

**UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF TENNESSEE**

IN RE:

T.R. SYSTEMS, INC.

Debtor.

Case No. 98-24044

Chapter 7

P. PRESTON WILSON, CHAPTER 7 TRUSTEE,

Plaintiff,

v.

Adversary Proceeding

No. 98-1243

T.R. SHELBY and EMILY SHELBY,

Defendants.

OPINION GRANTING AND DENYING SUMMARY JUDGMENT IN PART

The issue before the Court is whether the Defendants have valid perfected security interests in a contract, a certificate of deposit, and four pieces of equipment. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(K). Based on the analysis below, this Court concludes that the Defendants do not have perfected security interests in the contract or certificate of deposit and that the Court is without sufficient evidence to determine their interest in the equipment. The following constitutes findings of fact and conclusions of law in accordance with Federal Rule of Bankruptcy Procedure 7052.

FACTUAL SUMMARY

T.R. Systems, Inc. (“Debtor”) filed this voluntary Chapter 7 case on March 23, 1998, and P.

Preston Wilson (“Trustee”) was duly appointed as the Chapter 7 Trustee. The Trustee filed a complaint to determine the extent and priority of liens and a motion for summary judgment, and a hearing was held in this Court on June 10, 1999, at which counsel for both parties were present. T.R. Shelby and Emily Shelby (“Defendants”) claim perfected security interests in a contract, a certificate of deposit, and certain equipment owned by the Debtor at the time of filing the petition: an Eagle Tire cutter, serial number 793413; Clark Michigan loader, serial number 7AJC106; a Williams Nife hog, serial number 1984366; and a Propane forklift truck. The following facts are not disputed in the pleadings or in the oral response to the Trustee’s summary judgment motion.

On June 14, 1996, a UCC-1 Financing Statement was filed with the Tennessee Secretary of State showing T.R. Systems, Inc. as debtor, and T.R. Shelby and Emily Shelby, the Defendants, as secured parties. This Financing Statement, including the collateral list attached as “Exhibit A,” was also filed with the Decatur County Register on June 5, 1996. Following is the collateral list:

Exhibit A

- 1 - Transcriber
- 2 - Copiers
- 3 - IBM Computers
- Office Furniture
- Misc. Office Equipment
- 1 - Novatelle Phone
- 1 - Motorola Mobile Phone
- 1 - Gelco Office Trailer (SN # 84051327)
- Misc. Tools and Equipment
- 1 - Egal Tuf-CTU (SN # 793413)
- 1 - Columbus McKinnon Tire Shredder (SN # E-9131)
- 1 - Columbus McKinnon Tire Shredder (SN # E-9316)
- 1 - CM Classifier/Conveyor System (SN # E-9313)
- 1 - Magnet Head (SN # 23307)
- 1 - Nise-Hog with Access Valve (SN # 19330)

2 - Conveying Systems

1 - 1992 Ford F250 PK (4532)

1 - 1988 Ford F150 PK (6444)

1 - 1992 Utility Trailer

7 - 1984 Model Honn Pup Trailers (SN #'s 4805, 5520, 8502, 8486, 4698, 8258, & 4568)

Disconnects Electric:

1 - Soft Start #5

1 - 1974 Ford Box Truck

24,000 tons of tire shreds located at 2850 Steam Plant Road, Memphis, Tennessee

On September 15, 1997, the Debtor entered into a contract with Shelby County, Tennessee, to clean up waste tire materials located at 1288 Florida Street in Memphis, Tennessee. The Debtor completed its services prepetition, and the County paid \$118,741.00 to the Trustee, pursuant to the contract. The State of Tennessee documented removal of the shredded and whole tires from the site on June 4, 1998.

On October 27, 1997, First Bank in Lexington, Tennessee, issued a \$ 134,591.00 certificate of deposit to "T.R. Systems, Inc. and Tennessee Department of Environment and Conservation." The State of Tennessee held the certificate of deposit as a performance bond in connection with the solid waste clean-up project undertaken by the Debtor. The Trustee made a formal demand for turnover of the certificate of deposit on May 21, 1998, and after inspecting the subject facility and documenting proper closure on June 4, 1998, the State of Tennessee tendered and released the certificate of deposit to the Trustee.

DISCUSSION

The Defendants claim a perfected security interest in the certificate of deposit issued to "T.R. Systems, Inc. and Tennessee Department of Environment and Conservation." A certificate of deposit is

an instrument. See TENN. CODE ANN. § 47-3-104(j) (1996); *Continental Bankers Life Ins. Co. of the South v. Bank of Alamo*, 578 S.W.2d 625, 630 (Tenn. 1979) (stating that a certificate of deposit is an instrument and whether negotiable or non-negotiable is subject to the commercial paper statute). Cf. *First State Bank v. Morristown Lincoln-Mercury, Inc.*, *Stair v. Hamilton Bank of Morristown (In re Morristown Lincoln-Mercury, Inc.)*, 27 B.R. 801 (Bankr. E.D. Tenn. 1983) (holding that a reserve account was money and could be perfected only by possession). “A security interest in money or instruments (other than certificated securities or instruments which constitute part of chattel paper) can be perfected only by the secured party’s taking possession, except as provided in subsections (4) and (5) of this section and § 47-9-306(2) and (3) on proceeds.” TENN. CODE ANN. § 47-9-304 (1996) (amended in 1997 to delete reference to certified securities). The State of Tennessee had possession of the certificate of deposit until its June 4, 1998, inspection of the subject facility and subsequent tender and release of the certificate of deposit to the Trustee. The Defendants have not alleged that they had possession of the certificate of deposit, and under Tennessee law, absent possession, they have no perfected security interest therein. Their argument that they provided the funds to purchase the certificate of deposit is overcome by the fact that the certificate was issued to the Debtor and the state’s department.

The Defendants claim a perfected security interest in the contract with Shelby County. A contract is “the total legal obligation which results from the parties’ agreement as affected by . . . any . . . applicable rules of law.” TENN. CODE ANN. § 47-1-201(11) (1996 & Supp. 1998). Tennessee has eliminated the term “contract right” from the statute governing perfection and defines “any right to payment for goods sold or leased or for services rendered which is not evidenced by an instrument or chattel paper, whether or not it has been earned by performance” as an account. *Id.* § 47-9-106. Perfection of a security interest in an

account requires filing of a financing statement describing the account. *Id.* § 47-9-302. “[A]ny description of personal property . . . is sufficient whether or not it is specific if it reasonably identifies what is described.” *Id.* § 47-9-110 (1996). The financing statement does not list an account or a contract right, and the Defendants base their security interest in the contract on the statement’s listing of “24,000 tons of tire shreds located at 2850 Steam Plant Road, Memphis, Tennessee.” The “test of sufficiency of a description laid down by this section is that the description do the job assigned to it—that it make possible the identification of the thing described.” *Id.* cmt. The financing statement’s reference to tire shreds does not alert one to the existence of a contract, and the Defendants have not presented the Court with cases finding a perfected security interest in a contract when a financing statement did not list an account or a contract right. The financing statement fails to identify the contract for services and leaves the Defendants without a perfected security interest therein.

The Defendants assert perfected security interests in the Eagle Tire cutter, Clark Michigan loader, William Nife hog, and propane forklift truck, none of which are listed specifically in the financing statement. Equipment is a good that must be perfected by filing a financing statement “indicating the types, or describing the items, of collateral.” TENN. CODE ANN. § 47-9-402(1) (1996 & Supp. 1998). *See id.* §§ 47-9-109(2), 47-9-302. The financing statement lists “Misc. Office Equipment” and “Misc. Tools and Equipment,” sufficiently identifying the type of collateral, but the Trustee argues that specific descriptions of some equipment in the financing statement overcome the general reference to equipment. Tennessee adopted a system of “notice filing,” which requires interested parties to make further inquiry and results in case-by-case determinations of whether a description reasonably identifies the collateral. *See id.* § 47-9-402 cmt.2; *id.* § 47-9-110; *International Harvester Credit Corp. v. Nicholls (In re Richards)*, 455

F.2d 281, 282 (6th Cir. 1972) (providing system of notice filing was the fundamental purpose of the Uniform Commercial Code); *Cookeville Prod. Credit Ass'n v. Frazier*, 16 B.R. 674, 679 (Bankr. M.D. Tenn. 1981) (describing a case-by-case determination).¹ “Our first step in evaluating these financing statements is to determine whether these statements provide adequate notice ‘so that a subsequent creditor would reasonably make further inquiry.’” *CLC Equip. Co. v. Brewer (In re Value-Added Communications, Inc.)*, 139 F.3d 543, 545 (5th Cir. 1998). Because a reasonable inquiry may include a search for the security agreements, *see In re Richards*, 455 F.2d at 284,² and there has been no offer of proof of underlying security agreements in this proceeding, this Court is unable to determine whether the financing statement provides sufficient notice of interests in these four pieces of equipment until the parties

¹ A person has “notice” of a fact when:

- (a) he has actual knowledge of it;
- (b) he has received a notice or notification of it; or
- (c) from all the facts and circumstances known to him at the time in question he has reason to know that it exists.

A person “knows” or has “knowledge” of a fact when he has actual knowledge of it. “Discover” or “learn” or a word or phrase of similar import refers to knowledge rather than to reason to know.

TENN. CODE ANN. § 47-1-201(25)(1996 & Supp. 1998). “In light of that definition of knowledge, [TENN. CODE ANN. § 47-9-301(1)(b), (3) (1996 & Supp. 1998)] reflects a policy that a judgement lien creditor not be denied priority because he might have discovered the security interest.” *In re DG & Assocs., Inc.* 9 B.R. 94, 98 (Bankr. E.D. Tenn. 1981) (holding that the bank’s interest became unperfected because it failed to re-file a financing statement after learning of the debtor’s name change). “The underlying purpose of filing a financing statement is to give notice of the security interest. UCC § 9-402, Cmt. 2. To that end a financing statement must be accurate enough to give notice. UCC § 9-402(1) & (5). The general rule is that a security interest is not perfected by a filed financing statement which through some fault of the secured party does not give notice.” *Id.* at 96.

² The Fifth Circuit, unlike dicta in the Sixth Circuit’s opinion, *In re Richards*, 455 F.2d at 284, concluded that a reasonable inquiry did not include looking at the security agreement. *See In re Value-Added Communications, Inc.*, 139 F.3d at 546 n.5 (stating that “Article 9 financing statements are intended to give notice of the collateral covered by security interest”).

have an opportunity to present the Court with any relevant security agreement.³

The Court will observe, however, if the only issue of sufficiency of notice concerns the Eagle Tire Cutter, the financing statement contains a specific listing of “1-Egal Tuf-CTU (SN # 793413),” which the Defendant’s counsel pointed out at oral argument was quite close to the actual equipment description, “Eagle Tire cutter, serial number 793413.” The serial number is the same, and the financing statement appears to describe this equipment closely enough to place a third party on notice of a possible security interest claim. Also, the Trustee sold a “Williams Nife hog, serial number 198436,” while the financing statement described a “Nise-Hog (SN # 19330).” Here, the name is close enough to place a third party on notice, but the difference in serial number may indicate that another Nife (or Nise) hog existed. The latter discrepancy illustrates why a fact question exists as to the equipment.

CONCLUSION

This Court concludes that the bankruptcy estate’s interests in the contract and the certificate of deposit are not subject to any valid perfected security interests of the Defendants, and the Court grants the Trustee’s motion for summary judgment with regard to the contract and certificate of deposit. Pursuant to TENN. CODE ANN. § 47-9-301(1)(b), (3) (1996 & Supp. 1998), the unperfected security interests are subordinate to the rights of the Trustee. The Court cannot determine whether the estate’s interest in the Eagle Tire cutter, Clark Michigan loader, Williams Nife hog, and propane forklift truck are subject to any

³ The Court notes that the Trustee’s summary judgment motion did not rely upon the lack of a security agreement, and the Court is aware that a financing statement may also constitute a security agreement; however, a sufficient fact issue exists to prevent summary judgment as to the equipment.

valid perfected security interests until the Court has evidence of any relevant security agreement, and the Court denies summary judgment as to said equipment. A separate order will be issued, and that order will provide notice of a further opportunity to present proof of any security agreement of the equipment.

WILLIAM HOUSTON BROWN
UNITED STATES BANKRUPTCY JUDGE

DATED: _____

Russell W. Savory
Gotten, Wilson & Savory, PLLC
Attorney for Trustee
200 Jefferson Avenue, Suite 900
Memphis, TN 38103

James W. Surprise
Attorney for Defendants
780 Ridge Lake Blvd., Suite 202
Memphis, TN 38120