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Ray D. Henson

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LIENS — SEEN THROUGH A GLASS, DARKLY

RAY D. HENSON*

The pertinent facts in the recent case of *Hertzberg v. Associates Discount Corporation*[1] were these: On June 26, 1957 Freedman purchased a Chevrolet truck and executed a chattel mortgage on the truck to the seller. The mortgagee's interest was assigned to Associates Discount Corporation. The mortgage was properly recorded in Wayne County, Michigan on July 5, 1957, nine days after its execution. Freedman filed a voluntary petition in bankruptcy on January 2, 1958, and was adjudicated a bankrupt on that date. The bankrupt had possession of the truck from the time it was purchased until it was repossessed by Associates Discount at approximately the date of bankruptcy.

A Michigan statute provided:[2]

> Every mortgage . . . of goods and chattels . . . which shall not be accompanied by an immediate delivery and followed by an actual and continued change of possession of the things mortgaged, shall be absolutely void as against creditors of the mortgagor, and as against subsequent purchasers or mortgagees in good faith, unless the mortgage or a true copy thereof shall be filed . . . : Provided, however, That any such mortgage shall not be void in the case of insolvency proceedings as against the creditors of the mortgagor if filed within 14 days from the date thereof; . . .

The receiver (afterwards trustee) petitioned for an order that Associates Discount show cause why its lien should not be declared null and void under Section 70(c) of the Bankruptcy Act, which provides in part:[3]

> . . . The trustee, as to all property, . . . upon which a creditor of the bankrupt could have obtained a lien by legal or equitable proceedings at the date of bankruptcy, shall be deemed vested as of such date with all the rights, remedies, and powers of a creditor then holding a lien thereon by such proceedings, whether or not such a creditor actually exists.

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* B.S.L. 1947, LL.B. 1949, University of Illinois; Editor, Landmarks of Law (1960). Counsel, Continental Assurance Company, Chicago.

1 272 F.2d 6 (6th Cir. 1959), affirming In re Freedman, 168 F. Supp. 25 (E.D. Mich. 1958).

2 Mich. Comp. Laws § 566.140 (Supp. 1956). Compare UCC § 9-301(2).

3 30 Stat. 565 (1898), as amended, 11 U.S.C. § 110(c) (1952).

In this instance the secured creditor won. The court concluded that the powers of the trustee as a hypothetical creditor were to be determined by state law, that the Bankruptcy Act did not limit the extent to which the state might curtail these powers, and that the state statute did not strip the trustee of any powers, since the trustee had never acquired the power to invalidate the lien.

This result should not alarm lawyers in general, and it should not disappoint anyone in particular except, possibly, referees and trustees in bankruptcy.

The referee in this instance had held that the trustee could avoid Associates Discount's lien on the authority of *Constance v. Harvey*,[4] for if the trustee had all of the rights of the most perfect possible hypothetical creditor under state law, the state could not, by the technique employed here, take any of those rights away without conflicting with Bankruptcy Act, and such a conflict would avoid the state lien.[5] Until the proviso was inserted in the state statute quoted above, a mortgage had to be recorded immediately after execution or else it was void as to those extending credit between execution and recordation, and the intended effect of the proviso was to prevent avoidance of the lien in insolvency proceedings, including bankruptcy, if it were recorded within fourteen days of its execution.[6]

The perfection of a security interest by "relation back" is not an unusual doctrine, and in the case of the Michigan statute involved here, an instance of "relation back" is evident whether the recording

[4] 215 F.2d 571 (2d Cir. 1954), cert. denied, 348 U.S. 913 (1955). In this case on November 25, 1949, copies of a purchase money chattel mortgage were sent by the seller's attorney to Albany and to Watervliet for filing. The mortgage was filed in Albany but through an error it was returned unfiled by the Town Clerk in Watervliet. Under the state statute, the mortgage had to be filed in Watervliet, and this was accomplished in October 5, 1950. The buyer was adjudicated a bankrupt on October 23, 1951. Under New York law late filing was good against creditors becoming such after the filing. Since Section 70(c) of the Bankruptcy Act gave the trustee the status of a lien creditor as to any property on which a hypothetical creditor could have obtained a lien at the date of bankruptcy, the court at first thought it was necessary to determine when the petition in bankruptcy was filed. In denying a petition for rehearing the court sua sponte corrected its view of New York law and decided that it was not necessary that the petition in bankruptcy be filed before the mortgage was filed for the trustee to prevail. Under New York law an unfiled chattel mortgage was void as to a simple contract creditor becoming such, without notice, prior to the filing of the mortgage, so that it was possible for a creditor to obtain a lien at the time the petition in bankruptcy was filed, and the trustee was entitled to be put in the position of an "ideal" hypothetical creditor.

[5] In re Freedman, 168 F. Supp. 25, 27 (E.D. Mich. 1958). The referee was on fairly firm ground, it would appear, if it were necessary for him to attempt to follow the strained construction of the Bankruptcy Act adopted sua sponte by the Second Circuit in Constance v. Harvey.

[6] Ibid.

is "immediate" or within fourteen days. That is, if a purchase money security interest, such as this one, is in dispute, the usual assumption will be that it attached at the moment the purchaser acquired the chattel or his "rights" in it, and there is bound to be some interval between the "creation" of the security interest and the recording of the instrument which gives public notice of its existence.[7] When an extension of credit makes an acquisition possible, it is anomalous to deprive the "secured" creditor of his security for the undeserved benefit of a class of creditors who probably have not—except in someone's imagination—extended credit relying on the debtor's ownership of a specific chattel. Unless a sensible and practical reading is given to state statutes creating liens and to the Bankruptcy Act, all creditors will become unsecured creditors in bankruptcy. This may be a constitutionally permissible result, but it seems an unnecessary interference with business expectations.

In this age of credit financing, the greater the calculated risk, the higher the interest rate will be, if credit is extended at all. Surely Michigan, of all states, should be interested in protecting secured financers of motor vehicles and in creating a climate conducive to the purchase of automobiles as cheaply and as rapidly as possible in the light of the prime importance of automobile manufacturing to Michigan's economy and the fact that a majority of automobile sales cannot be consummated as cash transactions.

The nature of liens (and priorities) has received considerable judicial explication within recent years, and the problem is far from solved. It is worthy of more exploration, and a passage from the world's most readable book on logic furnishes a point of departure. The White Knight has told Alice that he will sing a song to comfort her, and "The name of the song is called 'Haddocks' Eyes'."

> "Oh, that's the name of the song, is it?" Alice said, trying to feel interested.
>
> "No, you don't understand," the Knight said, looking

[7] Under the Uniform Commercial Code, a security interest attaches when (1) there is an agreement that it attach, (2) value is given, and (3) the debtor has "rights" in the collateral (§ 9-204), and it is perfected by filing a financing statement, unless filing is excused (§ 9-302(1)), as it may be when the secured party takes and retains possession of the collateral (§ 9-305) or in the case of purchase money security interest in "consumer goods" other than fixtures and motor vehicles (§ 9-302(1)(d)), subject, however, to certain buyers taking free of the security interest unless it is recorded (§ 9-307(2)), and motor vehicles may be exempt from the Code's filing provisions (§ 9-302(3)). On Code security interests under the Bankruptcy Act, see Coogan, The Impact of Article 9 of the Uniform Commercial Code on the Corporate Indenture, 69 Yale L.J. 203, 241-49 (1959); Comment, The Commercial Code and the Bankruptcy Act: Potential Conflicts, 53 Nw. U.L. Rev. 411 (1958).

a little vexed. "That's what the name is *called*. The name really is '*The Aged, Aged, Man*'."

"Then I ought to have said, 'That's what the *song* is called'?" Alice corrected herself.

"No, you oughtn't: that's quite another thing! The *song* is called 'Ways and Means': but that's only what it's *called*, you know!"

"Well, what is the song, then?" said Alice, who was by this time completely bewildered.

"I was coming to that," the Knight said. "The song really *is* 'A-sitting On A Gate': and the tune's my own invention."[8]

The problem of proper names appears to be one of the most difficult problems in logic, at least to some logicians,[9] and this paper will offer no contribution towards a solution. But to apply Lewis Carroll's dialogue to a familiar situation, suppose we have in mind a particular geographical area in Italy. We in the United States may call the name of this area "Rome", but the *name*, in Italy, is "Roma". The area may be called "The Eternal City", and it is what it is: the congeries of people, places, things that we choose to refer to in the particular circumstances.[10]

To come home to our problem here, Professor MacLachlan has differentiated liens and priorities in this way: "A true lien is a property right existing and entitled to recognition as soon as it is created by contract, by conveyance, by legal process, or otherwise. A mere direction of the order of distribution in cases of insolvency or liquidation is only a priority in substance."[11]

It would appear that the major distinction between liens and priorities is to be drawn on the basis of *when* the differentiation becomes important. Neither a lien nor a priority will be said to exist unless money is owed, and it will not matter how we describe

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[8] Carroll, Alice's Adventure in Wonderland and Through the Looking-Glass 281 (Modern Library ed.).

[9] See e.g., Russell, Human Knowledge, Its Scope and Limits 72-84 (1948); Russell, My Philosophical Development 156-174 (1959); Quine, From a Logical Point of View, passim (1953).

[10] This analysis was suggested by R. W. Holmes, The Philosopher's Alice in Wonderland, 19 Antioch Review 133 (1959).

[11] MacLachlan, Improving the Law of Federal Liens and Priorities, 1 B.C. Ind. & Com. L.R. 73, 76 (1959). When using the label "property right", it is well to recall the words of Mr. Justice Holmes in Du Pont v. Masland, 244 U.S. 100, 102 (1917): "The word 'property' as applied to trade marks and trade secrets is an unanalyzed expression of certain secondary consequences of the primary fact that the law makes some rudimentary requirements of good faith."

the creditor's interest unless the debtor is involved in some kind of financial difficulty and cannot or will not pay the debt. Unless a debtor has "property" of some description, no debt can be paid, and when we are dealing in fact situations where either "lien" or "priority" may customarily be applied, the creditor clearly has some kind of "interest" in the debtor's property.

It would seem to be satisfactory to use the term "priority" to apply to a creditor's interest in a distribution of a debtor's assets on insolvency, as Professor MacLachlan suggests, when that creditor has had no *particular* interest in a specific asset at an earlier time. This usage leaves us with "lien" to apply to interests in specific assets which arose before insolvency and which are normally enforceable without regard to insolvency.

Whichever term we use is chosen because we have analyzed a set of facts and decided that such usage is proper.[12] There is nothing inexorable about the use of these words; others would do as well. The use of either "lien" or "priority" simply is a short-hand expression for saying that, in the analyst's opinion, the existence of a given set of facts will, if the proper motions are gone through, lead to a particular legal result.[13]

The set of facts in our legal problem is equivalent to what the "song really is" or to our geographical area. From these facts we draw a legal conclusion that a "money claim" exists, and this is what our song is called; it is our "Eternal City". The name of this claim may be, in our case, a lien, as in the name of the song or "Roma". We may call this name something else that conforms to our purposes, as "Rome" is preferred by some to "Roma", and if we are talking of something named "lien", we may sometimes call it a mortgage.[14] We may call it by a double name, such as tax lien,

[12] Bertrand Russell has observed that a child acquires the habit of using the word "dog" on appropriate occasions in the same way that other habits are acquired. He hears others use the word "dog" when a particular animal is present and presently he has the impulse to say "dog" at the appropriate time, or when he hears the word, he looks for the animal. With the acquisition of these two habits the child knows the meaning of "dog", he can use the word correctly, and he need know no more on the subject unless he becomes a lexicographer. Russell, My Philosophical Development 146 (1959). Russell limits this analysis of "meaning" to what he calls "object-words", of which the law has few or none, but this analysis is, nonetheless, helpful.

[13] I think this is a fair extension of Mr. Justice Holmes' comment that ". . . a legal duty so called is nothing but a prediction that if a man does or omits certain things he will be made to suffer in this or that way by judgment of the court; and so of a legal right." Holmes, "The Path of the Law" in Collected Legal Papers 167, 169 (1920). See also Ross, Tû-Tû, 70 Harv. L. Rev. 812 (1957).

[14] Admittedly liens and songs are not quite comparable, so this analogy is not completely satisfactory, but even Lewis Carroll was inconsistent in saying, "The song really is 'A-sitting On A Gate', because what the song really was, could only have been told by singing it.

mechanic's lien, or landlord's lien. We may say it is prior or subsequent, superior or inferior, general or specific, and recently it has become quite important to "know" whether it can be correctly called choate or inchoate.

It is tautological, and therefore true, to say, "A lien is a lien;"[15] but it is not helpful. Nevertheless, it has become a question of significance to ask, "When is a lien a lien?" (Obviously "lien" is used here in two different senses.) Within recent years a great many state-created "liens" have been held to be inchoate and not perfected, so that the federal priority or federal revenue lien has come ahead of them. This series of cases has created great consternation at the bar, and doubtless a great many expectations have been disappointed.[16] But the results here—as contrasted with the liens-in-bankruptcy cases —are intellectually defensible, if we analyze the nature of liens; and if we insist that an interest may be treated as a lien when it is not so-called, then we must surely concede that the mere use of the label does not foreclose an investigation into the nature of the product. The proper way to change the result in federal versus state lien contests is through legislation,[17] not through continual (and by now probably useless) criticism of the Supreme Court. The Court has wrestled with a very basic and significant set of problems: *What* is a lien? *When* is a lien? How is a lien created? Is there a period of gestation or does it emerge full-grown, as from Medusa's headless body? These problems are not simple, and they are worthy of more serious analytical thought than they have received. Liens are purely mental conceptions, and the difference between, for example, a coventional mortgage lien and the so-called floating lien of the Uniform Commercial Code is only one of degree, not kind.

If someone asks what a pencil is, the simplest and best way to answer the question is to hold up a pencil.[18] If someone asks what

[15] Such, at least, is the traditional, law-of-identity, Aristotelian learning. It was once subscribed to by Robert M. Hutchins; Sondel, The Humanity of Words 94 (1958). But in the non-Aristotelian view of general semantics, as in the non-verbal world of experience, tautologies have limited validity; that is, lien 1 is not lien 2, a lien (federal tax) is not a lien (mortgage), a mortgage lien is not a mechanic's lien, etc. See Johnson, People in Quandaries 7-10, 178-83, passim (1946).

[16] The articles on this subject are multitudinous. In general, see Kennedy, The Relative Priority of the Federal Government: The Pernicious Career of the Inchoate and General Lien, 63 Yale L.J. 905 (1954); MacLachlan, Improving the Law of Federal Liens and Priorities, 1 B.C. Ind. & Com. L.R. 73 (1959); Panel Discussion, Dangers Under Recent Federal Tax Lien Decisions, 14 Bus. Law. 12 (1958).

[17] Such legislation has, of course, been proposed. See Proceedings, Section of Real Property, Probate and Trust Law, American Bar Association, Part II, p. 89 (1957); Id., p. 78 (1958); Id., p. 56 (1959); MacLachlan, supra note 16, at 82.

[18] This is a favorite example of Korzybski, and, as he points out, the proper answer

a lien is, we cannot hold one up on exhibition. A lien—or priority—is not a physical *thing*. It is the name for a legal conclusion which we normally draw from certain assumed facts. The correctness of our conclusion will occasionally be tested in court, and the final answer given by a court is, for us, "law" whether we agree with it or not. In any case we can never point to any *thing* and call it a lien. It is a great problem in law—and it is a basis of distinction between law and the natural sciences—that we can never apply the same name to two exactly similar situations. There must be differences, and frequently they are not negligible, although for purposes of *stare decisis* we emphasize the similarities and minimize or ignore the differences. This problem is not confined to law, of course.[19] It would not be possible to carry on our normal business if we did not have the faculty of ignoring differences. We meaningfully use such words as "cow" by concentrating on the similarities we have observed, usually in the female members of the genus Bos, and ignoring individual variations. It is helpful to have one word to describe, individually or collectively, Bossie 1, Bossie 2, Bossie 3, etc.

As Mr. Justice Frankfurter has pointed out,[20] Justice Oliver Wendell Holmes explored the nature of meaning long before Ogden and Richards published their epochal work on *The Meaning of Meaning*, and these words of Mr. Justice Holmes ought always to be remembered:[21]

> We must think things not words, or at least we must constantly translate our words into the facts for which they stand, if we are to keep to the real and the true. I sometimes tell students that the law schools pursue an inspirational combined with a logical method, that is, the postulates are taken for granted upon authority without inquiry into their worth, and then logic is used as the only tool to develop the results. It is a necessary method for the purpose of teaching dogma. But inasmuch as the real justification of a rule of law, if there be one, is that it helps to bring about a social end which we desire, it is no less necessary that those who

to the question is non-linguistic. It is not accurate to say, "This *is* a pencil." The object we are talking about is not verbal. Korzybski, Science and Sanity 35 passim (4th. ed., 1958).

19 See, e.g., Ogden and Richards, The Meaning of Meaning 209 et seq. (1956 ed.). See also Cairns, "Language of Jurisprudence" in Language: An Enquiry Into its Meaning and Function 232 (Anshen ed. 1957); Probert, Law and Persuasion: The Language-Behavior of Lawyers, 108 U. of Pa. L. Rev. 35 (1959).

20 Frankfurter, "Mr. Justice Holmes" in Of Law and Men 158, 167 (1956).

21 Holmes, "Law in Science and Science in Law" in Collected Legal Papers 210, 238-39 (1920).

make and develop the law should have those ends articulately in their minds.

The Michigan recording statute involved in *Hertzberg* may, in fact, conflict with the Bankruptcy Act in some circumstances, but the result in that case was proper.[22] There have been enough mutations in the progeny of *Constance v. Harvey,* and there was no need for the Sixth Circuit to follow a Second Circuit decision which could well be restricted, as a precedent, to late mortgage filings in Watervliet.

[22] MacLachlan, Two Wrongs Make a Right, 37 Tex. L. Rev. 676 (1959).