

# INDIANA'S REVISED ARTICLE 9 AND OTHER DEVELOPMENTS IN COMMERCIAL AND CONSUMER LAW

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## INTRODUCTION

July 1, 2001 witnessed the long awaited arrival of Revised Article 9 to most of the United States. A culmination of over a decade's work,<sup>1</sup> Revised Article 9 will be in effect in all fifty states plus the District of Columbia as of January 1, 2002.<sup>2</sup> With these major changes to the law of secured transactions, the coming months will be a significant challenge to secured parties, practitioners, and the courts as the transition takes full effect. As Revised Article 9's provisions have been in force for only a short period, few of the unavoidable gaps and ambiguities have received judicial scrutiny. Indiana is not immune from the challenges posed by the adoption of Revised Article 9. Revised Article 9's changes not only represent a departure from numerous provisions in the old Article 9, but also present an additional hazard for many parties in Indiana because of several non-uniform amendments to the revised article.

Space does not permit a full treatise on the ramifications of Revised Article 9. Truly, others have already risen to the task.<sup>3</sup> Instead, my objective in this Article is to provide a sufficient framework of the present filing procedures in Indiana and to highlight and explain those provisions in which the Indiana General Assembly has departed from the uniform article. Also, reference both to comparable state departures from the uniform act and to Revised Article 9's official comments will be provided where applicable.

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1. The Permanent Editorial Board of the Uniform Commercial Code (U.C.C.) established a committee in 1990 to study the need for revising Article 9. See Donald W. Garland, *Revised Article 9: Understanding the Changes to Secured Transactions*, 64 TEX. B.J. 974, 974 (2001). Revised Article 9 was promulgated by the National Conference of Commissioners on Uniform State Law (N.C.C.U.S.L.) in 1998. See Ingrid Michelsen Hillinger & Michael G. Hillinger, *2001: A Code Odyssey (New Dawn for the Article 9 Secured Creditor)*, 106 COM. L.J. 105, 105 (2001).

2. New York, New Jersey, and Massachusetts enacted Revised Article 9 just days before the July 1, 2001 deadline. In addition, four states pushed forward the effective date of Revised Article 9 to allow more time for their filing offices to adjust to the changes. Connecticut's law becomes effective on October 1, 2001. Alabama, Florida, and Mississippi represent the final three states to come on board with effective dates of January 1, 2002. See Press Release, National Conference of Commissioners on Uniform State Laws, States Uniformly Enact U.C.C. 9 Revisions (July 2, 2001), available at <http://www.nccusl.org/nccusl/pressreleases/pr1-07-01.asp> (last visited Dec. 5, 2001).

3. See, e.g., JAMES J. WHITE & ROBERT S. SUMMERS, UNIFORM COMMERCIAL CODE: 1999 ARTICLE 9 SUPPLEMENT (4th ed. Supp. 1999); THE NEW ARTICLE 9: UNIFORM COMMERCIAL CODE (Corrine Cooper ed., 2d ed. 2000).

In the second part of this Article, I will discuss other major legislative developments and case law in the field of commercial law during the survey period.<sup>4</sup> Included in this discussion is an important, though questionably decided, opinion from the Indiana Supreme Court regarding payday loan creditors.<sup>5</sup>

### I. INDIANA'S REVISED ARTICLE 9

In a nutshell, Revised Article 9 makes the law of secured transactions more certain for the experienced practitioner and more daunting for the novice. As White and Summers explain in their treatise, "length and complexity" are the byproduct of resolving the ambiguities of the old Article 9.<sup>6</sup> Some of the major developments, discussed in further depth below, include an expansion of Article 9's scope, new priority rules, changes to choice-of-law rules, and changes to the enforcement provisions, to name but a few.

#### A. *The Scope of Article 9*

Article 9's basic scope provision, Indiana Code section 26-1-9.1-109,<sup>7</sup> sweeps a huge array of transactions into the fold. As subsection (a)(1) states, generally "a transaction, regardless of its form, that creates a security interest in personal property or fixtures by contract" is governed by Article 9.<sup>8</sup> The creation of a security interest makes Article 9 applicable, regardless of the transaction's form or the name parties assign to it.<sup>9</sup> Reference to Indiana Code section 26-1-1-201(37) must be made for the definition of "security interest."

Generally speaking, Revised Article 9 provides for sixteen categories of collateral that can be subject to a security interest. They are:

- Consumer Goods
- Farm Products
- Inventory
- Equipment
- Instruments
- Documents
- Accounts
- Deposit Accounts

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4. The survey period is from October 1, 2000 to September 31, 2001, although more recently decided cases will be included in this Article to make it as timely as possible.

5. The Indiana Supreme Court was still suffering from the onslaught of direct criminal appeals during the survey period. As the recently amended jurisdiction of the Indiana Supreme Court ends mandatory review of criminal cases imposing sentences greater than fifty years, practitioners should look to the Indiana Supreme Court to take a more direct role in shaping consumer and commercial law. See IND. CONST. art. VII, § 4 (amended 2000).

6. WHITE & SUMMERS, *supra* note 3, at 33.

7. Formerly IND. CODE § 26-1-9-102 (1995).

8. IND. CODE § 26-1-9.1-109(a)(1) (Supp. 2001).

9. See U.C.C. § 9-109 cmt. 2 (2000).

- Health Care Insurance Receivables
- Chattel Paper
- Electronic Chattel Paper
- Letter of Credit Right
- Commercial Tort Claims
- General Intangibles
- Investment Property
- Proceeds<sup>10</sup>

The above list, with the exception of one category, is mutually exclusive (i.e., the type of collateral does not change if in the same person's hands). The one category of collateral that can present problems to secured creditors is farm products. For instance, a farmer that grows and harvests corn possesses farm products. But after processing the corn, it converts into inventory. A secured party must be careful with regard to taking a security interest in a farmer's farm products. An imprecise or under-inclusive description of the collateral in the security interest may result in an invalid security interest.<sup>11</sup>

Indiana has made two non-uniform amendments to Article 9's scope provision. First, the uniform Article 9, subsection 9-109(d)(8) excludes several transactions, including:

a transfer of an interest in or an assignment of a claim under a policy insurance, other than an assignment by or to a health-care provider of a

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10. See IND. CODE §§ 26-1-9.1-102(a)(23) (Supp. 2001) (defining "consumer goods" as "goods that are used or bought for use primarily for personal, family, or household purposes"); 26-1-9.1-102(a)(34) (defining "farm products"); 26-1-9.1-102(a)(48) (defining "inventory"); 26-1-9.1-102(a)(33) (defining "equipment," a catch-all provision covering "goods other than inventory, farm products, or consumer goods"); 26-1-9.1-102(a)(47) (defining "instrument"); 26-1-9.1-102(a)(30) (defining "document" as a "document of title," which functions as a substitute for the actual goods (i.e., warehouse receipts, bills of lading)); 26-1-9.1-102(a)(2) (defining "account"); 26-1-9.1-102(a)(29) (defining "deposit account"); 26-1-9.1-102(a)(46) (defining "health-care-insurance receivable" as an "interest in or claim under a policy of insurance that is a right to payment of a monetary obligation for health-care goods or services provided"); 26-1-9.1-102(a)(11) (defining "chattel paper"); 26-1-9.1-102(a)(31) (defining "electronic chattel paper"); 26-1-9.1-102(a)(51) (defining "letter-of-credit right"); 26-1-9.1-102(a)(13) (defining "commercial tort claim" and excluding "damages arising out of personal injury to or the death of an individual"); 26-1-9.1-102(a)(42) (defining "general intangible"); 26-1-9.1-102(a)(49) (defining "investment property" as a "security, whether certificated or uncertificated, security entitlement, securities account, commodity contract, or commodity account"); 26-1-9.1-102(a)(64) (defining "proceeds").

11. A problem Revised Article 9 does not address is the whether a document labeled "lease" is a lease outside of Article 9's provisions or a security agreement. While a "nervous lessor" is permitted to file a financing statement under U.C.C. § 9-505, filing is not required. The distinction between a lease and a security agreement can be very tricky, and a careless secured party could find himself out in the cold in the event of a priority dispute. See generally WHITE & SUMMERS, *supra* note 3, at 39-50 (describing in detail the problem of differentiating between leases and security agreements).

health-care-insurance receivable and any subsequent assignment of the right to payment, but Sections 9-315 and 9-322 apply with respect to proceeds and priorities in proceeds.<sup>12</sup>

In its place, Indiana has carved out an exception in subsection 9-109(a)(7) to provide that “a transfer of an interest or a claim in a contractual right of a person to receive commissions or other compensation payable by an insurer” is an interest that falls within Revised Article 9.<sup>13</sup> Indiana’s subsection 9-109(d)(8) is amended to reflect these changes.<sup>14</sup>

The second non-uniform change is to section 9-109’s preemption provisions. Under the uniform 9-109(c)(2) and (3), Article 9 does not apply to the extent that

(2) another statute of this State expressly governs the creation, perfection, priority, or enforcement of a security interest created by this State or a governmental unit of this State;

(3) a statute of another State, a foreign country, or a governmental unit of another State or a foreign country, other than a statute generally applicable to security interests, expressly governs creation, perfection, priority, or enforcement of a security interest created by the State, country, or governmental unit . . . .<sup>15</sup>

These provisions provided that Article 9 would apply to security interests created by state or foreign governmental units except to the extent another statute governed the issue. Subsection (c)(2) would defer to all forum state statutes while subsection (c)(3) would defer to foreign statutes only if they contained rules specifically applicable to the security interests of the governmental unit.<sup>16</sup> Indiana’s revised Article 9 eliminates both of these provisions.<sup>17</sup> As such, subsection 9-109(c) provides that only federal law preempts Article 9.

### *B. Creation and Attachment of the Security Interest*

A secured party has two primary concerns. First, the secured party must ensure the enforceability of the security interest against the debtor—through creation of a security interest and attachment. Second, the secured party must ensure the priority of his interest against other third parties—through perfection. Generally, attachment and perfection are accomplished through the use of two forms: the security agreement, an agreement between the debtor and the secured party; and the financing statement, a filed form announcing the secured parties’

12. U.C.C. § 9-109(d)(8) (2001).

13. IND. CODE § 26-1-9.1-109(a)(7) (Supp. 2001).

14. No other state has made a comparable change to its Article 9 scope provision. See PENELOPE L. CHRISTOPHOROU ET AL., UNDER THE SURFACE OF REVISED ARTICLE 9: NON-UNIFORMITY AND FILING OFFICE PROCEDURES 3-18 (2001).

15. U.C.C. § 9-109(c)(2)-(3) (2001).

16. See *id.* cmt. 9.

17. Florida, Nevada, and West Virginia made comparable changes. See CHRISTOPHOROU ET AL., *supra* note 14, at 6, 11, 17-18.

security interest to the rest of the world.

Security interests “attach” when they become enforceable against the debtor with respect to the collateral specified in the security agreement.<sup>18</sup> The requirements for attachment are set out in Indiana Code section 26-1-9.1-203(b)-(c) (Supp. 2001). Those provisions provide:

(b) Except as otherwise provided in subsections (c) through (i), a security interest is enforceable against the debtor and third parties with respect to the collateral only if:

(1) value has been given;

(2) the debtor has rights in the collateral or the power to transfer rights in the collateral to a secured party; and

(3) one (1) of the following conditions is met:

(A) The debtor has authenticated a security agreement that provides a description of the collateral and, if the security interest covers timber to be cut, a description of the land concerned.

(B) The collateral is not a certificated security and is in the possession of the secured party under IC 26-1-9.1-313 pursuant to the debtor’s security agreement.

(C) The collateral is a certificated security in registered form and the security certificate has been delivered to the secured party under IC 26-1-8.1-301 pursuant to the debtor’s security agreement.

(D) The collateral is deposit accounts, electronic chattel paper, investment property, or letter-of-credit rights, and the secured party has control under IC 26-1-9.1-104, IC 26-1-9.1-105, IC 26-1-9.1-106, or IC 26-1-9.1-107 pursuant to the debtor’s security agreement.

As the official comments state, a valid security agreement requires the creditor give value, the debtor retains rights in the collateral, and an agreement plus “satisfaction of an evidentiary requirement.”<sup>19</sup> The failure to properly attach results in an unsecured status for the creditor.

Section 1-201(44) provides the definition of “value.”<sup>20</sup> Any consideration sufficient to support a simple contract and a preexisting debt satisfy the requirement of value, but attachment will not occur by gift. Because the security agreement involves a conveyance of a property interest, the debtor must also have some rights in the collateral. Section 9-204 provides that both after-acquired property clauses (a present loan for future collateral) and future advance clauses (present collateral for a future loan) are permissible.<sup>21</sup> Nevertheless, no attachment occurs until either the debtor acquires an interest in the property or the secured party gives value.

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18. U.C.C. § 9-203(a) (2001).

19. *Id.* cmt. 2.

20. IND. CODE § 26-1-1-201(44) (1998).

21. Section 9-204(b) is an exception for after-acquired property clauses. In the case of consumer goods or commercial tort claims, the debtor must generally acquire rights in them within ten days after the secured party gives value. *Id.* § 26-1-9.1-204(b) (Supp. 2001).

The final "evidentiary requirement" can be accomplished in a number of ways. The first and simplest would be the secured party's actual possession of the collateral.<sup>22</sup> A pawnshop would be a good example of this situation. As is discussed later, possession also works to perfect a secured party's security interest, so possession can work the two-fold purpose of enforcement of a security interest and perfection. Second, if the collateral is deposit accounts, electronic chattel paper, letter-of-credit right, or investment property, the security agreement may be evidenced by "control."<sup>23</sup> The third and most common way to satisfy this evidentiary requirement is through a security agreement.

A security agreement is "an agreement that creates or provides for the security interest."<sup>24</sup> It is both a contract and a deed conveying a property interest.<sup>25</sup> Third parties look to the security agreement to determine what collateral is covered, and therefore encumbered, and what collateral is available. The sufficiency requirements of the collateral's description in the security agreement, governed by section 9-108, is different than that in the financing statement, governed by section 9-504.<sup>26</sup> The description is sufficient if it "reasonably identifies what is described" or is "objectively determinable."<sup>27</sup> Listing the type of collateral (i.e., consumer goods, inventory, etc.) is sufficient, but super-generic descriptions such as "all the debtor's assets" are deficient.<sup>28</sup>

In addition to a sufficient description, a security agreement must also be "authenticated."<sup>29</sup> As defined by section 1-201(39), "signed" includes "any symbol executed or adopted by a party with present intention to authenticate a writing." As set out in section 9-102(a)(7), to "authenticate" includes the definition of "signed," but is expanded to allow for electronic and other non-written forms of security agreements.

Indiana made no material amendments to the uniform Revised Article 9. Following these procedures will establish a secured party's rights against the debtor. The additional step of perfection is required to establish lien priority against third parties.

### C. Perfection

Following the creation of a security interest and attachment, the secured party must then ensure perfection. Relevant only to third parties, perfection is the process by which secured parties, either through filing a finance statement, taking possession of the collateral, or taking "control" of the collateral, establish

22. *See id.* § 26-1-9.1-203(b)(3)(B).

23. *See id.* § 26-1-9.1-203(b)(3)(D).

24. U.C.C. § 9-102(a)(73) (2001).

25. *See* WHITE & SUMMERS, *supra* note 3, at 34.

26. *See id.* at 74. The description requirements for security agreements are more stringent than those for financing statements. *See id.* at 75.

27. *See* IND. CODE § 26-1-9.1-108 (Supp. 2001).

28. *See id.*

29. *See id.* § 26-1-9.1-203(b)(3)(A).

lien priority. In specific instances, perfection is automatic. The rules for perfection are generally found between U.C.C. sections 9-308 and 9-316.

1. *Automatic Perfection.*—Indiana Code section 26-1-9.1-309 provides that certain security interests are perfected automatically upon attachment. The most important of which is a purchase money security interest (PMSI) in consumer goods. A PMSI is created when a secured party provides money to the debtor that is used to acquire an interest in the collateral, and consumer goods are defined as “goods that are used or bought for use primarily for personal, family or household purposes.”<sup>30</sup> Other important security interests that are automatically perfected include the sale of payment intangibles or promissory notes and assignments of accounts, health care insurance receivables, or payment intangibles.<sup>31</sup>

2. *Perfection by Possession.*—Subsection 9-313(a) provides that a secured party can perfect a security interest in negotiable instruments, goods, instruments, money, or tangible chattel paper through possession.<sup>32</sup> Perfection of a security interest in certified securities is accomplished by taking delivery of the certified

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30. *Id.* § 26-1-9.1-102(23).

31. *See id.* § 26-1-9.1-309. That section reads as follows:

The following security interests are perfected when they attach:

(1) A purchase-money security interest in consumer goods, except as otherwise provided in IC 26-1-9.1-311(b) with respect to consumer goods that are subject to a statute or treaty described in IC 26-1-9.1-311(a).

(2) An assignment of accounts or payment intangibles which does not by itself or in conjunction with other assignments to the same assignee transfer a significant part of the assignor's outstanding accounts or payment intangibles.

(3) A sale of a payment intangible.

(4) A sale of a promissory note.

(5) A security interest created by the assignment of a health-care-insurance receivable to the provider of the health-care goods or services.

(6) A security interest arising under IC 26-1-2-401, IC 26-1-2-505, IC 26-1-2-711(3), or IC 26-1-2.1-508(5), until the debtor obtains possession of the collateral.

(7) A security interest of a collecting bank arising under IC 26-1-4-210.

(8) A security interest of an issuer or nominated person arising under IC 26-1-5.1-118.

(9) A security interest arising in the delivery of a financial asset under IC 26-1-9.1-206(c).

(10) A security interest in investment property created by a broker or securities intermediary.

(11) A security interest in a commodity contract or a commodity account created by a commodity intermediary.

(12) An assignment for the benefit of all creditors of the transferor and subsequent transfers by the assignee thereunder.

(13) A security interest created by an assignment of a beneficial interest in a decedent's estate.

*Id.*

32. *Id.* § 26-1-9.1-313.

securities.<sup>33</sup> Logically, possession is ineffective for certain categories of collateral such as accounts and general intangibles because the law does not recognize their embodiment in a tangible thing. Subsection 9-313 is a complex provision, and because possession comports poorly with modern commercial transactions, the reader is left to parse out perfection by possession elsewhere.

3. *Perfection by Control.*—Control is roughly the equivalent of possession described above. Under subsection 9-310(b)(8), a secured party is permitted to control deposit accounts, electronic chattel paper, investment property, and letter-of-credit rights for purposes of perfection. Generally speaking, control is the exclusive means for perfecting security interests in deposit account and letter-of-credit rights. Subsections 9-104 through 9-107 describe the procedures to acquiring “control” of these types of collateral.

4. *Perfection by Filing.*—The last and by far the most common method for perfecting a security interest is by filing a financing statement. White and Summers estimate that over ninety percent of security interests are perfected by filing a financing statement.<sup>34</sup> Subsections 9-502, 9-516 and 9-520 are the key provisions covering financing statements.

Subsection 9-502 sets out the three pieces of information that are essential to make the financing statement effective. They are (1) the name of the debtor, (2) the name of the secured party, and (3) a description of the collateral covered by the financing statement.<sup>35</sup> It is no longer essential that a financing statement include the debtor’s signature or the addresses of the parties, as did former subsection 9-402(1). These three pieces of information are the absolute requirements of any financing statement; deficiency in any will result in an ineffective filing.

Indiana made two non-uniform changes to section 9-502. First, 9-502(e) states that to the extent other provisions of the Indiana Code require the identification of the preparer of the financing statement, “the failure of the financing statement to identify the preparer does not affect the sufficiency of the financing statement.”<sup>36</sup> Second, section 9-502(f) requires that the secured party provide the debtor with a copy of the financing statement within thirty days of

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33. *See id.*

34. WHITE & SUMMERS, *supra* note 3, at 102.

35. IND. CODE § 26-1-9.1-502(a) (1998). Subsection 9.1-502(b) provides additional requirements to cover real property related collateral (e.g., fixtures). For this collateral, the financing statement must also:

- (1) indicate that it covers this type of collateral;
- (2) indicate that it is to be filed in the real property records;
- (3) provide a description of the real property to which the collateral is related that is sufficient to give constructive notice of a mortgage under the law of this state if the description were contained in a record of the mortgage of the real property; and
- (4) if the debtor does not have an interest or record in the real property, provide the name of a record owner.

*Id.*

36. *Id.* § 26-1-9.1-502(e).

filing. But again, a secured party's failure to meet this requirement does not affect the sufficiency or effectiveness of the financing statement.<sup>37</sup>

Subsection 9-503 provides what is required of a financing statement to give the name of the debtor.<sup>38</sup> For registered organizations, the financing statement is sufficient "only if the financing statement provides the name of the debtor indicated on the public record of the debtor's jurisdiction of organization which shows the debtor to have been organized."<sup>39</sup> In most other cases, the financing statement is sufficient: "(A) if the debtor has a name, only if it provides the individual or organizational name of the debtors; and (B) if the debtor does not have a name, only if it provides the names of the partners, members, associates, or other persons comprising the debtor."<sup>40</sup> Because the filings are indexed according to the debtor's name, a precise recitation of the debtor's name is absolutely crucial to provide adequate notice to third parties. Subsection 9-503(c) provides that trade names are insufficient, although if a search using the filing office's standard search logic would turn up the debtor's name, it would be sufficient.<sup>41</sup> The test for determining whether an error in the debtor's name is fatal is whether the error makes the financing statement "seriously misleading."<sup>42</sup> Importantly, section 9-507 provides that a financing statement must only satisfy the requirements of 9-502 *at the time of filing*. Subsequent events that cause the financing statement to become seriously misleading generally do not affect the financing statement's effectiveness.<sup>43</sup>

Subsection 9-504, establishing the requirements for a financing statement's description of the collateral, adopts the standard from section 9-108, covering security agreements, with one important caveat.<sup>44</sup> If the financing statement provides that it "covers all assets or all personal property" of the debtor, it is sufficient.<sup>45</sup> Otherwise, applying the standard set forth in section 9-108, a description of collateral is sufficient if it "reasonably identifies what is

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37. *Id.* § 26-9.1-502(f).

38. *Id.* § 26-1-9.1-503.

39. *Id.* § 26-1-9.1-503(a)(1).

40. *Id.* § 26-1-9.1-503(a)(4).

41. *See id.* § 26-1-9.1-506(c). This provision may save an otherwise insufficient financing statement.

(c) If a search of the records of the filing office under the debtor's correct name, using the filing office's search logic, if any, would disclose a financing statement that fails to sufficiently provide the name of the debtor in accordance with IC 26-1-9.1-503(a), the name provided does not make the financing statement seriously misleading.

*Id.*

42. *Id.*

43. *See id.* § 26-1-9.1-507. Nevertheless, if the debtor changes his name after filing, a financing statement is effective to perfect a security interest in collateral acquired within four months after the name-change. An amendment to the financing statement must be filed to perfect collateral acquired after the four-month window. *See id.* § 267-1-9.1-507(c).

44. *See id.* §§ 26-1-9.1-108, 26-1-9.1-504.

45. *See id.* § 26-1-9.1-504(2).

described."<sup>46</sup>

Section 9-516(b) sets out additional information that the financing statement should include. The secured party, in addition to the requirements of section 9-502, is required to:

- (A) provide a mailing address for the debtor;
- (B) indicate whether the debtor is an individual or an organization; or
- (C) if the financing statement indicates that the debtor is an organization, provide:
  - (i) a type of organization for the debtor;
  - (ii) a jurisdiction of organization for the debtor; or
  - (iii) an organizational identification number for the debtor or indicate that the debtor has none.<sup>47</sup>

Nevertheless, if the filing office accepts a financing statement that fails to meet the requirements of section 9-516 but satisfies section 9-502, the financing statement will be valid. But the opposite is not true. Any deficiency in section 9-502 requirements will render the financing statement ineffective. Moreover, if a filing statement satisfies the requirements of both 9-502 and 9-516(b) and the filing office refuses to accept it, an effective filing has occurred despite the rejection against everyone except "a purchaser of the collateral which gives value in reasonable reliance upon the absence of the record from the files."<sup>48</sup>

Subsection 9-501 specifies the appropriate filing locations. Generally speaking, the appropriate location for filing a financing statement is with the office of the secretary of state unless the collateral is real estate related, in which case the secured party should do a local filing.<sup>49</sup> Indiana made one non-uniform change to this section. Section 9-501(c)-(k) generally provides that until July 1, 2002, a secured party is allowed to make a local filing for farm products, farm equipment and accounts, or general intangibles arising from or relating to the sale of farm products.<sup>50</sup>

The adoption of Revised Article 9 represents a major challenge for Indiana practitioners. In addition to several non-uniform changes peculiar to Indiana, Revised Article 9 makes several significant changes to the prior version. By the time of this Article's publication, the transition rules will have likely worked their course. While Revised Article 9 is now the most complete and thorough U.C.C. section, practitioners should look to the appellate courts over the coming months to begin to tackle Article 9's difficult provisions.

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46. *See id.* § 26-1-9.1-108(a).

47. *Id.* § 26-1-9.1-516(b).

48. *Id.* § 26-1-9.1-516(d).

49. *Id.* § 26-1-9.1-501.

50. *Id.* § 26-1-9.1-501(c)-(k).

## II. OTHER COMMERCIAL AND CONSUMER LAW DEVELOPMENTS

### A. *Indiana Supreme Court*

The Indiana Supreme Court handed down a major decision against short-term, consumer loan businesses operating in Indiana. In *Livingston v. Fast Cash USA, Inc.*,<sup>51</sup> the United States District Courts for the Northern and Southern District of Indiana<sup>52</sup> certified the following question to the Indiana Supreme Court: “[I]s the minimum loan finance charge permitted by Indiana Code section 24-4.5-3-508(7), when charged by a licensed supervised lender, limited by Indiana Code section 24-4.5-3-508(2) or Indiana Code section 35-45-7-2?”<sup>53</sup> The Court answered in the affirmative. Justice Rucker authored the majority decision, in which Justice Boehm concurred in a separate opinion. Chief Justice Shepard filed the “loan” dissenting opinion.

While the facts of the case were not difficult, the interpretation of the badly worded statute was. The plaintiffs were consumers who had taken out short-term loans (anywhere from seven days to two weeks) ranging between fifty to \$400 from businesses engaged in providing “payday loans.”<sup>54</sup> The borrowers wrote post-dated checks for the principal and a fixed finance charge, ranging from fifteen to thirty-three dollars. Borrowers would incur another charge if they had insufficient funds when the loan came due.<sup>55</sup>

Plaintiffs brought suit against the lenders in federal court, alleging that although the lenders charged the minimum loan finance apparently permitted by Indiana Code section 24-4.5-3-508(7),<sup>56</sup> the finance charge exceeded the maximum annual percentage rate allowable under either Indiana Code section 24-4.5-3-508(2)<sup>57</sup> or section 35-45-7-2.<sup>58</sup> In other words, the plaintiffs argued

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51. 753 N.E.2d 572 (Ind. 2001).

52. Contrary to the court’s opinion, the cases pending in the Southern and Northern District Courts were dismissed without prejudice. *Livingston* was dismissed without prejudice on March 9, 2001. The parties had forty-five days to re-open the case following the supreme court’s decision on the certified question. The lead case of *Livingston v. Fast Cash USA, Inc.* was re-opened on September 13, 2001, and the case is again pending before Magistrate Judge Godich. Case information is available at <http://www.insd.uscourts.gov/caseinfo.htm> (last visited May 28, 2002).

53. 753 N.E.2d at 574.

54. *See id.*

55. *See id.* For instance, if the borrower took out a two-week loan and could not cover her check when due, the lender would issue a new loan for another two weeks (essentially for the money previously loaned) with additional finance charges. *See id.*

56. Regarding supervised loans not made pursuant to a revolving loan account, Indiana’s Uniform Consumer Credit Code (U.C.C.C.) states that a “lender may contract for and receive a minimum loan finance charge of not more than thirty dollars.” IND. CODE § 24-4.5-3-508(7) (1998). This statute is indexed for inflation, and at the time of suit, the figure had an adjusted value of thirty-three dollars.

57. The statute states the following:

(2) The loan finance charge, calculated according to the actuarial method, may not

that charging a thirty-three dollar finance charge on a two-week loan far exceeded the allowable loan finance charge annual percentage rate (APR), thirty-six percent, for loans under three hundred dollars.

Two seemingly conflicting provisions governing the finance charge lenders can assess are at the root of the argument, one limiting the APR and the other allowing a specific minimum finance charge. The applicable provision of subsection 3-508(2) states, "The loan finance charge, calculated according to the actuarial method, may not exceed the equivalent of the greater of . . . thirty six percent (36%) per year on that part of the unpaid balances of the principal which is three hundred dollars (\$300) or less . . ." <sup>59</sup> But in subsection 3-508(7), the statute goes on to provide: "With respect to a supervised loan not made pursuant to a revolving loan account, the lender may contract for and receive a minimum loan finance charge of not more than thirty dollars (\$30)." <sup>60</sup>

In reconciling these two provisions, the court took three opposing views. The majority opinion reasoned that subsection 3-508(7) was based on the assumption that loans would last at least one year, thus short-term lenders are prevented from taking advantage of this subsection. <sup>61</sup> Justice Boehm agreed that the statute was based upon an assumption, but instead reasoned that the provisions first assumes lawful loans (i.e., that lenders cannot contract for loan finance charges greater than those set by subsection 3-508(2) then seek refuge in subsection 3-508(7)). <sup>62</sup> Chief Justice Shepard, in dissent, took the most straightforward view of the statute. He reasoned that the legislature intended that

exceed the equivalent of the greater of either of the following:

(a) the total of:

- (i) thirty-six percent (36%) per year on that part of the unpaid balances of the principal which is three hundred dollars (\$300) or less;
- (ii) twenty-one percent (21%) per year on that part of the unpaid balances of the principal which is more than three hundred dollars (\$300) but does not exceed one thousand dollars (\$1,000); and
- (iii) fifteen percent (15%) per year on that part of the unpaid balances of the principal which is more than one thousand dollars (\$1,000); or

(b) twenty-one percent (21%) per year on the unpaid balances of the principal.

*Id.* § 24-4.5-3-508(2).

58. Indiana's loansharking statute states the following:

A person who, in exchange for the loan of any property, knowingly or intentionally receives or contracts to receive from another person any consideration, at a rate greater than two (2) times the rate specified in [Indiana Code section] 24-4.5-3-508(2)(a)(i), commits loansharking, a Class D felony. However, loansharking is a Class C felony if force or the threat of force is used to collect or to attempt to collect any of the property loaned or any of the consideration for the loan.

*Id.* § 35-45-7-2.

59. *Id.* § 24-4.5-3-508(2).

60. *Id.* § 24-4.5-3-508(7).

61. *Livingston v. Fast Cash USA, Inc.*, 753 N.E.2d 572, 576-77 (Ind. 2001).

62. *Id.* at 578-79 (Boehm, J., concurring).

“if the loan period is so short or the loan so small that [the loan finance] rate might produce just a few dollars, a minimum of \$33 may be charged.”<sup>63</sup> In one of the most quotable lines of the survey period, Chief Justice Shepard expressed the court’s frustration in parsing through this badly crafted statute. He proposed: “It has been awhile since we last encountered a statute in such serious need of revision. Our federal cousins might take comfort in knowing that, like them, we found the task of parsing its various provisions very difficult (but had nowhere else to send out for help).”<sup>64</sup>

To understand the disagreement among the opinions, it is necessary to frame these two conflicting provisions in their historical context. Curiously, none of the three opinions discussed the road subsection 3-508(7) traveled before settling in its present position. From 1971 until today, the basic idea encompassed by 3-508(7) has taken on various forms and appeared in different provisions of the U.C.C.C.

Indiana’s U.C.C.C. was enacted in 1971. As originally enacted, subsection 3-508 contained only a provision governing maximum loan finance charge percentage rates.<sup>65</sup> Instead, the provision capping a specific finance charge dollar amount was found in the U.C.C.C.’s prepayment section.<sup>66</sup> In pertinent part, it stated:

[T]he lender may collect or retain a minimum charge within the limits stated in this subsection if the loan finance charge earned at the time of prepayment is less than any minimum charge contracted for. The minimum charge may not exceed the amount of loan finance charge contracted for, or five dollars (\$5) in a transaction which had a principal of seventy-five (\$75) or less, or seven dollars and fifty cents (\$7.50) in a transaction which had a principal of more than seventy-five dollars (\$75).<sup>67</sup>

From its beginning, this provision worked to guarantee a minimum finance charge to lenders, either the “loan finance charge contracted for” or in the event of prepayment, a set dollar amount.

In 1982, subsection 3-508(7) was crafted by the Indiana General Assembly. In whole the section stated:

Notwithstanding subsection (2) [subsection 3-508(2)], with respect to a supervised loan not made pursuant to a revolving loan account, the lender may contract for and receive a minimum loan finance charge of not more than five dollars (\$5) when the original principal balance of the

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63. *Id.* at 580 (Shepard, C.J., dissenting). He went on to say, however, that the practice of charging a new fee each time a loan rolled over violated Indiana Code § 24-4.5-3.509, prohibiting sequential fee-charging practices. *Id.* at 581.

64. *Id.*

65. *Id.* § 24-4.5-3.508 (1971).

66. *Id.* § 24-4.5-3-210 (1971) (amended 1972).

67. *Id.* § 24-4.5-3-210(2).

obligation does not exceed seventy-five dollars (\$75), or not more than seven dollars fifty cents (\$7.50) when the original principal balance of the obligation exceeds seventy-five dollars (\$75).<sup>68</sup>

As initially drafted, subsection 3-508(7) acted as an explicit exception to 3-508(2)'s percentage limit on loan finance charges. Subsection 3-210(2) regarding prepayment remained the same. As such, the two provisions worked together. For loans over seventy-five dollars, lenders could impose a minimum finance charge of \$7.50, *regardless of the duration of the loan*. Accordingly, under subsection 3-210(2), lenders could collect up to this \$7.50 figure in the event of prepayment.

For ten years, these two provisions co-existed. In 1992, both were amended. Subsection 3-210(2) was completely reworked to its present form. It reads:

Upon prepayment in full of a consumer loan, refinancing, or consolidation, other than one (1) under a revolving loan account, if the loan finance charge earned is less than any permitted minimum loan finance charge (IC 24-4.5-3-201(6) or IC 24-4.5-3-508(7)) contracted for, whether or not the consumer loan, refinancing, or consolidation is precomputed, the lender may collect or retain the minimum loan finance charge, as if earned, not exceeding the loan finance charge contracted for.<sup>69</sup>

In the same year, subsection 3-508(7) was amended to the following: "Notwithstanding subsection (2), with respect to a supervised loan not made pursuant to a revolving loan account, the lender may contract for a minimum loan finance charge of not more than thirty dollars (\$30)."<sup>70</sup> The two provisions were changed significantly in 1992, but their basic effect remained the same. One stood as a clear exception to subsection 3-508(2)'s APR percentage limitation by establishing a specific dollar amount which lenders could collect, *regardless of amount or duration*. The other provided that, in the event of prepayment, lenders could collect the lesser of the amount contracted for or \$30, but recognized the lenders' ability to charge up to this maximum dollar amount.

The latest amendment to these two provisions occurred in 1994. The General Assembly, most likely acting under the auspices of Legislative Services, made a few changes to the language of the entire subsection 3-508, all of which appear to be minor word and nonsubstantive changes. One of these changes was to subsection 3-508(7). The words "notwithstanding subsection (2)" were deleted.<sup>71</sup> The whole of the other changes made to subsection 3-508 were very

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68. 1982 Ind. Acts 149, sec. 4.

69. 1992 Ind. Acts 14, sec. 30 (codified as amended at IND. CODE § 24-4.5-3-210(2) (1998)).

70. *Id.* at 4.

71. IND. CODE ANN. § 24-4.5-3-508 (West 1998). The historical and statutory notes in West's Annotated Code state that the 1994 changes "amended the section by deleting notwithstanding IC 24-4.5-1-106(1), from Subsec. (6); deleting notwithstanding subsection (2), from Subsec. (7), and making other nonsubstantive changes." *Id.*

minor, deleting gender specific pronouns and unnecessary cross-references. It seems highly unlikely that the changes made to 3-508(7) were ever intended to change the substantive meaning of the provision.

So what was the purpose and effect of this amendment? First, it is most probable that Legislative Services thought that the “notwithstanding subsection (2)” language was superfluous, and did not fully recognize the effect this amendment would have. However, one does not delete an exception simply by deleting its reference point. For instance, if “rule one” says “the sky is blue” and “rule two” says “notwithstanding rule one, the sky is pink on Sunday,” the force and effect of “rule two” is not lessened by deleting reference to “rule one.”

Both before and after the 1994 amendment, subsection 3-508(7) acts as an exception to 3-508(2). For nearly twenty years, the two provisions have acted harmoniously to set a specific, minimum dollar amount for loan finance charges, which is then cross-referenced in the prepayment provision. Deleting the language “notwithstanding subsection (2)” from 3-508(7) along with other minor and nonsubstantive language changes should not have meant an end to the general exception to 3-508(2). Remarkably, the majority of the court thought it should.

The majority turned the seemingly clear meaning of the two provisions on its head and said that these two provisions anticipated only one-year or longer loans, which in essence limits 3-508(7) to 3-210(2)'s construction and function, rather than the other way around. The major fallacy in the majority's opinion is a comparison of the 1971 U.C.C.C. with its present form without sufficient analysis of the effects the various amendments worked during the interceding thirty years. From its inception, 3-508(7) has been an exception to 3-507(2), unaffected by the language of 3-210(2). Justice Rucker, writing for the majority, offered:

Subsection 3-508 has been amended three times since 1971. However, each amendment has referred to the prepayment section 3-210. At present, subsection 3-508 as well as subsection 3-210 works substantially the same as it has always worked: a lender is allowed to charge up to the amount specified in subsection 3-508(7), limited by the total finance charge that was originally provided for in the contract. Hence, a two-week \$200 loan still generates \$2.77 in maximum interest.<sup>72</sup>

In this, I would respectfully argue that the majority is wrong. Subsection 3-210(2) states that if the loan finance charge actually earned is less than the minimum loan finance charge (set by 3-508(7)), the lender can collect or retain a *minimum loan finance charge* in the event of prepayment, not to exceed *the finance charge contracted for*.<sup>73</sup> In the example Justice Rucker provides, he incorrectly limits the amount collectable by the permissible APR requirements of subsection 3-508(2) rather than *the finance charge actually contracted for*.

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72. *Livingston v. Fast Cash USA, Inc.*, 753 N.E.2d 572, 576 (Ind. 2001) (footnote omitted).

73. IND. CODE § 24-4-5-3-210(2) (1998).

Thus, if the original agreement called for a set \$33 finance charge, following 3-10(2)'s wording, a lender could collect \$33 from the borrower in the event of prepayment.

While Justice Boehm in a separate concurring opinion justifies the majority's decision on separate grounds, he too is dogged by a failure to fully to grasp the actual wording and historical context of subsections 3-210(2), 3-508(2), and 3-508(7). As Justice Boehm framed the issue: "As I see it, the issue is whether the \$33 minimum loan finance charge provided by subsection 508(7) is collectible if it exceeds the loan finance charge allowed under subsection 508(2) for the loan as written for its full term."<sup>74</sup> Although Justice Boehm recognizes that subsection 3-508(7) "sets the amount of the minimum charge," he believes that it does not constitute an independent exception to 3-508(2)'s limits.<sup>75</sup> He argues that 3-508(2) alone caps the permissible finance charge. Like the majority, Justice Boehm fails to reconcile the historical framework of these subsections. As section 3-508(7) was originally enacted and continues to function, it acts as a specific exception to the APR limitations of section 3-508(2) and establishes a minimum dollar amount that can be assessed as a finance charge.

Without doubt, both the majority and concurring opinions set forth plausible policy arguments why such short-term lenders should be prohibited from collecting these exorbitant finance charges. In truth, I too find much that is abhorrent about this industry. But whatever one's view is of this industry—whether it is a predatory lending institution, whether it targets the poor and uneducated—to find it violates a section of Indiana Code requires a violation of the language of the statute. In this case there is no such violation.

At the heart of both the majority's and Justice Boehm's argument is the basic premise that the General Assembly never contemplated such a system of small amount, short-term loans. Fair enough. But what should the court do when faced with this question of statutory construction? As it has said many times, "The primary rule in statutory construction is to ascertain and give effect to the intent of the legislature. 'The best evidence of legislative intent is the language of the statute itself, and all words must be given their plain and ordinary meaning unless otherwise indicated by statute.'"<sup>76</sup>

The opinion that most held true to these cardinal rules of statutory construction was Chief Justice Shepard's dissenting opinion. He wrote:

I read subsection 508(7) to mean what it says, in straightforward terms . . . . [S]ubsection 508(7) [i]s an exception to subsection 508(2), and it makes \$33 a true "minimum loan finance charge" using the common meaning of the words . . . . Although subsection 3-508(7) does perform this additional function [i.e., providing loan prepayment limitations], I

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74. *Livingston*, 753 N.E.2d at 578 (Boehm, J., concurring).

75. *Id.*

76. *Chambliss v. State*, 746 N.E.2d 73, 77 (Ind. 2001) (citing *Bartlett v. State*, 711 N.E.2d 497, 501 (Ind. 1999)).

still find its primary purpose in its plain language.<sup>77</sup>

Unfortunately, his more straightforward, and what I consider correct, view could find no support among his colleagues, and three members of the court settled upon a much more strained, tenuous interpretation of the statute.

What are the effects of the supreme court's decision? A class action lawsuit is currently proceeding in federal district court, and according to J. Phillip Goddard, deputy director and chief counsel for the Indiana Department of Financial Institutions, borrowers who were charged more than thirty-six percent APR on these short-term loans should be entitled to restitution.<sup>78</sup> From the businesses' standpoint, while there were early reports of some payday loan companies going out of business, several have affiliated themselves with national banks organized in other states with higher or no interest rate limitations, thereby allowing them to bypass Indiana law.<sup>79</sup>

In another case, the Indiana Supreme Court addressed a difficult issue concerning express warranties under Indiana's version of the U.C.C. In *Rheem Manufacturing Co. v. Phelps Heating & Air Conditioning, Inc.*,<sup>80</sup> Phelps Heating & Air Conditioning ("Phelps") was a central Indiana contractor that installed Rheem furnaces in several new homes. Several of the furnaces malfunctioned, requiring Phelps to incur considerable expense repairing them, an estimated \$40,000 to \$65,000. Phelps sued, alleging breach of implied and express warranties. Rheem expressly warranted its furnaces against "failure under normal use and service," but limited the warranty to replacement parts, specifically disclaiming consequential damages, incidental damages, and costs of servicing the furnaces.<sup>81</sup>

At trial, Rheem sought summary judgment on the warranty claims alleging that damages were precluded because of the limitations under the express warranty and because of lack of privity under the implied warranties. The trial court denied this motion. On interlocutory appeal, the court of appeals affirmed the denial of summary judgment.<sup>82</sup> The supreme court accepted transfer and reversed as to the express warranty issue.<sup>83</sup>

Rheem first argued that summary judgment should have been granted as to the claim for lost profits because the warranty excluded consequential damages. Both parties agreed that the warranty's remedy, repair and replacement, failed of its essential purpose, but disagreed as to the construction of Indiana Code sections 26-1-2-719(2) and (3). Section 2-719(2) provides "[w]here circumstances cause an exclusive or limited remedy to fail of its essential

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77. *Livingston*, 753 N.E.2d at 580 (Shepard, C.J., dissenting).

78. See Denise G. Callahan, *Payday Decision Not Final*, IND. LAWYER, Aug. 29, 2001, at 1.

79. *Id.* at 22.

80. 746 N.E.2d 941 (Ind. 2001).

81. *Id.* at 944.

82. *Rheem Mfg. Co. v. Phelps Heating & Air Conditioning, Inc.*, 714 N.E.2d 1218 (Ind. Ct. App. 1999), *vacated by* 746 N.E.2d 941 (Ind. 2001).

83. *Rheem Mfg. Co.*, 746 N.E.2d at 956.

purpose, remedy may be had as provided in IC 26-1."<sup>84</sup> Section 2-719(3) provides that "[c]onsequential damages may be limited or excluded unless the limitation or exclusion is unconscionable. Limitation of consequential damages for injury to the person in the case of consumer goods is prima facie unconscionable, but limitation of damages where the loss is commercial is not."<sup>85</sup>

Arguing a literal reading of section 2-719(2), Phelps contended that when a remedy fails of its essential purpose, any remedy provided by 26-1 may be had, including consequential damages. This is known as the "dependent" view that overrides a contract's consequential damage exclusion.<sup>86</sup> On the contrary, Rheem argued that the two subsections operated "independently" and that the consequential damage exclusion survived the failure of the warranty's essential purpose. This is known as the "independent" view of subsections 2-719(2) and 2-719(3).<sup>87</sup>

The supreme court found the independent view more soundly reasoned and held that subsection 2-719(2) "does not categorically invalidate an exclusion of consequential damages when a limited remedy fails of its essential purpose."<sup>88</sup> The court gave four reasons for this conclusion. First, the court found the two subsections contemplated different legal standards.<sup>89</sup> Second, the independent view upheld the statutory construction maxim of giving full effect to every term.<sup>90</sup> Third, the independent view furthered the underlying legislative purposes of the U.C.C.<sup>91</sup> And finally, the court felt the independent view supported the policy of favoring the parties' freedom of contract.<sup>92</sup>

The supreme court next moved on to a discussion of Phelps' claim for labor expenses incurred while fixing the defective furnaces. Phelps claimed that it lost nearly \$100,000 as a result of servicing the furnaces. Notwithstanding the contract's express warranty excluding the recovery of labor expenses, Phelps argued that the warranty failed of its essential purpose and was therefore entitled to collect all damages.<sup>93</sup>

In determining whether the warranty failed of its essential purpose, the court first had to determine what the essential purpose was. The applicable warranty

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84. IND. CODE § 26-1-2-719(2) (1998).

85. *Id.* § 26-1-2-719(3).

86. *Rheem*, 746 N.E.2d at 947 (citing *Middletown Concrete Prod. v. Black Clawson Co.*, 802 F. Supp. 1135, 1151 (D. Del. 1992)).

87. *Id.* (citing *Waters v. Massey-Ferguson, Inc.*, 775 F.2d 587, 592-93 (4th Cir. 1985)).

88. *Id.* (citing *Schurtz v. BMW of N. Am., Inc.*, 814 P.2d 1108, 1112 (Utah 1991)).

89. *Id.* at 948 ("A limited remedy will be struck when it fails of its essential purpose; an exclusion of consequential damages fails when it is unconscionable.").

90. *Id.* at 948-49.

91. *Id.* at 949. The purposes are: "(a) to simplify, clarify, and modernize the law governing commercial transactions; (b) to permit the continued expansion of commercial practices through custom, usage, and agreement of the parties; (c) to make uniform the law among the various jurisdictions." IND. CODE § 26-1-1-102 (1998).

92. *Rheem*, 746 N.E.2d at 950.

93. *Id.* at 953.

provision provided that “[u]nder this Warranty, R[heem] will furnish a replacement part that will be warranted for only the unexpired portion of the original warranty.”<sup>94</sup> Further, the warranty provided that “[t]his Warranty does not cover any labor expenses for service, nor for removing or reinstalling parts. All such expenses are your responsibility unless a service labor agreement exists between you and your contractor.”<sup>95</sup> Additionally, officers of both Rheem and Phelps testified regarding the customary practice of furnace manufacturers and dealers. Both testified that it was custom for manufacturers to provide a one-year warranty on parts while the dealer typically provided a one-year warranty on labor.<sup>96</sup>

Looking at the record, the court determined that the purpose of the limited warranty was “to maintain a reasonable division of responsibilities between the manufacturer and the contractor when consumers experienced problems.”<sup>97</sup> The court then moved on to determine if the remedy failed of this purpose. It found the warranty served its purpose (i.e., Rheem supplied the parts for the malfunctioning furnaces and Phelps supplied the manpower to fix them). The court concluded that Phelps accepted this allocation of responsibility by dealing in Rheem furnaces.<sup>98</sup>

While the court stated that “a limited remedy fails when its application operates to deprive either party of the substantial value of the bargain,”<sup>99</sup> the court believed failure occurs only in “unusual circumstances” and in “relatively few situations.”<sup>100</sup> The court described a failure of a warranty’s essential purpose as occurring “when an unexpected circumstance arises and neither party accepted the risk that such circumstance would occur.”<sup>101</sup> This seems like an appropriate rule in commercial sales where the loss is almost entirely economic, but it could work harsh results in a consumer sales context. It appears the court left open the possibility of a different result in the area of consumer sales.<sup>102</sup>

The court went on to find that Phelps was not entitled to collect direct warranty damages because of its position as an intermediate seller.<sup>103</sup> Rather, Phelps’ claim sounded in indemnity and subrogation for the damages suffered by its customers. The supreme court remanded the case for determination of whether Phelps could recover on an indemnity theory.<sup>104</sup>

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94. *Id.* at 944.

95. *Id.*

96. *Id.* at 953.

97. *Id.* at 954.

98. *Id.* at 955.

99. *Id.* (quoting IND. CODE § 26-1-2-719 cmt. 1 (1998)).

100. *Id.* at 954 (citations omitted).

101. *Id.* at 955.

102. *See id.* (quoting *V.M. Corp. v. Bernard Dist. Co.*, 447 F.2d 864, 865 (7th Cir. 1971)) (“2-719 was intended to encourage and facilitate consensual allocations of risk associated with the sale of goods. This is particularly true where commercial, rather than consumer sales are involved.”).

103. *Id.* at 956.

104. *See id.*

*B. Court of Appeals' Decisions*

The Indiana Court of Appeals was active on a number of fronts in the areas of commercial and consumer law. In *Walker v. McTague*,<sup>105</sup> the secured party, Walker, who had sold business properties to the McTagues, reassumed management and control of the businesses after the McTagues filed for bankruptcy. The McTagues owed Walker over \$250,000. To satisfy the outstanding loan, Walker offered the business properties for sale via a sealed bid auction by placing notices in Lafayette and Indianapolis newspapers. This was the only notice of sale the McTagues received. The sole bid on the property was \$50,000, placed by a company controlled by Walker.<sup>106</sup> Walker then sought a deficiency judgment against the McTagues for the balance. After a bench trial, the trial court entered judgment for Walker in an amount of only \$7,400, representing two months unpaid rent still owed by the McTagues, and Walker appealed.

The court of appeals determined that advertisement through newspapers is not sufficient to satisfy the notice requirement to defaulting debtors.<sup>107</sup> It then applied a two-prong test for determining whether a sale is commercially reasonable following a deficient notice. The effect of Walker's failure to give the McTagues notice was "to require [Walker] to prove that the reasonable value of the collateral at the time of the sale was less than the amount of the debt and that the sale was performed in a commercially reasonable manner."<sup>108</sup> As to the first prong, the creditor must present "credible, independent evidence that the sale price of the collateral was equal to the fair value of the collateral, but was less than the indebtedness."<sup>109</sup> For the second prong, the court laid out multiple factors for determining if a sale was commercially reasonable. These factors include: (1) the price received by the secured party, (2) whether the collateral was sold retail or wholesale, (3) the total number of bids solicited and received, and (4) whether the time and place of sale were reasonably calculated to result in a reasonable number of bidders.<sup>110</sup>

While Walker presented evidence that the value of the business properties was \$250,000, because the sale resulted in only one bid, originated from Walker and was \$200,000 below the market value of the properties, the court of appeals held that the trial court did not err in concluding "that the sale was not conducted in a commercially reasonable manner."<sup>111</sup>

In *E & L Rental Equipment, Inc. v. Wade Construction, Inc.*,<sup>112</sup> the court of appeals was presented with a barter agreement in which E & L Rental Equipment

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105. 737 N.E.2d 404 (Ind. Ct. App. 2000).

106. *Id.* at 406-07.

107. *Id.* at 409.

108. *Id.* at 409-10 (citation omitted).

109. *Id.* at 410.

110. *Id.*

111. *Id.* at 411.

112. 752 N.E.2d 655 (Ind. Ct. App. 2001).

(E & L) argued that the value of Wade Construction's performance was deficient and demanded additional payment. Pursuant to an agreement whereby E & L promised to provide Wade Construction with the use of construction equipment and various goods including sand, limestone and gravel in exchange for Wade Construction's promise to provide E & L with recycling services, E & L provided Wade Construction with \$83,646 worth of goods and rental equipment between 1994 and 1997. In exchange, Wade Construction provided E & L with \$18,000 worth of recycling services.<sup>113</sup>

E & L argued first that the agreement was a lease and not a barter. Looking to the evidence, the court of appeals found several factors indicative of a barter agreement. First, E & L did not invoice Wade Construction for use of its rental equipment until twenty-six months after performance under the contract began. The court also found that the U.C.C.'s definition of "lease," "a transfer of the right to possession and use of goods *for a term* in return for consideration," helpful.<sup>114</sup> Not only did E & L not specify a specific period for the transfer of right to possession, but E & L would also occasionally retrieve its equipment from Wade Construction for its own use.<sup>115</sup>

In the alternative, E & L argued that the part of the agreement dealing with goods—that is, the sand, limestone and gravel—was covered by Article 2 of the U.C.C. The court of appeals concluded that Article 2 was applicable, but found the trial court's conclusion was no different.<sup>116</sup> Both parties had fully performed their obligation, and it was only because the value of Wade Construction's performance was significantly less than E & L's that E & L was complaining. In essence, E & L entered into a bad agreement and sought to be bailed out by the courts, an invitation the appellate court declined.<sup>117</sup>

In *Pioneer Hi-Bred International, Inc. v. Keybank National Ass'n*,<sup>118</sup> the court of appeals was faced with a federal statute preempting Article 9's regulations of secured transactions in agricultural products. In the case, farmers in Shipshewana executed several promissory notes in exchange for which they granted Keybank a security interest in their real and personal property, including the products of their land. Subsequently, the farmers obtained an additional loan from Pioneer, and Pioneer took a security interest in the proceeds from the sale of the farmers' crops. Pioneer did not file a financing statement.<sup>119</sup> When the farmers renewed their loans with Keybank, Keybank sent notice of their secured status to all parties, including Pioneer. After the farmers harvested and processed their crops, the proceeds of the sale were given to Pioneer. Later the next year, the farmers defaulted, and Keybank filed suit to collect on the proceeds of the

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113. *Id.* at 657.

114. *Id.* at 659 (emphasis in original) (citing IND. CODE § 26-1-2.1-103 (1998)).

115. *Id.*

116. *Id.* at 660.

117. *Id.* at 660-61.

118. 742 N.E.2d 967 (Ind. Ct. App. 2001).

119. *Id.* at 968-69.

previous year's crops.<sup>120</sup>

The court of appeals found that Indiana's Article 9 was preempted by federal regulations. The regulation provides that a buyer of farm products takes subject to a security interest if the buyer receives notice of another party's security interest within one year before the sale.<sup>121</sup> In this case, Pioneer received notice of Keybank's security interest on August 16, 1997, and Pioneer purchased the farmer's farm products on December 18, 1997.<sup>122</sup> The court held that Pioneer took subject to the security interest and was accountable to Keybank for the amount it paid to the farmers.<sup>123</sup>

In *Time Warner Entertainment Co. v. Whiteman*,<sup>124</sup> customers filed a class action against Time Warner alleging that the late fees it assessed were "excessive, unreasonable, and a penalty."<sup>125</sup> Time Warner charged \$4.65 to its customers who failed to pay by a certain date. The class action plaintiffs sought money damages and injunctive relief, and Time Warner argued that the voluntary payment doctrine barred relief for money damages. The trial court denied Time Warner's motion for summary judgment, and an appeal ensued to the court of appeals.

The court of appeals found that summary judgment was appropriate based upon the voluntary payment doctrine, which provides that "a voluntary payment made under a mistake or in ignorance of law, but with a full knowledge of all the facts, and not induced by any fraud or improper conduct on the part of the payee, cannot be recovered back."<sup>126</sup> The court determined that the two key factors under the voluntary payment doctrine are the payor's knowledge and fraud or imposition by the payor.<sup>127</sup>

As to the first factor, the court held that the "onus is upon the party making the payment to inquire about the reasonableness of the charge before making the

120. *Id.* at 970.

121. The regulation reads as follows:

- (d) Except as provided in subsection (e) and notwithstanding any other provision of Federal, State, or local law, a buyer who in the ordinary course of business buys a farm product from a seller engaged in farming operations shall take free of a security interest created by the seller, even though the security interest is perfected; and the buyer knows of the existence of such interest.
- (e) A buyer of farm products takes subject to a security interest created by the seller if—
  - (1)(A) within 1 year before the sale of the farm products, the buyer has received from the secured party or the seller written notice of the security interest . . . .

*Id.* at 971 (quoting 7 U.S.C. § 1631 (1985)).

122. *Id.* at 969, 972.

123. *Id.* at 972.

124. 741 N.E.2d 1265 (Ind. Ct. App. 2001).

125. *Id.* at 1267.

126. *Id.* at 1270 (quoting *City of Evansville v. Walker*, 318 N.E.2d 388, 389 (1974) (citation omitted)).

127. *Id.* at 1270-71.

payment, or perhaps before signing the contract that specifies the late charge.”<sup>128</sup> As to the second factor, the court determined that “in order to render payment compulsory, there must have been some necessity and such pressure must be brought to bear upon the person paying as to interfere with free enjoyment of his rights of person or property.”<sup>129</sup> The court of appeals held that potential loss of cable service or the threat of litigation does not rise to the level of compulsion necessary to satisfy the second factor of the voluntary payment doctrine.<sup>130</sup> Accordingly, the court found that summary judgment was appropriate as to the money damages claim.<sup>131</sup> Because a dispute existed on whether Time Warner’s late fee was disproportionate to its actual loss, the court determined that a genuine issue of material fact was in dispute and summary judgment was inappropriate.<sup>132</sup> The Indiana Supreme Court heard oral argument on the case, but denied transfer.

### CONCLUSION

It was an eventful survey period in the areas of consumer and commercial law. The new and highly technical Revised Article 9 finally arrived. Moreover, the supreme court and court of appeals issued a number of noteworthy decisions. As of May 2002, it appears that the supreme court has issued the last of the direct criminal appeals that have hampered its ability to address many areas of civil law, including commercial and consumer law. With this newfound docket freedom, Indiana practitioners should look to the supreme court for greater guidance and development in these areas.

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128. *Id.* at 1272.

129. *Id.* (quoting *Smith v. Prime Cable of Chicago*, 658 N.E.2d 1325 (Ill. App. Ct. 1995)).

130. *Id.*

131. *Id.*

132. *Id.* at 1275.

