

UNIFORM COMMERCIAL CODE COMMITTEE

REPORT PREPARED FOR THE SEPTEMBER 25, 2008 COUNCIL MEETING

1. Next Scheduled Meeting of the Committee.

None scheduled yet.

2. Council Approval.

No matters require Council approval.

3. Membership.

A Committee meeting was held in October, 2007, with 14 members in attendance.

4. Accomplishments Toward Committee Objectives.

On September 15, 2008, the attached summary of court decisions was sent to all Committee members.

5. Meetings and Programs.

Nothing recently.

6. Publications.

Nothing recently.

7. Legislative/Judicial Administrative Developments.

The ABA's joint task force on Filing Office Operations and Search Logic presently has three subcommittees at work on the following projects: (i) the possible use of driver's license names as a safe harbor for individual debtor names; (ii) formulating a possible response to or commenting on proposals of the International Association of Commercial Administrators to NCCUSL for changes to Article 9; and (iii) reviewing electronic filing in the various states.

8. Miscellaneous.

Nothing to report.

BARNES & THORNBURG LLP

MEMORANDUM

TO: All Members of the UCC Committee
FROM: Patrick E. Mears
DATE: September 15, 2008
RE: Recent Court Decisions Construing UCC Provisions

The following recent court decisions, copies of which accompany this memorandum, are summarized below:

1. *Metropolitan Alloys Corp. v. Considar Metal Making, Inc.*, 2007 WL 2874005 (E.D. Mich. Sept. 25, 2007) (Rosen, D.J.). In this case, the Plaintiff, Metropolitan Alloys Corporation (“Metropolitan”), commenced an action against Considar Metal Marketing, Inc. (“Considar”) for fraud, breach of contract and breach of an implied covenant of good faith and fair dealing arising from Considar’s repudiation of an oral contract requiring Considar to sell SHG zinc to Metropolitan. Metropolitan filed a motion to dismiss these claims. With respect to the fraud claim, Defendant asserted the “economic loss” doctrine announced by the Michigan Supreme Court in *Neilbarger v. Universal Cooperatives, Inc.*, 439 Mich. 512, 486 N.W.2d 612 (1992), which prohibits a disappointed purchaser of defective commercial goods to recover economic loss caused by a defective product. These purchasers may only recover damages under Article 2 of the UCC. Noting Michigan case law that carves out an exception to this doctrine for claims of fraud in the inducement, Judge Rosen denied the motion to dismiss the fraud count.

Judge Rosen also denied Metropolitan's motion to dismiss the breach of contract count under the statute of frauds contained in MCL 440.2201(1). Considerar's allegations in its Complaint that Metropolitan was estopped from asserting this defense due to Considerar's actions were sufficient in Judge Rosen's view to deny the motion concerning this count of the Complaint.

Finally, Judge Rosen granted Considerar's motion to dismiss the count alleging breach of an implied covenant of good faith and fair dealing on the ground that there is no such independent cause of action recognized by Michigan law.

2. *Fire & Ice Mechanical v. Bit Mat Products of Michigan*, Case No. 269978 (Mich. Ct. App. Oct. 11, 2007) (unpublished opinion). This action was commenced by the plaintiff for revocation of its acceptance of an allegedly defective thermal fluid heater. The heater suffered various breakdowns after its installation but was repaired by the defendant/seller after each such occurrence until the last one when the plaintiff voluntarily ceased using the heater. The Bay County Circuit Court entered a judgment of no cause of action against the plaintiff, who thereupon appealed to the Michigan Court of Appeals, which affirmed the decision below.

After reviewing the facts, the Michigan Court of Appeals agreed with the trial court that the alleged nonconforming nature of the goods did not "substantially impair" the value of the goods to the plaintiff and, therefore, the plaintiff was not entitled to revoke its acceptance of the heater under MCL 440.2608(1). The Court of Appeals also concluded that plaintiff's attempted revocation did not occur "within a reasonable time" after plaintiff discovered the defect, as required by MCL 440.2608(2). The limited warranty of repair or replacement of the heater contained in the contract documents was found not to have failed of its essential purpose. MCL 440.2719. Thus, the limited warranty stood firm and was not replaced by the warranties

contained in Article 2 of the UCC. Finally, the Court of Appeals agreed with the trial court that there was no evidence of a breach of the implied warranty of merchantability contained in MCL 440.2314.

3. *Capitol National Bank v. Department of Treasury*, Case No. 275926 (Mich. Ct. App. July 15, 2008) (unpublished decision). The relevant facts of this case (as best as they can be determined from the opinion) are as follows: In 1999, Capitol National Bank (the “Bank”) perfected a security interest in the personal property of its debtor, Rivard, Inc. to secure a loan. In September, 2003, the Michigan Department of Treasury (the “State”) filed a Notice of State Tax lien against Rivard, Inc. In January, 2005, the State sold the assets at auction to satisfy the tax lien. There is no indication in the opinion as to whether the Bank filed a UCC continuation statement with the Secretary of State or whether the Bank’s filed financing statement lapsed before the auction. Although the State failed to give written notice of the auction to the Bank, the Bank had prior actual notice of the auction and the officer responsible for the loan to Rivard attended the sale. The auction proceeds totaled \$55,000 and were kept by the State. In July, 2005, the Bank commenced a conversion action in the Michigan Court of Claims against the State, seeking the turnover of the auction proceeds. The State relinquished these proceeds to the Bank but then filed a counterclaim against the Bank seeking the return of those proceeds.

The sole issue at trial was “whether the auction was conducted in a commercially reasonable manner under Article 9 of the UCC and, if not, the amount of damages to which [the Bank] was entitled.” (Slip opinion, p. 2). At the trial’s conclusion, the Court of Claims held that the Bank failed to prove that the sale was not conducted in a commercially reasonable manner and rendered a verdict of no cause of action in the State’s favor. The State then appealed to the Court of Appeals.

On appeal, the State argued that the trial court's dismissal of the State's counterclaim because the State failed to give proper notice of the auction to the Bank constituted reversible error. The State's argument was rejected; there was evidence that the notice issue was properly raised and considered by the trial court to give the State the opportunity to address this issue.

The State then argued on appeal that the Bank should be deemed to have waived any claim of a "notice deficiency" under UCC Article 9 by failing to plead the lack of notice as an affirmative defense in the Bank's response to the State's counterclaim. This argument was also rejected on appeal. At this point in the opinion, the Court of Appeals embarked on a long and sometimes opaque discussion about whether, and to what extent, Article 9 applies to state tax liens. (Slip opinion, pp. 5-8).

The Court of Appeals, however, found "merit" to the State's "position that the trial court failed to adequately consider the effect of [the Bank's] actual notice of the auction sale on its entitlement to the sale proceeds." (Slip opinion, p. 8). In conclusion, the Court of Appeals held that the Court of Claims erred "to the extent that it found that [the Bank] was entitled to the \$55,000 in auction proceeds solely on the basis of [the State's] failure to follow statutory procedure." (Slip opinion, p. 10). The trial court's dismissal of the State's counterclaim was reversed and the action was remanded to the Court of Claims for further proceedings on the counterclaim.