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The Effect of Revised Article 9 On Consumer Transactions

DIANN M. BARTEK AND H. JOSEPH ACOSTA*

I. Introduction

Seeking to improve a body of law that governs trillions of dollars of commercial and consumer credit each year,¹ the American Law Institute and the National Conference of Commissioners on Uniform State Laws have sponsored² revisions to Article 9 ("Revised Article 9")³ of the Uniform Commercial Code ("UCC"), which constitute the first major changes to this uniform statute since 1972.⁴ Thus far, Revised Article 9 has been adopted by 25 state legislatures and introduced in 14 other states.⁵ With Revised Article 9's proposed effective date being July 1, 2001 ("Effective Date"),⁶ debtors and creditors alike will have a relatively short time to understand and comply

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¹ See National Conference Of Commissioners On Uniform State Laws, *New UCC Article 9 Revision, Governing Secured Transactions, Working Its Way Through State Legislatures* (Jan. 2000) <<http://www.nccusl.org/pressrel/ucc9799.htm>>.

² See *id.*

³ References in this article to "Revised Article 9" refer to Uniform Commercial Code, Article 9, 1999 Official Text. References in this article to Current Article 9 refer to the 1995 Official Text.

⁴ See Steven O. Weise, *An Overview Of Revised UCC Article 9*, in *THE NEW ARTICLE 9*, 1, 1 (Corinne Cooper ed. 1999).

⁵ States that have adopted Revised Article 9: Alaska, Arizona, California, Delaware, District of Columbia, Hawaii, Illinois, Indiana, Iowa, Kansas, Kentucky, Maine, Maryland, Minnesota, Montana, Nebraska, Nevada, North Carolina, Oklahoma, Rhode Island, South Dakota, Tennessee, Texas, Utah, Vermont, Virginia, Washington and West Virginia. States that have introduced Revised Article 9: Colorado, Florida, Idaho, Massachusetts, Michigan, Mississippi, Missouri, New Jersey, New Mexico, New York, South Carolina and Wyoming. See National Conference Of Commissioners On Uniform State Laws, *A Few Facts About Revised UCC Article 9, Secured Transactions (1998)* (as of September 2000) <http://nccusl.org/uniformact__factsheets/uniformacts-fs-ucca9.htm>.

⁶ See Uniform Commercial Code, Article 9, 1999 Official Text, § 9-701. Hereinafter, citations to Revised Article 9 will be referred to as "Rev. UCC § 9-____." Also, citations to Current Article 9 will be referred to as "Cur. UCC § 9-____."

with a statute that has "grown" from 5 parts, 55 sections and 136 subsections to 7 parts, 12 subparts, 134 sections and 443 subsections.⁷ As one esteemed colleague has recently noted, while we managed to survive the Y2K scare, now we must prepare for the secured transactions millennium bug—the implementation of Revised Article 9 in every state.⁸

This article attempts to address only the major changes in Revised Article 9 that impact the area of consumer transactions. While most of the changes in Revised Article 9 affect commercial transactions and relatively few changes were made in the consumer arena, there are still several significant revisions of which consumer borrowers and lenders should be made aware. In addition to these changes, this paper will discuss some of the problems that will persist after the implementation of Revised Article 9.

II. Overview of Changes Applicable Only to Consumer Transactions

A. New Definitions.

1. Consumer Transactions and Consumer—Goods Transactions.

While Current Article 9 does not contain a definition for secured transactions involving consumer debtors, Revised Article 9 defines a "consumer transaction" as one in which "(i) an individual incurs an obligation primarily for personal, family or household purposes, (ii) a security interest secures the obligation, (iii) the collateral is held or acquired primarily for personal, family or household purposes."⁹ A "consumer-goods transaction," is a subset¹⁰ of a consumer transaction in which the collateral is consumer goods.¹¹ "Consumer goods" continue to be defined as "goods that are used or bought for personal, family, or household purposes."¹² Mixed business and personal transactions may be characterized as "consumer-goods transactions," "consumer transactions," or neither, depending on the primary purpose of the transaction.¹³ The fact that some of the collateral or obligations incurred in such a transaction are for business purposes does not necessarily take the transaction outside the realm of a "consumer transaction" or "consumer-goods transaction," so long as the primary purpose of the trans-

⁷ Counting multiple alternatives within a subsection as 1 unit.

⁸ See G. Ray Warner, *Preparing For The New Article 9*, AM. BANKR. INST. J., February 2000, at 6.

⁹ See Rev. UCC § 9-102(a)(26).

¹⁰ See *id.*

¹¹ See Rev. UCC § 9-102(a)(24).

¹² See Cur. UCC § 9-109(1) and Rev. UCC § 9-102(a)(23).

¹³ See Rev. UCC. § 9-102 cmt. 7.

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action fits within the definitions assigned to "consumer transactions" or "consumer-goods transactions."¹⁴

The distinction between "consumer transactions" and "consumer—goods transactions" is important in the applicability of Revised Article 9's "consumer provisions." For instance, Revised Article 9 specifically states that in a "consumer transaction" a creditor may not take a debtor's deposit account(s) as collateral¹⁵ or use partial strict foreclosure as a remedy upon default.¹⁶ If the collateral in a "consumer transaction" consists of consumer goods, a security entitlement, a securities account, or a commodity account, the collateral description in a security agreement is *per se* insufficient if it describes this collateral merely by type.¹⁷ Revised Article 9 also clarifies that a creditor and its assignee in a "consumer transaction" may not circumvent the Federal Trade Commissions Holder in Due Course Rule.¹⁸ Furthermore, Revised Article 9 specifically excludes "consumer transactions" from certain bright line rules applicable to commercial transactions, e.g., a "rebuttable presumption" approach to deficiency claims in cases where a secured party has unreasonably disposed of collateral¹⁹ or a 10-day safe harbor for providing reasonable notice of collateral disposition.²⁰

In "consumer-goods transactions," Revised Article 9 contains specific provisions delineating the proper notice which secured parties must give regarding the disposition of collateral upon default.²¹ In a "consumer-goods transaction" where there is a deficiency or surplus after the disposition of collateral, the secured party is required to give an explanation to the debtor or consumer obligor, providing the calculation of this deficiency or surplus.²² Revised Article 9 also excepts "consumer-goods transactions" from the dual status approach adopted in commercial transactions, which preserves the status and priority of purchase money security interests in cross-collateralization cases.²³

2. Consumer Debtors and Consumer Obligors.

Revised Article 9 also redefines the role of a "debtor" in a secured trans-

¹⁴ See *id.*

¹⁵ See Rev. UCC § 9-109(d)(13).

¹⁶ See Rev. UCC § 9-620(g).

¹⁷ See Rev. UCC § 9-108(e)(2).

¹⁸ See Rev. UCC §§ 9-403(d), 9-404(d).

¹⁹ See Rev. UCC § 9-626(a)(4),(b).

²⁰ See Rev. UCC § 9-612(b).

²¹ See Rev. UCC § 9-614.

²² See Rev. UCC § 9-616(a), (b).

²³ See Rev. UCC § 9-103.

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action. Under Current Article 9, the term "debtor" includes both the person who owes the debt *and* the person who owns the collateral.²⁴ Under Revised Article 9, a "debtor" is the person who has an interest in the collateral other than a security interest or other lien,²⁵ while an "obligor" is the person who owes payment or performance on a secured obligation.²⁶ Consistent with these new definitions and perhaps as an attempt to provide a more precise body of law, Revised Article 9 also defines "consumer debtor,"²⁷ "consumer obligor,"²⁸ "original debtor"²⁹ and "new debtor."³⁰ Of course, the significance of these new definitions is that, in addition to understanding the terminology used in Revised Article 9, a secured party must revise its security documents to properly identify the roles of consumer borrowers and others that may be affected by the enforcement of security interests in collateral.

B. New Rules.

1. Description of Collateral.

Article 9 has traditionally required that a security agreement reasonably describe the collateral it covers, in order for a security interest to attach.³¹ However, Revised Article 9 will require secured parties in consumer transactions to re-evaluate the content of their security documents. First, Revised Article 9, unlike its predecessor, now specifies what collateral descriptions in security agreements are *per se* reasonable.³² Second, Revised Article 9 clarifies that, in consumer transactions, a security agreement must go beyond merely describing the collateral by types defined in the UCC, e.g., "consumer goods" or "investment property."³³ Such generic descriptions will be deemed insufficient to create a security interest under Revised Article 9.

²⁴ See Cur. UCC § 9-105(1)(d).

²⁵ See Rev. UCC § 9-102(a)(28)(A). This definition also includes a seller of accounts, chattel paper, payment intangibles, or promissory notes and a consignee.

²⁶ See Rev. UCC § 9-102(a)(59). This definition also includes a person that has provided property other than the collateral to secure payment of the secured debt or any other person otherwise accountable for the secured debt.

²⁷ See Rev. UCC § 9-102(a)(22) (consumer debtor defined as a debtor in a consumer transaction).

²⁸ See Rev. UCC § 9-102(a)(25) (consumer obligor defined as being a person who incurs an obligation primarily for personal, family or household purposes).

²⁹ See Rev. UCC § 9-102(a)(60).

³⁰ See Rev. UCC § 9-102(a)(56).

³¹ See Cur. UCC §§ 9-203(1),(2), 9-110 and Rev. UCC §§ 9-203(a), (b)(3)(A), 9-108(e).

³² Collateral is reasonably identified by: specific listing, category, type of collateral defined in the UCC (certain exceptions apply), quantity, computational or allocation formula or procedure, or any other method where the collateral is objectively determinable (certain exceptions apply).

³³ See Rev. UCC § 9-108(e).

Revised Article 9 describe the security interest. This section will be subject to Article 9,³⁵ which is a security interest. However, the financing statement must be filed against the property,³⁶ even if the security agreement is a financing statement of a security interest.

2.

Revised Article 9 security agreement must be "authenticated" and broadens the scope of the UCC], to encourage the use of authentication symbols, or electronic records to present intent to accept a recording of the transaction.⁴⁴ Thus,

³⁴ See Rev. UCC § 9-102(a)(22).

³⁵ See Rev. UCC § 9-102(a)(22).

³⁶ See Rev. UCC § 9-102(a)(22).

³⁷ See Rev. UCC § 9-102(a)(22).

³⁸ See Rev. UCC § 9-102(a)(22).

³⁹ See Rev. UCC § 9-102(a)(22).

⁴⁰ See Cur. UCC § 9-102(a)(22).

⁴¹ See Rev. UCC § 9-102(a)(22).

⁴² Rev. UCC § 9-102(a)(22).

⁴³ Rev. UCC § 9-102(a)(22).

⁴⁴ See Edwin E. Clark, Note, the concept of individual state authentication. In some states, Texas authentication. See Texas, a security interest in the communication the person using it.

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Revised Article 9 similarly requires financing statements to sufficiently describe the secured party's collateral.³⁴ In all cases, the collateral description will be sufficient if it complies with Section 9-108 of Revised Article 9;³⁵ which is also applicable to collateral descriptions in security agreements.³⁶ However, Revised Article 9 provides that a secured party may file a financing statement describing its collateral as "all assets" or "all personal property,"³⁷ even though such omnibus descriptions would invalidate a security agreement.³⁸ Perhaps, this was due in part to the realization that a financing statement is only intended to provide third parties with "notice" of a security interest.³⁹

2. "Signing" of Security Agreement.

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Revised Article 9 also changes the requirement that a debtor has to sign a security agreement.⁴⁰ Under Revised Article 9, a valid security agreement must be "authenticated" by the debtor.⁴¹ The term "authenticated" replaces and broadens the definition of "sign" or "signed," in Section 1-201 [of the UCC], to encompass authentication of all documents, not just writings.⁴² To authenticate means: (1) to sign; or (2) to execute or otherwise adopt a symbol, or encrypt or similarly process a record in whole or in part, with the present intent of the authenticating person to identify the person and adopt or accept a record.⁴³ The latter definition encompasses electronic transmissions.⁴⁴ Thus, a security agreement which a debtor authenticates does not

³⁴ See Rev. UCC § 9-504.

³⁵ See Rev. UCC § 9-504(1).

³⁶ See Rev. UCC § 9-203 cmt. 5 and § 9-108 cmt. 2.

³⁷ See Rev. UCC § 9-504(2).

³⁸ See Rev. UCC § 9-108(c), § 9-504 cmt. 2.

³⁹ See Rev. UCC § 9-502 cmt. 2 and § 9-504 cmt. 2.

⁴⁰ See Cur. UCC § 9-203(1)(a).

⁴¹ See Rev. UCC § 9-203(b)(3).

⁴² Rev. UCC § 9-102 cmt. 9(b).

⁴³ Rev. UCC § 9-102 (a)(7).

⁴⁴ See Edwin E. Smith, *Overview Of Revised Article 9*, 73 AM. BANKR. L.J. 1, 13 (1999). Note, the concept of authentication is not new to some jurisdictions. As Article 9 currently allows individual states to pass laws dealing with small loans, retail installments and the like, some states, Texas for one, have already adopted provisions that incorporate the concept of authentication. See TEX. BUS. & COM. CODE ANN. § 9.203(f) (Vernon Supp. 2000). In Texas, a security agreement is considered signed if a "digital signature" is transmitted with the communication. See *id.* A "digital signature" means an electronic identifier intended by the person using it to have the same force and effect as the use of a manual signature. See *id.*

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have to be in tangible form to be valid.⁴⁵ A computer-generated record can adequately create a security interest as long as the debtor has electronically transmitted her identity and acceptance of the record.

3. Notice Before Disposition of Collateral.

Under Revised Article 9 notice before disposition of collateral in a consumer—goods transaction *must* include all of the following:⁴⁶

- a description of the debtor, the secured party, and the collateral that is being disposed;
- the method of disposition;
- a statement that the debtor is entitled to an accounting of the unpaid debt and the charge, if any, for the accounting;
- the time and place of a public sale or the time after which any other disposition is to be made;⁴⁷
- a description of the recipient's liability for any deficiency;⁴⁸
- a telephone number from which the recipient can obtain the redemption price of the collateral;⁴⁹
- a telephone number or mailing address from which the recipient can obtain additional information concerning the disposition and the obligation.⁵⁰

The drafters of Revised Article 9 suggest that a creditor in a consumer—goods transaction adopt the model notice contained in Revised Article 9.⁵¹ It is important to note that a notification that lacks *any* of the information set forth above is “insufficient as a matter of law.”⁵² Further, it should be noted that Revised Article 9 provides a different model notification letter for use in commercial transactions; therefore, there is no “all purpose” notice. Creditors will be forced to correctly determine whether a transaction is a consumer-goods transaction before they send the required predisposition notice. Obviously in many situations the concern is minimal because the clas-

⁴⁵ Comments 2 and 3 of Rev. UCC § 9-203 also allude to the idea that a security agreement only serves some type of evidentiary function. Furthermore, Comment 4 of Rev. UCC § 9-203 states that the phrase “debtor's authentication of a security agreement contemplates the debtor's authentication of a record.” Revised Article 9 defines a “record” as including information which is stored in an electronic or other medium and is retrievable in perceivable form. See Rev. UCC § 9-102(a)(69).

⁴⁶ See Rev. UCC § 9-614(1).

⁴⁷ See Rev. UCC §§ 9-614(1)(A), 9-613(1).

⁴⁸ See Rev. UCC § 9-614(1)(B).

⁴⁹ See Rev. UCC § 9-614(1)(C).

⁵⁰ See Rev. UCC § 9-614(1)(D).

⁵¹ See Rev. UCC § 9-614 cmt. 3.

⁵² See Rev. UCC § 9-614 cmt. 2.

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sification of collateral is obvious. Additionally, Revised Article 9 provides a safe harbor for the creditor that acts in reasonable reliance on the debtor's representation concerning the purpose for which the collateral has been used, acquired, or held.⁵³

4. Explanation of Calculation of Surplus or Deficiency.

After a secured creditor has disposed of collateral, the creditor will either return any surplus to, or demand payment of any deficiency from (a more likely scenario), the appropriate party. Revised Article 9 requires a secured party in a consumer-goods transaction to send an "explanation" to each consumer obligor liable for any deficiency or, if applicable, to the debtor entitled to any surplus.⁵⁴ The "explanation" must be sent no later than when the secured party: a) initially demands, in writing, payment of the deficiency by the consumer obligor or, b) if applicable, remits the surplus to the debtor.⁵⁵ The secured party must also send an "explanation" within 14 days after it receives from a debtor or consumer obligor an authenticated record requesting the creditor to provide an "explanation."⁵⁶ An "explanation" *must* contain the following information *in the following order*:

- aggregate amount of debt secured by the disposed collateral calculated as of a specified date;⁵⁷
- the proceeds from the disposition of the collateral;⁵⁸
- the remainder after deducting the proceeds from the disposition of the collateral from the aggregate debt;⁵⁹
- expenses, related to the disposition of the collateral, and attorneys' fees secured by such collateral;⁶⁰
- credits not included in the aggregate debt;⁶¹ and
- deficiency or surplus amount.⁶²

5. Expansion of Duty of Good Faith.

Revised Article 9 adopts a definition of "good faith" that is more

⁵³ See Rev. UCC § 9-628(c)(1).

⁵⁴ See Rev. UCC § 9-616(b).

⁵⁵ See Rev. UCC § 9-616(b)(1)(A).

⁵⁶ See Rev. UCC § 9-616(b)(1)(B) (referencing a "request"); Rev. UCC § 9-616(a)(2) (defining "request"). Alternatively, the secured party may, within 14 days after receiving the consumer obligor's request, send the consumer obligor a record in which the secured party waives its right to any deficiency. Rev. UCC § 9-616(b)(2).

⁵⁷ See Rev. UCC § 9-616(c)(1).

⁵⁸ See Rev. UCC § 9-616(c)(2).

⁵⁹ See Rev. UCC § 9-616(c)(3).

⁶⁰ See Rev. UCC § 9-616(4).

⁶¹ See Rev. UCC § 9-616(5).

⁶² See Rev. UCC § 9-616(c)(6).

expansive than the current definition used by Article 1 of the UCC. The UCC "generally" imposes a duty of "good faith" on the performance and enforcement of any contract or duty governed by the UCC.⁶³ Article 1 of the UCC presently defines "good faith" as "honesty in fact in the conduct or transaction concerned."⁶⁴ Revised Article 9's independent definition of "good faith," expands the meaning [in Article 1] to include "the observance of reasonable commercial standards of fair dealing."⁶⁵ Revised Article 9 also provides that this new definition will apply to all transactions governed by Article 1's duty of "good faith,"⁶⁶ as well as transactions governed by sections in Revised Article 9 that specifically use the term "good faith."⁶⁷

With the expansion of the definition of "good faith" in Revised Article 9, the duty of "good faith" should become more prevalent in secured transactions. For instance, Revised Article 9 provides an illustration of how a proposal for strict foreclosure may be invalidated when made in bad faith. When a secured party proposes strict foreclosure in a situation in which the value of the collateral far exceeds the amount of the secured obligation, the proposal and deemed acceptance by the debtor may be voidable.⁶⁸ In such cases, Revised Article 9 suggests that a court may find that the secured party sent the proposal in bad faith, expecting to obtain a windfall when the debtor failed to object in a timely manner.

III. Default—Rules of Enforcement and Secured Creditor's Liability for Violation

The provisions in Part 5 of Current Article 9, dealing with the remedies of a secured party when a borrower defaults, have been moved to Part 6 in Revised Article 9 and have grown from 7 sections with 16 subsections to 28 sections with 91 subsections. One would assume, considering the number of new "default" sections and subsections, that major changes have been made in the consumer transaction arena. Quite to the contrary, the area of consumer

⁶³ See Cur. UCC § 1-203.

⁶⁴ See Cur. UCC § 1-201(19).

⁶⁵ Rev. UCC § 9-102(a)(43).

⁶⁶ See Cur. UCC § 1-203. Rev. UCC § 9-102(c) also states that Article 1 contains general definitions and principles of construction and interpretation applicable throughout Article 9.

⁶⁷ See Rev. UCC § 9-102 cmt. 19. The following Revised Article 9 subsections incorporate the term "good faith": § 9-321(a) (defining licensee in the ordinary course of business); § 9-330(a), (d) (determining when a purchaser of chattel paper or an instrument gains priority over a security interest in this collateral); § 9-403(b) (dealing with agreements that exonerate account assignees from claims/defenses of account debtors); § 9-405(a) (dealing with modifications of assigned contracts); § 9-615(g) (good faith error defense against other secured parties for disposition of collateral); and § 9-617(b) (dealing with the rights of a transferee of collateral after disposition by secured party).

⁶⁸ See Rev. UCC § 9-620 cmt. 11.

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transactions has been for the most part ignored; however, in this section of the paper, the major revisions relating to default in consumer transactions will be considered.

A. Commercially Reasonable Disposition.

Under Current and Revised Article 9, a secured party is generally free to declare default, take control of collateral and dispose of it, all without judicial assistance.⁶⁹ In a situation in which a secured party decides to sell collateral to reduce the amount owed by the obligor, both Current and Revised Article 9 provide that every aspect of this disposition, including the method, manner, time, place, and other terms, must be commercially reasonable.⁷⁰ Additionally, both Current and Revised Article 9 require the secured party to provide notice of this sale to the debtor and other interested parties.⁷¹ In cases involving consumer goods, however, Current Article 9 requires that notices be sent to debtors,⁷² while Revised Article 9 clarifies that notices must be sent to debtors *and* secondary obligors.⁷³ Revised Article 9 also clarifies that in all cases, consumer or commercial, the issue of sending timely notice is a question of fact, not a question of law.⁷⁴ However, in non-consumer cases Revised Article 9 creates a 10-day safe harbor for sending timely notification.⁷⁵ In other words, sending notice within 10 days of disposition is *per se* reasonable in commercial cases only; in consumer transactions, it depends on the particular circumstances involved.

As previously discussed herein, Revised Article 9 expands the information that must be included in a notice to dispose of consumer goods.⁷⁶ Revised Article 9 even provides a form that secured parties can use to provide reasonable notification,⁷⁷ although no particular phrasing in a dispo-

⁶⁹ Jean Braucher, *Deadlock: Consumer Transactions Under Revised Article 9*, 73 AM. BANKR. L.J. 83, 85 (1999) (citing Cur. UCC § 9.501 and Rev. UCC §§ 9-601(a), 9-609, 9-610(a),(b)).

⁷⁰ See Cur. UCC § 9-504(1),(3) and Rev. UCC § 9-610(a),(b).

⁷¹ See Cur. UCC § 9-504(3) and Rev. UCC § 9-611(c).

⁷² See Cur. UCC § 9-504(3).

⁷³ See Rev. UCC § 9-611(b),(c). Revised Article 9 defines a "secondary obligor" as an entity whose obligation is secondary or who has a right of recourse with respect to the obligation secured by collateral against the debtor, another obligor or property of either. See Rev. UCC § 9-102 (a)(71).

⁷⁴ See Rev. UCC § 9-612(a).

⁷⁵ See Rev. UCC § 9-612(b) and § 9-612 cmt. 3.

⁷⁶ See Rev. UCC § 9-614.

⁷⁷ See Rev. UCC § 9-614(3).

sition notice is required.⁷⁸ However, Revised Article 9 provides that other laws, besides the UCC, shall govern notices of disposition that are not in the form prescribed by Revised Article 9.⁷⁹ Thus, the prescribed notification, if properly completed, provides a safe harbor against violating Article 9,⁸⁰ and a potential safe harbor against violating other consumer protection laws.⁸¹

B. Strict Foreclosure.

Revised Article 9 also clarifies and restricts the use of strict foreclosure as a remedy in consumer transactions. Strict foreclosure is a procedure by which a secured party acquires the debtor's interest in collateral without the need for sale or other disposition allowed under the UCC.⁸² Expounding on the approach used in Current Article 9,⁸³ Revised Article 9 allows a secured party to accept collateral in full or partial satisfaction of a secured obligation.⁸⁴ However, in consumer transactions, Revised Article 9 proscribes partial strict foreclosure.⁸⁵ In other words, in a consumer transaction the secured party cannot accept the collateral in partial satisfaction of the debt and then expect to sue for a deficiency. Presumably, this restriction was in response to the concern that consumers might not understand the ramifications of partial strict foreclosure,⁸⁶ i.e., that the creditor may still sue for a deficiency after foreclosure.

Revised Article 9 also does away with the fiction that the secured party will be the only party proposing strict foreclosure.⁸⁷ The comments in Revised Article 9 even suggest that strict foreclosures should be encouraged, as they often produce better results for the parties involved.⁸⁸ In a consumer case in which the secured party wants to effectuate strict foreclosure, the debtor must, after defaulting, consent to strict foreclosure or fail to object to

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⁷⁸ See Rev. UCC § 9-614(2).

⁷⁹ See Rev. UCC § 9-614(6).

⁸⁰ See Rev. UCC § 9-614 cmt. 3.

⁸¹ Whether this Article 9 safe harbor will shield liability from consumer protection laws in cases where a secured party includes incorrect information in the proposed form will remain to be seen.

⁸² Rev. UCC § 9-620 cmt. 2.

⁸³ Cur. UCC § 9-505(2).

⁸⁴ Rev. UCC § 9-620(a).

⁸⁵ Rev. UCC § 9-620(g).

⁸⁶ See TIMOTHY R. ZINNECKER, THE DEFAULT PROVISIONS OF REVISED ARTICLE 9, at 124 (1999).

⁸⁷ See Rev. UCC § 9-620 cmt. 2.

⁸⁸ See Rev. UCC § 9-620 cmt. 2.

⁸⁹ See Rev. UCC § 9-620 cmt. 2.

⁹⁰ See Cur. UCC § 9-620 cmt. 2.

⁹¹ See Rev. UCC § 9-620 cmt. 2.

⁹² See *id.*

⁹³ See Rev. UCC § 9-620 cmt. 2.

⁹⁴ See Cur. UCC § 9-620 cmt. 2.

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this type of foreclosure within 20 days of receiving notice⁸⁰ (instead of 21 days under Current Article 9).⁸⁰ In cases in which a debtor or obligor proposes strict foreclosure, the secured party must consent through an authenticated record.⁸¹ Alternatively, the secured party is deemed to have consented if she sent the proposal of strict foreclosure to the debtor.⁸² A secured party's mere acceptance of the possession of the collateral or delay in collecting or disposing of the collateral will not create "constructive strict foreclosure."⁸³

Revised Article 9 further eliminates the requirement that a secured party must be in possession of collateral before she retains the collateral in satisfaction of the corresponding debt;⁸⁴ however, if the collateral consists of consumer goods, the collateral cannot be in the debtor's possession when she consents to strict foreclosure.⁸⁵

Finally, the strict foreclosure section in Revised Article 9 leaves a glaring omission from Current Article 9 with respect to the procedure that a secured party must follow in consumer cases when the debtor objects to strict foreclosure. Under Current Article 9, the secured party must dispose of the collateral in a commercially reasonable fashion after receiving an objection.⁸⁶ Although similarly prohibiting strict foreclosure after timely objection is made, Revised Article 9 does not require the secured party to dispose of the collateral after receiving this objection. Rather, under Revised Article 9 it seems that the secured party may retain possession of the collateral, even though it cannot retain the collateral in satisfaction of any debt.⁸⁷

C. Redemption.

Under Current Article 9, the right of redemption is given to the debtor and

⁸⁰ See Rev. UCC § 9-620(a)(1), (c)(2).

⁸⁰ See Cur. UCC § 9-505(2).

⁸¹ See Rev. UCC § 9-620 (b).

⁸² See *id.*

⁸³ See Rev. UCC § 9-620 cmt. 5.

⁸⁴ See Cur. UCC § 9-505(2), Rev. UCC. § 9-620 cmt. 7.

⁸⁵ See Rev. UCC § 9-620(a)(3).

⁸⁶ See Cur. UCC §§ 9-505(2), 9-504.

⁸⁷ Of course, the option of retaining the collateral is subject to the duty of good faith imposed by Articles 1 and 9. See Rev. UCC § 9-102(43). Thus, retaining the collateral for a prolonged period of time might constitute bad faith. Also note that Revised Article 9, like its predecessor, requires a secured party to dispose of consumer goods where it has received 60% of the cash price (purchase-money security interest) for these goods or 60% of the principal amount of obligations secured by these goods (non-purchase-money security interest). See Cur. UCC § 9-505(1) and Rev. UCC § 9-620(e).

any other party that has a security interest in the collateral in question.⁹⁸ Revised Article 9 extends this privilege to nonconsensual lienholders.⁹⁹ Revised Article 9 also delineates that redemption can occur anytime before a secured party has collected the collateral, disposed of the collateral, contracted to dispose of the collateral or has announced strict foreclosure of the collateral.¹⁰⁰ Current Article 9 only mentions that redemption can occur at any time before the secured party disposes or contracts for the disposition of the collateral, or announces strict foreclosure.¹⁰¹ The current wording creates confusion as to whether a secured party actually has to have possession of the collateral before the debtor has the option to redeem.¹⁰²

Revised Article 9 further prohibits a waiver of redemption rights in consumer-goods cases.¹⁰³ Under Revised Article 9, "[e]xcept in a consumer-goods transaction, a debtor or secondary obligor may waive the right to redeem collateral. . . only by an agreement to that effect entered into and authenticated after default."¹⁰⁴ The fact that this provision does not apply in consumer cases is further clarified by § 9-602(11) of Revised Article 9 which states that debtors and obligors generally cannot waive their right of redemption.¹⁰⁵ This provision changes the current opportunity in consumer cases to obtain a waiver of redemption rights after a consumer debtor has defaulted on a secured obligation.¹⁰⁶

D. Noncompliance Sanctions.

Revised Article 9 adopts the "rebuttable presumption" rule in commercial transaction cases for proof of a deficiency claim after a secured party disposes of collateral.¹⁰⁷ However, Revised Article 9 provides little guidance on how courts should determine similar deficiency claims in consumer cases.

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⁹⁸ *See* Cur. UCC § 9-506.

⁹⁹ *See* Rev. UCC § 9-623(a) cmt. 2. Note, while Revised Article 9 also mentions "secondary obligor" as a recipient of this privilege, for all intent and purposes, the term "debtor" under Current Article 9 also covers a "secondary obligor," thus not making this person or entity a new beneficiary of redemption rights.

¹⁰⁰ *See* Rev. UCC § 9-623.

¹⁰¹ *See* Cur. UCC § 9-506.

¹⁰² The comment to Cur. UCC § 9-506 creates this confusion by stating that "[u]nder this section so long as the secured party has not disposed of collateral *in his possession* or contracted for its disposition, and so long as his right to retain it has not become fixed under Section 9-505(2), the debtor or another secured party may redeem." (emphasis added).

¹⁰³ *See* Rev. UCC § 9-624(c).

¹⁰⁴ Rev. UCC § 9-624(c).

¹⁰⁵ Rev. UCC § 9-602(11) and 9-602 cmt. 5.

¹⁰⁶ *See* Cur. UCC §§ 9-501(3), 9-506.

¹⁰⁷ *See* Rev. UCC § 9-626 cmt. 3. The rebuttable presumption is currently applied in the majority of jurisdictions. *See* Smith, *supra* note 33, at 53. The minority approach is the

¹⁰⁸ *See* Rev. UC

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Under the newly adopted “rebuttable presumption” rule, a secured party in a non-consumer transaction need not prove compliance with the default provisions in Article 9, unless a debtor or secondary obligor places the secured party’s compliance at issue.¹⁰⁸ When compliance is at issue, the secured party has the burden of establishing that she complied with Article 9, e.g., that she conducted a commercially reasonable sale.¹⁰⁹ If the secured party does not prevail, the debtor or secondary obligor’s liability for deficiency is limited to the amount by which the sum of the secured obligation, expenses and attorney’s fees exceeds the greater of: (1) all proceeds from the collateral received by the secured party or (2) the amount of proceeds that would have been realized if the secured party had acted in a commercially reasonable manner.¹¹⁰ This latter amount is presumed to equal the amount owed, including the expenses and attorney’s fees of the secured party.¹¹¹ Although the rebuttable presumption sets up a bright line burden of proof in commercial cases, Revised Article 9 does not provide similar guidance in consumer transaction cases.¹¹² Instead, Revised Article 9 leaves the proper method of establishing—or barring—deficiency claims solely to the judiciary.¹¹³ Revised Article 9 even dictates that courts should not draw any inferences from the “rebuttable presumption” approach adopted for commercial cases.¹¹⁴

The statutory sanctions for noncompliance with the default provisions in Article 9 have also changed. Under Current Article 9, a person who does not comply with any provision in Part 5 of Article 9 (default provisions) is liable for any loss caused by this noncompliance.¹¹⁵ Revised Article 9 expands the scope of liability, by making a secured party liable for noncompliance with any provision in Article 9.¹¹⁶ In cases involving consumer goods, Revised

“absolute bar” rule, which bars a secured party from pursuing a deficiency claim if the secured party did not act in a commercially reasonable manner when disposing of the collateral. *See id.* A few other jurisdictions require the debtor to prove its loss (the “offset” rule). *See id.*

¹⁰⁸ *See* Rev. UCC § 9-626(a)(1).

¹⁰⁹ *See* Rev. UCC § 9-626(a)(2).

¹¹⁰ *See* Rev. UCC § 9-626(a)(3).

¹¹¹ *See* Rev. UCC § 9-626(a)(4).

¹¹² *See* Rev. UCC § 9-626(a).

¹¹³ *See* Rev. UCC § 9-626(b).

¹¹⁴ *See id.*

¹¹⁵ *See* Cur. UCC § 9-507(a).

¹¹⁶ *See* Rev. UCC § 9-625(b). For example, a secured party may be liable for noncompliance with Section 9-207 (duty of a secured party in possession of collateral) or 9-210 (duty to comply with request for accounting, etc.). *See* Rev. UCC § 9-625 cmt. 2.

Article 9 maintains the traditional statutory penalty¹¹⁷ for failing to comply with the default rules in Article 9 (Part 6 in Revised Article 9).¹¹⁸ However, Revised Article 9 also provides a new defense to a secured party who has acted on a mistaken belief, based on the representations of the debtor or obligor, that the transaction did not involve consumer goods and was not otherwise a consumer transaction or a consumer-goods transaction.¹¹⁹ This new defense not only exonerates a secured party from any liability for noncompliance with Article 9, it also protects the secured party's deficiency claim against the consumer obligor.¹²⁰

Revised Article 9 further creates new categories of supplemental¹²¹ liability for specific acts of noncompliance.¹²² As previously discussed herein, in a consumer-goods transaction a secured party must timely send a written explanation of any surplus or deficiency from the sale of repossessed collateral. Alternatively, the secured party may send the consumer obligor, 14 days after receiving a proper request, a record waiving the secured party's right to a deficiency claim.¹²³ Substantial compliance with these notice provisions absolves a secured party from any statutory penalties.¹²⁴ If the secured party does not provide the consumer obligor with the surplus/deficiency notice or the secured party does not waive its deficiency claim, the debtor or consumer obligor is entitled to recover \$500.00 from the secured party, upon showing that the incidence was a part of a pattern, or consistent with a practice, of noncompliance.¹²⁵

Additionally, the secured party in all cases must respond to a request by the debtor to: (1) account for unpaid obligations secured by collateral, (2) approve or correct a list that the debtor believes to be the collateral securing the unpaid obligations, or (3) approve or correct a statement that the debtor believes accurately reflects the unpaid obligations secured by collateral.¹²⁶ If the secured party, without reasonable cause, fails to respond, within 14 days,

¹¹⁷ Amount not less than the credit service charge plus 10% of the principle amount of the obligation or the time-price differential plus 10% of the cash price. *See* Rev. UCC § 9-625(c)(2) (applies to debtor and obligor) and Cur. UCC § 9-507(a) (applies to debtor).

¹¹⁸ *See* Rev. UCC § 9-625(c) and Cur. UCC. § 9-507(a).

¹¹⁹ *See* Rev. UCC § 9-628(c).

¹²⁰ *See id.*

¹²¹ In addition to those provided for in Rev. UCC § 9-625(b). *See* Rev. UCC § 9-616 cmt. 4.

¹²² *See* Rev. UCC § 9-625(e).

¹²³ *See* Rev. UCC § 9-616(b)(2).

¹²⁴ *See* Rev. UCC § 9-616(d).

¹²⁵ *See* Rev. UCC §§ 9-625(e)(5)-(6), 9-616(b)(1)-(2).

¹²⁶ *See* Rev. UCC § 9-210.

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to such a request, the debtor may recover an additional \$500.00 from the secured party.¹²⁷ Moreover, if the secured party fails to respond to the second (list of collateral) and third (statement of account) types of request, the secured party can only claim a security interest as shown on the debtor's proposed list or statement, if the debtor, or other party, has been reasonably misled by this omission.¹²⁸

Revised Article 9 further attempts to protect consumer debtors and obligors against certain low price dispositions of collateral. When a secured party, a person related to the secured party, or a secondary obligor seek to acquire collateral at a foreclosure sale, they often lack the incentive to maximize the proceeds from the sale of this collateral.¹²⁹ For instance, in a case where the secured party credit bids for the collateral, she can always pursue the obligor for any deficiency of the debt after the sale of the collateral.¹³⁰ As such, Revised Article 9 provides that a deficiency—or surplus—following the disposition of collateral to a secured party, a person related to the secured party, or a secondary obligor will be recalculated based on a disposition, complying with Part 6 of Revised Article 9, to a transferee other than a secured party, a person related to the third party, or a secondary obligor.¹³¹ However, the debtor or obligor can only obtain this reformed calculation if she proves that the proceeds realized from the prior disposition were significantly below the range of proceeds that an ideal disposition would have netted.¹³²

Interestingly enough, an earlier draft of Revised Article 9 included a good faith error defense which would have shielded a secured party from liability for clerical, calculation, computer malfunction, programming and printing errors, etc. . . notwithstanding the secured party's maintenance of procedures reasonably adopted to avoid such errors.¹³³ This defense would have made it less attractive to bring noncompliance claims against secured parties, even in "slam dunk" cases such as when notice of disposition was never sent, because this defense would have complicated issues concerning the secured party's intent and procedures, and thus made it more expensive

¹²⁷ See Rev. UCC §§ 9-625(f), 9-210.

¹²⁸ See Rev. UCC § 9-625(g).

¹²⁹ See Rev. UCC § 9-615 cmt. 6.

¹³⁰ See Rev. UCC §§ 9-601, 9-608, 9-615(d).

¹³¹ See Rev. UCC § 9-615(f).

¹³² See *id.*

¹³³ See Braucher, *supra* note 58, at 110-12 (citing Revised Article 9, Council Draft No. 3, Nov. 20, 1997, § 9-627(d)).

for consumers to litigate these issues.¹³⁴ Fortunately for consumer debtors and obligors, this good faith defense never made it to the final version of Revised Article 9.¹³⁵

E. Transition Rules.

Revised Article 9 has made significant changes in the methods in which secured parties must perfect and enforce their security interests.¹³⁶ For instance, in commercial and/or consumer transactions¹³⁷ entered into after the Effective Date, the creditor who prefers to perfect by filing must generally file a financing statement in the jurisdiction where the debtor is located,¹³⁸ not where the collateral is located.¹³⁹ In light of this new burden on secured parties, Revised Article 9 has adopted transition rules which allow preexisting, valid financing statements to remain effective after the Effective Date, until the earlier of (1) the date in which the financing statement would normally lapse under the law of the jurisdiction in which it was filed or (2) June 30, 2006.¹⁴⁰ If a financing statement expires within five years of filing—as is usually the case, the secured party must file a continuation statement¹⁴¹ or initial financing statement¹⁴² before the pre-Revised Article 9 filing lapses in order to maintain priority. However, in situations in which a secured party perfects its interest in a manner other than by filing, the secured party has one year to comply with Revised Article 9's requirements for perfection.¹⁴³

More importantly, any action to enforce a security interest created before or after the Effective Date must comply with the enforcement provisions of Revised Article 9.¹⁴⁴ This means, *inter alia*, that after July 1, 2001, a secured

¹³⁴ See *id.*

¹³⁵ See *id.* Also noteworthy is a proposed cap on statutory damages in class actions at the lessor of \$500,000.00 or 1% of the net worth of the secured party, which was part of an earlier draft of Revised Article 9 but never made it into the final version. See *id.*

¹³⁶ See Harry C. Sigman and Edwin E. Smith, *Revised Article 9's Transition Rules: Insuring a Soft Landing*, 55 BUS. LAW. 1065, 1066 (2000).

¹³⁷ Rev. UCC §§ 9-310(b)(2), 9-309(1) (automatic perfection for purchase money security interests in consumer goods).

¹³⁸ See Rev. UCC §§ 9-301(1), 9-307.

¹³⁹ See Cur. UCC § 9-103.

¹⁴⁰ See Rev. UCC § 9-705(c).

¹⁴¹ See Rev. UCC § 9-705(d).

¹⁴² See Rev. UCC § 9-706.

¹⁴³ See Rev. UCC § 9-705(a).

¹⁴⁴ See Rev. UCC § 9-702 cmt. 1 ("[A] secured transaction entered into under former Article 9 must be terminated, completed, consummated, and enforced under this [Revised Article 9]").

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party in a consumer-goods transaction must always provide the specific disposition notice prescribed by Revised Article 9,¹⁴⁵ regardless of whether the security interest was created before or after the Effective Date. Also, recall that Revised Article 9 shortens the time period within which a debtor, or other interested party, can object to the strict foreclosure of her property.¹⁴⁶ Note, however, that even though the enforcement provisions of Revised Article 9 take effect immediately after the Effective Date, any lawsuit or other proceeding commenced prior to the Effective Date is not affected by Revised Article 9. Nevertheless, it's safe to say that, in general, secured parties in consumer transactions should conform their enforcement practices to Revised Article 9 no later than July 1, 2001 or risk invalidating their deficiency claims and/or facing noncompliance sanctions.

IV. Progress?

Revised Article 9 took some steps toward better defining the rules in secured transactions. However, the multitude of revisions made little substantive changes to the rules governing consumer transactions.¹⁴⁷ This was perhaps a result of the political compromise between consumer creditor representatives and consumer advocates.¹⁴⁸ Each group was more willing to maintain the status quo than be faced with a uniform body of law that contained harmful provisions for its side. Nevertheless, some of the compromised changes in Revised Article 9 may resolve some of the problems prevalent in consumer transactions.

The cross collateralization of consumer debts will continue to cause problems in consumer cases. For instance, creditors who cross collateralize consumer debts will run into complications when a debtor files bankruptcy. In such cases, the creditor's purchase money security interest in consumer goods might be avoided by a bankruptcy trustee¹⁴⁹ or debtor,¹⁵⁰ if the creditor did not file a financing statement covering the collateral, or otherwise perfect its security interest in the collateral, before the commencement of the bankruptcy.

Additionally, the ineffective default provisions in Revised Article 9 will continue to hamper debtors from defending against misconduct by consumer

¹⁴⁵ See Rev. UCC §§ 9-612, 9-614.

¹⁴⁶ See Rev. UCC § 9-620(c)(2).

¹⁴⁷ See Braucher, *supra* note 58, at 83; Warner, *supra* note 8, at 19.

¹⁴⁸ See Braucher, *supra* note 58, at 83.

¹⁴⁹ See 11 U.S.C.A. §§ 544(a)(1), (b)(1) (West 1993 & Supp. 1999) (trustee's avoidance of unperfected liens).

¹⁵⁰ See 11 U.S.C.A. § 522(f)(1)(B) (West Supp. 1999) (debtor's avoidance of nonpossessory, nonpurchase money security interest).

creditors, who have traditionally had broad powers under Article 9. A debtor will not be able to rely on the "rebuttable presumption" rule in a case in which the creditor has clearly acted in an unreasonable manner. As to the statutory penalty for a creditor's failure to send a surplus/deficiency notice, a debtor will still face the evidentiary challenge of proving that the creditor's omission was a part of a pattern and practice she employs in consumer transactions. Even in a case in which the secured party purchases the collateral for an unreasonably low price and then sues for a deficiency, the debtor will have to show, in order to reduce or eliminate the deficiency claim, that the disposition of the collateral resulted in proceeds significantly lower than in an ideal disposition in an arms length transaction. Thus, it seems that Revised Article 9's default rules, while purportedly improving remedies for consumer debtors, still make it difficult for a debtor to recover from a monolithic creditor.

Moreover, Revised Article 9's attempt to define specific terms in secured transactions still leaves room for ambiguities. For example, take the rights of a consumer obligor in a secured transaction that involves a co-signor who gave additional collateral for the loan.¹⁵¹ When the obligor defaults and the secured party repossesses the collateral owned by the co-signor, does the secured party have to give disposition notice to the principle obligor of the secured debt? Recall, under Revised Article 9, in a consumer-goods transaction, the debtor or any secondary obligor must receive notice of disposition.¹⁵² So, clearly, if the secured party had sought to sell the obligor's collateral, then the co-signor would have been entitled to receive notice. But here, as the secured party is seeking to satisfy the debt owed by the co-signor, as a guarantor, the secured party arguably need only send notice to the co-signor, because the obligor of the underlying debt is not a debtor or secondary obligor as to the co-signor's obligations.¹⁵³ This outcome is somewhat confusing, considering that the obligor's rights will be affected by the sale of the co-signor's collateral.

Revised Article 9, as it governs consumer transaction, is not totally devoid of improvements. The requirement that security agreements be authenticated, instead of signed, may facilitate the proof of security interests in consumer retail transactions where the only proof of the transaction is a sales receipt which contains a notation that a security interest is granted on the items purchased to the issuer of credit. In such cases, it would be easier to prove that the debtor's authentication was effectively conveyed onto a valid security agreement (assuming reasonable description), thus creating a perfected

¹⁵¹ See Braucher, *supra* note 58, at 93.

¹⁵² See Rev. UCC § 9-611(c).

¹⁵³ See *id.*

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security interest in favor of the issuer of credit. Additionally, the inclusion of examples of *per se* reasonable descriptions in Revised Article 9 will help courts determine the validity of security agreements, as well as help creditors create security documents that clearly conform with Article 9.

Additionally, the new definition of good faith should serve to improve fair dealings between creditors and consumers. Revised Article 9's affirmative step in expanding the definition of good faith should call attention to the duty of honesty and fair dealing which govern transactions under the UCC.

Finally, Revised Article 9 adds some consumer protection provisions that may prove to help consumers change the practices of unscrupulous creditors. Revised Article 9 not only requires notification on disposition of collateral, it also defines what reasonable notification consists of and penalizes a creditor for failing to comply with this requirement. Revised Article 9 further penalizes a creditor for consistently failing to respond to account inquiries regarding a particular debt or particular collateral. This sanction can cost a creditor \$500.00 per violation, as well as reduce the amount of the creditor's security interest to the level alleged by the obligor. Because of the potential of class actions that exists today, the threat of being sanctioned \$500.00 for each of a multitude of infractions might prod consumer creditors to reevaluate their collection strategies and procedures to bring them into compliance with the letter and spirit of Revised Article 9.