Gilmore: Security Interests in Personal Property

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Since this is a book review and not a mystery story, let it be said at the outset that Professor Gilmore's treatise is a fine text covering the myriad problems of security interests in personal property; indeed, it is probably a great treatise. As a working lawyer, I am somewhat reluctant to give it this ultimate accolade, since that is probably more properly the province of the legal scholar, but the treatise is deserving of the working lawyer's tribute.

For the lawyer of today who is bombarded on all sides with reading material, the prospect of working through 1,346 pages of text material on a subject matter now largely covered by article 9 of the Commercial Code may seem a wearisome undertaking and I confess that the prospect made me regret the promise glibly made some months ago that I would write this review. However, in fact, it turned into a most pleasant labor, not only because Professor Gilmore writes with a style that is graceful, lucid, and always interesting, but more especially because repeatedly there appeared excellent discussions and analyses of vexing problems and the suggestion of...
countless additional problems which are lurking about the practice of security transactions.

As is to be expected, the treatise is largely concerned with article 9 of the Commercial Code, but it includes an excellent discussion of the development of pre-Code financing devices which is both fascinating as history—legal as well as economic—and an indispensable background for the interpretation and application of the Code. Having served both as an associate reporter and reporter for article 9 of the Code, Professor Gilmore is obviously well steeped in the knowledge of the development of the Code and the problems which remain to be solved in working under it. Indeed, one of the pleasures of reading this treatise is seeing evidences of the author's candor in exposing as treatise writer the occasional shortcomings of his work as reporter and comment writer for the Code itself (e.g., p. 345). He likewise finds occasion as treatise writer to reconsider and vary the views he has expressed as a law review author (e.g., pp. 814-15).

From the perspective of a practicing attorney, the value of a treatise is the amount of assistance that can be expected from it. Professor Gilmore's work satisfies this test as well as could be expected. He deals with countless problems in unrelated financing fields, analyzes them well, presents (and fairly) the opposing arguments, and supplies a wealth of citations to decisions, law review articles and other materials bearing on the problems. This is the type of practical assistance that lawyers need, especially in a field such as personal property security law, which Professor Gilmore properly characterizes (p. viii) as having been, for the past hundred years, an unstable body of law and which, in my opinion, is likely to continue to be such, the Code notwithstanding.

As Professor Gilmore proves to the reader time and again, article 9 is actually quite similar to its fellow articles in that the apparent simplicity which it provides is only a surface covering for some real booby traps. Thus, while obtaining an article 9 security interest is made as easy as falling off a log,1 the security interest, once taken and perfected, is circumscribed by a network of tight and sometimes unexpected limitations (p. 364). Some of the traps are as simple as the problem of whether the inclusion of a claim to "proceeds" in a financing statement will confer upon the debtor an implied power of sale (pp. 351, 729). Others, however, are novel and disconcerting, such as the problem of whether subordination agreements or negative pledge agreements are subject to the article 9 rules (chs. 37 & 38) and the suggested possibility that by the device of perfection other than by filing, a non-purchase-money lien may be given priority

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1. He argues, for instance, and quite convincingly, that a § 9-402 financing statement could well suffice as the sole paper work required to create—and perfect—a security interest, one Rhode Island decision to the contrary notwithstanding (pp. 347-48).
over the lien arising from an after-acquired property clause in a prior perfected security agreement (pp. 912-13). An additional trap, at least made possible by the Code, is, of course, the idea that the Code has removed all the old lets and hindrances so that creditors can now exact as security every conceivable property interest the debtor may have or thereafter ever hope to have. Professor Gilmore concedes that the Code draftsmen may have overshot their mark (pp. 364-65) and warns that

if secured parties rush in to take the fullest advantage of the so-called "floating lien" provisions of the Article and seek to tie up all the debtor's present and future assets, then there will undoubtedly be, next depression time, a rash of priority cases in unheard-of volume and in unfamiliar contexts [p. 779].

Indeed, his comment in connection with the current problems of the priority of federal tax liens, "the simpler the security agreement—the more it looks like the old-fashioned mortgage on Blackacre—the less likely it is to be questioned and drawn into litigation" (p. 1073) may well be a valid generalization for most security agreements under the Code.

The above is not to suggest that there can be no points of disagreement with the treatise. Like article 9 itself, the treatise does not give consideration to the special problems of mortgages on the fixed assets, real and personal, of a business, given to secure a long-term loan, such as the typical public utility trust indenture to secure bond issues. The five-year refiling requirement of article 9 has tended to make utility lawyers and bond counsel tear out their hair in horror and the wretched problems (well documented in section 21.7 of the treatise) of refiling or making a new filing after a lapse demonstrate that this reaction is by no means groundless. The result, of course, has been that a number of states have either amended the Code, by adding a new subsection (5) to section 9-302 so as to eliminate the refiling requirement in such cases where a trust indenture or mortgage has been properly recorded as a real estate mortgage, or have adopted special statutes which completely or partially remove this type of financing device from the operation of the Code.

A second example is that the treatise, like article 9, appears to

2. This is certainly litotes and not hyperbole, for unless the secured party in such a case is ready to meet every kind of credit requirement of the debtor, he will find himself either waiving his overbroad security interest more and more or drying up the debtor's business. Neither is a happy prospect, for the legal effect of repeated waivers is quite unpredictable.

3. Thus proving myself a member in good standing of the "Don't be a Pig" school of advice to article 9 lenders, mentioned at p. 779 of the treatise.

4. Connecticut and Virginia are typical.

5. ILL. REV. STAT. ch. 95, § 51 (1963); IND. ANN. STAT. § 54-513 (Burns Supp. 1966); N.Y. LIEN LAW ch. 33, art. 8, § 190 (McKinney 1966); OHIO REV. CODE ANN. § 1701.66 (Page 1966).
dismiss rather blithely the problem of whether a secured party has title as opposed to merely possessing a lien. The basis for disregarding this issue is that the question has become largely irrelevant, but on the contrary it may still be a matter of fighting interest, especially in bankruptcy cases.\(^6\) The Code ducks this problem altogether as a matter of statutory enactment and instead attempts, by a comment to the official text (U.C.C. section 9-507, comment 1), to advise the bankruptcy courts how to apply their law. Professor Gilmore echoes this approach at section 44.9.1 of the treatise. Probably both the Code and the text would have served us better by meeting this problem head on as a matter of security law, rather than dealing with it in this left-handed fashion.

There are other matters in the treatise which are either surprising or with which I am in disagreement. For instance, it is at least twice repeated (pp. 481, 902-03) that no one ever thought of placing a mortgage on file before the time when the loan was made, with the thought of having the filing become effective when the mortgage rights accrued. It is further suggested that such an advance filing would probably have been a nullity. This will undoubtedly come as a shock to many lawyers and bond counsel dealing with long-term trust mortgages, since advance filing is rather common in this field so as to enable counsel to furnish at the closing an opinion that the mortgage constitutes a valid and direct first lien on the property and has been duly recorded. The practice has ample legal sanction\(^7\) and has been so well established that this feature of the article 9 filing procedure provides no novelty whatsoever to practitioners in this field. Likewise, the cavalier attitude of the treatise toward a contract to lend money, in connection with the priorities problems raised by future advances, is somewhat shocking (pp. 926-29). Professor Gilmore suggests that "the contract to lend money is . . . a most peculiar animal; maybe it is not a contract at all; if it is, it is a contract which may be breached with impunity" (p. 926). It is doubtful whether bankers making a loan agreement take such a light view of their contracts and certainly in these years of rapidly rising interest rates, the thesis that the contract may be breached with impunity is at war with the facts. The possibility of substantial damages arising from the breach of such a contract may be remote so far as the reported cases show, but such a possibility is nevertheless present\(^8\) and the reports indicate that there has been a substantial amount of litigation over breaches of such contracts.\(^9\) Again, it is surprising that Professor Gilmore would suggest, in connection with Code section 1-102(3),


\(^7\) 4 *Pomeroy, Equity Jurisprudence* § 1197 (5th ed. 1941); 4 *American Law of Property* § 16.71 (1952).


\(^9\) Annots., 44 *A.L.R. 1486* (1929); 56 *A.L.R. 1408* (1929).
that a lawyer would never try to argue that a contract provision could be upheld because it is not "manifestly unreasonable," even though it might be in some degree unreasonable (p. 1130). Appellate lawyers are quite accustomed to arguing that trial court findings which are not "clearly erroneous" must be upheld even though they concede that the reviewing court might find some error on the basis of its own weighing of the evidence. Similarly, utility lawyers have had no qualms about defending tariff provisions or other utility practices as not being "unduly discriminatory," while conceding that some elements of discrimination could be claimed.

The failure to treat a few problems which have proved most vexing was also initially disappointing. For instance, one of the great headaches facing a lawyer when the Commercial Code becomes effective in his state is the need to resolve the continuing problems of what acts of compliance are required in transactions which overlap the effective date. The filing requirements as applied to long-term mortgages with after-acquired property clauses or future advance provisions, or both, are typical, but there are many others. Upon sober reflection I concede that these problems are of relatively short-term interest and, therefore, could well be deleted, but it would have been comforting to have had this matter thoroughly reviewed. A similar situation exists with respect to the fixture problem discussed at chapters 28 and 30 of the treatise, in that a very common lien involved in fixture-priorities cases is the statutory mechanic's lien. While mechanic's liens are generally excluded from Code coverage, one might well expect to find the problems they raise discussed in a general treatise on security interests in personal property. Here again, however, Professor Gilmore cannot fairly be faulted because the mechanic's lien statutes are by and large a wealth of confusion (see section 33.2 of the treatise) and undoubtedly such a discussion would have substantially prolonged the work without providing a corresponding amount of benefit.

Finally, I would have welcomed more treatment of the problems which remain after the Code's reversal of the Benedict v. Ratner\textsuperscript{10} principle, and, particularly, of the effect of the reversal on the possible continuing application of that principle to real estate interests and especially assignments of rent. Professor Gilmore calls attention to the problem,\textsuperscript{11} but dismisses it on the ground that the Benedict rule has simply not been applied to real estate mortgage transactions for a generation. In view of the special rules applicable to real estate mortgages under which a mortgagor is absolutely entitled to possession and to rents, issues, and profits, at least until default and possession taken by the mortgagee, there may not normally be much

\begin{itemize}
\item \textsuperscript{10} 268 U.S. 353 (1925).
\item \textsuperscript{11} Section 41.9, p. 1111 n.1.
\end{itemize}
room for the application of the Benedict principle. Yet it is still a source of concern under state fraudulent mortgage statutes, at least where a present security interest is sought to be made effective on the rents, even though the mortgagor is given some freedom to use and dispose of the rent proceeds. It would appear that at least one solution to the problem where it may exist is to determine at what stage the rents, issues, and profits, on being paid and converted into cash or bank deposits, lose their character as real property interests and become chattel interests which are subject to the Code. Here again, however, the question is an esoteric one (notwithstanding that it is encountered, though perhaps not recognized) and may be somewhat afield of the principal thrust of the treatise.

All in all, the foregoing will be recognized and accepted as niggling in the main, and it should in no way detract from the conclusion that Professor Gilmore's treatise is an excellent work and one which can be, and is herewith, enthusiastically recommended.

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13. By classic rules of real estate law, covenants running with the land, including rents due under leases, remain real estate interests until breach, but after breach become choses in action governed by personal property law. Frink v. Bellis, 33 Ind. 135 (1870); Page v. Lashley, 15 Ind. 152 (1860).