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HOUSE OF REPRESENTATIVES
COMMITTEE ON
FINANCIAL SERVICES
BILL RESEARCH & ECONOMIC IMPACT STATEMENT

BILL #: HB 3399

RELATING TO: Fraudulent asset transfers

SPONSOR(S): Representative Ogles

COMPANION BILL(S): SB 0602

ORIGINATING COMMITTEE(S)/COMMITTEE(S) OF REFERENCE:
(1) FINANCIAL SERVICES
(2)
(3)
(4)
(5)

I. SUMMARY:

A bulk sale of inventory, supplies, merchandise, or other material not sold in the ordinary course of a seller's business would be considered a fraudulent transfer pursuant to chapter 726, F.S., unless the buyer, prior to the sale:

(a) acquires a list of the seller's unsecured creditors from the seller; and
(b) gives notice of the proposed transfer to every unsecured creditor not less than 15 days prior to the proposed transfer.

Every unsecured creditor of the seller who, in turn, provides notice to the buyer of the creditor's unsecured claim within 15 days of the transfer shall be treated as if that creditor holds a security interest in the goods subject to the proposed transfer.

The buyer's failure to acquire a list of unsecured creditors from the seller and notify each creditor on the list shall obligate the buyer to pay the claims of the seller's unsecured creditor's claims to the extent of the seller's obligation. Nothing in the bill shall be construed to relieve the seller of any obligation to any unsecured creditor of the seller.

The bill does not have a fiscal impact.

II. SUBSTANTIVE RESEARCH:

A. PRESENT SITUATION:

Prior to 1993, before a bulk sale of materials, supplies, merchandise, or other inventory that was not sold in the ordinary course of the seller's business could be made to an individual, that individual was required to demand a list of the seller's unsecured creditors and notify each of those creditors of the impending sale. A "secured creditor" is one who has acquired some form of pecuniary assurance of payment of his debt, such as a mortgage, collateral or a lien. An "unsecured creditor" is one which has not acquired some form of pecuniary assurance. For instance, a bartender running a "tab" on a customer would be an "unsecured creditor."

Hypothetical:

> Joe, the owner of Joe's Stucco Contracting, opens an account with Contractor's Business Supply, a business which primarily sells construction materials to subcontractors on an account basis. Joe's (the business) owns three trucks, four mixers, and various ancillary construction materials necessary for the business of applying stucco to residential homes. Joe (the owner) looses three major residential accounts and quickly finds himself in arrears with those he purchased equipment and supplies (including Contractor's Building Supply). Joe seeks to get out of the construction business and finds a buyer for all of his equipment. Prior to completing the purchase, the buyer must first get a list of Joe's creditors and inform these creditors of the impending sale.

If the buyer failed to notify the creditors, the creditors (e.g., Contractor's Business Supply) could nullify the sale and treat the goods as if they still belonged to the seller. This procedure could be found in Chapter 676, F.S., which contained the provisions of Article 6 of the Uniform Commercial Code. Chapter 676 was repealed by Chapter 93-77, Laws of Florida. [1]

Using the facts as expressed in the above hypothetical, since the repeal of Chapter 676, the buyer of Joe's "business" (i.e., all of the stucco equipment) would not have to acquire a list of Joe's creditors and notify these creditors of the impending sale. Unless Contractor's Business Supply perfected their security interest on Joe's account by filing a financing statement with the Department of State (pursuant to Part IV of chapter 679, F.S., Florida's UCC chapter regarding secured transactions), Contractor's Business Supply would be an unsecured creditor. Unsecured creditors "stand" behind secured creditors when there is a priority of payment in, for instance, a bankruptcy proceeding. If

[1] According to separate staff analysis for bills which sought to repeal Chapter 676 (HB 977, and SB 710, the latter of which passed as Chapter 93-77, Laws of Florida), a then-contemporaneous study by the National Conference of Commissioners on Uniform Laws and the American Law Institute recommended the repeal of Article 6 for the following reasons: (a) compliance with Article 6 by buyers had substantially decreased due, in part, to the cost and delay involved and because many sellers indemnified the buyer or made other provisions for creditor claims; and (b) the Article 6 safeguards afforded little relief to aggrieved creditors if the inventory was already encumbered by a valid and perfected security interest.

Joe sold his business and left the vicinity to avoid payment of the account, and if Contractor's did not file a security interest, then Contractor's would have no immediate recourse against the buyer (unless fraud is involved in the transaction), and no recourse against Joe unless he could be found.

A security interest for an account like the one in the hypothetical may be perfected by filing a financing statement and a $25 filing fee with the Department of State, pursuant to Part IV of chapter 679, F.S. Each filing lapses on the expiration of a five year period, unless renewed by a separate filing. Amendments to the registered filing must be accompanied by a $12 fee.[2] Therefore, if the hypothetical Contractor's Business Supply maintains a total of 600 separate accounts statewide, it would cost a total of $15,000 to perfect security interests in each account, and would cost a total of $7,500 to file an amendment to each financing statement.

According to the Department of State, some of their largest filers (e.g., Sears, Goodyear) often file financing statements describing "...accounts now and hereafter acquired..." as a kind of "blanket" filing for certain accounts, which are renewed every five years. As an account acquires a new branch store, the financing statement is typically amended to include the new debtor.

B. EFFECT OF PROPOSED CHANGES:

A bulk sale of inventory, supplies, merchandise, or other material not sold in the ordinary course of the seller's business would be considered a fraudulent transfer pursuant to chapter 726, F.S., unless the buyer:

(a) acquired a list of the seller's unsecured creditors from the seller; and
(b) gave notice of the proposed transfer to every unsecured creditor of the seller not less than 15 days prior to the proposed transfer.

Pursuant to the remedies section of chapter 726, F.S., and subject to any defenses asserted by the transferee, the creditor may obtain a court order: "avoiding" the transfer to the extent necessary to satisfy the creditor's claim; enjoining against further disposition by the debtor or a transferee, or both; or, appointing a receiver to take charge of the transferred assets.

Every unsecured creditor of the seller who provided notice to the buyer of the creditor's unsecured claim within 15 days of the sale would be treated as if that creditor holds a security interest in the goods subject to the proposed sale.

The buyer's failure to acquire a list of unsecured creditors from the seller and notify each creditor on the list would obligate the buyer to pay the claims of the seller's unsecured creditor's claims to the extent of the seller's obligation. Nothing in the bill would be construed to relieve the seller of any obligation to any unsecured creditor of the seller.

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[2]Fees for filing financing statements under chapter 679 may be found in s. 15.091, F.S.

C. APPLICATION OF PRINCIPLES:

1. <u>Less Government:</u>

a. Does the bill create, increase or reduce, either directly or indirectly:

(1) any authority to make rules or adjudicate disputes?

N/A

(2) any new responsibilities, obligations or work for other governmental or private organizations or individuals?

N/A

(3) any entitlement to a government service or benefit?

N/A

b. If an agency or program is eliminated or reduced:

(1) what responsibilities, costs and powers are passed on to another program, agency, level of government, or private entity?

N/A

(2) what is the cost of such responsibility at the new level/agency?

N/A

(3) how is the new agency accountable to the people governed?

N/A

2. <u>Lower Taxes:</u>

a. Does the bill increase anyone's taxes?

N/A

b. Does the bill require or authorize an increase in any fees?

N/A

c. Does the bill reduce total taxes, both rates and revenues?

N/A

d. Does the bill reduce total fees, both rates and revenues?

N/A

e. Does the bill authorize any fee or tax increase by any local government?

N/A

3. Personal Responsibility:

a. Does the bill reduce or eliminate an entitlement to government services or subsidy?

N/A

b. Do the beneficiaries of the legislation directly pay any portion of the cost of implementation and operation?

N/A

4. Individual Freedom:

a. Does the bill increase the allowable options of individuals or private organizations/associations to conduct their own affairs?

Yes. The bill requires buyers of bulk merchandise or inventory that is not sold in the ordinary course of the seller's business to acquire a list of the seller's unsecured creditors and to notify each creditor of the proposed sale no less than 15 days of the sale.

b. Does the bill prohibit, or create new government interference with, any presently lawful activity?

Yes. The bill requires buyers of bulk merchandise or inventory that is not sold in the ordinary course of the seller's business to acquire a list of the seller's unsecured creditors and to notify each creditor of the proposed sale no less than 15 days of the sale.

5. Family Empowerment:

a. If the bill purports to provide services to families or children:

(1) Who evaluates the family's needs?

N/A

(2) Who makes the decisions?

N/A

(3) Are private alternatives permitted?

N/A

(4) Are families required to participate in a program?

N/A

(5) Are families penalized for not participating in a program?

N/A

b. Does the bill directly affect the legal rights and obligations between family members?

N/A

c. If the bill creates or changes a program providing services to families or children, in which of the following does the bill vest control of the program, either through direct participation or appointment authority:

(1) parents and guardians?

N/A

(2) service providers?

N/A

(3) government employees/agencies?

N/A

D. STATUTE(S) AFFECTED:

Chapter 726, F.S., relating to fraudulent transfers. Creates s. 726.202, F.S.

E. SECTION-BY-SECTION RESEARCH:

Section 1. Creates s. 726.202, F.S., requiring the buyer of bulk inventory from a seller, which sale is not in the ordinary course of business, to secure a list of the seller's unsecured creditors from the seller and notify those creditors within 15 days of the impending bulk sale. Any creditor of the seller who notifies the buyer with the 15 day period shall be treated as holding a security interest in the inventory subject to the sale. Failure to notify the unsecured creditors of the seller renders the sale fraudulent, and further obligates the buyer to pay the claims of the seller's unsecured creditors to the same extent as the seller is obligated. Nothing in this section shall be construed to relieve the seller of any obligation to any unsecured creditor of the seller.

Section 2. Establishes an effective date of October 1 of the year enacted.

III. <u>FISCAL RESEARCH & ECONOMIC IMPACT STATEMENT</u>:

A. FISCAL IMPACT ON STATE AGENCIES/STATE FUNDS:

1. <u>Non-recurring Effects</u>:

   None

2. <u>Recurring Effects</u>:

   None

3. <u>Long Run Effects Other Than Normal Growth</u>:

   None

4. <u>Total Revenues and Expenditures</u>:

   None

B. FISCAL IMPACT ON LOCAL GOVERNMENTS AS A WHOLE:

1. <u>Non-recurring Effects</u>:

   None

2. Recurring Effects:

   None

3. Long Run Effects Other Than Normal Growth:

   None

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

1. Direct Private Sector Costs:

   Buyers of bulk merchandise not sold in the ordinary course of a seller's business must notify unsecured creditors of the pending sale. Failure to notify the seller's unsecured creditors will obligate the buyer to pay the claims of the unsecured creditors to the extent seller is obligated to each creditor.

2. Direct Private Sector Benefits:

   Unsecured creditors must be notified within 15 days of a proposed sale of a debtor's bulk inventory sold not in the ordinary course of the seller's business, or the sale shall be considered a fraudulent transfer pursuant to Chapter 726, F.S. Unsecured creditors who receive notice of such a sale and return claims to the potential purchaser of the merchandise within that 15 day period shall be considered to hold a security interest in the merchandise. Unsecured creditors who are not notified of the sale by the buyer shall have their claims paid by the buyer to the same extent the seller is obligated to the creditor.

3. Effects on Competition, Private Enterprise and Employment Markets:

   Unless the seller indemnifies the buyer or makes other provisions for the claims of creditors, the sale of a majority of a business's supplies, merchandise, inventory, or other materials not in the ordinary course of the seller's business will be delayed while the process of creditor notification runs its course.

D. FISCAL COMMENTS:

   N/A

IV. CONSEQUENCES OF ARTICLE VII, SECTION 18 OF THE FLORIDA CONSTITUTION:

A. APPLICABILITY OF THE MANDATES PROVISION:

   N/A

B. REDUCTION OF REVENUE RAISING AUTHORITY:

N/A

C. REDUCTION OF STATE TAX SHARED WITH COUNTIES AND MUNICIPALITIES:

N/A

V. COMMENTS:

None.

VI. AMENDMENTS OR COMMITTEE SUBSTITUTE CHANGES:

N/A

VII. SIGNATURES:

COMMITTEE ON FINANCIAL SERVICES:

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