

12)

**(1) Band Saw**

As to the Band Saw, Terry will have the superior interest if the email sent by Chic was sufficient to form an authenticated agreement. The Band Saw is clearly equipment that is used by Chic, so it is important to see which people might have an interest in it. Under the UCC, there are various rules of priority between competing competitors. Here, it is important to distinguish between which creditors are perfected and which are not, when they perfected, what they perfected an interest in, and how. The interests of all of the creditors in the bandsaw is analyzed below:

First, Ivan will not have any interest in the bandsaw, or any of the other things for that matter, because he did not properly attach the security interest between he and Chic. In order to properly attach, one must give value to the borrower, the borrower must have rights in the collateral, and there must be a contract (authenticated security agreement) that properly identifies the parties. First, Chic's security interest did not qualify for after-acquired assets purchased, so the band saw is not included on that ground. Second, his description of the collateral secured in the security agreement is too broad ("all of Chic's assets"), and therefore it is unenforceable and Ivan is an unperfected creditor.

Second, Rufus has validly attached his security interest as to Chic's inventory and equipment because he gave value, Chic had rights, and they executed a validly authenticated security agreement (although it is also overly broad, it is effective as to equipment and inventory because they are specifically described). He also perfected his interest on June 30 by filing a financing statement with the SOS which named the debtor, the creditor, and described the assets that were secured, so he is a perfected creditor with regard to equipment and inventory, and he will have superior interests to Ivan in that regard.

Finally, Terry might have a valid purchase-money security interest (PMSI) in the bandsaw, depending on if it was validly attached and perfected. The issue with Terry's attachment/perfection is the security agreement and authorization: can an email serve as an authenticated agreement between the parties? Under the UCC, the answer is yes, as long as the attachment contains all of the accurate

information (names of debtor, creditor, description of collateral). Assuming the SA described the band saw, he validly attached it. The return email indicating his assent will take care of the necessary requirements for filing with the SOS (names, desc. of property, authorization, etc). Because of this, Terry validly perfected his PMSI on 3/2.

Take the facts above, Terry's security interest would be superior to Rufus because he was the first to either file or perfect. Even had Terry filed later, he may have still had the superior interest because PMSI's are given "super priority" under certain circumstances.

(Note: If for some reason Terry's authorization/filing was deficient, then Rufus would take the band saw because he validly perfected a security interest in all equipment.)

## **(2) Unfinished Cabinets and Lumber**

Here, we must determine whether the cabinets and the lumber are subject to security interests, and if so, which creditor prevails. First, we must classify the goods to see if the descriptions used by the creditors are accurate. The unfinished cabinets would be classified as inventory, as Chic is a cabinetmaker and he presumably sells them. The lumber, while it could conceivably be classified as equipment used in his business, is more likely to be classified as inventory also because it is "consumed" during the course of his business, i.e., the lumber is used to make the cabinets.

Because Terry's security interest only applied to the band saw, he is an unsecured creditor as to the rest of any remaining debt that is owed to him. Therefore, the "battle" for the superior interest here is between Ivan and Rufus. As discussed above in detail, Ivan's overbroad description in his security agreement resulted in a failure to "attach" the security interest--therefore he is also an unsecured creditor under these circumstances. Rufus, as the only person to validly attach and perfect an interest in the goods, will prevail up to the extent of his debt (\$900) (see above analysis). As to the rest of any leftover collateral, Ivan would have priority over Terry because between unsecured creditors, first in time prevails.

## SELECTED ANSWER

12)

1. Terry has priority interests in the band saw. Under the UCC, goods which are not consumed quickly in a business and which are not held by a business for sale, purchase or lease are defined as equipment. Here, the band saw would qualify as Chic's equipment, since the saw would be used in Chic's business to manufacture finished goods. A security interest is an interest in a good or goods as collateral for a loan. Both parties must intend that the property serve as collateral for a loan. A purchase money security interest is a special type of security interest wherein the creditor loans money specifically for the purchase of the good or goods that will serve as collateral for the loan. Here, Terry loaned money to Chic (in the form of credit) for the purchase of the saw with the intention that the saw would serve as collateral for the loan. As such, a purchase money security interest in the saw was created in favor of Terry.

A security interest attaches to the collateral upon the occurrence of all three of the following things: The debtor must have an interest in the goods, the creditor must give value for the debt and also, the parties must have a security agreement. The agreement must be in writing and sufficiently identify the collateral. Here, Chic obviously had an interest in the saw, as it was the subject of the purchase. Also, Chic gave value on the debt when he extended the credit for the purchase of the saw. However, the security agreement did not come until later. It is irrelevant that the security agreement is in the form of an email, as the transmission of the email by Chic would probably suffice as being considered as signed by Chic. The band saw was clearly identified in the agreement as were the parties to the contract. At the point of the receipt of the agreement, the security interest attached and was enforceable against Chic by Terry.

A purchase money security interest in equipment is automatically temporarily perfected for 20 days. Before the expiration of 20 days, the creditor must otherwise perfect to maintain its status as a perfected secured creditor. One method of perfection is filing a financing statement with the Secretary of State where the debtor resides. There are several requirements for a properly filed financing statement but the facts here do not indicate that the financing statement was improperly filed, so I will assume that it was sufficient. Here, Terry filed the financing statement perfecting his purchase money security interest in the saw.

Rufus, on the other hand, did the same, Rufus took a security interest in Chic's equipment, but not a purchase money security interest, as the interest was in consideration of a past debt. The requirements for attachment seem to have been met, as there is a signed security agreement, Chic has interest in the collateral and Rufus gave value for the collateral upon the issuance of the loan. Rufus filed a financing statement, sufficiently describing his interest in Chic's "equipment." The financing statement will not fail with regard to the equipment

because of the supergeneric description of his interest in Chic's "other assets." (which will be discussed later). The financing statement perfected Rufus's security interest in Chic's equipment as well, including the saw.

When two creditors claiming an interest in collateral are both perfected, the rules of priority provide that the first to file or perfect has a superior interest in the collateral. Further, purchase money security interests have a super-priority and will defeat a perfected security interest even if the pmsi was perfected last. Therefore, Terry's pmsi in the band saw will have priority.

2. Goods which are consumed in the course of business or are otherwise considered as raw materials would be defined under the UCC as inventory. The cabinets and lumber would be considered raw materials and as such, classified as inventory. As stated before, a security agreement must sufficiently and clearly identify the nature of the collateral or else the security agreement is insufficient and invalid for vagueness. A supergeneric term such as "all assets" is insufficient to put any party on notice of an interest in Chic's inventory or equipment, etc. As such, the security agreement executed with Ivan is insufficient and without the security agreement, as discussed before, Ivan's security interest did not attach to any collateral and certainly was not thereafter perfected. As such he is an unsecured general creditor of Chic.

Rufus's later security interest, which was properly attached and perfected as discussed above, was effective with respect to Chic's inventory, as Rufus sufficiently described the collateral in the security agreement. As such, Rufus is a perfected secured creditor and the rule of priority provide and a secured creditor (who is perfected or not) will prevail over an unsecured creditor. As such, Rufus's interest in the unfinished cabinet and lumber is superior to Ivan's interests.

**END OF EXAM**

Question 12 - Selected Answer

2. Rufus has a superior interest in the three unfinished cabinets and 500 board feet of solid-oak lumber.
1. Terry has a superior interest in the band saw. Terry has a purchase money security interest by virtue of the security agreement emailed to Chic on March 2. Though Chic never signed the agreement, the intent to create a security interest can be proved via the email and voicemail and there is a document creating the security interest. Terry then perfected his interest by filing a financing statement on March 2 with the Texas Secretary of State. Though Ivan purportedly created a security interest prior to Terry's, the description in the Ivan-Chic security instrument of "All of Chic's assets" was insufficient. A valid security instrument may not have a super generic description of collateral. Thus Ivan's security instrument and subsequent financing statement were insufficient to give him priority in the band saw, or any other of Chic's assets.
2. Rufus has a superior interest in the three unfinished cabinets and the 500 board feet of solid-oak lumber (as previously stated). Rufus and Chic created a valid security interest on June 30, with a valid description of the collateral. While the last portion of the collateral description may be invalid ("...all other assets"), the description of "all of Chic's inventory, equipment" is valid. The security instrument complied with the previously given \$500 was sufficient to attach a security interest to Chic's inventory and equipment. And the filing of a financing statement by Rufus was sufficient to perfect his interest. The description of collateral in Rufus' financing statement, though super generic, is not fatal, as a super generic description is permissible in financing statements but not security instruments. Rufus has priority over Ivan, for the same reasons as stated in (1), and cover Terry, because Terry's security interest is only in the band saw.
1. A purchase money security interest is automatically attached by its nature. Value is given to the debtor by virtue of the item purchased and the creditor automatically has an interest in the collateral.

END OF EXAM