



Fall 9-1-1963

Effect of the Uniform Commercial Code on Virginia Commercial Law: Bulk Sales and Article 6

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Recommended Citation

Effect of the Uniform Commercial Code on Virginia Commercial Law: Bulk Sales and Article 6, 20 Wash. & Lee L. Rev. 278 (1963).

Available at: <https://scholarlycommons.law.wlu.edu/wlulr/vol20/iss2/8>

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formance. It omits the requirement that the goods must be specified or ascertained. Therefore, specific performance of the contract is not limited to those situations in which the seller has broken a contract to deliver ascertained goods and the buyer's remedy at law is inadequate. Uniqueness is not the sole basis for the granting of specific relief. It may also be granted in "other circumstances."³² Therefore, if damages will not restore the buyer to his former position, specific performance may be granted even though the goods are not unique.³³ There is no Virginia authority directly on point with this UCC section.

Similarly, the UCC gives the buyer the right to goods in which he has an insurable interest if the seller becomes insolvent within ten days after receipt of the first installment of the price.³⁴ The buyer's right to the goods on the seller's insolvency no longer depends upon locating title in the buyer.

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BULK SALES AND ARTICLE 6

Bulk sales statutes are the result of an effort to protect creditors from unscrupulous merchants who dispose of the bulk of their inventory and abscond with the purchase money before their creditors can take action to secure their interests. Prior to widespread passage of the bulk sales laws, about the turn of the century, the common law and statutory remedies available to defrauded creditors permitted a tracing of the proceeds of the sale only where the seller actually intended to hinder, delay or defraud his creditors, or where the purchaser took as a donee, or for an inadequate consideration.¹

Modern bulk sales statutes fall generally into two types: the New York type,² which is in effect in Virginia,³ and the Pennsylvania type.⁴

³²UCC § 2-716(1).

³³The remedy of specific performance does not preclude damages or other relief. UCC § 2-716(2) provides that the decree for specific relief may also provide for payment of the price or damages.

³⁴UCC § 2-502. There are two limitations to this provision: (1) He must be a buyer and not a creditor; and (2) The seller's insolvency must have occurred within ten days after the receipt of the first installment of the price.

1. Hawkland, *Sales and Bulk Sales* 163 (ALI 1958).

²N.Y. Pers. Prop. Law § 44.

³Va. Code Ann. § 55-83 (Repl. Vol. 1959).

⁴Pa. Stat. Ann. tit. 69 §§ 521-529 (1939). This statute has been repealed and replaced by the UCC.

Both types of statutes require, in substance, that unless the seller and the purchaser take specified steps several days before the purchaser takes possession of the goods to acquaint the seller's creditors with the terms of the sale, these creditors may treat the purchaser as a receiver of the goods for their benefit. Both types of statutes require the seller to furnish the purchaser with a list of the seller's creditors. In turn the parties to the sale are required to furnish those creditors with some information regarding the proposed transfer.

Article 6 of the Uniform Commercial Code is a uniform bulk sales act which extends the Virginia bulk sales law to auction sales and provides particulars so as to eliminate some uncertainties in Virginia law. Because of the basic similarity of the Virginia bulk sales statute to Article 6, Virginia law on the subject is not greatly changed by the UCC, barring the enactment of certain optional provisions included in the Commercial Code, which are modeled on the Pennsylvania-type bulk sales statute.

States with the Pennsylvania type statute require the purchaser to distribute the proceeds of the sale pro rata among the creditors, according to the relative amounts of their claims. The UCC offers an optional section incorporating this method of making the transferee responsible for applying the consideration for the sale to the satisfaction of the creditor's claims. Section 6-106 requires the purchaser of the goods, who gives new consideration, to distribute the proceeds of the sale among the creditors listed by the transferor and those creditors who file a claim in writing within thirty days after general notice is given. If any of the claims are in dispute, a portion of the fund may be withheld pending settlement or adjudication of the claim. The comments suggest a number of ways of assuring that payments are made in actual satisfaction of valid claims.⁵

To date, the majority of the states that have adopted the UCC have rejected the "application of proceeds" section,⁶ apparently assuming that advance knowledge of the imminence of a bulk sale is sufficient protection to creditors who stand to be harmed by the transfer. Since such an assumption is not unreasonable, Virginia's enactment of the UCC without the optional Pennsylvania type provisions would make the transition to the uniform bulk sales statute less burdensome.

⁵UCC § 6-106, Comment, Point 3.

⁶The optional section has been adopted in Alaska, Kentucky, New Jersey, Oklahoma and Pennsylvania. The optional section has been omitted in Arkansas, Connecticut, Georgia, Illinois, Massachusetts, Michigan, New Hampshire, New Mexico, New York, Ohio, Oregon, Rhode Island and Wyoming, with Georgia adding its own stipulation with reference to the place where public notice will be given.

The Virginia statute defines a bulk sale as "the sale, transfer or assignment in bulk or any part of the whole of a stock of merchandise, or the fixtures pertaining to the conduct of a business of selling merchandise, otherwise than in the ordinary course of trade in the regular and usual prosecution of such business. . . ." Section 6-102 of the UCC defines a bulk sale as "any transfer in bulk and not in the ordinary course of the transferor's business of a major part of the materials, supplies, merchandise or other inventory."

Under both the UCC and Virginia statute, fraud is not a necessary prerequisite to an unlawful bulk sale. In the case of *Thomas Andrews & Co. v. Robinson*,⁸ the seller transferred the majority of his stock of merchandise to the purchaser in satisfaction of a pre-existing debt. A creditor of the seller, alleging violation of the bulk sales statute, was given judgment for the value of the goods, despite his admitting that there was no actual fraud in the case. This result would not be altered by the terms of UCC section 6-102.

A transfer under the UCC applies to a somewhat narrower range of transactions than the Virginia definition. The UCC only applies in a major part of the goods is transferred, a stronger requirement than Virginia law, which only requires "any part" of the goods to be sold outside the ordinary course of trade.

Neither the UCC nor the Virginia statute applies unless the sale is "in bulk." "In bulk" is the term used in Article 6 to determine whether successive transfers of parts of a business are covered by the statute. It also aids as a quantitative test.⁹

The UCC requires that the transfer be out of the ordinary course of the transferor's business, which appears to be a less strict requirement than Virginia's "out of the ordinary course of trade and the regular and usual prosecution of such business." Presumably under the UCC stipulation, it matters not that a particular sale would not be considered unusual in the business generally. All that is necessary is that the transfer be extraordinary as viewed in the light of the customary business of the seller.

The Virginia statute applies to "a stock of merchandise or the fixtures pertaining to the conduct of a business of selling merchandise." The UCC applies to "materials, supplies, merchandise or other

⁷Va. Code Ann. § 55-83 (Repl. Vol. 1959). *Canada v. Beasley & Bros.*, 132 Va. 166, 111 S.E. 251 (1922), held that a pretended transfer of a stock of merchandise from a husband to his wife and back to the husband, without any consideration for either "sale," was not a sale within the meaning of the Virginia bulk sales statute.

⁸155 Va. 362, 154 S.E. 514 (1930).

⁹Hawkland, *supra* note 1 at 165.

inventory," which in section 6-102(2) is further defined as follows: "A transfer of a substantial part of the equipment¹⁰ of such an enterprise is a bulk transfer if it is made in connection with a bulk transfer of inventory, but not otherwise." Assuming that "fixtures" in the Virginia statute and "equipment" in the UCC mean substantially the same thing, the UCC is more restrictive than Virginia law in its coverage of fixtures. If the business is of the type covered by the bulk sales act in Virginia, the sale of its fixtures may be within the purview of the statute whether or not such sale accompanies a transfer of the inventory stock. However, under the UCC a prior bulk sale of merchandise must accompany the transfer of the fixtures in order to bring the fixture sale under Article 6.

The Virginia case of *O'Conner v. Smith*,¹¹ held that the transfer of a collection of restaurant fixtures was not governed by the bulk sale statute, since the fixtures did not pertain "to the conduct . . . of buying and selling merchandise."¹² The same result obtains under section 6-102 of the UCC. The comments following this section specifically omit restaurants from the coverage of the article.

A question may arise as to whether the equipment provision is needed in Article 6 if it does not come into play until there has already been a bulk sale of inventory. It would appear, however, that without this provision a sale in bulk of the equipment of a merchandising establishment is not covered by Article 6 at all.

Section 6-102(3) provides that "the enterprises subject to this Article are all those whose principal business is the sale of merchandise from stock, including those who manufacture what they sell." The provision is designed to indicate to the courts that Article 6 should cover only those businesses in which unsecured credit is commonly extended on the faith of a stock of merchandise, but the protection of the statute is not limited to such creditors.

Section 6-103 itemizes transfers that are not subject to Article 6,¹³

¹⁰"Equipment is defined in UCC § 9-109(2) as follows: "Goods are 'equipment' if they are used or bought for use primarily in business (including farming or a profession) . . . or if the goods are not included in the definitions of inventory, farm products or consumer goods."

¹¹188 Va. 214, 49 S.E.2d 310 (1948).

¹²Id. at 221, 49 S.E.2d at 313.

¹³UCC § 6-103. The following transfers are not subject to this Article:

- "(1) Those made to give security for the performance of an obligation;
- "(2) General assignments for the benefit of all the creditors of the transferor, and subsequent transfers by the assignee thereunder;
- "(3) Transfers in settlement or realization of a lien or other security interest;
- "(4) Sales by executors, administrators, receivers, trustees in bankruptcy, or any public officer under judicial process;
- "(5) Sales made in the course of judicial or administrative proceedings for

although they come within the general definition of section 6-102(1). Sections 6-103(1) and 6-103(4) exempt the same transactions which are exempted from the Virginia bulk sales law.¹⁴ The transfers covered by these exemptions are the sort of transactions which may affect the bulk of a merchandiser's inventory but would not normally take place with intent to defraud creditors.¹⁵ While the Virginia statute does not mention them, the inclusion of these exemptions in a new bulk sales law would be beneficial as removing a cloud from otherwise entirely proper bulk transfers.¹⁶ It should be noted that transfers made to give security for the performance of an obligation are removed from the operation of Article 6, and instead are dealt with in Article 9.

Failure to comply with the requirements of the Virginia bulk sales statute makes the sale "void as against the creditors of the seller."¹⁷ The UCC provision says failure to follow the act makes the bulk transfer "ineffective against any creditor of the transferor." Although the terminology is different, the state is left free to determine what

the dissolution or reorganization of the corporation and of which notice is sent to the creditors of the corporation pursuant to order of the court or administrative agency;

"(6) Transfers to a person maintaining a known place of business in this State who becomes bound to pay the debts of the transferor in full and gives public notice of that fact, and who is solvent after becoming so bound;

"(7) A transfer to a new business enterprise organized to take over and continue the business, if public notice of the transaction is given and the new enterprise assumes the debts of the transfer and he receives nothing from the transaction except an interest in the new enterprise junior to the claims of creditors;

"(8) Transfers of property which is exempt from execution."

¹⁴Va. Code Ann. § 55-83(3) (Repl. Vol. 1959). "[N]othing contained in this section shall apply to sales by executors, administrators, receivers, assignees under voluntary assignments for benefit of creditors, trustees in bankruptcy, or by one acting under judicial process."

¹⁵UCC § 6-103(7) is especially beneficial, since it removes ordinary good faith business transactions from the coverage of the bulk sales law.

¹⁶The case of *United States v. Lankford*, 3 F.2d 52 (4th Cir. 1924), held that the giving of a deed of trust on stock of marine supplies to secure a pre-existing debt was not a sale or transfer within the purview of the Virginia bulk sales statute. The court decided that until payment or foreclosure under the deed of trust, the relation of the parties was not vendor and vendee, but rather debtor on the one side and creditor, secured by a lien, on the other.

The outcome of this case would not be changed by UCC §§ 6-103 and 9-111, which specifically shield from the operation of the Code "transfers in settlement or realization of a lien or other security interest."

¹⁷*Trimble v. Covington Grocery Co.*, 112 Va. 826, 72 S.E. 724 (1911), an early Virginia bulk sales case, held that only parties who are in fact creditors on the date of the sale are permitted to reach the goods in the hands of the transferee. Further, the mere serving of an attachment, without a final decree in the case, does not create a relationship of debtor and creditor which will entitle the attaching party to reach the goods.

action defrauded creditors may take, so the difference is relatively unimportant. Of course whether or not the provisions of the act are complied with, the transfer is good between the parties.¹⁸

Virginia law requires that the seller and purchaser "make a full detailed inventory showing the quantity and, so far as possible with the exercise of reasonable diligence, the cost price to the seller of each article to be included in the sale." This must be done at least ten days prior to the sale.¹⁹

Article 6 does not designate the point in time when the inventory is drawn (although in a prospering concern the inventory may change substantially from day to day), but does require preparation of "a schedule of the property . . . sufficient to identify it."²⁰ Notice of the proposed transfer must be given to creditors at least ten days²¹ before the transferee takes possession of the goods or pays for them.²² The property inventory stipulated in the UCC does away with the Virginia "cost price to the seller" requirement.²³

Both the UCC and Virginia law require the seller to produce a written list of the names and addresses of all creditors of the seller, showing the amount of the debt. The listing stipulations of the UCC are apparently more stringent than Virginia law since in order to comply with the UCC the seller must include not only existing creditors, but also the names of all persons who are known to the seller to assert claims against him, even though such claims are in dispute.²⁴ By the term "creditors," both the UCC and Virginia law contemplate creditors who supplied the inventory to be transferred in the bulk sale, and all miscellaneous parties who may have claims of any sort against the seller.²⁵ Both laws require the list of creditors to be given under oath.

Both the UCC and Virginia law require that the list of creditors

¹⁸Isaac Eberly & Co. v. Gibson, 107 Va. 315, 58 S.E. 591 (1907), held that failure to comply with the terms of the bulk sale statute is no defense on notes given by the transferee to the transferor in payment for the goods, where the transferee is setting up the defense.

¹⁹Va. Code Ann. § 55-83 (Repl. Vol. 1959).

²⁰UCC § 6-104 (1)(b).

²¹Some writers feel ten days is too short a time. "In view of the complexity often involved in investigating such transactions, it would seem that a fifteen-day period would be minimal, especially in the New York type jurisdictions where this is virtually the only protection afforded creditors." Weintraub and Harris, Bulk Sales Law and Adequate Protection of Creditors, 65 Harv. L. Rev. 418, 433 (1952).

²²UCC § 6-105.

²³Va. Code Ann. § 55-83(1) (Repl. Vol. 1959).

²⁴UCC § 6-104(2).

²⁵For examples of types of creditors who have been held to be entitled to attack a bulk sale, see Bulk Sales under the Code, 14 Wyo. L.J. 30 (1959).

and the schedule of property be preserved for six months following the sale and further that the papers be available for inspection by creditors of the seller. While the Virginia statute does not stipulate where the papers are to be kept the UCC permits filing in a public office as an alternative to the transferee himself preserving the papers for inspection.²⁶

Section 6-104(3) codifies the import of the Virginia statute, in that the seller is responsible for the completeness of the list, although the transferee must notify even omitted creditors of whom he has knowledge.²⁷ Of course the final responsibility to the creditors falls on the purchaser since, as is made clear in the comments,²⁸ a creditor omitted from the list may still levy on the goods after the transfer, as though they remained the property of the seller.

The burden of giving notice to creditors at least ten days prior to the sale continues to fall on the transferee under section 6-107 of the UCC, which, like section 55-83 of the Virginia Code, requires that creditors of the seller be informed of the plans to make a bulk transfer and the names and addresses of the parties to the sale.²⁹ Under the UCC the notification continues to be made in person or by registered or certified mail.³⁰ Virginia law simply says that the notice shall state the consideration to be paid for the goods and the time and manner of payment.³¹ Section 6-107 of the UCC requires that the notice to creditors to state specifically whether or not all the debts of the transferor are to be paid as they fall due as a result of the transaction and if so, the addresses to which creditors should send their bills.³² According to the comments, this "short form" notice is intended to facilitate honest and solvent transactions.

If the proceeds of the sale are not intended to be used to satisfy all creditors of the seller in full or if there is doubt about this, then the

²⁶Va. Code Ann. § 55-84 (Repl. Vol. 1959); UCC § 6-104.

²⁷UCC § 6-104(3). Of course even omitted creditors must have extended credit prior to the bulk transfer, which point in time is presumably determined by the provisions of Article 2 of the UCC.

²⁸UCC § 6-104, Comment, Point 2.

²⁹The list must show all other business names and addresses used by the transferor within three years last past so far as known to the transferee. UCC § 6-107(1)(b).

The 1962 Official Text of the UCC amends earlier versions of § 6-104(2) so as to provide that if the transferor is the obligor on outstanding debentures, he needs list only the name of the indenture trustee. The transferor is not responsible for the names of the current bondholders. This provision was first included in the New York version of the UCC.

³⁰UCC § 6-107(3).

³¹Va. Code Ann. § 55-83(3) (Repl. Vol. 1959).

³²UCC § 6-107.

notice must be considerably more detailed as to the property to be sold and the terms of the transaction.³³

Failure to comply with the notification requirements renders the transfer "ineffective" under the UCC and "void" under Virginia law as against creditors of the seller. For practical purposes the results should be the same under either wording.

The Virginia bulk sales law does not provide protection for creditors of the seller when the sale is made by public auction. Section 6-108 of the UCC is designed to fill the need for coverage of auction sales by placing on the auctioneer³⁴ the responsibility of receiving a list of the transferor's creditors and giving notice to all creditors listed,³⁵ at least ten days prior to the auction. The UCC makes it clear that failure of the auctioneer to perform his duties will not affect the validity of the buyer's title to the goods.³⁶ If the auctioneer, however, is aware that his actions violate the UCC, he becomes liable to the creditors of the transferor as a class for sums owed to them by the transferor, up to an amount not exceeding the net proceeds of the auction.³⁷

Creditors who extend credit after notice has been given are of course not entitled to notice.³⁸

³³UCC § 6-107(2) provides: "If the debts of the transferor are not to be paid in full as they fall due or if the transferee is in doubt on that point then the notice shall state further:

"(the location and general description of the property to be transferred and estimated total of the transferor's debts;

"(b) the address where the schedule of property and list of creditors . . . may be inspected;

"(c) whether the transfer is to pay existing debts and if so the amount of such debts and to whom owing;

"(d) whether the transfer is for new consideration and if so the amount of such consideration and the time and place of payment; [and]

["(e) if for new consideration the time and place where creditors of the transferor are to file their claims."]

This last bracketed provision is optional.

³⁴The auctioneer is defined as the person other than the transferor who directs, controls or is responsible for the auction. UCC § 6-108(3).

³⁵The notice must also be given to others known to the auctioneer to hold or asset claims against the transferor. UCC § 6-108(3)(b).

³⁶UCC § 6-108(4).

³⁷*Ibid.* Of course those states which have adopted § 6-106, the "applications of proceeds" section, have also adopted § 6-108(3)(c) which requires the auctioneer to assure that the net proceeds of the auction are distributed as required by § 6-106.

³⁸UCC § 6-109(1). These creditors are protected if § 6-106, requiring the proceeds of the sale to be applied to claims of all creditors, is enacted. In the same regard, UCC § 6-109(2) is an optional provision permitting the transferee or auctioneer to receive for sums paid to particular creditors of the transferor, not exceeding the sums believed in good faith at the time of payment to be properly payable to such creditors.