

# THE TRANSACTIONAL LAWYER

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## PERFECT TENDER IN TIME, REDEMPTION, AND THEIR IMPACT ON PREPAYMENT PREMIUMS

*Stephen L. Sepinuck*

Consider the following, not-entirely hypothetical, scenario. You are counsel to a lender contemplating a sizeable term loan to a commercial borrower. The parties agree that there is to be a prepayment premium if the borrower repays the loan before maturity but have yet to agree on what that premium will be or how it will be calculated. Nevertheless, the loan needs to close. So you recommend that the loan agreement contain a term prohibiting prepayment, recognizing that the lender could later waive that term for a fee. In essence, you recommend that the amount of the prepayment premium be decided later, if and when the borrower wishes to prepay. It is a clever idea. Will it work? Maybe. To explain why it might and why it might not, it is useful to take a brief detour.

### PERFECT TENDER IN TIME

Historically, the common law included something called the “perfect tender in time rule,” which provided that a borrower had no right to repay early unless the agreement so provided.<sup>1</sup> In a jurisdiction that adheres to this rule, the advice of the transactional lawyer in the scenario described above – to close now and negotiate the prepayment premium later – would appear to work.

But not all jurisdictions continue to follow the perfect tender in time rule. Indeed, the Restatement (Third) of Property

– Mortgages indicates that the law is now otherwise, and prepayment is permitted with respect to loans secured by real property.<sup>2</sup> But the Restatement might be more prescriptive than descriptive on this point. The Reporter’s Note identifies only four states that permit prepayment when the loan agreement is silent,<sup>3</sup> and it cites authorities in seven other states that continue to follow the perfect tender in time rule, which does not require the lender to accept payment before the due date.<sup>4</sup> Indeed, New York, whose law parties often choose to govern commercial loan agreements, is one of these latter states that continues to prohibit prepayment absent an express term to the contrary.<sup>5</sup> Thus, the perfect tender in time rule might remain the prevailing approach.

Nevertheless, even the jurisdictions that have abandoned the perfect tender in time rule, and permit prepayment, do so only when the loan expressly so provides or is silent on the issue.<sup>6</sup> They all acknowledge that a loan agreement can prohibit early repayment.<sup>7</sup> Thus, at least at first blush, it would appear that the loan agreement in the scenario described above could validly prohibit prepayment.

### THE RIGHT TO REDEEM

But what if the loan is secured and the borrower has a right to redeem the collateral? Does that redemption right effectively give the borrower a right to repay the loan at any time? Again, the answer is maybe.

If the collateral is real property, the answer appears to be no. According to Restatement (Third) of Property – Mortgages § 6.4(a), performance of the obligation secured by a mortgage may be made prior to the time the obligation is due, “except as restricted by agreement of the parties.”<sup>8</sup> Thus, if the parties have validly prevented early payment, the borrower has no right to redeem the collateral before payment is due.

If the collateral is personal property to which Article 9 of the Uniform Commercial Code applies, the answer is unclear. Section 9-623 provides that a debtor, secondary obligor, or lienholder may redeem collateral by fulfillment of all obligations secured by the collateral.<sup>9</sup> The section then expressly adds that redemption may occur “at any time before” the secured party has completed a collection, disposition, or acceptance of the collateral.<sup>10</sup> Although § 9-623 is located in Part 6, which is entitled “Default,” and thus the section might be thought to apply only after a default,<sup>11</sup> the language of the section does not appear to limit the right it creates to situations in which a default exists. Several other provisions in Part 6 of Article 9 expressly apply only “after default,”<sup>12</sup> but that phrase

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is conspicuously absent from § 9-623.<sup>13</sup> Thus, a strict reading of the language of § 9-623 appears to allow the debtor to redeem the collateral at any time, even if no default has occurred and even if payment is not yet due. In short, § 9-623 appears not only to have legislatively overruled the perfect tender in time rule, but to have prevented the parties to a secured transaction from prohibiting early prepayment.<sup>14</sup> The provision in no way interferes with the enforceability of a clause requiring a prepayment premium, but if the parties have not yet agreed to such a premium – as in the introductory scenario – § 9-623 would appear to give the debtor a statutory right to prepay.

Nevertheless, there are two somewhat related reasons why § 9-623 might not have this effect.

First, § 9-623 gives the debtor a right to redeem the collateral by “fulfillment” of all obligations secured by the collateral. It is not clear whether early repayment would, if prohibited under the loan agreement, “fulfill” the secured obligations. Put another way, it simply might not be possible to fulfill secured obligations that are not yet due if early payment is not permitted.

Second, although § 9-623 states that redemption requires fulfillment “of all obligations secured by the collateral,” official comment 2 states something quite different: that redemption “requires payment in full of all monetary obligations then due and performance in full of all other obligations then matured.” “If unmatured secured obligations remain,” the comment then adds, “the security interest continues to secure them.”<sup>15</sup> This comment suggests § 9-623 does not provide a right to prepay the secured obligation.<sup>16</sup> Unfortunately, this comment appears to contradict the statutory text, which as noted above authorizes redemption “at any time” before foreclosure.

It is perhaps possible to harmonize the comment with the statutory text. For example, the comment could be read as a sort of definition of what “redemption” means or accomplishes. But such an interpretation would make redemption under Article 9 something quite different from what it normally means. Instead of being a process that liberates the collateral from the lien,<sup>17</sup> it would effectively be a right to cure a default.

Perhaps instead, the comment’s reference to “unmatured” obligations should be interpreted to refer only to contingent obligations. For example, if the collateral secures, in addition to a loan, a covenant that the debtor has not yet violated, it would not be reasonable to think that the debtor could repay the loan and free the collateral from all liability for a future breach of that covenant.<sup>18</sup> This interpretation gives meaning – essential meaning – to the comment while limiting its conflict with the statutory text. The debtor can pay the secured obligation “at any time” – thus, regardless of whether it is matured – but the debtor cannot, of course, redeem the collateral from contingent secured obligations.

In sum, it seems unlikely that the drafters of Article 9 intended to give debtors a right to prepay their secured obligations – that is, a right to redeem the collateral by paying all matured and unmatured (but not contingent) debts. It seems even less likely that they intended to give debtors such a right when the agreement of the parties expressly provides otherwise. Indeed, a comment to § 9-623 suggests that they did not intend to give debtors such a right. But perhaps that is what they inadvertently did. There are no known cases that deal with this issue, and thus it is difficult to predict how a court would interpret and apply § 9-623 in a situation in which there were unmatured secured obligations.<sup>19</sup>

## CONCLUSION

A transactional lawyer representing the lender in the introductory scenario could still recommend that the client close now and deal with the prepayment premium later. If the loan is unsecured, it might be sufficient for the loan agreement to be silent about the borrower’s right to prepay, but an express prohibition on prepayment would almost assuredly work. If the loan will be secured by real property, the result should be the same. But if the loan is to be secured by personal property and the security interest will be governed by Article 9, § 9-623 might give the borrower a statutory right to prepay unmatured obligations. The lawyer could still advise the client to close now, but should inform the client of the risk in doing so.

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## Notes:

1. See, e.g., Megan W. Murray, *Prepayment Premiums: Contracting for Future Financial Stability in the Commercial Lending Market*, 96 *Iowa L. Rev.* 1037, 1042-43 (2011).
2. *Restatement (Third) of Property – Mortgages § 6.1* (“In the absence of an agreement restricting or prohibiting payment of the mortgage obligation prior to maturity, the mortgagor has a right to make such payment in whole or in part.”).
3. See *id.* Reporter’s Note (citing cases from Louisiana and Pennsylvania, and statutes from Florida and North Carolina).
4. See *id.* (citing cases from Alabama, Connecticut, Maryland, Nebraska, New Hampshire, New York, and West Virginia).
5. See, e.g., *Trilon Plaza, Inc. v. Comptroller of the State of New York*, 788 A.2d 146 (N.Y. 2001) (the perfect tender in time rule prohibits the debtor from compelling the creditor to accept prepayment). The New York rule apparently applies to all loans, not merely to loans secured by real property.

6. See [Fla. Stat. § 697.06](#) (“Any note which is silent as to the right of the obligor to prepay the note in advance of the stated maturity date may be prepaid in full by the obligor or his successor in interest without penalty.”) (emphasis added); [N.C. Gen. Stat. § 24-2.4](#) (“A borrower may prepay a loan in whole or in part without penalty where the loan instrument does not explicitly state the borrower’s rights with respect to prepayment or where the provisions for prepayment are not in accordance with law.”) (emphasis added).

7. See *Spillman v. Spillman*, [509 So. 2d 442](#) (La. Ct. App. 1987); *Mahoney v. Furches*, [468 A.2d 458](#) (Pa. 1983) (each indicating that the language of the agreement could validly prohibit early repayment). See also [Restatement \(Third\) of Property – Mortgages § 6.2\(a\)](#) (“Subject to the general requirement of good faith and fair dealing . . . , the power of courts to refuse enforcement of unconscionable contract terms . . . , and other applicable law, (i) an agreement that prohibits payment of the mortgage obligation prior to maturity is enforceable; and (ii) . . . an agreement requiring the mortgagor to pay a fee or charge as a condition of such payment is enforceable.”). See also the statutes quoted *supra* note 6.

8. [Restatement \(Third\) of Property – Mortgages § 6.4\(a\)](#).

9. U.C.C. § 9-623(a), (b).

10. U.C.C. § 9-623(c).

11. Moreover, U.C.C. § 9-601(a) and (d) provide that, “[a]fter default,” the debtor and the secured party have the rights provided in Part 6. This could be interpreted to mean that the rights delineated in Part 6 apply *only* after default, and not before. But such an interpretation is doubtful. There is no reason to think that the rules on acceptance of collateral, see U.C.C. §§ 9-620 – 9-622, apply only after default. More important, the rights and remedies provided to debtors and obligors in § 9-625 must apply whenever the secured party acts inappropriately, regardless of whether a default has occurred. Indeed, a secured party’s actions – such as in repossessing and disposing of the collateral – might be inappropriate precisely because no default has occurred.

12. See U.C.C. §§ 9-601(a), (d), 9-604(c), 9-607(a), 9-609(a), (c), 9-610(a), 9-617(a), 9-620(c)(1), (2), (f), 9-624(a), (b), (c). See also U.C.C. §§ 9-612(b), 9-613(c)(1)(A) (each using the phrase “after default,” but not as a predicate to a right or duty).

13. Comment 2 to U.C.C. § 9-623 does end with a parenthetical reference to “default,” and that reference could be read as implying that the provision is triggered by default. However, that implication is weak and seemingly belied by the statutory text.

14. The rights granted by § 9-623 cannot be varied by agreement prior to default. See U.C.C. §§ 9-602(11), 9-624(c).

15. § 9-623 cmt. 2. The Restatement makes a similar point with respect to contingent or unliquidated obligations:

On rare occasions, however, a mortgage may contain covenants the breach of which has damaged the mortgagee, and for which payment of the mortgage obligation in full may not provide complete redress. For example, a mortgage might contain a term prohibiting the mortgagor from competing with the mortgagee’s business for a fixed time period within a certain geographic radius. If the mortgagor breached this covenant, the mortgagee might suffer lost business profits as a result. A payment of the mortgage debt would not compensate for these lost profits, and the mortgagee might bring an action for damages. The fact that the mortgage debt had been paid in full would not bar such an action, and the mortgage would not be regarded as “extinguished” for this purpose.

Restatement (Third) of Property – Mortgages § 6.4 cmt. a.

16. There might be unmatured obligations for several different reasons. For example, the obligation might not yet be due and there might be no default, thereby precluding acceleration. Alternatively, even if a default has occurred, the lender might not have the right to accelerate the debt or might not have exercised its right to accelerate.

17. See *Black’s Law Dictionary* 1443 (rev. 4th ed. 1968).

18. Cf. [Restatement \(Third\) of Property – Mortgages § 6.4 cmt. a](#) (quoted *supra* n.15).

19. It is worth noting that the predecessor to current § 9-623 – old § 9-506 – had the same problem. The statutory text permitted redemption “[a]t any time before” foreclosure, but the official comment thereto stated that redemption “requires full payment of all monetary obligations then due and full performance of all other obligations then matured. If unmatured obligations remain, the security interest continues to secure the them.” The absence of known case law on this issue extends back through the entire time when old Article 9 was the law.



## A Few Additional Thoughts about Guaranties of Unenforceable Obligations

*Robert W. Ihne*

After reading Professor Stephen Sepinuck’s thought-provoking article, “Guaranties of Unenforceable Obligations,” in the [December 2019 issue](#) of *The Transactional Lawyer*, I would like to respond with a few thoughts of my own. In doing

so, I have been trying to make sense of my own intuitions about which defenses available to principal obligors should be waivable by guarantors. On the one hand, principles of freedom of contract suggest that any defense available to a principal obligor could be waived by a secondary obligor that is doing so freely and knowledgeably.

Professor Sepinuck's article acknowledges limits to this suggestion, however, such as where the underlying obligation is illegal. His conclusion that courts would not enforce a guaranty of such obligations – notwithstanding an explicit waiver of such a defense in the guaranty – seems clear to me as well (even if such limits are not all identified in the Restatement of the Law (Third) of Suretyship and Guaranty).

Our feelings about such cases may be based upon the idea that not only should any promise that is illegal not be enforceable, but also that anyone seeking to benefit from the promised illegal performance should not be able to benefit from either: (i) the underlying illegal promise; or (ii) an agreement by someone backing up that illegal promise – no matter how absolute and unconditional the underlying promise may have been worded or how strong the waivers of defenses by the secondary obligor may have been.

Such an idea, focusing on whether the obligee of a promise is deserving of performance of that promise by any party at all – whether by the principal obligor or any secondary obligor – seems to be what is driving my intuitions about the possibilities of waivers of defenses regarding both fraud and unenforceable penalties. Expressed in a perhaps overly simplistic manner, there seems something quite wrong with permitting an obligee of a legally indefensible promise (*i.e.*, a “bad-actor obligee” that is legally unable to collect on that promise) to recover from a guarantor, no matter how explicitly the guarantor may have waived all defenses available to the principal obligor. If the principal obligor does not have to pay such a bad-actor obligee because it has been fraudulently induced by that obligee to enter into the underlying agreement, how is it that such a bad-actor obligee nevertheless deserves to collect from the guarantor? Likewise, if the principal obligor does not have to fulfill its promise to a bad-actor obligee because the promise constitutes a penalty under the law not enforceable by that obligee, how is it that such a bad-actor obligee nevertheless deserves to collect from the guarantor?

In the context of Article 2A, cases and common sense indicate that even when a lease contains strong “hell or high water” language and/or a provision in which both lessor and lessee agree that the lease should be treated as an Article 2A finance lease, the lessee will not be required to keep paying a lessor which has fraudulently induced the lessee into the lease. One might argue based on freedom of contract principles that the lessee has agreed to keep paying no matter what, and that the lessee is free to sue the lessor for fraud while continuing to pay. I have not seen, however, that such an outcome has been supported in either cases or commentary.

The history of “hell or high water” lease obligations also does not lend support to the possibility of a guarantor's contractually agreeing to waive defenses against bad-actor obligees inasmuch as approval of such lease provisions were developed in the context of leases with lessors that are in the business of financing only – *i.e.*, lessors that do not supply the equipment and that are presumably innocent of any fraudulent representations that the lessee may have heard from the equipment supplier. But when fraud can be ascribed to a finance lessor – whether in developing its own fraudulent scheme to entice lessees or through its knowledge of, and possibly complicity with, a fraudulent supplier – a court will deny payment to such a bad-actor lessor/obligee.

Some may tend to conflate the issue of a guarantor's waiver of defenses available to the principal obligor with what the Restatement refers to as the standard “suretyship defenses” – defenses available to a guarantor which the Restatement indicates should be generally waivable. As Professor Sepinuck's article points out, these suretyship defenses are in another category altogether. These defenses result from actions or inactions of an obligee – usually after the transaction has begun – that changes the risks of the guarantor vis-à-vis its ability to recover from the principal obligor should the guarantor be called upon to pay (*e.g.*, release or modification of the underlying obligation, extending the time for the principal obligor to perform, impairing the value of collateral in a secured obligation). Such defenses, clearly waivable in most instances under present law relating to guaranties, are not the main subject of Professor Sepinuck's article. The issue in my mind is whether a guarantor may waive defenses available to a principal obligor of a bad-actor obligee, not whether actions or inactions of any obligee taken with respect to the principal obligor or property of that obligor prejudice the position of a guarantor.

There is another scenario arising in finance transaction law where an innocent principal obligor in a financing transaction, who may have been wronged by a bad-actor obligee, is nevertheless obligated to make all payments under the transaction because it has waived defenses that would otherwise be available to it. Commercial law requires innocent principal obligors who may have been defrauded by its bad-actor obligee to pay good faith, innocent assignees (*e.g.*, with no knowledge of such fraudulent conduct) of such a bad-actor obligee as long as the principal obligor has agreed to waive all defenses it may have against the bad-actor obligee (the only exception being an extreme form of fraud known as fraud in factum). This commercial law rule chooses the innocent assignee over the innocent principal obligor in order to facilitate the flow of commercial transactions. This rule does not, however, finally reward the bad-actor obligee, who although having been paid for the transaction by the innocent assignee, remains susceptible of being sued by the defrauded principal obligor.

Unlike the case just discussed, if a bad-actor obligee gets paid by a guarantor that has waived defenses of its principal



obligor, there does not appear to be any route for the bad-actor obligee to have to pay for its sins after it has been paid by the guarantor. I believe that section 24(1)(c) of the Restatement would prohibit the guarantor from seeking reimbursement from the principal obligor inasmuch as the principal obligor had a defense to the underlying obligation that was not available to the secondary obligor - due to its having waived that defense. If the principal obligor had a duty to reimburse its guarantor, a right to go after the bad-actor obligee would no doubt arise. But, of course, such a chain of events makes little sense if the principal obligor had no duty in the first place to pay the bad-actor obligee due to the (illegal, unfair) nature of the underlying obligation.

The foregoing was my way of expressing intuitions about fairness – that it would be unjust to reward an obligee which could not collect directly from its principal obligor, due to some legally recognized prohibition, by permitting it to collect indirectly from a guarantor that had waived defenses available to the principal obligor. I understand that there may be some cases and/or commentary adopting a contrary position; but my hope is that intuitions such as expressed herein might be taken into account to arrive at conclusions that are as fair as possible to all parties.

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## Revisiting Clauses that Purport to Bind Successors and Assigns

*Stephen L. Sepinuck*

A 2014 article in this newsletter<sup>1</sup> explored whether a typical successors and assigns clause serves any purpose. Such a clause often looks like the following:

**Successors and Assigns.** This Agreement is binding on and inures to the benefit of the parties and their respective [permitted] successors and assigns.

As the article noted, several experts on contract drafting have concluded that such a clause serves no purpose and can be safely excluded from all legal documents.<sup>2</sup> The article then explored a possible purpose of the clause that those authorities had not discussed: to help bind either the non-assigning party or the successor or assignee to an extension of the contractual

relationship, such as clause in a security agreement purporting to make the collateral secure future advances or a clause in a guaranty purporting make the guarantor responsible for future extensions of credit.<sup>3</sup> Ultimately, however, the article concluded that it is doubtful that a typical successors and assigns clause would reliably cover future advances made by or to a successor or assign, and if contracting parties wanted such a result they should expressly so state. Accordingly, the article concluded that a successor and assigns clause “serves no clear purpose and can be safely discarded.”<sup>4</sup>

However, in January, a successor and assigns clause played a key role in a case decided by the Connecticut Supreme Court: *Jenzack Partners, LLC v. Stoneridge Associates, LLC*.<sup>5</sup> So, let us explore that decision to see whether the previous advice needs to be rescinded or amended.

The case involved a 2006 construction loan from Sovereign Bank to Stoneridge Associates, LLC. In 2008, the promissory note evidencing the loan was modified, at which time Jennifer Tine guaranteed the debt and executed a mortgage to secure the guaranty. In 2012, the bank assigned the note and the mortgage securing the guaranty to Jenzack Partners. A few months later, Jenzack brought an action to foreclose the mortgage. Tine claimed that Jenzack lacked standing because, even though Jenzack had received an assignment of the note and the mortgage, it had not received an assignment of the guaranty. The trial court ruled for Jenzack, the Connecticut Appellate Court reversed, and then the Connecticut Supreme Court took up the case.

After finding that the language of the assignment did not resolve the matter,<sup>6</sup> the court turned to the language of the guaranty. Specifically, the court look to the following clause:

**14. Bind and Inure.** The provisions of this Guaranty . . . shall bind and inure to the benefit of the parties hereto and their heirs, successors and assigns . . . [T]he word “Lender” as used herein shall mean not only the original Lender named in the first paragraph of this Guaranty, but also all future holders of the Note and Loan Documents.

Relying on this language, the court ruled that the assignment of the note operated as an assignment of Tine’s guarantee.<sup>7</sup> The court noted that the Restatement (Third) of Suretyship and Guaranty provides for the same result in most cases,<sup>8</sup> but chose not to rely on the Restatement, deferring to another day whether to adopt that rule as a matter of law.<sup>9</sup> Thus, the parties’ version of a successors and assigns clause was crucial to the outcome.

But was it really? What the court failed to realize – apparently because none of the litigants mentioned it – was that the same result was mandated by statute.

Article 9 of the Uniform Commercial Code applies to most sales of promissory notes.<sup>10</sup> When it applies, the buyer’s interest in a promissory note is a “security interest,”<sup>11</sup> the buyer

is a “secured party,”<sup>12</sup> and the seller is a “debtor.”<sup>13</sup> Article 9 further provides that “[t]he attachment of a security interest in collateral . . . is also attachment of a security interest in a supporting obligation for the collateral.”<sup>14</sup> In other words, a guaranty follows the principal obligation.<sup>15</sup>

The court did not discuss the transaction by which the Stoneridge Associates note was assigned, so it is difficult to know for sure whether Article 9 governed that transaction. That is because not all assignments of promissory notes are sales. A gratuitous assignment, for example, would not be a “sale,” and hence would not be governed by Article 9.<sup>16</sup> Moreover, some sales of promissory notes are excluded from the scope of Article 9.<sup>17</sup> If the assignment of a promissory note is not governed by Article 9, then Article 9’s rule that a guaranty follows the note would not apply.

However, counsel for Jenzack has reported privately that the transaction was a sale, so in all likelihood, Article 9 applied and statutorily required the result that the court concluded was provided for by the parties’ successors and assigns clause. Even if Article 9 did not apply, the Restatement should yield the same result. After all, a guaranty has no usefulness divorced from the principal obligation to which it applies.<sup>18</sup>

## CONCLUSION

Despite the court’s decision in *Jenzack Partners*, there is still no clear purpose for a successors and assigns clause and no persuasive reason to include one in any agreement. While such a clause is unlikely to do any harm, and might even be used by a court to bolster its rationale for a decision,<sup>19</sup> the fact remains that successors and assigns clauses are incoherent. A transactional lawyer relying on such a clause to serve a particular objective would be better advised to draft language that addresses that objective directly.

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## Notes:

1. Stephen L. Sepinuck, *Successors & Assigns Clauses*, 4 [THE TRANSACTIONAL LAWYER](#) 4 (Apr. 2014).
2. See [id. at 5 & 6](#) (citing Tina Stark and Ken Adams, respectively).
3. [Id. at 6-7](#).
4. [Id. at 7](#).
5. [2020 WL 246428](#) (Conn. 2020).
6. [Id. at \\*4](#) (noting that the allonge to the note did not mention Tine’s guaranty).

7. [Id. at \\*6](#).
8. [Restatement \(Third\) of Suretyship and Guaranty § 13\(5\)](#) (“Except as otherwise agreed or as provided in subsection (1), an assignment by the obligee of its rights against the principal obligor arising out of the underlying obligation operates as an assignment of the obligee’s rights against the secondary obligor arising out of the secondary obligation.”).
9. [2020 WL 246428, at \\*6, n.9](#).
10. U.C.C. § 9-109(a)(3).
11. U.C.C. § 1-201(b)(35).
12. U.C.C. § 9-102(a)(73)(D).
13. U.C.C. § 9-102(a)(28)(B).
14. U.C.C. § 9-203(f).
15. See U.C.C. § 9-102(a)(78) (defining “supporting obligation”). See also § 9-102 cmt. 5f; § 9-203 cmt. 8.
16. See U.C.C. § 9-102(b) (adopting the definition of “sale” in § 2-106); U.C.C. § 2-106(1) (defining “sale” as “the passing of title from the seller to the buyer for a price.”). Unfortunately, U.C.C. § 2-102(1)(a) and (d) define “buyer” and “seller,” respectively, in reference to a transaction in goods, hence there is a slight snag in trying to apply the term “sale” in Article 9 to property other than goods.
17. See U.C.C. § 9-109(d)(4)–(7).
18. Complex issues can arise, however, if a guaranty supports multiple obligations which are separately assigned to different entities. See U.C.C. § 9-203 cmt. 8. But those are issues of priority, not attachment; even in such situations, the guaranty should follow each separately assigned obligation.
19. Given the ubiquitousness of successors and assigns clauses, a transactional lawyer should consider whether a court might – inappropriately – infer something unintended from the absence of such a clause.



## Recent Cases

### SECURED TRANSACTIONS

*In re Polk,*

[2019 WL 7342458](#) (Bankr. M.D. Ga. 2019)

Two transactions structured as a sale of future receivables were really loans secured by receivables because, even though there was a reconciliation provision and the agreement had an indefinite term, the agreement made bankruptcy an event of default, putting liability on the putative seller, and thus provided for guaranteed payment.

*In re Preston,*

[2019 WL 7604710](#) (Bankr. D. Kan. 2019)

A filed financing statement was ineffective to perfect a security interest granted by a debtor whose driver's license displayed his name as "D Dennis" Preston (without a period but with a space), because the financing statement listed in the field for his first personal name "D.Dennis" (with a period and no space) and a search under the debtor's driver's license name failed to disclose the financing statement.

*In re Jarvis,*

[2020 WL 211406](#) (Bankr. W.D.N.C. 2020)

A financing statement listing as secured party the agent of an initial lender, the loan from which the debtor had paid off, was not effective to perfect a security interest that the debtor later granted to a subsidiary of the initial lender. The filed financing statement was neither amended to identify the subsidiary as the secured party nor assigned to the subsidiary. It did not matter that the initial lender might have funded the loan by the subsidiary to the debtor.

*AFK Inc. v. Sonny's Enterprises LLC,*

[2020 WL 43219](#) (S.D. Fla. 2020)

Because the debtor cancelled the orders of its principal customer after a judgment was entered against the debtor, and those orders were replaced by orders with an entity affiliated with the debtor, the principal customer had no liability to the debtor. Consequently, the debtor's secured party had no cause of action against the customer for continuing to pay the affiliated entity after receiving the secured party's instruction to make payment directly to the secured party.

*Shaoxing Daqin Import & Export Co., Ltd. v. Notations, Inc.,*

[2019 WL 6498397](#) (S.D.N.Y. 2019)

Plaintiff brought a successor liability claim against a newly formed entity that purchased the debtor's assets at an Article 9 disposition. Defendant's motion for summary judgment was denied in part. With respect to an implied assumption of liabilities, there was evidence that: (i) the debtor told its customers that they should turn to the buyer after the acquisition; (ii) the buyer is operating out of the same location, employs many of the same employees, and provides the same services; and (iii) the buyer expressly asked the plaintiff to fulfill pending orders placed by the debtor and made payment for those orders. With respect to fraud, there was some evidence that the debtor and the buyer worked in concert to favor one of the debtor's unsecured creditors, which suggests that the consideration the buyer paid might have been inadequate, and that the debtor continued to build up debt very close to the time of the sale. However, summary judgment was granted on the claim of successor liability based on a de facto merger because there was no evidence of continuity of ownership, and on the claim based on the buyer being a mere

continuation of the seller because the debtor continued to exist and there was no identity of ownership.

## BANKRUPTCY ISSUES

*In re John Q. Hammons Fall 2006, LLC,*

[2020 WL 211466](#) (Bankr. D. Kan. 2020)

An oversecured creditor was entitled to post-petition interest at the contractual default rate because the loan agreement provided that an event of default occurs if the debtor or any guarantor files for bankruptcy protection and both the debtor and a guarantor had filed a bankruptcy petition. The contractual default rate of 9.33% – 5% higher than the non-default rate – was enforceable under Missouri law because it was a reasonable liquidated damages clause, not a penalty. The transaction was a sophisticated business loan supported by a securitized real estate mortgage conduit, with certificate holders and tax implications. Such a loan has a reduced market value when it goes into default, as well as some increased costs, not all of which were separately compensated under the loan agreement.

## LENDING, CONTRACTING & COMMERCIAL LITIGATION

*In re 3MB, LLC,*

[2019 WL 6701420](#) (Bankr. E.D. Cal. 2019)

A promissory note calling for interest after maturity at 4% more than the base rate of 6.27% was enforceable. An agreement for a higher interest rate after maturity is not, under California law, a liquidated damages clause that might be an unenforceable penalty. Instead, it provides for an alternative performance and compensates the bank for the lower value of the loan, since it no longer conforms to its expected duration. Even if the clause did provide for liquidated damages, it would still be enforceable because the increase in the interest rate is consistent with similar commercial loans, compensates for the increased risk of nonrecovery, and determining actual damages would be difficult.

*Bank of America v. New England Quality Service, Inc.,*

[2019 WL 6245756](#) (2d Cir. 2019)

A bank's waiver of covenant defaults in loan agreements coupled with its extension of the maturity dates did not waive the bank's right to enforce future defaults. Whenever the Bank waived a covenant default, it did so solely as to the specific loan and the particular covenant breached, and the loan agreements expressly provided that, "[i]f the Bank waives a default, it may enforce a later default." The borrowers' alternative estoppel argument fails for much the same reason; given the bank's statements and the language of the loan agreements, the borrowers could not have reasonably believed that the bank's conduct allowed them to breach covenants in the future.

*Gannett Fleming, Inc. v. Corman Construction, Inc.*,  
[2019 WL 6207616](#) (Md. Ct. App. 2019)

The trial court did not err in enforcing an arbitration clause in the parties' agreement even though the claim was barred by the applicable statute of limitations because the contract clause did not expressly state that claims outside the limitations period were not subject to arbitration. Of course, the arbitrator remains free to decide that the claim is not arbitrable or that the claim is untimely even if the demand for arbitration was not.

*Meuers Law Firm, P.L. v. Reasor's, LLC*,  
[2019 WL 6334273](#) (10th Cir. 2019)

A produce buyer was liable to the trustee of a PACA trust for the full purchase price of produce purchased from a seller that itself was subject to PACA, and could not set off the amount of the rebate that the seller agreed to pay the buyer. The seller's agreement to the setoff was a "transfer" of the seller's receivable and a breach of the PACA trust. The buyer was not a good faith purchaser for value because extinguishment of a preexisting debt is not a transfer for value.

*Langley v. MP Spring Lake, LLC*,  
[834 S.E.2d 800](#) (Ga. 2019)

A term in a residential lease agreement providing that "any legal action against [landlord] must be instituted within one year of the date any claim or cause of action arises" was, despite its broad language, limited to contract claims and did not cover the tenant's premises-liability tort claim.

*In re Motors Liquidating Co.*,  
[943 F.3d 125](#) (2d Cir. 2019)

A buyer that purchased substantially all of a manufacturer's assets at a § 363 sale free and clear of most liabilities but pursuant to an agreement providing that the buyer assumed the manufacturer's liability to third parties for death or injury caused by vehicles manufactured before the sale was not liable for punitive damages for claims relating to defects in those vehicles because punitive damages are not compensatory, and hence are not "for" death or other injury.

*Futuri Real Estate, Inc. v. Atlantic Trustee Services, LLC*,  
[835 S.E.2d 75](#) (Va. 2019)

A mortgagee that contractually subordinated its \$415,000 senior lien to its \$250,000 junior lien did not thereby unintentionally elevate the \$220,000 intermediate lien of a different mortgagee. Instead, the intermediate mortgagee was unaffected by the subordination agreement. As a result, the lien priority was as follows: the junior lien was first, followed by the senior lien to the extent of \$165,000 (\$415,000 – \$250,000), then the intermediate lien, and finally the \$250,000 remainder of the senior lien.

■ ■ ■

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## COMMERCIAL LAW AMICUS INITIATIVE UPDATE

### *Latest Activities – § 501(c)(3) Status – Request for Support*

The Commercial Law Amicus Initiative (“CLAI”) is delighted to make the following announcements.

On October 9, the Internal Revenue Service determined that CLAI qualifies as a tax-exempt charitable organization under § 501(c)(3) of the Internal Revenue Code, and hence donations to CLAI are potentially tax deductible by the donor. This determination will help advance CLAI’s stated mission:

1. To assist the courts in faithfully interpreting and applying the Uniform Commercial Code, other commercial statutes, and related common law, in order to achieve the laws’ underlying policies and to facilitate consistent decision-making by the courts;
2. To advance education at law schools by providing law students with training and practical experience in pro bono advocacy relating to the proper application and interpretation of commercial law; and
3. To offer research and recommendations on matters of commercial law to non-profit organizations such as the American Law Institute and the Uniform Law Commission, in connection with such organizations’ preparation of uniform or model legislation or restatements of the law.

On December 11, 2019, CLAI submitted an *amicus curia* brief in the case of *First State Bank Nebraska v. MP Nexlevel, LLC*, a case pending before the Nebraska Supreme Court. The brief, signed and filed by Professor [Anthony Schutz](#) (University of Nebraska College of Law), was principally authored by Professors [Jennifer S. Martin](#) (St. Thomas University School of Law) and [Stephen L. Sepinuck](#) (Gonzaga University School of Law), with the assistance of students at their respective schools. In the brief, CLAI demonstrates that buyers of accounts are “assignees” within the meaning of § 9-406(a), and that a lower court ruling to the contrary was erroneous. Anyone who wishes to receive a copy of the brief may request it by email to Professor Stephen L. Sepinuck at [sepinuck@gonzaga.edu](mailto:sepinuck@gonzaga.edu).

Oral argument in CLAI’s first case – *State v. Dix* – is scheduled for February 28 at 8:50am (mountain). The case, currently before the Idaho Supreme Court, deals with when a purchaser of goods acquires voidable title to the goods and when such a purchaser has the power to convey good title to a good faith purchaser for value. Oral arguments can be watched live on the court’s web site: [www.idahoptv.org/shows/idahoinsession/judiciary/](http://www.idahoptv.org/shows/idahoinsession/judiciary/) (note, CLAI will not be participating in the oral argument).

Finally, although all of CLAI’s work is performed by volunteers, CLAI needs funds to create and maintain a web site, pay court fees and printing costs associated with the filing of *amicus curiae* briefs, and pay travel expenses incurred to attend or participate in oral argument. Accordingly, **CLAI now gratefully accepts contributions from individuals and organizations who wish to support CLAI’s mission.\*** To make a contribution, please send a check, payable to Commercial Law Amicus Initiative, to Professor Stephen L. Sepinuck at Gonzaga University School of Law, P.O. Box 3528, Spokane, WA 99220.

\* Pursuant to a policy adopted by CLAI’s Board of Directors, CLAI does not accept financial contributions from anyone who: (i) is a party in a judicial proceeding in which CLAI is involved; (ii) controls or is employed by a party in such a proceeding; (iii) represents a party in such a proceeding; or (iii) is employed by or associated with a law firm that represents a party in such a proceeding. The full text of the policy is available from Professor Sepinuck upon request.