Repledge and Pre-Default Sale of Securities Collateral under Revised Article 9

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REPLEDGE AND PRE-DEFAULT SALE OF SECURITIES COLLATERAL UNDER REVISED ARTICLE 9*

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As used in this article, “Revised Article 9” refers to the 1999 Official Text of Article 9 (version dated March 8, 1999, with errata and amendments dated August 16, 1999 and October 13, 1999), together with conforming changes to other Articles. References to “Revised 9-XXX” and “R. § 9-XXX” are to sections of Revised Article 9. “Former Article 9” refers to the 1995 Official Text of Article 9. References to “Former 9-XXX” and “F. § 9-XXX” are to sections of Former Article 9. Provisions of the UCC outside Article 9 that are identical (or materially identical) in the 1995 Official Text and the 1999 Official Text are referred to simply as “section” and are cited as “U.C.C. § X-XXX.” References to versions of the UCC before the 1995 Official Text are cited as “U.C.C. § X-XXX” with a parenthetical identifying the version.

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INTRODUCTION

Commercial law reform is rarely revolutionary and rarely makes headlines.¹ Revised Article 9 of the Uniform Commercial Code ("UCC") is very much in that tradition of incrementalism. Although the revision rewrites Article 9 in its entirety, it effects no revolution. Nor is it driven by a single guiding theme. Rather, it makes a vast number of relatively modest and more or less unrelated revisions to Former Article 9. Many of the revisions implement recommendations made in the 1992 report by the study group on Article 9 appointed by the UCC's Permanent Editorial Board.² But the drafting committee's mandate was not defined by the study group's recommendations, and so the drafting committee could and did make whatever revisions seemed good to it.

So it came to pass that Revised Article 9 includes revisions addressed to a subject not heralded by the study group report: namely, a secured party's repledge of the debtor's collateral to secure the secured party's own obligation to a third party. These revisions appear in two cryptic provisions, Revised 9-207(c)(3) and 9-314(c), which are decrypted to some extent by lengthy Comments.

Observe that the term "repledge" refers to a pledge of the debtor's collateral by the secured party, to secure the secured party's own obligation to a third person. This is not to be confused with the more familiar situation in which the debtor grants a security interest in the same property to two secured parties, securing obligations which the debtor has to each. In defiance of etymology, repledge is often referred to as "rehypothecation."³ It is increasingly common—

1. Which may be just as well. Thus, the New York Times greeted the original UCC with the deflating headline Commercial Code is Held Defective. N.Y. TIMES, Mar. 12, 1956, at 35 (alluding to the report of the New York Law Revision Commission on the 1952 Official Draft). Still, the UCC is not without its fans among the wider public. For example, many news stories have noted its popularity among members of "anti-government militia groups," who believe only in "Magna Charta, the Bible and the Uniform Commercial Code." Militias Target Local Officials, S.F. HERALD EXAM' R, Mar. 31, 1997, at A-1. Given the proclivity of such groups for filing bogus financing statements against their enemies, a cynic who observes that Revised Article 9 abolishes the requirement that a financing statement be signed by the debtor, see Revised 9-502, and who is ignorant of the good reasons for that change, might be tempted to speculate that the change is in the nature of a reward to a favored interest group in grateful recognition of faithful support. But cf. R. §§ 9-509(a), 9-625(e)(3) (prohibiting unauthorized filings and imposing sanctions for violation of the prohibition).


3. "Hypothecation" derives from hypotheca, a term used in Roman law to denote a
though even less justified—to use the term "rehypothecation" to refer to any pre-default use of collateral by the secured party, including outright sale as well as repledge. This paper avoids the term "rehypothecation," less out of concern for linguistic purity than to avoid the differing connotations it has acquired.

Repledge is not a new idea. The traditional setting for repledge arises from so-called "margin lending" by stockbrokers: that is, the making of a loan by the broker to its customer, representing a portion of the cost of purchasing or carrying securities held by the broker for the customer's account. Margin loans are typically secured by the customer's pledge of those securities (often called "margin securities" in this context) to the broker. Traditionally, few brokers have had the wherewithal to make margin loans out of their own capital, so a broker typically would finance its margin lending by obtaining its own loan from a third party, commonly a bank, securing that loan by repledge of its customers' margin securities. In that setting, repledge has led a vigorous existence, evidenced by reported cases, for well over a century. As we will see, pre-UCC common law allowed a stockbroker to repledge a customer's margin securities, subject to certain limitations, even without the customer's consent. The UCC codified that common-law right in Former 9-207(2)(e). Revised Article 9 carries forward that right, with the common-law limitations removed, in Revised 9-207(c)(3). Repledges of securities are commonplace today, though repledges of other types of collateral seem to be all but unheard of.

Yet repledge has always been treated by successive drafters of the UCC as an ugly and unloved foundling, attended to only after more favored children have been tucked in for the night. The right of repledge did not appear at all in the original 1952 version of the UCC, security device in which the pledgor retains possession of the collateral. See John H. Wigmore, The Pledge-Idea: A Study in Comparative Legal Ideas (pt. 3), 11 HARV. L. REV. 18, 24, 30-31 (1897). It is therefore inappropriate to use "hypothecate" as a synonym for pledge, or "rehypothecate" as a synonym for repledge. However, BLACK'S LAW DICTIONARY 1287 (6th ed. 1990) so defines the term "rehypothecate," and in apparent deference to this common usage the term is used in that sense (in quotation marks) in section 8-504, Comment 2. A closer modern analogue to hypotheca would be the so-called "agreement to pledge," in which a broker grants a security interest in securities without delivery of possession or control. See R. § 9-309(10) & cmt. 6 (using the term "hypothecation" to refer to such transactions).


5. See infra text accompanying notes 19-21.
but rather was added as an afterthought in 1953. In the comprehensive 1994 revision of Article 8, the right of repledge set forth in Former 9-207(2)(e) was not amended, but that provision must be read with artistic license to operate sensibly under Article 8 as revised. Most recently, the provision which reflects the most noteworthy feature of Revised Article 9's theory of repledge, Revised 9-314(c)(2), made its debut in the March 1998 draft, at the very end of the revision process.

It is understandable why repledge has never been high on the agenda of any UCC drafting team. In the first place, in the traditional setting for repledge—that is, the financing by stockbrokers of margin loans to their customers—the state law of pledge was largely displaced by federal laws before the UCC was written. In particular, the property rights of margin customers in margin securities, which historically were crucial to determining how the broker's assets would


7. Former 9-207 by its terms applies only to collateral in the secured party's "possession," and hence does not literally apply to securities held through a securities intermediary or to uncertificated securities. The version of Article 8 in force between 1977 and 1994 contained a separate provision stating that the rights and duties set forth in Former 9-207 apply "to the extent they are applicable" to such nonpossessory securities collateral. See U.C.C. § 8-321(3)(b) (1978 Official Text). The 1994 revision of Article 8 deleted that provision without otherwise covering the subject. That omission was patently a drafting glitch. One way to circumvent it would be to construe broadly the term "possession"; another would be to apply the rules of Former 9-207 as a supplemental principle of law pursuant to section 1-103. Revised Article 9 fixes this glitch as to the right of repledge, in that Revised 9-207(c), which sets forth the right of repledge, now applies to collateral in the secured party's "control" as well as "possession." Curiously, a reference to "control" was not added elsewhere in Revised 9-207. Thus, for example, the basic duty to exercise reasonable care in the custody of collateral, set forth in Revised 9-207(a), literally applies only to collateral in the secured party's "possession." This appears to be a continuation of the same drafting glitch, as it seems unreasonable to suppose that the drafters intended that a secured party have no duty of care in any circumstances as to nonpossessory collateral. To take an extreme example, consider a secured party who knowingly and recklessly holds the securities collateral at a financially shaky intermediary which fails, occasioning loss.
be distributed if the broker went bankrupt, were made all but irrelevant by the enactment in 1938 of section 60e of the then-current Bankruptcy Act. The basic idea embodied in section 60e, though recodified and altered in many details, continues to be the foundation of the distributional schemes applicable to customers of an insolvent stockbroker under today’s law, as set forth in the Securities Investor Protection Act (“SIPA”) and the Bankruptcy Code. Furthermore, since 1940, rules issued by the Securities and Exchange Commission (“SEC”) have strictly regulated repledges of customer securities by stockbrokers.

In the second place, there has been virtually no meaningful case law on repledge, and very little scholarly commentary, since the UCC was promulgated. That too is a consequence of repledge historically having been a tool used almost exclusively by stockbrokers. As a practical matter the legal issues arising from a repledge by a stockbroker—or for that matter any repledge by any securities intermediary—are likely to be litigated only if the intermediary becomes insolvent. If the intermediary is solvent and hence able to produce the customer’s securities on demand, many customers may not know or care what the intermediary does with the securities in the meantime, and any customer who does know, care, and object is apt simply to move her securities to a different intermediary. Until the


12. The only sustained scholarly treatments appear to be 2 GRANT GILMORE, SECURITY INTERESTS IN PERSONAL PROPERTY § 42.10, at 1155-60 (1965), and Johnson, supra note 4.

13. For rare exceptions, see Bronner v. Goldman, 236 F. Supp. 713, 719 (D. Mass. 1964), aff’d, 361 F.2d 759 (1st Cir. 1966) (customer of failed securities firm unsuccessfully sued her lender on several theories, including wrongful repledge), and Schreiber Family Charitable Found. v. First Fin. Acceptance Co., 965 F. Supp. 397 (E.D.N.Y. 1997) (repledge of securities held not to violate agreement by the secured party not to encumber the securities; court
1930s the case reports were swollen with stockbroker bankruptcies, but since then insolvencies of securities intermediaries have become much less common, and insolvencies in which the intermediary has a shortfall of securities (or at least a shortfall for which the customer is not covered by insurance) are rare. Happy is the country with no history, and (so harried law revisers quite reasonably may conclude) happy is the niche of commercial law in which next to no reported cases arise.

But new transactional patterns have arisen. The broker's repledge of margin securities, though still extant, is old hat. A high-tech variant has evolved and spread with mutagenic speed during the last decade or so. This new transactional pattern arises out of a genre of sophisticated bilateral transactions referred to as "over-the-counter derivatives," or "OTC derivatives" for short. An OTC derivative transaction typically imposes upon one party, or both, an obligation to make one or more payments to the other party over time, the amount of each payment (and the identity of the party obliged to make the payment) being determined by a formula based on an external index, such as prevailing interest rates or commodity prices. Since at least the late 1980s it has been common for such transactions to provide that the net present value of the parties' respective future obligations under the transaction must be determined periodically, and that the party who is the net obligor must then provide credit support to secure its obligations under the transaction. Such credit support frequently takes the form of a pledge of U.S. Treasury or other marketable securities. If, as is typically the case, one party is a dealer in derivative transactions, it often will enter into an offsetting transaction with a third party, and the dealer will wish to have the right to repledge any collateral it receives under one of these two transactions in order to secure its own obligations under the other transaction. Hence the standard form of security documentation used in the United States for OTC derivative transactions, written by a trade association dominated by dealers, gives the secured party unfettered power to repledge the collateral. Indeed, the documentation goes further and also gives the secured party

reasoned that the secured party might have retrieved the repledged securities by pledging substitute collateral of its own). Schreiber seems flagrantly wrong, and is explicable only on the supposition that the court had little patience with the suit because the secured party was in fact solvent. See Barkley Clark, Law of Secured Transactions Under the Uniform Commercial Code ¶ 7.15[d] (Supp. 1998).
unfettered power to sell the collateral outright before default. If the secured party repledges or sells the collateral, the documentation allows the secured party to retain the proceeds for its own use, and it need not apply them to the pledgor's obligation, hold them separately as collateral, remit them to the pledgor, or otherwise account for them. Rather, the secured party's only duty is to return equivalent securities at the end of the deal.\textsuperscript{14}

The same liberal attitude toward use of pledged securities by the secured party prevails in other capital market transactions. For example, in a securities lending transaction, the borrower typically secures its obligation to return a "borrowed" security by pledging to the lender U.S. Treasury or other marketable securities. Standard documentation for these transactions likewise allows some lenders to repledge, sell, or otherwise dispose of that collateral without accounting for the proceeds.\textsuperscript{15}

So, after a sixty year hiatus, the commercial law of repledge matters again. The purpose of this paper is to summarize briefly how Revised Article 9 deals with repledge and its close kin, the pre-default sale of collateral. Limitations of space preclude exploration of important related topics, such as the common law that was applied to stockbrokers' repledges of their customers' margin securities in the early decades of this century, and the complex and doubtful nature of the property right of a pledgor of securities held through an intermediary under Article 8.

This paper focuses on repledge of securities, and it assumes that the reader is familiar with the provisions of the UCC dealing with the holding and transfer of securities. These are set forth principally in Article 8, with related changes to Article 9, as revised in 1994. Revised Article 9 carries forward the 1994 provisions with only minor

\textsuperscript{14} Paragraph 6(c) of the 1994 ISDA Credit Support Annex ("Bilateral Form—ISDA Agreements Subject to New York Law Only"), drafted by the International Swaps and Derivatives Association, Inc. (formerly the "International Swap Dealers Association, Inc.") states that, in general, the Secured Party will, notwithstanding Section 9-207 of the New York Uniform Commercial Code, have the right to... sell, pledge, assign, invest, use, commingle or otherwise dispose of, or otherwise use in its business any Posted Collateral it holds, free from any claim or right of any nature whatsoever of the Pledgor, including any equity or right of redemption by the Pledgor.

\textsuperscript{15} Section 3.2 of the Master Securities Loan Agreement (May 1993), drafted by The Bond Market Association, states in part that, if the lender is a broker-dealer, the lender "may pledge, repledge, hypothecate, rehypothecate, lend, relend, sell or otherwise transfer the Collateral..."
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substantive changes. 16 Furthermore, this paper deals with securities held and transferred through securities intermediaries, dealt with principally in Part 5 of Article 8, often referred to as the "indirect holding system." This is to be contrasted with the traditional "direct holding system," in which the beneficial owner of a security holds the security directly, with ownership typically evidenced by a possession of a certificate and transfer effected by physical delivery of the certificate. Because repledge transactions today would usually be expected to involve securities held at a securities intermediary, this paper assumes that setting unless otherwise indicated. In addition, this paper does not address issues of federal law that might apply to securities issued by the U.S. Treasury or government-sponsored enterprises. 17

Finally, a note on terminology. This can be confusing in repledge transactions, which by their nature involve two transactions between three parties, one of whom is playing the role of secured party in one transaction and debtor in the other. In this paper, the original debtor is referred to as the "Pledgor"; Pledgor pledges securities to "SP"; SP then repledges (or, where indicated, sells) the securities to "Transferee." Except where precision is important, this paper freely uses colloquial language instead of the precise but dense terminology of Articles 8 and 9 (e.g., "a customer holding securities in his account at his custodian" rather than "an entitlement holder having a security entitlement assets credited to the securities account


17. Securities issued by the U.S. Treasury and maintained on the books of the Federal Reserve Banks are governed by the so-called "TRADES Regulations," 31 C.F.R. pt. 357 (1998). Many government-sponsored enterprises have similar regulations. See Robert A. Wittie, Review of Recent Developments in U.C.C. Article 8 and Investment Securities, 52 BUS. LAW. 1575, 1576 n.5 (1997). These regulations apply federal substantive law to most aspects of transactions between Federal Reserve Banks and their participants, but defer to state law as to other aspects, and as to all aspects of transactions on the books of lower-tier intermediaries. These regulations further provide that, subject to certain exceptions, if the relevant state has not adopted Revised Article 9 (for this purpose defined to mean the 1994 Official Text of Article 8, and related conforming changes to Article 9 and other Articles), then that state will be deemed to have done so for purposes of these regulations. Because Revised Article 9 changes the 1994 Official Text, conforming changes to these regulations may be necessary. As of July 1999 the Treasury had not taken a position on the subject.
maintained by his securities intermediary").

I. THE UNLIMITED STATUTORY RIGHT OF REPLEDGE AND THE REDEFINITION OF "GOOD FAITH"

The text of Revised Article 9, like its predecessor, contains exactly one express reference to repledge. That reference appears in Revised 9-207, "Rights and Duties of Secured Party Having Possession or Control of Collateral," a section which has the rare honor of not having been renumbered from its predecessor. Subsection (c)(3) of Revised 9-207 reads as follows:

(c) Duties and rights when secured party in possession or control. Except as otherwise provided in subsection (d), a secured party having possession of collateral or control of collateral under Section 9-104, 9-105, 9-106, or 9-107:

....

(3) may create a security interest in the collateral.

The "except as otherwise provided" clause in the preface never applies to repledges of securities. So, under this provision, a secured party having "possession" of a security certificate pledged to it, or "control" of a security or security entitlement pledged to it (where "control" is defined in the precise sense introduced in the 1994 revisions to Article 8), may create a security interest in that collateral, without further ado, unless the secured party has agreed not to do so.

The secured party's right of repledge is markedly broader under Revised Article 9 than under Former Article 9. Former 9-207(2)(e) gave the secured party the right to repledge collateral only "upon terms which do not impair the debtor's right to redeem it." This codified the dominant rule under pre-UCC common law. Under that common-law rule, SP could not repledge to secure a debt larger than Pledgor's debt to SP, nor for a longer term than the term of Pledgor's debt to SP.19 If SP repledges within those constraints, Pledgor has the

18. Among other things, in order to avoid mind-numbing repetition of the word "security," the word "pledge" is used as a synonym for "security interest" and "grant a security interest," without any connotation of physical possession. The Article 8 terms "securities account" and "securities intermediary" are frequently clipped to "account" and "intermediary." A colloquialism often used is to the effect that "a customer holds securities through a securities intermediary." Under Article 8, a customer ("entitlement holder") does not "hold securities" at all, but rather has a security entitlement at the intermediary. "Security agreement" herein refers to the entire agreement between pledgor and secured party relating to the secured transaction. Revised 9-102(a)(73) defines the term to mean only the portion of the agreement that creates or provides for the security interest.

19. See RESTATEMENT OF SECURITY § 23 cmt. b (1941); CHARLES H. MEYER, THE LAW
ability, if need be, to redeem its collateral by doing no more than tendering payment of its debt directly to Transferee. Such a “non-impairing” repledge does not expose Pledgor to the risk of the creditworthiness of SP. However, Former 9-207(2)(e), like the common-law rule before it and like its successor in Revised Article 9, is merely a gap-filling provision, applicable only if the parties have not otherwise agreed. Under the common-law rule codified by Former 9-207(2)(e), it was universally recognized that Pledgor could contractually grant SP a right to repledge on terms that do “impair” Pledgor’s right to redeem. Indeed, since before the UCC was adopted, brokers routinely have obtained unrestricted contractual rights of repledge from their margin customers. That is because the only practical way for a broker to repledge is to repledge many or all of its customers’ margin securities in a single block to secure a single loan, a practice which does impair the ability of any one customer to redeem and hence is not authorized by Former 9-207(2)(e). If SP does make (rightfully or wrongfully) an “impairing” repledge to a Transferee who is entitled to the benefit of the adverse claim cut-off rules in Article 8, then Pledgor becomes subject to the risk of the solvency of SP, because if SP becomes insolvent Pledgor will be unable to recover its property from Transferee even if Pledgor pays the full amount of the debt Pledgor owes to SP.

The merits of the expanded right of repledge afforded by Revised 9-207(c)(3) are debatable. As noted in Comment 5, a secured party who intends to repledge normally obtains the pledgor’s consent anyway. So it might have been more logical to delete this gap-filling provision entirely. Practices would not have been affected so long as the text or Comments made clear that repledge is allowed to the extent permitted by agreement. Moreover, a gap-filling rule that does not put the pledgor at risk in the event of the secured party’s insolvency arguably would be more consonant with the usual norms of a secured transaction.

The unlimited right of repledge afforded by Revised 9-207(c)(3) may be less useful to a secured party than it first appears. Obviously
the secured party may not exercise that right if the security agreement forbids it. In this connection, a secured party should consider whether boilerplate imposing upon the secured party in general terms a duty of safekeeping with respect to the collateral might be construed as being inconsistent with repledge, unless the security agreement specifically allows repledge. If the secured party is a securities intermediary and is repledging securities that it has credited to a securities account it maintains for the pledgor (as would be the case in the traditional broker’s repledge of margin securities), then Article 8 compels the secured party to obtain the pledgor’s consent to the repledge in any event. The secured party must also procure the pledgor’s consent to the repledge to the extent required by other state laws, or by the SEC, or by other regulations to which the secured party may be subject.

Still, there is no question that the revision places a new burden on pledgors. Under Former Article 9, as a practical matter the secured party must negotiate contractual permission if it wants to be able to repledge, given that the statutory right in Former Article 9 is too limited to be of much practical use. The revision shifts onto the pledgor the burden of negotiating a limitation on the secured party’s now-unlimited statutory right. A pledgor should also reflect on whether it is now wise to allow its security agreement to contain broad language giving the secured party “all rights provided to a secured party by the UCC.”

Unpleasant surprises may be in store for both parties during the transition to Revised Article 9, but perhaps most notably for the pledgor. If a security agreement that is silent about repledge remains in effect after the effective date of Revised Article 9, the transitional rules will allow the secured party to take advantage of the expanded statutory right of repledge after the effective date. Unless the parties

22. See U.C.C. § 8-504(b).
23. Various state laws may prohibit or restrict repledge without the consent of Pledgor. See, e.g., N.Y. GEN. BUS. LAW § 339-e (McKinney 1988); N.Y. PENAL LAW § 165.00 (McKinney 1999). EGON GUTTMAN, MODERN SECURITIES TRANSFERS ¶ 19.03(1)(c), at 19-26 n.107 (3rd ed. 1987 & Supp. 1996) lists statutes and regulations in 26 states restricting repledge of customer securities by brokers, some of which contain restrictions that cannot be satisfied merely by customer consent. As applied to brokers, these state laws would appear to have been preempted in whole or part by § 15(h)(1) of the Exchange Act, 15 U.S.C § 78o(h)(1) (1997), added by the National Securities Markets Improvements Act of 1996, § 103(a), Pub. L. No. 104-290, 110 Stat. 3416 (1996). Brokers who wish to repledge customer securities as a practical matter generally must obtain customer consent as a result of the federal regulations noted supra note 11.
had reason to focus on repledge, the security agreement may well be silent on the subject. Hence it seems quite possible that, to the surprise of the pledgor, a security agreement negotiated under Former Article 9 that says nothing about repledge may allow the secured party to repledge without limitation after the effective date of Revised Article 9.

Transitional issues may arise for secured parties as well. For instance, the SEC regulations relating to brokers' repledges forbid a broker from repledging customer securities on terms that would allow the broker's pledgee to, in turn, repledge the securities for a sum greater than the customer debt owed to the broker. Hence if an existing security agreement between a broker and its pledgee does not prohibit such further repledges by the pledgee, the broker may be in violation of those regulations upon the effective date of Revised Article 9.

More lasting issues arise from the fact that the statutory right of repledge applies to any collateral, not just securities held through a securities intermediary. So if Pledgor delivers to SP any collateral having attributes of negotiability, SP may repledge it rightfully (unless SP has agreed not to do so), and if SP does repledge it to Transferee and then fails, Pledgor may be unable to recover it from Transferee even if Transferee is well aware that Pledgor is its true owner. For example, consider the case of Luckless Corporation, which borrows $100 from Finance Company, secured by a pledge of all of the capital stock of Sub, a wholly-owned subsidiary of Luckless. The stock, worth by reasonable estimates at least $200, is evidenced by a certificate, delivered to Finance Company at closing along with the customary blank stock power. If Luckless has not been alert enough to limit Finance Company's statutory right of repledge, Finance Company could rightfully repledge the Sub stock to MegaLender (together, if it chooses, with other pledged securities in Finance Company's loan portfolio and proprietary assets of Finance Company) in order to secure Finance Company's $10,000 debt to MegaLender. Luckless' ownership interest would not be an "adverse claim," because the repledge would be rightful, and so MegaLender would take the pledged stock free of Luckless' ownership interest even if MegaLender knew that Luckless was its owner. Hence if Finance

Company fails, Luckless may well lose the Sub stock, even if Luckless repays the $100 it owes. The likelihood that security documentation negotiated under Former Article 9 is silent or ambiguous about repledge is probably greater in a commercial lending transaction such as this than in the OTC derivatives market, in which participants have long been mindful of the risks posed by repledge.

Revised Article 9 provides one possible basis for limiting the facially-unlimited statutory right of repledge in some circumstances. That is the general duty of good faith in the performance and enforcement of every contract and duty within the UCC, imposed by section 1-203. The revision does not directly amend that section. But the revision follows the trend of other Articles and expands the definition of "good faith" to require not merely subjective "honesty in fact," but also compliance with an objective standard, namely "observance of reasonable commercial standards of fair dealing." As a result, a Pledgor might argue that exercise by SP of the statutory right of repledge (or, for that matter, even a contractual right of repledge) might be wrongful in a particular case because it violates "reasonable commercial standards of fair dealing." If Transferee were sufficiently knowledgeable about the provenance of the repledged shares and the relationship between Pledgor and SP, then Pledgor might argue that Transferee should be charged with notice of that wrongfulness and, hence, lose its protection under the adverse claim cut-off rules. As a result, a Pledgor might argue that exercise by SP of the statutory right of repledge (or, for that matter, even a contractual right of repledge) might be wrongful in a particular case because it violates "reasonable commercial standards of fair dealing." If Transferee were sufficiently knowledgeable about the provenance of the repledged shares and the relationship between Pledgor and SP, then Pledgor might argue that Transferee should be charged with notice of that wrongfulness and, hence, lose its protection under the adverse claim cut-off rules.

The duty of good faith performance under the UCC, like the similar duty of good faith and fair dealing applicable under the common law of contracts, is famously elusive. But exercise of a right

26. R. § 9-102(a)(43). This expanded definition of "good faith" by its literal terms applies only as that term is used within Article 9 (as per the preamble of Revised 9-102(a)). However, Comment 19 to Revised 9-102 states that the expanded definition was intended to be used for purposes of section 1-203 as that section may apply to contracts or duties within Article 9.

27. The phrasing in text ("notice") assumes that Pledgor is not an entitlement holder of SP with respect to the repledged securities, so that the adverse claim cut-off rule applicable to Transferee is section 8-502 (or, if the repledged security is directly held, as in the Luckless-MegaLender example, section 8-303). A similar "good faith" argument could be advanced by Pledgor if SP were Pledgor's securities intermediary with respect to the repledged securities, though the applicable cut-off rule then would be section 8-503(e). In that event, Pledger's argument would be that its consent to the repledge (which SP is required to obtain under section 8-504(b)) is qualified by SP's duty of "good faith."

28. See generally 2 E. ALLAN FARNsworth, Farnsworth on Contracts §§ 7.17, 7.17b (2nd ed. 1998). For a discussion applying the concept to Former Article 9 (which among other things observes that "at no time did the drafters, nor any of the groups commenting on proposed drafts of the Code, pay any attention to the role of good faith performance or enforcement in Article Nine"), see Dennis M. Patterson, Wittgenstein and the Code: A Theory of
of repledge is remote from the settings to which the doctrine is traditionally applied. A 1994 commentary by the UCC's Permanent Editorial Board states that, under the UCC, the doctrine is essentially a rule of contract interpretation, the purpose of which is to preserve the reasonable expectations of the contracting parties. For a pledgor to allow the secured party to repledge is a simple binary choice, and the main practical consequence of allowing it—that the pledgor takes the credit risk of the secured party with respect to return of the collateral—is easy to understand. That risk is similar to the kinds of risks reasonable people take every day, such as when deciding to sell goods on credit, or to hold money in a bank in excess of the FDIC's insurance coverage. If a pledgor agrees to assume that risk, there is no basis in the doctrine of good faith performance for tagging a secured party or its transferee with any adverse consequences.

The doctrine of good faith performance might more plausibly be invoked to prevent a secured party who does not have a contractual right of repledge in a security agreement negotiated under Former Article 9 from exercising the statutory right of repledge after the effective date of Revised Article 9. In such a situation, a Pledgor might with some plausibility argue that preservation of the parties' reasonable expectations requires SP to refrain from "impairing" repledges after Revised Article 9 becomes effective. As a practical matter, such a case is likely to arise only if SP subsequently fails and Pledgor seeks to recover its repledged securities from Transferee. To defeat Transferee's rights under the adverse claim cut-off rules, Pledgor would have to show that Transferee knew of the wrongfulness of SP's conduct. Pledgor thus would have to show, to begin with, that Transferee knew that the pledged securities were not SP's. That would seem difficult to establish for publicly-traded securities—though it might be less difficult in a case involving closely-held securities, as in the Luckless-MegaLender example. If Pledgor is able to establish Transferee's knowledge of Pledgor's ownership, Pledgor also would have to establish that Transferee knew of the wrongfulness of the repledge as against Pledgor. Even if Pledgor


29. See PERMANENT EDITORIAL BOARD FOR THE UNIFORM COMMERCIAL CODE, COMMENTARY NO. 10 (Feb. 10, 1994).

30. See U.C.C. § 8-105 & cmt. 2. "Knowledge" under the adverse claim cut-off rules in effect includes willful blindness as well as actual knowledge. See U.C.C. § 8-105(a)(1), (2) & cmt. 4.
succeeds in showing that Transferor knew that the Pledgor-SP security agreement is silent as to repledge (which again seems likely to be difficult), Transferee might reasonably counter by noting that the statute does, after all, provide an unlimited right of repledge following its effective date, and that the "good faith" standard should not be applied to subvert the plain language of the transitional rules.

How such a case would play out is unclear. But in any event, if after the effective date of Revised Article 9 Pledgor executes documentation that does not restrict the statutory right of repledge, it is hard to see how Pledgor would have a valid complaint if SP exercises that right. That's what gap-filling provisions are for.

In the long run, the unlimited statutory right of repledge provided by Revised 9-207(c)(3) may not be the most significant feature of Revised Article 9 relating to repledge. After a transitional period, forms will no doubt be modified to limit that right in appropriate settings. More interesting is what the revision has to say about the nature of the relationship between the pledgor and secured party if repledge or sale of the pledged securities is contemplated or effected. To that subject we now turn.

II. SECURED TRANSACTION OR SALE? CHARACTERIZING THE RELATIONSHIP BETWEEN PLEDGOR AND SECURED PARTY IF REPLEDGE OR NONACCOUNTABLE SALE IS PERMITTED

A. Introduction: The Case of the Missing Res

1. The Characterization Issue and Nonaccountable Sale

Consideration of extreme cases often helps to clarify matters, and so it is useful to begin by recalling a point made in the introduction and ignored until now. Standard security agreements widely used in connection with capital market transactions today provide that the secured party may, before default, not merely repledge the collateral, but also may sell the collateral outright and use the resulting proceeds for its own purposes. The secured party is still obliged to return "the collateral" to the pledgor when the pledgor's obligation has been satisfied, but if the secured party has sold the collateral, the secured party obviously can satisfy that obligation only by going into the market and purchasing equivalent securities for delivery to the pledgor.

Such consensual pre-default sales seem to be a relatively recent development. Outside the capital markets arena, it is not easy to
think of settings in which a secured party is given the right to sell the collateral before default. A distant analogy may be drawn to the operation of cash collateral arrangements, in which funds held by a secured party are invested in money market investments, which might be liquidated before maturity and reinvested in other such instruments. The right to select the investments to be liquidated is usually given to the debtor before default, but sometimes it is given to the secured party. However, such arrangements are not really very similar to the kinds of pre-default sales of collateral described in the preceding paragraph, because in such a cash collateral arrangement the security interest attaches to the proceeds, which remain identifiably the debtor's property and the res to which the security interest continues to attach. This is no more exciting than the standard floating lien on accounts and inventory, in which the collateral likewise turns over constantly. The mere fact that the secured party has the right to sell the collateral free of the debtor's interest, and does so, does not seem inconsistent with the characterization of the transaction as a secured transaction—at least so long as the secured party immediately accounts for the proceeds, either by holding them as substitute collateral, applying them to reduce the secured debt, or remitting them to the debtor. But characterization problems do arise if the secured party instead has the right to use the proceeds of sale for its own purposes, so that the res to which the security interest has attached is gone, but the obligation secured still remains. For brevity, this paper sometimes refers to such an arrangement as a "nonaccountable sale," it being understood that the reference is to a situation in which the pledgor's rights in the collateral have been cut off or subordinated (due to the operation of the adverse claim cut-off rules of Article 8 or otherwise) and in which the secured party is not obligated to account immediately for the proceeds in one of the foregoing ways.

The practice of permitting nonaccountable sale of pledged securities is doubtless attributable to the prevalence of the repurchase agreement ("repo") as a substitute for secured lending in the

31. Similarly unproblematic from a characterization standpoint are situations in which a secured party sells one item of fungible collateral and immediately replaces it with a substitute. See, e.g., Fedders Corp. v. Taylor, 473 F. Supp. 961, 974 (D. Minn. 1979), cited in Cohen v. Army Moral Support Fund (In re Bevill, Bresler & Schulman Asset Management Corp.), 67 B.R. 557, 588 (Bankr. D.N.J. 1986); see also MEYER, supra note 19, § 67 (noting stockbroker's right to substitute certificates for pledged margin securities at common law); RESTATEMENT OF SECURITY § 12 cmt. c (1941) (similar).
government securities markets. In a repo transaction, A sells to B a marketable security, typically a U.S. Treasury or federal agency security, for cash, with the parties simultaneously agreeing that B will sell to A, and A will purchase from B, an equivalent security on an agreed future date and for an agreed price (typically equal to the amount received by A in the initial sale, plus an amount equivalent to interest on that sale price to the repurchase date). Obviously such a transaction is economically equivalent to a secured loan by B, the repo buyer, to A, the repo seller. There has been a long-simmering debate as to whether repo transactions are properly characterized as sales or as secured loans, though much of the steam was taken out of the debate by amendments to the Bankruptcy Code and federal bank insolvency law that effectively exempt broad categories of repos (however characterized) from most of the usual consequences of an insolvency proceeding.32 The immediate point, however, is that repos have blurred the distinction in the marketplace between a pledge and a sale as to U.S. Treasury and federal agency securities. But from a commercial law perspective, a secured party’s outright sale of collateral is, at least at first blush—even second blush—conceptually quite different from repledging it. Former 9-207(2)(e) speaks in terms of a secured party’s right to “repledge” collateral; Revised 9-207(c)(3) modernizes the wording to “create a security interest” in collateral; but nothing in the text or history of either provision suggests that they have any application to an outright sale by the secured party.33 Unlike repledge, nonaccountable sale seems entirely alien to the traditional conception of a secured transaction. Many statements can be found in pre-UCC authorities dismissing out of hand any notion that a secured party may rightfully sell the collateral before default, an act conceived of as “separating the debt from the security” (evil), as contrasted with assigning a debt along with the collateral securing it (good)—though for the most part


those assertions were made without reference to the effect of consent by the debtor.\textsuperscript{34} Grant Gilmore likewise dismissed the notion that a secured party may rightfully sell collateral before default, but at least considered the effect of the debtor's consent:

Needless to say, the common law has always stigmatized such a transfer of a pledgor's property as a conversion. It may be safely assumed that the conversion would be a conversion still even if the pledge agreement authorized the pledgee to sell the property (without assigning the debt) whenever he felt like it. The Code says nothing about such unauthorized sales by secured parties in § 9-207 or in any other section. Such a sale would seem clearly enough to be a violation of the secured party's inescapable duty to use reasonable care in custody and preservation of the collateral so that we may conclude that the Code secured party has no more right to sell the collateral without assigning the debt than a common law pledgee did.\textsuperscript{35}

It is difficult to see why this should be so. Capitalist acts between consenting adults should be valid unless they injure third parties or offend public policy, and it is hard to see anything inherently harmful from either perspective about a nonaccountable sale by a secured party.\textsuperscript{36} The effect of such a sale is the same as if the debtor had

\textsuperscript{34} See, e.g., RESTATEMENT OF SECURITY § 23 (1941); EDWARD H. WARREN, MARGIN CUSTOMERS 388 (1941) ("Judges have repeatedly said that for a pledgee to separate the debt from the security is a conversion. So far as we know, no judge has ever questioned this principle—it is accepted as axiomatic."). Research has not located any reported case meaningfully considering the effect of consent on a pre-default sale of collateral. There are innumerable cases which, like the Restatement and Professor Warren's treatise, state that a pledgee cannot sell collateral before default without referring to the possible effect of consent, see, e.g., Rothschild v. Allen, 86 N.Y.S. 42, 44 (N.Y. App. Div. 1904), aff'd, 73 N.E. 1132 (N.Y. 1905); Douglas v. Carpenter, 45 N.Y.S. 219 (N.Y. App. Div. 1897), and there are many phrases which can be wrenched out of context, see, e.g., In re Salmon Weed & Co., 53 F.2d 335, 338 (2d Cir. 1931) (dictum: "a sale by a pledgee contrary to the terms of the agreement is a conversion"); Kittredge v. Grannis, 155 N.E. 88, 90 (N.Y. 1926) (disposition of margin securities to third party, assumed to be authorized, but still a conversion if the securities were sold by the broker "not for the account of the plaintiff, but with the preconceived idea of appropriating the proceeds"); Borden v. District of Columbia, 417 A.2d 402, 404 (D.C. 1980) (tax case; disposition of securities collateral by secured party held wrongful, despite language in security agreement allowing secured party to "use or hypothecate" the security); cf. Chittenden Trust Co. v. Marshall, 507 A.2d 965, 969 (Vt. 1986) (inexplicably suggesting that secured party may have breached of duty of care or violated redemption right by assigning secured debt together with collateral securing it).

\textsuperscript{35} 2 GILMORE, supra note 12, § 42.10, at 1156.

\textsuperscript{36} A nonaccountable sale might be argued to harm unsecured creditors of Pledgor, because from the perspective of Pledgor it trades the pledged security (or at least any excess of the value of the pledged security over the amount of Pledgor's debt to SP) for SP's personal obligation to Pledgor to replace the pledged security. But the same is true in any securities lending transaction, and, for that matter, in any sale of property on credit. The limits of a debtor's right, as against its unsecured creditors, to transfer its property are generally set by fraudulent transfer law, and a transfer of a security by Pledgor to SP in exchange for SP's personal obligation to return an equivalent security would not be a fraudulent transfer except in
transferred the security in question outright to the secured party, in exchange for the secured party's contractual undertaking to return an equivalent security to the debtor in the future. Such so-called "securities lending" transactions, described in more detail below, are commonplace today.

The basic problem posed by a nonaccountable sale is not that the transaction is somehow wrongful as against the pledgor despite the pledgor's consent. Rather, the problem is whether the relationship between the pledgor and the secured party after such a sale (or, perhaps, even before the sale, if the secured party is authorized to sell) ought to be characterized as a secured transaction. The essence of the definition of "security interest" is "an interest in personal property or fixtures which secures payment or performance of an obligation." If there is no res, there can be no security interest. So the most natural characterization of the relationship after the pledged securities are sold is not a secured transaction, but rather that the two parties are mutual creditors, "pledgor" still owing the underlying "secured obligation" to the "secured party" and "secured party" having a personal obligation to deliver to the "pledgor" a security equivalent to the "pledged" security following the payment of the underlying "secured obligation." (The terminology of secured transactions is inappropriate to the transaction as so characterized, of course, but it is convenient to continue to use that terminology with the quotation marks understood where appropriate.)

It is probably impossible to state a nontrivial legal proposition so self-evident that no contrary authority can be dredged up, and the proposition that there can be no secured transaction without a res is no exception. The notion of a secured transaction without a res is no less odd than the notion of a trust without a res, but courts have recognized the latter creature in a variety of settings. For example,
when construing, in a bankruptcy setting, a provision of the Internal Revenue Code that requires withholding taxes held by an employer to be "held in a special fund in trust for the United States," the U.S. Supreme Court held that this provision "creates a trust in an abstract 'amount'—a dollar figure not tied to any particular assets." This surely stretches the idea of thing-ness past any reasonable bounds. Likewise, a few courts have held, or at least have been willing to assume, that if A pays funds to B as a security deposit in connection with a lease or other obligation A owes to B, and if B is not required (by law or contract) to segregate the funds, and so deposits them into B's general account or otherwise expends them, then the relationship between B and A with respect to those funds is not that of debtor to creditor, but rather B has a security interest in "A's money."

But these contrary straws in the wind can be dismissed as

38. Begier v. Internal Revenue Serv., 496 U.S. 53, 55, 62 (1990) (preference challenge to prepetition payment to IRS by a debtor, made from debtor's general account, of an amount on account of withholding taxes collected by debtor but not segregated by it; held, payment not preferential because the funds were "trust funds" and hence not property of the debtor's estate). After Begier, similar reasoning has been applied to state and municipal taxes, declared by state law to be "trust fund" monies, that were collected but not segregated by the debtor. However, courts have tended not to apply the quoted statement with full vigor, but rather have groped desperately for a res (as by tracing trust-fund monies into the debtor's general account to which is applied a "lowest intermediate balance" rule). See, e.g., Texas Comptroller of Pub. Accounts v. Megafood Stores, Inc. (In re Megafoods Stores, Inc.), 163 F.3d 1063 (9th Cir. 1998); City of Farrell v. Sharon Steel Corp., 41 F.3d 92 (3rd Cir. 1994). For another trust with a most dubious res, see 1 GEORGE E. PALMER, THE LAW OF RESTITUTION § 2.14, at 182-83 (1978) (describing the so-called "swelling of assets" theory applied by some cases in the 1930s, under which a claimant did not have to trace a specific asset into an insolvent estate).

39. This has been litigated recently in numerous cases involving claims for payment of interest under Former 9-207(2)(c) on security deposits of various types. A disturbing number of these cases have held or assumed that an unsegregated security deposit involves a security interest in "money," though these cases have tended to be resolved against the plaintiffs on other grounds. See, e.g., Demitropoulos v. Bank One Milwaukee, 953 F. Supp. 974 (N.D. Ill. 1997) ("pledgor" did not prove that "secured party" actually earned interest on the "collateral"); Spina v. Toyota Motor Credit Corp., 703 N.E.2d 484 (Ill. App. 1998) (court assumed that security interest might exist in unsegregated security deposit, but simply held, based on other Illinois laws on security deposits, that legislature "never envisioned" auto lessors paying interest thereon under Former 9-207); Brooks v. General Motors Acceptance Corp., 1998 WL 122774 (N.D. Ill. 1998) (similar); Wiskup v. Liberty Buick Co., 953 F. Supp. 958 (N.D. Ill. 1997) (similar); see also In re Barr, 180 B.R. 156 (Bankr. N.D. Tex. 1995) (security interest in general intangibles held not to cover debtor's security deposit with electric utility, which was held to be "money"), aff'd, 383 F.2d 606 (5th Cir. 1967); In re Atlanta Times, Inc., 259 F. Supp. 820 (N.D. Ga. 1966) (equipment lessor held to have security interest in lessee's security deposit, as "money"); such security interest held to have been perfected by "possession"); cf. Yeager v. General Motors Acceptance Corporation, 719 So. 2d 210 (Ala. 1998) (auto lessor not liable for interest on unsegregated security deposit because the "language of the lease, with respect to security deposits, does not expressly and specifically indicate that the parties intended to create a security interest").

Grant Gilmore, who famously declared that "a right of set-off is not a security interest and has never been confused with one: [Article 9] might as appropriately exclude fan dancing," 1 GILMORE, supra note 12, § 10.8 at 315-16, must be turning in his grave.
exceptional, the trust-fund tax cases on the ground that they give effect to an extraneous statute that was perceived to supervene ordinary principles, and the security deposit cases on the ground that they are just plain wrong. The courts in the security deposit cases are by no means the first to have confused physical currency (which is all that “money” means, or at least ought to mean, in the UCC sense) with a chose in action for payment of money. This is merely an extension of the persistent illusion that when \( X \) deposits money in the bank, the bank stashes it in a box with \( X \)'s name on it. That illusion dies very hard.

Yet despite the textual and conceptual difficulty of characterizing a relationship as continuing to be a secured transaction after a nonaccountable sale, security agreements used in connection with capital markets transactions do permit such sale, as well as repledge, and continue to refer to the relationship thereafter as being a secured transaction. This is true of the standard security documentation used in the OTC derivatives market, for example, though that documentation also contains setoff provisions that recognize the possibility that the relationship may be recharacterized as that of mutual creditors.

This characterization issue arises in a particularly striking way in securities lending transactions. A typical securities lending arrangement involves two parties, broker \( B \) and investor \( C \). Broker \( B \) may have need of a security of a particular type that \( B \) does not own or control. A common reason is that one of \( B \)'s customers has instructed \( B \) to make a short sale of the security for the customer's account. The customer hopes that the price of the security will later fall, so that she may then close out her short position by purchasing the security at a lower price. In the meantime, \( B \) must deliver the security to whomever purchased it, and so if \( B \) does not have the security in his own inventory, \( B \) must borrow the security from investor \( C \), who has it in his, in exchange for \( B \)'s promise to return an equivalent security to \( C \) in the future. Notwithstanding the

40. See, e.g., In re Koreag, 961 F.2d 341 (2d Cir. 1992); Intershoe, Inc. v. Bankers Trust Co., 571 N.E.3d 641 (N.Y. 1991) (both holding forward foreign exchange transactions to be transactions in “goods” subject to Article 2). These bizarre decisions have been widely criticized. See, e.g., Thomas C. Baxter, Jr. & James H. Freis, Jr. Resolving Funds Transfer Disputes Related to Currency Exchange Transactions: What Law Governs? 1995 COMM. L. ANN. 297 (Louis F. Del Duca & Patrick Del Duca eds.). The proposed revisions to Article 2 will reverse them. See Proposed §§ 2-102(a)(21), 2-103(d) (Annual Meeting Draft, July 23-30, 1999); see also R. §§ 9-102 cmt. 5, 9-332 cmt. 2 (emphasizing that “money” under U.C.C. § 1-201(24) means physical currency, not funds credited to a deposit account).

41. See ISDA Credit Support Annex, supra note 14, paras. 8(a)(iii), 8(b)(iv)(A).
"borrowing/lending" terminology colloquially used, the transfer of the "loaned" security from C to B is, and is intended to be, an outright sale that divests C of any further property interest in the security—indeed, the whole point of the transaction is to allow B to make good delivery of the security to B's purchaser. Few Bs are sufficiently creditworthy to make it prudent for C to rely on B's unsecured promise to return an equivalent security, and for that reason (as well as regulatory requirements applicable to most Bs and Cs), B typically secures its obligation to C by pledging marketable securities, typically U.S. Treasury securities. Standard documentation allows C, if C is itself a broker-dealer, liberty to sell, repledge, or otherwise dispose of the pledged collateral, without accounting for the proceeds.

The piquant result is that B and C may wind up making mutual transfers of securities, and undertaking mutual obligations, that are completely symmetrical but which the documentation characterizes in two quite different ways. With respect to the "loaned" security delivered by C to B, C has no property right in the security once delivered to B, and B has only a personal obligation to return a like security to C. The documentation refers to that relationship between B and C as that of debtor and creditor. With respect to the U.S. Treasury securities delivered as "collateral" by B to C, C likewise may be entitled to sell the securities, free of B's rights, in which case C obviously has only a personal obligation to return a like security to B. But the documentation refers to this relationship as if it were a security interest by C in that now-vanished "collateral."

Nonaccountable sale thus poses in a pure form a characterization issue that might be called "the case of the missing res." Not the least

42. For example, on the borrowing side, a broker-dealer or government securities dealer that borrows securities from a customer must provide collateral with a market value equal to at least 100% of the market value of all outstanding securities loaned. See 17 C.F.R. §§ 240.15c3-3(b)(3), 403.4 (1998). Borrowing and lending of securities by broker-dealers is also subject to Federal Reserve Regulation T, 12 C.F.R. pt. 220 (1998), which does not presently impose a collateral requirement. On the lending side, various regulated entities, such as pension plans, mutual funds and banks, are subject to regulations which require them to obtain collateral when they lend securities. For an overview from a legal perspective, see Jon R. Lind & Gregory J. Nowak, Special Report on International Securities Lending: United States, INT'L FIN. L. REV. 31 (1991 Special Supp.), and the notes to the form of securities loan agreement prepared by The Bond Market Association, <www.bondmarkets.com/market/funding.shtml> (visited Oct. 1, 1999).

43. See supra note 15. Whether a pledge of securities on terms that permit nonaccountable sale or repledge might be treated as a securities lending transaction for regulatory purposes is beyond the scope of this paper.
of the many odd things about it is that in this instance the parties are seeking to contract into Article 9. In all the more familiar settings in which characterization issues arise, such as equipment leasing, sales of receivables and repo transactions, the parties label their relationship as being something—anything—other than a secured transaction.

2. The Characterization Issue and Repledge

Although not quite as extreme as outright sale of collateral, repledge also gives rise to a situation hard to reconcile with common intuitions about property rights. This is so even where the property rights can be associated with a discrete, identifiable thing and no questions of tracing arise. Consider the following simple repledge: Pledgor owes SP $50 and secures her debt by a pledge of a particular certificated security worth $60, the duly endorsed certificate being delivered to SP; SP then (with the consent of Pledgor) repledges that certificate to Transferee to secure SP's own obligation of $200 to Transferee. Pledgor still counts herself as being the owner of that security, but SP is also making use of the full value of the security—not merely the portion that secures Pledgor's debt to SP—in a way that only owners can normally do. One piece of property is doing the work of two. The situation is reminiscent of nothing so much as the doctrine of Miraculous Multiplication, invoked by medieval theologians to explain in a politic way the fact that the alleged fragments of the True Cross scattered throughout Europe, if gathered together, would fill a lumber yard. The doctrine does the job, after a fashion, but is unlikely to convince anyone who is not already a believer.

The notion that Pledgor is still the owner of the underlying thing gets stretched still further if we consider tracing problems that may arise. For example, assume SP is holding securities of the same series pledged by two different Pledgors and repledges some but not all of them; which Pledgor's securities are deemed to have been repledged and which retained? Moreover, one must consider the possibility of successive repledges, at each stage of which a similar tracing issue may arise: i.e., Transferee in turn repledges the security to secure an obligation Transferee owes to T-2, who in turn repledges the security to secure an obligation it owes to T-3, etc. It may be possible to contrive tracing rules to deal with such situations, but even someone sympathetic to tracing arguments may blanch at the notion that Pledgor is really still the owner of the underlying thing.
If Pledgor really is still the owner of the pledged security following its repledge by SP to Transferee, then it would seem quite plausible to conclude that in the event of Pledgor's bankruptcy the security would be deemed property of the Pledgor's estate and, hence, the automatic stay would prevent Transferee (or a remote repledgee, if Transferee itself repledged) from taking any action to foreclose upon the security repledged to it. The teaching of *United States v. Whiting Pools, Inc.* is that the debtor's estate includes property owned by the debtor even if the debtor's ownership interest is worthless because the property secures an obligation many times larger than the value of the property. If such a remote and tenuous ownership interest sucks the whole property into the maw of the bankruptcy court, why not Pledgor's ownership interest, too?

It is important to emphasize that the "sale or secured transaction" issue lurking behind repledge arises quite independently of any of the changes made in Revised Article 9. It is inherent in allowing SP to separate the debt from the collateral, as occurs in any "impairing" repledge, regardless of whether SP's authority to make the repledge derives from Pledgor's consent or from the expanded repledge rights granted by Revised Article 9. Nonaccountable sale likewise separates the debt from the collateral. But unlike a nonaccountable sale, the pre-UCC broker repledge cases provide substantial precedent for continuing to characterize the relationship between Pledgor and SP as being a secured transaction if the separation takes the form of a repledge—however illogical the distinction between a sale and an "impairing" repledge may be in this context.

In most settings involving the characterization of a transaction as a "lien" or "something else," courts have considered that because the issue implicates the rights of third persons (typically the creditors of one of the parties), it cannot be resolved solely on the basis of the label applied by the parties, but rather must be determined objectively based on the substantive attributes of the transaction.

Courts have proclaimed loudly and firmly their willingness to ignore labels in traditional settings, such as a deed absolute on its face coupled with the transferee’s agreement to convey the property back to the transferor upon payment of a stated sum, or a purported equipment lease that conveys to the lessee too many of the sticks in the bundle. Indeed, the compulsion to look to objective criteria was so strong that it overcame the explicit statement in the pre-1987 UCC that the “lease vs. security interest” determination was to be made on the basis of the parties’ intent. Courts routinely construed that in a Humpty-Dumpty fashion to mean not what the parties said they intended, or thought they intended, but rather the “objective manifestations of intent”—or in plainer language, the substantive attributes of the transaction, not the label the parties applied to it. In settings where courts have not had enough experience to develop settled rules, such as repo transactions and sales of receivables, courts by and large have tended to do the reasonable thing, and temporize. This temporization sometimes takes the form of listing every factor that strikes the court as conceivably relevant, “weighing” them, and pronouncing judgment; sometimes it takes the form of throwing up the hands and deferring to the parties’ label. One suspects, however, that if courts are left to wrestle with these characterization issues for long enough, they would in time develop and employ objective rules (perhaps while still flying the flag of “objective manifestations of intent,” the same rhetorical shift employed in the pre-1987 equipment lease cases).

Repledge defies this expectation. If Pledgor consents to an “impairing” repledge, SP may repledge the securities in a way that

47. Compare U.C.C. § 1-205(37) (1962 Official Text) (purported lease is security interest if “intended as security”) with id. (1995 Official Text) (omitting references to “intent” in this context and adding elaborate objective guidelines).


49. Thus, in the most influential case on characterization of repo transactions, Cohen v. Army Moral Support Fund (In re Bevill, Bresler & Schulman Asset Management Corp.), 67 B.R. 557 (D.N.J. 1986), Judge Debevoise, after a masterly exposition, threw up his hands and deferred to the parties’ label. For other cases on repos, including some which take the “list every conceivable factor” approach, see the authorities cited supra note 32. There is a voluminous literature on characterization of receivables sales, far outweighing (at least in volume) the relatively scanty case law. See, e.g., 1 JASON H.P. KRAVITT, SECURITIZATION OF FINANCIAL ASSETS § 5.03 (2nd ed. 1999) (giving primacy to the label); Peter V. Pantaleo et al., Rethinking the Role of Recourse in the Sale of Financial Assets, 53 BUS. LAW. 159 (1996) (giving primacy to extent of recourse); Thomas E. Plank, True Sale of Loans and the Role of Recourse, 14 GEO. MASON L. REV. 287 (1991) (giving primacy to the payment of full value).
wipes out all value Pledgor’s ownership interest might have. As a matter of substance, the difference between such a transaction and an outright sale to SP is little but the label. Yet courts historically respected the label. Before the wellsprings dried up around 1940, courts had plenty of experience over plenty of time with brokers’ repledges, but the cases seem not to have expressed any doubt in the cases that repledged securities remained the Pledgor’s property, so long as traceable, no matter how much Pledgor’s ownership interest might be squeezed by the repledge.

If the world were new, a different approach might be taken to the characterization issue, and the line distinguishing a pledge of securities from an outright sale could be drawn on the basis of whether the pledgor consented to separation of the debt from the collateral. In other words, the rule would be that if SP has the right to “impair” Pledgor’s redemption right (in the common law sense described earlier), as would be the case if SP is entitled to make an “impairing” repledge or a sale, then Pledgor has given SP more rights in the collateral than is consistent with Pledgor’s continued ownership, and the purported pledge to SP ought to be recharacterized as a sale (whether or not SP actually does make an “impairing” repledge or a sale). The leading scholarly commentary on characterization of repo transactions in fact makes essentially this argument, and for that reason contends that the “sale” label affixed to a repo transaction should be respected if the repo buyer has the right, as against the repo seller, to dispose of the security. This “consent to impairment” test would be simple and logical, and it would avoid the anomalies described above. But to adopt it would require throwing overboard the accumulated weight of the broker repledge cases, which always respected the “pledge” label notwithstanding Pledgor’s consent to “impairing” repledges by SP. Moreover, this “consent to impairment” test cannot peacefully co-exist with the unlimited right

50. Another way to sum up this approach would be to say that a purported pledge in which the secured party has the right to dispose of the collateral (through outright sale or “impairing” repledge) before default is not a secured transaction, but rather a disguised securities lending transaction. Of course, if carried through consistently in all legal contexts, this recharacterization could have unpleasant tax and regulatory consequences. But anyone with experience in securitization transactions should have no reason to gag at the prospect of arguing with a straight face that a transaction may have a characterization for commercial law and bankruptcy purposes that differs from its characterization for tax and regulatory purposes.

51. See Schroeder, supra note 32, at 1017-26. Professor Schroeder distinguished repledge from sale on the ground that repledge may not “impair the debtor’s right to redeem” under Former 9-207(2)(e), but did not acknowledge the long-standing precedent allowing the pledgor to permit “impairing” repledges.
of repledge granted by Revised 9-207(c)(3), because that test would cause all pledge transactions to which that gap-filling rule applies to be recharacterized as sales.

As a result, it seems likely that a pledge transaction will continue to be characterized in the traditional way as being a secured transaction in the underlying security, notwithstanding that an "impairing" repledge is permitted or effected, despite the dubious metaphysical underpinnings of that concept. Whether the same is true if outright sale is permitted or effected seems doubtful, given the lack of historical and textual support for that notion, and given the absence of even the nominal res arguably present in a repledge transaction. However, as we shall see, the Comments to Revised Article 9 contemplate the possibility that, following such a sale, the relationship between the parties might still continue to be a secured transaction—though not in the now-departed security, but rather in a different res.

B. In Quest of a Res: The Characterization Issue Under Revised Article 9

1. Parsing Revised 9-314(c)

Revised Article 9 addresses the foregoing characterization issue in an oblique way. What it says on the subject appears primarily in the Comments. Aside from the gap-filling rule giving the secured party the right to repledge, only a single provision in the text of Revised Article 9 is visibly geared to repledge or nonaccountable sale. That provision is Revised 9-314(c), which deals with the duration of perfection by control of investment property:

(c) Investment property: time of perfection by control; continuation of perfection. A security interest in investment property is perfected by control under Section 9-106 from the time the secured party obtains control and remains perfected by control until:
(1) the secured party does not have control; and
(2) one of the following occurs:
   (A) if the collateral is a certificated security, the debtor has or acquires possession of the security certificate;
   (B) if the collateral is an uncertificated security, the issuer has registered or registers the debtor as the registered owner; or
   (C) if the collateral is a security entitlement, the debtor is or becomes the entitlement holder.
This provision is patterned after the third sentence of Former 9-305, which dealt with the duration of perfection by possession:

A security interest is perfected by possession from the time possession is taken without a relation back and continues only so long as possession is retained, unless otherwise specified in this Article.

To modern eyes this sentence reads like a fortune-cookie proverb, a truism oddly expressed. The point of the first half of the sentence was to abolish any vestige of the "equitable pledge" doctrine, under which, before the 1938 amendments to the Bankruptcy Act, the taking of possession could "relate back" to the time the security agreement was entered into for purposes of determining whether the secured party received a preference. The point of the second half was the qualifying phrase "unless otherwise specified in this Article," which was an opaque cross-reference to the provisions of Former Article 9 that allow perfection to continue temporarily following return of the collateral to the debtor in certain circumstances. The two halves do not quite mesh (because the temporary perfection alluded to is not in fact "by possession"), and the "relation back" language is now archaic. So Revised 9-313(d), the provision which now deals with the duration of perfection by possession, brings forward the former language in a revised form that really is a truism:

If perfection of a security interest depends upon possession of the collateral by a secured party, perfection occurs no earlier than the time the secured party takes possession and continues only while the secured party retains possession.

Until very late in the drafting process, Revised Article 9 used parallel language to define the duration of perfection by control. The parallelism ended in the March 1998 draft, which added the language that became subsection (c) of Revised 9-314.

Subsection (c) of Revised 9-314 has nothing to do with the concerns that motivated the odd predecessor language of Former 9-305. In effect, subsection (c) says that if SP once has control of a pledged security, SP is deemed to remain perfected by control until SP gives it back to Pledgor (in whatever way is appropriate given how that security is held). Subsection (c) is addressed to the concern that if SP has repledged (or, perhaps, sold) the security, necessarily SP no longer "controls" it and hence (but for this provision) literally would

52. See F. § 9-305 cmt. 3. See generally 1 GILMORE, supra note 12, § 14.4.
53. See F. § 9-305 cmt. 3.
no longer be perfected in it.

Given the assumption that SP continues to have a security interest at all in “the security” or “the security entitlement” following such an event (an assumption which, as we have seen, may well be justified as to a repledge, less so as to a sale), this provision seems fair enough. Two textual points merit attention. First, subsection (c) deals only with continuation of perfection, and it does not by its terms give SP analogous comfort as to continuation of the benefit of the adverse claim cut-off rules in Article 8. In the indirect holding system, those rules generally protect only persons who hold or have control over security entitlements. If SP has repledged securities, SP will not remain their entitlement holder or retain control over them (absent bizarre circumstances). Clearly the adverse claim cut-off rules ought to be read in the same spirit as Revised 9-314(c), and SP should continue to receive the benefit of those rules notwithstanding a repledge.

Second, a drafting quibble can be raised about lack of reference to “securities accounts” in Revised 9-314(c). There are five kinds of investment property—“securities” (which come in two flavors, certificated and uncertificated), “security entitlements,” “securities accounts,” “commodity contracts,” and “commodity accounts”—and it is possible for a security interest to be perfected by control in each. Revised 9-314(c), however, lays down rules on duration of perfection by control only for securities and security entitlements, leaving the statute silent on the duration of perfection by control of a securities account (as well as commodity contracts and commodities accounts, which we shall ignore). Indeed, Revised Article 9, like its predecessor, does not literally define how a secured party obtains control of a securities account at all. It provides as follows:

A secured party having control of all security entitlements or commodity contracts carried in a securities account or commodity account has control over the securities account or commodity account. Literally this is not a definition, but merely an illustration of one way in which a secured party may obtain control over a securities account. Nor would it do to read this sentence as if it were a definition, and

54. See U.C.C. §§ 8-502, 8-503(e), 8-510(a).
55. See R. §§ 9-102(a)(49) (successor to F. § 9-115(1)(f)) (definition of “investment property”), 9-106 (successor to F. § 9-115(1)(e)), 9-314(a) (successor to F. § 9-115(4)(a)) (perfection of investment property by control); R. § 8-106 (definition of “control”).
56. R. § 9-106(c) (successor to F. § 9-115(1)(e)).
conclude that a secured party has control over a securities account if and only if the secured party has control over all security entitlements carried in the securities account. As discussed in more detail below, a security interest in a securities account is supposed to extend to certain rights in addition to security entitlements carried in the account. In particular, such a security interest is supposed to include the right to any credit balance owed to the customer by the securities intermediary, and that right is not itself a security entitlement. If the only way to obtain “control” over a securities account is to have control over all security entitlements carried in the securities account, a secured party could not have “control” over a securities account which happens to carry no securities but which still carries a credit balance. That would be absurd.

This is indeed a mere drafting quibble, because it seems obvious what “control” ought to mean as to a securities account: namely, an arrangement which would suffice to give the secured party control over all security entitlements carried in the account, whether or not there actually are any security entitlements so carried. The Comments make this reasonably clear. And, while formal consistency might have called for statement of a rule as to the duration of perfection by control in this case, it also seems obvious that, just as with duration of perfection by possession, it should last as long as it lasts.

A similar gap exists in the priority rules applicable to competing secured parties each of whom has control over investment property. Revised Article 9 contains such priority rules for each type of investment property, except for “securities accounts.” Common sense again readily supplies the priority rule that should be applied to competing controlling security interests in a securities account.

57. See infra Part II.B.2.c.

58. A secured party of logical bent might assert that it literally satisfies the definition of “control” postulated in the text, on the ground that it is trivially true that the secured party has control of “all security entitlements carried in the account” when the account is empty. Logically that is true, but by that reasoning it is equally true that everyone else in the world has control, too.

59. See R. § 9-106 cmt. 4 (carrying forward with minor changes language from F. § 9-115 cmt. 4 para. 7).

60. Consider a securities account which carries a credit balance, and which may or may not have security entitlements credited to it, and assume that competing secured parties have control over the securities account. What rule determines priority in the credit balance? If one of the secured parties is the securities intermediary, the special rule in Revised 9-328(3) (which applies to “securities accounts” as well as to “security entitlements”) would apply and give the securities intermediary priority. If, however, neither secured party is the securities intermediary, that special rule does not apply. Revised 9-328(2), which sets forth the general priority rules for competing control parties, does not literally apply, because it sets forth no priority rule for
These observations are fussy, but this is a point on which the fussiness is called for. "Control" is by design an artificial construct, to be construed strictly in accordance with its statutory definition. Fussiness is the price of insisting that courts follow the statute and nothing but the statute.

More fundamental than these drafting points is the fact that Revised 9-314(c) addresses only the duration of perfection following SP's repledge or sale of collateral. It does not say whether the relationship between Pledgor and SP remains a secured transaction at all. To that subject we now turn.

2. The "Doppelganger Theory" of Revised Article 9

Revised Article 9 touches on the characterization issue in the Comments, most pointedly in the following extraordinarily rich paragraph of Comment 3 to Revised 9-314:

In a transaction in which a secured party who has control grants a security interest in investment property or sells outright the investment property, by virtue of the debtor's consent or applicable legal rules, a purchaser from the secured party typically will cut off the debtor's rights in the investment property or be immune from the debtor's claims. See Section 9-207, Comments 5 and 6. If the investment property is a security, the debtor normally would retain no interest in the security following the purchase from the secured party, and a claim of the debtor against the secured party for redemption (Section 9-623) or otherwise with respect to the security would be a purely personal claim. If the investment property transferred by the secured party is a financial asset in which the debtor had a security entitlement credited to a securities account maintained with the secured party as a securities intermediary, the debtor's claim against the secured party could arise as a part of its securities account notwithstanding its personal nature. (This claim would be analogous to a "credit balance" in the securities account, which is a component of the securities account even though it is a personal claim against the intermediary.) In the case in which the debtor may retain an interest in investment property notwithstanding a repledge or sale by the secured party, "securities accounts" as such. The common-sense solution is to apply the priority rules of Revised 9-328(2) to the credit balance as if it were a security entitlement. This point did not arise under Former Article 9, under which the general rule was that all control secured parties shared pari passu. That priority rule was drafted to apply to all "investment property" and, hence, securities accounts. See F. § 9-115(5)(b).

61. See, e.g., R. § 8-106 cmt. 7.

62. Similar principles are alluded to, or are implicit in, Comments 5 and 6 to Revised 9-207, Comment 3 to Revised 9-623, and Example 6 to U.C.C. § 8-502 (an example added by Revised Article 9).
subsection (c) makes clear that the security interest will remain perfected by control.

So this Comment describes a case in which the relationship between Pledgor and SP may continue to be a secured transaction even following SP’s sale of the pledged securities. The theory of the Comment is that the purely personal claim for redemption which Pledgor has against SP following such sale may itself be viewed as the res of a continuing secured transaction between Pledgor and SP. The Comment applies that theory in one particular setting: namely, when the pledged securities were held in a securities account that Pledgor maintains with SP, as Pledgor’s securities intermediary. In that setting, the Comment suggests that SP’s personal obligation could be deemed “part of” that securities account, and, hence, be a species of investment property to which SP’s security interest could attach.63 As a result, even after SP sells the pledged securities, they would in effect have a shadowy, Zen-like continuing existence as between Pledgor and SP. SP’s personal obligation to Pledgor on account of Pledgor’s redemption right would serve as a doppelganger for an actual security entitlement (which disappeared with the sale of the securities), and the Comment in effect holds that in the right circumstances the ghost may be treated much as though it were the thing itself. This basic idea—that SP’s redemption obligation may be viewed as the res of a continuing secured transaction—may be dubbed the “Doppelganger Theory” (or the “Theory” for short).

The Doppelganger Theory is as ingenious and self-referential as an M.C. Escher print, and it calls for careful analysis.

a. The Doppelganger Theory and the Traditional Underpinnings of Repledge

To begin with, although the above Comment refers both to sale and repledge, the metaphysical underpinnings of the Theory differ from the traditional underpinnings of repledge. The Doppelganger Theory considers the res of the secured transaction between Pledgor and SP after a repledge or a sale to be SP’s personal obligation on account of Pledgor’s redemption right (which, for short, we shall often refer to simply as SP’s “redemption obligation”). By contrast, under the traditional conception of a repledge, the Pledgor was still

63. Comment 3 to Revised 9-314 uses the word “could,” not “would.” But if there are conditions to application of the Doppelganger Theory other than those discussed herein, it is not clear what they might be.
viewed as being the owner of the underlying security following a repledge, and the res of the secured transaction between pledgor and SP was still viewed as being that security. It might be argued that this traditional conception still applies in the case of a repledge, without any need to invoke the Doppelganger Theory. In the case of an outright sale, however, the underlying security is inarguably gone, and so the only possible way to continue to characterize the Pledgor-SP relationship as being a secured transaction following an outright sale (and, it should be noted, the above Comment specifically refers to that possibility) is to hunt up an alternative res. The only plausible candidate is SP's redemption obligation. Hence the Doppelganger Theory is more critical to the characterization issue in the case of a sale than a repledge. For specificity, the following discussion of the Doppelganger Theory focuses on the context of a sale, but the same analysis should apply to a repledge if it is necessary to invoke the Doppelganger Theory in that context at all.

b. The Scope of the Doppelganger Theory

The Doppelganger Theory, as stated in the above Comment, applies only to a limited class of pledge relationships. Specifically, the Comment applies the Theory only when SP is acting as Pledgor's securities intermediary and the pledged securities were held in a securities account maintained by Pledgor with SP, so that SP's redemption obligation may be deemed part of that securities account. As we will see momentarily, the logic of the above Comment implies one further condition: namely, that SP was granted a security interest in Pledgor's entire securities account, not merely the particular securities pledged by Pledgor.

Thus, the Comment would not apply to a simple pledge in which SP is not acting as Pledgor's securities intermediary and the pledge is perfected by transfer of the pledged securities from Pledgor's account at Pledgor's custodian to SP's account at SP's custodian. In that case, Pledgor has no securities account with SP, and so SP's redemption obligation cannot be deemed part of any such securities account. Furthermore, even if SP is a securities intermediary, the Comment would apply only if SP had been acting in that capacity with respect to the pledged securities.

Although the Comment does not explain why its application of the Doppelganger Theory is limited to situations in which the foregoing conditions are met, the evident reason is that, absent those
conditions, the Theory will lead to perfection and priority problems for SP. To see this, consider the consequences of applying the Doppelganger Theory if the conditions described in the Comment are not met. For example, assume that P-2 maintains a securities account with SP-2 in which the securities pledged by P-2 to SP-2 were originally held, and that SP-2’s redemption obligation following SP-2’s sale of the securities qualifies as being part of the securities account. Assume further that SP-2 was granted a security interest only in the pledged securities, and was not granted a security interest in Pledgor’s entire securities account. Does SP-2 have a perfected security interest in its redemption obligation after it sells the pledged securities?

SP-2’s redemption obligation, standing alone, is an obligation of SP-2 to deliver a security to P-2 upon the payment of P-2’s debt. Under the ordinary principles of Revised Article 9, that redemption obligation, standing alone, would appear to be a general intangible so far as Pledgor is concerned. That redemption obligation would also be proceeds of the original collateral, namely P-2’s now-vanished security entitlement with SP-2. Because the redemption obligation is identifiable, SP-2’s security interest in the original collateral should attach to the redemption obligation under the general rules applicable to proceeds. Under those rules, moreover, SP-2’s security interest in the redemption obligation would be perfected automatically for twenty days.

However, there is nothing in Revised Article 9 that would clearly prevent SP-2’s security interest in its redemption obligation from becoming unperfected after the twentieth day, absent some further action by SP-2. If SP-2’s redemption obligation were “cash proceeds,” SP-2’s security interest would continue perfected indefinitely. But SP-2’s redemption obligation, which is nonmonetary, would not seem likely to qualify as “cash proceeds,” at least not as a general matter.

A second potential candidate for continuing SP-2’s perfection after the twentieth day is Revised 9-314(c), discussed above. But that provision applies only to the duration of perfection in “investment

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64. See R. § 9-102(a)(42).
65. See R. §§ 9-102(a)(64) (successor to F. § 9-306(1)), § 9-315(a)(2) (successor to F. § 9-306(2)).
66. See R. § 9-315(c), (d).
67. See R. § 9-315(d)(2).
68. See R. § 9-102(a)(9) (successor to F. § 9-306(1)).
property.” Considered alone instead of as part of the securities account (as would seem necessary if, as we have assumed, SP-2 does not have a security interest in the entire securities account), SP-2’s redemption obligation seemingly would not be “investment property” at all: it is certainly not itself a securities account, a security entitlement, or a security.\(^6\) Rather, as noted above, standing alone it would seem to be a mere general intangible.

Accordingly, if SP-2 does not have a security interest in the entire securities account, then in order for SP-2 to continue perfected in its redemption obligation after the twentieth day, it would seem necessary for SP-2 to file a financing statement against P-2 covering SP-2’s redemption obligation, considered as a general intangible. Of course, in a pledge transaction such as this, the last thing a secured party wishes to do is to file a financing statement. Worse yet, even if SP-2 did file a financing statement, its security interest in its redemption obligation might be primed by a competing secured creditor who has previously filed a financing statement covering general intangibles.\(^7\)

These perfection and priority problems may be avoided if SP has a security interest in the securities account maintained by Pledgor with SP. In that case, SP automatically would have control over the securities account (by virtue of SP’s status as securities intermediary for the account), and, hence, SP would have a perfected security interest in the securities account, including its redemption obligation (assuming that the redemption obligation qualifies as being “part of” the securities account).\(^8\) Moreover, SP’s status as securities intermediary for the account would also cause SP’s security interest to prime any competing security interest.\(^9\)

This final example further illustrates the fact that Revised 9-314(c) rests on a basis different from that of the Doppelganger

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69. See R. § 9-102(a)(49) (successor to F. § 9-115(1)(f)).

70. SP’s security interest in the redemption obligation would not appear to qualify for the nontemporal priority in proceeds afforded by Revised 9-322(c), because that applies only to proceeds that are either “cash proceeds” or “of the same type” as the original pledged collateral.

71. See U.C.C. § 8-106(e). Literally this gives the secured party control only over “security entitlements” carried in a securities account, but as discussed in text accompanying supra note 59, that should be sufficient to establish control over the securities account itself.

72. See R. § 9-328(3). In addition, SP might also claim the benefit of the nontemporal priority in proceeds afforded by Revised 9-322(c), because the redemption obligation, considered as part of the securities account, would seem to be “of the same type” as the original collateral.
Theory. The rule on continued perfection in Revised 9-314(c) applies to a situation in which the res of the secured transaction is considered still to be the pledged security entitlement, as would be the case in a simple pledge, or in a pledge followed by a repledge under the traditional view of repledge. But the Doppelganger Theory assumes that the res of the secured transaction is SP's redemption obligation. In the preceding example, in which SP is Pledgor's securities intermediary and has a security interest in Pledgor's entire securities account, SP remains perfected in its redemption obligation by virtue of SP's continuing control over the securities account. In that setting, there is no need to refer to the special rule on continued perfection in Revised 9-314(c).

c. SP's Redemption Obligation as “Part of” Pledgor's Securities Account with SP

Assume that the conditions set forth in the Comment quoted above are met: Pledgor maintains a securities account with SP and pledges it to SP, and SP then sells the securities carried therein. In what circumstances will SP's redemption obligation be “part of” the securities account, as contemplated by that Comment?

SP's redemption obligation itself cannot be a “security entitlement”—or at least not a security entitlement to actual securities—because a securities intermediary has a duty to hold securities corresponding to the security entitlements of its entitlement holders, and SP would be in violation of that duty after it has sold the securities. Accordingly, the Comment does not characterize SP's redemption obligation as being a “security entitlement.” However, as the Comment notes, since the 1994 revisions to Article 8 other Comments have stated that a “securities account” includes certain personal rights against the intermediary as well as the security entitlements carried in the account. In particular, as noted earlier, the Comments contemplate that a security interest in a securities account includes a security interest on any credit balance owed by the intermediary to the customer:

Note also that given the broad definition of “securities account” in Section 8-501, a security interest in a securities account would also include all other rights of the debtor against the securities intermediary arising out of the securities account. For example, a security interest in a securities account would include credit

73. See U.C.C. § 8-504(a).
balances due to the debtor from the securities intermediary, whether or not they are proceeds of a security entitlement.\textsuperscript{74}

According to the Comment applying the Doppelganger Theory, just as with SP's personal obligation to pay a credit balance to Pledgor, SP's personal obligation to Pledgor on account of Pledgor's redemption right may be sufficiently associated with the securities account to be "part of" it, and hence picked up by a security interest in the securities account.

The notion that a securities account can include personal obligations of a securities intermediary that are not security entitlements is not a happy one. To begin with, that notion appears only in the Comments, not the statutory text. It is hard to square with the statutory definition of "securities account," which refers only to "financial assets" (which by definition are the subject of "security entitlements"), and contains no hook on which to hang any associated personal obligations of the intermediary that are not security entitlements.\textsuperscript{75} Moreover, it is unclear what qualifies a particular personal obligation of a securities intermediary as being sufficiently associated with a securities account to be deemed "part of" it. The Comments quoted above are vague on the point ("arise as part of," "arise out of"). Contrary to the proceeds-like concept these phrases might suggest, the Comment quoted immediately above makes a point of negating any need for a connection between the personal obligation and security entitlements previously carried in the account. In the case of a credit balance, perhaps the requisite association between the personal obligation and the securities account is simply the intermediary's fiat, in making this association in its own records and printing the credit balance on the customer's account statement. By that standard, an SP seeking to invoke the Doppelganger Theory following a nonaccountable sale should likewise generate account statements somehow reflecting its redemption obligation—though it could not, of course, do so by simply showing the sold securities to be still present in the account, as that would give rise to a security entitlement to such securities.

\textsuperscript{74} R. § 9-108 cmt. 4. See also R. § 9-102(a)(49) (successor to F. § 9-115(1)(f)(iii)) (definition of "investment property," which includes "securities account").

\textsuperscript{75} See U.C.C. §§ 8-102(a)(9), (17), 8-501(a).
d. Is It Possible to Have a Security Entitlement to a Personal Obligation of Ones' Own Securities Intermediary?

One possible way to avoid worrying about whether SP's redemption obligation is "part of" Pledgor's securities account would be to characterize Pledgor as having a security entitlement to SP's redemption obligation. In other words, the financial asset with which Pledgor's securities account would be credited following the sale would not be the pledged securities, which of course are gone, but rather SP's personal obligation to restore them. The definition of "financial asset" includes any "property that is held by a securities intermediary" for another person, provided that the intermediary has expressly agreed with the other person to treat the property as a financial asset. So SP's redemption obligation could be a financial asset if SP, acting as securities intermediary for Pledgor, agrees to treat it as a financial asset, provided only that it qualifies as "property that is held by a securities intermediary."

Whether SP's own redemption obligation to Pledgor is "property" which SP "holds" is a nice metaphysical question. Professor Rogers, the Reporter for the 1994 revisions to Article 8, has written that an intermediary's personal obligation with respect to a credit balance "would not fall within the Article 8 definition of security entitlement because a security entitlement is not merely a contractual claim." If followed, that position would likewise disqualify SP's redemption obligation. However, that position leads to consequences that seem distinctly anomalous. Assume that Bank, a securities intermediary, issues an ordinary debt obligation (such as a certificate of deposit, commercial paper note, or bond) that Customer purchases and has credited to her securities account at Bank. That debt obligation, when held by Bank for Customer, is likewise a mere contractual claim by Customer against Bank. Rogers' position would imply that Customer cannot have a security entitlement in that debt obligation—in unique contrast to all other debt obligations of all other issuers that Customer might carry in her account.

That result is hard to swallow, and there is no obvious reason why it must be choked down. Even a contractual claim, viewed in the right light, is a species of property ("chose in action"). Article 9 recognizes that fact, insofar as it allows an obligor to take a security

76. See U.C.C. § 8-102(a)(9).
77. 8 ROGERS, supra note 16, § 9-115:6, at 806-07.
interest in its own obligation. Although such transactions were perhaps not especially common under Former Article 9, there was nothing in Former Article 9 to prevent an obligor on a general intangible (for example) from taking a security interest in that obligation. The same is true under Revised Article 9. Indeed, Revised Article 9 may make the practice of taking a security interest in one's own obligation quite commonplace, because the revision allows a bank to take a security interest in the deposit obligation it owes to its customer. Allowing a securities intermediary's personal obligation on account of a credit balance to be characterized as a "security entitlement" presents no greater conceptual difficulty than the Comments' characterization of that obligation as being somehow "part of" that securities account even though it is not a security entitlement.

Hence, it seems plausible to suppose that SP's redemption obligation to Pledgor following repledge or sale of Pledgor's collateral likewise is eligible to be characterized as a security entitlement—not, to repeat, an entitlement to actual securities, but merely to SP's purely personal obligation—which would allow SP to sidestep the question of what it takes to qualify that redemption obligation as being "part of" the securities account.

3. Repledge and Nonaccountable Sale Under the Doppelganger Theory

The reward which the Doppelganger Theory offers in exchange for undertaking these conceptual acrobatics is not all that great. Pledgor obviously has the most at stake in the event of a repledge or nonaccountable sale, because Pledgor runs the risk that, in the event of SP's insolvency, Pledgor will be unable to recover its property. But the Doppelganger Theory helps Pledgor not a whit against that risk. The underlying securities are lost and gone forever once disposed of by SP to a Transferee protected against the assertion of adverse claims. All that Pledgor then has is SP's unsecured redemption

78. See R. § 9-340(b) & cmt. 3. As to the general principle that an obligor on a general intangible may have a security interest in that obligation, see In re Dillard Ford, Inc., 940 F.2d 1507, 1151 n.5 (5th Cir. 1991). See also Subcommittee on the Use of Deposit Accounts as Original Collateral, Report, in PERMANENT EDITORIAL BOARD FOR THE UNIFORM COMMERCIAL CODE, PEB STUDY GROUP UNIFORM COMMERCIAL CODE ARTICLE 9: APPENDICES TO REPORT 325, 333-34 (1992).

79. This generalization is subject to the qualification that if the disposition is a repledge, and if a court follows the traditional view that Pledgor remains the owner of the repledged
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obligation, and Pledgor’s situation is not improved at all by conceiving that obligation to be the res of a continuing secured transaction between Pledgor and SP.

Where does this leave Pledgor in the event of SP’s insolvency following SP’s disposition of the pledged securities? Whether or not the Doppelganger Theory applies, Pledgor is unlikely to have more than an unsecured claim against insolvent SP for the value of the securities thus disposed of. The only real question is whether Pledgor may offset the amount of its debt to SP against the amount of that claim. Such offset certainly would seem sensible. But this is a subject the UCC does not address, and Pledgor’s right to effect such an offset would be subject to the vagaries of the law of the relevant state.\(^8\) SP’s redemption obligation is not a garden-variety debt, being nonmonetary (an obligation to deliver a security) and in some sense contingent (SP need not deliver the security until Pledgor has paid its debt), and if the case law in the relevant state draws formalistic distinctions about the degree of mutuality required to sustain a setoff, SP’s insolvency administrator might be able to raise nonfrivolous arguments against setoff.\(^8\) In response, Pledgor can point to the pre-UCC broker insolvency cases, which allowed the customer to offset against her margin debt the value of the securities carried by the broker for her account which she was unable to reclaim, even if her inability to reclaim resulted from a rightful repledge by the broker.\(^8\)

collateral, then Pledgor may have certain residual rights against Transferee even if Transferee is entitled to the benefit of the adverse claim cut-off rules. Under the broker repledge cases, those residual rights would have included rights in the nature of marshalling (i.e., Transferee may be compelled to apply proprietary securities of SP before applying securities owned by customers, and to apply customer securities that were rightfully repledged before applying customer securities that were wrongfully repledged) and a right of Pledgor to redeem all the collateral pledged to Transferee by paying SP’s full debt to Transferee (Pledgor then becoming subrogated to SP’s rights with respect to securities owned by other customers that Pledgor so redeems). See RESTATEMENT OF SECURITY § 41 (1941); MEYER, supra note 19, § 75. However, a Pledgor who allows an impairing repledge cannot count on those rights being worth anything.

80. See R. § 9-109(d)(10) (successor to F. § 9-104(i)) (generally excluding setoff rights from Article 9).

81. For general discussions of setoff and its limitations, see 5 LAWRENCE P. KING, COLLIER ON BANKRUPTCY ¶ 553.01 (15th ed. 1998) [hereinafter COLLIER]; and Stephen L. Sepinuck, A Defense of Extending Article 9 to Cover Security Interests in Deposit Accounts as Original Collateral, 1995 COMM. L. ANN. 477, 510-20 (Louis F. Del Duca & Patrick Del Duca eds.).

82. See, e.g., Van Bomel v. Irving Trust Co. (In re Hoyt), 47 F.2d 654, 655 (S.D.N.Y. 1931); see also Cohen v. Savings Bldg. & Loan Co. (In re Bevill, Bresler & Schulman Asset Management Corp.), 896 F.2d 54 (3rd Cir. 1990); cf. In re Salmon Weed & Co., 53 F.2d 335, 340 (2d Cir. 1931) (broker who made wrongful repledge may recoup amount due from margin customer against damages recoverable for the conversion). See generally MEYER, supra note 19, § 169.
Pledgor might also try to sidestep any mutuality requirement by arguing that SP's redemption obligation arises out of the same transaction as Pledgor's debt to SP, and so Pledgor ought to be allowed to net the two obligations under a theory of recoupment.83 Drafting of the security documents to allow such setoff or netting explicitly may be a helpful safeguard, but one hopes that a court would not be so formalistic as to make that necessary.

Assuming that Pledgor is able to establish its right to setoff or recoupment as a matter of state law, Pledgor may also have to deal with further restrictions on setoff imposed by the insolvency law under which SP's estate is administered. For example, if SP is a debtor subject to a proceeding under the Bankruptcy Code, as a general rule any setoff against SP procedurally will be subject to the automatic stay, and substantively may be subject to a variety of limitations.84 Indeed, some courts have held that setoff is not allowed as of right in any case, but is always subject to the equitable discretion of the bankruptcy court.85 The Bankruptcy Code contains various special provisions applicable to OTC derivatives transactions that are broadly designed to allow the solvent party to such a transaction to close it out and apply any collateral it holds to its counterparty's obligations upon its counterparty's bankruptcy, without regard to the automatic stay. Those provisions, however, do not by their terms clearly authorize an offset by nonbankrupt Pledgor of the value of its pledged collateral against the obligation it owes to bankrupt SP.86

The Doppelganger Theory comes into its own as a tool for SP in

83. See generally 5 COLLIER, supra note 81, ¶ 553.10. The recoupment argument might draw analogical support from cases allowing recoupment as between a security deposit with a utility and an obligation for utility services. See, e.g., New York State Elec. & Gas Corp. v. McMahon (In re McMahon), 129 F.3d 93 (2d Cir. 1997). However, there are cases to the contrary. See, e.g., In re Village Craftsman, Inc., 160 B.R. 740 (Bankr. D.N.J. 1993).

84. See Bankruptcy Code §§ 362(a)(7) (automatic stay), 553 (setoff generally).

85. See, e.g., Dayton Sec. Assocs. v. Securities Group 1980 (In re Securities Group 1980), 74 F.3d 1103, 1114 (11th Cir. 1996); FNMA v. County of Orange (In re County of Orange), 183 B.R. 609, 615 (Bankr. C.D. Cal. 1995). Courts in some jurisdictions have likewise held that setoff may be subject to judicial discretion even under nonbankruptcy law. See, e.g., New Jersey Nat'l Bank v. Gutterman (In re County of Orange), 219 B.R. 543, 566 (Bankr. C.D. Cal. 1997). There is, however, contrary authority. See, e.g., In re Applied Logic Corp, 576 F.2d 952, 957 (2d Cir. 1978); 5 COLLIER, supra note 81, ¶ 553.02[3].

86. See Bankruptcy Code § 362(b)(17). For discussion of this provision as applied to repledge situations, see Johnson, supra note 4, at 981-89. This is one of several similar provisions of the Bankruptcy Code which afford special treatment to capital markets transactions. See generally Harold S. Novikoff, Special Bankruptcy Code Protections for Derivative and Other Capital Market Transactions, in UNDERSTANDING THE BUSINESS, BANKRUPTCY AND SECURITIES ASPECTS OF DERIVATIVES 95 (Practicing Law Institute, Martin J. Bienenstock & Thomas Mowers Mayer co-chairs, 1995).
the event that Pledgor defaults after SP has repledged or sold the pledged securities. SP's status in such a case may depend upon the nature of the disposition and a court's reaction to the characterization issues discussed earlier. If the disposition was a repledge and the court takes the traditional view of the characterization issue, the relationship between SP and Pledgor will continue to be viewed as a secured transaction, the res of which is the pledged securities. If, however, the court does not take the traditional view, or if the pledged securities were sold outright, then SP and Pledgor evidently will be deemed mutual creditors, in a relationship similar to a securities lending arrangement. In that case, SP's right to offset its redemption obligation against Pledgor's debt to SP will be subject to the vagaries of non-UCC setoff and recoupment law in much the same way as just discussed in the event of SP's insolvency. If SP is eligible to take advantage of the Doppelganger Theory, SP presumably ought still to be able to proceed under these setoff and recoupment theories, if it wishes. But the Doppelganger Theory adds another knife to SP's belt, in effect allowing SP to ignore the sale and continue to treat its relationship with Pledgor as a secured transaction. True, the res of that secured transaction would be SP's redemption obligation rather than a security entitlement representing an actual security. But as far as Pledgor, Pledgor's creditors, and the world at large are concerned, SP's redemption obligation is indistinguishable from such a security entitlement, at least so long as SP is solvent.

The relationship between SP and Pledgor in this situation is quite similar to the relationship between a bank and its customer in the event that the bank takes a security interest in a deposit account the customer maintains with the bank, as Revised Article 9 now permits. SP, like such a bank, may be able to exercise the rights of a secured creditor against the chose in action it owes, as well as rights of setoff or recoupment. The benefits to SP of having both sets of rights should be much the same as the benefits to such a bank. For example, if a tax lien is asserted against Pledgor, SP might fare better if it has the rights of a secured creditor instead of setoff rights alone.

87. See R. § 9-340(b) (bank may have a right of setoff against, and an Article 9 security interest in, the same deposit account). Revised 9-340(b) does not by its terms apply to obligations other than deposit accounts, but there is no reason why the principle it states should not apply to any obligations in which the obligor also has an Article 9 security interest.

88. Compare, e.g., Horton Dairy, Inc. v. United States, 986 F.2d 286 (8th Cir. 1993) (tax lien defeats unexercised right of setoff) with Trust Co. v. United States, 735 F.2d 447 (11th Cir.
4. Doppelganger Plus: A Road Not Taken by Revised Article 9

For all of this, the Doppelganger Theory may not come into play very often because, as discussed earlier, its applicability generally will depend upon SP being a securities intermediary, the pledged securities being originally credited to a securities account maintained by Pledgor with SP, and SP taking a security interest in the entire securities account. With relatively minor changes, Revised Article 9 might have extended the same basic idea to other pledge transactions. Call this hypothetical extension "Doppelganger Plus." As we have seen, SP's redemption obligation following a nonaccountable sale can be viewed as a general intangible owed to Pledgor, in which SP may claim a security interest under the ordinary rules governing proceeds. However, unless the special conditions described in the Comment are satisfied, SP's security interest in that obligation is at risk from a perfection and priority standpoint. The idea of Doppelganger Plus would be to modify Article 9 to deal with those perfection and priority risks directly. Specifically, Article 9 would be written to give SP an automatically and permanently perfected security interest in its own redemption obligation following a rightful repledge or nonaccountable sale, and the priority rules would be modified to provide that this security interest would have priority over any competing security interest (other than one which would have primed SP's security interest in the now-vanished security).

Doppelganger Plus would not be a radical textual departure, as Revised Article 9 already contains special perfection and priority rules that are not too dissimilar to these. As to perfection, Revised Article 9, like Former Article 9, already provides that certain security interests in securities are perfected automatically and permanently.\(^8\) As to priority in this special type of proceeds, Revised Article 9 already departs from the time-honored "first to file or perfect" rule and awards priority in proceeds of investment property on a nontemporal basis in certain circumstances.\(^9\) But the effect of adding such a wrinkle would be to complicate even further an already

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8. See R. § 9-309(9), (10).
9. See R. § 9-322(c).
complex statute, and reasonable minds could differ as to whether the benefit would be worth the price.

5. Redemption Rights

A loose end that should be tied up relates to the relationship between repledge and the debtor’s right to redeem the collateral. The right to redeem was fundamental to common-law pledge and to pre-UCC personal property security statutes.91 Former Article 9 codified the debtor’s redemption right, and aside from stylistic changes Revised Article 9 carries forward the former statutory language with only a few minor tweaks.92 Although the right is often thought of mainly in connection with the exercise of remedies (perhaps because of its placement in the portion of Article 9 which deals with default), the right applies before and after default. Both Former and Revised Article 9 sternly provide that the debtor may not waive that right before default.93

The Comments to Revised Article 9 give this familiar statutory language a novel-seeming twist. Specifically, several Comments dealing with repledge, including the one quoted above in connection with the Doppelganger Theory, describe the debtor’s redemption right as one that may be limited to a purely personal claim against the secured party for the return of equivalent property when the debt is paid off.94

91. As to redemption under the common law of pledge, see RESTATEMENT OF SECURITY §§ 37, 54, 55 (1941), and JOSEPH STORY, BAILMENTS § 345 (9th ed. 1878). As to redemption under pre-UCC personal property security statutes, see 2 GILMORE, supra note 12, § 44.2, at 1216-17.

92. See F. §§ 9-506 (right of redemption and permitted waiver), 9-501(3)(d) (nonvariability); R. §§ 9-623 (right of redemption), 9-602(11), 9-624(c) (nonvariability and permitted waiver). Unlike Former Article 9, the revision prohibits even post-default waiver of the right in a consumer-goods transactions, per Revised 9-624(c). Revised 9-623 extends the right to redeem to holders of nonconsensual liens (in addition to holders of Article 9 security interests, who had that right under Former Article 9).

93. The principal provisions relating to nonvariability are cited in the preceding footnote. An obscure provision of Former Article 9, Former 9-112, gives certain rights to a person who owns the collateral but is not the “debtor” (where “debtor” in this context evidently must be understood to refer to the obligor of the secured obligation), if the secured party knows of such person’s ownership of the collateral. Among other things, Former 9-112 states that the owner has the same right as the “debtor” to redeem the collateral, “[u]nless otherwise agreed.” This provision thus seemingly permits pre-default waiver of the right, at least in this one narrow instance. However, little significance should be attached to this ill-drafted provision. The evident purpose of Former 9-112 was to limit the secured party’s duties to such owner to circumstances in which the secured party knows of such person’s ownership. Revised Article 9 deals with the subject of non-obligor owners clearly and directly, and does not carry forward Former 9-112. See R. §§ 9-102(a)(28) & cmt. 2.a, 9-605, 9-628.

94. See R. §§ 9-207 cmts. 5-6, 9-314 cmt. 3, 9-623 cmt. 4.
At first sight this might seem a radical reinterpretation of the concept of redemption. If applied to collateral generally, it would not be easy to square with the secured party's nonwaivable duty to care for collateral in its possession. If as a general matter the debtor's redemption right is, or can be, rendered purely personal, one could argue that the debtor might just as well have the power to allow the secured party to put a match to the collateral, so long as the secured party agrees to return equivalent property in the future. Indeed, it is tempting to conceive of the debtor's right to redeem collateral *in rem* as not being a distinct "right" at all, but rather as a necessary predicate to defining a relationship as being a secured transaction in the first place. A purely personal redemption right obviously is not consistent with that conception.

These Comments refer to redemption as being a purely personal claim only in the context of repledge and sale of pledged securities, however, and not as a general proposition. In so doing, these Comments merely state openly a point that has always been implicit in the traditional view of repledge. Once it is conceded that SP may make an "impairing" repledge of the collateral (whether by virtue of Pledgor's consent or the new statutory gap-filling provision), SP has the power to wipe out the value of Pledgor's property interest in the collateral. To the extent that the value of Pledgor's property interest is impaired by the repledge, it has always been the case that, as a matter of substance, Pledgor's redemption right is a mere personal claim against SP. So, while conceiving of Pledgor's redemption right as a personal claim rather than as a property right may seem anomalous—indeed it *is* anomalous—that anomaly is inherent in the time-honored view that the Pledgor-SP relationship after an "impairing" repledge remains a secured transaction.

It is also some comfort that Article 9 has always contemplated situations besides repledge in which the relationship between debtor and secured party continues to be a secured transaction even though the debtor has no right to redeem the collateral. Such a situation

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95. See R. § 9-207(a) (successor to F. § 9-207(1)) (prescribing duty of care as to collateral in the secured party's possession); U.C.C. § 1-102(3) (duties of care prescribed by the UCC may not be waived). As discussed supra note 7, this duty of care literally applies only to collateral in the secured party's "possession," but it seems likely that this duty would also be held to apply to security entitlements and uncertificated securities over which the secured party has control.

96. This thought has been forcefully expressed in connection with real estate mortgages. See, e.g., RESTATEMENT (THIRD) OF PROPERTY: MORTGAGES §§ 3.1, 6.4 (1997); 4 JOHN NORTON POMEROY, EQUITY JURISPRUDENCE § 1193, at 569 (5th ed. 1941).
arises if a non-consumer debtor signs a written waiver of its redemption right after default. Another example arises if the secured party after default makes a contract to dispose of the collateral. In both situations the debtor's redemption right terminates, but the relationship between debtor and secured party evidently still continues to be a secured transaction until the secured party disposes of the collateral or agrees to take it by way of strict foreclosure.97 Indeed, under some pre-UCC security devices the debtor routinely lost its redemption right after default or repossession, even absent a waiver by the debtor or contract of sale by the secured party.98

CONCLUSION: How I learned to stop worrying and love Revised Article 9

Repledge is a messy subject. The notion on which it rests—that the relationship between a pledgor and secured party is a secured transaction rather than a sale, despite the secured party's right to separate the collateral from the debt—gives rise to irreducible anomalies. When these anomalies are considered together with the quite distinct metaphysical conundrums that arise when considering property rights in securities held through securities intermediaries, the result is a subject that will win no prize for tidiness.

To repeat, this messiness is not attributable to Revised Article 9 or the 1994 revisions to Article 8. Repledge was entrenched long before the UCC was written, let alone these particular revision projects, and the drafters had to play the cards they were dealt. Indeed, were it not for the order imposed on the legal infrastructure of the indirect holding system by the 1994 revisions to Article 8, the anomalies posed by repledge would barely be visible. If the accommodation of repledge in the UCC is reminiscent of a square peg whose edges have been filed just enough to allow it be hammered into a round hole, the blame should be placed on the judges of the previous century, now all safely dead. De mortuis nil nisi bonum.
