Rights and Remedies Between U.C.C. Article 9 Secured Parties with Conflicting Security Interests in Goods

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Debtors sometimes give security interests in the same property to several different creditors. Often, however, the property’s value is insufficient to support fully the multiple interests. Consequently, the relative priority of these interests becomes an important issue if the debtor defaults. Article 9 of the Uniform Commercial Code1 has a complete set of rules for determining the priority of conflicting security interests in the same personal property.2 Yet, Article 9 fails altogether to explain the privileges of priority.

The principal purpose of this Article is to examine a secured party’s rights and remedies when a subordinate secured party asserts control over goods in which both creditors have Article 9 security interests.3 A secured party is subordinate or junior when another creditor’s security interest is accorded priority under the provisions of Article 9. This Article is not concerned with the rules that determine priority between competing secured parties. Rather, it examines the circumstances under which, and the means by which, a secured party’s interest can be enforced against a junior secured party who has taken the collateral from the debtor.

Section I of this Article explains the doctrinal basis for allowing a secured party to repossess collateral from a junior secured party in possession of the property.4 Section II deals generally with a senior secured party’s correlative right to dispose of repossessed collateral notwithstanding the existence of a subordinate security interest in the property.5 This section

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1. Unless otherwise indicated, all references and citations in this article to the text and comments of the Uniform Commercial Code, hereinafter referred to simply as the Code or the U.C.C., are to the 1978 Official Text with Comments.

2. An extensive collection of priority rules is the predominant feature of Article 9, the rules of which “are principally concerned with the limits of the secured party’s protection against purchasers from and creditors of the debtor.” U.C.C. § 9-101 comment. U.C.C. § 9-312 collects the principal rules for determining priority between Article 9 secured parties.

3. Effectuation of priority when a subordinate buyer of the collateral has asserted control over the goods is discussed in Nickles, Enforcing Article 9 Security Interests Against Subordinate Buyers of Collateral, 50 GEO. WASH. L. REV. 511 (1982).

4. See text accompanying notes 8-47 infra.

5. See text accompanying notes 48-85 infra.
also details the duties that a foreclosing senior secured party owes a junior secured party and the junior’s remedies against the senior if these duties are breached.

Section III considers the question whether a secured party can recover the proceeds of collateral when a junior secured party has disposed of the property. A close examination of the provisions of Article 9 fails to reveal clear authority for giving the senior creditor a prior claim to the sale proceeds. Arguably, at least, the drafters intended that junior secured parties should retain the fruits of their own dispositions, because a senior secured creditor can follow the original collateral into a buyer’s hands and repossess it.

A senior secured party may be unwilling to retrieve collateral from a junior in possession and unable to recover the proceeds of a sale of collateral conducted by the subordinate secured party. An alternative pursued by some senior secured creditors is to sue for damages. They argue that, by exercising control over collateral, a junior secured party thereby converts a senior security interest in the property. Section IV makes clear that in some cases this argument is sound. A junior secured party is not absolutely immune from liability for conversion under the common law. Yet, the major theme of the final section of this Article is that a junior secured party’s repossession or disposition of collateral is not in itself a sufficient reason for imposing conversion liability.

I. REPOSSESSING THE COLLATERAL FROM A SUBORDINATE SECURED PARTY IN POSSESSION OF THE PROPERTY

Prior encumbrances on property do not preclude the debtor from granting to another creditor a security interest in the same collateral. Article 9 explicitly provides that the debtor’s rights in collateral may be voluntarily transferred by the creation of a security interest. Typically, however, security agreements deny the debtor the right to further encumber the collateral. Though such a provision in a security agreement cannot deprive the debtor of the power to give another creditor an interest in the property, the agreement can legitimately make doing so an event of default entitling the earlier secured party to repossess the collateral.

6. See text accompanying notes 86-155 infra.
7. See text accompanying notes 156-203 infra.
9. See id.
After repossessing the property from the debtor who has for any reason defaulted, a secured party can retain it against the claim of a subordinate secured party for the purpose of disposing of the collateral pursuant to Part 5 of Article 9. A senior secured party attempting to retake the collateral may discover, however, that the debtor also has defaulted under a security agreement with a junior secured party who already has repossessed the property. If the subordinate creditor has not already disposed of the collateral, the senior secured party may wish to take possession of the property in order to control foreclosure. The senior secured party faces an initial problem in establishing that his interest, which has priority, is entitled, for this reason or any other, to a superior, exclusive right to possess the collateral on the debtor’s default.

When a senior secured party attempts to repossess collateral from a junior secured party, the senior will argue that he is entitled to recover the property because section 9-503 gives him “the right to take possession of the collateral [on the debtor’s default].” This argument, however, is problematic. Section 9-503 gives “a secured party” the right to possession of the collateral on the debtor’s default; neither this right nor the section 9-504 right to dispose of collateral after repossession is granted exclusively to senior secured parties. Thus, the junior creditor may contend that because he, too, has the statutory rights to repossess the collateral and foreclose, the senior secured party cannot retake the property from him. The senior creditor’s response undoubtedly will be that section 9-503 does not expressly give a junior secured party the right to retain possession against the claim of a creditor whose security interest has priority under Article 9.

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13. Id. (emphasis added).

14. “A secured party after default may sell, lease or otherwise dispose of any or all of the collateral . . . .” Id. § 9-504(1) (emphasis added).

15. The court in Western Nat’l Bank v. ABC Drilling Co., 42 Colo. App. 407, 599 P.2d 942 (1979), was persuaded by such an argument. A junior secured party filed an action to replevy collateral from the debtor, but a senior secured party intervened and
The temptation is to conclude that the senior secured party should prevail simply because he has "priority." This conclusion is sound, however, only if the incidents of priority under Article 9 include a right of possession higher than or superior to that of a subordinate secured party who has repossessed the collateral. Some might decide solely on the basis of "common sense" that priority includes this right, but one person's common sense is another person's nonsense. Any such right must be founded on firmer ground.

In cases involving pre-Code security devices, the courts universally recognized that a senior secured creditor has a right on the debtor's default to replevy or otherwise take the property from a junior creditor who had repossessed it. Yet, these pre-Code cases cannot be cited as establishing a monolithic common-law principle that today's courts, on the authority sought possession based on the priority of its interest. The trial court gave possession to the subordinate creditor and authorized it to sell the collateral. The senior creditor complained of this on appeal, but the appellate court affirmed the trial court's actions:

A secured creditor has a right to possession of collateral upon the default of the debtor. The right to possession is not limited by the statute to the creditor whose security interest has the higher priority. Thus it was not error for the trial court to award possession to Western [the junior secured party], which was the first secured party to seize the [collateral] after default.

Similarly it was not error for the trial court to order the [collateral] to be sold to the buyer which Western had procured.

Id. at 412, 599 P.2d at 946 (citation omitted). See also Consolidated Equip. Sales, Inc. v. First State Bank & Trust Co., 627 P.2d 432, 438 (Okla. 1981) ("Section 9-503 makes no distinction between secured parties of graduated priorities . . . ."). But see cases cited at note 44 infra. The court's holding in Western Nat'l Bank is contrary to the proposition argued in this Article that a junior secured party's right to possession must yield to the superior, exclusive right of a senior secured party to take the collateral when the debtor defaults. See text accompanying notes 16-47 infra.

of section 1-103, 17 can perpetuate under Article 9. Collectively, the cases do not forge a rule that, as a matter of common law, priority in itself, no matter how determined, gives a senior secured creditor the right to replevy collateral from a subordinate secured creditor. Many of the decisions ultimately can be justified on the basis of the theoretical underpinnings of the various pre-Code security devices. Some of these conceptual supports, however, are largely outmoded under Article 9 and do not underlie the existence or effectiveness of modern security interests in personality. For example, when deciding disputes between chattel mortgagees, some courts reasoned that the earlier creditor held defeasible title to the collateral that, for purposes of foreclosure, became absolute on the debtor's default. As the absolute owner, this chattel mortgagee and no one else was entitled to possession of the collateral if the mortgagee chose to retake the property. 18

The courts that followed the early, orthodox theory of conditional sales also had a theoretically consistent reason for allowing a conditional vendor to recover possession of collateral from a mortgagee or other purchaser or creditor of a vendee who failed to pay for the goods he had bought. Because the vendor had retained title to the property, the vendee had no interest—at least no "property" interest—in the collateral to encumber or otherwise convey. 19 Therefore, inasmuch as the vendee could not con-

Mercantile Co., 113 Wis. 493, 501, 89 N.W. 507, 510 (1902). For other cases, see notes 18-20, 27, 32, 34 infra. See generally 2 L. JONES, THE LAW OF CHATTEL MORTGAGES AND CONDITIONAL SALES § 497 (6th ed. 1933); 3 id. § 1353.

17. This section provides that "[u]nless displaced by the particular provisions of this Act, the principles of law and equity . . . shall supplement its provisions." U.C.C. § 1-103.


19. 3 L. JONES, supra note 16, § 1263, at 336. "For a long time the strict notion was prevalent . . . that the possession of property was all the buyer [under a conditional sales contract] received until full payment had been made. This was not considered an interest which he could alienate . . . ." Id. Therefore, the conditional sale . . . stood in no need of validation by means of a recording act. It differed from the chattel mortgage because the latter was amorphous; and it was unlike the pledge in that the man who extended credit did not have possession. The conditional sale was not a security device because there was no right of redemption, and because the vendor, unlike the lender with pledge or chattel mortgage, could not assert a right in the goods after taking judgment on the debt. Hence this strict contract-bailment agreement would stand up against the purchaser's judgment creditors, nor would a bona fide purchaser acquire any rights. . . . The vendee, having no title or any real or apparent authority to sell the goods, had nothing which he could transfer to a purchaser; and the latter was bound by the rule that makes any man look into his vendor's title. The only exception was where the contract expressly gave the vendee leave to resell. Glenn, The Conditional Sale at Common Law and as a Statutory Security, 25 VA. L. REV. 559,
vey title he did not have, the subsequent transferee had no title from which to assert a right of possession as against the vendor.20

Pre-Code cases have little relevance to disputes between Article 9 secured parties if the results of these cases are attributable to a strict "title" theory of security, because section 9-202 provides that location of title is immaterial to the application of the provisions of Article 9.21 Their relevance is further diminished by section 9-311, which implies that debtors retain rights in collateral and expressly provides that these rights can be encumbered.22 Article 9, however, does not undermine the reasoning of other pre-Code cases in which a secured creditor's right to repossess property from the debtor's transferee was based on some ground other than a title theory of security.

575-76 (1939). See generally Harkness v. Russell, 118 U.S. 663 (1886); Ensley Lumber Co. v. Lewis, 121 Ala. 94, 25 So. 729 (1898); Baals v. Stewart, 109 Ind. 371, 9 N.E. 403 (1886); Coggill v. Railroad Co., 69 Mass. (3 Gray) 545 (1854); Sumner v. Woods, 71 Mo. 121 (1879); Weeks v. Pike, 60 N.H. 447 (1881); Marvin Safe Co. v. Norton, 48 N.J.L. 410, 7 A. 418 (1886); Ballard v. Burgett, 40 N.Y. 403 (1886); Sanders v. Keber, 28 Ohio St. 630 (1876); Lockwood Bros. v. Frisco Lumber Co., 22 Okla. 31, 97 P. 562 (1908); McComb v. Donald's Adm'r, 82 Va. 903, 5 S.E. 558 (1888). As these cases and those cited in note 20 infra make clear, giving possession of the collateral to the vendee was not in itself sufficient to clothe the debtor with apparent authority over the property or to estop the vendor from asserting his title to the property. See also I S. Williston, THE LAW GOVERNING SALES OF GOODS AT COMMON LAW AND UNDER THE UNIFORM SALES ACT § 324 (2d ed. 1924). For the contrary, minority view, see Gilbert v. Nat'l Cash Register Co., 176 Ill. 288, 296-98, 52 N.E. 22, 25-26 (1898). The Illinois courts were later forced to abandon the Gilbert holding, however. See Sherer-Gillett Co. v. Long, 318 Ill. 432, 434-35, 149 N.E. 225, 225-26 (1925); American Type Founders Co. v. Metropolitan Credit & Discount Corp., 271 Ill. App. 380, 391 (1933).


21. Section 9-202 provides: "Each provision of this Article with regard to rights, obligations and remedies applies whether title to collateral is in the secured party or in the debtor." U.C.G. § 9-202.

22. Section 9-311 provides:

The debtor's rights in collateral may be voluntarily or involuntarily transferred (by way of sale, creation of a security interest, attachment, levy, garnishment or other judicial process) notwithstanding a provision in the security agreement prohibiting any transfer or making the transfer constitute a default. Id. § 9-311. The purpose of this section is "[t]o make clear that in all security transactions under this Article, the debtor has an interest (whether legal title or an equity) which he can dispose of and which his creditors can reach." Id. comment 1.
Under the pre-Code law, most courts eventually recognized that debtors in various types of security arrangements retained some interest in the collateral that they could sell or encumber. This included conditional vendees of goods purchased under contracts of sale in which the vendors purported to retain full and absolute title to the property sold. Nevertheless, although a conditional vendee had some "title" or "ownership" or "property" in the collateral, this interest, whatever its nature, was conditioned or qualified by the terms and legal incidents of the sales contract that governed the purchase of the goods. Except when recording statutes provided otherwise, the vendee could not convey to any transferee a title better than or rights superior to his own with respect to the collateral. Concomitantly, because a conditional vendee in default had

23. Regarding the right of a chattel mortgagee to sell or further encumber the collateral, see 2 L. JONES, supra note 16, §§ 454-473. The pre-Code uniform act governing mortgages specifically provided that a mortgagor could "sell, mortgage, or otherwise dispose of his interest" in the property. UNIF. CHATTEL MORTGAGE ACT § 20 (act withdrawn 1943).


Although most courts recognized that a vendee had a transferable interest in the collateral, they disagreed about the nature of the interest and how to define or characterize it: It has been variously called "right," "interest," "property," and "special property." It is not solely an equitable interest, for certain rights are purely legal rights, viz., the right, when not in default, to have and maintain replevin proceedings for the possession of the chattel, even against the vendor, and the right to pay the amount due and succeed to full title and ownership. The vendee has, in some jurisdictions, been called the equitable owner . . . but, if so, he must be an equitable owner vested with legal rights . . . .


According to the general common law rules of property one may ordinarily transfer that which he has but no more, and one's creditors may ordinarily take by appropriate legal process that which their debtor had but no more. These elementary rules are as applicable to the divided property interests involved in conditional sales as they are to the more familiar undivided property interest of complete and absolute ownership of goods. . . .

Applying the familiar rule that one cannot convey more than he has, it is held by the overwhelming weight of authority, in cases in which recording acts do not apply, that a transfer by the conditional buyer to a third party, even
no right to possession of the collateral as against the vendor,\textsuperscript{26} the vendee's transferee acquired no such right and was required to yield possession of the property.\textsuperscript{27}

\textsuperscript{26} Though it be to a party who is a purchaser for value without notice, does not cut off the original conditional seller's interest. . . . Subsequent mortgagees or other encumbrancers for value from the conditional buyer stand in this respect like purchasers, succeeding to the limited interest of their respective transferors.\textit{Id.} (footnotes omitted). \textit{See also} 1 J. Benjamin, \textit{A Treatise on the Law of Sale of Personal Property} §§ 425-426 (C. Corbin 4th American ed. 1883); 3 L. Jones, \textit{supra} note 16, §§ 1273, 1275; 1 S. Williston, \textit{The Law Governing Sales of Goods at Common Law and Under the Uniform Sales Act} § 326 (2d ed. 1924).

The Sales Act of 1906 was the first uniform law to validate conditional sales of goods and protect the security interest of the vendor; this statute and later versions thereof did so by providing "where goods are sold by a person who is not the owner thereof. . . . the buyer acquires no better title to the goods than the seller had . . . ." \textit{Unif. Sales Act} § 23(1), 1 U.L.A. 379 (1950) (act withdrawn 1951). That the effect of this provision was to sanction conditional sales and make them enforceable against even bona fide purchasers for value is made clear by cases such as Sherer-Gillett Co. v. Long, 318 Ill. 432, 434, 149 N.E. 225, 226 (1925). But \textit{see} Anchor Concrete Mach. Co. v. Pennsylvania Brick & Tile Co., 292 Pa. 86, 90, 92-93, 140 A. 766, 767-68 (1928).

The effect of recording statutes on the interests and rights of conditional vendors and chattel mortgagees is discussed at text accompanying notes 30-37 infra.

\textsuperscript{27} In the comparatively few cases in which the courts articulated reasons for this result, the "no better title" rule is sometimes mentioned and apparently applied. \textit{See}, e.g., Sherer-Gillett Co. v. Long, 318 Ill. 432, 434, 149 N.E. 225, 226 (1925); Phend v. Midwest Eng'g & Equip. Co., 93 Ind. App. 165, 170, 177 N.E. 879, 880 (1931) (no "stronger" title). In other cases a slightly different formulation of the rule is given. For example, in Fairbanks, Morse & Co. v. Parker, 167 Ark. 654, 269 S.W. 42 (1925), the court explained the result this way:

In conditional sales of personal property, where the title is retained by the vendor until the purchase price is paid, the vendee acquires an interest that he can sell or mortgage without the consent of the vendor, but the vendor's right to recover the property, if the purchase price of the property is not paid, is not prejudiced by such sale or mortgage.\textit{Id.} at 658, 269 S.W. at 43 (citation omitted).

In another case the court explained that, on default, the debtor lost whatever interest he had acquired in the collateral. \textit{See} Thirlby v. Rainbow, 93 Mich. 164, 168, 53 N.W. 159, 160 (1892). The implication is that, consequently, his transferee is left with no interest on which to base a right of possession. These explanations, especially the last one, are conceptually close to the reasoning that justifies a vendor's right to replevy on the basis that the vendee never acquired an interest to convey to a transferee. \textit{See} text accompanying notes 19-20 infra. It is often impossible to determine whether the courts were basing the vendor's superior right to possession on the orthodox theory of conditional sales, holding that the vendee never acquired any interest to convey, or on the rule that, although he had some interest in the collateral, it was limited and gave his transferee no greater rights with respect to the property than the vendee had. \textit{See}, e.g., Cottrell & Sons Co. v. Carter, Rice & Co., 173 Mass. 155, 159, 53 N.E. 375, 376 (1899); cases cited in notes 19-20 supra.

Whichever view was followed, however, the underlying premise was that the vendee could not convey title better than his own. This appears to be the fundamental reason
This rule, that no one can convey more than he has, is a fundamental common-law principle that can be applied under Article 9 except in cases when its priority rules provide otherwise. Therefore, when the dispute is between an earlier Article 9 secured party entitled to priority over a subsequent secured party, this principle and the pre-Code cases applying it can be relied on to support the senior creditor's right to replevy the collateral from the later, junior creditor. Section 9-503 confirms that a debtor in default has no right to continued possession of the collateral; and, if the subsequent, junior creditor's rights are no greater than the debtor's, the junior is also bound to relinquish the property to the senior secured party.

This common-law principle, however, does not justify an Article 9 secured party's act of replevying goods in a case when, though he is entitled to priority, he encumbered the collateral after the junior creditor's security interest attached to the property. There is, however, a modern justification for allowing the senior creditor to recover the collateral in this situation, and it has an analog in pre-Code law. By the last half of the nineteenth century, chattel mortgage recording statutes had been enacted in virtually every state; eventually, a large number of states also provided for the filing of conditional sales contracts and other security instruments. These statutes effectively created an exception to the common-law principle that one can convey no more than he has. The statutes allowed a subsequent mortgagee or other purchaser from the debtor to assert rights with respect to the collateral—including the right to possess it—that were superior to the claim of an earlier secured creditor whose supporting the results in a host of cases holding that a vendor can recover possession of collateral from the vendee's transferee. In addition to cases cited in this note, see the cases cited in notes 16, 20 supra; Annot., 87 A.L.R. 941 (1933); and 2A U.L.A. § 47, at 57-58 (1924). See also 3 L. JONES, supra note 16, § 1353; Note, Rights of the Conditional Vendee's Creditors, Purchasers and Mortgagees Under a Valid Conditional Sale, 30 COLUM. L. REV. 372, 374-75, 379-80 (1930). See generally authorities cited in note 25 supra.

28. See U.C.C. § 1-103; Barnett v. Everett Trust & Sav. Bank, 13 Wash. App. 332, 334-35, 534 P.2d 836, 837-38 (1975). In certain cases, however, recording statutes or statutory priority rules may effectively displace this common-law principle. See text accompanying notes 30-44 infra. This is true, too, of the rules of priority in Article 9.

29. Any right the debtor has to possess the property is lost when he defaults, because the law specifically provides that "a secured party has on default the right to take possession of the collateral." U.C.C. § 9-503.

30. Sketches of many of these statutes are provided in 1 L. JONES, supra note 16, §§ 190-235.

31. For examples of this type of provision, see UNIF. TRUST RECEIPTS ACT §§ 7, 13, 9C U.L.A. 249, 263-65 (1957) (act withdrawn 1951); UNIF. CONDITIONAL SALES ACT §§ 5-8, 10-11, 14, 2 U.L.A. 6-15, 16-19, 23-25 (1922) (act withdrawn 1943). The Trust Receipts Act was adopted in 32 states. R. BRAUCHER & R. RIEGERT, INTRODUCTION TO COMMERCIAL TRANSACTIONS xxxviii-xxxix (1977). The Conditional Sales Act was adopted in 11 states. Id. However, many states retained the conditional sales statutes that had been enacted prior to the promulgation of the uniform law. See generally UNIF. CONDITIONAL SALES ACT app., 2 U.L.A. 43-244 (1922) (act withdrawn 1943).
interest was properly recorded, if at all, after the debtor had transferred his interest to the later claimant.\textsuperscript{32}

This result was not founded simply on some common-law notion that priority of interest determines priority of possession and gives the senior creditor a superior, exclusive right to possession of the collateral on the debtor's default. Rather, it can be attributed to the usual wording of pre-Code recording statutes. These statutes provided that unfiled chattel security instruments were "void" or "not valid" against persons who subsequently acquired interests in the collateral for value and in good faith from the debtor in possession of the property.\textsuperscript{33} As against persons protected by


\textsuperscript{33.} For examples of these statutes, see the abstracts of chattel mortgage recording statutes collected in 1 L. JONES, supra note 16, §§191-235, and the abstracts of laws requiring the filing of conditional sales contracts collected in 3 id. §§1008-1056. For another collection of conditional sales statutes, see UNIF. CONDITIONAL SALES ACT app., 2 U.L.A. 43-244 (1922) (act withdrawn 1943). The uniform law governing such sales contracts used similar language:

Every provision in a conditional sale reserving property in the seller, shall be void as to any purchaser from or creditor of the buyer, who, without notice of such provision, purchases the goods or acquires by attachment or levy a lien upon them, before the contract or a copy thereof shall be filed as hereinafter provided, unless such contract or copy is so filed within ten days after the making of the conditional sale.

\textit{Id.} § 5, 2 U.L.A. 6 (emphasis added) (act withdrawn 1943). The typical chattel mortgage statute provided:

Every mortgage or conveyance intended to operate as a mortgage of goods or chattels . . . which is not accompanied by an immediate delivery, and followed by an actual and continued change of possession of the things mortgaged, is absolutely void [against creditors of the mortgagor and purchasers of the mortgaged property] unless the mortgage or a true copy thereof is filed as directed in this article.

1 G. GILMORE, SECURITY INTERESTS IN PERSONAL PROPERTY § 2.2, at 26 (1965) (emphasis added) (footnote omitted) (quoting a New York lien law repealed when Article 9 was adopted in that state).
these statutes, a creditor could not assert a superior right to possession of the collateral because the security instrument under which he claimed the property was technically voided by statute. In cases involving prior, unfiled chattel mortgages, the result was a carry-over of the early view held by courts before recording statutes were enacted that a chattel mortgage was fraudulent against subsequent purchasers if the mortgagor retained possession of the collateral. Filing a mortgage under registry laws was simply a substitute for delivering the collateral to the mortgagee. If a proper filing was not effected and the mortgagor retained possession, the security agreement was invalid against later purchasers from the debtor.


35. See 1 G. Gilmore, SECURITY INTERESTS IN PERSONAL PROPERTY § 2.1 (1965); Glenn, The Chattel Mortgage as a Statutory Security, 25 VA. L. REV. 316, 324-27 (1939). Initially, most courts did not take such a view of conditional sales contracts, and the vendor could enforce his reservation of title against everyone, including good faith purchasers for value. See 1 S. Williston, The Law Governing Sales of Goods at Common Law and Under the Uniform Sales Act §§ 324-326 (2d ed. 1924); Glenn, The Conditional Sale at Common Law and as a Statutory Security, 25 VA. L. REV. 559, 564-65 (1939); see also F. Tiffany, HANDBOOK OF THE LAW OF SALES § 44, at 135-38 (2d ed. 1908); 2A U.L.A. §§ 47-48, at 46-56 (1924). Yet, [i]n conditional sales transactions, the problem of hardship on parties dealing with the conditional buyer in possession, because of the secret reserved interest of the conditional seller, is very similar to that which is so familiar in connection with chattel mortgages.

Vold, The Divided Property Interests in Conditional Sales, 78 U. PA. L. REV. 713, 730 (1930). Eventually, courts began to find fault with conditional sales because they were thought to approximate the retention of what was denominated a secret lien, for which judicial abhorrence was professed, and on account of the element of potential fraud which they possessed, especially as against the creditors, vendees, or mortgagees of the conditional buyer, they were often assailed, even by courts that, nevertheless, upheld them. These considerations began to influence the legislatures, resulting in enactments requiring such contracts to be filed or recorded as a matter of protection to creditors of the buyer, and supposedly innocent purchasers from him, therebyemasculating the time-honored maxim, caveat emptor, as to conditional sales . . .

3 L. Jones, supra note 16, § 932, at 34 (footnote omitted).

36. 1 L. Jones, supra note 16, §§ 176, 190.

37. See, e.g., Copeland v. Tennessee Valley Bank, 238 Ala. 364, 365-66, 191 So. 243, 245 (1939); Heitzman v. Hannah, 206 Iowa 775, 780, 221 N.W. 470, 472 (1928); Heyman
At first glance, Article 9 appears to displace completely the pre-Code cases allowing a senior secured creditor to replevy collateral from a junior creditor in which the justification can be founded ultimately on an underlying theory of security law that characterized the junior's interest as fraudulent or otherwise void. Section 9-205 explicitly negates the notion that a security arrangement is fraudulent simply because the debtor keeps and controls the collateral.\(^{38}\) In addition, Article 9 nowhere provides that subordinate security interests are "void" against the holder of a superior claim. Nevertheless, the rule under pre-Code recording statutes, that an unfiled security instrument is void against certain purchasers and others, has a latter-day relative among the provisions of Article 9. It is section 9-201, which provides: "Except as otherwise provided by this Act a security agreement is effective according to its terms between the parties, against purchasers of the collateral and against creditors."\(^{39}\)

Section 9-201 confirms the right of a senior secured party to replevy from a junior secured party the collateral repossessed by the junior; and the reason for this result, which is based on section 9-201, is strikingly similar to that based on the language of pre-Code recording statutes. Typically, Article 9 security agreements expressly give the secured party the right to repossess collateral on the debtor's default; even if they did not, this section 9-503 right will be implied by the law as part of the parties' agreement.\(^{40}\) Therefore, every secured party can argue on the basis of section 9-201 that their right to possession of the property is enforceable against all classes of claimants mentioned in the section, including other

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\(^{38}\) Section 9-205 provides: "A security interest is not invalid or fraudulent against creditors by reason of liberty in the debtor to use, commingle or dispose of all or part of the collateral . . . ." U.C.C. § 9-205.

\(^{39}\) Id. § 9-201.

\(^{40}\) The first uniform statute to make clear that a secured creditor has a right on the debtor's default to take possession of the collateral was the Uniform Conditional Sales Act. See UNIF. CONDITIONAL SALES ACT § 16, 2 U.L.A. 27 (1922) (act withdrawn 1943). This provision gave a conditional seller that right whether or not the security instrument expressly provided for it; for example, the right to possession was implied by law. See 2A U.L.A. § 100, at 138-39 (1924). U.C.C. § 9-503 is merely a copy of Uniform Conditional Sales Act § 16. See 2 G. GILMORE, SECURITY INTERESTS IN PERSONAL PROPERTY § 44.1, at 1212 (1965).

In precise terms, the U.C.C. § 9-503 right to repossess, if implied, will be part of the parties' "contract," not their "agreement." Compare U.C.C. § 1-201(3) (definition of agreement), with id. § 1-201(11) (definition of contract). See generally 1 A. CORBIN, CORBIN ON CONTRACTS §§ 17-20 (1960); 3 id. § 561. Despite U.C.C. § 9-201's use of the term "agreement," this provision cannot be interpreted to mean that only some of the parties' total rights and obligations—those comprising their agreement—are enforceable. Even though there may be aspects of the parties' "contract" that are not within their "agreement," these aspects govern the legal relationship between them with the same force as those.
secured parties.41 A subordinate secured party cannot assert this right against a senior secured party, however, because the rule of section 9-201, that a security agreement is effective against purchasers of the collateral and others, is subject to exceptions created by Article 9.42 The commentary to section 9-201 makes clear that an exception exists when a creditor’s security interest is subordinated under the priority rules of Article 9 to that of another secured party.43 The negative implication of this provision is, therefore, that the terms of a junior secured party’s security agreement, including his right to possession of the collateral on the debtor’s default, are ineffective against another secured party whose interest is given priority by Article 9.

So interpreted, section 9-201 effectively equates priority of interest, however established under Article 9, with priority of possession, and it gives a senior secured party a higher, superior, and exclusive right to possession of the collateral without regard to when his security interest attached to the property. A subordinate secured party’s right to possession of the collateral, which is based on the expressed or implied terms of his security agreement with the debtor, is simply not assertable by him in a contest with a senior secured party, because these terms are ineffective against a creditor whose security interest has priority under Article 9. Thus, a senior secured party is entitled to recover possession of the collateral from a subordinate secured party who has repossessed it.44

that are expressed by the parties or inferred from the circumstances of their transaction; it has never been thought that rights and duties arising or resulting from a contractual relationship are any less potent solely for the reason that their source is law other than the law of the expressed agreement itself.

41. U.C.C. § 9-201 does not specifically mention secured parties as a separate class of claimants against whom a security agreement is effective, but it does mention “purchasers,” which is a term that includes secured parties. See U.C.C. § 1-201(32), (33); see also Burk v. Emmick, 637 F.2d 1172, 1174 (8th Cir. 1980); B & P Lumber Co. v. First Nat’l Bank, 147 Ga. App. 762, 764, 250 S.E.2d 505, 507 (1978).

42. Section 9-201 begins with the caveat: “Except as otherwise provided by this Act.” U.C.C. § 9-201.

43. The comment to § 9-201 provides: “In general the security agreement is effective between the parties; it is likewise effective against third parties. Exceptions to this general rule arise where . . . . this Article subordinates the security interest . . . . or defeats the security interest . . . .’” Id. § 9-201 comment.

This conclusion can rest squarely and solely on section 9-201. Section 9-201 is an independent basis for a senior secured party’s right to replevy collateral from a junior secured party in every dispute between such claimants regarding possession of the property. Thus, when the contest is between a senior creditor who also happens to be the earlier secured party and a subsequent secured party whose interest is, for whatever reason, subordinate under Article 9, there is no need to rely on the common-law rule that no one—in this case the debtor—can convey to a later creditor greater interest or rights in property than he has. Undoubtedly, however, the right of a senior Article 9 secured party to recover the collateral in such a case is bolstered by this fundamental rule of property law. Additionally, a senior, but subsequent, Article 9 secured party’s right to replevy from a junior secured party whose interest first attached is bolstered by pre-Code cases recognizing this right under the statutory ancestors of section 9-201. Nevertheless, section 9-201 alone can support the conclusion that no matter when his interest attached to the property, a senior Article 9 secured party has, on the debtor’s default, a superior, exclusive right to possession of the collateral. This is a corollary privilege based on and accompanying the priority of his interest.

If a junior secured party wants to keep or regain possession of the collateral so that he can control foreclosure, his recourse is to satisfy the senior creditor’s security interest in the property. Part 5 of Article 9 explicitly recognizes the right of “any other secured party” to redeem collateral. If, however, the junior secured party is unwilling to satisfy

45. For discussion of the application of this common-law rule in pre-Code secured transactions cases, see text accompanying notes 23-29 supra.
46. For discussion of these cases, see text accompanying notes 30-37 supra.
47. See U.C.C. § 9-506. This section provides:
At any time before the secured party has disposed of collateral or entered into a contract for its disposition under Section 9-504 or before the obligation has been discharged under Section 9-505(2) the debtor or any other secured party may unless otherwise agreed in writing after default redeem the collateral by tendering fulfillment of all obligations secured by the collateral as well as the expenses reasonably incurred by the secured party in retaking, holding and preparing the collateral for disposition, in arranging for the sale, and to the extent provided in the agreement and not prohibited by law, his reasonable attorneys’ fees and legal expenses.

Id. Under pre-Code law a junior secured creditor also was entitled to redeem the collateral from a senior secured creditor. See, e.g., Hampton v. Stewart, 240 Ala. 2, 3, 194 So. 509, 510 (1940); Dame v. C.H. Hanson & Co., 212 Mass. 124, 126, 98 N.E. 589, 589 (1912); Schmittid v. Moore, 120 Mich. 199, 202, 202, 79 N.W. 196, 196 (1899); Le Flore v. Miller, 64 Miss. 204, 206-07, 1 So. 99, 100 (1887); Williamson v. Gottschalk, 1 Mo. App. 425, 430 (1876) (no right to redeem, however, after proper disposition); Schnitzer v. Fruehauf Trailer Co., 283 A.D. 421, 426, 128 N.Y.S.2d 242, 248 (1954); Brown v. Smith, 13 N.D. 580, 582-84, 102 N.W. 171, 172-73 (1904); Dickerson v. Cleland, 120 S.C. 221, 222, 112 S.E. 920, 920 (1922) (redemption must occur, however, before valid disposition of property); De Luce v. Root, 12 S.D. 141, 145, 80 N.W. 181, 182
the superior interest, the senior creditor’s priority entitles him to possess the collateral and control its disposition. Priority, however, does not entitle a secured party to repossess the collateral and foreclose without respecting certain other rights that Part 5 of Article 9 gives to a junior secured party whose interest, though subordinate, survives the senior creditor’s repossession of the property.

II. ACCOUNTABILITY TO SUBORDINATE SECURED PARTIES WHEN SENIOR SECURED PARTY REPOSSESSES AND DISPOSES OF COLLATERAL

A junior secured party does not lose his security interest in collateral simply because the property has been repossessed from him or the debtor by a senior secured party.\(^{48}\) The subordinate security interest continues in the original collateral until the senior creditor disposes of the goods under Part 5 of Article 9, usually by selling the property at a public or private sale. This sale ordinarily terminates both security interests in the original collateral,\(^{49}\) but the disposition gives rise to claims to the proceeds of the sale.\(^{50}\) The senior secured party who conducted the sale has a prior right to as much of the proceeds as is necessary to satisfy the expenses of foreclosure and his superior interest.\(^{51}\)

With respect to any remaining sale proceeds, however, the junior creditor may be entitled to have them paid directly to him by the senior creditor who conducted the disposition.\(^{52}\) Even if the surplus funds are

\(^{48}\) Even if the repossession itself amounts to a “disposition” of the collateral, the subordinate security interest follows the property pursuant to the general rule that “a security interest continues in collateral notwithstanding sale, exchange or other disposition thereof.” U.C.C. § 9-306(2).

\(^{49}\) “When collateral is disposed of by a secured party after default, the disposition transfers to a purchaser for value all of the debtor’s rights therein, discharges the security interest under which it was made and any security interest or lien subordinate thereto.” Id. § 9-504(4) (emphasis added). See, e.g., Heyboer v. Kolberg, 493 F. Supp. 137, 139 (W.D. Mich. 1980).

\(^{50}\) The word “claims” is used rather than “interests” because it is not clear that the sale proceeds are “proceeds” under U.C.C. § 9-306(1), in which a security interest continues under § 9-306(2) until the funds are actually “received by the debtor.” See text accompanying notes 99-141 infra. This does not mean, however, that the secured party conducting the sale and a junior secured party do not otherwise have claims to the sale proceeds even before any proceeds are paid to the debtor. See U.C.C. § 9-504(1); text accompanying notes 51-53 infra.

\(^{51}\) Article 9 specifically provides that these debts are to be paid first from the proceeds of sale, prior to the satisfaction of any subordinate interests. U.C.C. § 9-504(1)(a)-(c).

\(^{52}\) Article 9 specifically directs that after a secured party who has disposed of col-
paid to the debtor, the subordinate secured party has a superior right to them as against the debtor and the other secured party who disposed of the original collateral. Because he will have a claim to these surplus proceeds, a subordinate secured party has a right to expect that the sale of the original collateral will be properly conducted by the senior creditor and that he will get his share of the sale proceeds. Article 9 protects these expectations. It makes a secured creditor who disposes of collateral accountable to another secured party for failing to comply with the requirements of Part 5 regarding disposition of collateral and distribution of proceeds resulting therefrom; in both respects, however, accountability is conditioned.

A secured party who has sold the collateral is explicitly directed to apply surplus proceeds in "the satisfaction of indebtedness secured by any subordinate security interest in the collateral." For failing to remit these proceeds to a junior secured party entitled to them, the senior creditor is presumably liable for damages equalling the amount of the misdirected proceeds. This liability, however, will not exceed the obligation secured by the subordinate security interest. Moreover, the senior creditor's lateral pays the expenses of the disposition and satisfies his own security interest, he must apply any remaining sale proceeds to the satisfaction of indebtedness secured by any subordinate security interest in the collateral if written notification of demand therefor is received before distribution of the proceeds is completed. If requested by the secured party, the holder of a subordinate security interest must seasonably furnish reasonable proof of his interest, and unless he does so, the secured party need not comply with his demand.

*Id.* § 9-504(1)(c) (emphasis added). This is a conditional requirement imposed on the senior secured party who sold the property. *See id.* § 9-504 comment 2; *see also* text accompanying notes 54-58 infra.

53. The surplus funds actually received by the debtor are undoubtedly "proceeds," and, if these proceeds are identifiable, then a security interest continues in them. *See U.C.C.* § 9-306(1)-(2). The junior creditor's unsatisfied security interest thus follows these proceeds, which have become "collateral" to which he is entitled as against the debtor. *See id.* §§ 9-105(1)(c), 9-201, 9-503. Because the secured obligation owed to the senior creditor has been satisfied, he has no security interest that will continue in the surplus proceeds. "Value" is necessary to create a security interest, *see id.* §§ 9-203(1)(b), 1-201(44), and, if the value supporting a security interest is repaid or otherwise satisfied and no new value is given that the parties agreed would perpetuate its existence, the security interest terminates. *See, e.g.*, Bank of Lexington v. Jack Adams Aircraft Sales, Inc., 570 F.2d 1220, 1225 (5th Cir. 1978).


55. The subordinate creditor has no interest in, or claim to, any excess proceeds beyond...
responsibility to pay surplus proceeds to a junior creditor does not arise unless (a) "written notification of demand therefor is received before distribution of the proceeds is completed," and (b) the junior creditor furnishes "reasonable proof of his interest," if this proof is requested by the senior secured party. If either of these conditions is not satisfied, the senior creditor has no duty to remit surplus proceeds to the junior secured party and no liability for failing to do so.

Even if the senior secured creditor has no duty to remit surplus proceeds to the junior secured party, the senior may nevertheless be liable to the junior for damages caused by failing to comply with other Part 5 requirements with respect to the disposition of the original collateral. Of principal importance is the provision requiring that, in some cases, the secured party conducting a sale of collateral must send notification of the disposition to other secured parties. A senior secured party controlling foreclosure cannot be liable for this omission, however, unless the junior secured creditor was entitled to notification, which is never true when the collateral is consumer goods. The junior is entitled to notification when the collateral is nonconsumer goods only if the senior selling the collateral seasonably receives from the junior "written notification of a claim of an interest in the collateral." If this notice of claim is prop-

See U.C.C. § 9-504(1)(c), reproduced at note 52 supra. The debtor is entitled to the remaining proceeds. See id. § 9-504(2).

56. Id. § 9-504(1)(c).
57. Id.
58. See Louis Zahn Drug Co. v. Bank of Oak Brook Terrace, 95 Ill. App. 3d 435, 440, 420 N.E.2d 276, 279 (1981); U.C.C. § 9-504(1)(c). The subordinate creditor may nevertheless follow the proceeds into the hands of the one who received them—probably the debtor—because his security interest continues in these sale proceeds as "proceeds" as long as they remain identifiable. See id. § 9-306(1)-(2).
59. A secured party who disposes of collateral is liable to certain other secured parties for "any loss caused by a failure to comply with the provisions of [Part 5]." U.C.C. § 9-507(1).
60. See id. § 9-504(3).
61. Id.

This represents a change from earlier versions of Article 9, which required the giving of notice, except in cases involving consumer goods, by any other person who has a security interest in the collateral and who has duly filed a financing statement indexed in the name of the debtor in this state or who is known by the secured party to have a security interest in the collateral. U.C.C. § 9-504(3) (1962 Official Text). Thus, the liability of one secured party to another for not complying with Part 5 by failing to send notice of disposition could be triggered solely by constructive notice emanating from the other's filed financing statement. See, e.g., Stephens v. Bank of Camilla, 133 Ga. App. 210, 211-12, 210 S.E.2d 358, 360 (1974), aff'd, 234 Ga. 293, 216 S.E.2d 71 (1975).
erly given by a junior secured party who is not sent notification of the disposition of nonconsumer goods collateral, the senior creditor who conducted the sale is liable under section 9-507(1) for "any loss" caused thereby.63

Damages under this section also may be imposed on a senior secured party if he fails to comply with another principally important Part 5 requirement: when collateral is disposed of by sale, the disposition must be in "every respect . . . commercially reasonable."64 One secured party's liability to another for conducting a commercially unreasonable sale is also conditioned, however, by section 9-507(1). The complaining creditor must have been "entitled to notification" of the disposition65 or his security interest must have been "made known to the secured party prior to the disposition."66 Reason to know or constructive notice will not trigger liability.67 Yet, in any case in which a senior secured party has repossessed the collateral from a junior secured party, it appears likely that the existence of the subordinate security interest will actually become known or, more precisely, will be "made known" to the senior creditor long before he disposes of the property.68 Thus, in this type of case the junior secured

63. This is true because, if another secured party is entitled to notification of disposition, then the provisions of Article 9 require that notice be sent to him; by failing to send such notification, the secured party who sold the collateral will have failed to comply with the provisions of Part 5 and thus will be liable under U.C.C. § 9-507(1). See Heyboer v. Kolberg, 493 F. Supp. 137, 139-40 (W.D. Mich. 1980); Young v. Golden State Bank, 39 Colo. App. 45, 49, 560 P.2d 855, 859 (1977); Stephens v. Bank of Camilla, 133 Ga. App. 210, 211-12, 210 S.E.2d 358, 360 (1974), aff'd, 234 Ga. 293, 216 S.E.2d 71 (1975). These three cases involved other secured parties entitled to notification of disposition under the different rules of an earlier version of Article 9. Regarding the difference between the present version and earlier versions with respect to when other secured parties are entitled to notification of sale, see note 62 supra.

64. U.C.C. § 9-504(3).

65. Id. § 9-507(1). The situations in which another secured party is entitled to notification of disposition are discussed at text accompanying notes 59-63 supra.


67. This is true because the Code defines "knows" or "knowledge" of a fact to mean "actual knowledge of it. 'Discover' or 'learn' or a word or phrase of similar import refers to knowledge rather than to reason to know." Id. § 1-201(25) (emphasis added). Under a previous version of Article 9, however, the liability of one secured party to another for conducting a commercially unreasonable sale was triggered by constructive notice of the other's interest. Section 9-507(1) read the same, but another secured party was entitled to notification of disposition if he had filed a financing statement. See U.C.C. § 9-504(3) (1962 Official Text), reproduced at note 62 supra. Therefore, solely for the reason that he had duly filed a financing statement in the state, this other secured party could recover damages if he did not receive such notification or if the secured party selling the collateral failed to comply with the provisions of Part 5 in any other way.

68. Is there a difference between a secured party knowing of another security interest by (a) somehow learning about it and (b) having it made known to him? The effect is the same: he actually knows of its existence. Yet, "made known," as used in U.C.C. § 9-507(1), seems to imply that the other creditor must take some affirmative action to alert the secured party controlling foreclosure of his interest. To be considered on this issue is that the alternative trigger on the foreclosing creditor's liability to another secured party under U.C.C.
party ordinarily will be entitled to recover under section 9-507(1) for “any
loss” caused by a senior creditor's failure to conduct a commercially
reasonable sale of the collateral.\(^6\)

How to calculate damages according to the “any loss” standard of
section 9-507(1) is not explained in the provision itself or elsewhere in
Article 9. Under pre-Code law, if a senior secured creditor improperly
disposed of collateral, his conduct was characterized as a conversion.\(^7\) Of
course, the junior creditor could not recover the full value of the collateral,
but could recover only the value of his interest therein.\(^7\) This value was
calculated by determining the market value of the property as of the time
of the conversion and subtracting therefrom the amount of the senior
creditor’s encumbrance.\(^7\) A senior secured party’s liability to a subor-
dinate secured party under section 9-507(1) for failing to comply with the

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\(^{6}\) § 9-507(1) is entitlement to notification, which places a burden squarely on the other secured
party of affirmatively giving notice of his interest. See U.C.C. § 9-504(3); text accompa-
nying notes 59-63 supra. It is also relevant that under a previous version of Article 9,
another secured party was entitled to notification if his security interest was perfected
by filing or was “known by the secured party” controlling foreclosure. U.C.C. § 9-504(3)
(1962 Official Text) (emphasis added), reproduced at note 62 supra. Under this same
version, the alternative condition on one secured party’s liability to another under U.C.C.
§ 9-507(1) was whether the other’s security interest had been “made known to the secured
party prior to the disposition.” Id. § 9-507(1) (1962 Official Text) (emphasis added). The
current text preserves this condition. U.C.C. § 9-507(1). The use of different language
could imply a substantive difference between “made known” and “known by.”

If U.C.C. § 9-507(1) does impose an affirmative duty on the other secured party to
make his security interest known, conduct short of giving written notice will suffice.
See Louis Zahn Drug Co. v. Bank of Oak Brook Terrace, 95 Ill. App. 3d 435, 442, 420

\(^{7}\) This is undoubtedly true; yet, the possibility that one secured party may ever
be liable to another for a commercially unreasonable disposition of collateral is confirmed
by only a very few cases. See, e.g., Liberty Nat'l Bank & Trust Co. v. Acme Tool Div.
of the Rucker Co., 540 F.2d 1375, 1382 (10th Cir. 1976); Louis Zahn Drug Co. v. Bank
of Oak Brook Terrace, 95 Ill. App. 3d 435, 442, 420 N.E.2d 276, 280 (1981); Barry

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provisions of Part 5 also should be calculated in this manner, whether or not the misconduct is technically characterized as a conversion. When a proper sale is conducted, the junior secured party can expect to receive only the surplus proceeds that remain after the senior creditor has satisfied the expenses of foreclosure and his own superior security interest. Compliance with the provisions of Part 5 theoretically assures that the true value of the collateral—its market value—will be realized upon the disposition; a proper sale will squeeze the maximum proceeds from the collateral and increase the likelihood and amount of surplus proceeds that the subordinate creditor can claim. If the senior creditor’s sale of the collateral is improperly conducted, the junior secured party’s actual loss is the amount that would have remained after subtracting the legitimate expenses of foreclosure and the senior creditor’s security interest from the amount that would have been produced by a proper sale—the fair market value of the collateral. Measuring the junior secured party’s “any loss” under section 9-507 in this way is essentially identical to the method used in pre-Code cases of this sort, and, more important, it will put the subordinate creditor “in as good a position as if the other party [the senior secured party] had fully performed,” which is the express purpose of the Code remedies.

The junior creditor may not be in as good a position, however, if the usual pre-Code measure of damages is applied when a senior secured party sells the collateral after having wronged the junior secured party by refusing a proper and timely offer to redeem the property. Section 9-506 gives “any other secured party” the right of redemption; yet, a senior creditor’s wrongful refusal to allow a subordinate secured party to redeem will not affect, theoretically or practically, the amount of proceeds resulting from the sale of collateral. Therefore, the subordinate creditor will not be compensated for this wrong if the senior secured party’s only penance is that he must account for the market value of the collateral less the amount of his superior interest. If the senior creditor in all other respects com-

73. See U.C.C. § 9-504(1); text accompanying notes 48-58 supra.
74. U.C.C. § 1-106(1). In the few Article 9 cases in which junior secured parties have sued senior secured parties for failing to comply with Part 5, damages have been determined in a manner consistent with the method used in similar pre-Code cases: See, e.g., Liberty Nat’l Bank & Trust Co. v. Acme Tool Div. of theucker Co., 540 F.2d 1375, 1381-83 (10th Cir. 1976); Heyboer v. Kolberg, 493 F. Supp. 137, 139-40 (W.D. Mich. 1980); Young v. Golden State Bank, 41 Colo. App. 480, 482-83, 589 F.2d 1381, 1382 (1978); Food City, Inc. v. Fleming Cos., 590 S.W.2d 754, 761 (Tex. Civ. App. 1979). But see United States v. Mid-States Sales Co., 336 F. Supp. 1099, 1103-04 (D. Neb. 1971) (senior secured party who improperly disposed of collateral apparently lost priority status as a result); cf. Nickles, Rethinking Some U.C.C. Article 9 Problems—Subrogation; Equitable Liens; Actual Knowledge; Waiver of Security Interests; Secured Party Liability for Conversion Under Part 5, 34 Ark. L. Rev. 1, 142-77 (1980) (arguing that a debtor’s “any loss” under U.C.C. § 9-507(1) should be calculated according to the common-law conversion measure of damages).
75. U.C.C. § 9-506, reproduced at note 47 supra.
plied with Part 5, he may escape liability if theory holds true and the sale proceeds in fact equalled the market value of the collateral.

This result cannot be justified on the basis that the junior secured party actually lost nothing as a result of being denied his right of redemption. He may not have been damaged in the limited sense that, had he been allowed to redeem and had he then sold the collateral himself, his position would have been no better in terms of net realization from the property. Nevertheless, a secured party who redeems may choose to foreclose without selling the collateral, or he may choose not to foreclose at all. Possibly, he may decide to return the property to the debtor because he fears that, without the use of the collateral, the debtor’s financial condition will worsen. The secured party may hope that, given the property and some time, the debtor will be able to satisfy fully the creditor’s claim. Denying a junior secured party his right to redeem prevents him from pursuing this and other possible alternatives to disposing of the collateral by selling it himself. Not having these alternatives is itself a loss caused by the senior creditor’s denial of the junior’s right of redemption; and this and any consequential losses are not measured by the traditional formula for conversion damages, because this formula forces the senior secured creditor to account only for the collateral’s market value less the amount of his interest.

In a pre-Code case, *Walker v. Houston,* the California Supreme Court recognized the inappropriateness of using the traditional formula to calculate the damages recoverable by the junior creditor in this kind of case. The court took a decidedly different approach by reasoning that when a junior secured creditor’s offer of redemption is refused, the senior creditor loses his interest in the property. The senior becomes an unsecured creditor.

76. Selling the collateral is clearly not the only permissible method of disposition. A secured party may “sell, lease or otherwise dispose of any or all of the collateral.” *Id.* § 9-504(1) (emphasis added). Moreover, there is an alternative to disposition. Strict foreclosure is possible in some cases, which means that the secured party retains the collateral in satisfaction of the secured debt. *See id.* § 9-505.

77. 215 Cal. 742, 12 P.2d 952 (1932).

78. In *Walker* the senior creditor was a conditional vendor of the collateral, who had reserved title to the goods, and the subordinate secured party was a chattel mortgagee. The court’s analysis was simple and straightforward:

> The title is reserved for security only. The buyer has the full right of possession and use unless he defaults, and may secure title by performance of his obligation without any further assent by the seller. The sole interest of the seller is in the receipt of the price, and his reserved title cannot be used for any other purpose. Hence it follows that tender of the balance of the price should have the effect of discharging the title of the seller and vesting such title in the buyer . . . . The right of a mortgagee or purchaser from the conditional buyer to make such tender with the same effect as if made by the buyer himself is also recognized, even where the conditional sales contract contains express restrictions against sale, assignment or mortgage. *Id.* at 746-47, 12 P.2d at 954 (citations omitted). That a secured creditor’s interest in real or personal property is lost when he refuses a valid tender of the outstanding obligation is an established common-law principle that applies whether the debtor himself, as
who still has recourse against the debtor on the underlying obligation, but not against the collateral that formerly secured it. If the senior creditor nevertheless disposes of the goods to which he now has no claim, he thereby converts them and becomes liable to the junior creditor whose interest has become superior. When collateral is converted by one with a subordinate interest or no interest whatsoever in the property, the secured creditor entitled to priority can recover from the converter the full amount of his superior interest up to the collateral's worth, with no offset for any subordinate interest in the property or for any unsecured claim against the debtor.

Can the approach taken by the court in *Walker* be followed in an Article...
case in which a senior secured party wrongfully refuses a junior secured party's offer of redemption and then sells the collateral? Section 9-507(1) clearly provides a compensatory remedy against a secured party who fails "to comply with the provisions of this Part": the injured party can recover "any loss" caused thereby. Because section 9-506 is a "provision" of Part 5, it might be argued that the "any loss" remedy is exclusive and that the Walker approach is thereby displaced under the Code. There are two responses to this argument, however. First, the commentary to section 9-507(1) suggests that the "any loss" recovery is designed to remedy noncompliance with requirements having to do with the sale or other disposition of collateral pursuant to section 9-504. Thus, violations of section 9-506 may not be within the ambit of the second sentence of section 9-507(1), which provides for the "any loss" recovery.

Second, even if such violations are covered by this segment of section 9-507(1), the sentence literally provides only a remedial measure of damages. It does not necessarily preclude the application of substantive common-law principles, under which secured creditors who refuse a proper offer of redemption may thereby lose their interest in the collateral and

81. U.C.C. § 9-507(1).
82. But cf. Wells v. Central Bank, 347 So. 2d 114, 120-21 (Ala. App. 1977) (unlawful refusal to permit debtor to redeem is a conversion and the debtor can pursue either a common-law action for conversion or the remedy provided under U.C.C. § 9-507(1)).
83. The first comment to the section provides in pertinent part:
   The principal limitation on the secured party's right to dispose of collateral is the requirement that he proceed in good faith . . . and in a commercially reasonable manner. See Section 9-504. In the case where he proceeds . . . in a contrary manner, it is vital both to the debtor and other creditors to provide a remedy for the failure to comply with the statutory duty . . . . The section . . . provides for damages where the unreasonable disposition has been concluded . . . .
   U.C.C. § 9-507 comment 1, at 768 (emphasis added).
84. The principle that led to the result in Walker, that when a secured creditor unlawfully refuses a proper tender of payment, he thereby loses his interest in the collateral, 215 Cal. at 748, 12 P.2d at 954, did not begin and end with this case. Rather, it is well established in California by a long series of cases. See, e.g., Leet v. Armbruster, 143 Cal. 663, 668-70, 77 P. 653, 654-55 (1904) (debtor’s transferee tendering to real estate mortgagee); Loughborough v. McNevin, 74 Cal. 250, 254, 14 P. 369, 371 (pledge transaction), aff’d en banc, 74 Cal. 250, 15 P. 773 (1887); Wagner v. Shoemaker, 29 Cal. App. 2d 654, 656-57, 85 P.2d 229, 230-31 (1938) (real estate). The California courts often relied on a provision of the California Civil Code which provides that "[a]n offer of payment or other performance, duly made, though the title to the thing offered be not transferred to the creditor, stops the running of interest on the obligation, and has the same effect upon all its incidents as a performance thereof." CAL. CIV. CODE § 1504 (West 1954) (emphasis added). But it cannot be argued that reliance on this provision limits the persuasive force of Walker to those jurisdictions having a similar enactment. There is ample evidence that the rule under which a secured creditor loses his lien by wrongfully refusing to allow redemption is a firmly and widely established principle of the common law. See, e.g., Mitchell v. Roberts, 17 F. 776, 780 (E.D. Ark. 1883); McCalla v. Clark, 55 Ga. 53, 56 (1875) (pledge transaction); Schleiff v. McDonald, 45 Idaho 620, 627, 264 P. 866, 868 (1928) (tender by chattel mortgagor’s transferee); Pierce v. Hasbrouck, 49 Ill. 23, 25 (1868) (by implication); Simon Casady & Co. v. German Sav. Bank, 159 Iowa 149, 154-55, 140
be guilty of conversion for thereafter disposing of the property. When these
principles are followed, it remains necessary to determine the damages
suffered by the junior secured party whose interest was elevated on the
basis of the common law and whose collateral was thereafter sold by the
formerly senior secured creditor. Section 9-507(1) could be consulted for
this purpose.85 Thus, the substantive principles of common law and the

N.W. 401, 403 (1913); Ramsdell v. Tewksbury, 73 Me. 197, 199 (1882) (dictum); Dame
v. C.H. Hanson & Co., 212 Mass. 124, 126, 98 N.E. 589, 589 (1912); Avery v. Midwest
Commercial Credit Co., 254 Mich. 324, 326-27, 236 N.W. 798, 799 (1931); Tompkins
v. Batie, 11 Neb. 147, 150, 7 N.W. 747, 747 (1881) (dictum); Bailey v. Colby, 34 N.H.
29, 35 (1856); Frost v. Yonkers Sav. Bank, 70 N.Y. 553, 558, 561 (1877) (tender by
junior real estate mortgagee); Barbee v. Scoggins, 121 N.C. 135, 143, 28 S.E. 259, 262
(1897); Bartel v. Lope, 6 Or. 321, 327 (1877); Ratcliff v. Vance, 9 S.C.L. (2 Mill) 349,
350 (1818) (pledge transaction); Texas Auto Co. v. Clark, 12 S.W.2d 655, 657-58 (Tex.

It might be argued, however, that virtually everywhere the common-law principle is
displaced by U.C.C. §3-604, which provides that "[a]ny party making tender of full
payment to a holder when or after it is due is discharged to the extent of all subsequent
liability for interest, costs and attorney's fees." Security interests are not mentioned; thus,
perhaps, they are not discharged by a proper tender. There are several responses to this
argument. First, obligations secured by collateral will not always be embodied in negotiable
instruments, and U.C.C. Article 3 usually will not apply to any aspect of such an arrange-
ment. Second, even if the secured debt is evidenced by an instrument and, therefore,
§3-604 applies, the fact that security interests are not mentioned-in the provision does
not necessarily imply an intention by the drafters to keep them alive after a proper tender.
Third, the section governs only the rights and liabilities with respect to the instrument
itself and does not govern those with respect to ancillary agreements or provisions for
security. Finally, U.C.C. §3-604 explains only the effect of a party making a tender to
a holder. A junior encumbrancer ordinarily will not be a party to the instrument, and
in a rare case the senior creditor may not be a holder. In either case other law would
have to be consulted to determine the effect of tender by the subordinate creditor.

85. There is precedent for teaming liability based on common-law conversion with
 damages founded on the "any loss" recovery allowed under U.C.C. §9-507(1). See, e.g.,
Consolidated Equip. Sales, Inc. v. First State Bank & Trust Co., 627 P.2d 432, 438 (Okla.

The "any loss" recoverable under U.C.C. §9-507(1) might be calculated as it is under
the common law when the wrongdoer's conduct is characterized as a conversion
of the collateral and of the injured secured creditor's now superior interest in the property. See
text accompanying note 80 supra. This method of calculation may be easier to accept in
light of the cases suggesting that, by refusing a proper offer of redemption, a secured
creditor thereby converts the collateral, or that he converts it when he thereafter disposes
of the property. For pre-Code cases, see Walker v. Houston, 215 Cal. 742, 747, 12 P.2d
952, 954 (1932); note 79 supra. For Article 9 cases, see Draughon v. General Fin. Credit
Corp., 362 So. 2d 880, 886 (Ala. 1978); Owens v. Automobile Recovery Bureau, Inc.,
544 S.W.2d 26, 32 (Mo. App. 1976).

The suggestion that this conduct by a senior secured party amounts to conversion
is not necessarily inconsistent with the argument that a mere sale of collateral by a junior
secured party does not in itself constitute conversion of the property. See text accompan-
ying notes 182-91 infra. When a secured party denies another creditor the right to redeem
the property, he thereby refuses to give possession of the collateral to a party rightfully
entitled to have the property. Aside from any sale of the collateral, this refusal can itself
amount to a conversion. See text accompanying notes 175-81 infra.
section 9-507(1) remedy can be applied not only consistently, but together in tandem, and this may support the view that the latter does not displace the former in this type of case.

Even if a junior creditor’s exclusive remedy is section 9-507(1), a senior secured party who wrongfully refuses a subordinate secured party’s offer to redeem and thereafter sells the collateral may not completely avoid damages for his wrong. Making a senior secured party account for the collateral’s market value less the amount of his own interest is only one method of judging an injured junior creditor’s “any loss” caused by the senior secured party’s noncompliance with the provisions of Part 5. Courts surely can devise other methods for determining “loss” under section 9-507(1). One approach is to base loss on the provable damages actually suffered by the subordinate creditor. Courts should be especially flexible when calculating damages resulting from a senior secured party’s illegal denial of another secured party’s right to redeem, because traditional approaches may not compensate, or only coincidentally compensate, the subordinate creditor for the wrong suffered.

The risk that a senior secured creditor will be liable for failing to comply with the provisions of Part 5 of Article 9 is one reason a senior secured party may be unwilling to repossess collateral from a junior secured party and dispose of it himself. The senior creditor may prefer to let the subordinate secured party keep the property and attempt to enforce the priority of his superior security interest in some other way.

III. CLAIMING PROCEEDS RECEIVED BY THE SUBORDINATE SECURED PARTY UPON FORECLOSURE CONTROLLED BY HIM

After a secured party repossesses collateral, he must deal with it pursuant to Part 5 of Article 9. Ordinarily, the property is sold at a public or private sale for the purpose of satisfying the security interest of the party who conducts the disposition. Whenever a subordinate secured party sells collateral, however, a senior creditor may argue that he has a superior claim to the sale proceeds based on the priority of his security interest in the original collateral, and that the junior secured party must, therefore, account for the proceeds. This argument has intuitive appeal. If, as against a subordinate secured party, a senior creditor is entitled to possession of the original collateral because of the superiority of his security interest, it seems logical that he should also be entitled to the fruits of the property if his interest and priority continue with respect to these proceeds. Yet, nothing in Article 9 clearly and explicitly gives a senior secured party a prior right to the proceeds of a foreclosure sale conducted by a junior secured party; several provisions strongly imply that no such right exists.

86. Several Article 9 provisions seem at first glance to implicitly support a senior secured party’s claim to proceeds of collateral disposed of by a subordinate secured party. One of them is § 9-507(1), which makes it clear that a secured creditor who disposes of col-
Section 9-504 details how the proceeds of a Part 5 disposition must be applied. Expenses of retaking and selling the collateral are paid first; the security interest of the party who conducted the sale is then satisfied.

Later can be liable to other secured parties if the disposition fails in any respect to comply with the Part 5 requirements of Article 9. This section does not limit possible accountability to subordinate secured parties; the one conducting the sale is potentially liable to "any person entitled to notification or whose security interest has been made known to the secured party [who conducted the sale] prior to the disposition." U.C.C. § 9-507(1) (emphasis added). "Any person" surely includes a creditor with a superior security interest in the collateral. The fact that a senior secured party may recover under § 9-507(1) for a defective sale by a junior secured party implies that the senior creditor has a claim to proceeds of the disposition. The reason for this implication is that, notwithstanding sale by a subordinate secured party, a secured creditor's security interest will follow the collateral into the buyer's hands, and the property can be repossessed from him. See authorities cited in notes 145-46 infra. Therefore, why should a senior secured party ever be entitled to complain about the particulars of a Part 5 sale by a junior secured party? Surely the drafters intended that only a person who had a stake in the outcome of the disposition could recover for a defective sale; therefore, the only possible answer is that, despite continuation of his security interest in the original collateral, the senior creditor also has a claim to proceeds resulting from the junior creditor's disposition.

This does not necessarily mean, however, that a senior secured party has a prior right to all proceeds resulting from a junior creditor's sale of collateral. A senior creditor generally should be able to recover for a defective sale if he has any stake in the outcome, i.e., a claim to any proceeds that conceivably might result from a junior creditor's disposition of collateral. Undoubtedly, the senior secured party has a right to those surplus proceeds that potentially may exist and be paid to the debtor under U.C.C. § 9-504(2) after the subordinate creditor satisfies his own interest pursuant to § 9-504(1). See text accompanying notes 99-103 infra. The right to these surplus proceeds alone is a sufficient explanation for giving a senior secured party a cause of action against a junior secured party who conducts an improper foreclosure sale of collateral. The more proceeds that result from the collateral's disposition, the more likely it is that surplus proceeds will remain. A sale conducted according to law will theoretically produce the most proceeds that can be expected from a disposition held within a reasonable time after the collateral's disposition. Thus, a senior secured party has a basis for complaining about an improper sale if only for the reason that it may decrease the likelihood and amount of surplus proceeds. Consequently, § 9-507(1) does not necessarily imply that a senior secured party has a superior claim to sale proceeds that are generated by a junior creditor's sale of collateral and that are applied by this subordinate secured party in the manner prescribed by § 9-504(1).

It might also be argued that, at least in some cases, U.C.C. § 9-312 gives the senior secured party a superior claim to sale proceeds received by the junior creditor. Subsections (3) and (4) of § 9-312 seem explicitly to insure that a purchase money secured party with priority in the original collateral also has priority in proceeds (certain "cash proceeds" in the case of § 9-312(3)). One problem with this argument is that it begs the question. What does priority in and of itself imply and allow? Article 9 offers few hints and expressly provides nothing with respect to the administration or enforcement of priority. Another problem with the argument is the further assumption that proceeds of a Part 5 sale by a junior secured party are "proceeds" under § 9-306(1) in which a security interest continues under § 9-306(2). This may not be true. See text accompanying notes 99-141 infra. For this and other reasons, § 9-306(2) may not itself give a senior secured party a prior right to the proceeds of a junior secured party's sale of the original collateral. See text accompanying notes 99-155 infra.

87. U.C.C. § 9-504(1)(a).
88. Id. § 9-504(1)(b).
Next, if any proceeds remain, any subordinate security interest is satisfied if its holder has made a proper and timely demand.90 Nothing whatsoever is paid to the debtor.90 Nothing whatsoever is provided with respect to senior security interests.91 The negative inference is that, as far as proceeds are concerned, a secured party who disposes of collateral pursuant to Part 5 is not accountable to a creditor with a superior security interest. This inference is strengthened by the rule of statutory construction expressio unius est exclusio alterius: the mention of one thing implies the exclusion of the other.92 Because section 9-504(1) lists the items to be paid from the proceeds of the collateral’s disposition, it implies negatively that no others are to be satisfied.

This inference is further strengthened when the legislative history of section 9-504 is considered. Under the Spring 1950 Proposed Draft of the Uniform Commercial Code, a secured lender who sold collateral was directed to apply the proceeds of the sale “to reasonable expenses of retaking, holding, preparing for sale and selling and to the satisfaction of the indebtedness.”93 Under this version of section 9-504, any remaining surplus was paid to the debtor,94 and no provision was made for satisfying senior security interests. This draft of the Code was discussed in May 1950 at a meeting of the American Law Institute and the National Conference of Commissioners on Uniform State Laws. This meeting produced several changes in the evolving Article 9;95 among them was an expanded directive concerning the application of proceeds resulting from a foreclosure sale of collateral.

Section 9-504 was rewritten to require that sale proceeds be distributed, in the following order, to:

- (a) the reasonable expenses of retaking, holding, preparing for sale, selling and the like to the extent the recovery thereof is not prohibited by law or agreement;
- (b) the satisfaction of indebtedness secured by any security interest or lien having priority over the security interest under which the disposition is made unless with the consent of the owner of such prior interest or lien the disposition is made specifically subject thereto or unless such owner refuses to accept such proceeds;

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89. Id. § 9-504(1)(c). See text accompanying notes 54-58 supra.
90. U.C.C. § 9-504(2).
94. Id.
95. See U.C.C. (September 1950 Revisions of Articles 2, 4, and 9).
(c) the satisfaction of the indebtedness secured by the security interest under which the disposition is made;
(d) the satisfaction of indebtedness secured by any subordinate security interest in the collateral if written notification of demand therefor is received before distribution of proceeds is completed.

The secured lender must account to the debtor for any surplus . . . .

Thus, for the first time, the drafters expressly provided for the satisfaction of senior security interests before all other interests. This was a short-lived provision, however. It did not appear in section 9-504 of the 1951 Proposed Draft and never became a part of the official text. No reason was given for failing to include the proposal in later versions of section 9-504. One reasonable explanation is that the drafters simply decided against giving a senior secured party a right to the proceeds of a sale of collateral conducted by a junior secured party.

Some might argue that a senior secured party's right to such proceeds is not dependent on an express provision in section 9-504 and that Article 9 otherwise establishes this creditor's claim to the proceeds of a junior secured party's sale of collateral. The section most likely to be relied on to sustain this argument is section 9-306(2), which gives a secured party a continuing security interest "in any identifiable proceeds including collections received by the debtor." In the recent case of Consolidated Equipment Sales, Inc. v. First State Bank & Trust Co. the court cited this section to support the conclusion that once the junior secured party achieved repossession, it "had an obligation to turn proceeds of the sale of the collateral over to . . . the senior secured party."

96. Id. § 9-504(1) (emphasis added).
97. This draft required the proceeds of disposition to be applied, in the following order, to:
   (a) the reasonable expenses of retaking, holding, preparing for sale, selling and the like to the extent the recovery thereof is not prohibited by law or agreement;
   (b) the satisfaction of indebtedness secured by the security interest under which the disposition is made;
   (c) the satisfaction of indebtedness secured by any subordinate security interest in the collateral if written notification of demand therefor is received before distribution of the proceeds is completed.
98. The reason was not that the drafters in later versions for the first time provided for continuing a senior security interest in the very collateral that was sold. Provision for this was made in early versions, including the September 1950 draft, which also expressly directed that, after deduction of reasonable sale expenses, proceeds of the sale of collateral were to be applied first to satisfy senior security interests. See U.C.C. § 9-504(1) (September 1950 Revisions of Articles 2, 4, and 9).
100. 627 P.2d 432 (Okla. 1981).
101. Id. at 438. The issue has seldom been squarely faced and addressed in the reported cases, but a few courts have hinted or implied that a junior secured party who disposes of collateral is accountable to a senior secured party for the sale proceeds. See, e.g., United
Reliance on section 9-306(2) is problematic, however. The major problem is that the section can be interpreted to condition the continuation of a security interest in any proceeds on the debtor’s receipt thereof. When a junior secured party sells collateral, he, and not the debtor-obligor, receives the proceeds. Under this interpretation, a senior secured party would have no interest in proceeds received and retained by the subordinate creditor and thus no basis under Article 9 on which to assert a superior claim to the proceeds. The senior creditor could claim only the surplus proceeds, if any, paid to and actually received by the debtor.

The correctness of this interpretation depends largely on whether the phrase “received by the debtor” modifies the word “proceeds” in the second clause of section 9-306(2), or only the word “collections.”

The comment to section 9-306 states that its purpose is to state “a


The case referred to in text, Consolidated Equipment Sales, does not actually hold that a junior secured party must account to a senior secured party for proceeds resulting from the subordinate creditor’s sale of the property. Instead, the court held that the junior secured party who sold the collateral and applied the proceeds to his own debt was liable to the senior creditor for conversion of the original collateral and accountable for this property’s value, but was not liable for the sale proceeds that resulted from the disposition. A junior secured party’s liability generally for conversion of the original collateral is discussed at text accompanying notes 156-203 infra. For criticism of cases such as Consolidated Equipment Sales, in which this liability is founded on the subordinate creditor’s sale of the collateral plus the diversion of sale proceeds, see text accompanying notes 197-203 infra.

102. Regarding this issue, Professor Henson stated:

The definition of “proceeds” in Section 9-306(1) says the term “includes whatever is received” but it does not say by whom the proceeds must be received. Section 9-306(2) states that the security interest “continues in any identifiable proceeds including collections received by the debtor.” This provision is capable of being read to say that proceeds, which include collections, must be received by the debtor, or that the proceeds need not be received by the debtor but the security interest will in any event continue in identifiable proceeds regardless of who receives them and it will also continue in collections received by the debtor.

R. HENSON, HANDBOOK ON SECURED TRANSACTIONS UNDER THE UNIFORM COMMERCIAL CODE § 6-1, at 197 (2d ed. 1979). The courts do not agree on how to resolve the ambiguity. See authorities cited in note 113 infra.

103. The secured party who conducts the disposition of collateral “must account to the debtor for any surplus,” U.C.C. § 9-504(2) (emphasis added), which apparently is what remains after the sale proceeds have been distributed according to U.C.C. § 9-504(1). The junior secured creditor who sold the collateral will have no claim to these surplus proceeds because his security interest will have been satisfied pursuant to U.C.C. § 9-504(1)(b). The debtor’s right to the proceeds obviously will be subordinate to the senior secured party’s claim; the surplus is property in which the senior secured party’s security interest continues, i.e., collateral. See id. §§ 9-105(1)(c); 9-201; 9-306(1)-(2); 9-503.
secured party's right to the proceeds received by a debtor."¹⁰⁴ This language seems to make the debtor's receipt an explicit condition to the continuation of a security interest in any and all proceeds, not just those in the form of collections. This comment is consistent with earlier versions of section 9-306 that more clearly limited proceeds in which a security interest continued to those received by the debtor. In the Spring 1950 Proposed Final Draft of the Code, section 9-306 provided that if "collateral is sold, exchanged, collected or otherwise disposed of by the debtor the security interest continues in any identifiable proceeds received by the debtor."¹⁰⁵ In this version "received by the debtor" unquestionably modifies "proceeds." Identical language appeared in the Spring 1951 Proposed Final Draft¹⁰⁶ and in the 1952 Official Text.¹⁰⁷ The modern phraseology of section 9-306(2), containing the words "including collections," was initially proposed in the 1956 Recommendations of the Editorial Board¹⁰⁸ and became a part of the official text in 1957.¹⁰⁹ The section was rewritten simply "for clarity"¹¹⁰ and not, by any account, to enlarge the category of property known as "proceeds" in which a security interest will continue.¹¹¹

¹⁰⁴. Id. § 9-306 comment 1 (emphasis added).
¹¹¹. The scope of this category also is not affected by a later change in the first clause of U.C.C. § 9-306(2). From 1957 to 1972, § 9-306(2) provided:

Except where this Article otherwise provides, a security interest continues in collateral notwithstanding sale, exchange or other disposition thereof by the debtor unless his action was authorized by the secured party in the security agreement or otherwise, and also continues in any identifiable proceeds including collections received by the debtor.

U.C.C. § 9-306(2) (1957 Official Text with Comments) (emphasis added). The words "by the debtor" and "his action" in the first clause were deleted from the official version in 1972. See U.C.C. § 9-306(2) (1972 Official Text with Comments). The drafters gave no reason for this change, but its apparent effect is to broaden "the rights of secured parties to preserve their interest under a disposition of assets effected by persons other than the debtor." El Paso County Bank v. Charles R. Milisen & Co., ___ Colo. App. ___, 622 P.2d 594, 596 (1980). What is preserved by the first clause of § 9-306(2), however, are security interests solely in the very property that is sold; this part of the provision does not govern security interests in proceeds of this property. Whether a security interest continues in proceeds is controlled exclusively by the second clause of the section, and the drafters chose not to delete the critical words "by the debtor" from this part of the provision. Consequently, a broadening of the rights of a secured party under § 9-306(2) (first clause) with respect to the very property that is disposed of does not necessarily imply a corresponding enlargement of his interest under § 9-306(2) (second clause) to cover the proceeds of this property. The whole purpose for making the change in the
A few courts have concluded that property received in exchange for collateral is "proceeds" as defined in section 9-306(1)\(^{112}\) and that a security interest continues in these proceeds under section 9-306(2) even though someone other than the debtor actually receives them.\(^{113}\) Most of these cases are easily distinguished, however, for they involve a resale of collateral by someone to whom the debtor-obligor sold the property. The transferee in such a case may himself be a "debtor," so that proceeds received by him as a result of his own sale of the original collateral are proceeds "received by the debtor" or, at least, by "a" debtor. The term "debtor" is broadly defined by Article 9 to mean:

the person who owes payment or other performance of the obligation secured, whether or not he owns or has rights in the collateral, and includes the seller of accounts or chattel-paper. Where the debtor and the owner of the collateral are not the same person, the term "debtor" means the owner of the collateral in any provision of the Article dealing with the collateral, the obligor in any provision dealing with the obligation, and may include both where the context so requires.\(^{114}\)

A buyer from the debtor-obligor acquires his seller’s residual rights and interests with respect to the collateral,\(^{115}\) and these probably include title,
albeit an encumbered title. Thus, the transferee seems clearly to qualify as an "owner" within any common and traditional meaning of the term, and, consequently, he may be a "debtor" within the meaning of Article 9 if the property he buys continues to be "collateral." This is confirmed by the drafters' comment that "debtor" includes a person to whom "property is transferred subject to the secured debt of the transferor . . . ."

Nothing in the text or commentary of Article 9 clearly provides that a junior "secured party" who disposes of collateral may at the same time be a "debtor" with respect to that collateral simply because he has a security interest in the property. Each term is the other's virtual antonym. Additionally, nothing suggests that having a security interest in itself constitutes "ownership" of the collateral for Article 9 purposes. Title does

116. Even if the secured party is the seller of the goods and purports to retain title to the collateral, title nevertheless passes to the buyer according to the rules of U.C.C. § 2-401. The seller's attempted reservation of title can have only the limited effect of reserving a security interest. Id. § 2-401(1).

117. "A person who has the totality of rights, powers, privileges and immunities which constitute complete property in a thing . . . is the 'owner' of the 'thing' or 'owns' the 'thing.'" 1 RESTATEMENT OF PROPERTY § 10 comment b (1936). This clearly describes the debtor-obligor, and by granting a security interest to the secured party, he is not deprived of his status as "owner." See id. comment c. "Thus an owner of an automobile may mortgage it . . . and still properly be said to be the owner." Id. The transferee of all of this person's rights and interests with respect to the property, which collectively amounts to "ownership," is thus properly called the property's owner.


120. It is possible that, for other reasons, a secured party may also be a debtor. For instance, a junior secured party may be a "debtor" if he, too, is personally obligated on the debt owed the senior secured party. In such a case the subordinate creditor is a "debtor" because he "owes payment or other performance of the obligation secured." Id. § 9-105(1)(d). Also, a secured party may become a debtor if he sells to another the chattel paper that evidences the obligation owed to him. Id. Even in this case, however, he may not be both a secured party and a debtor. If he sells his security interest so that it no longer exists in his favor, he may lose his status as a secured party. The buyer of the chattel paper becomes the secured party. See id. § 9-105(1)(m). Possibly, however, the secured party who owns chattel paper may create a security interest in the property instead of selling it. In such a case he will be the secured party vis-a-vis the account debtor, and he will be the debtor vis-a-vis the creditor to whom he granted a security interest in the chattel paper.

121. The definition of "debtor" appears at text accompanying note 114 supra. "Secured party" is defined to include "a lender, seller or other person in whose favor there is a security interest." Id. "Security interest" means an interest in personal property or fixtures which secures payment or performance of an obligation." Id. § 1-201(37). The term "secured party" implies a person who is owed an obligation; "debtor" suggests the person who owes it either in the sense that he is personally liable for the obligation or that his property stands as security therefor. The secured party is the person in whose favor a security interest exists, and the debtor is the person against whom it operates.

122. This does not necessarily mean, however, that a secured party qua secured party
not pass to the secured party under Article 9, and property generally is transferred to him only in the sense that he is given, or otherwise acquires, a security interest in, or with respect to, collateral. A secured party only encumbers the property of the debtor. He may own his security interest in the collateral and thus have the power and right to transfer this interest, but a secured party is not, for Article 9 purposes, the owner of the base property itself in any usual or conventional sense of the term. Thus, it seems unlikely that a secured party qua secured party is also a debtor for any purpose under Article 9.

...
Assume, however, that, in terms of his relationship to a senior secured party, the holder of a subordinate security interest can, in some instances for this reason alone, be an owner of the collateral and thereby a "debtor" as Article 9 defines this term. The conclusion does not necessarily follow that section 9-306(2) supports a senior secured party's claim to the proceeds received by a junior secured party upon his disposition of collateral. Aside from the issue whether such an expansive definition of "debtor" is appropriate to use in this type of case or for this particular provision, there is another, less abstract problem with basing such a claim on the section that conditions the continuation of a security interest in proceeds on the debtor's receipt thereof. When a secured party disposes of collateral, he sells his rights and the debtor-obligor's rights with respect to the property. Thus, he loses any interest in the property and any basis for claiming ownership of it. Consequently, though he may have been a "debtor" before the sale, he is not a "debtor" at the critical time after the sale when he receives the proceeds thereof. The result is that the proceeds received by the junior secured party are not "received by the debtor." This dilemma cannot be resolved because he "owns" the proceeds which are "collateral" and thus he is a "debtor" with respect to this property. This is illogical because the proceeds will not be collateral unless a security interest continues in them, which is true only if the junior creditor is a "debtor" at the time the proceeds are "received by" him.

Even though a subordinate secured party qua secured party may not himself be a "debtor" at the time he receives the proceeds of his foreclosure sale or at any other time, it is nevertheless possible to argue that the proceeds are in a sense "received by the debtor" when this nondebtor secured party gets them. The nondebtor secured party must use and apply the proceeds according to the dictates of Part 5 of Article 9, and this benefits the debtor-obligor because his contractual obligations are thereby reduced. Thus, the secured party is acting in the debtor's stead by accomplishing

127. The definition of "debtor" in U.C.C. § 9-105(1)(d) is quoted at text accompanying note 114 supra.
128. "Debtor," as used in U.C.C. § 9-306(2), means the owner of the collateral only if the provision is one "dealing with the collateral." U.C.C. § 9-105(1)(d). Even if the section is such a provision, it also must be decided what, if any, significance attaches to the drafters' use of the word "the" in the phrase "received by the debtor." Is the word "the" a limitation in itself with respect to the proceeds in which a security interest continues? If the drafters meant received by any debtor, why did they not provide "received by a debtor"? Cf. id. § 9-306 comment 1 ("This section states a secured party's right to the proceeds received by a debtor on disposition of collateral . . . ").
129. See id. § 9-504(4).
130. "Collateral" means the property subject to a security interest . . . ." Id. § 9-105(1)(e).
131. See id.
132. See id. § 9-306(2).
133. See id. § 9-504(1)-(2).
what the debtor is legally required to do—pay his debts—whether or not the debtor has received the proceeds. Remember, too, that a secured party who disposes of collateral is selling his and the debtor’s rights with respect to the property; so, to an extent, the seller is acting for the debtor as a representative. Therefore, on the basis of this agency, receipt of the sale proceeds is equivalent to receipt by the debtor himself. A basic problem with this argument is that, in essence, “received for the debtor” is equated with “received by the debtor.” Nothing in Article 9 explicitly supports this equation. Moreover, an implied agency analysis is conceptually somewhat hard to accept because the interests of a debtor and any of his creditors are generally adverse.

There is a very direct, but questionable, way to get around the “received by the debtor” language in section 9-306(2) so that a senior secured party can found, on this provision, a claim to proceeds received by a junior secured party who sells the original collateral: Ignore it. Though he did not address the present problem of conflicting claims by secured parties to proceeds of a Part 5 disposition of collateral, Professor Ray Henson has argued that section 9-306(2) should generally be interpreted to recognize the continuing security interest in proceeds even though they are not “received by the debtor,” since they would not be received by the debtor in some sense if they were deposited directly in a special account, or if a receiver or trustee were appointed and such a person actually received the proceeds, or if the appointment of a receiver or trustee resulted in the secured party’s withholding amounts due pending a determination of entitlement or payment into court. In these unusual circumstances when the security interest in proceeds is needed most strongly by the secured party, it would be anomalous to cut off the security

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134. See id. § 9-504(4).
135. Even if on this basis the “received by the debtor” requirement of U.C.C. § 9-306(2) is satisfied, the only direct consequence is that the senior secured party has a continuing security interest in the proceeds of the junior secured party’s sale of the original collateral. This in itself does not necessarily establish that the senior creditor has a superior claim to the proceeds, see note 143 infra, or that the junior creditor must distribute the sale proceeds to persons other than those listed in U.C.C. § 9-504(1)-(2). See text accompanying notes 141-43 infra.
136. Another way around the troublesome language is to circumvent U.C.C. § 9-306(2) entirely. This could be possible when the security agreement between the senior secured party and the debtor-obligor expressly covers the property received by the junior creditor upon his sale of the original collateral. Arguably, § 9-306(2) is not controlling in such a case because the secured party does not claim an interest in the proceeds under this section, but rather, on the basis of § 9-203(1) and the parties’ explicit agreement. Part 5 applies even in this case, however, so that, regardless of the foundation for the senior creditor’s claim to the sale proceeds, their distribution would be governed by U.C.C. § 9-504(1)-(2), which does not provide for the satisfaction of senior interests.
interest because of inartistic drafting which is at best ambiguous.\textsuperscript{137}

Contrary to Henson's assertion, however, there is no ambiguity with respect to what the phrase "received by the debtor" modifies in the second clause of section 9-306(2);\textsuperscript{138} the drafting history of section 9-306 dispels any doubt that it modifies "proceeds" and not just "collections."\textsuperscript{139} Also, the phrase cannot today be easily ignored or its significance as law discounted on the supposition that its presence was due to the slip of the pen in the hand of one of the early artists who first drafted Article 9. The phrase has been perpetuated in all versions of the Code\textsuperscript{140} despite other changes in section 9-306, including the deletion in 1972 of the same language from the first clause of section 9-306(2).\textsuperscript{141}

Henson's principal point, however, is that, from a certain policy perspective, it makes little sense in some instances to deny a secured party an interest in proceeds simply because technically they were not received by the debtor. Yet, even if he is correct and the rule should be that in some cases security interests continue in proceeds no matter who receives them, there are still problems with relying on section 9-306(2) to support the specific assertion of a senior secured party that he has a superior claim to the proceeds of collateral sold by a junior secured party. They are problems that persist whether the "received by the debtor" condition is ignored or whether, by some interpretative magic, the condition is satisfied when the junior creditor receives the proceeds. One principal problem arises from a fundamental canon of statutory construction, generalia specialibus non derogant: general words do not derogate from the special. If section 9-306(2) is interpreted to give a senior secured party an interest in the proceeds of a junior secured party's sale of the original collateral, this provision will conflict with section 9-504(1), which negatively implies that a subordinate creditor who sells collateral is not responsible for satisfying a senior security interest and thus is not accountable to the superior secured party for the proceeds.\textsuperscript{142} The former section is more general than the latter, and, according to this accepted maxim of statutory construction, the more specific provision, section 9-504(1), will control.\textsuperscript{143}

\textsuperscript{137} R. Henson, Handbook on Secured Transactions Under the Uniform Commercial Code § 6-1, at 197-98 (2d ed. 1979).

\textsuperscript{138} Henson makes clear elsewhere that he considers U.C.C. § 9-306(2) ambiguous in terms of what "received by the debtor" modifies in the second clause of the provision. See note 102 supra.

\textsuperscript{139} See text accompanying notes 104-11 supra.

\textsuperscript{140} This becomes clear upon consideration of the various proposed and official texts beginning with the 1949 draft, which provided that an inventory financer's security interest continued "on the proceeds received by the borrower." U.C.C. § 7-322(2) (May 1949 Draft) (emphasis added).

\textsuperscript{141} See note 111 supra.

\textsuperscript{142} See text accompanying notes 87-98 supra.

\textsuperscript{143} See E. Crawford, The Construction of Statutes § 167 (1940). In particular cases there may be other problems with relying on § 9-306(2) to support the specific asser-
A further, persistent problem is the absence of any remedially important need for giving a senior secured party a claim to the proceeds of a subordinate secured party's sale of collateral. Senior creditors will surely disagree with this assertion, and they likely will argue that the effect of denying them a superior claim to the sale proceeds is to undermine the significance of their priority over the junior secured party. Yet, the only direct result of denying senior creditors a prior claim to the sale proceeds is the elimination of a remedy with respect to certain property. This denial does not leave them without collateral, nor does it preclude any remedy against the subordinate secured party. The significance of a senior secured party's priority is recognized in other ways and his interest is amply protected.

Upon the sale of the original collateral, the junior creditor's interest and any security interest or lien subordinate to his own are terminated along with the debtor's rights in the property.\textsuperscript{144} Any senior security interest survives, however.\textsuperscript{145} Consequently, its holder can follow the collateral
into the hands of the buyer, who must yield possession of the collateral\footnote{146} or, in some cases, pay damages if he is unwilling or unable to return the property.\footnote{147} Buyers at forced sales traditionally have been required to assume the risk that superior encumbrances and other interests will survive the disposition of the property to them. They can protect themselves in many cases by examining the public record,\footnote{148} and in every case they can ensure against such risks by requiring the seller to warrant expressly that no higher or greater rights to the property exist.\footnote{149}

If the collateral can be readily repossessed from the buyer who purchased it at the foreclosure sale, the senior secured party has not been harmed by the junior creditor’s disposition of the property. In other cases the senior creditor may recover damages for conversion of the original collateral from the buyer\footnote{150} or the subordinate secured party.\footnote{151} Also, the senior may trace and claim surplus proceeds of this property paid to and actually received by the debtor pursuant to section 9-504(2).\footnote{152} Therefore, the priority of a senior secured party’s interest can be fully vindicated without giving him a claim to the proceeds of a foreclosure sale conducted by a junior secured party. This may explain the negative implication of

\begin{quote}
\footnote{146} The junior secured party’s sale of the collateral does not terminate the senior security interest. \textit{See} note 145 \textit{supra}. Because it is unlikely that the buyer of the property will be entitled to priority as against the senior secured party under the priority rules of Article 9 (Is such a buyer one not in the ordinary course under \textsection{9-301(1)(c)?), the buyer will take the collateral subject to the continuing security interest. As between a secured party and a subordinate buyer of collateral, the former has the right to possession of the property on the debtor-obligor’s default. \textit{See} U.C.C. \textsection{9-201, 9-503}; Nickles, \textit{supra} note 3, at 512-17, 520-25; authorities cited in Nichles, \textit{supra} note 3, at 513 nn.10, 12; 515 n.18; 523 nn.52-53.

\footnote{147} If the buyer is unable or unwilling to return the collateral to the secured party, he may be liable for conversion of the property. \textit{See} generally Nickles, \textit{supra} note 3, at 520-36. For pre-Code authorities, see cases cited in note 189 \textit{infra}.

\footnote{148} Ordinarily, the senior secured party’s interest in the original collateral will have been perfected in the usual way, which is to file a financing statement. \textit{See} U.C.C. \textsection{9-302(1)}. Consequently, the buyer at the foreclosure sale conducted by a junior creditor can in most cases actually check the public records for a hint that a senior interest exists. If, for some reason, the senior secured party’s interest is not perfected, the buyer may be protected by U.C.C. \textsection{9-301(1)(c) because he is probably a buyer \textit{not in the ordinary course}. If this section applies, the buyer will take free of the senior security interest on the basis of this rule of priority “to the extent that he gives value and receives delivery of the collateral without knowledge of the security interest and before it is perfected.” \textit{Id}. The buyer also may be protected if the senior secured party has consented to the junior creditor’s disposition of the collateral so that the senior interest fails to continue in the property. \textit{See} \textit{id}. \textsection{9-306(2) (first clause); \textit{cf.} Anderson v. Case, 28 Wis. 505, 507-09 (1871) (pre-Code case).}

\footnote{149} There is no implied warranty to this effect in a Part 5 sale of collateral. \textit{See} note 189 \textit{infra}.

\footnote{150} \textit{See} generally Nickles, \textit{supra} note 3, at 520-36.

\footnote{151} \textit{See} text accompanying notes 156-203 \textit{infra}.

\footnote{152} \textit{See} text accompanying notes 99-103 \textit{supra}; \textit{see also} note 103 \textit{supra}.
\end{quote}
section 9-504(1), which is that a secured party who disposes of collateral is not accountable to a senior secured party for proceeds of the disposition. It also may suggest that, when enforcing priority in this type of case, the intended approach is for the senior secured party to pursue the original collateral in the buyer's hands. Meanwhile, the subordinate secured party can get on with the process of distributing the proceeds of his sale in accordance with the literal dictates of section 9-504(1).

This approach is neatly supported by a straightforward construction of sections 9-306(2) and 9-504 and is perfectly consistent with the plain meaning and logical implications of these and other provisions of Article 9. Yet, various policy concerns support giving a senior secured party a claim to the proceeds of a junior creditor's foreclosure sale. The effect of not recognizing such a claim is to require a second sale of the same property. Because he cannot recover the proceeds of the junior's disposition, a senior secured party also must dispose of the collateral after repossessing it from the buyer at the first sale. Arguably, at least, requiring this second sale is economically inefficient, if not wasteful.

Moreover, the approach of forcing a senior secured party to pursue the original collateral discourages buying at foreclosure sales. If security interests entitled to priority are not satisfied from sale proceeds, buyers at every foreclosure sale must be willing to gamble on whether any outstanding senior interests will be enforced against them. Perhaps, however, the law should not discourage buying at foreclosure sales, on the theory that the larger the pool of potential buyers, the higher will be the prices paid at all foreclosure sales. In any case involving multiple secured parties, the amount received from one sale may not be greater than what would have been received from two or more sales of the property to gamblers. Nevertheless, an enlarged pool of potential buyers at foreclosure sales—and larger pots of proceeds—surely will benefit debtors and secured parties generally and as a class, especially in the more typical case in which there is only one secured party who claims the pot.

These concerns may suggest that an unexpressed principle or policy underlies Article 9 which supports giving a senior secured party a prior right to the proceeds of a junior creditor's disposition of collateral. If so, the courts are licensed to go beyond the statute's literal dictates and construe its provisions liberally. Specifically, the courts may implement "a statutory policy with liberal and useful remedies not provided in the statutory text." Thus, the plain meaning and logical implications of

153. See text accompanying notes 87-98 supra.
154. See U.C.C. § 1-102(1). Exercising this authority is especially likely with respect to issues and problems not envisaged by the Code drafters. Possibly, the drafters did not anticipate sales of collateral by junior parties and thus did not have the resulting problems in mind when they wrote the relevant provisions. See generally Roemer & Zeller, Inc. v. Ace Transmission Center, Inc., 114 Misc. 2d 415, 451 N.Y.S.2d 601 (Sup. Ct. 1982).
155. U.C.C. § 1-102 comment 1.
sections such as 9-306 and 9-504 may be preempted by a pervasive spirit of priority that supports giving a senior secured party a claim to the proceeds of a junior creditor's sale of collateral. In determining whether this preemption is proper, the ultimate issue may be this: Who is the more legitimate prime target when a secured party seeks to enforce the priority of his interest in collateral lawfully disposed of by a subordinate secured party? Is it the junior creditor himself? Or is it the person who bought from this creditor at a forced sale and who is a target because his rights as a buyer also are subordinate to the senior secured party's interest?

In judging the soundness of the approach that requires a senior secured party to pursue the original collateral, an important consideration is that the approach has a fail-safe feature supplied by the common law. The junior creditor, in essence, guarantees that the senior secured party's priority over him will be vindicated because, if the senior cannot easily repossess the original collateral from the buyer, the junior is answerable for conversion of this property.

IV. SUING THE SUBORDINATE PARTY FOR CONVERSION

Because the priority of a senior secured party's interest gives him, on the debtor's default, a superior right to possession of the collateral for purposes of foreclosure, he may take the property from a junior secured party who has repossessed it.156 Recovering the collateral is not always the only remedy that the senior creditor can pursue on the basis of this right, however. An alternative remedy in some cases is an action against the subordinate secured party for conversion of the collateral. According to the Restatement (Second) of Torts,

[c]onversion is an intentional exercise of dominion or control over a chattel which so seriously interferes with the right of another to control it that the actor may justly be required to pay the other the full value of the chattel.157

A conversion action is intended to vindicate the plaintiff's right to possession of the property as against the defendant. The plaintiff need not establish that he owns the property in order to recover; he need establish only that his claim to the property is superior to the defendant's claim.158 When a default occurs under the senior creditor's security agreement, the senior has the right to control the property: the right to take possession, dispose of the property, and apply the proceeds in satisfaction of the senior's interest.159 A junior secured party dealing with the property after this default

156. See text accompanying notes 12-47 supra.
158. See id. § 225; 4 id. § 895 comments a-e (1979); 1 F. HARPER & F. JAMES, THE LAW OF TORTS § 2.8 (1956); W. PROSSER, HANDBOOK OF THE LAW OF TORTS § 15, at 93-97 (1971); Warren, Qualifying as Plaintiff in an Action for a Conversion, 49 HARV. L. REV. 1084, 1086-1100 (1936).
159. See text accompanying notes 12-51 supra; see also, e.g., Bank of Lexington v. Jack
thus may be liable for conversion if his conduct *seriously interferes* with the senior creditor's rights with respect to the collateral. Section 9-311 does not in itself provide a general defense for the junior creditor.160 This provision permits a debtor to subject the collateral to more than one encumbrance. Yet, it does not authorize any encumbrancer or other transferee to deal with the property in a way that adversely affects the superior rights of another whose interest in the goods has priority under Article 9.161

The most difficult problem in virtually every conversion case is judging whether the defendant's conduct was so offensive that justice requires him, in effect, to buy the property or, if the plaintiff is a secured party, to satisfy the plaintiff's interest in the collateral.162 According to those who restated the law of torts the second time, there are no absolute rules:

There is probably no type of conduct with respect to a chattel which is always and under all circumstances sufficiently impor-

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160. This section provides:

The debtor's rights in collateral may be voluntarily or involuntarily transferred (by way of sale, *creation of a security interest*, attachment, levy, garnishment or other judicial process) notwithstanding a provision in the security agreement prohibiting any transfer or making the transfer constitute a default.

**U.C.C. § 9-311 (emphasis added).**

161. The sole purpose of § 9-311 is simply "[t]o make clear that in all security transactions under this Article, the debtor has an interest . . . which he can dispose of and which his creditors can reach." *Id.* § 9-311 comment 1. The courts have interpreted the provision to mean only that

the interest of the debtor in the collateral may be transferred by him even though

the security agreement purports to prohibit such transfer and makes the transfer a default. However, the fact that the collateral may be transferred voluntarily or involuntarily does not destroy or adversely affect a prior perfected security interest, without the consent of the secured party.

**Sturdevant v. First Sec. Bank, 37 Mont. Adv. Sh. 259, 262-63, 606 P.2d 525, 528 (1980)** (citations omitted). The section may legitimize certain conduct of the debtor or third parties in some cases. For examples, see **Citizens Bank v. Perrin & Sons, Inc., 253 Ark. 639, 640-41, 498 S.W.2d 14, 15 (1972)**, and text accompanying notes 175-77 *infra*. Nevertheless, the courts generally have not construed the section as giving blanket immunity to subordinate transferees or creditors whose dealings with the collateral have (at least in the court's view) a significant adverse impact on the senior secured party's rights with respect to the property. **See generally First Nat'l Bank v. Stamper, 93 N.J. Super. 150, 225 A.2d 162 (Law Div. 1966); Production Credit Ass'n v. Nowatzki, 90 Wis. 2d 344, 280 N.W.2d 118 (1979).** Cases such as **Citizens Bank, supra,** do not contradict this proposition. In **Citizens Bank** the Arkansas Supreme Court held that the sale of collateral by a subordinate claimant of the property did not in itself make the creditor liable to the secured party for conversion. Section 9-311 was relied on, as were the following facts: (1) the property's continued accessibility in the buyer's hands, and (2) the lack of any adverse effect on the secured party's right to enforce its security interest in the property against the buyer. **253 Ark. at 640-41, 498 S.W.2d at 15-16.**

162. The usual measure of compensatory damages in a conversion action is the full value of the property at the time the tort was committed. An exceptional measure is used, however, when the plaintiff is not the sole owner of the goods but, rather, holds only a limited
tant to amount to a conversion, since the interference with the
right of the plaintiff may in each case be either trivial or serious.
Not only the conduct of the defendant, but also its consequences,
are to be taken into account.\textsuperscript{163}

This means that the nature of the defendant's conduct, in itself, is never
conclusive on the issue of liability; instead, under the approach advocated
by the Restatement (Second) of Torts, the effect of his conduct on the plain-
tiff's rights in the particular case is ordinarily the controlling
consideration.\textsuperscript{164} What the defendant has done per se is less important than
the consequences of what he has done. Few cases, however, seem to sup-
port this approach when deciding conversion liability in secured transac-
tion cases. Especially when secured parties have sued junior claimants
of collateral for dealing with the property, the courts have rarely investigated
the actual consequences to the plaintiff in the particular case and taken
these consequences into account before imposing conversion liability on
the defendant.\textsuperscript{165} Rather, the courts traditionally have assumed that cer-
tain conduct always amounts to conversion whether or not the plaintiff
was in fact harmed by the defendant's acts.

The original Restatement of Torts reflects this tendency. It categorizes
and discusses various ways of committing conversion\textsuperscript{166} and nowhere explic-
itly suggests that, as a general principle, the absence of adverse conse-
quences or other considerations may mitigate against a finding of conver-
sion liability. Like the original, the Restatement (Second) details various ways
of committing conversion.\textsuperscript{167} Unlike the original Restatement, however, the
more recent version contains an introductory section in the chapter on
conversion\textsuperscript{168} that provides certain overriding principles which govern every
case in which conversion is alleged, notwithstanding the nature of the
defendant's conduct. This section, section 222A, first defines conversion
so as to limit liability to interferences with the plaintiff's rights over the

\begin{itemize}
  \item interest in them. In such a case he generally recovers only the value of his interest. \textit{See}
  4 Restatement (Second) of Torts § 927 (1979). This exception to the normal measure
  of damages is well established, having been recognized very early by American courts.
  \textit{See} Warren, \textit{Qualifying as Plaintiff in an Action for a Conversion}, 49 Harv. L. Rev. 1084,
  1108-09 (1936). Therefore, if the plaintiff is an Article 9 secured party, he recovers in
  the ordinary case the value of his security interest, i.e., the amount secured by the col-
  lateral that has been converted, not to exceed the full value of the property. \textit{See} Nickles,
  supra note 3, at 536-39.
  \item 1 Restatement (Second) of Torts § 222A comment d (1965).
  \item That the effect of the defendant's conduct is often the determining factor in con-
  version cases was a conclusion reached by Prosser in an article that was the source of
  some commentary and illustrations that appear in the Restatement (Second)'s chapter on
  conversion. \textit{See} Prosser, \textit{The Nature of Conversion}, 42 Cornell L.Q. 168, 171-73 (1957);
  \textit{see also} 1 Restatement (Second) of Torts § 222A & comments (1965).
  \item \textit{See}, \textit{e.g.}, cases cited in notes 175, 182 infra; \textit{see also} cases cited in Nickles, supra
  note 3, at 523 nn.52-53, 527 n.62, 529 n.70, 533 n.93.
  \item See 1 Restatement of Torts §§ 223-242 (1934).
  \item See 1 Restatement (Second) of Torts §§ 223, 226-237, 241A-242 (1965).
  \item Id. § 222A.
\end{itemize}
property which are so serious that justice requires the defendant to buy
the goods.\textsuperscript{169} Second, section 222A lists some factors by which the
seriousness of the defendant’s conduct can be measured.\textsuperscript{170} It is in con-
nection with this listing that the drafters make clear the importance of
always considering the consequences of the defendant’s conduct.\textsuperscript{171} They
undoubtedly agreed with Dean Prosser’s conclusion that, under the law
of conversion as it eventually developed in this country, the determining
factor in conversion cases is often not the character of the defendant’s
act, but “its effect.”\textsuperscript{172}

The \textit{Restatement (Second)} approach to deciding conversion liability,
emphasizing the consequences to the plaintiff, should be followed in cases
in which the plaintiff is a secured creditor. Although scant authority sup-
ports using this approach in such cases, common sense and fairness cer-
tainly do. Because this approach focuses on the seriousness of the defend-
ant’s interference and on the consequences to the plaintiff, liability will
result in the ordinary case only if the plaintiff’s right to control the col-
lateral was materially affected as a result of the defendant’s conduct. To
impose conversion liability in other cases seems harsh and unjustified,
considering the usual measure of damages in conversion actions.\textsuperscript{173} Prosser
believed the courts had effectively confined conversion to major inter-
ferences because of a “recognition of the fact that the significance of con-
version lies in the measure of damages . . . and that the tort is therefore
. . . limited to those wrongs which justify imposing it.”\textsuperscript{174} It hardly seems
just to award substantial damages to a plaintiff who in fact has not suf-

\begin{itemize}
  \item[169.] Id. § 222A(1), reproduced at text accompanying note 157 \textit{supra}.
  \item[170.] Subsection (2) provides:
    In determining the seriousness of the interference and the justice of requiring
    the actor to pay the full value, the following factors are important:
    \begin{itemize}
      \item[a] the extent and duration of the actor’s exercise of dominion or control;
      \item[b] the actor’s intent to assert a right in fact inconsistent with the other’s
              right of control;
      \item[c] the actor’s good faith;
      \item[d] the extent and duration of the resulting interference with the other’s
              right of control;
      \item[e] the harm done to the chattel;
      \item[f] the inconvenience and expense caused to the other.
    \end{itemize}
  \end{itemize}

\begin{itemize}
  \item[171.] See id. § 222A comment d.
  \item[172.] Prosser, \textit{The Nature of Conversion}, 42 \textit{Cornell L.Q.} 168, 173 (1957). \textit{See also 1 \textit{Restatement (Second) of Torts} § 222A comment d (1965) (“Not only the conduct of
    the defendant, but also its consequences, are to be taken into account.”}).
  \item[173.] The usual measure of damages is “the value of the subject matter or of [the plain-
    tiff’s] interest in it at the time and place of the conversion.” \textit{4 \textit{Restatement (Second) of Torts} § 927(1)(a) (1979)}. Regarding the measure of damages when the plaintiff is an
    Article 9 secured party, see note 162 \textit{supra}.
    of the \textit{Restatement (Second)} believed this, too. \textit{See 1 \textit{Restatement (Second) of Torts} § 222A comment c (1965).}
\end{itemize}
ferred to any material extent as a consequence of the defendant’s conduct.

Under the Restatement (Second) approach, therefore, conversion liability should not be imposed on a junior secured party simply because he repossessed collateral from the debtor who, at the time, was also in default under a security agreement with the plaintiff, a senior creditor. The subordinate creditor may be willing to immediately yield possession of the property intact should the senior secured party ask for it. In this case the impact of the repossession on the senior creditor’s rights is probably inconsequential; if so, the subordinate creditor is not guilty of conversion for this conduct alone, because the senior secured party has not in fact been injured thereby.175

This conclusion is unaffected by the general rule that
[0]ne who receives possession of a chattel from another with the intent to acquire for himself or for a third person a proprietary interest in the chattel which the other has not the power to transfer is subject to liability for conversion to a third person then entitled to the immediate possession of the chattel.176
This rule does not govern the situation in which a junior secured party has repossessed collateral to which a senior secured party has an immediate right of possession. The junior creditor does not take possession for the purpose of acquiring an interest in the goods; he takes possession in order to enforce a preexisting interest that the debtor undoubtedly had the power to create, whether or not the property was already encumbered by the senior security interest.177 Even if the rule can be applied to this type of situation, it has no application in a case in which “receipt of the chattel . . . is so temporary, trivial or unimportant as not to amount to a conver-


176. 1 RESTATEMENT (SECOND) OF TORTS § 229 (1965).

177. See U.C.C. § 9-311, reproduced at note 160 supra.
This situation characterizes the effect of a junior secured party’s repossession of collateral if he is willing to immediately return it upon demand by the senior creditor. The senior creditor thus suffers no serious injury to his rights or interest as a result of the subordinate creditor’s conduct.

The result may be different, however, and liability for conversion may ensue if, for example, the junior creditor refuses the senior secured party’s demand for the collateral’s return. “An express, unqualified, or improperly qualified refusal to surrender the chattel, which puts the plaintiff to the necessity of a lawsuit to recover his property, is clearly a conversion.” Liability even in this clear case, however, can be founded ultimately on the consequences to the plaintiff and not pinned solely on the nature of the defendant’s conduct. In the face of such a refusal, the senior creditor, in order to take possession of the collateral, would be required to proceed by action in court to replevy the property. This would force the senior to delay foreclosure, risk depreciation of the collateral, sustain unwarranted and added inconvenience and expense, and, in the final accounting, reduce the value of the security interest in the property. These consequences will likely result when a junior secured party steadfastly refuses a senior creditor’s demand for the return of the collateral. Therefore, one can safely generalize that such conduct will usually and justifiably subject the defendant to conversion liability.

Ordinarily, however, the consequences of the defendant’s conduct depend on the facts of each particular case. Thus, when a senior secured party sues a junior secured party for conversion of collateral, the court should not decide liability on the basis of the type of conduct involved. Rather, in each case the court should impose liability only if the conse-

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178. 1 RESTATEMENT (SECOND) OF TORTS § 229 comment b (1965) (emphasis added).
179. Id. § 237 comment g.
180. In addition, an express refusal to return the property may be the manifestation of a specific intention to interfere deliberately with the plaintiff’s superior right to control the collateral and, also, a manifestation of the defendant’s lack of good faith. These factors are important in themselves when judging the seriousness of the defendant’s conduct. See id. § 222A(2), reproduced at note 170 supra.
quences to the plaintiff justify it. Ample justification exists if recovery of the collateral has been made impossible or significantly more time consuming, expensive, or difficult, so that the effect is to diminish materially the value of the collateral to the senior secured party.

Unfortunately, many courts seem not to take an approach that requires considering anew in each conversion action the consequences of the defendant’s conduct. This is especially true when a junior secured creditor has not only repossessed the collateral from the debtor but also has disposed of it. The apparently widespread belief is that a disposition of collateral by a third-party claimant amounts in itself to a conversion. Yet, this belief lacks a sound theoretical foundation. It is true that, as a general rule, “one who makes an unauthorized delivery of a chattel to a person not entitled to its immediate possession is subject to liability for conversion.”


Appropriation of the sale proceeds by the junior secured creditor was sometimes separately mentioned by the courts, suggesting that this is a necessary, additional ingredient of the tort. See, e.g., McFadden v. Hopkins, 81 Ind. 459, 461 (1882); Eade v. First Nat’l Bank, 117 Or. 47, 52, 242 P. 833, 834 (1926); First Nat’l Bank v. Baldridge, 37 S.D. 606, 608, 159 N.W. 130, 131 (1916); Godair v. Tillar, 19 Tex. Civ. App. 541, 545, 47 S.W. 553, 556 (1898); Lowe v. Wing, 56 Wis. 35, 59, 19 S.W. 892, 893 (1882). For an Article 9 case, see Consolidated Equip. Sales, Inc. v. First State Bank & Trust Co., 627 P.2d 432, 438 (Okla. 1981). See also text accompanying notes 197-203 infra.

Also, in cases where the junior buyer of collateral has disposed of the property, the courts have regularly imposed conversion liability without considering the consequences to the senior party. See Nickles, supra note 3, at 523 n.53, 533 n.93.

Similarly, persons asserting subordinate judicial and statutory liens against collateral have routinely been found liable when they enforced their encumbrances against collateral by selling the property or having it sold. See, e.g., Bradford v. Roberts, 46 Colo. 330, 333, 104 P. 391, 391 (1909); Cooper v. Citizens Bank, 129 Ga. App. 261, 263, 199 S.E.2d 369, 371-72 (1973); Lawson v. Robertson, 51 Idaho 551, 554-55, 7 P.2d 946, 947 (1932); Marco Fin. Co. v. Solbert Indus., 534 S.W.2d 469, 472-74 (Mo. App. 1975); Black, Sivalls & Bryson v. Loobbourrow, 176 Okla. 506, 510-11, 57 P.2d 836, 840-41 (1935); Terry v. Spearman, 259 S.W. 563, 565-66 (Tex. Comm’n App. 1924);
It is also true that, when a junior secured party disposes of collateral he has repossessed from a debtor who has also defaulted under a security agreement with a senior secured party, this senior creditor, and not the junior creditor's transferee, is entitled to possession of the collateral. Nevertheless, disposing of property to someone not entitled to its immediate possession does not result in strict liability. The general rule of liability for misdelivery of goods is subject to the overriding principle

under which there is a conversion only where the actor exercises a dominion or control over the chattel which so seriously interferes with the right of another to control it that the actor may justly be required to pay the other the full value of the chattel.

An unauthorized delivery "may be so minor an interference that it does not amount to a conversion." As in all cases in which conversion is

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183. 1 RESTATEMENT (SECOND) OF TORTS § 235(1) (1965).

184. The junior secured party's sale of the collateral does not terminate the senior secured party's security interest. See text accompanying notes 144-46 supra; notes 145-46 supra. Because it is unlikely that the buyer of the property will be entitled to priority as against the senior secured party under the rules of Article 9, the buyer will take the collateral subject to the continuing security interest. As between a secured party and a subordinate buyer of the collateral, the former has the right to possession of the property on the debtor's default. See U.C.C. § 9-503; Nickles, supra note 3, at 512-17; authorities cited in Nickles, supra note 3, at 513 nn.10, 12; 515 n.18; 523 n.52.

185. 1 RESTATEMENT (SECOND) OF TORTS § 235 comment c (1965).

186. Id.
alleged, "'[n]ot only the conduct of the defendant, but also its consequences, are to be taken into account.'"\textsuperscript{187}

When a secured party repossesses collateral, he must dispose of it pursuant to Part 5 of Article 9; typically, the property will be sold at a public or private sale. Such a sale, however, does not terminate all security interests in the property. Only the interest of the secured party conducting the sale and subordinate interests are terminated.\textsuperscript{188} Consequently, when a junior secured party sells the collateral at a foreclosure sale, the junior does not thereby terminate a senior creditor’s security interest. The senior’s interest continues in the property, and the collateral can be repossessed from the buyer.\textsuperscript{189} If the collateral remains readily accessible and undamaged in the hands of a cooperative buyer so that the senior secured party can easily repossess the collateral intact, the junior creditor should not be liable for conversion; the junior creditor’s interference with the senior creditor’s rights is minor and unactionable when measured in terms of the consequences of the junior’s conduct.\textsuperscript{190}

\textsuperscript{187} Id. § 222A comment d.
\textsuperscript{188} See U.C.C. § 9-504(4).
\textsuperscript{189} See authorities cited in notes 145-46 supra. If the buyer is unable or unwilling to return the collateral to the secured party, the buyer himself may be liable for conversion. See Nickles, supra note 3, at 520-36. For pre-Code authority, see Hopkins v. Anderson, 218 Cal. 62, 67, 21 P.2d 560, 562 (1933); Scoggins v. General Fin. & Thrift Corp., 80 Ga. App. 847, 850, 57 S.E.2d 686, 688 (1950); Lorain Steel Co. v. Norfolk & B. St. Ry., 187 Mass. 500, 501, 73 N.E. 646, 646 (1905).

Does a buyer who must return collateral to the senior creditor or pay damages for converting it have recourse against the junior secured party? He certainly has none based on breach of an implied warranty of title under Article 2. When goods are sold, the seller ordinarily warrants by operation of the law that “the goods shall be delivered free from any security interest . . . of which the buyer at the time of contracting has no knowledge.” U.C.C. § 2-312(1)(b). It is not clear that this provision applies to a foreclosure sale of collateral by a secured party; even if it does, however, this warranty is “excluded . . . by circumstances which give the buyer reason to know that the person selling does not claim title in himself or that he is purporting to sell only such right or title as he or a third person may have.” Id. § 2-312(2). The circumstances of a Part 5 disposition of collateral under Article 9 have the effect of excluding any implied warranty of title by the secured party conducting the sale. See id. § 2-312 comment 5; cf. Bogstad v. Anderson, 143 Minn. 336, 338-39, 173 N.W. 674, 675 (1919) (pre-Code case indicating no warranty of title implied upon sale of collateral when a chattel mortgagee forecloses).

190. Several courts have indicated or suggested that a mere sale of collateral by a third-party claimant of the property does not in itself render this person liable for conversion to a senior secured creditor. See, e.g., Leasing Serv. Corp. v. American Nat’l Bank & Trust Co., 19 U.C.C. Rep. Serv. 252, 265-66 (D.N.J. 1976); Citizens Bank v. Perrin & Sons, Inc., 253 Ark. 639, 640-41, 488 S.W.2d 14, 15 (1972); Harris v. Grant, 96 Ga. 211, 214, 23 S.E. 390, 391-92 (1895), further opinion sub nom. DeVaughn v. Harris, 103 Ga. 102, 29 S.E. 613 (1897); Nichols v. Sheldon Bank, 98 Iowa 603, 605-06, 67 N.W. 582, 583 (1896); Public Fire Ins. Co. v. Detroit Garages, Inc., 264 Mich. 500, 502, 250 N.W. 290, 290 (1933); Seaboard Consumer Discount Co. v. Landau’s, Inc., 167 Pa. Super. 180, 183-84, 74 A.2d 737, 738 (1950); Midland Nat’l Bank & Trust Co. v. Peterson, 229 Wis. 19, 20-21, 281 N.W. 683, 683-84 (1938). In some of these cases this conclusion is based on the assumption that the secured creditor can pursue and replevy the
If, however, the consequences of the disposition are more substantial and make the senior party's recovery of the property from the buyer impossible or materially more difficult or costly, the result arguably may be different. For example, a junior claimant should be liable for conversion if, as a direct consequence of his conduct, the property is put literally or practically beyond the senior creditor's reach.\(^\text{191}\) Also, the junior claimant should be liable if he sells the collateral to a buyer who then places it beyond the senior secured party's reach. The buyer from the subordinate secured party may have removed the collateral a great distance, or he may have destroyed it or commingled it with other property. Alternatively, this buyer may hold the collateral intact at a nearby location yet steadfastly refuse the senior creditor's demand for its return. In all these cases the senior secured party suffers serious, adverse consequences, and the junior creditor should be accountable in conversion.\(^\text{192}\)

Collateral from the ultimate transferee. In other cases, however, courts have expressly indicated that the possibility of the senior secured creditor doing this does not shield the third-party claimant from conversion liability. See, e.g., Bingham v. Harby, 91 S.C. 121, 124, 74 S.E. 369, 371 (1912); Universal Credit Co. v. Gasow-Howard Motor Co., 73 S.W.2d 909, 910-11 (Tex. Civ. App. 1934).


\(^{192}\) A subordinate secured party may not be completely defenseless, however, even if for some reason he is guilty of converting the original collateral or if, on any basis, a prima facie case is made against him for liability with respect to this property or its proceeds. This creditor may rely on the equitable doctrine of marshalling of assets and argue that, in any case, it shields him from liability to the extent that the senior secured party has other security. According to this doctrine,

> [w]here there are two creditors of the same debtor, one creditor having a right to resort to two funds of the debtor for payment of his debt, and the other a right to resort to one fund only, the court will so "marshal" or arrange the funds that both creditors are paid as far as possible. "A person having resort to two funds shall not by his choice disappoint another, having one only." Though the doctrine has several applications, marshalling as between mortgagees is perhaps the most usual.


The marshalling doctrine is not fully and completely displaced under Article 9. The drafters recognized that marshalling may be appropriate when the conflicting interests are those of a secured party and a lien creditor. See U.C.C. § 9-311 comment 3. It remains unclear, however, whether and how it applies in disputes between secured parties. Compare S. Lotman & Son, Inc. v. Southeastern Fin. Corp., 288 Ala. 547, 549, 263 So. 2d 499, 500 (1972) (marshalling not required), with Community Bank v. Jones, 278 Or. 647, 679-80, 566 P.2d 470, 488-89 (1977) (marshalling required).


Creditors of debtors have been more successful in using the marshalling doctrine against Article 9 secured parties. See In re Jack Green's Fashions, 597 F.2d 130, 133 (8th Cir.
The junior may argue, however, that consequences such as these result directly from the conduct of the subsequent transferee or from some other cause not attributable to him. For this reason, the junior secured party may assert that he is not personally responsible for the consequences and thus is not answerable to the senior. There are several reasons why this argument should fail. First, a junior claimant who resells collateral causes, or is responsible for, whatever consequences ensue when the property is in the hands of a later transferee, in the sense that, "but for" the subordinate creditor's resale, the transferee would never have acquired the property. Second, the reselling creditor might be expected to have foreseen the actions of a subsequent transferee, and, for this reason, there may be a "proximate causation" link between the creditor's act of reselling the property and its fate in the hands of the buyer. Third, there is some authority that, while a junior creditor's acts may not in themselves amount to conversion, the junior nevertheless can be liable as a converter when what he has done is coupled with serious adverse consequences over which he had no control and that do not result directly from his conduct.\(^\text{193}\)

Deciding a subordinate secured party's liability for conversion based on the occurrence or nonoccurrence of consequences beyond his control

193. Consider the following sets of illustrations set forth by Dean Prosser:

**TAKING THE CHATTEL**

1. A, leaving a restaurant, by mistake takes B's hat from the rack, believing it to be his own. When he reaches the sidewalk he puts on the hat, discovers his mistake, and immediately returns it to the rack. This is not a conversion.

3. The same facts as in Illustration 1, except that as A reaches the sidewalk and puts on the hat a sudden gust of wind blows it from his head, and it goes down an open manhole and is lost. This is a conversion.

**REMOVING THE CHATTEL**

15. A takes possession of a house, and finds B's furniture in it. He requests B to remove the furniture, and B does not do so. A then removes the furniture to a storage warehouse, stores it in the name of B, and notifies B that he may come and get it. This is not a conversion.

18. The same facts as in Illustration 15, except that while the furniture is in
and for which he is not personally and directly responsible is equivalent to imposing on him the risk of the goods’ loss. This approach represents a compromise between two extreme positions. If the consequences that ensue when the collateral is in the hands of a later transferee are not considered, the typical junior creditor will almost always escape liability for conversion unless the resale in itself amounts to a conversion of the property. Labeling a resale itself a conversion, however, means that the subordinate secured party is absolutely liable solely on the basis of the character of his acts. This is inconsistent with the approach of the Restatement (Second), and, in addition, it seems unfair to impose liability on the defendant even though the plaintiff could possibly have recovered the property without suffering any material loss or injury. Yet, from the senior party’s viewpoint, complete immunity for the junior creditor seems unfair, too. After all, in Professor Warren’s words, the defendant who resells property thereby sends it “afloat on a sea of persons, strangers to [the plaintiff who] must go and chase it.” This is effective and memorable prose; nevertheless, the plaintiff in a particular case may have a short and successful chase and find that no one has acted to “sink” the property or otherwise harm it or the plaintiff’s interest in it. The compromise approach suggested here recognizes this possibility, and under this approach the junior creditor is neither absolutely liable nor completely immune from liability. The junior’s liability in each case depends on the severity of the consequences to the senior, albeit consequences not directly caused by the junior, who justly should not be allowed to recover the value of his interest unless the value of the collateral to him has in fact been significantly lessened.

the warehouse, and before B can remove it, it is destroyed by fire. This is a conversion.

\[\ldots\]\n
**WITHHOLDING THE CHATTEL**

37. A stores his car in B’s locked garage. A comes to get the car and demands it. B intentionally delays half an hour in giving A the key to the garage. This is not a conversion.

\[\ldots\]\n
39. The same facts as in Illustration 37, except that during the delay of half an hour a fire breaks out in the garage, and the car is destroyed before it can be removed. This is a conversion.

Prosser, *The Nature of Conversion*, 42 CORNELL L.Q. 168, 174-75, 177-78, 180-81 (1957). These same examples appear in 1 RESTATEMENT (SECOND) OF TORTS § 222A illustrations (1965). These examples may explain what Prosser meant when he wrote that the consequences to the plaintiff “relate back to the [defendant’s] act and affect it, so that they may transform a mere trespass into a conversion.” Prosser, *The Nature of Conversion*, 42 CORNELL L.Q. 168, 184 (1957) (emphasis added). In terms of analysis, it should make no difference that in these illustrations the fortuity involved an act of nature and not the conduct of a third person; this is especially true because the latter is more easily foreseen than the former.

In some cases adverse consequences caused directly by the transferee, also may render the transferee liable for conversion. The transferee’s liability should not absorb the subordinate secured party of liability, however. Although a succession of conversions raises interesting questions regarding the plaintiff’s measure of damages, a subsequent conversion of the same property by someone else does not erase or cure the wrong that another converter has committed.

A junior secured creditor’s liability for conversion of collateral occasionally has been founded on the junior’s sale of the property together with his failure to remit the sale proceeds to the senior secured party. Yet, the junior secured creditor’s use of the sale proceeds for his own purposes should not be viewed as a pivotal act, nor should it be considered together with other conduct, when deciding whether he has converted the original collateral. First, as against the junior secured party, the senior creditor may not have a superior claim to the sale proceeds. In this case the subordinate creditor should be allowed to apply them in any way he sees fit, without accumulating liability with respect to the original collateral. Second, if the senior secured party has a superior claim to the sale proceeds so that these proceeds may be recovered from the junior, this is a reason which by itself supports the conclusion that the junior secured party cannot be liable under the common law for conversion of the original

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197. Both of these acts—not just one of them—seem to be the bases of liability in a few Article 9 cases. See, e.g., United States v. Minster Farmers Coop. Exch., Inc., 430 F. Supp. 566, 571 (N.D. Ohio 1977); Consolidated Equip. Sales, Inc. v. First State Bank & Trust Co., 627 P.2d 432, 438 (Okla. 1981). The same is true in pre-Code cases in which the junior creditor either sold the collateral himself or was somehow connected to the debtor’s disposition of it. See, e.g., Bank of Odenville v. Union State Bank, 212 Ala. 52, 52, 101 So. 666, 666 (1924); First Nat’l Bank v. American State Bank, 73 Colo. 254, 256, 215 P. 473, 475 (1923); Morrison v. Eley, 190 Ill. App. 374, 390 (1914); Enterprise Foundry & Mach. Works v. Miners’ Elk horn Coal Co., 241 Ky. 779, 790, 45 S.W.2d 470, 475 (1931); Bank of Kennett v. Clayton, 245 S.W.2d 678, 684 (Mo. App. 1951); Eade v. First Nat’l Bank, 117 Or. 47, 52, 242 P. 833, 834 (1926); Highland Park State Bank v. Continental Nat’l Bank, 300 S.W.2d 304, 308 (Tex. Civ. App. 1957); see also pre-Code authorities cited in note 182 supra.
198. See text accompanying notes 86-155 supra.
199. In every case, however, a secured party who disposes of collateral must apply the proceeds, after satisfying his own interest, in accordance with the literal dictates of U.C.C. § 9-504(1)-(2). Yet, nothing in Part 5 requires a secured party who has disposed of collateral to satisfy senior interests. See text accompanying notes 87-98, 141-43 supra.
collateral. The senior's remedy should be limited to recovering the sale proceeds.

Presumably, if a secured party properly forecloses, the sale will produce the most proceeds that reasonably can be expected within a reasonable time after the collateral's repossession. Except in an unusual case, it is hard to imagine that the amount of proceeds will vary significantly depending on the fortuity of which secured party conducts the disposition. Each secured party is bound to satisfy the Part 5 requirements of Article 9. Moreover, because all of a debtor's creditors are often located within the proximate vicinity of the debtor's residence or place of business, the market for disposing of the collateral generally will be the same no matter which secured party controls foreclosure. Therefore, if the senior creditor has a prior claim to the proceeds of the sale that allows him to recover the sale proceeds from the junior secured party, the senior, for this very reason, has not suffered adverse consequences as a result of the junior's repossession and disposition of the collateral. Thus, in this case justice surely does not require the imposition of conversion liability on the subordinate secured party with respect to the original collateral. The senior secured

200. This reasoning fails, of course, if the junior secured party conducts an improper sale of the collateral, i.e., one that does not comply with Part 5 of Article 9. Noncompliance does not necessarily mean, however, that the subordinate creditor is liable under the common law to the senior secured party for conversion of the property. Liability for improperly disposing of collateral is expressly provided for in Article 9 itself:

If the disposition has occurred the debtor or any person entitled to notification or whose security interest has been made known to the secured party prior to the disposition has a right to recover from the secured party any loss caused by a failure to comply with the provisions of this Part.

U.C.C. § 9-507(1). Yet, other secured parties, including those with senior interests, have no right to notice of disposition when the collateral is consumer goods. See id. § 9-504(3). With nonconsumer goods, however, other secured parties must be notified only in the unlikely event that they have given timely and written notice of their interests to the creditor conducting the foreclosure. See id.

As a practical matter, therefore, a senior secured party ordinarily will be entitled to recover under U.C.C. § 9-507(1) for an improper disposition only if, prior to the sale, the senior creditor's interest was "made known" to the subordinate secured party who sold the property. See id. § 9-507(1). Constructive notice or reason to know will not be sufficient to trigger the subordinate secured party's accountability to the senior creditor. See notes 67-68 supra. It is unlikely that § 9-507(1)'s conditions on liability of one Article 9 secured party to another for wrongful foreclosure could be avoided by the plaintiff predicing his cause of action on common-law conversion and not the statute. The court could easily conclude that § 9-507(1) does not provide an alternative remedy, but rather codifies or provides a substitute for conversion liability and, at the same time, limits the circumstances under which liability for wrongful foreclosure can be imposed. Thus, by providing conditionally for the recovery of damages by one secured party from another who improperly disposes of collateral, § 9-507(1) effectively displaces any common-law action. Some cases may possibly be read as suggesting the outright displacement of conversion as a basis of liability of one secured party to another for an improper foreclosure of collateral under Part 5 of Article 9. See, e.g., Liberty Nat'l Bank & Trust Co. v. Acme Tool Div. of the Rucker Co., 540 F.2d 1375, 1382 (10th Cir. 1976); Barry v. Bank of New Hampshire, 112 N.H. 226, 229, 293 A.2d 755, 755, 757 (1972); cf. Thurmond
party receives from the collateral’s disposition what he would have received had he conducted the sale himself, and this is true even if the senior creditor is for some reason unable to reach the original collateral.

The senior secured party actually may be in a better position because of the sale if the original collateral can still be reached. If the senior had conducted the sale himself, his interest in the original collateral would have terminated, and his security would consist only of the proceeds of the disposition. However, because a junior secured party disposed of the property, the senior creditor’s security interest continues in the original collateral and follows it into the hands of the buyer. If the senior secured creditor also has a claim to the proceeds of the junior secured party’s disposition, the senior creditor’s security may effectively be doubled because he can perhaps apply these proceeds to the debt owed him and, if any deficiency exists, still reach the original collateral in the buyer’s hands. It would be difficult in such a case to establish that the junior secured party’s

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v. Elliott Fin. Co., 141 Ga. App. 574, 576, 234 S.E.2d 153, 155 (1977) (debtor cannot sue secured party’s agent for conversion for conducting a commercially unreasonable sale of collateral; only remedy is statutory action for damages under § 9-507(1)).

Of course, the displacement of a common-law action based on conversion would be less consequential if liability on this basis is similarly conditioned. Under pre-Code law, secured creditors who improperly disposed of collateral were held liable for conversion to other secured creditors with interests in the property. For cases in which senior secured parties were liable to junior secured parties, see note 70 supra. For a case in which a junior secured creditor was liable to a senior secured creditor for failing to conduct a proper foreclosure of collateral, see Schumacher v. R-B Freight Lines, 73 S.D. 535, 538-39, 45 N.W.2d 458, 460 (1950). Cases such as Schumacher are rare because to recover in conversion from a junior secured party, a senior encumbrancer under pre-Code law did not need to show that the subordinate creditor failed to follow the proper procedures for disposing of collateral; he could recover solely on the basis that the junior creditor disposed of the property. See authorities cited in note 182 supra. In many of these cases the facts reveal that the defendant knew of the plaintiff’s interest in the property, but actual knowledge of the conflicting interest is not clearly established as an absolute prerequisite to liability; simple notice may have been the only condition. See, e.g., Penney v. Miller, 131 Ala. 593, 600, 33 So. 668, 670 (1901). However, notice is not sufficient in itself to establish one secured party’s accountability to another under § 9-507(1). See notes 63-64 supra.


202. For a discussion of the senior creditor’s continuing interest, see notes 145-46 supra.

If the buyer is unwilling or unable to return the collateral, he may have to respond in damages for conversion. See generally Nickles, supra note 3, at 520-36. Yet, considerations of justice and fairness arguably should shield the buyer from conversion liability if the senior secured party can reach the proceeds of a sale by the junior creditor. Presumably, or at least theoretically, a proper sale by the subordinate secured party should have yielded the same amount of proceeds that would have resulted had the senior creditor disposed of the property himself pursuant to Part 5 of Article 9. If the senior secured party’s remedy is limited to recovering these proceeds, he is in essentially the same position he would have occupied had he conducted the sale of the collateral himself.

203. Cf. U.C.C. § 9-306 comment 3 (if the debtor makes an unauthorized transfer of collateral, “[t]he secured party may claim both proceeds and collateral, but may of course have only one satisfaction”).
proper sale of the collateral amounted to a conversion of the property, because the senior creditor may view the resulting consequences as favorable.

Thus, when a junior secured party properly disposes of the original collateral, a senior secured party is not harmed if he can recover the sale proceeds. Even if the senior cannot recover these proceeds, the junior's sale of the collateral will have caused no harm if the senior can easily reclaims this property from the junior's transferee. Imposing conversion liability on the junior secured party is not justified in either case, because his conduct causes no significant adverse consequences. The senior secured party's recovery is equivalent to that which he would have obtained had the junior not intervened.

V. CONCLUSION

Upon the debtor's default, secured parties have the right to possession of the collateral so that they can dispose of it and apply the proceeds to satisfy the debt owed to them.\textsuperscript{204} This right is enforceable not only against the debtor but also against subordinate secured parties who have themselves repossession the property and are preparing to sell it.\textsuperscript{205} The senior secured party can replevy the collateral or otherwise take it from the junior creditor and thereafter control foreclosure, taking care not to impair the junior secured party's continuing, though subordinate, interest.\textsuperscript{206}

Less certain are the rights and remedies of a secured party when a subordinate secured party has already disposed of the collateral. There is no clear right to claim the sale proceeds received upon the collateral's disposition.\textsuperscript{207} Moreover, an award of damages against the junior creditor for conversion of the goods is proper only if his handling of the property seriously interferes with the right of the senior secured party to possession of the collateral. Such an interference is not an inevitable result of a sale of the property: the senior security interest survives the disposition, and the property can be repossessed from its buyer.\textsuperscript{208} Whether having to pursue this buyer amounts to a serious interference with a senior secured party's possessory right is an issue that should be determined on a case-by-case basis.\textsuperscript{209}

A senior secured party's right to possession has not seriously been impaired when, although the collateral has been sold by a junior secured party, it can easily be repossessed intact from the ultimate transferee. In this case a secured party will have no recourse against a subordinate secured

\textsuperscript{204} See id. §§ 9-503, 9-504.
\textsuperscript{205} See text accompanying notes 8-47 supra.
\textsuperscript{206} Regarding the duties owed a junior secured party by a senior secured party who has undertaken to dispose of collateral, see text accompanying notes 48-85 supra.
\textsuperscript{207} See text accompanying notes 86-155 supra.
\textsuperscript{208} See authorities cited in note 145 supra.
\textsuperscript{209} See text accompanying notes 156-203 supra.
party who repossessed and disposed of collateral. Yet, such recourse would be unjustified and unnecessary because the senior creditor suffers no significant actual loss. Furthermore, the priority of the senior’s security interest is vindicated because the interest survives the disposition and is enforceable against the buyer of the collateral. A junior secured party should be forced to pay damages for conversion only when his conduct seriously impairs the value of the senior creditor’s interest. In other cases he should be allowed to follow freely the course that Part 5 of Article 9 charts for all secured parties, not just those with senior interests.