

BULK TRANSFERS UNDER ARTICLE 6 OF THE IOWA UNIFORM COMMERCIAL CODE REVISITED

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The May 1970 issue of the *Drake Law Review* contained an article written by one of the co-authors which examined the Iowa version of article 6 of the Uniform Commercial Code,¹ commonly referred to as "Iowa Bulk Transfer Law."² Recently, the American Bar Association's Committee on the Uniform Commercial Code made recommendations for certain changes in article 6.³ The primary purposes of this article are (i) to review decisions which pertain to article 6 rendered subsequent to the previous article (thus assuming familiarity with the previous article), and (ii) to suggest some sample forms for the Iowa lawyer to utilize in connection with bulk transfers which are included within article 6. A secondary purpose of this article is to compare the developing law with the changes to article 6 which have been proposed by the ABA Uniform Commercial Code Committee.

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1. Hansell, *Bulk Transfers Under Article 6 of the Iowa Uniform Commercial Code*, 19 DRAKE L. REV. 275 (1970).

2. IOWA CODE §§ 554.6101-.6111 (1981).

3. ABA COMM. ON THE U.C.C., SUBCOMM. ON THE REVISION OF ARTICLE 6 OF THE U.C.C., REPORT TO THE A.B.A. 1981 [HEREINAFTER SUBCOMMITTEE REPORT].

I. INTRODUCTION

The primary purpose behind the adoption of the bulk transfer provisions as set forth in article 6 of the Uniform Commercial Code (U.C.C.)⁴ is to afford protection to the persons who extend credit to business enterprises,⁵ and to give those creditors the opportunity to protect their claims against a transfer by the unscrupulous businessman to a bona fide purchaser of the business assets.⁶ To that end, article 6 requires that in order for transactions which come within its ambit to be effective against creditors, the *transferee* must give notice to the transferor's creditors that a transfer in bulk is about to take place and allow them an opportunity to protect their claims.⁷ Absent compliance with the provisions of article 6, the purchased property remains subject to the risk of attachment or levy by creditors of the transferor.⁸

Creditors of a business enterprise are, of course, protected to some extent by the general body of law in Iowa concerning fraudulent conveyances,⁹

4. References herein to the various sections of the Uniform Commercial Code will be cited by U.C.C. section number except where referring to a particular state statute.

5. *Yarbrough v. Rogers*, 300 So. 2d 286, 287 (Fla. 1974).

6. *Reed v. Anglo Scandinavian Corp.*, 298 F. Supp. 310 (E.D. Cal. 1969).

7. IOWA CODE § 554.6105 (1981).

8. In states which have adopted the U.C.C. section 6-106 optional provision, the transferee also will assume personal liability to the creditors. Iowa has not adopted that section. See note 99 *infra* for adopting states.

9. A 1971 Alabama case contains the classic elements of a fraudulent conveyance. In *McKissick v. Foremost-McKesson, Inc.*, 441 F.2d 811 (5th Cir. 1971), the plaintiff McKissick sought to enjoin the sale of two businesses pursuant to a levy of execution obtained by Foremost on the grounds that he, and not the judgment debtor, was the owner of the businesses. *Id.* at 812. The underlying cause of action was a suit by Foremost against a Clarence Hull d/b/a Milbrook Drug based upon an open account owing by Hull in the amount of \$11,493.10. At a deposition of Hull on February 26, 1969, Hull testified that he was the sole owner of the two businesses, and further admitted that he owed Foremost a large sum of money but did not know the exact amount thereof. *Id.* Subsequently, Foremost was granted a summary judgment in the amount of \$11,493.10, and Foremost levied on the businesses. *Id.* Following a sale of the entire inventory of one of the businesses, the United States Marshal proposed to sell the assets of the second business. At that point McKissick (who at that time was an inmate of Maxwell Air Force Base Federal Prison) contacted the Federal Marshal claiming that he was the owner of the businesses and the sale was postponed pending a hearing on the ownership of the business. At the hearing it was developed that three days after the Hull deposition, Hull executed a bill of sale to McKissick, his brother-in-law, "for past debts amounting to \$17,000.00." McKissick also claimed that he owned the second business even though no consideration was claimed to have passed nor any written instrument executed to effect the transfer. The court had little trouble in finding that the sale to the brother-in-law was fraudulent as to the creditors of the business, and further found that whereas no notice was given to known creditors of the business enterprises, pursuant to the Alabama U.C.C. § 6-105, both of the transactions were void as to creditors of the businesses. *Id.* at 814-15.

The common law of fraudulent conveyances as it exists in Iowa deals "not with absolutes but rather with badges or indices of fraud." *Rouse v. Rouse*, 174 N.W.2d 660, 667 (Iowa 1970). Among the badges or indices of fraud are inadequacy of consideration, insolvency of the trans-

but that protection is quite limited in its scope and would not provide adequate property protection for a creditor where the transferor-debtor had received adequate consideration for the property and then simply absconded with the proceeds. This loophole in the fraudulent conveyances law is intended to have been plugged by the provisions of article 6.¹⁰

A mere promise by the bulk seller that he will pay the creditors of the business does not satisfy article 6.¹¹ Compliance with article 6 in a covered

feror, and the pendency or threat of third-party creditor litigation. *Id.* The fraudulent conveyances law would also reach a transfer for purposes of collateral in certain circumstances but, as in article 6, such a transfer, even if other creditors are jeopardized, would be rarely set aside.

"A creditor may take security for the debt due him, even though he is aware that the purpose of the debtor in giving it is to hinder, delay and defeat, thus to defraud, other creditors. (Authorities cited). But if the creditor know[s] of the fraudulent purpose of the debtor, and accept[s] the mortgage wholly or in part to aid in accomplishing it, he participates in the wrong, and the mortgage is fraudulent against creditors, although it was only a reasonable amount of property to secure a valid debt."

Id. at 668 (emphasis original). Those factors are not alone determinative of a fraudulent conveyance such as to require a cancellation of the conveyance. The attacking party still has the burden of showing the grantee's intentional participation therein. *Id.*

A transfer of property which is exempt from execution is not subject to avoidance as a fraudulent conveyance. Any conveyance or purported conveyance of exempt property cannot be in fraud of creditors, as the property would have been exempt from general execution in any event. *Clay v. Koppel*, 193 N.W.2d 525, 528 (Iowa 1972).

10. *Hawklund, The Trouble With Article 6 of the U.C.C.: Some Thoughts About Section 6-104*, 82 Com. L. J. 361 (1977) [hereinafter cited as *Hawklund-104*]. As the title of Professor Hawklund's series of articles would suggest, there has been some feeling that article 6 is not as effective as it might have been. Article 6 "has been criticized as having not been drafted in clear, concise and explicit language, and further criticized on the grounds that its looseness and over-flexibility is out of place in a technical formal statute designed to protect creditors against fraudulent conveyances and dissipation of proceeds." *Wiklund Wholesale Co. v. Tile World Factory Title*, 57 Ill. App. 3d 269, —, 372 N.E. 2d 1022, 1024-25 (1978) (Pusateri, J., concurring).

11. *Atlas Merchandising Co. v. Johnny's Cal. Mkt., Inc.*, 25 U.C.C. Rep. 1427 (Pa. Ct. of Common Pleas 1977) (referring to the application of optional section 6-106). In *Atlas Merchandising*, Johnny's California Market, Inc., had agreed to sell to Brodak all of its business assets and inventory. At the time of the transfer, plaintiff was a creditor and notice of the sale was given pursuant to article 6. After the sale had been consummated, however, Brodak failed to pay the amount due plaintiff by Market. Brodak argued that since he had not agreed to discharge the debts of Market he should not be held liable. Further, he argued that the agreement between himself and Market, which provided that the transferor would pay all existing debts, constituted compliance with the U.C.C. The court cited section 6-106 (optional) to refute Brodak's argument that in extracting a promise from his transferor to pay off all existing debts, he complied with the act. *Id.* at 1428. The court noted that section 6-106 expressly states that the purpose of the section is to give the transferor's creditors direct protection against improper dissipation by the transferor of the consideration received for the transfer. *Id.* In this regard the court stated:

If we were to hold that the procedure used here constituted compliance with the act, then every purchaser of a business could escape responsibility by inserting a provision in the sales agreement to the effect that the seller would pay all existing debts. This

transaction is not mandatory, and a failure to comply with the terms thereof is not a ground for rescission of a sale contract where compliance with the article was not required by the buyer under the contract.¹² On the other hand, an agreement between the parties to a transaction that article 6 shall not apply to the transaction does not foreclose a creditor from asserting its claims against the transferee, despite the provisions of U.C.C. section 1-102(3) which allows variance of U.C.C. provisions by agreement.¹³ Parties to a transfer can nevertheless agree not to comply with article 6 and provide for private indemnification without violating the law.¹⁴ It has been held that article 6, in effect, creates a new cause of action or right of action on behalf of a creditor.¹⁵

It should be noted that the fact that a transfer may be ineffective as to certain creditors because of a failure to comply with article 6 does not mean a transferee becomes personally responsible for the *original debt* of the transferor.¹⁶ The transferee's exposure is limited to the property received in the bulk transfer.

Since the enactment of the Uniform Commercial Code Bulk Transfers Law in Iowa in 1966, the annotations to the Iowa Code do not indicate any case wherein article 6 was determinative of the issues. In a case decided by the Iowa Supreme Court in 1967, the court applied the pre-U.C.C. Bulk Sale Act¹⁷ and not the Iowa U.C.C. Thus, there does not appear to be a single Iowa Supreme Court case which has substantively considered the provisions of article 6 of the U.C.C.

II. ENTERPRISES AND TRANSACTIONS SUBJECT TO THE BULK TRANSFER LAW

In order for a transaction to be within the purview of article 6, the transaction must involve a business enterprise which is described in article 6 as being governed thereby. The principal business of the enterprise must be the sale of merchandise from stock¹⁸ and various factors are to be considered in making a determination as to the principal business of a company. Among those factors is the percentage of business or gross receipts generated from the sale of merchandise as opposed to assembling the units or

is exactly what the bulk transfer provisions of the code were designed to prevent.

Id. at 1428-29.

12. *Herrick v. Robinson*, 267 Ark. 576, —, 595 S.W.2d 637, 645 (1980).

13. *Fifth Third Bank v. Kentucky Club, Inc.*, 590 S.W.2d 686 (Ky. 1979).

14. *Mercantile Financial Corp. v. P & F Indus., Inc.*, 63 A.D.2d 1014, 406 N.Y.S.2d 357 (1978).

15. *Indon Indus., Inc. v. Charles S. Martin Distr. Co.*, 234 Ga. 845, 218 S.E.2d 562 (1975).

16. *Bill Voorhees Co. v. R & S Camper Sales, Inc.*, 605 F.2d 888 (5th Cir. 1979).

17. Iowa Code § 555.1 (1962) (repealed 1965 Iowa Acts, ch. 413, § 10102).

18. U.C.C. § 6-102. The Subcommittee Report would amend section 6-102(3) to subject businesses whose "assets, tangible and intangible, have a fair market value before the bulk transfer of \$10,000 or more and whose principal business is the sale or rental of inventory" to the provisions of article 6. See Subcommittee Report, *supra* note 3, at 6.

other activity. It is a factual question to be determined by the jury.¹⁹ The property transferred must be of a particular nature, (e.g., tangible property, not contract rights or good will),²⁰ and the transfer itself must be a transfer not in the ordinary course of business, of inventory, by a business enterprise the principal business of which is the sale of merchandise from stock.²¹ It is the act of *transfer* which is the significant event, and not the type or the amount of consideration received therefor. The notice to the creditors is necessary to allow the creditors to become aware that a transfer in bulk is about to take place so that the creditors then may examine the sale and determine whether or not they should intervene.²² The intent of the parties is irrelevant as to whether a transfer is subject to article 6.²³

In order for a transfer to qualify as a transfer in bulk, the sale must be an extraordinary one, a rare and irregular event occurring but a few times in the life of a merchant.²⁴ In *In re Albany Brick Co.*,²⁵ a bankruptcy case, the bankrupt had transferred \$36,000 worth of inventory to the defendant-buyer. The amount represented approximately one-third of the total inventory of the bankrupt who had two other business locations with inventory. The consideration for the transfer was a reduction in the indebtedness owed by the bankrupt to the defendant-buyer. No attempt was made to comply with article 6 and the parties to the transaction contended that the transaction was not subject to article 6 because the transfer was not of a "major part" of the inventory as stated in article 6 as one of the criteria for a bulk sale.²⁶ The \$36,000 of inventory was less than 50% of the total inventory in the three locations, and the buyer contended that the term "major part" meant more than 50% and thus there was no bulk transfer. The court agreed.²⁷ The bankruptcy trustee in *Albany Brick* had contended that article 6 applied to transfers of a major part of the inventory of an "enterprise," and that "enterprise" meant the one location at Jacksonville, Florida. Since the whole of that inventory had been transferred, the trustee argued the transfer thus fell within article 6. The court determined that "enterprise" would embrace the total operation and would include the inventory at all

19. *Marlick Constr. Co. v. T. Lynn Davis Realty & Auction Co.*, 140 Ga. App. 867, 232 S.E.2d 147 (1977).

20. *Standard Milling Co. v. Yoss*, 16 U.C.C. Rep. 815 (N.Y. Sup. Ct. 1975).

21. See *Hansell*, *supra* note 1, at 276 for further discussion of this point.

22. *Danning v. Daylin, Inc.*, 488 F.2d 185 (9th Cir. 1973).

23. *European-American Bank & Trust Co. v. County of Nassau*, 97 Misc. 2d 549, 411 N.Y.S.2d 851 (1978).

24. *First Nat'l Bank v. Crone*, 157 Ind. App. 665, —, 301 N.E.2d 378, 382 (1973).

25. 12 U.C.C. Rep. 165 (D.C. Ga. 1972).

26. U.C.C. § 6-102(1). The Subcommittee Report adopts a definition of "major part" as being "more than fifty percent in fair market value of the transferor's total inventory or equipment located in the United States and its territories as of the time the transfer is made." See Subcommittee Report, *supra* note 3, at 1.

27. *In re Albany Brick Co.*, 12 U.C.C. Rep. 165, 167 (D.C. Ga. 1972).

three locations, stating: "If the word 'enterprise' is to be construed as only the individual locations, it should be done by the legislature."²⁸ In this case the three locations were Jacksonville and Tallahassee, Florida, and Albany, Georgia.

Article 6 does not define the scope of the "enterprise" and the courts can be expected to make such a determination based upon the facts of each case. The creditor in *Albany Brick* may well have relied upon the inventory at all three locations and thus was not prejudiced (at least under article 6) by the transfer of all of the inventory of one location. In other factual situations, however, it may be unfair to allow a transfer to be excluded from article 6 simply because there were a number of separate locations where inventory was held by the same owner, and in those situations the "enterprise" may be restricted to certain locations.²⁹

To become subject to the provisions of article 6, there must be a transfer of "inventory". Section 9-109(4) of the U.C.C. states that goods are

"inventory" if they are held by a person who holds them for sale or lease or to be furnished under contracts of service, or if he has so furnished them, or if they are raw materials, work in process, or materials used or consumed in a business. Inventory of a person is not to be classified as his equipment.³⁰

28. *Id.*

29. See *National Bank v. Frydlewicz*, 67 Mich. App. 417, 241 N.W.2d 471 (1976). In *Frydlewicz*, there also was some question as to the scope of the "enterprise" represented the entire business or each outlet for the purpose of determining whether the sale was of a "major part" of the inventory. The court found that the enterprise must be construed as representing each retail outlet so as to effectuate the purpose of the bulk sale law. *Id.* at ___, 241 N.W.2d at 474.

30. U.C.C. § 9-109(4). Comment 3 of U.C.C. section 9-109(4) states:

The principal test to determine whether goods are inventory is that they are held for immediate or ultimate sale. Implicit in the definition is the criterion that the prospective sale is in the ordinary course of business. Machinery used in manufacturing, for example, is equipment and not inventory even though it is the continuing policy of the enterprise to sell machinery when it becomes obsolete. . . . When an enterprise is engaged in the business of leasing a stock of products to users (for example, the fleet of cars owned by a car rental agency), that stock is also included within the definition of 'inventory'. . . . In general it may be said that goods used in a business are equipment when they are fixed assets or have, as identifiable units, a relatively long period of use; but are inventory, even though not held for sale, if they are used up or consumed in a short period of time in the production of some end product.

Id. comment 3. The *Frydlewicz* court noted that items transferred in a bulk sale must be inventory, i.e. held "for sale or lease." *National Bank of Royal Oak v. Frydlewicz*, 67 Mich. App. at ___, 241 N.W.2d at 474. Further, "[t]he transferor enterprise must have as its principal business . . . the sale of merchandise from stock." *Id.* at ___, 241 N.W.2d at 474 (quoting *First Nat'l Bank v. Crone*, 157 Ind. App. 665, 301 N.E.2d 378 (1973)).

The transfer must not be in the ordinary course of the transferor's business, and the items transferred must constitute a major part of the transferor's inventory. "Major part" has been defined as "meaning something more than 50%." Whether 'major' is a quantitative or qualitative determination remains an open question; one which courts

One court has held that an exchange of inventory for other inventory is a transfer subject to article 6.³¹ While the provisions of article 6 are generally intended to prevent fraud on the part of the transferor and/or the transferee, an additional intention is to protect creditors against a sale for an inadequate consideration, even assuming the good faith of the transferor and the transferee. It is not the receipt of cash nor the lack thereof which is the evil article 6 is designed to prevent, but rather *the transfer itself* which may affect the interests of the creditors and of which the creditors ought to receive notice in order to protect their interests. While it is true that "[t]he purpose of a bulk transfer statute is to keep merchandise and inventory as a cushion available to satisfy the claims of creditors," it has been held that a businessman may not exchange his inventory for another type of inventory *even with equivalent value*, and avoid article 6.³² The creditor is to be allowed to police *any* bulk transfer, and the advance notice of the sale, whatever the consideration therefor, provides creditors the opportunity to investigate the sale prior to its consummation in order to determine whether or not any action is appropriate in order to protect their interests.³³

"Owners of hotels, restaurants and bars will generally have substantial investments in buildings and in other fixtures, making it unlikely that they will sell their inventories and disappear overnight, thereby jeopardizing the interests of their creditors."³⁴ Bulk transfers of such businesses generally have been held to be exempt from article 6.³⁵ A beauty shop or beauty salon is not subject to article 6 "because ordinarily that type of business is primarily a service business as opposed to one dealing primarily in the selling of merchandise."³⁶ Also, a transfer by a small loan company of its notes receivable is not an article 6 transfer³⁷ as the terminology of "materials, supplies, merchandise or other inventory" was held to refer only to *goods or things* which are kept for sale in the ordinary course of business.³⁸

have approached on an ad hoc basis. Ordinary course means day-to-day operation. *National Bank v. Frydlewicz*, 67 Mich. App. 417, —, 241 N.W.2d 471, 473-74 (1976)(citations omitted).

31. *Danning v. Daylin, Inc.*, 488 F.2d 185 (9th Cir. 1973).

32. *Id.* at 188.

33. *Id.*

34. *See Uarco, Inc. v. Peoples Bank & Trust Co.*, 414 F. Supp. 1219, 1220 (E.D. La. 1976)(data processing services business not subject to article 6).

35. U.C.C. § 6-102, comment 2; *De La Rosa v. Tropical Sandwiches, Inc.*, 298 So. 2d 471 (Fla. 1974); *Kentucky Club, Inc. v. Fifth Third Bank*, 590 S.W.2d 686 (Ky. 1979). Note, however, that the Subcommittee Report recommends inclusion of restaurants and bars as being subject to the bulk transfer laws when such businesses transfer a major part of their *equipment*. *See Subcommittee Report, supra* note 3, at 8-11. *See also All Nite Garage, Inc. v. A.A.A. Towing, Inc.*, 85 Nev. 193, 452 P.2d 902 (1969) (towing service business); *Buckley's, Inc. v. Tell-Mall, Inc.*, 93 Mich. App. 570, 287 N.W.2d 3 (1979) (restaurant).

36. *Yarbrough v. Rogers*, 300 So. 2d 286, 287 (Fla. 1974).

37. *Credithrift Financial Corp. v. Guggenheim*, 232 So. 2d 400 (Fla. 1970).

38. *Id.* at 401.

III. TRANSACTIONS EXCLUDED

Probably the most commonly used transfers which are excluded from article 6 are those which either grant a security interest in property or transfer property in satisfaction of a security interest.³⁹ In order for a transfer to be excluded as having been "made to give security for the performance of an obligation"⁴⁰ it is not necessary that the security interest be a purchase money security interest nor that new value be exchanged for the transfer. Thus, even if a transaction may be subject to attack as a preference under the bankruptcy laws it will not be, per se, violative of article 6. Such a transfer may be, of course, nevertheless avoided by a trustee in bankruptcy.⁴¹

The exceptions of transfers which are "made to give security for the performance of an obligation" and transfers "in settlement or realization of a lien or other security interests,"⁴² particularly wherein the opportunity is present to make a bulk transfer by way of security for an antecedent debt, have been criticized as allowing avoidance of the very purpose of the bulk transfer provisions. For example, a lender and a debtor can utilize the sections by the debtor granting the lender a security interest on account of an antecedent debt in all of the debtor's inventory (or inventory and equipment) and subsequently the lender may enforce its security interest and compel a sale of the property to satisfy the then secured obligation.⁴³

In *Pastimes Publishing Co. v. Advertising Displays*,⁴⁴ a situation was presented where that very vehicle could have been utilized by the parties. Pastimes Publishing Co. had ceased doing business as a book publisher some time in 1967 and was indebted to many creditors, among which was Midland Paper Company to whom Pastimes owed approximately \$34,000 for

39. U.C.C. §§ 6-103(1), (3).

40. U.C.C. § 6-103(1).

41. See *Transport Equip. Co., v. Guaranty State Bank*, 518 F.2d 377 (10th Cir. 1975). This point has been discussed at length by Professor Hawkland in his essay relating to section 6-103. Professor Hawkland suggests that the result of allowing a "bulk mortgage" and thus permitting a creditor to obtain a better position than another creditor with respect to an antecedent debt, "simply reflects the well-established state policy that preferences which do not violate the Bankruptcy Act are innocuous." Hawkland, *The Trouble with Article 6 of the U.C.C.: Some Thoughts About Section 6-103*, 82 COMML. L. J. 113, 115-16 (1977) [hereinafter cited as Hawkland-103].

42. U.C.C. §§ 6-103 (1), (3).

43. Hawkland-103, *supra* note 41, at 116.

44. 6 Ill. App. 3d 414, 286 N.E.2d 19 (1972). The *Pastimes* court further apparently found it necessary to avoid not only the initial transfer of the books to the third party, but also the assignment of the account receivable. The court reasoned that since the transfer of the "inventory" was ineffective, no account receivable could have arisen which could have been transferred to the creditor. *Id.* at ___, 286 N.E.2d at 22. The court went on to state that since the creditor failed to give notice of the assignment, the sale was ineffective as to other creditors. *Id.* at ___, 286 N.E.2d at 21-22. Such analysis was probably based upon the court's view of the transaction as a single event and not as two independent transactions. *Id.* at ___, 286 N.E.2d at 22. As valid as such a view may have been, the court's analysis is unfortunate.

prior purchases. On August 23, 1968, Pastimes sold its entire inventory which consisted of printed volumes of books to a third party for approximately \$27,000. On September 16, 1968, Pastimes assigned the receivable from the third party to Midland and executed a security agreement granting a security interest therein to secure Midland on its open account owing by Pastimes. The court, at the behest of other creditors, voided the transfer of the inventory and found that the transfer had not complied with article 6 and that there should be an equitable lien in favor of the creditors of Pastimes which was superior to the lien claimed by Midland.⁴⁵ Because the sale was ineffective as to the creditors of Pastimes, the court reasoned, nothing had been conveyed out of which an account receivable could have arisen and in which Midland could have taken a security interest.⁴⁶ The court apparently inferred some degree of collusion between Midland and Pastimes. In its discussion of the failure to give the article 6 notice to creditors, the court stated that "Midland and Pastimes failed to give notice to creditors as required by [s]ections 6-105 and 6-104 of the Commercial Code and consequently the sale to [the third party] was ineffective against Pastimes' creditors who without notice of the assignment were unable to protect their claims against Pastimes."⁴⁷ That comment is interesting in that the court refers to notice as apparently having been required of Midland, and further refers to the fact that the creditors were not made aware of the "assignment" where the assignment in the case relates not to an assignment of the inventory but rather to the assignment of the account receivable.⁴⁸

Even assuming that the provisions of article 6 applied to the transaction set forth in the *Pastimes* case, the creditor and the debtor could have accomplished the same end by utilizing the criticized provisions of section 6-103. Thus, the debtor could have granted to the creditor a security interest in the inventory of books on account of the antecedent debt, and subsequently the creditor could have declared the debtor to be in default and realized on its collateral pursuant to the terms of the security agreement. Each of the transfers would have been outside of the provisions of article 6, and the creditor would have been in the same position as that which it was attempting to attain by the apparently surreptitious method employed. This rather facile method of avoiding the specific provisions of article 6, of course, is not without its problems. The exemption granted by section 6-103(3) applies to a *security interest* and, arguably, would not apply to a purported secured transaction which in reality was intended to be a sale.⁴⁹

The *Pastimes* case raised other interesting problems with article 6 which were not addressed by the Illinois court. Pastimes had ceased its op-

45. *Id.* at —, 286 N.E.2d at 21.

46. *Id.* at —, 286 N.E.2d at 22.

47. *Id.*

48. *Id.*

49. See Hawkland-103, *supra* note 41, at 116.

erations as a going concern in 1967, and the attacked transfers took place in August and September of 1968. Thus, for the better part of a year the transferor had not conducted any business whatsoever. The transfer was, as noted by the court, clearly not in the ordinary course of the transferor's business;⁵⁰ but, on the other hand, at the time of the transfer Pastimes arguably was not an enterprise "whose principal business [was] the sale of merchandise from stock."⁵¹ If that had been the case, then the transaction was not within the ambit of the provisions of article 6, and the transfer should not have been held ineffective upon that basis. The character of the property as inventory, however, was not affected by the cessation of business. Once property has been defined as inventory under the U.C.C., the character of that property generally will not change in connection with bulk sales transactions entered into by the debtor. The goods were inventory when purchased and when the trade creditors relied upon the stock of merchandise in the extension of their credit.⁵²

The transaction of the *Pastimes* case does not set forth a factual pattern lending itself to the application of article 6, which has as its underlying purpose the protection of creditors against the merchant selling his stock and pocketing the proceeds, or paying his creditors less than he owes them.⁵³ In the *Pastimes* situation, the trade creditors certainly must have been aware of the fact that Pastimes was no longer actively engaged in business, and should have been concerned about whether or not their accounts would be paid. Thus, it is hard to muster much sympathy on their behalf on an equitable basis as against the creditor which acted to protect its own interest, albeit belatedly. The utilization of article 6 to achieve equity in situations where prudent commercial practice would have properly protected each creditor does not seem appropriate.

A repossession of inventory property by a secured creditor, whether or not that secured creditor has taken such steps as may have been necessary to perfect its security interest, generally is exempt from the provisions of article 6,⁵⁴ and an unsecured creditor has no standing to complain of a repossession and retention of the collateral in satisfaction of a debt.⁵⁵ Likewise, it is no defense to an action for a deficiency judgment that the initial repossession and sale of collateral was illegal and ineffective because the repossession did not comply with article 6. Such repossessions and sales are

50. *Pastimes Publishing Co. v. Advertising Displays*, 6 Ill. App. 3d at ___, 286 N.E.2d at 21.

51. U.C.C. § 6-102(3). *But see* *Danning v. Daylin, Inc.*, 488 F.2d 185 (9th Cir. 1973) (termination of business does not free transferor of bulk sale of former inventory).

52. *In re Watertown Tractor & Equip. Co.*, 94 Wis. 2d 622, 289 N.W.2d 288 (1980).

53. U.C.C. § 6-101, comment 2.

54. *United States Shoe Corp. v. Cudmore-Neiber Shoe Co.*, 419 F. Supp. 135 (W.D.S.D. 1976).

55. *Id.* *But see* *Starman v. John E. Wolfe, Inc.*, 490 S.W.2d 377 (Mo. 1973).

specifically excluded from article 6.⁵⁶

The assumption of an antecedent debt by a third party transferee is fair and adequate consideration for a transfer of property under general fraudulent conveyance law, and also may be used to avoid the application of article 6. In *American Metal Finishers, Inc. v. Palleschi*,⁵⁷ a bank had a security interest in all of the property of a transferor. The transferor made a bulk transfer to a third party transferee in return for which the transferee assumed the debt to the bank. Creditors of the transferor contended that the transfer was violative of article 6 and that the transfer should be voided.⁵⁸ The court held there had been no prejudice to anyone in that the bank could have taken the property in satisfaction of the debt and then transferred the property to the third party transferee. There was no "invidious reason" for using the mechanism of one transfer rather than two.⁵⁹ The transfer was in full satisfaction or realization of a security interest and thus exempt from the article 6 notice provisions.⁶⁰

An analogous case arose in *Mayfield Dairy Farms, Inc. v. McKenney*.⁶¹ In that case, between 1974 and June 1, 1977, defendant Shrout was the owner of a grocery business. On June 1, 1977, he sold the business to McKenney for \$62,791. At that time, F.G. Shrout (not the owner) held a security interest in fixtures and equipment in the amount of \$48,791 which he had taken when he sold the business in 1974. Subsequently, McKenney borrowed \$30,000 from a bank and paid a portion to F.G. Shrout as a partial payment on their debt. F.G. Shrout released his security interest and allowed the bank to take a first security interest in the furnishings and equipment. McKenney also executed a note to F.G. Shrout for the balance and gave him a second security interest in the fixtures and equipment. At the time of the sale, defendant Shrout was indebted to Mayfield Dairy for \$10,000 on merchandise sold and delivered to his store. This obligation was not disclosed to McKenney and there was no compliance with article 6. Mayfield then sought a judgment against defendant Shrout and McKenney, claiming that since there was no compliance with article 6, the sale was ineffective as to it, and further claiming that the security interests of F.G. Shrout and the bank were subordinate to its claim because they knew or should have known that there was no compliance with article 6.⁶² The buyer and seller had not insisted on compliance with article 6, and the bank and F.G. Shrout contended that they were not parties to the transfer and only had taken security interests in the property. The court held that the transfer was for

56. *United States v. Gore*, 437 F. Supp. 344 (E.D. Pa. 1977).

57. 55 A.D.2d 499, 391 N.Y.S.2d 170 (1977).

58. *Id.* at ___, 391 N.Y.S.2d at 171.

59. *Id.* at ___, 391 N.Y.S.2d at 171.

60. *Id.* at ___, 391 N.Y.S.2d at 172.

61. 27 U.C.C. Rep. 1088 (Tenn. Ct. App. 1979).

62. *Id.* at 1089.

purposes of security only and that as such it was excepted from the terms of article 6 pursuant to U.C.C. sections 6-103(1) and 9-111.⁶³ As noted by the U.C.C. reporting service editor, the transfer from seller to buyer was not made to give security for the performance of an obligation, but was a sale of goods in which F.G. Shrout held a security interest.⁶⁴ The entire transaction, however, might have been viewed as a transfer in settlement or realization of a lien or other security interest, and hence exempted under section 6-103(3).

IV. LIST OF CREDITORS

The responsibility for the accuracy of the list of creditors rests solely with the *transferor*,⁶⁵ absent the knowledge of the transferee that the list was somehow inaccurate. It is important to be aware that the list of creditors should include not only those who are in fact creditors, but also those who claim creditor status or who assert any claim against the transferor, even if those claims are disputed. Although article 6 does not reflect the concepts of constructive notice or knowledge,⁶⁶ the prudent transferee will examine court dockets in the relevant jurisdictions, conduct U.C.C. filing searches, and take other such action to assure that claimants who may have a basis to assert constructive knowledge on the part of the transferee are included in the list of creditors. Secured creditors as well as unsecured creditors are entitled to notice.⁶⁷

In *Adrian Tabin Corp. v. Climax Boutique, Inc.*,⁶⁸ the buyer in a bulk sale had received an affidavit of "no creditors" from the seller and had no actual knowledge of any creditors. The New York Court of Appeals was asked to determine whether the transferee nevertheless had a duty to make careful inquiry as to the possible existence of creditors, and held that the transferee had no such duty.⁶⁹ The trial court had set aside the sale on the basis that the transferee had not requested an examination of the seller's books and had not questioned the source of the inventory involved in the sale, holding that the purchasers had not made a careful inquiry of the seller

63. *Id.* at 1090.

64. *Id.*

65. U.C.C. § 6-104.

66. *Federal Ins. Co. v. Pipeco Steel Corp.*, 125 N.J. Super. 563, 312 A.2d 510, 511 (1973); *Adrian Tabin Corp. v. Climax Boutique, Inc.*, 34 N.Y.2d 210, 212, 313 N.E.2d 66, 68 (1974). The Subcommittee Report would impose upon the transferee the duty to conduct at least some investigation as to the existence of creditors. A transfer would be ineffective where an error or omission was "reasonably discoverable by the transferee," e.g. revealed in the transferor's book-keeping records or ascertainable by "reasonable inquiry" concerning the transferor's creditors. See Subcommittee report, *supra* note 3.

67. See *Automatic Truck and Trailer Wash Centers, Inc. v. Eastamp, Inc.*, 320 So. 2d 79 (Fla. 1975).

68. 40 A.D.2d 146, 338 N.Y.S.2d 59 (1972), *aff'd*, 34 N.Y.2d 210, 313 N.E.2d 66 (1974).

69. *Id.* at —, 338 N.Y.S. at 60-61.

as to existing creditors and thus acted at their peril.⁷⁰ The appellate court reasoned that because "knowledge" means "actual knowledge" under the U.C.C.,⁷¹ a bulk sale may not be set aside as to creditors not listed in the affidavit of whom the transferee had no knowledge.⁷² Parenthetically, the intermediate appellate court (which had reversed the trial court) noted that the purchasers had no reason to disbelieve the truthfulness of the affidavit, and held in favor of the buyer, explaining

that even were the purchasers under a duty to make careful inquiry, they complied with that responsibility in this case by making a lien search and by making inquiry of the seller's attorney, who represented that all creditors had been paid and that he had seen the checks sent out to them in payment of the seller's obligation.⁷³

Absent knowledge of an inaccuracy in the list of creditors, the transfer is effective even against creditors who were not listed.⁷⁴ But it should be noted that any creditor technically can take advantage of non-compliance. Even a creditor who is listed will not be precluded from claiming non-compliance with article 6 if a defect exists elsewhere in the transfer.

The status of a person as a creditor is determined as of the time immediately prior to the transfer. A person who becomes a creditor *because of* the transfer is not protected by article 6 and is not entitled to the notice.⁷⁵

V. SCHEDULE OF PROPERTY

The preparation of the schedule of property to be transferred is essential to obtain the protection of article 6. The property schedule must set forth a list of all property to be transferred and the property must be described in sufficient detail to allow identification of each item.⁷⁶ This schedule must be preserved by the transferee for a period of six months *following the transfer*.⁷⁷

There is little litigation on the question of the accuracy of the schedule of property, perhaps because of the practical difficulties in defending such an error if one is made. Neither transferor nor transferee can very easily claim that it transferred or received property of which it was not aware. Further, a creditor who has discovered a bulk sale or who was notified thereof, and who examined the schedule of property required to be kept or recorded, would be immediately apprised of the location of the property

70. *Id.* at ___, 338 N.Y.S.2d at 61.

71. U.C.C. § 1-201(25).

72. *Adrian Tabin Corp. v. Climax Boutique, Inc.*, 40 A.D.2d at ___, 338 N.Y.S.2d at 61-62.

73. *Id.* at ___, 338 N.Y.S.2d at 62.

74. *Fico, Inc. v. Ghingher*, 287 Md. 150, ___, 411 A.2d 430, 435 (1980).

75. *Brown v. Superior Pontiac-GMC, Inc.*, 352 So. 2d 576, 577 (Fla. 1977) (dissenting shareholder not an article 6 creditor).

76. U.C.C. § 6-104.

77. *Id.*

(i.e., either the transferor or transferee would have it) and that creditor can easily ascertain the status of his interest.

Where an attempt has been made to comply with article 6, the transferee undoubtedly will make every effort to make the schedule of property accurate, as by so doing he is serving his own best interest. Unlike the list of creditors, the transferee has the knowledge necessary to make the property schedule accurate.

VI. NOTICE

The notice which is to be provided to creditors is the heart of article 6.⁷⁸ Section 6-105 provides that a bulk transfer is ineffective against creditors of the transferor "unless at least ten days before [the transfer] the transferee gives notice of the transfer *in the manner* and to the persons hereinafter provided."⁷⁹ The ten-day period has been held by one court as being calculated by excluding *both* terminal days.⁸⁰ Thus, a notice mailed on the second day of the month and a transfer on the twelfth was not in compliance.⁸¹ Section 6-107, however, states that "the notice in any case shall be delivered personally or sent by registered or certified mail. . . ."⁸² Reading the two sections together makes it clear that the notice is simply to be sent at least ten days before the date of the transfer. Thus, the cases such as *Starman v. John E. Wolfe, Inc.*,⁸³ which construe the phrase "gives notice" to mean that the creditors must actually *receive* the notice ten days prior to the transfer, are clearly wrong, particularly in light of the fact that U.C.C. section 1-201(38) defines "send" as meaning "to deposit in the mail or deliver for transmission by any other usual means of communication."⁸⁴ The definition of the word "send" in the U.C.C. includes the following statement: "The receipt of any writing or notice within the time at which it would have

78. *Starman v. John E. Wolfe, Inc.*, 490 S.W.2d 377, 384 (Mo. 1973).

79. U.C.C. § 6-105 (emphasis added).

80. *Goodyear Tire & Rubber Co. v. Tabs, Inc.*, 26 U.C.C. Rep. 1290, 1295 (Conn. Super. Ct. 1979).

81. *Id.* at 1294-95.

82. U.C.C. § 6-107.

83. 490 S.W.2d 377 (Mo. 1973). In *Starman v. John E. Wolfe, Inc.*, the Missouri Court of Appeals said: "In order to satisfy [section 6-105] the transferee should give notice to creditors so that they *receive* notice at least ten days prior to taking possession of the goods or prior to paying for them." *Id.* at 384 (emphasis added). The case has been criticized by Professor Hawkland because the statute requires only that the transferee "give" notice of the transfer. See Hawkland-104, *supra* note 10, at 362. "Give" is defined in U.C.C. section 1-201 (26) as "taking such steps that may be reasonably required to inform the other in ordinary course whether or not such other actually comes to know it." Professor Hawkland suggests that "actually, the draftsmen undoubtedly meant that the notice must be *sent* ten days before the transfer." Hawkland-104, *supra* note 10, at 362. The recommendations of the Subcommittee Report would amend section 6-105 to require a fifteen day notice period. See Subcommittee Report, *supra* note 3.

84. U.C.C. § 1-201(38).

arrived if properly sent has the effect of a proper sending."⁸⁵ Thus, if it became necessary to defend a notice of less than ten days it would seem arguable as within the literal reading of the U.C.C. that the bulk transfer was in compliance with the terms of article 6 if that notice were personally delivered to the creditors on or before the same date those creditors would have received the notice had it been sent through the mail. Since section 6-105 only requires that the transferee *give notice* at least ten days before the transfer, and since a notice will comply with article 6 if it is *sent* by registered or certified mail, and since a notice can qualify as having been sent if it is simply delivered within that same time period within which it would have been delivered had it been placed in the U.S. Mail, then a notice delivered one or two days into the ten day period arguably should qualify. It should be noted, however, that section 6-107 allows a notice to be sent by registered or certified mail or "delivered personally" to the creditors,⁸⁶ and this language may counter any argument that a late personal delivery qualifies as proper notice.

VII. CREDITOR REMEDIES

Compliance with article 6 does not in any way release the transferor from his liability on the original debt,⁸⁷ and the creditor retains all his traditional remedies against the transferor.⁸⁸

A transfer which does not comply with article 6 is technically ineffective against any creditor.⁸⁹ The term "creditor" has been interpreted to mean only those persons who hold liquidated claims, rather than those persons who assert potential liability for a breach of contract.⁹⁰ This is logical in light of the general purpose of article 6 as a vehicle to protect the trade creditors of a business who are relying on its stock of goods and its nature as a going concern to be paid. A dissenting stockholder is not such a creditor.⁹¹ It also has been held that a taxing body such as the IRS or a state department of revenue with respect to tax liability of the transferor is not such a creditor.⁹² Article 6 will not, however, prevent a state in its tax-collecting status from pursuing the property in the hands of a transferee.⁹³ A prudent transferee is still well advised to provide notice to the Internal Revenue Ser-

85. *Id.*

86. U.C.C. § 6-107.

87. *McClain v. Laurens Glass Co.*, 127 Ga. App. 316, 193 S.E.2d 195 (1972).

88. *American Express Co. v. Bomar Shoe Co.*, 125 Ga. App. 408, —, 187 S.E.2d 922, 924 (1972).

89. U.C.C. § 6-104.

90. *Aluminum Shapes, Inc. v. K-A-Liquidating Co.*, 290 F. Supp. 356, 358 (W.D. Pa. 1968).

91. *Brown v. Superior Pontiac-GMC Inc.*, 352 So. 2d 576, 577 (Fla. 1977).

92. *Richards v. Blackman*, 233 Ga. 739, 213 S.E.2d 638, 640 (1975).

93. *Harbor Air Service, Inc. v. State*, 88 Wash. 2d 359, —, 560 P.2d 1145, 1147 (1977).

vice, the State Department of Revenue and the County Treasurer of the county wherein the goods are kept.⁹⁴

It has been held that a garageman who holds an artisan's lien upon certain property qualifies as a "creditor" under the terms of article 6, and may utilize the provisions which declare a bulk transfer to be ineffective as to creditors who have not received a proper notice of the transfer.⁹⁵ Secured creditors, whether by the grant of a security interest or by executing on a judgment, will prevail over unsecured creditors in the distribution of property the transfer of which was avoided under article 6.⁹⁶

A mere failure to comply with the requirements of article 6 does not render the sale or contract void as between the parties, although the seller's alleged failure to comply may give rise to a claim of fraud or misrepresentation vitiating the agreement.⁹⁷

The lack of straightforward provisions of article 6 pertaining to the remedies of which aggrieved creditors may avail themselves has caused difficulty for the courts in ascertaining exactly what form of remedy to allow such creditors. The remedy sections of article 6 were purposefully left open by the drafters of the U.C.C. for the states to fashion non-uniform provisions.⁹⁸ Where an unsecured creditor has not received notice of a bulk sale, and where the proceeds of the bulk sale have been dissipated and the transferred property sold to bona fide purchasers by the transferee, the creditor finds itself at a distinct disadvantage under the provisions of article 6. The drafters provided an optional section 6-106 which placed a duty upon the transferee to assure that the consideration received in the bulk transfer was utilized to pay the listed debts of the transferor. The optional section, however, has not been adopted by a large number of states⁹⁹ and in the interest of protecting the good faith transferee, the unsecured creditor may appear to be disadvantaged.¹⁰⁰

94. See Hansell, *supra* note 1, at 285.

95. *Johanna Farms, Inc. v. Elliott Equip. Co.*, 278 Md. 137, —, 360 A.2d 436, 440-41 (1976).

96. *In re Bulk Sale of Clement*, 18 U.C.C. Rep. 1280, 1283 (Pa. Ct. of Common Pleas 1976); *Huguelet v. M & M Ass'n., Inc.*, 375 So. 2d 1150, 1151 (Fla. 1979).

97. *Martinez v. Clemente*, 19 U.C.C. Rep. 652 (N App. Div. 1976).

98. U.C.C. § 6-111, comment 2.

99. Optional section 6-106 has been adopted, with some variations, in the following jurisdictions: Alaska, California, Florida, Idaho, Kansas, Kentucky, Maryland, Minnesota, Mississippi, Montana, New Jersey, North Dakota, Oklahoma, Pennsylvania, South Dakota, Tennessee, Texas, Utah, Virgin Islands, Washington, and West Virginia.

100. Where the parties to a transfer which is subject to the provisions of article 6 have complied with the provision thereof regarding notice to the creditors, and where the only omission has been the exclusion of a judgment creditor from the list of creditors (unbeknownst to the transferee), the judgment creditor which has been omitted is not permitted to assert a claim against either the transferee or an escrow fund which may have been established pursuant to the optional U.C.C. section 6-106 for payment of creditors of the transferor. In such a situation, the judgment creditor is in a position where he cannot attach the goods themselves

While a transfer which does not comply with article 6 is ineffective as to creditors, the general remedy of such creditors is to bring an *in rem* action against the goods,¹⁰¹ or to simply proceed against the transferor. Reaching a transferee in the form of a money judgment is difficult.¹⁰² The theories under which creditors have attempted to secure money judgments against transferees are generally based upon either assumption of the debt of the transferor, conversion, a tracing theory, or for the value of the property which had been disposed of by the transferee by means of a constructive trust. It is well established that non-compliance with article 6 does not impose liability upon the transferee for the original debt of the transferor.¹⁰³ In the conversion theory, the right of action for conversion depends upon the creditor's right to possession of the property, and since the unsecured creditor is not entitled to possession this theory is generally unsuccessful.¹⁰⁴ The tracing theory is generally asserted to claim either the price paid by the transferee or the proceeds of the transferee's sale to a bona fide purchaser. The success of this theory, however, depends upon whether or not the funds may be traced and collected and thus presents fairly difficult practical problems. The constructive trust theory is more easily applied where the action against the transferee is based upon his accountability for the property which was received in bulk, as the practical tracing problems are thereby eliminated. However, in the absence of the adoption of the optional U.C.C. section, the courts have substantial difficulty in imposing such a burden on the transferee where the property no longer is in its possession, and in general the transferee has not been held personally liable for the value of disposed-of bulk property to an unsecured creditor who has not received notice of a bulk sale.¹⁰⁵

which had been transferred in the bulk sale nor can he even share on a prorata basis with the other creditors who are to be paid from the escrow fund. The omitted creditor follows all of the listed creditors in order of priority and can receive proceeds of the established fund (if there be such) only to the extent that proceeds remain available after payment of all of the other creditors which proceeds would pursuant to the sale or escrow agreement be paid over to the transferor. *Fico v. Ghingher*, 287 Md. 150, 411 A.2d 430 (1980).

101. In cases where Article 6 does not apply to the transfer, a creditor nevertheless may pursue the goods in the hands of a transferee under an equitable lien theory. In *Nelson v. Pampered Beef-Midwest, Inc.*, 298 N.W.2d 281 (Iowa 1980), the court imposed an equitable lien upon certain property which had been transferred without satisfying unsecured creditors of the transferor. *Id.* at 288. The court noted that such a transfer may occur in a way which affords unsecured creditors no remedy, but discussed circumstances in which such creditors may have rights *in rem* against the transferred goods or *in personam* against the transferee. *Id.* at 285-86.

102. See *H.L.C. Imports Corp. v. M & L Siegel, Inc.*, 98 Misc. 2d 179, 413 N.Y.S.2d 605 (1979).

103. *Get It Kwik of Am., Inc. v. First Ala. Bank*, 361 So. 2d 568 (Ala. 1978); *Cornelius v. J & R Motor Supply Corp.*, 468 S.W.2d 781 (Ky. 1971).

104. *Charles S. Martin Distrib. Co. v. Indon Indus., Inc.*, 134 Ga. App. 179, 213 S.E.2d 900, *rev'd on other grounds*, 234 Ga. 845, 218 S.E.2d 562 (1975).

105. See, e.g., *Bill Voorhees Co. v. R & S Camper Sales of Birmingham, Inc.*, 605 F.2d 888

The rights of a bankruptcy trustee vis-a-vis existing creditors of a bankrupt transferor were examined in *In re Gruber Industries, Inc.*¹⁰⁶ In *Gruber*, Gruber Brothers, a business enterprise, transferred its assets to Gruber Industries, Inc., which assumed all liabilities of the transferor. A creditor of Gruber Brothers was not notified pursuant to article 6 of the pending transfer. Subsequently, Gruber Industries filed a chapter XI petition in bankruptcy. The creditor who had not been notified levied on the property, and the trustee for Gruber Industries enjoined its enforcement. The creditor contended that its interest in the transferred property was prior to that of the trustee because of the failure to comply with the provisions of article 6. The court found, however, that the transfer was not void but merely voidable, and until some action was taken by the creditor of the transferor, the transferred property was lawfully that of the transferee and thus was subject to the satisfaction of its debts.¹⁰⁷ The trustee in bankruptcy intervened prior to any action taken by the creditor to enforce its rights under article 6 and the creditor's interest was thus subordinate to the lien creditor status of the bankruptcy trustee.¹⁰⁸

A good general discussion of several article 6 issues is found in *National Bank v. Frydlewicz*.¹⁰⁹ In December of 1968, Frydlewicz asked the bank for a loan of \$20,000 to purchase inventory for his furniture business. The business was a retail outlet for a furniture wholesale company which was owned and operated by Frydlewicz. As collateral for the loan, Frydlewicz gave the bank a security interest in all of the inventory of the outlet store. Frydlewicz declared bankruptcy in September of 1969. In March of 1969, Frydlewicz agreed to lease the business to National Unclaimed Furniture Showrooms, and National agreed to purchase all of the inventory. During the negotiations, Frydlewicz represented to National that there were no liens of any kind against the inventory. No further statements were requested from Frydlewicz and no notice was given of the inventory purchase. In May of 1970, the bank served a writ of attachment on National against the inventory located in its showroom. The court determined that the bank was an unperfected secured creditor as it had filed its financing statement with the county recorder rather than with the secretary of state as required by the Michigan Uniform Commercial Code.¹¹⁰ The court found that the status of National was dispositive of the case and that "one of three legal positions could be ascribed to National: (1) a buyer in the ordinary course of business,

(5th Cir. 1979). But see *Cornelius v. J & R Motor Supply Corp.*, 468 S.W.2d 781 (Ky. 1971).

106. 345 F. Supp. 1076 (E.D.N.Y. 1972).

107. *Id.* at 1078.

108. See Hawkland-104, *supra* note 10, at 364-65. Professor Hawkland takes the position that the *Gruber* case was wrong. *Id.* Compare *In re Gruber Indus., Inc.*, 345 F. Supp. 1076 (E.D.N.Y. 1972) with *In re Rome Furniture Mart, Inc.*, 20 U.C.C. Rep. 1009 (M.D. Ga. 1976.)

109. 67 Mich. App. 417, 241 N.W.2d 471 (1976).

110. *Id.* at —, 241 N.W.2d at 473.

(2) a buyer not in the ordinary course of business, or (3) a transferee in bulk."¹¹¹ If National had been a buyer in the ordinary course of business, its interest in the property would have had priority over even a perfected security interest. As a buyer not in the ordinary course of business, its interest would have been superior to that of the bank. Uniform Commercial Code section 9-301(1) provides that

an unperfected security interest is subordinate to the rights of . . . in the case of goods, . . . a person who is not a secured party and who is a transferee in bulk or other buyer not in ordinary course of business to the extent that he gives value and receives delivery of the collateral without knowledge of the security interest and before it is perfected.¹¹²

The court found National to be a transferee in bulk, and examined the transaction to determine whether the provisions of section 9-301 applied. In order for a transferee in bulk to qualify for such preferred treatment against an unperfected secured creditor, the transfer must have been in compliance with article 6. The court held that the closing of a retail store and bulk sale of its stock constituted an extraordinary transaction, meeting the requirement that a bulk transfer is an extraordinary event, "one occurring few times in the life of a merchant."¹¹³ Further, the court found the case to be prototypical of the situation which article 6 was designed to prevent. Article 6 attempts to protect a creditor from a "merchant, owing debts, who sells out his stock in trade to anyone for any price, pockets the proceeds, and disappears leaving the creditors unpaid."¹¹⁴ But for the bulk sales law, the bank might have been without a remedy.

There was a dispute in the *Frydlewicz* case as to the amount of liability owed by the bulk transferee to the secured party. The lower court had awarded \$17,000, and the transferee argued that it was liable to the secured party for the transferred property or to the extent of the value of the property in the hands of the transferee.¹¹⁵ The transferee claimed that value was \$13,600, the price which it had paid to the transferor. The court stated that "where the remedy utilized is money damages, the amount of the award is the fair market value of the transferred items."¹¹⁶ In connection therewith, there exists a general principle that where no question is raised that the amount paid by the transferee was not the fair value of the property, that amount represents the maximum liability of the transferee. The court found, however, that the fair market value of the collateral was in fact in issue and since the purpose of the bulk transfer law is to prevent transfers which defraud creditors, "whenever the transfer is made at less than the

111. *Id.* at ___, 241 N.W.2d at 473.

112. U.C.C. § 9-301(1).

113. *National Bank v. Frydlewicz*, 67 Mich. App. at ___, 241 N.W.2d at 474.

114. U.C.C. § 6-101, comment 2(b).

115. *National Bank v. Frydlewicz*, 67 Mich. App. at ___, 241 N.W.2d at 474.

116. *Id.* at ___, 241 N.W.2d at 474.

wholesale cost, value should automatically be put in question."¹¹⁷

VIII. LIMITATION OF ACTIONS

While the term varies somewhat in a few states, nearly all of the states that have adopted article 6 have utilized the six-month limitation period of U.C.C. section 6-111,¹¹⁸ which provides that no action may be brought under article 6 more than six months after the date the transferee took possession of the property, or the transfer was discovered if it had been concealed.¹¹⁹ The limitation period relates to actions brought against the transferee to assert the creditors' rights under article 6, and is not intended to place any further limitation on actions against the transferor or among the creditors.¹²⁰ The limitation does not cut off rights of creditors of the transferor where those rights had been perfected under other applicable state law. For example, in *Johanna Farms, Inc. v. Elliott Equip. Co., Inc.*,¹²¹ a mechanic was not precluded from exercising his rights under an artisan's lien after the six-month period expired.

The limitation period set forth in section 6-111 operates to preclude actions based upon non-compliance with article 6 after a period of six months.¹²² The limitation period, however, is extended in the situation where the transfer has been concealed, and the statute begins to run upon the date of discovery. The concealment necessary, however, has been interpreted to be active concealment, and not a mere non-disclosure of transfer or a failure to give a public notice regarding same.¹²³ That is, a lack of disclosure is not the same as a concealment. The extension period for discovery contemplates a willful concealment with intent to conceal or defraud, and a creditor cannot obtain an extension of the statutory limitation period simply because it did not receive notice and did not realize the transfer had taken place.¹²⁴ Some courts have gone so far as to conclude that a transfer has been concealed if no notices are sent to the creditors,¹²⁵ but the correct in-

117. *Id.* at —, 241 N.W.2d at 474.

118. All adopting states have utilized the six-month period except California (1 year), Florida (1 year), and Georgia (12 months).

119. U.C.C. § 6-111.

120. *Palmeri v. Adams*, 4 Ill. App. 3d 881, 280 N.E.2d 266 (1972). The limitation period also is subject to the laws of the various jurisdictions which may allow a claim to attach to the transferee outside of the provisions of article 6. The Oregon wage laws provide, for example, that unpaid wages become the obligation of a successor to a business and such claims therefore are not cut off by the article 6 limitation period. *State v. Ben Jacques Chevrolet Buick, Inc.*, 16 Ore. App. 552, 520 P.2d 366 (1974).

121. 278 Md. 137, 360 A.2d 436 (1976).

122. U.C.C. § 6-111.

123. *Aluminum Shapes, Inc. v. K-A-Liquidating Co.*, 290 F. Supp. 356, 358 (W.D. Pa. 1968).

124. *Id.*

125. *See E. J. Trum, Inc. v. Blanchard Parfums, Inc.*, 33 A.D.2d 689, 306 N.Y.S.2d 316

terpretation should be that non-compliance standing alone does not constitute concealment for purposes of extending the limitation period.¹²⁶

The limitation period set forth in section 6-111 applies only to actions which are brought against a party based upon a failure to comply with the provisions of article 6. The short period of limitation of actions is not applicable to actions brought against the transferor which may have arisen out of the bulk sale (for example, the submission of a willfully false affidavit to the transferee) but which do not depend upon the ineffectiveness of the transfer for the basis upon which the action is brought.¹²⁷

IX. AUCTION SALES

Section 6-108 relating to auction sales¹²⁸ has had virtually no attention by the courts. The Attorney General of Iowa rendered an opinion dated January 24, 1974, on the question of whether in a bulk transfer the "auctioneer" was responsible for mortgaged property, if he acts only as the selling agent and does not actually handle money.¹²⁹ The Attorney General opined that an "auctioneer" includes the individual who conducts the auction, even though he does not handle money and acts only as a selling agent, and that the liability is joint and several with other persons who direct, control or are responsible for the auction.¹³⁰

X. FORMS

The following forms are suggested for use when a transaction is contemplated which falls within the scope of article 6 of the Iowa U.C.C. The forms may be adapted by the attorney to fit particular factual situations and reference must be made, of course, to the statutory provisions of article 6 of the Iowa U.C.C. concerning information to be included in the various forms.¹³¹

(1979).

126. See *Aerolineas Argentinas v. Hansen & Yorke Co.*, 12 U.C.C. Rep. 329, (N.Y. Civ. Ct. 1973).

127. *Palmeri v. Adams*, 4 Ill. App. 3d 881, 280 N.E.2d 266 (1972).

128. See Hansell, *supra* note 1, at 290 for a general discussion.

129. [1974] REP. ATT'Y GEN. IOWA 369.

130. *Id.*

131. Reference also should be made to the text of this article and of the previous article, Hansell *supra* note 1, for completion of the forms.

**DEMAND BY TRANSFEREE
FOR
LIST OF CREDITORS¹³²**

TO: _____ (Transferor)

Pursuant to Article 6 of the Iowa Uniform Commercial Code and pursuant to the agreement between the parties, the undersigned Transferee demands that a list of your creditors be delivered immediately to the undersigned, which list must be in compliance with Article 6 of the Iowa Uniform Commercial Code and the Agreement of Sale between the parties.

Dated: _____

Transferee

Address

132. IOWA CODE § 554.6104(1)(a) (1981).

LIST OF CREDITORS AND CLAIMANTS¹³³

OF

(Transferor)(Date)

Name of Creditor or Claimant	Business Address	Amount of Debt or Claim	Whether Secured or Unsecured	Whether Disputed or Undisputed
---------------------------------	---------------------	----------------------------	------------------------------------	--------------------------------------

Total Debts or Claims \$ _____
 (estimate if some
 amounts are unknown)

STATE OF IOWA)
) SS.
 COUNTY OF _____)

I, (Name of Transferor), Transferor, hereby state that I have prepared the foregoing list of creditors and claimants in accordance with Iowa Code section 554.6104 (1981), that it is a true and complete listing of all of my creditors and persons asserting claims against me for any reasons whatsoever, and that the facts stated above are true, correct and complete as I verily believe.

 Transferor

Subscribed and sworn to (or affirmed) before me this ____ day of _____, 19____.

 Notary Public in and for
 said County and State

133. *Id.* § 554.6104(2).

SCHEDULE OF PROPERTY OF (Transferor) , TRANSFEROR¹³⁴

Date

<u>Quantity</u>	<u>Description</u>	<u>Serial No.</u>	<u>Location</u>	<u>Value</u>
-----------------	--------------------	-------------------	-----------------	--------------

Dated: _____

Transferor_____
Transferee

134. *Id.* § 554.6104(1)(b)-(c).

NOTICE TO CREDITORS¹³⁵
(Short Form)

Date

TO: (Name and Address of Creditor)

This is to advise:

(1) That _____ (Transferor), hereinafter referred to as "Transferor" of _____ (Business Address(es)) will make a bulk transfer under Article 6 of the Iowa Uniform Commercial Code (Chapter 554, Code of 1981) on or after _____ (Date) to _____ (Transferee), hereinafter referred to as "Transferee," of _____ (Business Address(es)).

(2) That, insofar as known to the Transferee, all other business names and addresses (in addition to the name and address in (1) above) used by the Transferor within three years last past are as follows:

(Here list all business names and addresses used by the Transferor within the last three years.)

(3) That all of the debts of the Transferor are to be paid in full as they fall due as a result of the transaction. Creditors should send their bills to the following:

(Name and address of place where creditors are to send their bills.)

Transferee

Address

135. *Id.* § 554.6107(1). Use this short form only if the creditors are to be paid with the proceeds of the transactions.

NOTICE TO CREDITORS¹³⁶
(Long Form)

Date

TO: (Name and Address of Creditor)

This is to advise:

(1) That _____ (Transferor), hereinafter referred to as "Transferor" of _____ (Business Address[es]) will make a bulk transfer under Article 6 of the Iowa Uniform Commercial Code (Chapter 554, Code of 1981), on or after _____ (Date) to _____ (Transferee), hereinafter referred to as "Transferee," of _____ (Business Address[es]).

(2) That, insofar as known to the Transferee, all other business names and addresses (in addition to the name and address in (1) above) used by the Transferor within three years last past are as follows:

(Here list all business names and addresses used by the Transferor within the last three years.)

(3) The location of the property to be transferred is _____ (Address) _____; the estimated total of the debts of the Transferor is \$ _____; a general description of the property to be transferred is: (Here describe generally the property, such as "All of the Transferor's inventory of washing machines, dryers, refrigerators," or else state that the Schedule of Property is attached.)

(4) The Schedule of Property and List of Creditors may be inspected and copied at _____ (Address), _____ from _____ a.m. to _____ p.m., until _____ (a date at least 6 months from the transfer).

(5) The Transferor is to pay existing debts; said debts total \$ _____ and are owed as follows:

136. *Id.* § 554.6107(2).

Persons to whom owingAmounts owing

(or)

(5) The Transferor is not to pay existing debts.

(6) The transfer is for new consideration. The amount of the new consideration is \$ _____. The time and place of the payment of the new consideration is _____ (Time and Place).

(or)

(6) The transfer is not for new consideration.

Transferee_____
Address

