

community BANKER

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Welcome to the latest issue of the COMMUNITY BANKER.

The Community Banker is prepared by attorneys at Olson & Burns P.C. to provide information pertaining to legal developments affecting the field of banking. In order to accomplish this objective, we welcome any comments our readers have regarding the content and format of this publication. Please address your comments to:

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The attorneys at Olson & Burns represent a wide range of clients in the financial and commercial areas. Our attorneys represent more than 30 banks throughout North Dakota.

POP QUIZ - PERFECTING AN ARTICLE 9 SECURITY INTEREST

When a lender takes security interest in collateral, priority over third parties, including the bankruptcy trustee is necessary to repayment. Test your priority skills with the following fact situations.

Donna Defaulter bought a table from Sydney Seller to use in the conference room in her real estate office. Donna promised to pay the \$1,500 cost price in 15 equal monthly installments; she also signed a security agreement giving Sydney an interest in the table to secure the unpaid purchase price. Sydney did not file a financing statement, believing that as the seller, he has an automatic security interest in the conference table. Before she made even one payment, Donna went out of business and she defaulted on her contract with Sydney. Unfortunately, Donna also owes Brian Banker \$1,800. Brian has obtained a judgment and a writ of execution, pursuant to which the sheriff seized and sold the table at a public sale for \$950.



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1. Who gets the \$950 - Donna Defaulter, Sydney Seller, or Brian Banker?

If you said Brian Banker, you are correct. Under N.D.C.C. § 41-09-02(1)(ii) the conference table is “equipment.” “Equipment” means goods other than inventory, farm products, or consumer goods. The table is not inventory for resale, it’s certainly not farm goods, and because it’s for use in her business, it isn’t consumer goods.

Sydney Seller neglected to file a financing statement to perfect his security interest in the table at the time of the levy and Brian’s lien takes priority.

2. What if Sydney Seller filed a financing statement covering the table prior to the sheriff’s levy. Now who gets the \$950?

Under N.D.C.C. § 41-09-02(1)(ii), filing a financing statement is a valid method of perfection of the security interest in the table. Because Sydney was perfected by filing a financing statement as of the time of Brian’s levy, Sydney has priority over Brian and he gets the \$950.

3. What if Donna Defaulter had purchased the table for use in the dining room of her home? Now who gets the \$950?

Sydney Seller will. No filing or other step is required to perfect a purchase-money security interest in consumer goods (other than goods such as motor vehicles that are subject to a statute or treaty). N.D.C.C. § 41-09-29(1). Sydney’s automatically-perfected security interest has priority over Brian’s lien.

4. Assume the same facts as in #2, except that the collateral sold by Sydney Seller is a 1999 Ford Taurus. Who gets the \$950 in this fact scenario?

Brian Banker gets the \$950. Filing a financing statement will not perfect Sydney’s security interest in a motor vehicle. Other than vehicles held for sale as inventory, perfection is accomplished by indicating the security interest on the certificate of title to the vehicle or by holding the title by possession of the secured party. N.D.C.C. § 35-01-05.1(1) and N.D.C.C. § 41-09-31(1)(b).

5. Assume the same facts as in #2, except that the collateral sold by Sydney Seller is an old Cessna that Donna had planned to restore; assume that even in its disintegrating condition it still had to be registered. Who gets the \$950 in this fact scenario?

Brian Banker gets the \$950. Under N.D.C.C. § 41-09-31(1)(a), if there is a federal statute governing the perfection of collateral, filing a financing statement in North Dakota is not an effective way to perfect. Civil aircraft of the United States are perfected according to a federal statute, 49 U.S.C. §§ 44107-11, so Sydney’s filed financing statement was *not* effective to perfect his security interest in the Cessna. The proper place to file was with the FAA in Oklahoma City (this includes aircraft, engines and propellers, and spare airplane parts). So, even though he filed his financing statement *before* Brian’s levy, he’s unperfected and Brian has priority.

6. Brian Banker lends \$50,000 to Donna Defaulter and takes a security interest in her office equipment to secure the loan. Subsequently, Donna gives a security interest in the very same equipment to Monty's Money Brokers and the sheriff levies on the office equipment pursuant to a judgment against Donna obtained by Larry Liencreditor.

Generally, which of the following statements best describes the parties' priority under Revised Article 9?

(i) Brian Banker has a claim to the equipment that is superior to any claim made by Donna Defaulter, Monty's Money Brokers or Larry Liencreditor.

(ii) Brian Banker has a claim to the equipment that is superior to any claim made by Donna Defaulter and Monty's Money Brokers, but not a claim made by Larry Liencreditor.

(iii) Brian Banker has a claim to the equipment that is superior to any claim made by Donna Defaulter and Larry Liencreditor, but not a claim made by Monty's Money Brokers.

(iv) Brian Banker has a claim to the equipment that is superior to any claim made by Donna Defaulter but not a claim made by Monty's Money Brokers or Larry Liencreditor.

If you said (i), you are correct. Generally, under N.D.C.C. § 41-09-11(1), a security interest is effective against the debtor and third parties claiming an interest in the collateral except as provided otherwise in North Dakota's UCC. We say "generally" because there are various exceptions to § 41-09-11(1)'s rule, but this rule will govern if there are no applicable exceptions. The scenario above gave no facts which would indicate an exception.

7. In each of the above scenarios, there is a winner and a loser and there is no pro rata distribution. True or false?

True. Under the various rules of the UCC, *one* party has priority over the others. One wins and the others lose. At best, other creditors can stand in line in order of priority such as a second priority, third priority, fourth priority interest, etc. In that case, they should hope the collateral is worth a lot so they are paid out of the surplus.

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