

# CHAIR'S COLUMN

March 2009



The UCC Committee is continually striving to provide its members on a timely basis with important information about developments in commercial law and commercial practice. Anyone with a suggestion for a project the Committee should undertake or with an idea about how the Committee can better fulfill its mission should contact me.

## Proposed PEB Commentary

The Permanent Editorial Board for the Uniform Commercial Code has proposed a new commentary relating to UCC sections 4A-502(d) and 4A-503. The proposed commentary provides that neither the originator nor the beneficiary of a funds transfer has any property claim to the value held by an intermediary bank and, therefore, neither a creditor of the originator nor a creditor of the beneficiary may attach that value by levy, garnishment or the like. A full copy of the proposed commentary appears at the end of this column. Anyone wishing to comment on the proposal may do so by May 8. Instructions on where to submit comments are on the first page of the proposal.

## Article 9 Revisions

The Joint Review Committee for Article 9 of the Uniform Commercial Code held its third meeting on March 6-8 in Chicago. A complete report of that meeting is available on the UCC Committee [web page](#). The Joint Review Committee plans to have a draft set of revisions ready for a first reading at the ULC's annual meeting this summer. After further Committee review, the revisions will be presented to the ALI for consideration and approval in the spring of 2010 and to the ULC for consideration and approval in the summer of 2010.

## Spring Meeting

As you no doubt know by now, the Spring Meeting of the ABA Business Law Section will be in Vancouver this year from April 16-18th. A complete copy of the Committee's schedule is attached, but here are a few highlights.

### Programming

The UCC Committee is sponsoring three CLE programs during the meeting:

***Non-uniformity: Is It the Spice of Life or a Recipe for Disaster?***

**Thursday, April 16 at 2:30-4:30pm**

***How Well Do You Know Your Neighbor? What's New and What's Different about Canadian Secured Transactions***

**Friday, April 17 at 2:30-4:30pm**

***What Every Commercial Lawyer Needs to Know About the Restatement (Third) of Restitution and Unjust Enrichment***

**Saturday, April 18 at 1:00-3:00pm**

***Stump the Chumps Returns!***

On Friday April 17 at 1:30-2:30pm, the Committee's ever popular *Stump the Chumps* will be making a return after a one-year hiatus. Attendees will be given the opportunity to pose questions to a panel of commercial law experts consisting of:



Kristen D. Adams



Katherine S. Allen



E. Carolan Berkley



Richard L. Goldfarb



Norman M. Powell

Questions may also be submitted in advance by e-mail to me at [ssepinuck@lawschool.gonzaga.edu](mailto:ssepinuck@lawschool.gonzaga.edu).

***UCC Committee Award for Exceptional Service***

Also at 1:30pm on Friday, April 17, immediately before *Stump the Chumps* begins, the Committee will bestow its Award for Exceptional Service on a most worthy individual. Past recipients are Fred Miller (2006) and Barkley Clark (2007). Come help us honor a colleague who has dedicated amazing amounts of time and energy to the improvement of commercial law generally and the UCC in particular.

***UCC / ComFin Dinner***

Finally, the UCC Committee and the Commercial Finance Committee will be holding their customary joint dinner on Thursday, April 16. A copy of the registration form for that dinner is also attached. I hope to see you in Vancouver.

Stephen L. Sepinuck  
Professor, Gonzaga University School of Law  
[ssepinuck@lawschool.gonzaga.edu](mailto:ssepinuck@lawschool.gonzaga.edu)

**BUSINESS LAW SECTION SPRING MEETING**  
**APRIL 16-18, 2009**  
**Vancouver, BC**

Thursday, April 16			
Time	Commercial Finance		UCC
9:00-9:30am			
9:30-10:00am	Joint Subcm. Mtg: Int'l Com. Law (UCC) & Cross-Border Secured Trans. (ComFin)	Joint Subcommittee Meeting: Leasing (UCC) & Lease Financings (DBF)	
10:00-10:30am			
10:30-11:00am	<b>Program: Syndicated Loan Markets in the U.S. and Canada</b>		
11:00-11:30am			
11:30-12:00pm			
12:00-12:30pm			
12:30-1:00pm			Subcommittee Meeting: Letters of Credit:
1:00-1:30pm	Subcommittee Meeting: Creditors' Rights	Subcommittee Meeting: Loan Documentation	Joint Subcommittee Meeting: General Provisions & Sales
1:30-2:00pm			
2:00-2:30pm			
2:30-3:00pm	Subcommittee Meeting: Loan Workouts	Subcommittee Meeting: Aircraft Financing (starts at 2:00)	<b>Program: <i>Non-uniformity: Is It the Spice of Life or a Recipe for Disaster?</i></b>
3:00-3:30pm			
3:30-4:00pm	Subcommittee Meeting: Lender Liability		
4:00-4:30pm			
4:30-5:00pm			
5:00-5:30pm			
5:30-6:00pm			
6:00-6:30pm			UCC/Com Fin Joint Dinner
6:30-7:00pm			
7:00-7:30pm			
7:30-8:00pm			
8:00-8:30pm			

**Friday, April 17**

<b>Time</b>	<b>Commercial Finance</b>	<b>UCC</b>
8:00-8:30am	<div style="display: flex; justify-content: space-between;"> <div style="width: 30%; border-right: 1px solid black; padding-right: 5px;">                     Subcommittee Meeting: Aircraft Financing                 </div> <div style="width: 30%; border-right: 1px solid black; padding-right: 5px;">                     Subcommittee Meeting: Agricultural &amp; Agri-Business Financing                 </div> <div style="width: 30%; padding-left: 5px;">                     Subcommittee Meeting: Investment Securities:                 </div> </div>	
8:30-9:00am		
9:00-9:30am		
9:30-10:00am		
10:00-10:30am		
10:30-11:00am		
11:00-11:30am		
11:30-12:00pm		
12:00-12:30pm		
12:30-1:00pm	Task Force Meeting: Model Intercreditor Agreement	Joint Subcommittee Meeting: Payments: Discussion of ULC Payment Study Project
1:00-1:30pm		
1:30-2:00pm		<b>Committee Meeting: <i>Stump the Chumps &amp; Presentation of UCC Award of Exceptional Service</i></b>
2:00-2:30pm	<b>Committee Forum: <i>How Well Do You Know Your Neighbor? What's New and What's Different about Canadian Secured Transactions</i></b>	
2:30-3:00pm		
3:00-3:30pm		
3:30-4:00pm		
4:00-4:30pm	Subcommittee Meeting: IP Financing	
4:30-5:00pm	Leadership Meeting	Leadership Meeting
5:00-5:30pm		
5:30-6:00pm		
6:00-6:30pm		
6:30-7:00pm		
7:00-7:30pm		
7:30-8:00pm	Section Dinner	
8:00-8:30pm		
8:30-9:00pm		

**Saturday, April 18**

Time	Commercial Finance	UCC
8:30-9:00am	Joint Subcommittee Meeting: Secured Lending (Com Fin) & Secured Transactions (UCC)	
9:00-9:30am		
9:30-10:00am		
10:00-10:30am	Joint Task Force Meeting on Commercial Finance Terms	
10:30-11:00am	<b>Program: <i>Commercial Law Developments</i></b> <b>(UCC co-sponsoring)</b>	
11:00-11:30am		
11:30-12:00pm		
12:00-12:30pm		
12:30-1:00pm	Subcommittee Meeting: Real Estate Finance	
1:00-1:30pm		
1:30-2:00pm		
2:00-2:30pm		<b>Program <i>What Every Commercial Lawyer Needs to Know About the Restatement (Third) of Restitution and Unjust Enrichment</i></b>
2:30-3:00pm		
3:00-3:30pm	Joint Task Force Meeting on Filing Office Operations & Search Logic	
3:30-4:00pm		
4:00-4:30pm		
4:30-5:00pm		
5:00-5:30pm		

American Bar Association ♦ Section of Business Law  
**Commercial Finance & Uniform Commercial Code Joint Committee Dinner**

**The Terminal City Club**  
837 West Hastings Street  
Vancouver, BC

**Thursday, April 16, 2009**  
7:00 PM – Cocktail Reception (Cash Bar)  
8:00 PM - 11:00 PM - Dinner

**DINNER RESERVATION FORM**

Name: \_\_\_\_\_ Member ID# \_\_\_\_\_

Firm: \_\_\_\_\_

Address: \_\_\_\_\_

City: \_\_\_\_\_ State: \_\_\_\_\_ Zip: \_\_\_\_\_

Business Telephone: \_\_\_\_\_ Fax: \_\_\_\_\_

Accompanied by: \_\_\_\_\_

Are special arrangements needed for the physically challenged? \_\_\_\_\_

**DINNER FEE**

\_\_\_\_\_ # of tickets @ \$100 each = \$ \_\_\_\_\_

Please let us know of any special dietary needs you may have: \_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

**METHOD OF PAYMENT**

\_\_\_\_\_ Enclosed check (made payable to the American Bar Association)

\_\_\_\_\_ MasterCard \_\_\_\_\_ Visa \_\_\_\_\_ American Express

Card #: \_\_\_\_\_ Exp. Date: \_\_\_\_\_

Signature: \_\_\_\_\_

**Please return this registration form and your payment no later than March 26, 2009; 5:00PM Central Standard Time to:**

Toyin Alaka  
American Bar Association ♦ Section of Business Law  
321 N. Clark Street  
Chicago, IL 60654  
[alakat@staff.abanet.org](mailto:alakat@staff.abanet.org)  
Phone (312) 988-5564; Fax (312) 988-5578

*(Faxed reservations must include credit card payment)*

**Refund Policy: Requests for refunds on ticketed events will be granted only if the request is received in writing prior to Thursday, March 26, 2009. No refunds will be granted after that date. To request a refund, please email Toyin Alaka at the above email address.**

**Permanent Editorial Board for the Uniform Commercial Code**

**PEB COMMENTARY NO. \_\_\_\_  
SECTIONS 4A-502(d) and 4A-503**

**Draft for Public Comment**

**February 27, 2009**

*Comments on this draft must be submitted by no later than May 8, 2009.*

Comments may be submitted as follows:

by email to [ddissinger@ali.org](mailto:ddissinger@ali.org)

or

by mail to  
Deanne Dissinger, Associate Deputy Director  
The American Law Institute  
4025 Chestnut Street  
Philadelphia, PA 19104

This draft is available online at:

[www.ali.org/index.cfm?fuseaction=projects.proj\\_ip&projectid=4](http://www.ali.org/index.cfm?fuseaction=projects.proj_ip&projectid=4).

PEB COMMENTARY NO. \_\_\_\_  
SECTIONS 4A-502(d) and 4A-503

## INTRODUCTION

A funds transfer is a series of payment orders starting with an originator's order to the originator's bank to cause a sum certain amount of money to be paid to a beneficiary. The series of payment orders culminates with a beneficiary bank crediting the account of a beneficiary for that sum certain. U.C.C. § 4A-104(a) (definition of funds transfer). Generally the originator owes the beneficiary a debt and the series of payment orders is a mechanism used to make a transfer of value through the debiting and crediting of bank accounts from the originator to the beneficiary. The funds transfer often involves one or more intermediary banks that receive a payment order from the originator's bank or another bank and that intermediary bank issues its own payment order to another bank or the beneficiary's bank. Several cases have raised the issue of whether a creditor of the beneficiary may serve creditor process on an intermediary bank and thus "capture" the value transfer while it is in process.

Article 4A provides that the creditor of the beneficiary may not serve creditor process on any bank other than the beneficiary's bank. U.C.C. § 4A-502(d). Official Comment 4 to Section 4A-502 further explains the concept:

A creditor of the originator can levy on the account of the originator in the originator's bank before the funds transfer is initiated . . . but cannot reach any other funds *because no property of the originator is being transferred*. A creditor of the beneficiary cannot levy on property of the originator and until the funds transfer is completed by acceptance by the beneficiary's bank of a payment order

for the benefit of the beneficiary *as the beneficiary has no property interest in the funds transfer which the beneficiary's creditor can reach* (emphasis supplied).

Official Comment to Section 4A-503 further explains both Sections 4A-502(d) and 4A-503 are designed to prevent interruption of a funds transfer after it has been set in motion and that, in particular, intermediary banks are protected.

A funds transfer is a series of payment orders that create contractual obligations only as to the sender and receiver of each payment order. Those contractual obligations are not the property of either the originator or the beneficiary. In a simple funds transfer, the originator instructs its bank, the originator's bank, to debit the originator's account and order the beneficiary's bank to credit the beneficiary. Those instructions are payment orders. U.C.C. § 4A-103 (definition of "payment order," "beneficiary" and "beneficiary's bank"; § 4A-104 (definition of "funds transfer," "originator" and "originator's bank"). See also Regulation J, 12 C.F.R. § 210.26 (governing payment orders issued to or by the a federal reserve bank). The originator is the "sender" of the payment order and the originator's bank is the "receiving bank." U.C.C. § 4A-103 (definitions of "sender" and "receiving bank"). If the originator's bank accepts the originator's payment order, the originator owes an obligation to the originator's bank to fund that payment order with sufficient credits to pay the amount of the payment order. U.C.C. § 4A-402(b). The originator's bank owes an obligation to the originator to execute the accepted payment order according to the instructions of the originator. U.C.C. § 4A-302.

In execution of the originator's payment order, the originator's bank may send its own payment order to the beneficiary's bank, but more commonly it will send its payment order to an intermediary bank. U.C.C. § 4A-104 (definition of "intermediary bank"). The originator's bank

is the sender of its payment order and the intermediary bank is the receiving bank of that second payment order. Upon acceptance of that second payment order, the intermediary bank owes an obligation to the originator's bank, not the originator, to execute its own payment order that replicates *the originator's bank's payment order* (emphasis supplied). U.C.C. § 4A-302 (obligation in execution owed by receiving bank to its sender). The originator's bank, not the originator, owes payment of the originator bank's payment order to the intermediary bank. U.C.C. § 4A-402(b) (sender owes obligation to pay the amount of an accepted payment order to its receiving bank). In the event the originator does not have sufficient credits to cover its payment order, but the originator's bank's payment order has been accepted by the intermediary bank, the originator's bank still owes a payment obligation to the intermediary bank. The intermediary bank has no right of recovery against the originator, but only has a right of recovery against the originator's bank (its sender) for payment of the payment order.

Further, the intermediary bank will then issue its own payment order to the beneficiary's bank for the beneficiary's bank to credit the account of the beneficiary when the beneficiary's bank accepts that payment order. Accordingly, the intermediary bank owes an obligation to pay for that order to the beneficiary bank, not the beneficiary. U.C.C. § 4A-402(b). Upon the beneficiary bank's acceptance of the payment order, it is the beneficiary's bank that owes an obligation to pay the beneficiary, usually by crediting an account of the beneficiary. U.C.C. § 4A-404. See also Regulation J §§ 210.28, 210.29, 210.30, 210.31 and 210.32.

In summation, under the Article 4A structure, the issuance and acceptance of payment orders create rights and obligations only as between (i) the sender of the payment order and its receiving bank (e.g., between originator and originator's bank as to the originator's payment

order), (ii) the originator's bank and an intermediary bank as to the originator's bank's payment order, and (iii) the beneficiary bank that has accepted a payment order and the beneficiary.

Accepted and executed payment orders thus create contractual obligations that result in a series of credits and debits to bank accounts rather than transferring property of the originator to the beneficiary.<sup>1</sup> A receiving bank owes its contractual obligation to its sender in execution of the payment order and the sender owes its contractual obligation to pay the amount of the payment order to its receiving bank. The intermediary bank has no contractual obligation to the originator or beneficiary and neither the originator or the beneficiary have any contractual obligation to the intermediary bank. Thus, credits in an intermediary bank are credits in favor of the originator's bank, *and are not property of either the originator or the beneficiary* (emphasis supplied).

## DISCUSSION

In a series of cases applying Admiralty Rule B regarding attachment, the federal courts in New York have held that the intermediary bank in a funds transfer is holding "property" of the originator or beneficiary and have thus allowed creditor process on an intermediary bank in an effort to collect a debt owed by either the originator or the beneficiary (as the case may be).<sup>2</sup>

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<sup>1</sup>This analysis is the same as that under Uniform Commercial Code Article 8 § 8-502 in the context of the indirect holding system for securities. That process also involves credits and debits to "securities accounts." Official Comment 2 to § 8-502 states that because securities trades are typically settled on a net basis (as are funds transfers under § 4A-403), it would ordinarily be impossible for anyone to trace the path of any particular security. Even if there were only one trade, however, the "security entitlement of the buyer [in the Article 4A context, the credit to the beneficiary's account] *is not the same item of property that formerly was held by [seller] . . . , but is a new package of rights that . . . [buyer] acquired against [the securities intermediary]*" (emphasis supplied).

<sup>2</sup>Federal Rules of Civil Procedure, Supplemental Rules for Certain Admiralty and Maritime Claims, Admiralty Rule B(1)(a) permits attachment of "the defendant's tangible or intangible personal property" in the hands of named garnishees and thus allows garnishment of such property held by a bank.

*See, e.g.,* Winter Storm Shipping, Ltd. v. TPI, 310 F.3d 263 (2d Cir. 2002), cert. den. 539 U.S. 927 (2003); Aqua Stoli Shipping Ltd. v. Gardner Smith Pty Ltd., 460 F.3d 434 (2d Cir. 2006); Consub Delaware LLC v. Schahin Engenharia Limitada and Standard Chartered Bank, 534 F.3d 104 (2d Cir. 2008); Navalmar (U.K.) Ltd. v. Welspun Gujarat Stahl Rohren, Ltd., 485 F. Supp. 2d 399 (S.D.N.Y. 2007); Compania Sudamericana de Vapores S.A. v. Sinochem Tianjin Co., 2007 WL 1002265 (S.D.N.Y. 2007); but see Seamar Shipping Corp. v. Kremikovtzi Trade Ltd., 461 F. Supp. 2d 222 (S.D.N.Y. 2006).

These decisions stem from the opinion of the court in *Winter Storm* that the value held by the intermediary bank is property of either the originator or the beneficiary. Under Article 4A, which is also adopted federal law in Regulation J for funds transfers through a federal reserve bank, the originator does not have any claim against the intermediary bank for return of the value in the event the funds transfer is not completed. Rather the only party with a claim against the intermediary bank is the sender to that bank, which is typically the originator's bank. In an uncompleted funds transfer, it is the originator's bank that must refund the value to the originator. U.C.C. § 4A-402(d). The intermediary bank owes its refund obligation to its sender, the originator's bank, not the originator. The originator's bank must refund to the originator even if it cannot recover from the intermediary bank.<sup>3</sup> The beneficiary likewise has no claim to

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<sup>3</sup>A simple example illustrates these courts' error in conflating privity based contract claims between two parties to create property rights in a third party. Assume A owes B an obligation, B owes C an obligation, and C owes D an obligation. Under garnishment law, D cannot garnish A to satisfy the obligation C owes D. A holds no property of C (A owes B). Now substitute the Article 4A terms to this simple example. A is the intermediary bank who has received payment of a payment order issued by B, the originator's bank, and C is the originator. D is the garnishing creditor. The court in *Winter Storm* and its progeny have in essence allowed D (the originator's creditor) to garnish A (the intermediary bank) to collect on the debt C (the originator) owes to D.

any payment from the intermediary bank. The beneficiary's only claim to the funds is against its bank, the beneficiary bank, and then only when the beneficiary bank has accepted the payment order. U.C.C. § 4A-404. The intermediary bank thus holds no property of either the originator or the beneficiary. Since Admiralty Rule B does not define what is "property" of a party, normally courts look to other law on that issue.

Other law is sufficient to define the parties' rights in a funds transfer. Article 4A is uniform law, enacted in every state in the United States, and Regulation J, which adopts in large part Article 4A's provisions, is uniform in applying to all funds transfers through the federal reserve system. Both define uniformly the rights of parties in a funds transfer. The *Consub* court reasoned that leaving the functional usefulness of Rule B attachments to the vagaries of the laws of fifty states would create a measure of anarchy, but was seemingly unaware that U.C.C. Article 4A is uniform law in all U.S. jurisdictions and is adopted federal law.<sup>4</sup> The court also failed to explain how Rule B provides any basis for determining whether anyone had any "property" rights in the value held at the intermediary bank.<sup>5</sup>

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<sup>4</sup>The courts following *Winter Storm* have ignored not only the applicable law directly on point regarding property rights, but have also ignored applicable precedent pre-dating Article 4A. The court in *Reibor International Limited v. Cargo Carriers (Kacz-Co.) Ltd.*, 759 F.2d 262 (2d Cir. 1985) considered whether the CHIPS credit involved was property subject to attachment under the Admiralty Rules. The court said that federal law generally governs questions as to the validity of Rule B attachments, but the Admiralty Rules themselves offered little guidance and so the court agreed with the district court that state law more directly in point should be turned to. This is entirely consistent with respect to other contexts where federal law relies on state law to determine whether property is involved, such as in bankruptcy. *See, e.g., Butner v. United States*, 440 U.S. 48 (1979). The court also stated it turned to state law partly to minimize disruptive divergences between state and federal law, freeing garnishees from the burden of keeping track of yet another difference between state law and federal law.

<sup>5</sup> The *Consub* court also believed that the *Winter Storm rule* was not shown to be unworkable. Note that U.C.C. Article 4A is substantially premised on the ability to net obligations because of the large sums involved. U.C.C. § 4A-403. If a particular creditor can

## CONCLUSION

In uniform law under UCC Article 4A and under Regulation J, neither the originator or the beneficiary of a funds transfer have any property claim to the value held by an intermediary bank in a funds transfer. Thus, neither a creditor of an originator nor the creditor of a beneficiary may successfully issue creditor process<sup>6</sup> to an intermediary bank as the intermediary bank is not holding property of either the originator or the beneficiary. To the extent that the cases cited earlier indicate to the contrary, that reasoning is disapproved and should not be followed.

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seize funds and frustrate that plan, the resultant systemic risk may well provide the demonstration that the *Winter Storm* approach and its progeny is unworkable.

<sup>6</sup> “Creditor process” means levy, attachment, garnishment, notice of lien, sequestration, or similar process issued by or on behalf of a creditor or other claimant with respect to an account. As to “account,” see “authorized account” defined in § 4A-105(a)(1).