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# Socrates, Syllogisms, and Sadistic Transactions: Challenges to Mastering U.C.C. Article 9 Through Deductive Reasoning

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# Socrates, Syllogisms, and Sadistic Transactions: Challenges to Mastering U.C.C. Article 9 Through Deductive Reasoning

Timothy R. Zinnecker\*

It is tragic that our law schools do not have an orientation course in logic. We had that great line from Professor Kingsfield in *The Paper Chase*: “You come in here with a head full of mush and you leave thinking like a lawyer.” The Socratic method is the most valuable tool to train students to think like a lawyer. Yet the students—and unfortunately too many of their professors—apparently do not know the elements of deductive and inductive reasoning.

– Hon. Ruggero J. Aldisert<sup>1</sup>

## INTRODUCTION<sup>2</sup>

In 2007, an essay entitled “*Logic for Law Students: How to Think Like a Lawyer*” appeared in the *University of Pittsburgh Law Review*.<sup>3</sup> The essay, co-authored by federal appellate judge Ruggero J. Aldisert and two of his law clerks, opens with this statement: “Logic is the lifeblood of American law.”<sup>4</sup> Prompted by Professor Kingsfield’s famous line above,<sup>5</sup> the co-authors then

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<sup>1</sup> See Howard J. Bashman, *20 Questions for Senior Circuit Judge Ruggero J. Aldisert of the U.S. Court of Appeals for the Third Circuit*, [http://howappealing.law.com/20q/2003\\_07\\_01\\_20q-appellate-blog\\_archive.html](http://howappealing.law.com/20q/2003_07_01_20q-appellate-blog_archive.html) (last visited Oct. 24, 2009).

<sup>2</sup> Much of the text and many of the accompanying footnotes in the Introduction and Part I of this article will also appear in the companion article referenced *infra* at note 15 and accompanying text.

<sup>3</sup> Ruggero J. Aldisert et al., *Logic for Law Students: How to Think Like a Lawyer*, 69 U. PITT. L. REV. 1 (2007).

<sup>4</sup> Aldisert, *supra* note 3, at 1. Not every federal appellate judge concurs. See Richard A. Posner, *The Jurisprudence of Skepticism*, 86 MICH. L. REV. 827, 833–34 (1988) (suggesting that “the life of the law really cannot be logic”). Cf. O. W. HOLMES, JR., *THE COMMON LAW* 1 (1881) (“The life of the law has not been logic; it has been experience.”).

<sup>5</sup> The oft-quoted line is from the following soliloquy delivered by Professor Charles Kingsfield to his first-year contracts class at Harvard Law School:

The study of law is something new and unfamiliar to most of you—unlike any schooling you have ever been through before. We use the Socratic method here: I call on you, ask you a question, and you answer it. Why don’t I just give you a lecture? Because through my questions you learn to teach yourselves.

ask, "What is thinking like a lawyer?" They offer this response: "It means employing logic to construct arguments."<sup>6</sup> The authors contend that "our law schools do not give students an orientation in the principles of logic,"<sup>7</sup> which, in their opinion, "does violence to the essence of the law."<sup>8</sup> They then express the essay's purpose:

[W]e endeavor to explain, in broad strokes, the core principles of logic and how they apply in the law school classroom. Our modest claim is that a person familiar with the basics of logical thinking is more likely to argue effectively than one who is not. We believe that students who master the logical tenets laid out in the following pages will be better lawyers and feel more comfortable when they find themselves caught in the spotlight of a law professor on a Socratic binge.<sup>9</sup>

The authors then expound on these "core principles of logic," discussing for several pages both deductive reasoning through syllogisms<sup>10</sup> and inductive reasoning by analogy.<sup>11</sup>

I teach Secured Transactions<sup>12</sup> once (and sometimes two or three times) each year. The course introduces students to many of the legal rules that govern transactions in which personal property (rather than real estate) secures payment of a financial obligation. Particular attention is given to U.C.C. Article 9<sup>13</sup> and selected provisions of the United States Bankruptcy Code.<sup>14</sup>

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Through this method of questioning, answering, questioning, answering, we seek to develop in you the ability to analyze that vast complex of facts that constitute the relationships of members within a given society. Questioning and answering. At times, you may feel that you have found the correct answer. I assure you that this is a total delusion on your part. You will never find the correct, absolute, and final answer. In my classroom, there is always another question, another question to follow your answer. Yes, you're on a treadmill. My little questions spin the tumblers of your mind. You're on an operating table; my little questions are the fingers probing your brain. We do brain surgery here. You teach yourselves the law, but I train your mind. You come in here with a skull full of mush, and you leave thinking like a lawyer.

*The Paper Chase* (Twentieth Century Fox 1973). For his portrayal of the "stuffy, crusty, brilliant, and despotic" law professor, the 71-year-old John Houseman received the Oscar for Best Supporting Actor. See 1973 Academy Awards Winners and History, <http://www.filmsite.org/aa73.html> (last visited Oct. 24, 2009).

The movie was based on the book of the same title, published in 1970, and authored by John Jay Osborn, Jr., who, coincidentally, clerked on the United States Court of Appeals for the Third Circuit during the 1971-72 term, during Judge Aldisert's tenure. THE AALS DIRECTORY OF LAW TEACHERS 872 (2007-08).

<sup>6</sup> Aldisert, *supra* note 3, at 1.

<sup>7</sup> *Id.* at 2.

<sup>8</sup> *Id.*

<sup>9</sup> *Id.* (footnote omitted).

<sup>10</sup> *Id.* at 3-12.

<sup>11</sup> *Id.* at 16-20.

<sup>12</sup> Some of my customers prefer the moniker "Sadistic Transactions" (hence the title).

<sup>13</sup> One commercial law professor describes Article 9 as "the crowning achievement of the UCC project, and perhaps of the entire uniform law enterprise." See Edward J.

This article, together with a companion article (*Syllogisms, Enthymemes, and Fallacies: Mastering Secured Transactions Through Deductive Reasoning*<sup>15</sup>), respond to Judge Aldisert's co-authored plea for a renewed emphasis on logic and deductive reasoning in the classroom, from my perspective as a Secured Transactions professor. Both articles begin with an introduction to the syllogism, the classic form of deductive reasoning. But the two articles then travel different paths.

Following Part I's introduction to syllogistic analysis, Part II of this article offers seven reasons why Article 9 itself may hinder the effective use of syllogisms in a Secured Transactions course.<sup>16</sup> First, Article 9 occasionally redefines ordinary terms in an unconventional and counter-intuitive manner, which may lead students to reach logical, but incorrect, conclusions when crafting a syllogistic argument. Second, Article 9 sometimes fails to warn the reader that compliance with a straightforward statutory provision may dictate a conclusion that is logical, yet yields disastrous consequences. Third, Article 9 can lead to incorrect conclusions because selected rules cannot be read literally. Fourth, Article 9 occasionally adopts rules that are inconsistent with policy-based analysis, which may lead students to craft incorrect major premises and, accordingly, to reach erroneous conclusions. Fifth, sometimes a rule of Article 9 triggers a result so unexpected and inconsistent with the norm that a logical approach to its understanding is undermined. Sixth, Article 9 occasionally adopts a rule that is so illogical as to render futile any attempt to understand it logically. And seventh, many of the

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Janger, *Predicting When the Uniform Law Process Will Fail: Article 9, Capture, and the Race to the Bottom*, 83 IOWA L. REV. 569, 571 (1998). See also Lawrence Ponoroff & F. Stephen Knippenberg, *Having One's Property and Eating it Too: When the Article 9 Security Interest Becomes a Nuisance*, 82 NOTRE DAME L. REV. 373, 374 (2006) ("Powerful, creative, comprehensive yet elegant, Article 9 is generally regarded as the most innovative of the Code's articles.") (footnote omitted). My students are not so effusive in their praise, often asking if Article 9 was drafted in a foreign language and then translated. I hesitate to disclose to them that Grant Gilmore, the principal architect of Article 9, taught French at Yale University for a few years before enrolling in its law school at the age of 29. See Robert M. Jarvis, *Gilmore and Black at 50*, 38 J. MAR. L. & COM. 135, 139-40 (2007).

<sup>14</sup> 11 U.S.C. §§ 101 *et seq.* (2006).

<sup>15</sup> The manuscript of the companion article will be circulated to law journals in spring 2010. A pre-publication draft is available by contacting the author.

<sup>16</sup> Notwithstanding these statutory roadblocks, the companion article will contend that Secured Transactions is an ideal course in which legal principles can be introduced, analyzed, and mastered through deductive reasoning. The article will illustrate—through ten examples covering each of the five major topics of the Secured Transactions course (attachment, perfection, priority, default, and bankruptcy)—how narrative analysis can be expressed as deductive syllogisms, and how deductive syllogisms can be the foundation for enhanced narrative analysis. The article will also examine enthymemes (deductive reasoning which requires the audience to infer part of the argument) and review the formal fallacies which can undermine the logic of the syllogistic argument.

statutory rules of Article 9 are riddled with exceptions, frustrating the ability to easily craft the major premise of the syllogism. The article then offers a brief conclusion (and a glimpse of hope).

### I. DEDUCTIVE REASONING AND THE SYLLOGISM

Judge Aldisert and his co-authors open their discussion of deductive reasoning by noting its widespread application, and thus its importance. They suggest that “90 percent of legal issues can be resolved by deduction”<sup>17</sup> and contend that “deductive reasoning . . . is the driving force behind most judicial opinions.”<sup>18</sup> In their opinion, the form in which deductive reasoning most often appears is the syllogism—“a label logicians attach to any argument in which a conclusion is inferred from two premises.”<sup>19</sup>

The authors then introduce the reader to syllogisms by offering “the immortal example of logicians everywhere”<sup>20</sup>:

All men are mortal.

Socrates is a man.

Therefore, Socrates is mortal.<sup>21</sup>

The first statement (“All men are mortal.”) is “the major premise,” which “states a broad and generally applicable truth.”<sup>22</sup> The second statement (“Socrates is a man.”) is “[t]he minor premise” and “states a specific and usually more narrowly applicable fact.”<sup>23</sup> The third statement (“Therefore, Socrates is

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<sup>17</sup> Aldisert, *supra* note 3, at 2.

<sup>18</sup> *Id.* at 3.

<sup>19</sup> *Id.* See also LEWIS H. LARUE, GUIDE TO THE STUDY OF LAW: AN INTRODUCTION 172 (2nd ed. 2001) (“In the kingdom of law, the syllogism reigns supreme.”); Daniel S. Goldberg, *I Do Not Think It Means What You Think It Means: How Kripke and Wittgenstein’s Analysis on Rule Following Undermines Justice Scalia’s Textualism and Originalism*, 54 CLEV. ST. L. REV. 273, 276 (2006) (“The syllogism is perhaps the touchstone of modern legal method.”); Amy E. Sloan, *Erasing Lines: Integrating the Law School Curriculum*, 1 J. ASS’N LEGAL WRITING DIRECTORS 3, 4 n.4 (2002) (“Whatever its shortcomings, however, syllogistic reasoning remains at the core of much legal analysis and is, in many respects, the starting point of a first-year law student’s education in law and argumentation.”).

<sup>20</sup> Vincent A. Wellman, *Practical Reasoning and Judicial Justification: Toward an Adequate Theory*, 57 U. COLO. L. REV. 45, 91 n.206 (1985).

<sup>21</sup> Aldisert, *supra* note 3, at 3. This example (sometimes in a slightly different format) makes an occasional appearance in judicial opinions. See, e.g., Tyler v. Cain, 533 U.S. 656, 672–73 (2001) (Breyer, J., dissenting); Dukes v. Wal-Mart, Inc., 474 F.3d 1214, 1245 (9th Cir. 2007) (Kleinfeld, J., dissenting); Bird, Marella, Boxer & Wolpert, et al. v. Superior Court, 106 Cal. App. 4th 419, 430 (2003).

<sup>22</sup> Aldisert, *supra* note 3, at 4. Cf. PATRICK J. HURLEY, A CONCISE INTRODUCTION TO LOGIC 260 (6th ed. 1997) (defining the “major term” as “the predicate of the conclusion” and the “minor term” as “the subject of the conclusion”).

<sup>23</sup> Aldisert, *supra* note 3, at 4.

mortal.”) is “the conclusion,” which “draws upon these premises and offers a new insight that is known to be true based on the premises.”<sup>24</sup> The authors then reveal this important observation:

[T]he three parts of a syllogism—the two premises and the conclusion—are themselves built from three units. Logicians call these units “terms.” Two terms appear in each statement: the “major term” in the major premise and conclusion, the “minor term” in the minor premise and conclusion, and the “middle term” in the major and minor premises but not in the conclusion. Notice that the middle term covers a broad range of facts, and that if the conclusion is to be valid, the minor term must be a fact that is included within the middle term. Although the jargon can get confusing, the basic idea isn’t hard to grasp: Each statement in a syllogism must relate to the other two.<sup>25</sup>

The syllogism strikes me as an ideal instruction tool in Secured Transactions, a course built on a foundation of statutory rules, most of which are codified in U.C.C. Article 9. Article 9 reveals how a debtor may create an enforceable security interest in its property.<sup>26</sup> It provides rules that address perfection of a security interest.<sup>27</sup> The statute devotes twenty-three provisions to priority matters,<sup>28</sup> twenty-seven to filing concerns,<sup>29</sup> and twenty-eight to default issues.<sup>30</sup> Additionally, Article 9 includes a list of eighty (EIGHTY!) defined terms!<sup>31</sup> Given Article 9’s attention to detail and exhaustive coverage, Secured Transactions seems like an ideal course in which to emphasize syllogistic analysis. State the rule (major premise). State the relevant facts (minor premise). Draw a conclusion.<sup>32</sup> How hard can this be?<sup>33</sup>

<sup>24</sup> *Id.*

<sup>25</sup> *Id.* at 6.

<sup>26</sup> See generally U.C.C. § 9-203(a), (b) (2009). Statutory citations are to the American Law Institute’s 2009–2010 edition of the Uniform Commercial Code Article 9.

<sup>27</sup> See generally §§ 9-301 through 9-316.

<sup>28</sup> See §§ 9-317 through 9-342.

<sup>29</sup> See §§ 9-501 through 9-527.

<sup>30</sup> See §§ 9-601 through 9-628.

<sup>31</sup> See § 9-102(a)(1)–(80). Article 9 also incorporates definitions found elsewhere in the U.C.C. See § 9-102(b), (c).

<sup>32</sup> See James M. Boland, *Legal Writing Programs and Professionalism: Legal Writing Professors Can Join the Academic Club*, 18 ST. THOMAS L. REV. 711, 722 (2006) (suggesting that, in describing the syllogism, “the most important concept to grasp is that the major premise states the rule of law, the minor premise states the facts relevant to the major premise, and the conclusion flows logically from the premises”).

<sup>33</sup> The syllogism bears a striking resemblance to the traditional “IRAC” formula on which all law students are weaned, an observation shared by others. See, e.g., Adam Todd, *Neither Dead Nor Dangerous: Postmodernism and the Teaching of Legal Writing*, 58 BAYLOR L. REV. 893, 938 (2006) (observing that “the deductive syllogism [is] commonly known by the acronym IRAC”); Jill J. Ramsfield, *Is “Logic” Culturally Based? A Contrastive, International Approach to the U.S. Law Classroom*, 47 J. LEGAL EDUC. 157, 186 n.117 (1997) (“IRAC is the acronym for Issue, Rule, Application, Conclusion that is often taught to first-year students as an adaptation of the syllogism’s major premise,

From my side of the lectern, the approach holds quite an attraction. But Article 9 has been my traveling companion for over fifteen years, so maybe my perspective is not shared by the student who journeys at my side for only fifteen weeks. My students and I can readily conclude that Socrates must be mortal if we know that all men are mortal and Socrates is a man. But using that simple illustration as a template to master a complex and technical collection of statutory provisions may appear impossible to the typical student. The task is not impossible, but it may be daunting. Some of the challenges are created by Article 9 itself and are examined in Part II.

## II. STATUTORY ROADBLOCKS TO THE EFFECTIVE USE OF THE SYLLOGISM

Given its emphasis on statutory analysis, Secured Transactions is a course where deductive reasoning can be an effective, and oft-used, teaching tool. But Article 9 itself creates roadblocks which may frustrate learning through syllogistic analysis. This part of the article highlights seven areas of concern.

### A. "What we've got here is failure to communicate."<sup>34</sup>

The major premise of the syllogism—"All men are mortal"—is the rule of law. In Secured Transactions, the rule of law is most often drawn from Article 9 (e.g., "A secured party may perfect a security interest in the debtor's equipment by filing a financing statement."). The minor premise of the syllogism—"Socrates is a man"—is a factual statement. In Secured Transactions, the factual statement is extracted from a case or a problem (e.g., "Alamo Bank filed a financing statement against BizCorp's equipment in which Alamo Bank has an enforceable security interest."). The conclusion of the syllogism—"Therefore,

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minor premise, and conclusion."); Brooks R. Fudenberg, *Unconstitutional Conditions and Greater Powers: A Separability Approach*, 43 UCLA L. REV. 371, 445 n.284 (1995) ("The well-known IRAC (Issue, Rule, Application, Conclusion), would take the form of syllogisms. For example, after one identifies the issue, the next steps are to find the rule (major premise), do the application (minor premise), and reach a conclusion.").

<sup>34</sup> Most film buffs will recognize this quotation from *Cool Hand Luke* (Warner Bros. 1967). The line is spoken by "the Captain" (Strother Martin) and addressed to Luke (Paul Newman), who is having difficulty conforming to rural prison life after being sentenced to a chain gang for destroying several parking meters. The line is #11 on the American Film Institute's list of "*AFI's 100 Years . . . 100 Movie Quotes*." See <http://connect.afi.com/site/DocServer/quotes100.pdf?docID=242> (last visited Nov. 8, 2009).

Initially, Telly Savalas was cast as the title character, but he was in Europe and refused to fly to the United States. The producers did not wait for Savalas to return by boat and instead chose to cast Paul Newman. See Telly Savalas News and Trivia, [http://www.celebritywonder.com/html/Tellysavalas\\_trivia1.html](http://www.celebritywonder.com/html/Tellysavalas_trivia1.html) (last visited Oct. 24, 2009).

Socrates is mortal”—is a truth drawn from the major and minor premises. In Secured Transactions, the student reviews the rule of law and the factual statement and reaches a conclusion (*e.g.*, “Alamo Bank has perfected its security interest in BizCorp’s equipment.”).

Observe, however, that a party may reach an incorrect conclusion if terms common to both premises have different meanings. Perhaps the author of the major premise—the rule maker—defines “man” as “all males over 21 years of age.” Suppose the author of the minor premise—the fact finder—defines “man” as “all males who have reached puberty.” Because the authors of both premises are not singing from the same hymnal, the syllogism will yield an incorrect conclusion if Socrates has reached puberty but is not over 21 years of age.<sup>35</sup> And this problem can arise in a Secured Transactions course because Article 9 occasionally redefines ordinary terms in an unconventional and counter-intuitive manner, which may lead students to reach logical, but incorrect, conclusions.

Consider, then, the following three examples which examine some basic Article 9 terminology.

**Example #1:** Roger, a lawyer, is an avid collector of scarce baseball cards. Last week he purchased the “Mona Lisa” of baseball cards—a rare Honus Wagner<sup>36</sup> card released in 1909 by the American Tobacco Company—for \$3.25 million.<sup>37</sup> He keeps the card in a temperature-

<sup>35</sup> Cf. Posner, *supra* note 4, at 834:

Even the syllogism about Socrates would be unimpressive if the speaker were a lexicographical dictator (O’Brien in 1984?) who could redefine ‘man’ and ‘mortal’ at a stroke of the pen; or if Socrates were a boy, a god, a character in fiction, or a hermaphrodite; or if listeners had imperfect command of the speaker’s language.

This point hit home for me during a recent discussion with a colleague. We were talking about his clerkship and whether he enjoyed life in Charleston. He made some comments that suggested to me that we had very different opinions of Charleston. Of course we did. He was talking about Charleston, West Virginia, but I assumed we were talking about Charleston, South Carolina.

<sup>36</sup> Honus Wagner, a longtime shortstop for the Pittsburgh Pirates, “was a sensational hitter, a brilliant base-runner and a flawless fielder” and “is considered by many to be baseball’s greatest all-around player.” See Honus Wagner Biography, <http://www.honuswagner.com/biography.htm> (last visited Oct. 24, 2009). He is one of five members of the inaugural class inducted into baseball’s hall of fame in 1936 (along with Ty Cobb, Walter Johnson, Christy Mathewson, and Babe Ruth). See Dan Holmes, *The First Five: A Look at the Original Members of the Baseball Hall of Fame*, Feb. 18, 2007, [http://www.baseballhalloffame.org/news/article.jsp?ymd=20070218&content\\_id=571&vkey=hof\\_new](http://www.baseballhalloffame.org/news/article.jsp?ymd=20070218&content_id=571&vkey=hof_new).

<sup>37</sup> The reader who believes Roger overpaid should note that a Wagner “T206” card once owned by hockey legend Wayne Gretzky sold for \$2.8 million in September 2007, only six months after selling for \$2.35 million. See NBCSports.com, *1909 Wagner card sells for record \$2.8 million*, Sept. 6, 2007, <http://nbcsports.msnbc.com/id/20629113/>. A recently published book recounts the history of this card, what the dust jacket describes as the “holy grail” of baseball card collecting. See MICHAEL O’KEEFFE & TERI THOMPSON,

controlled safety deposit box at his bank.

Under Article 9, the Honus Wagner card is:

- A. equipment.
- B. a consumer good.
- C. investment property.

**Example #2:** A retail store sells stand-alone software disks, music and book CDs, and movie DVDs. Most customers buy these products for personal, family, or household use.

Under Article 9, the items in the store are:

- A. general intangibles.
- B. inventory.
- C. consumer goods.

**Example #3:** Jennifer, a recent college graduate, received a \$15,000 business loan last week. The bank required Jennifer's parents to provide adequate collateral.<sup>38</sup> Jennifer and both parents executed the promissory note, obligating themselves jointly and severally.

Under Article 9:

- A. both parents are debtors.
- B. both parents and Jennifer are debtors.
- C. Jennifer is the only debtor.

Most students select an answer based on the following reasoning. In Example #1, Roger is a natural person, rather than a dealer, so the baseball card is a consumer good (or perhaps investment property if Roger was motivated to purchase the card because its market value is likely to increase with time). Equipment? How silly. In Example #2, the retail store is in the business of selling the software, CDs, and DVDs, so the items are inventory (or perhaps consumer goods if a customer's intended use is relevant). They cannot be general intangibles because the disks have a tangible quality. In Example #3, Jennifer is a debtor because she applied for and received the loan proceeds and executed the promissory note. Her parents, too, are debtors because they executed the promissory note. In each instance, the

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THE CARD: COLLECTORS, CON MEN, AND THE TRUE STORY OF HISTORY'S MOST DESIRED BASEBALL CARD (2007).

<sup>38</sup> If Jennifer intended to use the loan proceeds for a personal, family, or household purpose (instead of a business purpose), then the bank's insistence on collateral might constitute an "unfair act or practice" under the Federal Trade Commission Act. See 16 C.F.R. §§ 444.2(a)(4) (2009) (indicating that a lender commits an unfair act or practice if it takes or receives from a consumer a non-possessory, non-purchase money, security interest in household goods); 444.1(d) (defining a "consumer" as "a natural person who seeks or acquires goods, services, or money for personal, family, or household use"); 441.1(i) (defining "household goods").

student uses reasoning to reach a conclusion that is logical—yet possibly wrong.

In Example #1, the card is movable, so it is a “good”<sup>39</sup> and cannot be “investment property”<sup>40</sup> (even if Roger may have been partially motivated to purchase the card for its probable appreciation in value<sup>41</sup>). The four mutually-exclusive categories of goods are consumer goods, inventory, farm products, and equipment.<sup>42</sup> The baseball card might not be a “consumer good” because it is stored in a vault and not being “used” for a “personal, family, or household” manner.<sup>43</sup> Roger, an attorney, is

<sup>39</sup> See § 9-102(a)(44) (defining “goods” as “all things that are movable when a security interest attaches” and expressly excluding, among other types of collateral, “investment property”).

<sup>40</sup> *Id.* (expressly excluding from the definition of “goods” several types of collateral, including “investment property”). See also § 9-102(a)(49) (limiting “investment property” to securities [defined at § 8-102(a)(15)], security entitlements [§ 8-102(a)(17)], securities accounts [§ 8-501(a)], commodity contracts [§ 9-102(a)(15)], and commodity accounts [§ 9-102(a)(14)]).

<sup>41</sup> I use a casebook in which the authors pose a problem involving a Ming Dynasty horse statue kept by a consumer debtor in a temperature-controlled bank vault. In classifying the statue, the authors write: “Is the statue ‘investment property’? NO. Investment property is a term of art defined in § 9-102(a)(49). It includes stocks, bonds, etc. Investment property is not goods. The statue is goods (moveable, tangible, etc.). Goods held for investment purposes are either equipment or inventory.” RAYMOND T. NIMMER, ET AL., *COMMERCIAL TRANSACTIONS: SECURED FINANCING—CASES, MATERIALS, PROBLEMS*, 155, 159 (3rd ed. 2003) (Teacher’s Manual, Problem 3.11). I believe that goods held for investment purposes also may be “consumer goods.” But that point does not detract from the authors’ conclusion (with which I agree) that an acquisition motivated by investment sentiment does not convert a “good” into “investment property.”

<sup>42</sup> See § 9-102 cmt. 4.a. (first paragraph).

<sup>43</sup> See § 9-102(a)(23) (defining “consumer goods”). With respect to the Ming Dynasty horse statue, one of the authors “thinks the statue is equipment . . . the residual category of goods . . . because [the owner] was not using the statue for personal, household or family purposes. Indeed, was he ‘using’ the statue at all?” This author acknowledges, however, that a court “might conclude the statue is consumer goods. Students do so every year.” See NIMMER, *supra* note 41, at 159. Professor Ken Kettering, however, believes that a purchase “for the sheer pleasure of ownership” is “personal use” and contends that an “argument that [the owner] isn’t ‘using’ it because it’s tucked away in a vault is just a bad pun. He can’t enjoy it unless he hangs it on a wall, rubs it over his body? Nonsense.” See Memorandum from Ken Kettering to Tim Zinnecker, dated August 20, 2008 (copy on file with author). The fact that prominent commercial law scholars can disagree on the classification further illustrates my point.

The distinction between a “consumer good” and “equipment” is important for several reasons. First, if the security agreement or financing statement describes the collateral by type, choosing the incorrect label may dictate whether the secured party has a security interest or the security interest is perfected. See §§ 9-203(b)(3)(A) (requiring the debtor to authenticate a security agreement “that provides a description of the collateral”); 9-502(a)(3) (indicating that a financing statement is sufficient if it “indicates the collateral”); 9-108(b)(3) (permitting collateral descriptions by “type of collateral defined” by Article 9). Second, a purchase-money security interest in many consumer goods, but not equipment, may be perfected automatically upon attachment. See § 9-309(1). Third, some of the default provisions in Part 6 of Article 9 apply only to consumer goods. See, e.g., §§ 9-620(e) (imposing mandatory dispositions of consumer goods in some instances); 9-624(c) (prohibiting waiver of redemption rights in consumer

not holding the card for sale or lease in the ordinary course of his business (at least absent evidence that he sells his cards on a regular basis), and the card does not otherwise fit within the definition of "inventory."<sup>44</sup> And even if Wagner spent time on a "farm club" roster,<sup>45</sup> neither the card (nor Wagner himself) would be a "farm product."<sup>46</sup> So it can be plausibly argued that the card may fall within the residual category: equipment.<sup>47</sup>

In Example #2, the various software disks, music CDs, and movie DVDs are not "consumer goods" in the hands of the retail store. The fact that most customers purchase the items for personal, family, or household use is irrelevant (until the customer is the debtor and becomes the party whose primary use dictates the proper label). Nor are the items necessarily "inventory," even though the retail store is in the business of selling these tangible products. "Inventory" applies only to "goods,"<sup>48</sup> but the definition of "goods" excludes "a computer program embedded in goods that consist solely of the medium in which the program is embedded."<sup>49</sup> The stand-alone software

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goods); 9-625(c) (permitting recovery of minimum statutory damages for secured party's noncompliance if collateral is consumer goods).

<sup>44</sup> See § 9-102(a)(48) (defining "inventory") and cmt. 4.a ("Implicit in the definition [of "inventory"] is the criterion that the sales or leases are or will be in the ordinary course of business.").

<sup>45</sup> A "farm club" is a minor league baseball team. The term is credited to baseball executive Branch Rickey, who jokingly observed that minor league teams in small rural towns were "growing players down on the farm like corn." See Minor League Baseball: Information From Answers.com, <http://www.answers.com/topic/minor-league-baseball> (last visited Oct. 19, 2009). Rickey, who earned a law degree from the University of Michigan, was instrumental in integrating major league baseball. His accomplishments included signing African-American Jackie Robinson and later drafting the first Latin-American superstar, Roberto Clemente (who reached the 3,000-hit milestone on the last day of the 1972 season and then tragically died on December 31, 1972, in a plane crash while on a humanitarian mission to Nicaragua). See John Stiglich, *Branch Rickey: Forgotten American Hero*, THE MICHIGAN DAILY, May 7, 2006, available at <http://www.michigandaily.com/content/john-stiglich-branch-rickey-forgotten-american-hero>; 'Clemente' Tells Story of a True Baseball Hero, <http://www.npr.org/templates/story/story.php?storyId=5369849> (last visited Oct. 19, 2009).

<sup>46</sup> See § 9-102(a)(34) (defining "farm products" to include crops and livestock that are the subject of a "farming operation").

<sup>47</sup> See § 9-102(a)(33) (defining "equipment" as "goods other than inventory, farm products, or consumer goods").

<sup>48</sup> See § 9-102(a)(48) ("Inventory" means goods . . . ).

<sup>49</sup> See § 9-102(a)(44) (penultimate sentence of definition). See also 9A WILLIAM D. HAWKLAND ET AL., UNIFORM COMMERCIAL CODE SERIES [REV] § 9-102.10 at 9-135 (2000) ("[A] program embedded in goods that consist solely of the medium in which the program is embedded is not a good, such as a diskette."); Ralph J. Rohner, *Leasing Consumer Goods: The Spotlight Shifts to the Uniform Consumer Leases Act*, 35 CONN. L. REV. 647, 693 (2003) (observing that "a computer program that the consumer downloads into a home computer is likely to be treated as 'software' and not goods, even though the software is embedded in a tangible plastic disk") (footnote omitted).

disks fall within the exclusionary language,<sup>50</sup> as might the music CDs and movie DVDs if the audio and video data are accompanied by a computer program. But even if these audio and video disks consist solely of data and are not accompanied by a computer program, the value of the disks is not the tangible disks themselves but the data on the tangible disks.<sup>51</sup> These disks, then, could be “general intangibles.”<sup>52</sup>

Finally, in Example #3, Jennifer is not a debtor, even though she has joined her parents in executing the promissory note and incurring liability for repayment. Jennifer’s parents are offering the collateral, so they are “debtors.”<sup>53</sup> But Jennifer does not have any property interest in the collateral, so she is not a “debtor” even though she is the direct beneficiary of the loan proceeds and is contractually obligated to repay the loan.<sup>54</sup>

<sup>50</sup> The software disks probably are “software,” defined at § 9-102(a)(75) and, therefore, are expressly included within the definition of “general intangibles” at § 9-102(a)(42).

<sup>51</sup> See *In re Information Exch., Inc.*, 98 B.R. 603, 604–05 (Bankr. N.D. Ga. 1989) (concluding nonfiling creditor’s possession of computer tape did not perfect a security interest because the collateral—the information and programming on the tape, rather than the tape itself—was a “general intangible” and not a “good”); *Page v. Hotchkiss*, 52 U.C.C. Rep. Serv. 2d 365, 368–71 (Conn. Super. Ct. 2003) (initially concluding under U.C.C. Article 2 that software developed by Hotchkiss for Page was a programming “service” rather than a “good,” and then observing under U.C.C. Article 9 “that what Hotchkiss provided was not goods since what was provided was a modified computer program embedded in a convenient medium for Page to access” and that “[t]he real object of Page’s purchase was the intellectual property which had been loaded and stored on a transferable medium”). Cf. *In re C Tek Software, Inc.*, 117 B.R. 762, 767–68 (Bankr. D.N.H. 1990) (relying on *In re Bedford Computer Corp.*, 62 B.R. 555, 567 (Bankr. D.N.H. 1986), to conclude that “the source code is more tangible than intangible because ‘the source code . . . cannot exist independent from the actual hardware components to which it gives operational life’”).

<sup>52</sup> Determining whether the CDs and the DVDs are “inventory” or “general intangibles” is important for several reasons under Article 9. For example, using one—but not both—terms in the collateral description in the security agreement or financing statement could leave the secured party at best with an unperfected security interest in the items and at worst no security interest in the items. See §§ 9-203(b)(3)(A) (requiring the debtor to authenticate a security agreement “that provides a description of the collateral”); 9-502(a)(3) (indicating that a financing statement is sufficient if it “indicates the collateral”); 9-108(b)(3) (permitting collateral descriptions by “type of collateral defined” by the U.C.C.). Also, a secured party can perfect a security interest in inventory, but not general intangibles, by taking possession. See § 9-313(a) (listing “goods” but not “general intangibles”).

<sup>53</sup> See § 9-102(a)(28) (defining “debtor” as “(A) a person having an interest . . . in the collateral . . .”).

<sup>54</sup> See § 9-102 cmt. 2.a. (exs. 2 and 3). Because Jennifer has incurred a payment obligation on a secured debt, she is an “obligor” under § 9-102(a)(59)(i). Correctly identifying the “debtor” is important for a variety of reasons. For example, most security interests are memorialized in a written security agreement, which must be authenticated by the “debtor.” See § 9-203(b)(3)(A). Also, if the secured party disposes of the collateral following default, the “debtor” usually is entitled to receive an asset disposition notice under § 9-611(c)(1) and any surplus proceeds under § 9-615(d)(2).

The preceding discussion, then, illustrates one possible roadblock to the effective use of syllogisms in a Secured Transactions course. Article 9 occasionally redefines ordinary terms in an unconventional and counter-intuitive manner, which may lead students to reach logical, but incorrect, conclusions.

B. "[B]ecause thou hast not given him warning, he shall die in his sin."<sup>55</sup>

Socrates decides to attend law school (he's curious to know more about this "Socratic method" that seems to be so popular with the students). The application form states: "Your application is complete only if it includes an undergraduate transcript, two letters of reference, a recent LSAT score, and \$50." So Socrates completes and personally delivers the application form, together with the other requested materials, to the admissions committee. Several months come and go, and Socrates does not hear from the admissions committee. He contacts the committee and receives a short letter, the body of which states: "The admissions committee has not yet reviewed your application because your file is missing a 'personal essay.' We have filled all slots for the incoming class, but we encourage you to apply again next year." Alas (for Socrates), the application form failed to direct Socrates to a paragraph found elsewhere in the law school's literature which gives the admissions committee the discretion to decline to review an application file that fails to include a "personal essay." According to the form, Socrates submitted a complete application. He can logically conclude from the statement on the form, and his compliance with the form's requests, that his application will not be ignored by the admissions committee because his file fails to provide additional information not mentioned on the application form. But his logical conclusion has led to an unwelcome result.

And Article 9 sets a similar trap for the unwary by occasionally failing to warn the reader that compliance with a straightforward rule may render a logical conclusion, but yield disastrous consequences.

Consider the following hypothetical. To secure repayment of a \$25,000 loan, BizCorp grants to SmallBank an enforceable security interest in all of BizCorp's current and future accounts, equipment, and inventory. SmallBank will perfect its security interest by filing a financing statement with the appropriate

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<sup>55</sup> *Ezekiel* 3:20 (King James). It gets worse: "... and his righteousness which he hath done shall not be remembered : but his blood will I require at thine hand." *Id.* Yikes!

filing office.<sup>56</sup> Section 9-502 states that a financing statement “is sufficient only if it: (1) provides the name of the debtor; (2) provides the name of the secured party . . . ; and (3) indicates the collateral covered by the financing statement.”<sup>57</sup> SmallBank’s lawyer prepares the following form for filing:

FINANCING STATEMENT

NAME OF DEBTOR:	<i>BizCorp</i>
NAME OF SECURED PARTY:	<i>SmallBank</i>
COLLATERAL:	<i>BizCorp’s current and future accounts, equipment, and inventory</i>

She submits the form, along with the correct fee and an instruction letter, to the appropriate filing officer. The filing officer timely informs SmallBank’s lawyer that it has rejected the filing.<sup>58</sup>

TRUE or FALSE: Because SmallBank’s filing provided all of the information required by § 9-502(a), the filing officer improperly rejected the filing.

Most students will compare the information on the form (minor premise) against the information required by § 9-502 (major premise) and conclude that the filing is “sufficient.” These students then conclude that because the filing is “sufficient” (e.g., adequate, proper, correct, etc.),<sup>59</sup> the filing officer improperly rejected the filing. But this logical rationale leads to an incorrect conclusion. In fact, the rejection was proper!

Concerned that filing officers might exercise too much discretion when deciding whether to accept a financing statement, the drafters provided an exclusive list of grounds for rejection.<sup>60</sup> Those grounds include the omission of specific pieces

<sup>56</sup> See § 9-310(a) and cmt. 2 (stating the general rule that a financing statement will perfect an enforceable security interest in most types of collateral).

<sup>57</sup> § 9-502(a).

<sup>58</sup> See § 9-520(b) (requiring the filing officer to “communicate to the person that presented the [financing statement] the fact of and reason for the refusal . . . in no event more than two business days after the filing office receives the [financing statement]”).

<sup>59</sup> Cf. §§ 9-520(c) (noting that a “filed” financing statement which satisfies § 9-502(a) is “effective”); 9-520 cmt. 3 (referring to a financing statement which complies with § 9-502 as “legally sufficient to perfect a security interest”).

<sup>60</sup> See Steven L. Harris & Charles W. Mooney, Jr., *Revised Article 9 Meets the Bankruptcy Code: Policy and Impact*, 9 AM. BANKR. INST. L. REV. 85, 100 n.83 (2001) (noting the inclusion of provisions for the purpose of “limiting the grounds upon which a filing office may reject a financing statement”); Christopher S. Bose, *A Trap for the Unwary: Revised UCC Article 9’s Deceptive Technical Guillotine for Financing Statements*, 55 CONSUMER FIN. L.Q. REP. 152, 152 (2001) (noting the drafters’ “competing consideration . . . to restrain instances where filing offices reject attempted filings on improper grounds”).

of information *not required* by § 9-502, including: (i) a mailing address for the secured party,<sup>61</sup> (ii) the mailing address for the debtor,<sup>62</sup> and (iii) an indication of whether the debtor is an individual or an organization<sup>63</sup> (and, if the latter, the type of organization, the jurisdiction of organization, and an organizational identification number<sup>64</sup>). In effect, then, Article 9 bifurcates information into two classes: information necessary for an effective filing (§ 9-502(a)), and information necessary to avoid rejection by the filing office (§ 9-516(b)).<sup>65</sup> Because the filing submitted by SmallBank's lawyer failed to include these pieces of information, the filing officer had several legitimate grounds for rejecting the filing.<sup>66</sup>

Section 9-502(a) specifically describes SmallBank's filing as "sufficient" because it includes the information mandated by the subsection. But surprisingly (at least to students who retain an amateur status), a "sufficient" filing can be rejected, an act which effectively leaves the secured party unperfected. Certainly the reader deserves some warning that § 9-502(a) is potentially misleading and may trap the unwary.<sup>67</sup> So where is this warning found? The reader will find no cautionary language in subsection (a)<sup>68</sup> or any of the other three statutory subsections of § 9-502.<sup>69</sup>

<sup>61</sup> See § 9-516(b)(4).

<sup>62</sup> See § 9-516(b)(5)(A).

<sup>63</sup> See § 9-516(b)(5)(B). See also §§ 1-201(b)(25) (defining "organization"); 9-102(c) (incorporating definitions in Article 1).

<sup>64</sup> See § 9-516(b)(5)(C)(i)–(iii).

<sup>65</sup> One author describes the "analysis of this bifurcation" of information as "increasingly complex." Lawrence R. Ahern, III, "Workouts" Under Revised Article 9: A Review of Changes and Proposal for Study, 9 AM. BANKR. INST. L. REV. 115, 148 (2001). See also Richard H. Nowka, *Minor Errors in 'In-Lieu-Of' Statements Under U.C.C. Section 9-706: Did the Drafters of Revised Article 9 Forget the Safety Net?*, 42 BRANDEIS L.J. 721, 729–30 (2004) (observing the "interesting drafting peculiarity" of §§ 9-502 and 9-516). Cf. Ingrid Michelsen Hillinger & Michael G. Hillinger, 2001: A Code Odyssey (New Dawn for the Article 9 Secured Creditor), 106 COM. L.J. 105, 144 (2001) ("If [the information stated in § 9-502(a)] is all that Revised Article 9 requires by way of valid financing statement, you might legitimately wonder why the initial financing statement form included in revised section 9-521 asks for considerably more information.").

<sup>66</sup> The information required by § 9-516(b) "assists searchers in weeding out 'false positives,' i.e., records that a search reveals but which do not pertain to the debtor in question." § 9-520 cmt. 3.

<sup>67</sup> Bose, *supra* note 60, at 157 ("Section 9-502(a) may lead the less experienced Article 9 reader to believe that the requirements for a financing statement are simple, easy, and nontechnical, thereby trapping the unwary into a failure to achieve perfection of the security interest.").

<sup>68</sup> Subsection (a) does direct the reader to subsection (b) if the filing covers as-extracted collateral, timber to be cut, or goods which are or may become fixtures. § 9-502(a) ("Subject to subsection (b) . . .").

<sup>69</sup> The reader who reviews the accompanying "Official Comments" may stumble across this inconspicuous and rather innocuous statement: "In addition, the filing office must reject a financing statement lacking certain other information formerly required as a condition of perfection (e.g., an address for the debtor or secured party). See Sections 9-516(b), 9-520(a)." § 9-502 cmt. 4. Most of us who have been anointed to teach Secured

Nor will the reader observe any red flags in either of the two neighboring statutes, §§ 9-501 and 9-503.<sup>70</sup> Not until several sections (and pages) later are the grounds for rejecting a “sufficient” filing tucked away—in § 9-516(b).<sup>71</sup>

The foregoing analysis reveals another potential difficulty in presenting material in a Secured Transactions course in a syllogistic format. Article 9 occasionally fails to warn the reader that compliance with a straightforward rule may yield both a logical conclusion and disastrous consequences.

C. “How clever you are, my dear! You never mean a single word you say.”<sup>72</sup>

Socrates is flying to Chicago to present a paper on the musings of noted philosopher L. P. Berra.<sup>73</sup> He arrives at the airport and notices several signs that state: “Each passenger is limited to one carry-on article. No exceptions.” Socrates observes a passenger in the boarding line with a laptop

Transactions, however, will attest that few of our students read the Official Comments on a consistent basis. Cf. Dale Beck Furnish, *The Creation and Notice of Security Interests in Movable Property*, 36 U.C.C. L.J. 99, 107 n.17 (2003) (concluding that “[o]nly the rigorously compulsive and insightful reader of the statute is likely to make the connection” between §§ 9-502(a) and 9-516(b) because the “only clue” is “hidden” in § 9-502 cmt. 4).

<sup>70</sup> These two sections address filing location and sufficiency of party names, respectively.

<sup>71</sup> Section § 9-520(a) states that a filing officer “shall refuse to accept” a financing statement for any reason stated in § 9-516(b), which might prompt the reader to conclude that a rejectable financing statement cannot be effective. That conclusion, although logical, is incorrect. See § 9-520(c) (indicating that the filing is effective, “even if the filing office is required to refuse to accept it for filing under subsection (a),” but affording protection under § 9-338 to specific parties who may have relied on incorrect information in the filing). See also Robert M. Lloyd, *The New Article 9: Its Impact on Tennessee Law (Part I)*, 67 TENN. L. REV. 125, 173 (1999) (referring to the “convolution” that exists between §§ 9-520(a) and 9-516(b)).

<sup>72</sup> Penned by playwright Oscar Wilde and spoken by Lady Hunstanton to Mrs. Allonby in *A Woman of No Importance* (act 2). See OSCAR WILDE, *A WOMAN OF NO IMPORTANCE*, in 6 THE COMPLETE WORKS OF OSCAR WILDE 65 (The Aldine Publishing Co., 1910). Readers may not know that Wilde was christened with three middle names (Fingal O’Flahertie Wills), and, despite his magic as a wordsmith, authored only one novel: *THE PICTURE OF DORIAN GRAY*. See H. MONTGOMERY HYDE, *OSCAR WILDE: A BIOGRAPHY* 5, 148 (1975).

<sup>73</sup> Known as “Yogi” to his friends. His most profound thoughts include the following: “This is like *deja vu* all over again.” “You can observe a lot just by watching.” “Nobody goes there anymore; it’s too crowded.” “If you come to a fork in the road, take it.” “Texas has a lot of electrical votes.” “You should always go to other people’s funerals; otherwise, they won’t come to yours.” See *Things People Said: Yogi Berra Quotes*, <http://www.rinkworks.com/said/yogiberra.shtml> (last visited Oct. 19, 2009). Yogi Berra also was one of baseball’s greatest catchers. During his 19-year career with the New York Yankees, he won the American League M.V.P. award three times and played on 14 pennant-winning teams and 10 World Series championships. He was elected to the Hall of Fame in 1972. See National Baseball Hall of Fame and Museum, *Yogi Berra*, <http://www.baseballhalloffame.org/hofers/detail.jsp?playerId=110925> (last visited Oct. 19, 2009).

computer, a briefcase, and a small garment bag. Socrates, who has never flown before this trip, logically concludes, from the signs, that this passenger will be asked to check two of the items.<sup>74</sup> But the passenger is permitted to board the airplane with all three items! Socrates discovers that he is sitting next to this passenger. Socrates expresses amazement that the passenger could carry the laptop computer, the briefcase, and the small garment bag onto the plane. "Doesn't the sign tell all passengers to limit themselves to one carry-on article?" Socrates asks. "Yes," says the passenger, "but you can't read the sign literally."

And a student who reads Article 9 literally may confront the same predicament of reaching logical, but incorrect, conclusions.<sup>75</sup>

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<sup>74</sup> He also might logically conclude that the passenger carrying a six-inch screwdriver and long knitting needles will have those items confiscated. Maybe not! See TSA: Prohibited Items, <http://www.tsa.gov/travelers/airtravel/prohibited/permitted-prohibited-items.shtm#4> (last visited Oct. 19, 2009); TSA: Transporting Knitting Needles & Needlepoint, [http://www.tsa.gov/travelers/airtravel/assistant/editorial\\_1252.shtm](http://www.tsa.gov/travelers/airtravel/assistant/editorial_1252.shtm) (last visited Oct. 19, 2009). Snow globes (how deadly!), of course, are a no-no. See TSA: Prohibited Items, <http://www.tsa.gov/travelers/airtravel/prohibited/permitted-prohibited-items.shtm#11> (last visited Oct. 19, 2009).

<sup>75</sup> Judge Learned Hand once wrote: "There is no surer way to misread any document than to read it literally . . ." *Guisseppi v. Walling*, 144 F.2d 608, 624 (2nd Cir. 1944) (Hand, J., concurring). Perhaps rigid adherence to the text should be discouraged if a literal reading will render an absurd result or the reader is confronting a matter unforeseen by the author. But I do not raise either of those situations.

One of Judge Hand's best-known law clerks was constitutional scholar Gerald Gunther, who took more than twenty years to research and write what one reviewer for *The New York Times* called "the fullest, most sensitive, most penetrating of judicial biographies." See Ari L. Goldman, *Gerald Gunther, Legal Scholar, Dies at 75*, N.Y. TIMES, Aug. 1, 2002, available at <http://www.nytimes.com/2002/08/01/us/gerald-gunther-legal-scholar-dies-at-75.html>.

In the biography of his mentor, Professor Gunther recounts this amusing story from his clerkship, concerning Judge Hand's request for Gunther's critique of a draft of a dissenting opinion in *United States v. Remington*, 208 F.2d 567 (1953):

After seven weeks, he handed his most recent effort to me. "Now look at this one; see if this one holds water any better." I studied the new draft for several hours and returned to his desk. Hand looked up eagerly: "Well, will it wash?" I responded that portions of the opinion now seemed reasonably airtight, but there were still weaknesses in other sections. Hand looked at me darkly, pain and annoyance clouding his face. He heaved a deep sigh, then picked up a small paperweight on his desk and threw it in my general direction, missing me by only a narrow margin. "Damn," he shouted, "I can't go on forever like this! Thirteen drafts and it's still not satisfactory? Son, I get paid to decide cases. At some point, I have to get off the fence and turn out an opinion. Enough!" I had never heard Hand speak in such anger. I turned pale and retreated, shaken, to my desk in the adjacent office. I flung my head down on the desk and tried to regain my composure. After a minute or so, I felt a hand gently tapping the back of my head. Judge Hand, in his stocking feet, had silently left his desk, come into my office and hoisted himself to a sitting position on my desk. I raised my face and looked up into his bemused countenance. "Now, now," he gently consoled, "you can't take it that way! It's all part of the job! Don't take it so hard—you did your job; I have to do mine."

A party that wins a lawsuit against a debtor may become a “lien creditor,” defined as “a creditor that has acquired a lien on the property involved by attachment, levy, or the like.”<sup>76</sup> For example, Jane might acquire a lien on Sarah’s jewelry after Jane wins her defamation lawsuit against Sarah, or SmithCorp might obtain a lien on the inventory of JonesCo following SmithCorp’s successful litigation against JonesCo for breach of contract.<sup>77</sup>

As a general rule, a priority dispute between a lien creditor and the Article 9 secured party turns on whether the secured party holds a perfected security interest in the debtor’s property when the competing creditor first becomes a “lien creditor” (*i.e.*, when its lien initially encumbers the debtor’s property).<sup>78</sup> So, Lender will enjoy priority in Sarah’s jewelry if Lender holds a perfected security interest in the jewelry when Jane acquires her lien, but SmithCorp will enjoy priority if its lien on the JonesCo inventory arises before Lender obtains a perfected security interest in the inventory.

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That evening, my wife came to pick me up at the office so that we could go together to a social engagement. She told me that she had encountered Hand on her way in and that he had chided her, “Come on, now, you’ve been married three or four years. Don’t you ever yell at him? You must yell at him once in a while. He’s not used to it. He’s got to get used to people yelling at him!”

GERALD GUNTHER, *LEARNED HAND: THE MAN AND THE JUDGE* 620–21 (1994).

<sup>76</sup> § 9-102(a)(52)(A). The term also includes certain assignees and receivers, and the dreaded trustee in bankruptcy (also known as “the prince of darkness”). *Id.* at (B)–(D).

<sup>77</sup> The procedures necessary for the lien to attach to the debtor’s personal property vary among the states:

but ordinarily a creditor first must obtain a judgment against the debtor and then secure a writ of execution ordering the sheriff to levy on the debtor’s property. Some states, of course, allow the creditor to obtain a lien on personal property without first obtaining a judgment as in a prejudgment attachment[.]

HAWKLAND, *supra* note 49, § 9-317:2 at 9-271 (footnote omitted). *See also* Thomas M. Ward, *Ordering the Judicial Process Lien and the Security Interest under Article Nine: Meshing Two Different Worlds (Part I—Secured Parties and Post-Judgment Process Creditors)*, 31 ME. L. REV. 223, 234–64 (1980) (discussing creation, characteristics, and timing of “liens” and resulting “lien creditor” status under different state laws).

<sup>78</sup> *See* § 9-317(a)(2)(A). The statute states that the Article 9 security interest is subordinate, or junior, to the rights of a person who becomes a lien creditor “before” the security interest is perfected. The statute’s use of “before” effectively gives the Article 9 security interest priority in the case of a tie, which may arise when the lien attaches simultaneously with the moment of perfection. This may occur when the secured party has taken all steps necessary to perfect its security interest in the debtor’s current and future assets, but the debtor has not yet acquired the particular asset subject to the lien.

The statute also awards priority to the secured party who, when the lien attaches, has a security agreement in place that covers the asset and has already filed a financing statement. *See* § 9-317(a)(2)(B). Unlike the rule in (A), the rule in (B) protects the secured party who lacks perfection only because it has yet to give value. *See* §§ 9-203(b)(1) (requiring value as a condition to enforceability); 9-203(a) (indicating that an enforceable security interest “attaches to collateral”); 9-308(a) (requiring attachment as a prerequisite to perfection).

Unless its collateral is a consumer good, a purchase-money creditor (e.g., the dealer who sells on credit, or the third-party financier whose funds are used by the debtor to purchase the item from the dealer) must file a financing statement to perfect its purchase-money security interest.<sup>79</sup> Whether the purchase-money creditor is the dealer or the third-party financier, the creditor most often will not file its financing statement until sometime after the actual sale occurs and the buyer/debtor takes possession of the asset. Under the general priority rule, then, the purchase-money creditor takes the risk that someone may become a "lien creditor" against the asset before the financing statement is filed. In an effort to accommodate this risk and acknowledge this typical business practice ("sell first, file later"), the general priority rule is expressly subject to the following purchase-money carve out:

[I]f a person files a financing statement with respect to a purchase-money security interest before or within 20 days after the debtor receives delivery of the collateral, the security interest takes priority over the rights of a . . . lien creditor which arise between the time the security interest attaches and the time of filing.<sup>80</sup>

This rule protects the purchase-money creditor from losing priority to a party who becomes a lien creditor against the asset after the security interest attaches to the asset and before the security interest is perfected, if the secured party perfects its security interest by filing a financing statement against the asset no later than the twentieth day after the debtor receives delivery of the asset. On a timeline, then, the important events occur in this order: (1) the purchase-money security interest attaches; (2) a party becomes a "lien creditor" against the asset; and (3) the purchase-money creditor files its financing statement. The only other important event is the date on which the buyer/debtor takes delivery of the asset.

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<sup>79</sup> The technical requirements of a purchase-money security interest are found in § 9-103. Section 9-309(1) states the general rule that a purchase-money security interest in most consumer goods is perfected at attachment (often referred to as "automatic" perfection). The negative implication is that a purchase-money security interest in collateral other than consumer goods—such as inventory and equipment—is not automatically perfected at attachment. Instead, perfection of the security interest requires some additional step, usually the filing of a financing statement.

<sup>80</sup> § 9-317(e). See also § 9-317(a)(2) ("except as otherwise provided in subsection (e) . . ."); Grant Gilmore, *The Purchase Money Priority*, 76 HARV. L. REV. 1333, 1387 (1963) (referring to "the business practice of filing after delivery in cases of purchase money security interests in collateral other than inventory" as justification for the grace period, and then observing that "if the debtor insists that he must have the goods today, the purchase money financier can deliver them, without sacrificing his . . . priority, provided he perfects" within the prescribed grace period).

All of this seems rather straightforward. So consider the following hypothetical. ABC Florist Company buys, and takes possession of, a new delivery van on May 1. Dealer retains a purchase-money security interest in the van that attaches on that date. Smith, a successful litigant against ABC in a recent lawsuit, becomes a "lien creditor" against the van on May 3. Mindful of applicable state laws governing encumbrances on non-inventory motor vehicles, Dealer does not file a financing statement against the van. Instead, Dealer complies with applicable motor vehicle laws and submits paperwork to the applicable government office, which then issues a certificate of title marked to show Dealer's security interest. Dealer's date of perfection is May 18. A few weeks later, Smith and Dealer squabble over the van. *Which creditor has priority in the vehicle?*

Under the general priority rule of § 9-317(a), Smith enjoys priority because she became a "lien creditor" on May 3, several days before Dealer became perfected on May 18. A student may address the relevance of the purchase-money exception with the following syllogism:

A purchase-money creditor must timely file a financing statement to enjoy priority over a lien creditor whose interest arose between attachment and filing.

Dealer, a purchase-money creditor (stipulated), did not file a financing statement.

Dealer does not enjoy priority over a lien creditor whose interest arose between attachment and filing.<sup>81</sup>

The syllogism states the rule, analyzes whether facts are present which satisfy the requirements of the rule, and draws a logical conclusion from that analysis. So why is the conclusion wrong? Because the rule cannot be read literally!

The rule protects a purchase-money creditor who timely "files a financing statement."<sup>82</sup> Read literally, then, a person who timely complies with certificate-of-title laws cannot invoke the rule. But the drafters of Article 9 did not intend for the rule to be read literally. Instead, the rule is to be read as if it referred to a person who timely "files a financing statement *or complies with the requirements of a statute, regulation, or treaty described in Section 9-311(a).*" An example of a statute mentioned in § 9-311(a) is a "certificate-of-title statute . . . which provides for a

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<sup>81</sup> Smith is such a lien creditor, a point hopefully addressed in one or more separate syllogisms.

<sup>82</sup> § 9-317(e).

security interest to be indicated on the certificate as a condition or result of perfection.”<sup>83</sup>

How is the student supposed to know that the meaning of “files a financing statement” is something other than its plain meaning? One might assume that the statutory language of § 9-317(e) should be the first place to look for some clue. But no clue exists in subsection (e), or in any of the other subsections of § 9-317. The critical statutory language is found several sections (and pages) earlier. Section 9-311(b) states in relevant part: “Compliance with the requirements of a [certificate-of-title] statute . . . described in subsection (a) for obtaining priority over the rights of a lien creditor is equivalent to the filing of a financing statement under this article.”<sup>84</sup> But § 9-311 is never cross-referenced in the body of § 9-317! Perhaps the student will stumble across the reference to § 9-311 in the concluding paragraph of the eighth (and final) Official Comment to § 9-317.<sup>85</sup> But why should the reader not find such an important cross-reference in the statutory language itself?<sup>86</sup>

Article 9 strives to use straightforward, unambiguous, statutory language. But as noted in the preceding analysis, sometimes that language fails to tell the reader the full story. Such incomplete language, when read literally, can lead to incorrect conclusions. This inability to apply the statutory language at face value is yet another reason why mastering the legal principles in a Secured Transactions course through syllogisms can be challenging.

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<sup>83</sup> § 9-311(a)(2).

<sup>84</sup> § 9-311(b). *See also* §§ 9-311(a)(2) (requesting states to “list any certificate-of-title statute covering automobiles, trailers, mobile homes, boats, farm tractors, or the like, which provides for a security interest to be indicated on the certificate as a condition or result of perfection”); 9-102(a)(10) (defining “certificate of title”).

<sup>85</sup> Official Comment 8 to § 9-317 is captioned “Purchase-Money Security Interests.” The first paragraph discusses subsection (e). The second paragraph states:

Section 9-311(b) provides that compliance with the perfection requirements of a statute or treaty described in Section 9-311(a) “is equivalent to the filing of a financing statement.” It follows that a person who perfects a security interest in goods covered by a certificate of title by complying with the perfection requirements of an applicable certificate-of-title statute “files a financing statement” within the meaning of subsection (e).

§ 9-317 cmt. 8.

<sup>86</sup> The same issue arises in § 9-315, which addresses continued perfection in proceeds. *See* § 9-315(d)(1)(A) (referring to “a filed financing statement”) and cmt. 6 (indicating that compliance with perfection requirements under a statute or treaty described in § 9-311 falls within the intended meaning of the phrase “filed financing statement”).

Article 9 offers evidence that the drafters knew how to cross-reference § 9-311 when discussing filed financing statements. *See, e.g.*, §§ 9-611(c)(3)(B), (C); 9-621(a)(2), (3).

D. “Policy considerations cannot override our interpretation of the text[.]”<sup>87</sup>

In July, Socrates and Francois-Marie Arouet<sup>88</sup> were in a car accident. Arouet suffered a temporary injury to his back, which greatly affected his mobility. Arouet completed all necessary paperwork and obtained a six-month permit to park in spaces reserved for persons with physical disabilities. By October, Arouet’s mobility had returned to normal. Socrates, relying on the policy underlying the issuance of the six-month permit, believes that Arouet’s parking permit is no longer effective. He is surprised to discover, under the applicable law, that the parking permit remains effective for the full six months from issuance.

Relying on a statute’s underlying policy to determine its proper application may be a logical approach. But where there exists a disconnect between the policy and the text, such statutory construction may lead to incorrect conclusions. And that can happen in a Secured Transactions course.

Students learn early in the semester two basic priority rules: (1) a secured claim beats an unsecured claim; and (2) a perfected secured claim trumps an unperfected secured claim.<sup>89</sup> After mastering the rules for creating an enforceable security interest,<sup>90</sup> students turn their attention to the methods of perfection. The most popular method of perfecting a security interest is filing a financing statement with the appropriate state official,<sup>91</sup> the purpose of which “is to give notice to creditors and other interested parties that a security interest exists in property of the debtor.”<sup>92</sup>

<sup>87</sup> *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 188 (1994).

<sup>88</sup> Most readers know Arouet by his pen name, “Voltaire.” He once remarked, “Behind every successful man stands a surprised mother-in-law.” See *Voltaire Quotes*, <http://www.brainyquote.com/quotes/authors/v/voltaire.html> (last visited Oct. 24, 2009). He also owned sixty walking sticks, twenty more than another contemporary French philosopher, Jean Jacques Rousseau. See *Canes, So Much More Than Walking Sticks*, [http://www.liveauctiontalk.com/free\\_article\\_detail.php?article\\_id=583](http://www.liveauctiontalk.com/free_article_detail.php?article_id=583) (last visited Oct. 24, 2009). Apparently their shared appreciation for the cane was the only matter on which they agreed. See *Rit Nosotro, Voltaire and Rousseau*, <http://www.hyperhistory.net/apwh/essays/comp/cw20/VoltairRousseau32200123.htm> (last visited Oct. 24, 2009) (noting “their hatred for one another was well-known during their lifetime”).

<sup>89</sup> Article 9 codifies these two rules in §§ 9-201(a) and 9-322(a)(2), respectively.

<sup>90</sup> See *generally* § 9-203(a), (b).

<sup>91</sup> See § 9-310(a) (stating the general rule that “a financing statement must be filed to perfect all security interests”) and cmt. 2 (noting “a central Article 9 principle” that “[f]iling a financing statement is necessary for perfection of security interests”).

<sup>92</sup> *Peoples Bank v. Bryan Bros. Cattle Co.*, 504 F.3d 549, 559 (5th Cir. 2007) (quoting *In re Glasco, Inc.*, 642 F.2d 793, 795 (5th Cir. 1981)). See also *In re Perry Hollow Mgmt. Co., Inc.*, 297 F.3d 34, 40 (1st Cir. 2002) (referring to “the intended purpose of the filing requirement, which is to give proper notice that a secured interest exists”); *Allstate Fin. Corp. v. United States*, 109 F.3d 1331, 1335 (8th Cir. 1997) (“The purpose of filing

With this background in mind, assume that BankOne perfected a security interest in SmithCorp's current and after-acquired equipment, inventory, and accounts by filing a financing statement in July 2006 with the appropriate Texas official. In February 2007, SmithCorp sold a valuable piece of its equipment to JonesCorp without BankOne's knowledge or consent. In July 2007, SmithCorp changed its legal name to "HarrisCorp."

BankTwo made a secured loan to JonesCorp in November 2008 and obtained and perfected a security interest in JonesCorp's current and after-acquired equipment, inventory, and accounts by filing a financing statement that month with the appropriate Texas official. Before funding the loan, BankTwo searched the U.C.C. records and found no financing statements filed against JonesCorp.

BankThree made a secured loan to HarrisCorp in November 2008 and obtained and perfected a security interest in HarrisCorp's current and after-acquired equipment, inventory, and accounts by filing a financing statement that month with the appropriate Texas official. Before funding the loan, BankThree searched the U.C.C. records and found no financing statements filed against HarrisCorp.

In January 2009, two priority disputes erupt: BankOne and BankTwo are fighting over the piece of equipment sold by SmithCorp to JonesCorp in February 2007, and BankOne and BankThree are contesting the priority in a piece of equipment purchased by HarrisCorp in October 2007.

A student who is asked to resolve these two priority disputes might rule against BankOne in both cases. BankOne's security interest in the two pieces of equipment was perfected by a filed financing statement. BankTwo's search against "JonesCorp" failed to reveal BankOne's filing. BankThree's search against "HarrisCorp" yielded the same result. BankOne's filing failed to achieve its stated purpose, giving notice of its security interest. Because BankOne's filing failed to accomplish its notice function, its filing should be deemed ineffective. Absent an effective filing, BankOne's security interest is unperfected and is subordinate to the perfected claims held by BankTwo and BankThree.

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financing statements is to put creditors on notice of existing interests in the debtor's property."); *Nw. Acceptance Corp. v. Lynnwood Equip., Inc.*, 841 F.2d 918, 921 (9th Cir. 1988) (observing that the financing statement "serves the purpose of putting subsequent creditors on notice that the debtor's property is encumbered" (quoting *Thorp Commercial Corp. v. Northgate Indus., Inc.*, 654 F.2d 1245, 1248 (8th Cir. 1981))); § 9-502 cmt. 2 (referring to the system of "notice filing").

Reformatted as a syllogism, the analysis might look like this:

**First syllogism (addressing BankOne's continued perfection):**

A financing statement that fails to accomplish its "notice" function is ineffective to perfect a security interest.

Searches performed by BankTwo and BankThree reveal that BankOne's financing statement failed to give "notice" of its security interest in equipment either sold by SmithCorp to JonesCorp or purchased by HarrisCorp following the name change from SmithCorp.

BankOne's financing statement, which failed to accomplish its "notice" function, is ineffective to perfect its security interest in the two pieces of equipment.

**Second syllogism (addressing priority):**

A perfected security interest has priority over an unperfected security interest.<sup>93</sup>

The secured claims held by BankTwo and BankThree in the equipment are perfected by effective filings; the secured claim held by BankOne in the equipment is no longer perfected because the financing statement has become ineffective.

Perfected security interests held by BankTwo and BankThree enjoy priority over the unperfected security interest held by BankOne.

Whether in narrative form or syllogisms, the analysis—buttressed by policy—and conclusions drawn therefrom are logical. Nevertheless, BankOne enjoys priority over both BankTwo and BankThree. Its financing statement continues to perfect the security interest in the equipment sold by SmithCorp to JonesCorp, under a rule that states: "A filed financing statement remains effective with respect to collateral that is sold . . . and in which a security interest . . . continues."<sup>94</sup> Its financing statement also continues to perfect the security interest in the equipment purchased by HarrisCorp shortly after the name change from "SmithCorp," under the rule that states: "the financing statement is effective to perfect a security interest in collateral acquired by the debtor before, or within four months after, the [name] change" but "is not effective to perfect a security interest in collateral acquired by the debtor more than four

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<sup>93</sup> For statutory authority, see § 9-322(a)(2).

<sup>94</sup> § 9-507(a). Observe that the financing statement remains effective post-disposition only if the underlying security interest survives the disposition, a matter addressed in § 9-315(a). BankOne's security interest in the equipment sold by SmithCorp to JonesCorp remains after the sale because BankOne did not authorize the disposition free of its security interest. See § 9-315 cmt. 2 (second paragraph). The moral of the story for BankTwo is that it "must inquire as to [JonesCorp's] source of title and, if circumstances seem to require it, search in the name of a former owner [*e.g.*, "SmithCorp"]." § 9-507 cmt. 3.

months after the [name] change.”<sup>95</sup> Because BankOne filed its financing statement in 2006, long before BankTwo and BankThree filed their financing statements in 2008, BankOne continues to enjoy priority in the disputed collateral,<sup>96</sup> notwithstanding the fact that its continued perfection rests on a financing statement that failed to accomplish its notice function.

This discussion illustrates another possible hurdle to the effective use of syllogisms in Secured Transactions. Article 9 occasionally adopts rules that are inconsistent with policy-based analysis, which may lead to incorrect major premises and, accordingly, erroneous conclusions.

E. “Consistency, madam, is the first of Christian duties.”<sup>97</sup>

Socrates and John Ford<sup>98</sup> have been discussing films which received the most Academy Award nominations in particular years. Ford mentions that *Gone With The Wind*, *All About Eve*, *Ben-Hur*, *Schindler’s List*, and *Titanic* received the most nominations in their respective years.<sup>99</sup> Each film also was

<sup>95</sup> § 9-507(c). This name-change rule requires BankThree to consider the past and the future. BankThree must determine prior names used by HarrisCorp and search for financing statements filed under those prior names (such as “SmithCorp”). BankThree must also monitor HarrisCorp for any future name changes and, if necessary, timely file a name-change amendment within four months of the change. See § 9-507(c)(2) and cmt. 4.

<sup>96</sup> See § 9-322(a)(1) (stating the general rule that a secured party who files or perfects first enjoys priority).

<sup>97</sup> Penned by Charlotte Bronte, and spoken by Mr. Brocklehurst to Mrs. Reed in Chapter 4 of *JANE EYRE*. See CHARLOTTE BRONTE, *JANE EYRE* 28 (Bantam Classic 1981) (1847). Perhaps Bronte’s most beloved work, *JANE EYRE* was originally published in 1847 under the pseudonym “Currer Bell.” See Charlotte Bronte, <http://academic.brooklyn.cuny.edu/english/melani/cs6/bronte.html> (last visited Oct. 24, 2009). One of the more famous film adaptations premiered in 1944 and features Joan Fontaine in the title role and Orson Welles as Edward Rochester. A very young Elizabeth Taylor appears in an uncredited role, and the screenplay is written, in part, by Orson Welles’ co-founder of The Mercury Theatre: John Houseman (who, as noted earlier in footnote 5, portrayed Professor Charles Kingsfield many years later). See *Jane Eyre* 1944, <http://www.imdb.com/title/tt0036969/> (last visited Oct. 24, 2009); Art Pierce, Orson Welles, The Mercury Theatre, and The Campbell Playhouse, <http://www.mercurytheatre.info/history> (last visited Oct. 24, 2009).

<sup>98</sup> John Ford won the Oscar for Best Director four times, a record. The films for which he won the award are *The Informer*, *The Grapes of Wrath*, *How Green Was My Valley*, and *The Quiet Man*. He also received a nomination for *Stagecoach*. Although no one has received as many wins, other famous directors have garnered more nominations, including Woody Allen (six), Frank Capra (six), Martin Scorsese (six), Steven Spielberg (six), Fred Zinnemann (seven), David Lean (seven), Billy Wilder (eight), and William Wyler (twelve). See Best Director Facts & Trivia, <http://www.filmsite.org/bestdirs.html> (last visited Oct. 24, 2009).

<sup>99</sup> See All About Oscar: Academy Award Trivia and Statistics, <http://www.reelclassics.com/Articles/General/oscar-trivia-article.htm> (last visited Oct. 24, 2009) (*All About Eve* and *Titanic* tied with fourteen nominations in their respective years while *Gone With the Wind* was a close runner-up with thirteen.); *Ben-Hur* 1959, <http://www.imdb.com/title/tt0052618/awards> (last visited Oct. 24, 2009) (accumulating twelve nominations); 1993 Academy Awards Winners and History, <http://www.filmsite>

named “Best Picture.”<sup>100</sup> Ford also informs Socrates that *A Streetcar Named Desire*, *Mary Poppins*, *Who’s Afraid of Virginia Woolf?*, *Reds*, and *Tootsie* received the most nominations in their respective years.<sup>101</sup> These films were nominated for, but did not win, the “Best Picture” award.<sup>102</sup> Ford then tells Socrates that *Dreamgirls* led all films released in 2006 with eight nominations.<sup>103</sup> Based on the preceding information, Socrates logically concludes that *Dreamgirls* was a “Best Picture” nominee, if not a winner. Socrates is wrong.<sup>104</sup> *Dreamgirls* is the only film to receive the most Academy Awards nominations in its year of eligibility and not receive a “Best Picture” nomination.<sup>105</sup> So much for precedent!

Article 9 has been known to address a specific concern with a series of rules that render a consistent and predictable result—except, for some unexplained reason, in one instance. As happened to Socrates in the preceding paragraph, this unanticipated departure from what all other related rules suggest is the norm may lead students to logically reach an incorrect conclusion.<sup>106</sup>

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.org/aa93.html (last visited Oct. 24, 2009) (*Schindler’s List* tied *Ben-Hur* with twelve nominations).

<sup>100</sup> See Academy Awards, USA, [http://www.imdb.com/Sections/Awards/Academy\\_Awards\\_USA/](http://www.imdb.com/Sections/Awards/Academy_Awards_USA/) (last visited Oct. 24, 2009).

<sup>101</sup> See 1951 Academy Awards Winners and History, <http://www.filmsite.org/aa51.html> (last visited Oct. 24, 2009) (*A Streetcar Named Desire* earned twelve nominations); 1964 Academy Awards Winners and History, <http://www.filmsite.org/aa64.html> (last visited Oct. 24, 2009) (*Mary Poppins* earned thirteen nominations); 1966 Academy Awards Winners and History, <http://www.filmsite.org/aa66.html> (last visited Oct. 24, 2009) (*Who’s Afraid of Virginia Woolf?* also earned thirteen nominations); 1981 Academy Awards Winners and History, <http://www.filmsite.org/aa81.html> (last visited Oct. 24, 2009) (*Reds* accumulated twelve nominations); 1982 Academy Awards Winners and History, <http://www.filmsite.org/aa82.html> (last visited Oct. 24, 2009) (*Tootsie* had ten nominations).

<sup>102</sup> The respective “Best Picture” films were: *An American in Paris* (1951 Academy Awards Winners and History, *supra* note 101); *My Fair Lady* (1964 Academy Awards Winners and History, *supra* note 101); *A Man For All Seasons* (1966 Academy Awards Winners and History, *supra* note 101); *Chariots Of Fire* (1981 Academy Awards Winners and History, *supra* note 101); and *Gandhi* (1982 Academy Awards Winners and History, *supra* note 101).

<sup>103</sup> See 2006 Academy Awards Winners and History, <http://www.filmsite.org/aa06.html> (last visited Oct. 24, 2009).

<sup>104</sup> The five “Best Picture” nominees in 2006 were *The Departed* (winner), *Babel*, *Letters From Iwo Jima*, *Little Miss Sunshine*, and *The Queen*. See 2006 Academy Awards Winners and History, *supra* note 103.

<sup>105</sup> See No Best Picture Nomination for ‘Dreamgirls,’ <http://www.msnbc.msn.com/id/16767796/> (last visited Oct. 24, 2009).

<sup>106</sup> Asking a student to craft a rule by observing other rules may suggest that I am moving from deductive reasoning to inductive reasoning. Judge Aldisert describes inductive reasoning as:

a form of logic in which big, general principles are divined from observing the outcomes of many small events. In this form of inductive logic, you reason from multiple particulars to the general . . . . Thus, inductive reasoning is a

As a general rule, a filed financing statement is effective for five years.<sup>107</sup> Students may be asked to analyze whether certain post-filing events might shorten the five-year duration of effectiveness. Those events may include the following:

- \* the debtor changes its name from "SmithCorp" to "JonesCorp";
- \* the debtor relocates its entire business from Houston to Dallas (the same state of the original filing) or Chicago (a different state from the original filing);
- \* the debtor converts several units of "inventory" (collateral) to in-house use as "equipment" (not collateral); and
- \* without the secured party's consent, the debtor disposes of some collateral by selling its chattel paper to FinCo (incorporated under the laws of the same state of the original filing) and its accounts to PrimeCo (incorporated under the laws of a different state).

The name change has no immediate impact on the continued effectiveness of the original filing. Under the applicable rule, the filing remains effective through the end of the five-year period to perfect a security interest in collateral acquired by the debtor either before the name change or within four months after the name change.<sup>108</sup> The filing, however, will not remain effective to perfect a security interest in collateral acquired by the debtor more than four months after the name change unless the secured party files a name-change amendment within that four-month period.<sup>109</sup>

The debtor's in-state change of address has no immediate or future impact on the continued effectiveness of the original filing,<sup>110</sup> presumably because a search against the debtor's name after the address change will continue to reveal the original filing.<sup>111</sup> Whether an out-of-state address change may impact the effectiveness of an original filing is dictated by the type of debtor.

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logic of probabilities and generalities, not certainties. It yields workable rules, but not proven truths.

Aldisert, *supra* note 3, at 12-13. Because my concern is with an existing statutory provision, rather than with the creation of a gap-filling rule that may be subject to some discretionary application, I do not believe that I have moved completely into the realm of inductive reasoning. That certainly is not my intent.

<sup>107</sup> See § 9-515(a).

<sup>108</sup> § 9-507(c)(1).

<sup>109</sup> § 9-507(c)(2). A name-change amendment filed more than four months after the name change is effective to perfect a security interest in collateral acquired by the debtor more than four months after the name change, but the effectiveness does not commence until the filing date of the amendment. *Id.* at cmt. 4. This gap in perfection exposes the secured party to a risk of nonpriority against former subordinate creditors who have climbed up the priority ladder.

<sup>110</sup> § 9-507(b).

<sup>111</sup> Financing statements are indexed "according to the name of the debtor." § 9-519(c)(1).

If the debtor is a corporation, limited partnership, or other “registered organization,”<sup>112</sup> then a mere address change has no effect. The correct place to file a financing statement against a registered organization is with the chartering state, whether or not the entity has a physical presence in that state,<sup>113</sup> so the original filing continues to give notice. But notice is frustrated if the out-of-state relocation involves a natural person, or an organization other than a registered organization (e.g., a general partnership), because the proper place to file a financing statement is the state in which the debtor has its principal residence or place of business, respectively.<sup>114</sup> The financing statement will remain effective, but only until the end of the four-month period following the relocation; thereafter, the financing statement is ineffective.<sup>115</sup>

The debtor’s change in the use of its property which converts collateral (e.g., “inventory”) to non-collateral (e.g., “equipment”) has no effect on the continued effectiveness of the financing statement (which lists “inventory” but not “equipment” as collateral).<sup>116</sup>

The debtor’s sale of assets to an in-state purchaser has no impact on the original filing. The debtor’s sale of assets to an

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<sup>112</sup> See § 9-102(a)(70) (defining “registered organization”) and cmt. 11 (listing corporations, limited liability companies, and limited partnerships as examples).

<sup>113</sup> See §§ 9-301(1) (indicating that “while a debtor is located in a jurisdiction, the local law of that jurisdiction governs perfection”); 9-307(e) (stating that a registered organization “organized under the law of a State is located in that State”).

<sup>114</sup> See §§ 9-301(1); 9-307(b)(1) (individuals), (2) (organizations with one place of business). If the debtor is an organization with multiple business locations, the debtor is located in the state of its “chief executive office.” § 9-307(b)(3) and cmt. 2 (defining “chief executive office” as “the place from which the debtor manages the main part of its business operations or other affairs” and “is the place where persons dealing with the debtor would normally look for credit information”).

<sup>115</sup> § 9-316(a)(2). If the four-month period ends after the standard five-year period of effectiveness, then the out-of-state relocation renders the financing statement ineffective at the end of that five-year period. § 9-316(a) (stating that perfection continues “until the earlie[r] of: (1) the time perfection would have ceased under the law of that jurisdiction; [and] (2) the expiration of four months after a change of the debtor’s location to another jurisdiction”).

<sup>116</sup> § 9-507(b) (indicating that, unless either the debtor has changed its name or the facts involve a “new debtor” and application of § 9-508, “a financing statement is not rendered ineffective if, after the financing statement is filed, the information provided in the financing statement becomes seriously misleading”). See also § 9-338 cmt. 3 (“Except as provided in Section 9-507 with respect to changes in the debtor’s name, an otherwise effective financing statement does not become ineffective if the information contained in it becomes inaccurate.”).

Implicit in the analysis is the assumption that the property is never subject to a certificate-of-title law. A financing statement will perfect a security interest in a dealer’s inventory of motor vehicles. § 9-311(d). If, however, the dealer converts one of the vehicles to in-house use as equipment, the financing statement no longer perfects the security interest in that vehicle. Instead, the secured party must comply with the certificate-of-title law. See § 9-311 cmt. 4 (last sentence).

out-of-state purchaser does impact the original filing, although the impact is not immediate. The underlying security interests in the chattel paper and accounts survive the dispositions,<sup>117</sup> and the original filing continues to perfect those security interests,<sup>118</sup> even though a search against the purchasers will not reveal the filing against the seller/debtor. The financing statement remains effective to perfect the security interest in the chattel paper sold to the in-state purchaser until the end of its standard five-year duration. But the filing remains effective to perfect the security interest in the accounts sold to the out-of-state buyer for only one year.<sup>119</sup>

All of these post-filing events frustrate the notice function in whole (the financing statement cannot be found) or in part (the filing can be found but contains incorrect information). Nevertheless, these examples illustrate that post-filing mischief never has an *immediate* impact on the continued effectiveness of the financing statement. At best, the filing remains effective for the remainder of its standard five-year life; at worst, the filing remains effective for a grace period of either four months or one year. A secured party, therefore, should periodically monitor its debtor's behavior, but it has no concerns that any misbehavior will abruptly terminate the effectiveness of its filing.<sup>120</sup>

So consider one more example. Lender makes a \$1 million loan to SmithCorp, a Texas corporation, secured by an enforceable security interest in SmithCorp's current and after-acquired inventory. Lender files its financing statement in Texas. Two years later, SmithCorp merges with and into WilliamsCorp, a Delaware corporation. WilliamsCorp, the

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<sup>117</sup> § 9-315(a)(1).

<sup>118</sup> § 9-507(a). Nevertheless, the purchaser may have a superior claim to the chattel paper under § 9-330(a) or (b).

<sup>119</sup> § 9-316(a)(3) (stating that, unless the standard five-year life of a filing will end earlier and trigger application of subsection (a)(1), a security interest remains perfected until "the expiration of one year after a transfer of collateral to a person that thereby becomes a debtor and is located in another jurisdiction"); § 9-316 cmt. 2 (observing that the longer one-year period (rather than a four-month period) "is necessary, because, even with the exercise of due diligence, the secured party may be unable to discover that the collateral has been transferred to a person located in another jurisdiction"). The purchaser of the accounts, PrimeCo, has become a "debtor" by acquiring an interest in property that remains "collateral" for the debt owed by the seller to its creditor. § 9-102(a)(28)(A). PrimeCo is "located in another jurisdiction" because it is incorporated under the laws of a state other than the state in which the financing statement was filed against the seller.

<sup>120</sup> The central issue is whether mischief which undermines the notice function of the filing creates a risk that should be borne by the filer, or the searcher. Perhaps the best discussion of this issue is found in PEB Commentary No. 3, dated March 10, 1990 (reprinted in THE AMERICAN LAW INSTITUTE, UNIFORM COMMERCIAL CODE 1156-59 (2009)), which addresses whether unauthorized asset dispositions should create a refiling obligation for the filer, or a title-tracing obligation for the searcher.

surviving entity, acquires all of SmithCorp's assets and assumes all of SmithCorp's debts. Three months later, WilliamsCorp makes an inventory purchase of \$100,000. *Does Lender hold a perfected security interest in this post-merger inventory?*

Initially, an astute student may question whether Lender can claim *any* security interest in the inventory purchased by WilliamsCorp, as Lender's security agreement was with SmithCorp, not WilliamsCorp. And absent a security agreement, no security interest exists.<sup>121</sup> But WilliamsCorp's acquisition of SmithCorp's assets and assumption of its debts makes WilliamsCorp a "new debtor,"<sup>122</sup> so SmithCorp's security agreement binds WilliamsCorp and no new security agreement is necessary to create an enforceable security interest in the post-merger inventory acquired by WilliamsCorp.<sup>123</sup>

The student then addresses the question asked: Does Lender have a *perfected* security interest in the post-merger inventory? Lender's filing is recorded against "SmithCorp" and will not be found by searching against "WilliamsCorp." Additionally, Lender filed its financing statement where SmithCorp is incorporated (Texas), but WilliamsCorp is incorporated in a different state (Delaware). Notwithstanding these concerns, however, the student may logically conclude—based on earlier observations of the effect, if any, that post-filing mischief may have on a financing statement—that Lender's filing remains effective for at least four months (if not longer). The student may even cite § 9-508, which states that the financing statement remains effective to perfect a security interest in inventory acquired by WilliamsCorp within four months after the merger, even though the difference between the name of the original debtor—"SmithCorp"—and the new debtor—"WilliamsCorp"—renders the filing seriously misleading.<sup>124</sup>

But that result is wrong, although the error is far from obvious.

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<sup>121</sup> See § 9-203(b)(3)(A)–(D).

<sup>122</sup> See §§ 9-102(a)(56) (defining "new debtor" as "a person [WilliamsCorp] that becomes bound as debtor under Section 9-203(d) by a security agreement previously entered into by another person [SmithCorp]"); 9-203(d) (stating that a "person [WilliamsCorp] becomes bound as debtor by a security agreement entered into by another person [SmithCorp] if, by operation of law other than this article or by contract . . . (2) the person [WilliamsCorp] becomes generally obligated for the obligations of the other person [SmithCorp] . . . and acquires . . . all or substantially all of the assets of the other person [SmithCorp]").

<sup>123</sup> See § 9-203(e) and cmt. 7.

<sup>124</sup> See § 9-508(b). Lender can perfect a security interest in inventory acquired after the four-month period by filing a financing statement against "WilliamsCorp" in Delaware. § 9-508(b)(2).

The four-month rule of § 9-508, codified in subsection (b) and paraphrased above, applies only if “a filed financing statement . . . is effective under subsection (a).”<sup>125</sup> Subsection (a) states in relevant part:

[A] filed financing statement naming an original debtor [SmithCorp] is effective to perfect a security interest in collateral in which a new debtor [WilliamsCorp] has or acquires rights *to the extent that the financing statement would have been effective had the original debtor [SmithCorp] acquired rights in the collateral.*<sup>126</sup>

What does the quoted language mean? I read it as requiring the collateral acquired by the new debtor to fall within the description of the collateral found in the financing statement filed against the original debtor (an interpretation shared by one of the drafters<sup>127</sup>). For example, a filing against SmithCorp’s “inventory” is effective to perfect a security interest in WilliamsCorp’s “inventory.” The language cannot address any concern with the difference between the names of the original debtor (“SmithCorp”) and the new debtor (“WilliamsCorp”), because that matter is expressly addressed by subsection (b). And if the language is intended to address any jurisdictional differences between the original debtor (located in Texas) and the new debtor (located in Delaware), one might reasonably argue that the drafters should have—and could have—been less obtuse,<sup>128</sup> especially since the difference in jurisdictions does not prevent the filing from remaining effective to perfect a security interest in the collateral transferred from the original debtor to the new debtor for as long as one year.<sup>129</sup> It will be the rare student who reads the statutory language of § 9-508 and appreciates that the change in jurisdiction *immediately* renders

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<sup>125</sup> § 9-508(b).

<sup>126</sup> § 9-508(a) (emphasis added).

<sup>127</sup> See Harry C. Sigman, *The Filing System Under Revised Article 9*, 73 AM. BANKR. L.J. 61, 81 (1999) (noting that § 9-508 continues the effectiveness of a filed financing statement against a new debtor “to the extent that the financing statement would have been effective had the original debtor acquired rights in the collateral, e.g., *the collateral falls within the indication of collateral provided in the financing statement*”) (emphasis added); *id.* at 61 n.\* (indicating that Mr. Sigman was the ALI representative on the NCCUSL Article 9 Drafting Committee).

<sup>128</sup> For example, subsection (a) § 9-508 could have been drafted as follows (revised language italicized):

Except as otherwise provided in this section, a filed financing statement naming an original debtor is effective to perfect a security interest in collateral in which a new debtor, *located in the same jurisdiction as the original debtor*, has or acquires rights to the extent that the financing statement would have been effective had the original debtor acquired rights in the collateral.

Alternatively, the following sentence could have been added to the end of subsection (c): “This section also does not apply if the original debtor and the new debtor are located in different jurisdictions.”

<sup>129</sup> See §§ 9-508(c), 9-507(a), and 9-316(a)(3).

the filing ineffective to perfect a security interest in any post-merger collateral. But buried in the Official Comments to § 9-508 is evidence of that intended result:

Moreover, if the original debtor and the new debtor are located in different jurisdictions, a filing against the original debtor would not be effective to perfect a security interest in collateral that the new debtor acquires or has acquired from a person other than the original debtor. See Example 5, Section 9-316, Comment 2.<sup>130</sup>

Whether confronted with the confusing language of § 9-508(a), or the clear message tucked away in Official Comment 4, the student is left to revise her earlier analysis and conclude that Lender's original filing is not effective to perfect its security interest in any post-merger inventory acquired by WilliamsCorp.

The foregoing analysis reveals yet another possible obstacle to the effective use of syllogisms in Secured Transactions. Article 9 occasionally adopts a rule that, for no apparent reason, yields a result so unexpected and inconsistent with the norm that a logical approach to its understanding is undermined.

F. "If the law supposes that," said Mr. Bumble, . . . "the law is a ass—a idiot."<sup>131</sup>

While attending the Houston Livestock Show and Rodeo,<sup>132</sup> Socrates purchases a pair of cowboy boots for \$200.<sup>133</sup> After

<sup>130</sup> § 9-508 cmt. 4. As Kenny Bania might exclaim, "That's gold, Jerry! Gold!" See The Fatigues, <http://www.seinfeldscripts.com/TheFatigues.html> (last visited Oct. 24, 2009).

<sup>131</sup> CHARLES DICKENS, OLIVER TWIST 463 (The New American Library, Inc. 1961) (1838). Associate Justice Harry A. Blackmun is one of two members of the Supreme Court of the United States to drop this quote into an opinion. See *Estate of Wilson v. Aiken Industries, Inc.*, 439 U.S. 877, 880 n.3 (1978) (Blackmun, J., concurring). (Justice John Paul Stevens also borrowed the line in *Califano v. Goldfarb*, 430 U.S. 199, 223–24 n.10 (1977) (Stevens, J., concurring).) Justice Blackmun took his judicial oath on June 9, 1970, exactly one hundred years to the day of the death of Charles Dickens. See *Members of the Supreme Court of the United States*, <http://www.supremecourtus.gov/about/members.pdf> (last visited Oct. 21, 2009); Charles Dickens Biography and Works, <http://www.onlineliterature.com/dickens/> (last visited Oct. 21, 2009).

<sup>132</sup> According to its website, the HLSR is the third largest fair or festival in North America (the general attendance in 2009 exceeded 1.8 million) and the largest rodeo in the world (26,285 livestock competitions and horse show entries in 2009). See Frequently Asked Questions Houston Livestock Show and Rodeo, <http://www.hlsr.com/about/faq.aspx> (follow the "How does the Show impact the city?" hyperlink and the "What's unique about the Houston Livestock Show?" hyperlink) (last visited Oct. 21, 2009). Entertainers from "A" to "Z" have performed on its concert stages through the years, including Ashanti, Tony Bennett, Johnny Cash, Bill Cosby, Bob Dylan, Alicia Keys, Barry Manilow, Olivia Newton-John, Elvis Presley, REO Speedwagon, Randy Travis, and ZZ Top. See Entertainment History Houston Livestock Show and Rodeo, <http://www.hlsr.com/concerts/past-performers.aspx> (last visited Oct. 21, 2009).

<sup>133</sup> Can you believe that someone would pay \$75,000 for a pair of cowboy boots? See Neal Santelmann, *Most Expensive Cowboy Boots*, April 4, 2006, [http://www.forbes.com/2006/04/03/cowboy-boots-expensive\\_cx\\_ns\\_0404feat.html](http://www.forbes.com/2006/04/03/cowboy-boots-expensive_cx_ns_0404feat.html).

returning to his hotel, Socrates decides to take a walk in his new footwear. While waiting for a streetlight to change, a law enforcement officer hits the siren, jumps out of the car, and arrests Socrates. Dumbfounded, Socrates asks, "What's the charge, officer?" The officer replies, "It is a misdemeanor in Texas to wear cowboy boots while adorned in a toga." And Socrates retorts, "Well that's just silly."<sup>134</sup>

Whatever your word choice (silly, stupid, idiotic, dumb, etc.), some laws just make no sense. When learning those laws, it may be best to park your deductive reasoning at the classroom door. That suggestion just may be appropriate when teaching one particular (and, in my opinion, "silly") provision of Article 9. Consider the following hypothetical.

Meredith, an architect, wants to buy a Steinway grand piano for her home. She cannot afford to buy a new piano from her local Steinway dealer,<sup>135</sup> so she has been reviewing advertisements posted by private owners in the weekend newspaper. Meredith visits the home of one seller, whose recently-deceased spouse was the family musician who played for personal satisfaction. After playing the piano for twenty minutes, she agrees to pay the asking price of \$22,000 and takes delivery that week. Eight months later, Friendly Finance contacts Meredith and informs her that it financed the seller's purchase of the piano and continues to hold a perfected security interest in it. Friendly Finance informs Meredith that if she does not pay the seller's unpaid debt of \$14,000, then Friendly Finance will exercise its contractual and statutory rights and remedies, including repossessing and selling the piano. Meredith had no prior knowledge of her seller's financing arrangement or Friendly Finance's security interest. She has no intention of paying \$14,000 to make this problem disappear and tells Friendly Finance to pursue collection from her seller, who

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<sup>134</sup> To my limited knowledge, Socrates has not violated any actual law. Apparently, however, Texas does have (or has had) some "silly" laws. See *Stupid Texas Laws*, [http://www.idiotlaws.com/dumb\\_laws/texas/](http://www.idiotlaws.com/dumb_laws/texas/) (last visited Oct. 21, 2009).

<sup>135</sup> Steinway & Sons, formed in 1853, builds approximately 5,000 pianos each year, and each piano takes about one year to craft. See *Steinway Piano: Through the Years*, May 21, 2008, <http://www.articlesbase.com/music-articles/-steinway-piano-through-the-years-421850.html>. I purchased a new Steinway baby grand piano in the mid-1990's for approximately \$24,000, so a new Steinway grand piano that the typical consumer would purchase for personal use probably costs at least \$30,000–\$35,000 today. Several years ago, singer George Michael paid over \$2 million for the upright Steinway piano on which John Lennon composed "*Imagine*." See Stephen M. Silverman, *George Michael Buys Lennon Piano*, PEOPLE MAGAZINE, Oct. 23, 1997, <http://www.people.com/people/article/0,,621306,00.html>. Readers interested in learning more about Steinway pianos may wish to read RONALD V. RATCLIFFE, *STEINWAY* (1989) or view the documentary movie *Note by Note: The Making of the Steinway L1037* (Plow Productions, LLC 2007).

received \$22,000 from Meredith. *Did Meredith acquire the Steinway grand piano subject to, or free and clear of, Friendly Finance's security interest?*

Most students will favor Meredith in this dispute. She purchased the piano for a fair price, and she had no knowledge of the security interest. Meredith is an innocent purchaser for value, so Steinway's recourse should be limited to the seller, who received sales proceeds more than sufficient to pay off the purchase debt.<sup>136</sup>

Sounds great, right? That may be the result under Article 9. Then again, it may not. The correct result probably will turn on a single factor: whether Friendly Finance filed a financing statement.

As a general rule, a security interest remains effective against purchasers of the collateral, unless the secured party has authorized the sale free of (rather than subject to) its security interest.<sup>137</sup> Apparently Friendly Finance did not consent to its debtor's sale of the piano, so its security interest survived the disposition unless Article 9 provides buyers with protection.

The primary carve outs for buyers of goods are stated in § 9-320. Subsection (a) states that "a buyer in the ordinary course of business . . . takes free of a security interest created by the buyer's seller, even if the security interest is perfected and the buyer knows of its existence."<sup>138</sup> This rule permits consumers and non-consumers to purchase items at Wal-Mart, Target, Home Depot, Barnes & Noble, and other retailers without being concerned that the items serve as inventory collateral and may be subject to superior property claims held by an unknown creditor.<sup>139</sup> Meredith's seller was not in the business of selling pianos, so subsection (a) offers her no protection.

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<sup>136</sup> As a general rule, a creditor has an enforceable (and often perfected) security interest in proceeds traceable to its collateral. See §§ 9-203(f); 9-315(a)(2), (c), (d). See also § 9-102(a)(64) (defining "proceeds").

<sup>137</sup> See §§ 9-201(a) (stating the general rule that "a security agreement is effective according to its terms . . . against purchasers of the collateral"); 9-315(a)(1) (stating the general rule that "a security interest . . . continues in collateral notwithstanding sale . . . or other disposition thereof unless the secured party authorized the disposition free of the security interest").

<sup>138</sup> § 9-320(a). See also §§ 1-201(b)(9) (defining "buyer in ordinary course of business"); 9-102(c) (incorporating Article 1 definitions).

<sup>139</sup> The buyer who is purchasing a unit of inventory may not need the protection of § 9-320(a). Many secured parties consent to inventory dispositions free and clear of their security interests; those security interests, then, effectively terminate at the point of sale. See § 9-315(a)(1). See also § 9-320 cmt. 6 ("If the secured party authorized the sale in an express agreement or otherwise, the buyer takes free under Section 9-315(a) without regard to the limitations of this section.").

But perhaps Meredith is protected by subsection (b), which permits her to acquire the piano free of the security interest held by Friendly Finance if five conditions are met. First, her seller must have used the piano “primarily for personal, family, or household purposes.”<sup>140</sup> Rephrased, the piano must have been a “consumer good” in the hands of her seller.<sup>141</sup> Meredith can prove this condition, as the seller’s spouse played the piano for personal enjoyment. Second, Meredith must have bought the piano without knowledge of Friendly Finance’s security interest,<sup>142</sup> a fact which she can prove. Third, she must give “value,”<sup>143</sup> met by her \$22,000 payment. Fourth, the piano must be a “consumer good” in Meredith’s hands.<sup>144</sup> Meredith is an architect, not a professional musician, so she can satisfy this condition. And fifth, Meredith must have purchased the piano before Friendly Finance filed a financing statement against it.<sup>145</sup>

Subsection (b), sometimes referred to as the “garage sale” exception,<sup>146</sup> applies only if the debtor sells a consumer good. The overwhelming number of security interests in consumer goods are purchase-money security interests.<sup>147</sup> Because Friendly Finance financed its debtor’s purchase of the piano, which secures repayment of the credit extended, its security interest is a purchase-money security interest.<sup>148</sup> The debtor used the piano as a consumer good, so the purchase-money security interest was automatically perfected at attachment.<sup>149</sup> Therefore, Friendly Finance’s sole purpose in filing a financing statement is *not to perfect* its security interest, *but to protect* its security interest—

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<sup>140</sup> § 9-320(b).

<sup>141</sup> See § 9-102(a)(23) (defining “consumer goods” as “goods that are used or bought for use primarily for personal, family, or household purposes”).

<sup>142</sup> § 9-320(b)(1).

<sup>143</sup> *Id.* at (b)(2). See also §§ 1-204 (defining “value” to include “any consideration sufficient to support a simple contract”); 9-102(c) (incorporating definitions from Article 1).

<sup>144</sup> § 9-320(b)(3).

<sup>145</sup> *Id.* at (b)(4).

<sup>146</sup> See WILLIAM H. LAWRENCE, ET AL., UNDERSTANDING SECURED TRANSACTIONS 268 (4th ed. 2007) (observing that § 9-320(b) is “sometimes referred to as the ‘garage-sale’ rule”); Robert M. Lloyd, *The New Article 9: Its Impact on Tennessee Law (Part II)*, 67 TENN. L. REV. 329, 342 (2000) (noting that former § 9-307(2)—the predecessor statute to § 9-320(b)—was “commonly called the ‘garage sale exception.’”). Professor Lloyd notes the irony of the label: “In spite of its name, the rule is not important in the garage sale situation, where the lender is unlikely to try to track down its collateral. Instead, the rule becomes important when consumers buy and sell big-ticket items like boats, expensive guns, or jewelry.” *Id.* at 342.

<sup>147</sup> There are at least two reasons for this, one practical and the other legal. First, most consumer goods have insufficient value to service any debt other than the purchase-money debt. Second, a secured party who claims a non-PMSI in a household good may incur the wrath of the Federal Trade Commission. See 16 C.F.R. § 444.2(a)(4) (2009).

<sup>148</sup> See § 9-103(a), (b).

<sup>149</sup> See § 9-309(1).

against a possible property claim asserted under § 9-320(b) by an unauthorized consumer purchaser of the collateral, such as Meredith.

So Meredith wins if Friendly Finance did not file, but she loses if Friendly Finance filed.

But why should Meredith's victory or defeat turn on whether Friendly Finance filed a financing statement? The purpose of filing a financing statement is to give notice of a possible security interest in the collateral.<sup>150</sup> Implicit in that policy, however, is the premise that the party to whom notice is directed *will search the public records and discover the filing*. But the average consumer who is purchasing an expensive item—from a neighbor, a co-worker, or a stranger, and in response to a casual conversation, a bulletin-board announcement, a newspaper advertisement, or an online solicitation—has never heard of U.C.C. Article 9 (I'm shocked!) or appreciate (much less know where and how to discover) that a financing statement (“financial statement?”<sup>151</sup>) may have been filed against the item. Article 9 should indeed resolve the potential dispute between Friendly Finance and Meredith, but Meredith's victory or defeat should not turn on a fortuitous event whose purpose is divorced from reality.<sup>152</sup>

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<sup>150</sup> See *supra* note 92.

<sup>151</sup> As I grade Secured Transactions exams I tell myself that the one error for which I will subtract points is an incorrect reference to a “*financial* statement” instead of a “*financing* statement.” But then I recall that judges often make the same mistake. See, e.g., *HomeAlert Corp. v. Concert Co.*, No. 08-912, 2008 WL 5134756, at \*2 (W.D. Pa. Dec. 5, 2008) (referring to “the filing of a UCC Financial Statement Amendment”); *Whoops Transport, Inc. v. Blue Ribbon Commodity Traders, Inc.*, 2008 WL 2367213, at \*1 (D. Puerto Rico June 6, 2008) (“Bancorp filed a financial statement concerning the security interest”); *Carlmont Capital Special Purpose Corp. II v. Healthcare for Women, S.C.*, No. 2:07-cv-1018-RLH-GWF, 2008 WL 150372, at \*2 (D. Nev. Jan. 10, 2008) (“HfW filed UCC-1 financial statements”); *Heck v. Buhler*, 07-21-C, 2007 WL 4256967, at \*4 n.5 (M.D. La. Nov. 30, 2007) (“he filed his UCC-1 Financial Statement”); *U.S. v. Pinkston*, SA-06-CA-0732 OG (NN), 2007 WL 1437690, at \*2 (W.D. Tex. May 14, 2007) (“the government presented the UCC Financial Statement”); *Agriliance, L.L.C. v. Farmpro Serv., Inc.*, 328 F. Supp. 2d 958, 966 (S.D. Iowa 2003) (“filed the appropriate financial statement”); *EH Yacht, LLC v. Egg Harbor, LLC*, 84 F. Supp. 2d 556, 560 n.2 (D.N.J. 2000) (“the UCC financial statement”); *21 West Lancaster Corp. v. Main Line Restaurant, Inc.*, 614 F. Supp. 202, 203 (E.D. Pa. 1985) (“financial statements were timely filed”); *U.S. v. Trans-World Bank*, 382 F. Supp. 1100, 1103 (C.D. Cal. 1974) (“a financial statement filed with the California Secretary of State”); *In re Tamis*, 398 B.R. 124, 126 (Bankr. D.N.J. Dec. 17, 2008) (“The Chase security interest was perfected by the recordation of a UCC-1 financial statement”); *1st Bank v. Windler*, 60 P.3d 998, 999 (Mont. 2002) (“two financial statements filed in 1990 and 1994”); *LBM, Inc. v. Rushmore State Bank*, 543 N.W.2d 780, 785 (S.D. 1996) (“a valid and filed financial statement”); *Texas Beef Cattle Co. v. Green*, 883 S.W.2d 415, 425 (Tex. Ct. App. 1994) (“filed financial statements”); *Simmons Oil Corp. v. Holly Corp.*, 796 P.2d 189, 197 (Mont. 1990) (“Holly filed UCC financial statements in Montana.”).

<sup>152</sup> See Linda J. Peltier, *Buyers of Used Goods and the Problem of Hidden Security Interests: A New Proposal to Modify Section 9-307 of the Uniform Commercial Code*, 36

The preceding discussion illustrates that Article 9 occasionally adopts a rule that appears to be so illogical as to render futile any attempt to understand it logically. And illogical rules can frustrate the ability to learn the core principles in a Secured Transactions course through syllogisms.

G. “There is no exception to the rule that every rule has an exception.”<sup>153</sup>

Socrates and legendary actor Clark Gable are discussing the “leap year” phenomenon. Clark is a reluctant participant, given that on February 29, 1940, he failed to win the Oscar for Best Actor for his portrayal of Rhett Butler in *Gone With The Wind*.<sup>154</sup>

HASTINGS L.J. 215, 253 n.164 (1985) (observing that “the outcome under § 9-307(2) [the predecessor statute to § 9-320(b)] would seem more dependent upon fortuity than reason”).

<sup>153</sup> James Thurber (1894-1961). See James Thurber Quotes, [http://www.brainyquote.com/quotes/authors/j/james\\_thurber\\_3.html](http://www.brainyquote.com/quotes/authors/j/james_thurber_3.html) (last visited Oct. 21, 2009). Thurber had two brothers, one of whom shot James in the eye with an arrow during a game of “William Tell,” leading to blindness in that eye. See The Thurber House, <http://www.thurberhouse.org/james/james.html> (last visited Oct. 21, 2009). Almost ninety years earlier, another little boy—who later became famous throughout the world—had an eye accident. The boy was only three years old when he entered the workshop of his father, a harness maker. As he had seen his father do on many occasions, the boy took a sharp tool and tried to cut a piece of leather. The tool slipped and entered his eye. The injured eye became infected, and the infection spread to his other eye, leaving the boy blind. But his blindness led him, at the age of fifteen, to develop a system of communication that has been used by millions of blind people to read and write. The little boy’s name? Louis Braille. See A New Method: The Story of Louis Braille, <http://louisbrailleschool.org/resources/louis-braille/louis-braille-childhood/> (last visited Oct. 21, 2009).

<sup>154</sup> The award went to Robert Donat, for his portrayal of a shy “classics” teacher at an English boarding school, in *Goodbye, Mr. Chips*. See 1939 Academy Awards Winners and History, <http://www.filmsite.org/aa39.html> (last visited Oct. 21, 2009). *Gone With The Wind* did win several other Academy Awards, including the award for Best Picture, Best Director (Victor Fleming), Best Actress (Vivien Leigh), Best Screenplay, and Best Supporting Actress (Hattie McDaniel, the first African-American nominee and winner). *Gone With the Wind* (1939), <http://www.imdb.com/title/tt0031381/awards> (last visited Oct. 21, 2009). The film is the earliest of only four films to win the awards for Best Picture, Best Director, Best Actress, and Best Screenplay and not capture the award for Best Actor. The other three films are: *Mrs. Miniver* (Walter Pidgeon was nominated but lost to James Cagney in *Yankee Doodle Dandy*) (see 1942 Academy Awards Winners and History, <http://www.filmsite.org/aa42.html> (last visited Oct. 21, 2009)); *Annie Hall* (Woody Allen was nominated but lost to Richard Dreyfuss in *The Goodbye Girl*) (see 1977 Academy Awards Winners and History, <http://www.filmsite.org/aa77.html> (last visited Oct. 21, 2009)); and *Terms of Endearment* (Jack Nicholson was nominated for, and won, the Oscar for Best Supporting Actor; the Oscar for Best Actor was awarded to Robert Duvall in *Tender Mercies*) (see 1983 Academy Awards Winners and History, <http://www.filmsite.org/aa83.html> (last visited Oct. 21, 2009)). Twelve films have captured the awards for Best Picture, Best Director, Best Actor, and Best Screenplay but not the award for Best Actress: *The Best Years Of Our Lives*, *On The Waterfront* (although Eva Marie Saint won the Oscar for Best Supporting Actress), *The Bridge On The River Kwai*, *A Man For All Seasons*, *Patton*, *The French Connection*, *Kramer vs. Kramer* (although Meryl Streep won the Oscar for Best Supporting Actress), *Gandhi*, *Amadeus*, *Rain Man*, *Forrest Gump*, and *American Beauty*. See Oscar’s Greatest Films and Sweeps and its Most Surprising Loser, Jan. 29, 2008, [http://www.associatedcontent.com/article/560801/oscars\\_greatest\\_films\\_and\\_sweeps\\_and.html?cat=37](http://www.associatedcontent.com/article/560801/oscars_greatest_films_and_sweeps_and.html?cat=37). Only three films in the history of the Academy Awards

Socrates states the general rule: a year divisible by four, such as 1960 and 2004, is a leap year. “So 1900 was a leap year, too,” suggests Clark. “No,” says Socrates. “The general rule is subject to an exception: a year divisible by 100 is not a leap year.” Clark replies, “Then 2000 was *not* a leap year.” “Sorry, no,” says Socrates. “A year divisible by 400 *is* a leap year.”<sup>155</sup> Clark, expressing some annoyance, responds, “So your general rule is subject to an exception, which itself is subject to an exception.” “Right!” exclaims Socrates. “What do you think of that?” To which Clark retorts, “Frankly, my dear, . . .”<sup>156</sup>

When rules are subject to a myriad of exceptions, crafting the major premise of a syllogism becomes challenging. “All men are mortal” is a premise much easier to master than “All men are mortal, other than any male who (i) is a Southern Baptist with a law degree from BYU; (ii) teaches commercial law; (iii) follows the St. Louis Cardinals baseball team; (iv) enjoys playing the piano; (v) favors novels authored by Harlan Coben, Pat Conroy, Jeff Shaara, and Daniel Silva; and (vi) has two beautiful daughters and a ‘Proverbs 31’ wife.”<sup>157</sup> To a great extent, Article 9 raises the same concern: drawing a major premise from its rules can be difficult because many of its rules are riddled with exceptions. In fact, some variation of the phrase—“except as otherwise provided in subsection [x]”—appears *more than 100 times* in its text!<sup>158</sup>

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have captured the so-called “grand slam,” winning the Oscar for Best Picture, Best Director, Best Actress, Best Actor, and Best Screenplay: *It Happened One Night*, *One Flew Over The Cuckoo’s Nest*, and *The Silence Of The Lambs*. *Id.*

<sup>155</sup> For a general discussion of the leap year phenomenon, see Burkald Polster & Marty Ross, *Leaping to conclusions*, Mar. 3, 2008, <http://www.theage.com.au/news/education-news/leaping-to-conclusions/2008/02/29/1204226993941.html>.

<sup>156</sup> The full quote—“*Frankly, my dear, I don’t give a damn.*”—comes in at #1 on the American Film Institute’s list of “*AFI’s 100 Years . . . 100 Movie Quotes.*” See <http://connect.afi.com/site/DocServer/quotes100.pdf?docID=242> (last visited Oct. 21, 2009). Two other lines from *Gone With The Wind* also made the list: “*After all, tomorrow is another day!*” (#31) and “*As God is my witness, I’ll never be hungry again.*” (#59). *Id.* *Casablanca* has the most lines on the list (six). *Id.*

<sup>157</sup> Hey, I guess I must be immortal!

<sup>158</sup> See §§ 9-105(1), 9-108(a), 9-108(b), 9-108(b)(3), 9-108(b)(6), 9-108(d), 9-109(a), 9-201(a), 9-202, 9-203(b), 9-204(a), 9-207(a), 9-207(b), 9-207(c), 9-209(a), 9-301 (preamble), 9-301(1), 9-301(3), 9-305(a), 9-307(b), 9-307(f), 9-308(a), 9-309(1), 9-310(a), 9-311(a), 9-311(b), 9-311(c), 9-312(b), 9-312(b)(2), 9-313(a), 9-315(a), 9-316(d), 9-317(a)(2), 9-317(b), 9-317(c), 9-317(e), 9-319(a), 9-320(a), 9-320(b), 9-322(a), 9-322(c), 9-322(d), 9-323(a), 9-323(b), 9-323(d), 9-323(f), 9-324(a) (twice), 9-324(b) (twice), 9-324(d) (twice), 9-324(f) (twice), 9-325(a), 9-327(2), 9-327(3), 9-327(3), 9-330(c), 9-330(d), 9-334(d), 9-334(h), 9-335(c), 9-336(e), 9-340(a), 9-340(b), 9-341, 9-401(a), 9-403(b), 9-403(f), 9-404(b), 9-406(d), 9-406(f), 9-407(a), 9-407(b), 9-408(a), 9-501(a), 9-502(b), 9-506(b), 9-507(b), 9-508(a), 9-512(b), 9-513(d) (twice), 9-514(a), 9-514(b), 9-515(a), 9-515(b), 9-515(e), 9-516(a), 9-519(c), 9-525(a), 9-525(b), 9-601(a), 9-601(d), 9-601(g), 9-602, 9-611(b), 9-612(a), 9-620(a), 9-625(c), 9-626(a)(3), 9-702(a), 9-702(b), 9-703(b), 9-705(c), and 9-707(c). As used in the context of an exception, the phrase “subject to” also appears several times. See §§ 9-306(a), 9-322(d), 9-322(f), 9-324(b), 9-324(d), 9-326(a), 9-403(e), 9-404(b), 9-404(c),

Take, for example, the general rule that resolves priority disputes between two perfected secured creditors: priority is awarded to the secured party who first files its financing statement or otherwise perfects its security interest (whichever is earlier).<sup>159</sup> Given that a security interest in almost all forms of collateral can be perfected by a financing statement,<sup>160</sup> the practical effect is that the rule awards priority to the party who files first. The statute clearly warns the reader that the rule is subject to other exceptions found either in § 9-322<sup>161</sup> or elsewhere in Part 3 of Article 9.<sup>162</sup>

So consider the following, and rather typical, scenario. Lender makes a \$2 million loan on July 20<sup>163</sup> to BizCorp, a Texas corporation that sells and leases office and residential furniture through its stores located in Houston, Dallas, and San Antonio. To secure repayment, BizCorp executes on that date a written security agreement that grants to Lender a security interest in BizCorp's "*accounts, chattel paper, commercial tort claims, deposit accounts, documents, equipment, general intangibles, instruments, inventory, investment property, and letter-of-credit rights.*" The security agreement includes an after-acquired property clause and a future advance clause, and it additionally describes the commercial tort claims that exist on July 20.<sup>164</sup> Lender files its financing statement (accurate and complete in all respects and authorized by BizCorp) on July 20. A few days later, Lender's counsel receives a U.C.C. search report from the Texas Secretary of State dated July 30, showing no filings

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9-405(c), 9-406(a), 9-406(b), 9-406(c), 9-406(d), 9-406(f), 9-406(g), 9-406(h), 9-502(a), 9-512(a) (twice), 9-604(b), 9-604(c), and 9-625(b).

<sup>159</sup> § 9-322(a)(1).

<sup>160</sup> Notable exceptions include collateral subject to perfection requirements stated in other state or federal law (e.g., motor vehicles which require lien notation on the certificate of title), deposit accounts and letter-of-credit rights (control only), and money (possession only). See §§ 9-311(a), 9-312(b).

<sup>161</sup> See § 9-322(a) ("Except as otherwise provided in this section . . .").

<sup>162</sup> See § 9-322(f)(1) (stating that the general rule of subsection (a) is "subject to . . . the other provisions of this part").

<sup>163</sup> July 20 is one of the most notable dates in world history. Neil Armstrong took mankind's first steps on the moon on July 20, 1969. Also on that date I celebrated my tenth birthday, an event of considerably less importance (except, perhaps at the time, to me).

Twenty-one years later, on July 20, 1990, William J. Brennan, Jr., concluded his distinguished career as an Associate Justice on the Supreme Court of the United States. See Members of the Supreme Court of the United States, <http://www.supremecourtusgov/about/members.pdf> (last visited Oct. 26, 2009).

<sup>164</sup> See § 9-108(e)(1) (stating that a reference to a "commercial tort claim" without additional language "is an insufficient description"). Notwithstanding the inclusion of an after-acquired property clause, future commercial tort claims will not be part of the collateral. See § 9-204(b)(2).

against BizCorp other than Lender's financing statement. BizCorp has no other secured debt or secured creditors.

Relying on the baseline "first to file or perfect" rule, a student may conclude that BizCorp has, and will continue to have, priority in all of the collateral in which a security interest may be perfected by filing.

But that conclusion is riddled with exceptions, including the following:

- Lender's security interest may not enjoy priority in a dispute with any future "buyer in the ordinary course of business" who claims the benefits afforded to such a party by § 9-320(a);
- Lender's security interest may not enjoy priority in a dispute with any future secured party claiming the superpriority status afforded to purchase-money security interests under § 9-324;
- Lender's security interest may not enjoy priority in a dispute with any secured party claiming priority under § 9-325 in future collateral acquired by BizCorp;
- Lender's security interest may not enjoy priority in a dispute with any secured party claiming priority under § 9-326 in collateral transferred by BizCorp to a "new debtor;"
- Lender's security interest may not enjoy priority in a dispute with any future secured party claiming an enforceable security interest in investment property perfected by control (§ 9-328(1));
- Lender's security interest may not enjoy priority in a dispute with any future "purchaser" who enjoys the benefits afforded to such a party by § 9-330;
- Lender's security interest may not enjoy priority in a dispute with any future "holder" or "purchaser" who enjoys the benefits afforded to such a party by § 9-331;
- Lender's security interest may not enjoy priority in a dispute with any future "transferee" who enjoys the benefits afforded to such a party by § 9-332;
- Lender's security interest may not enjoy priority in a dispute with any future creditor claiming a "possessory lien" under § 9-331; and
- Lender's security interest in collateral acquired by BizCorp more than four months after it makes a seriously misleading name change may become unperfected and lose priority unless Lender timely refiles (§ 9-507(c)).

No doubt there are others,<sup>165</sup> but the exceptions listed above are sufficient in number to illustrate the difficulty of stating a general rule in a manner that acknowledges its exceptions.

The preceding discussion illustrates another possible obstacle to the effective use of syllogisms in Secured Transactions. Article 9 occasionally adopts a rule that is subject to one or more exceptions. And a rule stripped of its exceptions may, when stated as a major premise, lead to an incorrect legal conclusion.

### CONCLUSION

Judge Aldisert and his co-authors have called for a renewed emphasis on deductive reasoning in the classroom, with special attention given to the syllogism. Syllogistic reasoning requires the audience to craft a major premise (usually a legal rule) and a minor premise (often a statement of fact), and then draw from those two premises a conclusion. Students often find that correctly stating the legal rule can be quite challenging, but imperative to reaching a sound conclusion. That challenge dissipates in a statutory course, such as Secured Transactions, where the rules are codified. Perhaps more than many law school courses, then, Secured Transactions is a course in which the syllogism can be a useful learning tool in introducing, analyzing, and mastering the intricacies of Article 9. But, as illustrated in the preceding pages, Article 9 itself hinders the effective use of syllogistic reasoning.

Given these statutory roadblocks, then, should those of us who have been anointed to teach Secured Transactions simply dismiss Judge Aldisert's plea for more deductive reasoning in our classroom? Absolutely not. Notwithstanding these codified quirks, many of the legal issues introduced in the course can indeed be examined and resolved through syllogistic analysis. But that is a topic for another day—and a companion article.<sup>166</sup>

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<sup>165</sup> For example, the secured party may be concerned about the scope of its priority when the competing claimant is the Internal Revenue Service, a topic which I have explored in previous articles. See Timothy R. Zinnecker, *Resolving Priority Disputes Between the IRS and the Secured Creditor Under Revised UCC Article 9: And the Winner is . . . ?*, 34 ARIZ. ST. L.J. 921-66 (2002); Timothy R. Zinnecker, *When Worlds Collide: Resolving Priority Disputes Between the IRS and the Article Nine Secured Creditor*, 63 TENN. L. REV. 585-688 (1996).

<sup>166</sup> See *supra* note 15 and accompanying text.