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## **RECENT DEVELOPMENTS IN COMMERCIAL LAW 2009-2010**

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## RECENT DEVELOPMENTS IN COMMERCIAL LAW 2009-2010

### I. UCC ARTICLE 9 -- PERSONAL PROPERTY SECURED TRANSACTIONS.

#### A. Scope of Article 9 and Existence of Security Interest.

##### 1. *Consignment.*

- ***Fariba v. Dealer Services Corp., 178 Cal. App. 4th 156, 2009 Cal. App. LEXIS 1649, 70 U.C.C. Rep. Serv. 2d 193, 2009 WL 319538 (Cal. App. 4th Dist. 2009).***

In a priority dispute between an auto dealer's consignor and secured party, the consignor's title had priority, where the secured party had actual knowledge that the auto dealer was substantially engaged in selling the goods of others. In this case of first impression, the California court described two exceptions to the rule that consigned goods in the possession of the consignee are subject to the claims of its creditors: (i) the consignor files a UCC financing statement, or (ii) the consignee is generally known to its creditors to be in the business of selling the goods of others. The court then read this second exception as a kind of constructive notice imputed to the competing secured party, and found that it would be a nonsensical reading of the statute to protect the consignor if a competing creditor had constructive notice but not if it had actual notice.

- ***In re Music City RV, LLC (Waldschmidt v. Adams), 304 S.W.3d 806, 2010 Tenn. LEXIS 86 (Tenn. 2010).***

This case involved the bankruptcy of a recreational vehicle dealer. Several individuals asserted that they had consigned certain vehicles to the dealer to be sold, and that those vehicles therefore were their own property and not property of the estate. Transactions that qualify as "consignments" under Article 9 are now treated as security interests, so that the consignor (as secured party) must perfect its interest, but these transactions were excluded from the Article 9 definition because the RVs were consumer goods. The trustee argued unsuccessfully that the consignments in this case were still subject to the claims of creditors as "sale or return" transactions under T.C.A. § 47-2-326.

In response to a question certified by the Bankruptcy Court for the Middle District of Tennessee, the Tennessee Supreme Court held that UCC Article 2 no longer applies to consignment transactions that do not qualify as consignments under UCC Article 9. All the consignment language in the pre-2001 version of T.C.A. § 47-2-236 was moved to Article 9, even though the caption still says "consignment." In a true consignment, the goods are not sold by the consignor to the consignee, but to the ultimate buyer, and there is no "sale" of goods covered by Article 2. Therefore, an "orphan" consignment--one that does not fit in the Article 9 definition -- is governed by common law, not the UCC.

- ***Excel Bank v. National Bank of Kansas City, 290 S.W.3d 801, 69 U.C.C. Rep.Serv.2d 1105 (Mo. Ct. App. 2009).***

A floor plan lender had a blanket security interest in a car dealer's inventory perfected by a properly filed financing statement. A third party delivered vehicles to the car dealer for

the dealer to sell from its lot on behalf of the third party. The third party retained possession of the title certificates. The floor plan lender repossessed all vehicles on the lot, and the third party sued the floor plan lender to regain possession of its vehicles. The court affirmed the trial court's decision granting summary judgment to the floor plan lender, finding that the third party had delivered the vehicles on consignment. A consignment is treated as a purchase money security interest, but the third party had not filed a financing statement or given a purchase money notice to preserve its rights. Possession of the certificates of title is not relevant to perfection when vehicles are in the possession of a dealer.

2. *Lease v. Security Interest.*

- ***Uni Imaging Holdings, LLC, 70 U.C.C. Rep.Serv.2d 902, 2010 WL 148422 (Bankr. N.D.N.Y. 2010).***

Debtor, a lessee under a 66-month lease of magnetic resonance imaging equipment, sought to characterize the lease as a secured sale. The court held that residual price of 13% of the original cost was not nominal and that debtor had not carried its burden of proof to characterize the lease as a secured sale.

B. Collateral Types and Descriptions.

- ***In re U. S. Ins. Group, LLC (Jahn v. Cornerstone Cmty. Bank), 2009 Bankr. LEXIS 3986 (Bankr. E.D. Tenn. 2009).***

Collateral description including accounts, commission accounts and books related to the commission accounts was adequate to cover insurance agent's "book of business" without need to use either that term or "general intangibles."

- ***In re CHA Hawaii LLC, 71 U.C.C. Rep.Serv.2d 206, 2010 WL 797285 (Bankr. D. Hawaii 2010).***

Collateral description in security agreement excluded "accounts," as defined in Article 9. The court held that the term "accounts" included Medicare and Medicaid payments (as "healthcare insurance receivables") but not disproportionate share hospital (DSH) payments, which are supplemental to Medicare and Medicaid. Therefore the DSH payments were included in the collateral.

C. Attachment and Perfection.

1. *Attachment.*

- ***In re Propex, Inc., 415 B.R. 321 (Bankr. E.D. Tenn. 2009).***

Committee of unsecured creditors sought to avoid a loan document amendment that imposed unrealistic covenants as a fraudulent conveyance; asserted a claim for deepening insolvency; alleged that reperfecting a security interest was a fraudulent conveyance; and claimed that the lender's security agreement did not extend to environmental permits.

The bankruptcy court dismissed the fraudulent conveyance and deepening insolvency claims (holding that Tennessee would not recognize a claim for deepening insolvency), but held that the debtor in fact had no rights in the environmental permits to which the lender's security interest could attach.

2. *Perfection by Filing – Debtor's Name.*

- ***Hastings State Bank v. EDM Corp. (In re EDM Corp.), 2010 WL 1929772, 71 UCC Rep.Serv.2d 876 (B.A.P. 8th Cir. 2010).***

A financing statement did not provide the correct name of the corporate debtor where a trade name was added to the debtor's name ("EDM Corporation d/b/a EDM Equipment"). The debtor's name must be the name indicated on the public record of its organizational jurisdiction, under UCC § 9-503, and only that name. Further, since a search performed against the correct legal name ("EDM Corporation") using the Nebraska Secretary of State's standard search logic did not disclose the existence of the financing statement, it was seriously misleading under UCC § 9-506(c).

- ***Trane Company v. CGI Mechanical, Inc., 2010 WL 2998516 (D.S.C. 2010).***

In a priority dispute between a federal tax lien and a judgment lien, the notice of federal tax lien was effective even though it used a prior name of the taxpayer/debtor, where the judgment creditor had done business with the debtor for years under the old name and continued to use the old name in some correspondence. A search under the new name would not have disclosed the tax lien notice, but the court held that a reasonably diligent search conducted by this particular creditor should have included the debtor's old name. The court relied in part on the decision in *In re Spearing Tool and Manufacturing Co.*, 412 F.3d 653 (6th Cir. 2005), *cert. denied* 549 U.S. 810 (2006).

- ***In re Crystal Cascades Civil, LLC (United States v. Buenting), 52 BCD 12 200, Bankr. LEXIS 2612 (B.A.P. 9th Cir. 2009).***

The IRS filed a notice of federal tax lien in the correct place in Nevada to cover real property. The notice identified the taxpayer as "Crystal Cascades, LLC" instead of "Crystal Cascades Civil, LLC". After the IRS filed its notice, a bank filed deeds of trust against the taxpayer's real property. When the taxpayer went bankrupt, the bank proceeded against the real property collateral. The IRS learned of this and asserted that it had the prior lien.

The bank argued that the notice filed by the IRS did not satisfy the federal regulation requiring that the notice be filed "in such a manner that a reasonable inspection of the [applicable real property] index will reveal the existence of the lien." At issue was whether the similarity of the taxpayer's actual name to the name filed by the IRS was sufficient that a "reasonable" inspection of the Nevada records would have revealed the notice. The court held that in Nevada a title searcher could reasonably search under the exact correct name of the relevant party without searching variants of the taxpayer's

name. Therefore, the IRS notice was not sufficiently filed and the bank had the prior lien on the real property.

- ***In re Lohrey Enterprises, Inc., 71 U.C.C. Rep.Serv.2d 406, 2010 WL 147916 (Bankr. N.D.Calif. 2010).***

A financing statement filed against “Lohrey Investments LLC” was ineffective to perfect against equipment owned by “Lohrey Enterprises, Inc.”

3. *Perfection by Filing – Termination.*

- ***In re S.J. Cox Enterprises Inc. (Peoples Bank of Kentucky, Inc. v. U.S. Bank, N.A.), 68 U.C.C. Rep.Serv.2d 761, 2009 WL 939573 (Bankr. E.D.Ky. 2009).***

A UCC termination statement filed by a bank employee erroneously identified another secured party’s financing statement. The court determined that the filing was not filed by a person authorized under UCC § 9-509, but then ignored UCC § 9-510, which provides that a filing is only effective if filed by a person authorized to file it under UCC § 9-509. Instead, the court relied on case law under former Article 9 and held that the unauthorized termination statement was still effective, leaving the secured party unperfected. The court did find that the bank that filed the statement was liable to the other secured party for damages under UCC § 9-625.

4. *Perfection by Certificate of Title.*

- ***In re Ritchie (Palmer v. Washington Mutual Bank), 416 B.R. 638, 2009 Bankr. LEXIS 2950 (B.A.P. 6th Cir. 2009).***

The BAP affirmed the bankruptcy court’s holding that the bank’s security interest in a manufactured home was unperfected under Kentucky law because its security interest had not been noted on the certificate of title, and that the bank’s security interest therefore could be avoided by the bankruptcy trustee. The manufactured home remained personal property because the debtor had not taken the steps required under the applicable Kentucky statute (K.R.S. § 186A.297) to convert it to real property. The only way to perfect the bank’s security interest therefore was by notation of the lien on the certificate of title.

The bank made several arguments, all of which failed. First, because the home was not real property, the bank’s *lis pendens* filed in a previous state court action was not effective under state law. For the same reason, any constructive notice that may have been provided by the *lis pendens* would not have protected the bank from the trustee’s strong arm powers as a hypothetical lien creditor as to personal property, even if it may have provided constructive notice to the trustee as a hypothetical bona fide purchaser of real property. Finally, the bankruptcy court’s holding was not inconsistent with the state court’s previous holding in the case that the bank had an “equitable lien” on the manufactured home, because an “equitable lien” is essentially an unperfected security interest and, as such, would still be avoidable by the trustee.

- ***Johnson v. Branch Banking & Trust Co.*, 2010 Ky. LEXIS 152 (Ky. June 17, 2010).**
- ***In re Johnson (Brock v. Branch Banking & Trust Co.)*, 2010 U.S. App. LEXIS 13588 (6th Cir. 2010).**

In response to a question certified by the Sixth Circuit of Appeals, the Kentucky Supreme Court held that a motor vehicle lien is not perfected under Kentucky law until the certificate of title is actually issued with the notation of lien, under K.R.S. § 186A.190, and is not perfected upon delivery to the county clerk of the application and required paperwork under K.R.S. § 186A.195(5). This latter statute creates only a timing mechanism for priority purposes, providing for perfection to relate back if the lien is actually noted on the certificate within 20 days after it is created.

The Sixth Circuit then affirmed the decision of the BAP, holding that the bank's lien was not perfected until the certificate was actually issued, was not perfected within 20 days after it was created, and was therefore avoidable as a preference.

- ***In re Scott (Boston v. Chrysler Fin. Servs. Americas LLC)*, 427 B.R. 123, 71 U.C.C. Rep.Serv.2d 314 (Bankr. S.D. Ind. 2010).**

Under Indiana law, the assignee of a security interest perfected by notation on a certificate of title was not required to be named on the certificate of title to continue perfection. The court analyzed UCC § 9-311(c), which provides that the duration and renewal of a security interest perfected by compliance with a state's certificate of title statute are governed by that statute, and found that the Indiana certificate of title statute did not clearly require the assignee to be named on the certificate. The court also analyzed UCC § 9-311(b), which provides that compliance with a state's certificate of title statute is the equivalent of filing a financing statement, and UCC § 9-310(c), which provides that it is not necessary to file a financing statement amendment to preserve perfection upon assignment of a security interest. The court relied on Comment 4 to UCC 9-310, which states that an assignee should not be required to take action to have the certificate of title reflect the assignment or the assignee's name, unless the statute expressly provides to the contrary. (The court also castigated the trustee for presenting a number of ridiculous arguments and ignoring UCC §§ 9-310 and 9-311.)

- ***Fitzpatrick v. Toyota Motor Credit Corp. (In re Hartline)*, 2009 Bankr. LEXIS 2907 (Bankr. E.D. Tenn. Sept. 9, 2009).**

Under T.C.A. § 55-3-126, the creditor's security interest in a motor vehicle was perfected when the lien application (with appropriate paperwork and fee) was submitted to the clerk, even though the initial certificate of title was lost and a replacement certificate with a lien notation was not issued until almost 2 years after the application had been submitted. This was not a case where the lien had been released and then a new certificate of title was issued, but merely a replacement of the original title. The court noted that the trustee's reliance on *Still v. First Tenn. Bank, N.A.*, 900 S.W.2d 282, 285 (Tenn. 1995), was misplaced, since this decision was effectively overruled by amendments to the certificate of title statutes in 1996.

5. *Perfection by Control – Securities Accounts and Deposit Accounts.*

- ***Fifth Third Bank v. Lincoln Financial Securities Corp., 2009 U.S. Dist. LEXIS 102668, 2009 WL 2523444 (W.D. Ky. 2009).***

A securities intermediary breached a control agreement when it reversed trades of securities in the securities account, where the control agreement included a waiver of all the securities intermediary's rights to liens, encumbrances, claims and rights of setoff. In the control agreement, the securities intermediary had represented and warranted the market value of the securities held in the account as of the date of the control agreement, but then reversed the purchases of those securities when the debtor's check for the purchase was returned for insufficient funds. On motion for reconsideration, the court rejected efforts of the securities intermediary to reargue the case, but vacated the judgment to the extent necessary to confirm that the court's calculation of the judgment amount was correct. *Fifth Third Bank v. Lincoln Fin. Sec. Corp.*, 2009 U.S. Dist. LEXIS 102668 (W.D. Ky., Nov. 4, 2009).

- ***In re Alexander (Flener v. Alexander), 429 B.R. 876 (Bankr. W.D. Ky. 2010).***

Alexander had a deposit account with the Bank, and instructed the Bank to withdraw funds from the deposit account to invest in certificates of deposit ("CDs") to be issued through the Certificate of Deposit Account Registry Service ("CDARS"). The CDARS network allows a customer's bank ("Relationship Bank") to invest the customer's funds in multiple certificates of deposit issued by other banks in the network, while the Relationship Bank issues certificates of deposit for customers of other banks. Alexander granted the Bank a security interest in his deposit accounts and his interest in certain of the CDs to secure a loan made to Alexander by the Bank. When the CDs matured, funds were paid into Alexander's account and the Bank set off against the funds. In Alexander's chapter 7 bankruptcy case, the trustee sued to recover the funds, arguing that the Bank's security interest was not perfected. The Bank argued that its security interest was perfected by control. The court held that the Bank's security interest was limited to Alexander's deposit accounts, and that once the funds were withdrawn from the deposit account to invest in the CDs, Alexander's account was no longer a deposit account but a security entitlement under a securities account maintained by the Bank as a securities intermediary. The Bank no longer had control of the withdrawn funds and did not have control of the CDs issued by other banks. Finally, the security agreement did not describe the security entitlement or securities account with specificity as required under UCC § 9-108 for consumer debtors.

- ***In re Cumberland Molded Products, LLC (Limor v. First National Bank of Woodbury), 2010 Bankr. LEXIS 1853; 53 Bankr. Ct. Dec. 82 (B.A.P. 6th Cir. 2010), reversing 69 U.C.C. Rep.Serv.2d 371, 2009 WL 2208582 (Bankr. M.D. Tenn. 2009).***

A bank had a perfected security interest in its customer's deposits when the customer filed Chapter 7. The Trustee asked the customer to turn over the bank account, which the customer did and the bank permitted. Later the bank asserted its security interest in the

funds and the Trustee sought to retain the funds for the benefit of the estate, arguing that the bank had lost its rights when it allowed the payment to the Trustee.

The bankruptcy court granted the Trustee's motion for summary judgment awarding the Trustee the funds. The BAP reversed and remanded. The BAP rejected the Trustee's arguments under § 544 (the bank's perfected security interest was not a "secret lien" of the sort that section addresses) and UCC § 9-332 (affording protection to transferees of funds, but a remittance to a Chapter 7 Trustee is not a transfer in this sense).

- ***Full Throttle Films, Inc. v. National Mobile Television, Inc., 180 Cal. App. 4th 1438, 103 Cal. Rptr. 3d 560, 2009 Cal. App. LEXIS 2118 (Cal. App. 2d Dist. 2009).***

A judgment creditor levied upon the bank accounts of its judgment debtor. A finance company affiliate of the depository bank claimed a prior security interest in the accounts and tendered control agreements to show perfection. The trial court awarded the finance company priority in the accounts.

On appeal, the court reversed the trial court's holding. The court found that the trial court's record did not demonstrate that the accounts subject to the finance company's control agreements were the accounts that had been levied, so the control agreements did not establish perfection. The court noted that perfection in the deposits could also have been accomplished by filing, but the record did not reflect such a filing. (This discussion seems to suggest that a filing is sufficient to perfect in deposit accounts in general, but may have been an attempt to refer to the possible perfection in the deposit account as proceeds of other collateral).

D. Priority.

- ***In re QuVIS, Inc., 71 UCC Rep.Serv. 2d 801 (Bankr. D. Kan. 2010).***

Debtor and several lenders entered into a loan and security agreement, granting security interests in the collateral to all of the lenders. Debtor filed an initial financing statement naming all the lenders as secured parties, and later filed amendments to add new lenders as they joined into the loan agreement. The initial financing statement lapsed, and some of the lenders, but not all of them, filed new individual financing statements, each naming only the particular lender as secured party. In the debtor's bankruptcy case, the re-filing lenders asserted that they were secured creditors, but the other lenders were not. The other lenders argued that the new filings had been filed on behalf of all the lenders, and that payments should be made to all the lenders on a pro-rata basis as provided in the loan agreement. The court held that nothing in the loan agreement authorized any lender to file financing statements on behalf of any others, so that only the re-filing lenders were perfected, with priority based on the order of their filings. Also, since the lenders were no longer similarly situated or acting collectively, the provisions in the loan agreement for pro-rata sharing of collateral no longer applied.

- ***1st Source Bank v. Best-One Tire of Crossville, Inc.*, 70 U.C.C. Rep.Serv.2d 227, 2009 WL 2170167 (E.D. Tenn. 2009).**

Tires, wheels and lug nuts on a vehicle are accessions to the vehicle. Under UCC § 9-335, a security interest in accessions to a motor vehicle perfected by filing is subordinate to a security interest in the vehicle and accessions perfected by noting the lien on the certificate of title.

- ***In re Lombardo's Ravioli Kitchen, Inc. (Lagalia v. People's United Bank)*, 2009 WL 3257492, 70 U.C.C. Rep.Serv.2d 418, 2009 Bankr. LEXIS 3267 (Bankr. D. Conn. 2009).**

Initial lender had a properly perfected security interest in debtor's assets pursuant to a security agreement including a future advances clause. Second lender perfected a security interest against certain of debtor's assets. Initial lender thereafter made additional loans to the debtor. In a priority dispute between the two lenders, initial lender had priority as first-to-file, regardless of when its various advances were made.

- ***United States ex rel. Solera Constr. v. J.A. Jones Constr. Group*, 71 U.C.C. Rep.Serv.2d 416, 2010 WL 1269938, 2010 U.S. Dist. LEXIS 34065 (E.D.N.Y. 2010).**

A bank had a properly perfected security interest in debtor's assets, which lapsed when the bank's financing statement was not continued. The bank thereafter filed an effective financing statement. A judgment creditor issued a levy during the gap between the bank's filings. The levy was returned with no assets found. Magistrate found that the judgment creditor's rights were not perfected by the levy and that bank's re-filed financing statement gave it priority under Article 9's "first-to-file" general priority rule.

- ***In re Montagne v. Montagne*, 413 B.R. 148, 2009 Bankr. LEXIS 3103, 52 Bankr. Ct. Dec. 39 (Bankr. D. Vt. 2009).**

A lender had a properly perfected first priority security interest in cows. When the cows were sold, the resulting check was deposited to the escrow account of the lawyer for the former wife of a principal of the debtor company. The lender sought to hold the former wife liable for conversion of the funds.

The court found that the lender's right to possession of the proceeds of the sale of the cows was sufficient that it could assert a claim of conversion. The former wife asserted the protection of UCC § 9-332, which allows recipients of funds to keep them unless taken in "collusion with the debtor in violating the rights of the secured party." The court denied the lender summary judgment because it found inadequate information in the record to determine whether the 9-332 defense was available.

- ***In re Delco Oil, Inc., 2010 WL 918058, 71 UCC Rep.Serv.2d 302 (11th Cir. 2010).***

Secured party had a perfected security interest in all the debtor's assets, and objected to debtor's post-petition use of cash collateral. Between the cash collateral motion and hearing, the debtor made several payments to a supplier. When the court denied the debtor's motion to use cash collateral, the secured party sought to recover the payments from the supplier. The court agreed with the supplier's argument that it was a transferee of cash and took the payments free of the security interest, under UCC § 9-332, but held that the security interest had been perfected while the funds were in the debtor's deposit account, and the secured party could thus recover the post-petition transfers under the Bankruptcy Code. The court also noted that no control agreement was necessary to perfect as to the deposit account, since the funds were proceeds of the original collateral.

E. Assignments and Assignees.

- ***Summit Financial Resources LP v. Kathy's General Store, Inc., 2010 WL 1816685, 71 U.C.C. Rep.Serv.2d 500 (D. Kan. 2010).***

Kathy's General Store ("Store") was a combination service station, convenience store, and clothing/gift shop. The Store regularly purchased motor fuel from a supplier, and prepaid the supplier by depositing credit card proceeds into the supplier's bank account, generally resulting in a credit balance in favor of the Store. Then when the supplier delivered fuel, it would generate an invoice and offset against the Store's credit balance. A factor purchased the supplier's accounts receivable, notified the Store and, pursuant to UCC § 9-406, instructed the Store to make all payments to the factor. The supplier told the Store to ignore the notice, and the Store continued depositing credit card proceeds into the supplier's account under the existing pre-payment procedure. The factor sued the Store to recover the payments. The court found that the Store was not an "account debtor" subject to UCC § 9-406, however, because it has not incurred any monetary obligation to the supplier. Because the Store had prepaid for all fuel delivered, the Supplier never had a right to payment that could be assigned to the factor.

- ***Ta Chong Bank Ltd. v. Hitachi High Techs. Am., Inc., 2010 U.S. App. LEXIS 13861 (9th Cir. Cal. July 7, 2010).***

Assignee of account had no interest separate from assignor/debtor, and thus had no right to collect directly from account debtor after debtor's claim against account debtor had been discharged in bankruptcy.

- ***Regions Bank v. Wyndham Hotel Mgmt. Inc., 2010 U.S. Dist. LEXIS 23371 (M.D. Tenn. Mar. 11, 2010).***

A property owner entered into a Hotel Management Agreement ("HMA") for an operator to manage its property. The HMA provided for exclusive venue in Illinois. The owner granted a security interest in the HMA to its bank to secure a loan. This security interest was acknowledged by the operator in a Subordination, Nondisturbance and Attornment

Agreement (“SNDA”) among the owner, operator, and the bank. The project failed, a disagreement arose between the bank and the hotel operator as to their respective obligations regarding the property, and the bank sued in the United States District Court for the Middle District of Tennessee. The hotel operator sought dismissal in reliance on the forum selection clause contained in the HMA, to which the bank was not a party.

The court dismissed the bank’s action, applying the rule that a non-signatory to a forum selection clause in a contract may be bound if the non-signatory is “closely related” to the dispute such that it is “foreseeable” that the non-party will be bound by the clause. In the court’s view, the bank received a collateral assignment of the HMA and thus was aware of, and took subject to, its provisions, and the dispute with the operator was sufficiently tied to the HMA that the bank should be required to pursue its action in Illinois.

F. Default and Remedies.

1. *Repossession.*

- ***Scott v. Houston, 2010 Tenn. App. LEXIS 153 (Tenn.Ct.App. Feb. 26, 2010).***

Punitive damages for retaliatory repossession were appropriate under the unusual circumstances of this case. The individual debtor’s employer ran a gambling ring and financed the employee’s purchase of a car through an affiliate. When she cooperated with the state in criminal prosecution against the employer, the affiliate repossessed and foreclosed on her car, even though she had paid all the principal and interest, arguing that she had not paid late fees (which had not been charged), and demanded that she pay off a relative’s car loan too.

2. *Sale of Collateral.*

- ***Regions Bank v. Trailer Source, Inc., 2010 Tenn. App. LEXIS 351 (Tenn.Ct.App. May 21, 2010).***

This is the second Court of Appeals decision on this case. In the first decision, the court held that a senior secured party’s obligation to conduct a commercially reasonable sale of collateral extends to an unperfected junior secured party, even though the junior secured party would not be entitled to notice of sale under UCC § 9-611. The court then remanded the case to determine whether the senior lender (Regions) had a duty to conduct a commercially reasonable sale in this case and, if so, whether the sale had been commercially reasonable.

In this second decision, the court held that the commercial reasonableness requirement in UCC § 9-610 applied to the senior secured party, even though the collateral was actually sold by the debtor and was never in the secured party’s possession. The court noted that the test was not whether the collateral was in the secured party’s possession, but whether the secured party was in control of the sale.

In this case, Regions had a perfected security interest in used vehicles held for sale by the dealer-debtor, and had filed suit to obtain the certificates of title from another bank,

stating in that suit that it intended to conduct a UCC sale of the vehicles. The debtor found a buyer and sold the vehicles itself, with Regions' consent, and Regions agreed to deliver the titles to the buyer upon payment of the sale proceeds to Regions.

The court noted that there were several "unique" factors in this case, including the secured party's express statement that it intended to conduct a foreclosure sale and its "leveraging" of its position to ensure that it received the sale proceeds. The court ultimately found that the sale had been commercially reasonable, and further emphasized that its ruling was narrow and would not apply to a secured party's simple release of its collateral.

3. *Strict Foreclosure.*

- ***SunTrust Equipment Finance & Leasing Corp. v. A&E Salvage, Inc., 2009 WL 3584333 (E.D.Tenn. 2009).***

A lender sued a corporate borrower and its guarantors to recover a loan. The lender had already repossessed its equipment collateral. The guarantors asserted that the lender had to elect its remedies and could not sue them for judgment once it had repossessed the collateral. The court held that the lender was free to pursue the collateral and the guarantors at the same time.

- ***2010 Tenn. Pub. Act 100: Payment of Personal Property Tax from Article 9 Foreclosure Sales.***

This bill amended T.C.A. § 67-5-2003(h), which imposes upon Article 9 secured creditors who sell collateral the duty to determine and withhold from the sale any unpaid personal property taxes arising from the sold property, and T.C.A. § 67-5-1805, which provides a mechanism for valuation of the property and allocation of the tax. Noncompliance renders the foreclosing lender liable for the tax.

## II. UCC ARTICLE 2 – SALES.

- ***Holt v. Wilmoth, 2010 Tenn. App. LEXIS 302 (Tenn.Ct.App. Apr. 30, 2010).***

Sellers sold to a buyer the real property and inventory used in a retail lamp business. One of the sellers estimated the value of the inventory at between \$450,000 and \$500,000. The inventory was sold to buyer for \$250,000 paid by issuance of a promissory note. Buyer found the value of the inventory to be low and only realized \$65,000 on resale. Sellers sued to recover the balance due on the purchase money note and buyer counterclaimed, raising the defense of inadequate consideration and arguing in briefs that the sellers had intentionally misrepresented the value of the inventory. The trial court determined that there was no intentional misrepresentation, but it awarded no relief to either party, apparently because it felt it would be inequitable to award relief.

The court of appeals awarded the sellers judgment on their note, holding that while principles of equity can be relevant to a sale transaction governed by Article 2, they were not invoked in this case. The court of appeals disregarded the misrepresentation issue, as

it had not been raised in the pleadings. The court of appeals also refused to delve into the adequacy of consideration (noting that a total failure of consideration is a more appropriate consideration for a court).

### III. UCC ARTICLE 2A – LEASES.

- ***Walker v. Frontier Leasing Corp., 2010 Tenn. App. LEXIS 226 (Tenn. Ct. App. Mar. 30, 2010).***

Plaintiffs had obtained a judgment for fraud in a previous action against their equipment vendor. The vendor had assigned to a leasing company one of the equipment leases signed by plaintiffs in the course of the vendor's fraud. In this action, plaintiffs sought relief against the leasing company, alleging that the vendor was the agent of the leasing company and the leasing company was thus tainted with the vendor's fraud. The court affirmed the trial court's dismissal of the complaint, finding the lease to be a "financing lease" under Article 2A for which the "hell or high water" clause effectively shielded the lessor from liability for the actions of the equipment vendor.

### IV. GUARANTIES, PREPAYMENTS AND OTHER CONTRACTS.

- ***Thompson v. Davis, 308 S.W.3d 872 (Tenn. Ct. App. 2009), perm.app. denied 2010 Tenn. LEXIS 208 (Tenn. Feb. 22, 2010).***

Three individuals formed a corporation that owned the Memphis Pharaohs arena football team. As it needed capital, they all signed individually for each of two loans and gave the funds to the corporation. The corporation was not successful and left the two loans outstanding in material part when it ceased business. Two of the three owners paid the lenders and then sought contribution from the third owner. The court affirmed the trial court's holding that the two owners were entitled to contribution, citing T.C.A. § 47-3-116 (although there was no finding that the loans involved the issuance of a negotiable instrument).

- ***First Peoples Bank v. Hill, 2010 Tenn. App. LEXIS 354 (Tenn. Ct. App. May 26, 2010).***

Father who co-signed son's promissory note remained liable on the note, even though it was replaced by a renewal note evidencing additional bank loans made to the son without the father's knowledge (but with a forged guaranty provided by the son). The original note contained waiver language agreeing that renewals and the like would not discharge or release parties to the note. The bank's internal accounting records showing the balance of the original note as zero when the second note was issued did not affect the status of the second note as a renewal, not a discharge, of the original note.

- ***In re Touse, Inc., 2009 WL 3519403 (Bankr. S.D.Fla. Oct. 30, 2009).***

Subsidiaries guaranteed first- and second-lien lenders who made loans to enable parent and sister affiliates of the subsidiaries to fund settlement payments. In the bankruptcy of the subsidiaries, a successful fraudulent conveyance challenge left their guaranties and

the collateral securing them avoided; payments they had made were disgorged; the lenders were charged with the diminution in value of the subsidiaries' property in the relevant period; and litigation costs were charged to the lenders.

The subsidiaries were apparently of questionable solvency when the guaranties were undertaken, and they received no direct value from the payments they made. Under these facts, a fraudulent transfer challenge is not in itself an unusual event. But the court attacked the transaction with unusual relish.

In rejecting the lenders' good faith transferee defense, the court considered the solvency opinion issued for the closing and determined that the opinion had negative value for the lenders. It was ordered and issued over a very brief period of time and the substantial fee was contingent upon a favorable opinion.

The court also disregarded the fraudulent conveyance savings language in the loan documents, finding them to be attempts to frustrate Sections 548 and 541 of the Bankruptcy Code and inherently ambiguous and unenforceable under New York state contract law.

- ***NPS, LLC v. Ambac Assurance Corp., 2010 U.S. Dist. LEXIS 16988 (D. Mass. Feb. 25, 2010).***

NPS (an affiliate of the New England Patriots), could not avoid paying a prepayment premium upon its redemption of 30-year bonds covered by a financial guaranty insurance agreement with Ambac. The court rejected all NPS's arguments that Ambac's downgraded credit ratings had caused the auction bonds to fail so that NPS was compelled to redeem them, that Ambac had fraudulently induced NPS to enter into the agreement by holding itself out as a good risk, that the prepayment premium was an unenforceable penalty, and that its non-payment should be excused on grounds of frustration of purpose or impossibility.

- ***2010 Tenn. Pub. Act 908: Codification of Equitable Doctrine of Unclean Hands.***

This bill created new T.C.A. §§ 16-1-201 through 206, codifying the doctrine of unclean hands and making it specifically applicable to commercial transactions, including lending transactions. The bill provides that the doctrine may be asserted against any successor-in-interest of a wrongdoer except against a holder in due course of a negotiable instrument.

V. UCC ARTICLES 3, 4 AND 4A - NEGOTIABLE INSTRUMENTS, BANK DEPOSITS AND COLLECTIONS, FUNDS TRANSFERS.

1. Article 3.

- ***Contour Industries v. U.S. Bancorp.*, 69 UCC Rep.Serv.2d 426, 2009 WL 2146160 (E.D. Tenn. 2009).**

An employee with responsibility to handle incoming payments intercepted checks payable to his employer, forged indorsements on the checks, and deposited them to his personal account. The employer sued the depository bank for conversion to recover the amount of the stolen checks. The bank moved for summary judgment, invoking UCC § 3-405(b), which would protect the bank from liability as long as it accepted the checks in good faith. The court refused to dismiss the conversion claim, stating that even under Tennessee's relaxed, non-uniform definition of "good faith" for this purpose, the bank's good faith was at issue because it had violated its own internal policies in accepting the checks over an extended period of time.

- ***In re Prebul Jeep, Inc.*, 71 UCC Rep.Serv.2d 220, 2009 WL 4348602 (Bankr.E.D.Tenn. 2009).**

Plaintiff lender received two checks from its borrower just before the borrower filed bankruptcy. Plaintiff sued the borrower's bank claiming that plaintiff was entitled to payment as a holder in due course of the two checks. In denying plaintiff's motion for summary judgment, the court found that although plaintiff's status as a holder in due course would allow it special rights to recover from the borrower that issued the check, it does not entitle plaintiff to recover from the issuing bank on the checks. The bank had not "accepted" the checks and their issuance did not constitute an assignment of funds.

- ***Reger Development LLC v. National City Bank*, 592 F.3d 759; 2010 U.S. App. LEXIS 1165 (7th Cir. 2010), cert denied, *Reger Dev. v. Nat'l City Bank*, 2010 U.S. LEXIS 5447 (U.S. June 28, 2010).**

Demand note really was payable on lender's demand, notwithstanding references to default and due date in note.

2. Article 4.

- ***Bluff Springs Apartments, Ltd. v. Peoples Bank of the South*, 2010 Tenn. App. LEXIS 356 (Tenn. Ct. App. May 26, 2010).**

A real estate developer was engaged in check kiting. The depository bank froze all accounts associated with the developer in August of 2003, including tenant deposit accounts for housing projects developed under Rural Development Agency programs. Depository bank set off against the funds in September of 2006. Developer and the project entities sought recovery of the funds in various accounts after the setoff.

The court of appeals affirmed the trial court's holding that the bank breached its deposit contract in setting off against the accounts styled as tenant deposit accounts for the developer's obligations. The developer's claims made against the bank as to other accounts was barred by the three-year statute of limitations on conversion.

Counsel to the Rural Development Agency stated that the agency took no position, although he was prepared to assert the federal government's "nanny-nanny-boo-boo defense" if necessary.

3. *Article 4A.*

- ***ReAmerica, S.A. v. Wells Fargo Bank International, 70 UCC Rep.Serv.2d 126, 2009 WL 2432731 (2d Cir. 2009).***

A consultant to the plaintiff company acquired the plaintiff's authorization code and initiated wire transfers from plaintiff's account. Plaintiff sought to recover the wired amounts from the defendant bank that sent the wires. The court dismissed the plaintiff's action, holding that the one-year statute of repose in UCC § 4A-505 barred the action, including common-law claims arising from the unauthorized transfers..

- ***In re Bancredit Cayman Ltd. (Bancredit Cayman Ltd. v. Regions Bank Corp.), 70 UCC Rep.Serv.2d 545, 2009 WL 3762337 (Bankr. S.D. Fla. 2009).***

Plaintiff liquidator of a Cayman entity alleged that defendant bank honored a transfer of funds from the Cayman entity that was not properly authorized. Plaintiff argued various common-law claims incidental to the transfer. Defendant bank sought summary judgment on the grounds that Article 4A of the UCC applied and that the one-year statute of repose under UCC § 4A-505 had passed. The court granted summary judgment to the defendant bank, holding that Article 4A governed all claims stated by plaintiff.

- ***Fischer & Mandell LLP v. Citibnak, N.A., 20120 WL 2484205, 72 UCC Rep.Serv.2d 270 (S.D.N.Y. 2010).***

A bank customer instructed its bank to send two wire transfers, believing that a check deposited into the customer's account represented good funds. When the check was returned for insufficient funds, the bank charged the wire transfer amounts back to the customer. The customer sued the bank, on grounds of (i) breach of contract (for executing the wire transfer without good funds in the customer's account), and (ii) negligence (for not canceling the wire transfer upon customer's notice of cancellation). First, the court held that the breach of contract action was not pre-empted by the UCC, because both Article 4 and Article 4A (at least in this case) allow the parties to vary their responsibilities by agreement, but that the bank had not breached that agreement. Second, the court held that the negligence claim was preempted by Article 4A and could only succeed if the bank's actions did not comply with Article 4A. The bank had already executed on the customer's payment order before receiving the cancellation notice, and under § 4A-211 was not obligated to cancel its own payment order. The customer's negligence claim thus failed as well.

## VI. JOINT CREDIT FACILITIES.

- *Highland Crusader Offshore Partners LP et al. v. Lifecare Holdings Inc.*, 377 Fed.Appx. 422, 2010 WL 1849293 (5th Cir. 2010).

A debtor sought to obtain consent to an amendment to a joint credit facility. The debtor secretly offered different amounts of fees to the different lenders in the group for their approval. One of the lenders brought an action against the borrower and the agent lender for breach of contract, fraud, and a variety of other grounds. The court of appeals affirmed the lower court's dismissal of the lender's claim.

## VII. REAL PROPERTY.

### 1. Recording Tax.

- *Higdon v. Regions Bank*, 2010 Tenn. App. LEXIS 331 (Tenn.Ct.App. May 13, 2010).

A deed of trust lien was not limited to the original loan amount on which recording tax was paid under T.C.A. § 67-4-409(b), where the deed of trust included a dragnet clause and a future advances clause. The lien secured future advances, including amounts later paid by the lienholder to pay off a prior lien on the property. The later advances related back to the date of the original deed of trust recording for priority purposes. The court rejected the debtor's argument, which was based solely on cases decided under the pre-1987 version of the recording tax statute, and confirmed that the amended statute does not limit a lien to the amount of indebtedness on which the tax was paid.

### 2. Foreclosure Sales.

- *2010 Tenn. Pub. Act 1001: Deficiency Judgments After Real Estate Foreclosure Sales.*

This bill created new T.C.A. § 35-5-117, which establishes a procedure for the determination of deficiency judgments after foreclosure sales of real property. The process allows the foreclosing lender a rebuttable assumption that the foreclosure sale price was the fair market value of the property.