

Permanent Editorial Board for the Uniform Commercial Code

PEB COMMENTARY NO. 21

**USE OF THE TERM “ASSIGNMENT” IN ARTICLE 9 OF THE UNIFORM
COMMERCIAL CODE**

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PREFACE TO PEB COMMENTARY

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A *PEB Commentary* should come within one or more of the following specific purposes, which should be made apparent at the inception of the Commentary: (1) to resolve an ambiguity in the Uniform Commercial Code by restating more clearly what the PEB considers to be the legal rule; (2) to state a preferred resolution of an issue on which judicial opinion or scholarly writing diverges; (3) to elaborate on the application of the Uniform Commercial Code where the statute and/or the Official Comment leaves doubt as to inclusion or exclusion of, or application to, particular circumstances or transactions; (4) consistent with U.C.C. § 1-102(2)(b),* to apply the principles of the Uniform Commercial Code to new or changed circumstances; (5) to clarify or elaborate upon the operation of the Uniform Commercial Code as it relates to other statutes (such as the Bankruptcy Code and various federal and state consumer protection statutes) and general principles of law and equity pursuant to U.C.C. § 1-103;† or (6) to otherwise improve the operation of the Uniform Commercial Code.

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* Current U.C.C. § 1-103(a)(2).

† Current U.C.C. § 1-103(b).

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INTRODUCTION

Article 9 of the Uniform Commercial Code (the “UCC”) addresses in Part 4 the rights of third parties in secured transactions. The third parties are typically “account debtors,”¹ i.e., persons obligated on accounts,² chattel paper,³ or general intangibles⁴ (including payment intangibles⁵). However, many of the provisions of Part 4, instead of referring to a “debtor,”⁶ “secured party,”⁷ and “security interest,”⁸ all of which terms are defined in the UCC, refer to an “assignor,” an “assignee,” and an “assignment,” or sometimes to an “assigned contract,” none of which terms are defined in the UCC.⁹

This Commentary explains what constitutes an “assignment” and the scope of the terms “assignor” and “assignee” in relation to the statutory scheme of Article 9.

DISCUSSION

Article 9 applies to both a sale of certain payment rights—accounts, chattel paper, payment intangibles, and promissory notes (for convenience, referred to herein as “specified payment rights”)—and to the grant of an interest in specified payment rights to secure an obligation.¹⁰ Put another way, Article 9 applies both to an outright assignment of ownership of specified payment rights and to an assignment of specified payment rights for security. The terms “debtor” and “secured party” are defined to include the participants in both types of transactions.¹¹

¹ U.C.C. § 9-102(a)(3) (defining “account debtor”).

² U.C.C. § 9-102(a)(2) (defining “account”).

³ U.C.C. § 9-102(a)(11) (defining “chattel paper”).

⁴ U.C.C. § 9-102(a)(42) (defining “general intangible”).

⁵ U.C.C. § 9-102(a)(61) (defining “payment intangible”).

⁶ U.C.C. § 9-102(a)(28) (defining “debtor”).

⁷ U.C.C. § 9-102(a)(73) (defining “secured party”).

⁸ U.C.C. § 1-201(b)(35) (defining “security interest”).

⁹ Section 9-403 addresses an agreement of an account debtor not to assert claims or defenses against an “assignee.” Section 9-404 addresses the rights acquired by an “assignee” and certain claims and defenses that an account debtor can assert against an “assignee.” Section 9-405 focuses on modifications to an “assigned contract.” Section 9-406 sets forth the rights of an account debtor when notified of an “assignment.” Sections 9-406, 9-407, 9-408, and 9-409 generally address certain contractual and legal restrictions on “assignment.” Section 9-209 describes certain duties of a secured party if an account debtor has been notified of an “assignment.”

¹⁰ See U.C.C. § 9-109(a)(1), (3).

¹¹ Section 9-102(a)(28) states that a “debtor” includes both “a person having an interest, other than a security interest or other lien, in the collateral, whether or not the person is an obligor” and “a seller of accounts, chattel paper, payment intangibles, or promissory notes.” Section 9-102(a)(73) states that a “secured party” includes both “a person in whose favor a security interest is created or provided for under a security agreement” and “a person to which accounts, chattel paper, payment intangibles, or promissory notes have been sold.” U.C.C. § 9-102(a)(73). In addition, Section 1-201(b)(35) defines a “security interest” to include both “an interest in personal property ... which secures payment or performance of an obligation” and “any interest of ... a buyer of accounts, chattel paper, a payment intangible, or a promissory note in a transaction that is subject to Article 9.” U.C.C. § 1-201(b)(35).

For ease of reference, we refer in this Commentary to a security interest that secures an obligation as a “SISO.”

Article 9’s use of the term “assignment,” and the correlative terms “assignor” and “assignee,” is largely historical. Former versions of Article 9 used these terms as they were used in general contract law.¹² In that context, it was understood that an “assignment” could be either an outright transfer of ownership of a specified payment right or a SISO in a specified payment right.¹³ The 1999 revisions of Article 9 retained that terminology to avoid any suggestion that the scope or substance of the applicable rules had been changed. Although revised Article 9 does not define the terms “assignment,” “assignor,” and “assignee,” Comment 26 to Section 9-102 states that “[d]epending on the context, [the term “assignment”] may refer to the assignment ... of an outright ownership interest or to the assignment ... of a limited interest, such as a security interest.” Accordingly, unless there is good reason for any of these terms to apply more narrowly, each applies, as appropriate, both to an outright assignment of ownership and to a SISO.

Some courts have interpreted the term “assignment,” especially in the context of Section 9-406(a),¹⁴ as referring only to an outright assignment of ownership. This narrow reading of the term “assignment” is contrary to the use of the term in Article 9 and the holdings of other courts¹⁵ and is incorrect.

Section 9-406(a) provides that, when an account debtor receives a notification from an assignor or an assignee that a specified payment right has been assigned to the assignee and an instruction to pay the assignee, the account debtor may thereafter discharge its obligation to make the payment owed by paying the assignee. After receipt of the notification and payment instruction, the account debtor may not discharge the account debtor’s payment obligation by paying the assignor. Under some courts’ erroneously narrow interpretation, Section 9-406(a) applies only when the assignment is a sale of the specified payment right and does not apply when the assignment is a SISO.¹⁶

¹² See generally RESTATEMENT (SECOND) OF CONTRACTS ch. 15, “Assignment and Delegation” (AM. LAW INST. 1981) (using “assignment” to refer interchangeably to the outright transfer of a right under a contract and to the creation of a security interest in a right under a contract).

¹³ See U.C.C. § 9-406, cmt. 5 (“Former Section 9-318(4) rendered ineffective an agreement between an account debtor and an assignor which prohibited assignment of an account (whether outright or to secure an obligation)...”); 7 THOMAS M. QUINN, QUINN’S UNIFORM COMMERCIAL CODE COMMENTARY AND LAW DIGEST (Rev. 2d ed. 2011), at 961-62 (discussing former U.C.C. § 9-318). Case law under former U.C.C. § 9-318 was consistent with the broad interpretation of the term “assignment” to include both an outright transfer and a SISO. See, e.g., *First Nat’l Bank of Boston v. Thomson Consumer Elecs., Inc.*, 84 F.3d 397, 399 (11th Cir. 1996); *Bank of Waunakee v. Rochester Cheese Sales, Inc.*, 906 F.2d 1185, 1190 (7th Cir. 1990); *In re Johnson*, 439 B.R. 416, 432 (Bankr. E.D. Mich. 2010), *aff’d on other grounds*, No. 10-14292, 2011 WL 1983339 (E.D. Mich. May 23, 2011).

¹⁴ See, e.g., *Durham Capital Corporation v. Ocwen Loan Servicing, LLC*, 777 F. App’x 952 (11th Cir. 2019), citing *IIG Capital LLC v. Archipelago, L.L.C.*, 36 A.D.3d 401, 404 (N.Y. App. Div. 2007).

¹⁵ See, e.g., *ARA Inc. v. City of Glendale*, 360 F. Supp. 3d 957 (D. Ariz. 2019); *Nisbet, Inc. v. Wells Fargo Bank*, No. SA-14-CV-00469-RP, 2015 WL 1408839 (W.D. Tex. Mar. 26, 2015) (order denying motion to dismiss for failure to state a claim); *Swift Energy Operating, L.L.C. v. Plemco-South, Inc.*, 157 So. 3d 1154 (La. Ct. App. 2015).

¹⁶ Presumably, under the narrow interpretation, if the assignment is a SISO in a specified payment right and is therefore outside of the scope of Section 9-406(a), other law determines whether an account debtor may discharge the account debtor’s payment obligation by paying the assignee or by continuing to pay the assignor after receipt of the notification and instruction.

There is no policy reason to limit the term “assignment” in Section 9-406, or elsewhere in Article 9, to an outright transfer of ownership. Doing so would place a burden on the account debtor to determine whether the assignment was a sale or a SISO in order to know whether, for example, the obligations and rights in Part 4 apply to the account debtor. That burden is both heavy and unjustifiable. The account debtor is not a party to the assignment transaction and typically has no basis for making that determination. Nor does it make sense to require the account debtor to obtain the assignment documentation from the assignor or the assignee, and then to analyze the transaction between the assignor and the assignee to ascertain whether the transaction is actually a sale, merely to be confident that the account debtor may discharge its payment obligation by paying the assignee or to have other rights, claims, duties, and defenses of an account debtor under Part 4. Given the difficulty that courts often have in determining whether an assignment of a payment right is a sale or a SISO,¹⁷ an account debtor should not be expected to make that determination.¹⁸ In the context of Section 9-406(a), for example, all that should matter to the account debtor is to know whom the account debtor may pay in order to discharge the account debtor’s payment obligation.¹⁹ Similarly, an assignee often would not have certainty on whether Part 4 of Article 9 applies to its rights or whether the common law of contracts applies. This lack of certainty would have a negative effect on the availability of financing.

One court has expressed the view that the narrow interpretation of the term “assignment” is consistent with Article 9’s “legislative scheme.” According to the court, because a secured party’s right to enforce a SISO in a specified payment right is addressed in Section 9-607, there is no need for Section 9-406(a) to afford to such a secured party a “parallel” right.²⁰ However, the court failed to consider subsection (e) of Section 9-607. That subsection states, in relevant part, that “[t]his section does not determine whether an account debtor ... owes a duty to a secured party.” In other words, Sections 9-607 and 9-406 address different rights. Section 9-607 addresses the rights of a secured party *vis-à-vis the debtor* to collect a specified payment right. Section 9-406 addresses a secured party’s rights *against the account debtor* to collect a specified payment right. If Section 9-406—and Part 4 of Article 9 more generally—did not apply to an assignment constituting a SISO, there would be a gap in Article 9: nothing in Article 9 would address the rights, claims, duties, and defenses of an account debtor with respect to that type of assignment.

¹⁷ “In many commercial financing transactions the distinction is blurred.” U.C.C. § 9-109, cmt. 4.

¹⁸ Similarly, an assignor should not have to make these judgments to determine if Part 4 applies to rights that the assignor may have under Part 4, such as the assignor’s right under U.C.C. § 9-405 to make good faith modifications to an assigned contract that bind the assignee.

¹⁹ See U.C.C. § 9-406, cmt. 5 (applying U.C.C. § 9-406(a) to an account debtor’s right to a discharge on an account that secures an obligation). Likewise, there is no reason to limit the term “assignment” in the opposite direction, i.e., to a SISO in a specified payment right to the exclusion of a sale of the specified payment right, as the court apparently did in *Contrarian Funds, LLC v. Woodbridge Group of Companies (In re Woodbridge Group of Companies)*, 606 B.R. 201 (D. Del. 2019). In this decision dealing *inter alia* with the anti-assignment provisions in Section 9-406 and 9-408, the court incorrectly held that Section 9-408(a), rather than Section 9-406(d), applied to the assignment of a promissory note that secured an obligation and that neither Section applied to the sale of a promissory note. The court misunderstood Section 9-406(e). That section provides that Section 9-406(d) does not apply to the sale of a promissory note, and Section 9-408(b), which provides that Section 9-408(a) specifically does apply to the sale of a promissory note. For a critique of the *Woodbridge* decision, see Bruce A. Markell, *The Road to Perdition: 180 Equipment, Woodbridge and Liddle Pave the Way*, 39 BANKRUPTCY LAW LETTER 1 (Nov. 2019); see also Stephen L. Sepinuck, *Personal Property Secured Transactions*, 74 THE BUSINESS LAWYER, 1291, 1297-98, and Carl S. Bjerre and Stephen L. Sepinuck, *Spotlight*, 9 THE TRANSACTIONAL LAWYER (Feb. 2019), each of which critiques the bankruptcy court’s decision upheld by the district court.

²⁰ *Durham*, 777 F. App’x at 956.

As explained in Section 1-103(a)(2), one of the purposes of the UCC is “to permit the continued expansion of commercial practices through custom, usage, and agreement of the parties.” The narrow interpretation of the term “assignment” in Part 4 would undermine that purpose. Suppose, for example, that pursuant to Section 9-406(a), a debtor who has granted a SISO in a specified payment right notifies the account debtor that the right has been assigned and instructs the account debtor that payment is to be made to a particular assignee. The narrow interpretation would leave to other law whether the account debtor may discharge the account debtor’s payment obligation by paying the debtor or by paying the secured party. The broader interpretation makes clear when the account debtor may discharge the account debtor’s payment obligation by paying the debtor and when the account debtor may discharge the obligation by paying the secured party.²¹ The broader interpretation creates greater certainty for both the secured party and the account debtor and is consistent with expectations in commercial practice.²²

The broader interpretation of the term “assignment” is relevant not only for Section 9-406(a) but also for other provisions of Article 9 in which the term “assignment” is used, such as in the balance of the provisions of Part 4 and in Section 9-209. Likewise, the term “assignor” in those provisions includes a debtor who grants a SISO, and the term “assignee” includes the secured party in whose favor such a security interest is granted.

AMENDMENTS TO OFFICIAL COMMENTS

With the discussion in this Commentary in mind, the Official Comments to Section 9-401 are amended to add the following new Official Comment:

8. Use of the Term “Assignment.” The term “assignment,” as used in this Article, refers to both an outright transfer of ownership and a transfer of an interest to secure an obligation. See Comment 26 to Section 9-102 and PEB Commentary No. 21, dated March 11, 2020.

In addition, Official Comment 26 to Section 9-102 is amended as follows:

26. Terminology: “Assignment” and “Transfer.” In numerous provisions, this Article refers to the “assignment” or the “transfer” of property interests. These terms and their derivatives are not defined. This Article generally follows common usage by using the terms “assignment” and “assign” to refer to transfers of rights to payment, claims, and liens and other security interests. It generally uses the term “transfer” to refer to other transfers of interests in property. Except when

²¹ Some courts have expressed skepticism that a secured party is entitled to sue an account debtor whose payment obligation to the debtor has not been discharged under U.C.C. § 9-406(a). *See, e.g., Forest Capital, LLC v. BlackRock, Inc.*, 658 F. App’x 675 (4th Cir. 2016). However, if the account debtor has not been discharged under U.C.C. § 9-406(a) on its contractual obligation to the debtor, the account debtor remains liable to the debtor. Article 9 gives the secured party the right to enforce the debtor’s rights against the account debtor. *See* U.C.C. § 9-607.

²² *See, e.g., FORMS UNDER ARTICLE 9 OF THE UCC, AMERICAN BAR ASSOCIATION BUSINESS LAW SECTION UNIFORM COMMERCIAL CODE COMMITTEE* (3d ed. 2016) at 595-96. Form 4.6 is a form of “Demand for Payment on Account Debtor of Borrower.” The form, invoking U.C.C. § 9-406, assumes that the account debtor is obligated on collateral that secures a loan by the secured party to a debtor who is the “borrower.”

used in connection with a letter-of-credit transaction (see Section 9-107, Comment 4), no significance should be placed on the use of one term or the other. Depending on the ~~context~~ substance of the transaction, each term as used in this Article ~~may refer~~ refers to the assignment or transfer of an outright ownership interest, ~~or~~ to the assignment or transfer of a limited interest, such as a security interest, or both. See Comment 8 to Section 9-401 and PEB Commentary No. 21, dated March 11, 2020.