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NOTES AND COMMENTS

DEFICIENCY JUDGMENTS FOR SECURED CREDITORS AFTER NONCOMPLIANCE WITH UCC SECTION 9-504(3): THE OKLAHOMA APPROACH

I. INTRODUCTION

When a debtor defaults on his obligation to a secured creditor, the creditor looks to Article 9 of the Uniform Commercial Code ("UCC") to determine his rights and remedies.¹ Of the remedies available to the secured creditor, repossession and resale of collateral is the most commonly used.² The UCC outlines the procedure for disposition of the collateral,³ but does not explicitly state whether a secured party that fails to comply with these requirements waives the right to a deficiency judgment.⁴ Consequently, a controversy has arisen which has led to different judicial approaches.

Oklahoma case law has clearly eliminated an approach that completely bars a noncomplying secured creditor from obtaining a deficiency

1. See U.C.C. § 9-501 (1990).

2. JAMES WHITE & ROBERT S. SUMMERS, *HANDBOOK OF THE LAW UNDER THE UNIFORM COMMERCIAL CODE* § 26-9 (2d ed. 1980). See also BARKLEY CLARK, *THE LAW OF SECURED TRANSACTIONS UNDER THE UNIFORM COMMERCIAL CODE* ¶ 4.06 (2d ed. 1988).

3. U.C.C. § 9-504(3) provides in part:

Disposition of the collateral may be by public or private proceedings and may be made by way of one or more contracts. Sale or other disposition may be as a unit or in parcels and at any time and place and on any terms but every aspect of the disposition including the method, manner, time, place and terms must be commercially reasonable. Unless collateral is perishable or threatens to decline speedily in value or is of a type customarily sold on a recognized market, reasonable notification of the time and place of any public sale or reasonable notification of the time after which any private sale or other intended disposition is to be made shall be sent by the secured party to the debtor, if he has not signed after default a statement renouncing or modifying his right to notification of sale.

4. In general, deficiency is that part of a secured obligation which remains after crediting the original debt with net proceeds accruing from the sale of the security by the creditor. Thus, a deficiency judgment is a judgment or decree for that part of a secured debt not realized from the sale of the collateral. See *Okmulgee Motor Sales Co. v. Prentice*, 371 P.2d 723 (Okla. 1962).

judgment.⁵ The case law is not clear, however, concerning what the secured creditor must do to obtain a deficiency judgment if the UCC requirements have not been followed. The best judicial approach requires the noncomplying secured creditor to overcome a presumption that the proceeds of the sale equaled the value of the outstanding debt by proving that the amount of the debt exceeded the fair market value of the collateral at the time of the sale.

II. THE PROBLEM

How should the law balance the right of a creditor to recover the full balance of an outstanding debt from a defaulting debtor with the right of a debtor to receive the fair market value of his property, the collateral, as a credit toward that debt? When a debtor defaults on an obligation to a secured creditor, the UCC allows the creditor to take possession of the collateral.⁶ The creditor may dispose of the collateral and apply the proceeds first to the expenses of the sale and finally to offset the indebtedness.⁷ Unless otherwise agreed between the debtor and the secured creditor, the debtor remains liable for any deficiency that results when the proceeds of the sale are less than the amount of the outstanding debt.⁸ UCC section 9-504(3) prescribes proceedings for the disposal of collateral by the secured party and mandates that every aspect of the proceedings be conducted in a "commercially reasonable"⁹ manner.¹⁰ This section also requires that the secured party give "reasonable notice"¹¹ to the debtor concerning the time and place of the sale.¹² When the creditor fails to comply with the requirements of notice and commercial reasonableness, UCC section 9-507(1) provides the debtor the right to recover from the creditor any damages incurred.¹³ One example of

5. *Beneficial Fin. Co. v. Young*, 612 P.2d 1357, 1359 (Okla. 1980).

6. U.C.C. § 9-503 provides in part: "Unless otherwise agreed a secured party has on default the right to take possession of the collateral."

7. U.C.C. § 9-504(1).

8. U.C.C. § 9-504(2) provides in part: "[U]nless otherwise agreed, the debtor is liable for any deficiency." Although the Code does not define what "any deficiency" means, it is usually interpreted as the deduction of the collateral sales proceeds from the outstanding debt of the debtor. WHITE & SUMMERS, *supra* note 2, § 26-9.

9. For a discussion of what constitutes "commercial reasonableness," see generally C. David Stinson, *Secured Transactions: Commercial Reasonability of Secured Party's Sale of Collateral After Default Under 9-504(3)*, 29 OKLA. L. REV. 486, 497-505 (1976).

10. U.C.C. § 9-504(3); *supra* note 3.

11. For a discussion of what constitutes "reasonable notice," see Nancy J. West, *The Deficiency Judgment in Illinois and the Notice Requirement of UCC 9-504(3): Are Illinois Courts on the Right Track?*, 1981 S. ILL. U. L.J. 419, 426-29.

12. U.C.C. § 9-504(3); *supra* note 3.

13. U.C.C. § 9-507(1) provides in part:

damage that a debtor might suffer is loss of the debtor's equity interest when the collateral is sold for well under its market value. The debtor could also face a greater deficiency on his debt to the creditor than would have existed if a reasonable sale had taken place.

An interpretation problem developed because the Code does not state whether a secured party's right to recover a deficiency is contingent on its compliance with the requirements of notice and commercial reasonableness.¹⁴ The judicial approaches to this dilemma range from completely barring a deficiency recovery by a noncomplying creditor to allowing the deficiency judgment regardless of the creditor's noncompliance with the Code.¹⁵ These judicial variations have generally fallen into one of three distinct categories.¹⁶

III. THE THREE APPROACHES

A. *The Absolute Bar Approach*

The absolute bar rule¹⁷ requires compliance with Code provisions as a condition precedent to a creditor's recovery of a deficiency judgment.

If the disposition has occurred the debtor or any person entitled to notification or whose security interest has been made known to the secured party prior to the disposition has a right to recover from the secured party any loss caused by a failure to comply with the provisions of this Part.

14. See *Leasco Computer, Inc. v. Sheridan Indus., Inc.*, [1990] 6G Bender's U.C.C. Serv. (MB) § 9-504, No. 95, at A-124 (N.Y. Civ. Ct. 1975). One of the Code's drafters, Grant Gilmore, admits that the drafters did not consider the relationship between the debtor's liability for a deficiency and the secured party's liability for noncompliance with the 9-504(3) requirements. II GRANT GILMORE, *SECURITY INTERESTS IN PERSONAL PROPERTY* § 44.9.4 (1965).

15. See *Leasco Computer*, [1990] 6G Bender's U.C.C. Serv. (MB) § 9-504; WHITE & SUMMERS, *supra* note 2, § 26-15.

16. See CLARK, *supra* note 2, ¶ 4.12(4); Arthur J. Rosner, *A Creditor's Right to a Deficiency Judgment Under Article 9 of the Uniform Commercial Code: Effect of Lack of Notice*, 42 BROOKLYN L. REV. 56, 61 (1975); Howard Foss, *The Noncomplying Secured Party's Right to a Deficiency*, 21 UCC L.J. 226 (1989).

17. Some courts applying the absolute bar approach are: Arkansas (*First State Bank of Morrilton v. Hallett*, 722 S.W.2d 555 (Ark. 1987)); California (*C.I.T. Corp. v. Anwright Corp.*, 237 Cal. Rptr. 108 (Ct. App. 1987)); Connecticut (*Hertz Commercial Leasing Corp. v. Dynatron, Inc.*, 427 A.2d 872 (Conn. Super. Ct. 1980) (dicta)); Delaware (*Wilmington Trust Co. v. Conner*, 415 A.2d 773 (Del. 1980)); District of Columbia (*Randolph v. Franklin Inv. Co.*, 398 A.2d 340 (D.C. 1979)); Iowa (*Rock Rapids State Bank v. Gray*, 366 N.W.2d 570 (Iowa 1985)); Kentucky (*Bank Josephine v. Conn*, 599 S.W.2d 773 (Ky. Ct. App. 1980)); Maine (*Camden Nat'l Bank v. St. Clair*, 309 A.2d 329 (Me. 1973)); Maryland (*First Nat'l Bank of Md. v. DiDomenico*, 487 A.2d 646 (Md. 1985)); Michigan (*Honor State Bank v. Timber Wolf Const. Co.*, 391 N.W.2d 442 (Mich. Ct. App. 1986)); Missouri (*Smith v. Mark Twain Nat'l Bank*, 805 F.2d 278 (8th Cir. 1986)); Montana (*Westmont Tractor Co. v. Continental I, Inc.*, 731 P.2d 327 (Mont. 1986)); Nebraska (*Deutsche Credit Corp. v. Hi-Bo Farms, Inc.*, 398 N.W.2d 693 (Neb. 1987)); New York (*Central Budget Corp. v. Garrett*, 368 N.Y.S.2d 268 (App. Div. 1975)); Ohio (*Liberty Nat'l Bank of Fremont v. Greiner*, 405 N.E.2d 317 (Ohio Ct. App. 1978)); Texas (*Tanenbaum v. Economics Lab., Inc.*, 628 S.W.2d 769 (Tex. 1982)); Utah (*Pioneer Dodge Ctr., Inc. v. Glaubensklea*, 649 P.2d 28 (Utah 1982)); Vermont (*In re Wayne Ford-Chrysler, Inc.*, 38 B.R. 174 (Bankr. D. Vt. 1984)); Washington (*Service Chevrolet, Inc. v.*

The creditor is barred from obtaining a deficiency judgment in the event he fails to give the debtor proper notice of the sale of collateral or to conduct the sale in a commercially reasonable manner.¹⁸ By far, the true application of the absolute bar is the harshest approach.

Pre-Code law generally barred a deficiency judgment in similar situations of creditor misbehavior.¹⁹ The Uniform Conditional Sales Act ("U.C.S.A.")²⁰ had sections that closely paralleled sections 9-504(2) and 9-507(1) of the Code.²¹ Courts, with few exceptions, demanded literal compliance with the complicated U.C.S.A. provisions as a condition precedent to the seller's recovery of any deficiency.²² Professor Gilmore, one of the UCC drafters, argues that under the minimal formal requirements of Article 9, relative to the requirements under U.C.S.A., it is quite reasonable that compliance be a condition precedent to a deficiency recovery. Furthermore, Professor Gilmore contends that if the Code drafters had proposed to overthrow the firmly established and generally accepted construction of the older statute, such intent would surely have been manifested in clear and unambiguous language.²³

Some courts, considering both the ease with which a creditor can comply with the UCC rules and the severe detriment that a debtor suffers in the case of noncompliance, have decided that the absolute bar is an appropriate debtor remedy. Additionally, courts consider the absolute bar approach as a strong deterrent to creditor noncompliance.²⁴ A failure to give notice can never be considered harmless, absolute bar proponents contend, because in all likelihood it will deny the debtor his right of redemption under section 9-506 and severely disadvantage the debtor defending against a deficiency action.²⁵ Hence, the strongest possible incentives for secured party compliance must be in place to guarantee the debtor an opportunity to protect his interests.²⁶

On the other hand, detractors of the absolute bar rule respond that

Sparks, 660 P.2d 760 (Wash. 1983) (en banc); Wyoming (Jackson State Bank v. Beck, 577 P.2d 168 (Wyo. 1978)).

18. Crocker Nat'l Bank v. Emerald, 270 Cal. Rptr. 699, 703-04 (Ct. App. 1990).

19. II GILMORE, *supra* note 14, § 44.9.4.

20. The UNIF. CONDITIONAL SALES ACT, 2 U.L.A. (1922) was a uniform act promulgated by the National Conference of Commissioners on Uniform State Laws in 1918. It was adopted by several states, but was later integrated into the UCC and is no longer in use.

21. II GILMORE, *supra* note 14, § 44.9.4.

22. *Id.*

23. *Id.*

24. Randolph v. Franklin Inv. Co., 398 A.2d 340, 345-47 (D.C. Ct. App. 1979).

25. *Id.*

26. *Id.*

courts have no right to bar the deficiency judgment expressly provided for in section 9-504(2) and doing so is an unfair penalty.²⁷ The absolute bar is viewed as harsh and punitive since it is not based on the debtor's actual loss or damages.²⁸ These opponents of the absolute bar approach argue that no sound policy requires the injection of such a drastic punitive element into a commercial context.²⁹

B. *The Rebuttable Presumption Approach*

If a secured party does not meet the requirements of the Code, the rebuttable presumption rule³⁰ allows the court to presume that the repossessed collateral had a fair market value equal to the outstanding debt, and therefore the debtor owes no deficiency. The burden shifts to the creditor to overcome the presumption and prove that a deficiency exists. To meet this burden, a creditor must prove the fair market value of the collateral at the time of sale and show that the amount of the debt exceeded that value.³¹

By requiring the creditor to establish the fair market value of the collateral, independent of the amount realized at the sale, not only is the

27. *Associates Capital Servs. Corp. v. Riccardi*, 408 A.2d 930, 933 (R.I. 1979).

28. *State Bank of Towner v. Hansen*, 302 N.W.2d 760, 767 (N.D. 1981).

29. *Valley Mining Corp. v. Metro Bank*, 383 So. 2d 158, 164-65 (Ala. 1980); *Hall v. Owen County State Bank*, 370 N.E.2d 918, 927 (Ind. Ct. App. 1977); *Cornett v. White Motor Corp.*, 209 N.W.2d 341, 344 (Neb. 1973).

30. Some courts applying the rebuttable presumption approach are: *Alaska (United Bank Alaska v. Dischner*, 685 P.2d 90 (Alaska 1984)); *Colorado (1st Charter Lease Co. v. McAl, Inc.*, 679 P.2d 114 (Colo. Ct. App. 1984)); *Connecticut (Tennant Co. v. Martin's Landscaping, Inc.*, 515 A.2d 665 (Conn. Super. Ct. 1986)); *Florida (Weiner v. American Petrofina Mktg. Inc.*, 482 So. 2d 1362 (Fla. 1986)); *Georgia (Emmons v. Burkett*, 353 S.E.2d 908 (Ga. 1987)); *Hawaii (Liberty Bank v. Honolulu Providoring Inc.*, 650 P.2d 576 (Haw. 1982)); *Idaho (Snake River Equip. Co. v. Christensen*, 691 P.2d 787 (Idaho Ct. App. 1984)); *Illinois (First Galesburg Nat'l Bank & Trust Co. v. Joannides*, 469 N.E.2d 180 (Ill. 1984)); *Indiana (Hall v. Owen County State Bank*, 370 N.E.2d 918 (Ind. Ct. App. 1977)); *Kansas (Medling v. Wecoe Credit Union*, 678 P.2d 1115 (Kan. 1984)); *Minnesota (Chemlease Worldwide Inc. v. Brace, Inc.*, 338 N.W.2d 428 (Minn. 1983)); *Mississippi (United States v. Bryant*, 628 F. Supp. 1444 (N.D. Miss. 1986)); *Nevada (U C Leasing, Inc. v. Laughlin*, 606 P.2d 167 (Nev. 1980)); *New Jersey (Ingersoll-Rand Fin. Corp. v. Miller Mining Co.*, 817 F.2d 1424 (9th Cir. 1987)); *New Mexico (Clark Leasing Corp. v. White Sands Forest Prods., Inc.*, 535 P.2d 1077 (N.M. 1975)); *New York (General Elec. Credit Corp. v. Durante Bros. & Sons*, 433 N.Y.S.2d 574 (App. Div. 1980)); *North Carolina (Church v. Mickler*, 287 S.E.2d 131 (N.C. Ct. App. 1982)); *North Dakota (Lindberg v. Williston Indus. Supply Corp.*, 411 N.W.2d 368 (N.D. 1987)); *Oregon (FDIC v. Tempest Fugat*, 707 P.2d 81 (Or. Ct. App. 1985)); *Pennsylvania (Savoy v. Beneficial Consumer Discount Co.*, 468 A.2d 465 (Pa. 1983)); *Rhode Island (Associates Capital Servs. Corp. v. Riccardi*, 408 A.2d 930 (R.I. 1979)); *Tennessee (Investors Acceptance Co. of Livingston v. James Talcott, Inc.*, 454 S.W.2d 130 (Tenn. Ct. App. 1969)); *Washington (Rotta v. Early Indus. Corp.*, 733 P.2d 576 (Wash. Ct. App. 1987)); *Wisconsin (Ford Motor Co. v. Lyons*, 405 N.W.2d 354 (Wis. Ct. App. 1987)).

31. *Smith v. Paige*, 11 U.C.C. Rep. Serv. 2d (Callaghan) 1000, 1006 (Va. Cir. Ct. 1990).

true deficiency determined, but any damages of the debtor are also established. If the fair market value turns out to be more than the amount realized by selling the collateral, the difference represents the debtor's damages. The debtor would recover these damages through the reduction of the amount of the deficiency. The creditor would only be entitled to the difference between the newly established fair market value and the debt, and would forfeit the amount of the debtor's damages, or the difference between the market value and the amount realized at the sale.

The court that formulated the rebuttable presumption rule emphasized that simple considerations of fair play require that the burden of proof as to the debtor's damages be shifted to the misbehaving creditor. After all, the creditor's actions made it difficult for the debtor to prove the extent of the loss with reasonable certainty.³² Advocates of this approach contend that the burden shifting rule adequately protects the debtor's right to notice without risking a harsh forfeiture by the creditor in cases where the debtor suffered no actual damage.³³

When the creditor fails to give the debtor notice or to hold a commercially reasonable sale, the actual loss to the debtor could range from an amount greater than the deficiency to no loss at all. In a case of nominal damages, allowing the absolute bar creates a windfall for the debtor and another strong argument for the rebuttable presumption approach over the absolute bar approach.³⁴

Critics of the rebuttable presumption approach argue that when the debtor is prevented from attending the sale by a failure of notice, being expected to refute the evidence of the secured party is unfair because the creditor has all the relevant information concerning the sale and the collateral.³⁵ Moreover, the rebuttable presumption is a "legal fiction" not easily implied from UCC provisions.³⁶ Rebutting the presumption may allow a creditor to deny a debtor the express protections of notice and commercial reasonableness provided under section 9-504(3) and his redemption rights under section 9-506.³⁷ Opponents also argue that shifting the burden to the creditor is unfair when the debtor's default created

32. *Norton v. National Bank of Commerce of Pine Bluff*, 398 S.W.2d 538 (Ark. 1966).

33. *Smith*, 11 U.C.C. Rep. Serv. 2d (Callaghan) at 1006.

34. *Emmons v. Burkett*, 353 S.E.2d 908, 911 (Ga. 1987); *First Galesburg Nat'l Bank & Trust Co. v. Joannides*, 469 N.E.2d 180, 182-83 (Ill. 1984).

35. *State Nat'l Bank of Evanston v. Northwest Dodge, Inc.*, 438 N.E.2d 1345, 1349 (Ill. App. Ct. 1982).

36. *Leasco Data Processing Equip. Corp. v. Atlas Shirt Co.*, 323 N.Y.S.2d 13, 17 (N.Y. App. Div. 1971).

37. *Tanenbaum v. Economics Lab., Inc.*, 628 S.W.2d 769, 772 (Tex. 1982).

the original problem.³⁸

C. *The Set-off Approach*

The set-off approach³⁹ does not require a secured creditor to comply with Code requirements to obtain a deficiency judgment. Instead, the debtor must prove that he suffered a loss due to noncompliance by the creditor, which may then be used as a set-off against the amount of the deficiency.⁴⁰ The set-off rule is based on the premise that section 9-507(1) provides the debtor's exclusive remedy for damages incurred because of a creditor's noncompliance with the prescriptions of the UCC. Under the set-off approach the debtor has the burden of proving the extent of his damages.⁴¹ This approach is used by fewer courts than the other two approaches.⁴²

Proponents of the set-off theory correctly point out that section 9-504(2) expressly entitles a secured party to a deficiency and does not condition it on compliance with other Code sections.⁴³ Advocates state that section 9-507(1) is a debtor's sole remedy because it is the only specific UCC provision regarding damages caused by creditor misbehavior.⁴⁴ Courts have ruled that not only is the relief under section 9-507(1) a debtor's exclusive remedy, but it arguably affords the debtor adequate compensatory relief in accordance with the Code.⁴⁵

Critics of the set-off rule argue that by allocating the burden of proof to the debtor, the rule penalizes the debtor for the creditor's misconduct. Additionally, if the Code provisions can effectively be ignored, there is minimal incentive to the secured party to comply.⁴⁶ Critics argue that the burden is too great since the debtor must prove both noncompliance on the part of the secured party and also that the noncompliance resulted

38. Note, *Remedies for Failure to Notify Debtor of Disposition of Repossessed Collateral Under the UCC*, 44 U. COLO. L. REV. 221, 232 (1972).

39. Some jurisdictions adopting the set-off approach are: Alabama (*First Ala. Bank of Montgomery v. Parsons*, 426 So. 2d 416 (Ala. 1983)); Arizona (*Gulf Homes, Inc. v. Goubeaux*, 664 P.2d 183 (Ariz. 1983) (en banc)); New York (*Stanchi v. Kemp*, 370 N.Y.S.2d 26 (App. Div. 1975)); Washington (*Grant County Tractor Co. v. Nuss*, 496 P.2d 966 (Wash. Ct. App. 1972)).

40. 1A PETER F. COOGAN, *SECURED TRANSACTIONS UNDER U.C.C. § 8.06[2]* (1984).

41. See generally *Grant County Tractor Co. v. Nuss*, 496 P.2d 966 (Wash. Ct. App. 1972).

42. 1A COOGAN, *supra* note 40.

43. Alan Aronowitz, *Secured Creditor's Right to a Deficiency Judgment After Misbehavior Under U.C.C. § 9-504(3): Which Judicial Approach Should Texas Adopt?*, 21 HOUS. L. REV. 359, 374-75 n.91 (1984).

44. William E. Hogan, *Pitfalls in Default Procedure*, 2 UCC L.J. 244, 257 (1970).

45. *Jones v. Morgan*, 228 N.W.2d 419, 423 (Mich. Ct. App. 1975).

46. *Mack Fin. Corp. v. Scott*, 606 P.2d 993, 996 (Idaho 1980).

in a specific amount of loss.⁴⁷

This approach also has inherent proof problems. If the secured party fails to give notice, the debtor might not have the opportunity to attend the sale. When that happens, pertinent information known by the creditor, such as the number of bidders and industry customs, will be missed by the debtor. Therefore, the debtor will have problems overcoming his burden, both in proving the value of the collateral for purposes of quantifying the deficiency and in determining if the circumstances of the sale were commercially reasonable.⁴⁸

D. *Variations on the Three Approaches*

Authors commenting on this subject have promoted several variations of the three primary approaches as potential improvements in the law of deficiency judgments. One author suggests drawing a line between consumer and commercial transactions because the unsophisticated consumer cannot be expected to understand the intricacies of what constitutes a commercially reasonable sale.⁴⁹ Hence, creditor noncompliance should be deterred with the absolute bar approach to protect the interests of these unwary consumers.⁵⁰ A commercial entity, on the other hand, is in a better position to understand the requirements of a commercially reasonable sale of property and to fend for itself. In those instances the rebuttable presumption approach would suffice.⁵¹ This approach involves, however, a double standard, which is generally disfavored in the law. Moreover, the basic premise may be defective, given the great number of small business commercial transactions and the relative savvy of some consumers.

Another suggestion distinguishes secured party and debtor actions.⁵² The underlying theory is that the party who asserts the affirmative of an issue should have the burden of proving the issue.⁵³ Thus, a creditor seeking a deficiency judgment must first prove the commercial reasonableness of the sale as required in the rebuttable presumption approach. A debtor seeking damages under section 9-507(1) must prove

47. First Ala. Bank of Montgomery v. Parsons, 426 So. 2d 416, 421 (Ala. 1983).

48. See generally Tanenbaum v. Economics Lab., Inc., 628 S.W.2d 769 (Tex. 1982); Honor State Bank v. Timber Wolf Constr. Co., 391 N.W.2d 442 (Mich. Ct. App. 1986).

49. CLARK, *supra* note 2, ¶ 4.12(4).

50. *Id.*

51. *Id.*

52. Michael P. Donaldson, *The Commercially Reasonable Disposition of Collateral Under Article 9 of the UCC: The Question of the Burden of Proof*, 20 UCC L.J. 307, 310-11 (1988).

53. *Id.*

that the sale was not commercially reasonable as required in the set-off approach.⁵⁴ This was the logic of the Oklahoma Supreme Court in *First National Bank & Trust Co. of Enid v. Holston*.⁵⁵

A third argument advocates flexibility and judicial discretion to use the rule that best fits the specific situation.⁵⁶ For example, in a case of failure of notice, the absolute bar rule should be applied to protect the debtor who had no opportunity to protect his own interests. But, in a case of a commercially unreasonable disposition of collateral, the rebuttable presumption rule is more appropriate to force the creditor to prove compliance with the Code.⁵⁷ However, this method would deny parties to secured transactions the predictability required in the commercial business environment.

IV. THE OKLAHOMA POSITION

Before the Supreme Court of Oklahoma had a chance to consider the issue, it arose in *Dynalectron Corp. v. Jack Richards Aircraft Co.*,⁵⁸ a federal case applying Oklahoma law. That court ruled that under the law in Oklahoma, a creditor was not entitled to a deficiency judgment unless the sale of the collateral was commercially reasonable.⁵⁹ Since this was a relatively unexplored area of Oklahoma law, no case authority was cited for this conclusion. Rather, the court referred to a treatise on the UCC that supported the absolute bar rule.⁶⁰

Five years later in *First National Bank & Trust Co. of Enid v. Holston*,⁶¹ the Oklahoma Supreme Court ruled: "Before the secured creditor may recover a deficiency judgment, the sale must have been made in a commercially reasonable manner with proper notice, otherwise the debtor may recover damages for commercially unreasonable sale."⁶² The court missed its opportunity to clear up the Oklahoma position. Rather than clearly differentiating between an absolute bar of the deficiency judgment and a recovery for damages by the debtor under section 9-507(1), this holding blended the two together in an attempt to cover all

54. *Id.*

55. 559 P.2d 440, 444 (Okla. 1976).

56. Foss, *supra* note 16.

57. *Id.*

58. 337 F. Supp. 659 (W.D. Okla. 1972).

59. *Id.* at 663.

60. *Id.* ("The creditor is not entitled to a deficiency judgment unless the sale of the collateral was conducted in a manner which was commercially reasonable." (quoting 4 RONALD A. ANDERSON, UNIFORM COMMERCIAL CODE § 9-504:28 (2d ed. 1971))).

61. 559 P.2d 440 (Okla. 1976).

62. *Id.* at 443.

the bases. Did the court mean to say that a deficiency judgment is contingent upon the secured party following the rules or that a deficiency judgment is allowed no matter what, subject only to a set-off for actual damages of the debtor?

What *First National Bank* is quite clear on, however, is that the burden of proving whether the sale of collateral was commercially reasonable is on the party raising the question.⁶³ Where the secured party seeks a deficiency judgment he would carry the burden; but where the debtor pursues the damage remedy allowed under section 9-507(1), the burden shifts to the debtor.⁶⁴ That same year in *Davidson v. First Bank & Trust Co.*, the Oklahoma Supreme Court included a sentence which gave the impression that the absolute bar rule was applicable: "In other words the mortgagee is not entitled to a deficiency judgment."⁶⁵ The sentence was never to have been included in the final draft and, indeed, the case was re-published with the sentence deleted.⁶⁶

The definitive Oklahoma statement on this issue evolved in *Beneficial Finance Co. v. Young*.⁶⁷ This 1980 case expressly overruled the above mentioned sentence from *Davidson*, although the court denied it was ever the law of Oklahoma.⁶⁸ The Supreme Court of Oklahoma reasoned that the absolute bar approach was punitive in nature and against the intent of the Code.⁶⁹ The court pointed out that the debtor's protection against noncompliance was provided by the Code drafters in section 9-507(1) and expressed the opinion that this provided adequate protection for the debtor.⁷⁰ They ruled that to withhold a creditor's right to a deficiency judgment would not only protect the debtor but would also penalize the creditor.⁷¹ Because the sale of the collateral was necessitated by the default of the debtor in the first place, the court decided that punishing the creditor for noncompliance in the absence of malice, fraud, or oppression would be unjustified.⁷²

63. *Id.* at 444.

64. *Id.*

65. 559 P.2d 1228, 1231 (Okla. 1976), *partially overruled by* Beneficial Fin. Co. v. Young, 612 P.2d 1357 (Okla. 1980).

66. *Davidson v. First Bank & Trust Co.*, 609 P.2d 1259, 1262 (Okla. 1977), *modifying* 559 P.2d 1228 (Okla. 1976).

67. 612 P.2d 1357 (Okla. 1980).

68. *Id.* at 1359.

69. *Id.*

70. *Id.*

71. *Id.*

72. *Id.*

Furthermore, the court cited section 1-106 as supportive of its position that exemplary damages are allowed only in those instances expressly provided in the Code or by other rules of law and that no such damages were provided for noncompliance with section 9-504(3).⁷³ Therefore, since the effect of the absolute bar rule is similar to an award of exemplary damages, it is contrary to express UCC provisions.

V. A MIDDLE GROUND

Secured parties need the ability to enforce their security agreements against the collateral of their defaulting debtors with a minimum of hardship and red tape. Without this ability, credit for both consumers and businesses would become more restricted. At the same time, the debtor must be protected from abuse by overreaching or uncaring creditors who must act responsibly concerning the disposition of the debtor's property. Presumably the intent of the Code was to further both these goals.⁷⁴

The rebuttable presumption approach provides a middle ground from which both of these goals can be addressed.⁷⁵ Unlike the absolute bar approach, the rebuttable presumption approach does not risk harshly punishing a creditor for a mere technicality that causes no actual damage to the debtor. On the other hand, the rebuttable presumption approach avoids placing a seemingly insurmountable burden of proof upon the debtor as in the set-off approach.⁷⁶

A. *Barring the Absolute Bar Rule*

One of the principle arguments for absolutely barring a creditor's deficiency judgment when that creditor has failed to give reasonable notice or dispose of the collateral in a commercially reasonable manner, as required by the Code, is the precedent set by pre-Code law.⁷⁷ Courts, with few exceptions, required a strict adherence to the provisions of the U.C.S.A. which preceded the UCC.⁷⁸ The U.C.S.A. treated the question of the debtor's liability for a deficiency and the creditor's liability for any failure to comply with Code requirements in sections that were basically

73. *Id.*

74. *First Nat'l Bank & Trust Co. of Enid v. Holston*, 559 P.2d 440, 443 (Okla. 1976).

75. *Smith v. Paige*, 11 U.C.C. Rep. Serv. 2d (Callaghan) 1000, 1006 (Va. Cir. Ct. 1990).

76. Aronowitz, *supra* note 43, at 395.

77. Note, *The Right to an Article 9 Deficiency Judgment Without 9-504 Notice of Resale*, 7 VAL. U. L. REV. 465, 471 (1973).

78. II GILMORE, *supra* note 14, § 44.9.4.

comparable to UCC sections 9-504(3) and 9-507(1).⁷⁹ Therefore, the argument goes, the UCC did not alter this link between compliance and the right to a deficiency judgment.⁸⁰

Actually, the UCC was enacted because the stringent system of regulation under the U.C.S.A. had failed.⁸¹ The U.C.S.A. had established burdensome requirements which had little practical benefit.⁸² As indicated by the official comment, the UCC was designed to supercede prior legislation such as the U.C.S.A.⁸³ The aim of Article 9 was to provide "a simple and unified structure within which the immense variety of present-day secured financing transactions can go forward with less cost and with greater certainty."⁸⁴ Rather than continue the requirement of stringent enforcement, the UCC has relaxed these standards in an attempt to add flexibility for the creditor in obtaining the highest realization from the collateral.⁸⁵ The only restriction placed on the disposition is that it be commercially reasonable.⁸⁶

Furthermore, the U.C.S.A. allowed public sales and auctions, requiring creditors to give notice to both the debtor and the public.⁸⁷ A failure to give notice under these rules would defeat the very policy of the sale since an unnotified public could certainly not attend the sale. Under the U.C.S.A. the harshness of the penalty to the creditor matched the harshness of the consequences of his actions. The notice requirement under the UCC has been relaxed to require "reasonable" notice rather than the exacting requirements of the U.C.S.A.⁸⁸ Since private sales are encouraged,⁸⁹ and the only notice required to be given the debtor is notice of the time after which the private sale will take place,⁹⁰ a lack of notice assumes a less harsh consequence under the UCC than it did under the U.C.S.A.

A final difference between the Code and the U.C.S.A. pertains to the

79. *Id.*

80. *Id.*

81. Grant Gilmore, *Article 9 of the Uniform Commercial Code Part V—Default*, 7 CONF. ON PERS. FIN. L.Q. 4, 7 (1952).

82. *Id.*

83. U.C.C. § 9-101 cmt.

84. *Id.*

85. U.C.C. § 9-504 cmt 1.

86. *Id.*

87. UNIF. CONDITIONAL SALES ACT § 19, 2 U.L.A. 30 (1922).

88. U.C.C. § 9-504 cmt. 5.

89. *Id.* cmt. 1.

90. U.C.C. § 9-504(3).

purpose of denying a deficiency judgment. Under the U.C.S.A. the denial of the deficiency judgment was intended to operate as a deterrent and therefore was penal in nature.⁹¹ The Code, on the other hand, specifically rejects the notion of special or penal damages.⁹² The Oklahoma Supreme Court, in deciding not to bar a secured party's right to a deficiency judgment in an instance of noncompliance with the Code, agreed that such a forfeiture would go beyond compensatory damages and therefore was outside the intent of the Code.⁹³

Rather than look to pre-Code law, which is not controlling, an analogy to a Code provision outside of Article 9 proves enlightening. Article 2, which refers to sales, provides that when a buyer rejects acceptance of goods, the seller may resell the goods and recover damages.⁹⁴ The notice provision in section 2-706 is similar to section 9-504 and substantiates the idea that failure to comply with the Code should not result in a loss of a right to a deficiency judgment.⁹⁵ Unlike section 9-504, section 2-706 makes compliance with its requirements an express condition precedent to the seller's right to recover the difference between the sale price and the contract price.⁹⁶ Although the seller who fails to comply with the requirements of section 2-706 loses his right to use the sale price as an absolute measure of damages, he may still recover damages based on the market value of the goods.⁹⁷ This comparison of Code sections shows that the drafters intended that a secured party (or a seller) not lose all rights in the collateral for a failure to comply with the Code. Instead, the burden of proving true market value to establish damages becomes the responsibility of the seller.

Another aspect of the absolute bar approach to be considered is the "all or nothing" situation arising from the application of the rule. Under this rule, a court is faced with denying a deficiency altogether or allowing a deficiency based on the sale price of the collateral. It is easy to imagine a variety of judicial interpretations of the standard, "commercially reasonable." A commercially unreasonable sale of collateral does not necessarily mean that the collateral was sold for less than its fair market value. A sale might fall outside the parameters of a jurisdiction's definition of

91. Note, *supra* note 77, at 474.

92. U.C.C. § 1-106 which provides in part: "[N]either consequential or special nor penal damages may be had except as specifically provided in this Act or by other rule of law."

93. *Beneficial Fin. Co. v. Young*, 612 P.2d 1357, 1359 (Okla. 1980).

94. U.C.C. § 2-706(1).

95. Note, *supra* note 77, at 478.

96. U.C.C. § 2-706(1).

97. *Id.* cmt. 2.

commercially reasonable and yet produce the full value of the debtor's property from the sale. In such a case, the debtor suffers no actual loss and yet the court is faced with denying the creditor a deficiency for which the debtor is truly liable. A court faced with this unfair result of the absolute bar rule might stretch the definition of "commercially reasonable" to avoid the harsh result.

B. *Rebuttable Presumption or Set-Off?*

Although it is clear that Oklahoma has ruled out the absolute bar of a deficiency judgment when the creditor has failed to meet the requirements of the Code,⁹⁸ it is unclear whether there is a presumption that the value of collateral equals the outstanding debt at the time of sale. The court in *First National Bank & Trust Co. of Enid* established that a creditor seeking a deficiency judgment has the burden of proving Code compliance.⁹⁹ If the secured party fails to prove the commercial reasonableness of the sale or sufficient notice to the debtor, is the burden on him to prove that the value of the collateral was less than the debt and that there is therefore a deficiency (the rebuttable presumption approach)? Or, will the burden lie with the debtor to prove damages under section 9-507(1) to be set-off against any deficiency (the set-off rule)? By not expressly ruling on which party has the burden of proof as to the value of the collateral when a creditor seeks a deficiency judgment, the *Beneficial* court has left Oklahoma with an ambiguous position.

Several writers addressing this issue, when listing the jurisdictions that have adopted the various approaches, list *Beneficial*, and therefore Oklahoma, under the set-off approach.¹⁰⁰ The *Beneficial* court did refer to section 9-507(1) as adequate protection for the debtor.¹⁰¹ The court pointed out that if the creditor's noncompliance results in damage to the debtor, the debtor has a right to recover those damages.¹⁰² Admittedly, this language sounds similar to that of the proponents of the set-off approach.¹⁰³ Subsequent cases have discussed a creditor being able to recover a deficiency judgment even after failing to comply with the Code requirements, subject to liability for any damages caused by the

98. *Beneficial*, 612 P.2d at 1359.

99. *First Nat'l Bank & Trust Co. of Enid*, 559 P.2d at 444.

100. *Hoch v. Ellis*, 627 P.2d 1060, 1069 (Alaska 1981) (Burke, J., dissenting); 1A COOGAN, *supra* note 40; *Donaldson*, *supra* note 52; *Foss*, *supra* note 16.

101. *Beneficial*, 612 P.2d at 1359.

102. *Id.*

103. See generally *Jones v. Morgan*, 228 N.W.2d 419, 423 (Mich. Ct. App. 1975).

noncompliance.¹⁰⁴

Courts interpreting Oklahoma law have had trouble determining where to place the burden of proving the value of the collateral at the time of sale. In 1989, a Federal Bankruptcy Court in the Eastern District of Oklahoma ruled that this burden was on the secured party,¹⁰⁵ but interestingly cited a 1971 federal case that applied Arkansas law,¹⁰⁶ rather than an Oklahoma case.

The state of the law on this issue in Oklahoma must be clarified. If the intent of the court in *Beneficial* was to adopt the set-off approach and place the burden of proving damages squarely on the debtor, the law should be changed. The set-off approach not only penalizes the debtor for the misbehavior of the creditor, but also makes the requirements of notice and commercial reasonableness moot.¹⁰⁷ Even if the creditor fails to prove that he complied with the Code requirements, the debtor would get no relief unless he could prove specific damages.¹⁰⁸ Proving damages would require that the debtor establish the value of collateral that, in most cases, had already been disposed of without appraisal. In cases where the creditor failed to give notice, the debtor would not even have the benefit of having witnessed the sale to help him determine the reasonableness of the value received.¹⁰⁹

The rebuttable presumption approach goes to the heart of the issue. Rather than focusing on whether the sale was commercially reasonable, it focuses on the purpose for that requirement, which is to assure that the fair market value of the collateral or credit for that amount is received by the debtor. Placing the burden of proving the market value of the collateral at the time of the disposition on the secured party is reasonable and protects the debtor's interest in the collateral. The creditor should not be able to use the amount received for the collateral as evidence of its value.¹¹⁰ The creditor, having possession of the collateral, is in the best position to ascertain its true value.¹¹¹ This responsibility should not represent a great burden on the creditor, assuming that his motivation is to receive the maximum proceeds from the collateral. This motive should

104. *Equico Lessors, Inc. v. Wetsel*, 576 F. Supp. 13, 18 (W.D. Okla. 1983); *First State Bank of Oilton v. Perryman*, 746 P.2d 706 (Okla. App. 1987).

105. *In re Reed*, 102 B.R. 243, 246 (Bankr. E.D. Okla. 1989).

106. *Leasing Assoc. v. Slaughter & Son*, 450 F.2d 174 (8th Cir. 1971).

107. *See generally Mack Fin. Corp. v. Scott*, 606 P.2d 993 (Idaho 1980).

108. *See generally First Ala. Bank of Montgomery v. Parsons*, 426 So. 2d 416 (Ala. 1982).

109. *See Randolph v. Franklin Inv. Co.*, 398 A.2d 340, 345 (D.C. 1979).

110. *Smith v. Paige*, 11 U.C.C. Rep. Serv. 2d (Callaghan) 1000, 1006 (Va. Cir. Ct 1990).

111. *In re Nardone*, 70 B.R. 1010, 1016 (Bankr. D. Mass. 1987).

exist since the creditor has no assurance that he will be able to collect any deficiency from the defaulting debtor. The first step in obtaining the maximum value from the sale of an item is to establish its worth. By assuring that the maximum proceeds are received for the collateral, the creditor is protecting not only the debtor's interests but his own as well.

Consider the following example. A lender loans a borrower eight thousand dollars and takes a security interest in the debtor's car. The debtor eventually goes into default and the creditor repossesses the car and sells it for five thousand dollars. When the creditor sues for the three thousand dollar deficiency, assuming he cannot prove compliance, the burden falls on him to prove the fair market value. Assume that the evidence shows the value at the time of sale to have been six thousand dollars. The debtor is liable for the true deficiency of two thousand dollars. The creditor suffers the actual cost of his apparently commercially unreasonable sale, the one thousand dollar difference between the sales price and the fair market value. This method allows the creditor to recover the full amount of the debt owed to him, without the risk of a severe penalty, subject only to obtaining the full value for the collateral of which he is in charge. It ensures that the debtor will only be liable for the true deficiency and not one inflated by a below market sale of his property and that the creditor will be motivated to hold a commercially reasonable sale in the first place.

Either through specific legislation or a ruling by the Supreme Court, Oklahoma should lay to rest any question of which party has the burden of proof. If the creditor failed to prove compliance with the Code, a rebuttable presumption that the proceeds of the sale equaled the value of the outstanding debt would arise.¹¹² The burden of overcoming this presumption would fall on the creditor, thereby protecting the interests of the debtor as the Code intended. It should be made clear that a secured creditor may recover a deficiency judgment from the debtor if he proves either (1) that reasonable notice of the sale was provided to the debtor and the sale was performed in a commercially reasonable manner, or (2) that the amount of the debt exceeded the fair market value of the collateral at the time of the sale by the amount of the deficiency sought.¹¹³

112. *Mack*, 606 P.2d at 996.

113. *Smith*, 11 U.C.C. Rep. Serv. 2d (Callaghan) at 1006.

VI. CONCLUSION

Many jurisdictions have faced or will face the difficult task of determining a legal question which was apparently overlooked by the Code drafters.¹¹⁴ Having considered the relative merits of the three judicial approaches, the rebuttable presumption approach seems to most closely conform with the goals and policies of the Code. In light of this, and due to the fact that the law is presently unclear, Oklahoma should explicitly adopt the rebuttable presumption approach.

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114. II GILMORE, *supra* note 14, § 44.9.4.

