benefit all creditors and other equity investors. Asset lenders, smaller unsecured creditors, and equity owners (where such ownership exists and is widely dispersed) do not have the

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221. Another example would be commercial tort claims. The need to specifically describe them and the inability to *ex ante* create security interests in after-acquired commercial tort claims restricts secured parties' access to this collateral class. See *id.* § 9-108(e)(1). Again, a detailed consideration of this rule is outside the scope of this article, but it can be noted that, as with judgments and insurance proceeds, commercial tort claims are not typically part of the operational assets of most businesses. Therefore, unlike money, they are of less universal concern to debt investors. Although such assets would be of concern to an individual debt investor in a particular debtor whose business depends on such assets, such a debtor is difficult to imagine.

222. If a debtor has granted a security package over all assets, it is unlikely that there will be a second creditor in such a position. If a second creditor has been granted a second ranking lien on the whole business, it is likely such a creditor will leave monitoring to the first ranking creditor.

223. See Mokal, *supra* note 180, at 6-14.

economic incentive to conduct such monitoring of a business or its management. On the other hand, repeat debt investors, such as banks, have created large resources to receive and analyze detailed information on debtors.

Further, having security over the entire business creates a different incentive than asset lending when it comes to evaluating defaults and remedies against specific collateral. Asset lenders will seek recovery against specific assets, even if this has the unintended result of harming assets not subject to their security. However, assuming that the single asset is not sufficient to satisfy the entire claim, debt investors must consider how seeking recovery against a specific asset will affect the remaining collateral pool. It may, therefore, be efficient for all other investors in an enterprise (unsecured lenders, trade creditors, asset lenders, and equity investors) to have a main creditor with the incentive, through an all-encompassing security package, to monitor and influence the whole business.<sup>224</sup>

This is not to say that asset lenders are either inefficient or valueless economic participants and should not also be accommodated in Article 9. Article 9 should make accommodations for both types of lenders. The change to the perfection rules for money and deposit accounts would not solve the problem of debt investors completely. Nevertheless, it would be a major step toward facilitating the all-encompassing coverage of a security device like the floating charge while preserving the current status of devices like the fixed charge.<sup>225</sup>

## VII. CONCLUSION

Money is a type of personal property that is difficult to categorize. People's understanding of money today has been influenced by its history as goods of intrinsic value, its later change to a writing representing a right to payment, and its current fiat status as only a government-defined concept. Therefore, one may best evaluate Article 9's treatment of money by considering it in light of the UCC's treatment of analogous property types, specifically goods, instruments, and bank accounts.

The history of money does not reveal a rational justification for providing a different perfection rule for money and deposit accounts than for goods, instruments, payment intangibles, and investment property. This article has enumerated significant advantages to permitting permissive filing for money and deposit accounts. Permissive filing establishes consistency with goods, as well as with all forms of value in the payment system. Debtors that use money as their stock in trade, that require large amounts of money to settle

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224. *See id.*

225. As discussed *supra*, this change would not preclude reserving some assets for the benefit of unsecured creditors. This could be achieved in the Bankruptcy Code. If such a policy is seen as desirable, this could be done by reserving a specific percentage of all assets rather than just money remaining in the possession of a debtor at the time of insolvency. *See* Mokal, *supra* note 180, at 11-12.

transactions, or that primarily provide services would benefit. They would finally be able to engage in credit transactions on an equal footing with those debtors who sell goods and who receive payment in forms other than cash. Permitting filing is consistent with the UCC's goal of encouraging notice of nonpossessory interests in property; it also would correct the current situation that creates undisclosed interests in money when security interests in money are perfected by possession.

Against this background of benefits, the above discussion also addressed a series of possible objections. Most may be resolved by acknowledging the need to retain the priority given to transferees of money and recipients of payments from deposit accounts. Secured parties who perfect by possession and transferees should take priority over secured parties who perfect by filing. Secured parties with control of deposit accounts, including the depository bank, should also take priority over secured parties who merely file.

Finally, the difference between asset lenders and debt investors must be accommodated. English law facilitates this through the differences between a fixed and a floating charge. The changes proposed in the preceding discussion would allow the option of a "fixed charge" over specific money or deposit accounts, which would be perfected by possession or control, or a "floating charge" over pools of these assets that would be perfected by filing. As in England, perfection by filing would provide a weaker priority position, effectively only over the trustee in bankruptcy. Lenders relying on filing would also lose priority to certain third-party transferees. The proposed changes to the perfection rule for money and deposit accounts would increase the borrowing base for debt investor transactions and lower the cost of secured credit for some debtors. A rule permitting perfection by filing when creating a security interest in money would significantly improve the position of both creditors and debtors in the market.