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Bulk Transfers

By ROBERT S. DORSEY

The Uniform Commercial Code, as enacted by the Kentucky Legislature in 1958, is scheduled to become a part of the Kentucky Revised Statutes on July 1, 1960. The UCC contains an article on bulk transfers and repeals the present Kentucky Bulk Sales legislation. Insofar as major changes in present law, the effect of the UCC on bulk transfers is more apparent than real.

BACKGROUND

Bulk sales legislation is designed for the protection of creditors of the dishonest merchant. Its origin in this country goes back to the turn of the century, and now all states have some sort of legislation covering bulk sales or transfers. Generally speaking, bulk sales statutes have been confined to sales in bulk by the ordinary merchant of his usual merchandise. But to the practitioner in advising a particular client, such statements and the decisions are not always helpful, because each situation must stand on its own facts and the statute speaks only in general and frequently undefined terms. In commercial practice today, the bulk sales law is often more of an impediment to business than a benefit. It is usually impossible to comply strictly with the terms of the law, particularly where the assets of a reasonably large enterprise are being sold. As a going concern, its creditors come and go, and business cannot stop to ascertain all creditors at a given point in time. Yet the careful practitioner is reluctant, and rightfully so, to give an unconditional opinion that the bulk sales law does not apply to a particular transaction or that his client has complied.

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1 Hereinafter referred to as UCC.


3 See Note, 33 Harv. L. Rev. 717 (1920).

**PRINCIPLES OF SOME KENTUCKY DECISIONS**

The Kentucky Bulk Sales Act is constitutional, and not an unreasonable interference with property rights. A sale in violation of the Bulk Sales Act is merely *voidable* at the option of the creditor who pursues his remedy within the statutory period, and a seller may validate a sale made without notice by paying or otherwise satisfying his creditors.

It has also been held that any lien which may arise by virtue of the Bulk Sales Act is discharged by the prompt payment of creditors as their bills fall due. But the Kentucky Court of Appeals has held that a petition which simply alleged that the buyer purchased in bulk all the merchandise and all the fixtures of the business in violation of the Bulk Sales Act set forth a sufficient cause of action although the type of business involved was not mentioned. However, it has been made clear that the Bulk Sales Act is solely for the benefit of creditors of the seller. As between the buyer and the seller, a sale in violation thereof is neither void nor voidable. As stated by Corbin, the ordinary bulk sales statute "merely makes it [the sale] voidable against both parties for the benefit of creditors."

**DEFINITION**

Section 6-102 defines "bulk transfers" 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 (Section 9-109) of an enterprise subject to this Article. [Emphasis added.]

Section 6-103 lists eight specific types of transfers excepted from Article 6. The exceptions are: (1) transfers to give security for performance of an obligation; (2) general assignments for the benefit of all the transferor's creditors, and subsequent transfers by the assignee; (3) transfers in settlement or realization of a lien or other security interests; (4) sales by personal

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5 Dwiggins Wire Fence Co. v. Patterson, 166 Ky. 278, 179 S.W.2d 244 (1915).
7 Denton v. White, 223 Ky. 640, 4 S.W.2d 412 (1928).
8 Montgomery v. Koch, 251 S.W.2d 235 (Ky. 1952).
9 Dorr v. Smith, 259 S.W.2d 459 (Ky. 1953).
10 6 Corbin, Contracts § 1514 at 977-8 (1951).
representatives, receivers, trustees in bankruptcy, or any public officer under judicial process; (5) sales made in the course of judicial or administrative proceedings for the dissolution or reorganization of a corporation, if notice is sent to the corporation's creditors pursuant to court or administrative agency order; (6) transfers to a person maintaining a known place of business in Kentucky who becomes bound to pay the debts of the transferor in full and gives public notice thereof, and is solvent thereafter; (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 if the transferee assumes the debts of the transferor and receives nothing from the transaction except an interest in the new enterprise junior to the claims of creditors; and (8) transfers of property exempt from execution.

Also excluded from the application of Article 6, by the definition of "bulk transfer" as set forth in section 6-102(1), is any transfer in bulk which is in the ordinary course of the transferor's business. Thus, Article 6 attempts to place no obstacle in the face of transactions in the ordinary course of a business.

The definition of "bulk transfer" also provides that the transfer, in order to be subject to the proscriptions of the law, must be of a major part of the materials, supplies, merchandise, or other inventory of a business subject to this Article.

The words of limitation, "a business subject to this Article," are defined in section 6-102(3) as:

enterprises . . . whose principal business is the sale of merchandise from stock, including those who manufacture what they sell.

Although this writer is not aware of a Kentucky decision expressly upon the point of whether the sale of a manufacturing plant and other assets of a business are covered by our present Bulk Sales Act, under bulk sales laws similar to that of Kentucky it has been held that such transactions are not within the purview of such laws. It would seem that this result should follow under the UCC. It has been suggested that the words "includ-

11 UCC § 6-102(1).
12 As defined in UCC § 9-109.
13 Ramey-Milburn Co. v. Sevick, 159 Ark. 358, 252 S.W. 20 (1923) (one veneer mill and four sawmills); Gitt v. Hoke, 301 Pa. 31, 151 Atl. 585 (1930), (entire plant which manufactured penholders and can openers).
ing those who manufacture what they sell,” are not applicable to manufacturers in general but apply only to “those manufacturers who are principally engaged in the sale of merchandise from stock (e.g., a small bakery which sells retail).” That this is the best view seems obvious if Article 6 is to protect those persons whom it was designed to protect, i.e., creditors who became such in reliance upon the debtor’s merchandise, but is not to serve as an impediment to bulk transfers by persons where such reliance was not a factor in the establishment of the debtor-creditor relationship.

**Subject Transfers — Compliance**

If it is determined that the bulk transfer contemplated is covered by the UCC, then in order for the transfer to be effective against creditors of the transferor certain steps must be followed.

The seller must prepare a verified list of his existing creditors and a schedule of the property transferred. The buyer must preserve the list and schedule for six months and permit the inspection and copying of such list and schedule or file them in the office of the county court clerk. The list of creditors must contain the names and business addresses of the creditors, the amounts due them, when known, and the names of all persons asserting claims against the transferor and known to him, even though such claims are in dispute.

If the foregoing steps are followed, the transfer will not be rendered ineffective by errors or omissions in the list of creditors if the transferee had no knowledge thereof. Apparently the “knowledge” required is actual knowledge.

Sections 6-105 and 6-106 are the sections providing the protection to the creditors of the transferor. Section 6-105 states that any subject transfer is ineffective against any creditor of the transferor unless the transferee, at least ten days before he takes possession of the goods or pays for them, whichever first occurs, gives notice of the transfer. The form and manner of the notice to be given is spelled out in section 6-107.

The final requirement and safeguard of the creditors is that

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15 UCC § 6-104(3).
16 UCC § 1-201(25).
the proceeds (purchase price) must be applied by the transferee to pay those debts of the transferor which are either shown on the list furnished or filed in writing in the place stated in the notice sent to the creditors, within thirty days after the mailing of such notice.\textsuperscript{17} With respect to any debts in dispute, the necessary sum may be withheld pending a determination,\textsuperscript{18} and if the consideration to be paid for the merchandise transferred is insufficient to pay all of the creditors, a pro rata payment is directed.\textsuperscript{19}

Section 6-107 provides that the notice required shall state that a bulk transfer is about to be made; the names and business addresses of the transferor and transferee, and all other business names and addresses used by the transferor within three years last past so far as known to the transferee; and whether or not all the debts of the transferor are to be paid in full as they fall due as a result of the transaction, and if so, the address to which creditors should send their bills. If, however, the transferor's debts are not to be paid in full as they fall due, or if the transferee is in doubt on that point, the notice must state in addition: the location and general description of the property to be transferred and an estimate of the total of transferor's debts; address where the schedule of property and list of creditors (as required by section 6-104) may be inspected; whether the transfer is to pay existing debts and if such is the case the amount thereof and to whom owing; whether the transfer is for new consideration, and, if so, the amount thereof, time and place of payment, and time and place where creditors of the transferor are to file their claims.

This notice must be either delivered personally or sent by registered mail to all creditors shown on the section 6-104 list, whether their claims are in dispute or not, and to all other persons known to the transferee to hold or assert claims against the transferor.

The transfer is ineffective against any particular creditor if notice is not given to him within the time limits provided in section 6-105, or if the form and manner of delivery of the notice is not as required by section 6-107.

\textsuperscript{17} UCC § 6-106(1).
\textsuperscript{18} UCC § 6-106(2).
\textsuperscript{19} UCC § 6-106(3).
WHAT CREDITORS ARE PROTECTED?

Section 6-109(1) provides that the transferor's creditors afforded the protection of Article 6 "are those holding claims based on transactions or events occurring before the bulk transfer..." [emphasis added]. However, creditors who become such after the "notice" to creditors is given are not entitled to notice. This latter type creditor is afforded the protection of the article only if he is diligent and files his claim in writing in the place stated in the notice within thirty days after the mailing of such notice.20

Even though a transferee's title to the subject property may be defective because of failure to comply with Article 6, a purchaser from him for value in good faith and with notice of the non-compliance takes title free of such defect.21

"Notice" is defined to include a situation wherein such a purchaser, from all the facts and circumstances known to him at such time, has reason to know that there was such non-compliance.22 A purchaser who pays no value or who takes with notice of the non-compliance takes subject to the defect in title.

The present Kentucky statute of limitations with respect to violations of the Bulk Sales Act is four months. This is extended to six months by the UCC, and in addition the statute is tolled against concealed transfers until discovery.23

AUCTION SALES

There is a special section of Article 6 (section 6-108) relating to bulk transfers by auction.

The seller is required to furnish the auctioneer with a list of his creditors and assist him in the preparation of a schedule of the property to be sold. It is the duty of the auctioneer to receive and retain the list of creditors and prepare and retain the schedule of property for six months as provided in section 6-104. The auctioneer must give notice of the auction personally or by registered mail at least ten days prior thereto to all persons shown on the list of creditors and to all other persons known to him to hold or assert claims against the transferor. The auc-

20 UCC § 6-106(1).
21 UCC § 6-110(2).
22 See UCC § 1-201(25)(c).
23 UCC § 6-111.
tioneer must also see to the application of the net proceeds from the auction sale in accordance with the provisions of section 6-106.

The failure of the auctioneer to comply with the provisions of the subject section does not affect the validity of the sale or the title of the purchasers, but if the auctioneer knows that the auction constitutes a bulk transfer his failure to comply makes him liable to the creditors to the extent of the net proceeds of the auction. If the "auctioneer" consists of several persons their liability is joint and several.

This section effects no substantial change in current Kentucky law. However, it does make possible a literal compliance with the statute which is currently impossible, for at present the auctioneer is literally required to give advance notice of the price to be paid for the goods to be sold which he obviously cannot do.

**Summary**

The provisions of the UCC with respect to bulk transfers would appear to represent some improvement over the present Kentucky bulk sales legislation (Kentucky Revised Statutes, chapter 377). The exceptions provided by subsections (6) and (7) of section 6-103 will cover a great many of the sales and transfers made. Thus, neither the typical corporate sale of assets and assumption of liabilities situation or the incorporation of a proprietorship or partnership will be subject to Article 6 if the tests of section 6-103(6) and (7), respectively, are met. The definition accorded enterprises subject to the article seems to be consistent with present law, and perhaps somewhat clearer, by providing that only those enterprises whose principal business "is the sale of merchandise from stock" are subject. It is unfortunate that the phrase "sale of merchandise from stock" could not have been better defined or otherwise delimited.

The continuance of the present Kentucky law by the UCC in covering bulk sales by auction is beneficial. As stated above, literal compliance with the law by auctioneers will now be possible.

While Article 6 will not serve as a panacea for attorneys whose clients are either creditors of persons about to make bulk transfers or those actually making the transfer, it may to some degree make more salutary the law of bulk transfers.
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