



Perfection of Vendor Interests in New Mexico Real Estate Contracts Under Revised Article 9 of the UCC

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Because of the 2001 adoption of Revised Article 9 of the Uniform Commercial Code (the “Code”), filing financing statements and performing UCC searches should become routine when either buying, or lending on, a seller’s interest in a real estate contract (the “seller’s contract interest”).

1. History Of Perfecting Security Interests In Real Estate Contracts In New Mexico Prior to Revised Article 9

For many years, New Mexico real estate contracts have served as a seller financing vehicle to facilitate the sale of real estate (the “property”). The real estate contract (a “contract”) is an alternative to a note and mortgage. The contract has the advantage, subject to certain limitations, of allowing a seller to quickly retake title to the property if an uncured default occurs.

Under a contract, the seller takes a stream of payments over time and the buyer takes immediate possession and enjoyment of the property. Upon fulfillment of the contract, the seller releases a deed conveying title to the buyer. That deed and (usually) a special warranty deed (for the purpose of re-conveying title to the property to the seller if a default occurs) are typically placed in escrow. If the buyer defaults (usually by failing to cure a breach after a 30-day demand letter), the seller either sues for the balance due or takes back the property by obtaining and recording the special warranty deed from escrow. New Mexico courts allow a buyer to avoid a forfeiture if the forfeiture “shocks the conscience” of the court.¹

The seller’s contract interest may be sold

or encumbered. The seller’s contract interest is often bought and sold in a secondary market. Before the adoption of the 2001 Revised Article 9 of the Code, the standard method to affect an assignment or collateral assignment of a seller’s contract interest was to record an assignment or collateral assignment of the contract, together with a deed conveying bare legal title to the assignee or collateral assignee, subject to the assignment or collateral assignment.

Before the enactment of Revised Article 9, a question arose as to whether a lender taking a security interest in a seller’s contract interest was also required to file a financing statement to perfect a security interest in the contract. In *Simpson v. First National Bank*, 56 BR 586 (1986), bankruptcy Judge Mark McFeeley ruled that contract assignments given to a lender by a debtor in possession were “general intangibles” under pre-revised Article 9 §55-9-106 and were required to be perfected by filing. Since no financing statement had been filed by the lender, the debtor was able to avoid the lender’s security interest in the contract. The judge rejected the lender’s view that the contract could be perfected by possession alone. After this decision, many lawyers routinely advised lenders to file financing statements when taking a security interest in a seller’s contract interest.

On certification from the 10th Circuit, *Anthony v. Alsup*, 114 N.M. 95, 835 P.2d 811 (1992), addressed whether a collateral assignment of a seller’s contract interest was perfected by a lender only by recording or if a filed financing statement was required.

A seller’s contract interest had long been

characterized as personalty², but *Anthony* held that Section 55-9-104(j) of the pre-revised Article 9 excluded a seller’s contract interest from the operation of Article 9. Section 9-104(j) provided that “[t]his article does not apply ... to the creation or transfer of an interest in a lien on real estate, including a lease or rents thereunder.” *Anthony* stated: “[f]rom a purely practical standpoint, parties tracing the history of a title to real property would customarily search the records of the county recorder where the land is located and not the Office of the Secretary of State.” *Anthony*, 114 N.M. at 99.

After *Anthony*, recording the collateral assignment was all that was required to perfect the lender’s security interest in a seller’s contract interest.

2. Revised Article 9

Article 9 was revised in 2001. Is *Anthony* still good law? Does perfection of a lien on a seller’s contract interest require a filed financing statement? Must a *buyer* of a seller’s contract interest also file a financing statement even though that buyer is not lending the seller anything?

Anthony relied heavily on official comments to the Code. However, when the legislature enacted Revised Article 9 the comments also changed. In a footnote to *Anthony*, the Court “recognize[d] that the comments represented the opinions of the National Conference of Commissioners of Uniform Statute [sic] Laws and the American Law Institute” and that “[t]he purpose of the comments are [sic] to explain the Code; thus promoting uniformity of interpretation.”³ The new comment to §55-

¹ See *Huckins v. Ritter*, 99 N.M. 560, 562, 661 P.2d 52, 54 (1983).

² See, e.g., *Marks v. City of Tucumcari*, 93 N.M. 4, 595 P.2d 1199 (1979).

³ 114 *Anthony*, N.M. at 98, Footnote 1.

9-102(3), now §55-9-109(b), states:

It also follows from subsection (b) that an attempt to obtain or perfect a security interest in a secured obligation by complying with nonarticle 9 law, as by an assignment of record of a real property mortgage, would be ineffective.

In “Transfers by Vendors of Interests in Installment Loan Contracts: The Impact of Revised Article 9 of the Uniform Commercial Code,” 38 *Real Property, Probate and Trust Journal*, No. 3 Fall 2003, at 427, professor Dale Whitman states that “the proper method of perfecting a security interest in a vendor’s position under an installment loan contract was controversial prior to the adoption of Revised Article 9,” noting the position of many courts on this issue, including the New Mexico Supreme Court in *Anthony*. He declares, however, that “[r]evised Article 9 clears up the controversy about whether security interests in the payment stream and the supporting real estate rights must be separately perfected.” *Id.*

Under Revised Article 9, a right to a stream of payments arising from a sale of property is an “account” pursuant to §9-102(a)(2)(i). In that section, an “account” includes “a right to payment of a monetary obligation, whether or not earned by performance . . . for property that has been sold, leased, licensed, assigned or otherwise disposed of . . .”

In the usual case, perfection of a security interest in an account is accomplished by filing a financing statement.⁴ §55-9-310. Thus, under Revised Article 9, a lender desiring to perfect a security interest in a seller’s contract interest as collateral should always file a financing statement. If the

borrower (the debtor) is a New Mexico resident or, if an entity, is organized in New Mexico, the filing office should be the New Mexico Secretary of State. As a practical matter, the collateral assignment should also be recorded.

An outright sale of a seller’s contract interest *also* requires a filed financing statement. Section 55-1-201(37) includes in the definition of “security interest” *any* interest of a *buyer* of accounts. As mentioned above, an account includes a seller’s contract interest. Thus, the buyer of a seller’s contract interest is buying an account as defined by the Code which, in turn, is defined as a security interest which must, therefore, be perfected by filing a financing statement.

If a buyer of a seller’s contract interest records only an assignment of the contract but does not file a financing statement, that interest remains unperfected. If the original seller sells the seller’s contract interest to a second buyer who then properly files a financing statement, many, if not most, lawyers might well think that the first buyer’s act of recording would give constructive notice of the assignment to the second buyer and, therefore, the first buyer would prevail in an action determining the owner of the seller’s contract interest, despite the fact that the first buyer did not file a financing statement. However, § 55-9-322(a)(2) provides that as to conflicting security interests in the same collateral, the secured party who files a financing statement first wins, regardless of actual or constructive notice of the unperfected security interest.

The buyer or lender should also record the assignment or collateral assignment to prevent the original seller from wrongfully

exercising rights of forfeiture and then selling or encumbering to a *bona fide* buyer or encumbrancer without notice of the rights of the assignee (or wrongfully releasing the contract buyer from further liability under the contract after which that buyer sells the underlying real property to a bona fide buyer for value). In such cases, the recording act may protect the rights of the *bona fide* buyer or encumbrancer.

As Whitman states, “The inescapable conclusion is that Article 9 does indeed trump the recording acts.” *Id.* at 443. Thus, a buyer of a seller’s contract interest, or a lender claiming a security interest in a seller’s contract interest, must perform a UCC search and file a financing statement in connection with the transaction.

At least until a New Mexico appellate court declares otherwise, UCC-1’s and UCC searches should become routine procedure when either buying or lending on a seller’s contract interest.

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⁴ A limited exception to this rule is found at §55-9-309(2), which provides for automatic perfection of an account if the assignor is selling or encumbering only an insignificant portion of the assignor’s accounts. In the usual case involving contracts, the contract assigned or used as collateral will be a significant portion of the seller’s “accounts.” Any prudent lender would file a financing statement rather than rely on an argument as to whether the transferred contract was significant or not.