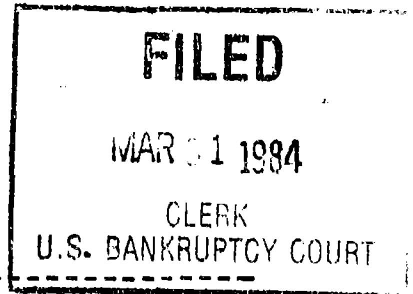

UNITED STATES BANKRUPTCY COURT

WESTERN DISTRICT OF WISCONSIN

In re: Case Number:

REOROWICZ CONSTRUCTION COMPANY, INC. WF11-83-01842

Debtor.

FINDINGS OF FACT
CONCLUSIONS OF LAW
AND
ORDER FOR REINSTATEMENT OF FUNDS

Debtor-in-possession Reorowicz Construction Company, Inc., by its attorney, Terrence J. Byrne, having filed a motion for reinstatement of funds in the hands of Citizens National Bank of Stevens Point; and a hearing having been held on said motion; and the movant appearing by its attorney; and Citizens National Bank of Stevens Point appearing by its attorney, Gary R. Akavickas of Terwilliger, Wakeen, Piehler, Conway & Klingberg, S.C.; and the Court having heard the arguments of counsel, considered the submitted briefs, and reviewed the record and file herein, FINDS:

1. That the Debtor-in-possession, Reorowicz Construction Company, Inc., filed for relief under Chapter 11 of the Bankruptcy Code on November 14, 1983.

2. That, on or about March 31, 1980, Citizens National Bank of Stevens Point (the Bank) loaned the Debtor $275,000.

3. That the proceeds of said loan were applied by the Debtor toward the purchase of the assets of another construction and excavating company.

4. That said loan was evidenced by a promissory note (the purchase note) guaranteed by the Small Business Administration and the Debtor's president, Henryk Reorowicz.

5. That the purchase note was secured by a General Business Security Agreement (GBSA) signed by the Debtor.

6. That, with the exception of the name of the Bank, the GBSA is a preprinted form which provides, in fine print, after the heading "1. Security Interest":

> The undersigned ("Debtor(s)") grants The Citizens National Bank of Stevens Point ("Bank") a security interest in [a laundry list of tangible and intangible property interests] and all proceeds and products of the foregoing. . . to secure all Debtor's debts, obligations and liabilities to Bank arising out of existing or future credit granted by Bank to Debtor. . .

7. That affidavits filed in regard to the motion at bar present differing versions of the parties' subjective understanding regarding the transaction set forth above; but that, for the sole purpose of ruling on the motion at bar, the Court will assume that

it was expressed and contemplated by the parties that the Debtor might require further operating capital to maintain the viability of its business. See Affidavit of Kenneth Schmidt paragraph 3 (Jan. 20, 1984).

8. That, on July 28, 1980, the Bank and the Debtor entered into the first of a series of loans for Debtor operating capital (the documents evidencing same are not before the Court).

9. That said series of loans culminated on August 10, 1981, when outstanding operating capital loans were consolidated and renewed as a $50,000 promissory note (the consolidated note).

10. That the consolidated note was drafted on a form which includes a section marked:

> FOR BANK CLERICAL USE ONLY
> COLLATERAL CODE

and that, immediately below this language is typed:

> Specific, personal guaranty of Henryk Reorowicz dated 8/10/81 in the amount of $50,000.00.

11. That, on October 9, 1981, the consolidated note was renewed (first renewal note).

12. That the first renewal note was drafted on the same form as the consolidated note (see Finding 10) and, immediately below

the pre-printed language set forth at Finding 10, provided:

(see over)

and, on the reverse, provided:

> Specific Personal Guarantee of Henryk K. Reorowicz dated August 10, 1981, in the amount of $50,000, machinery, equipment and accounts receivable.

13. That, on or about January 28, 1982, the first renewal note was renewed (the second renewal note).

14. That the collateral notation on the second renewal note is substantially similar to the first renewal note, <u>see</u> Finding 12, with the exception that the word "machinery" is absent.

15. That on December 2, 1982, the second renewal note was renewed(the note at bar).

16. That the collateral notation on the note at bar is substantially similar to the first renewal note, <u>see</u> Finding 12.

17. That affidavits filed in regard to this motion present differing versions of the parties' subjective understanding regarding the note at bar; but that, for the sole purpose of ruling on the motion at bar, the Court will assume that Kenneth Schmidt, Vice-President of the Bank, told Henryk Reorowicz, President of the Debtor, that the note at bar would be secured by the GBSA. <u>See</u> Affidavit of Kenneth Schmidt, <u>supra</u> Finding 7, at paragraph 4.

18. That, on October 6, 1983, with the Debtor in default of the note at bar, the Bank removed funds from the Debtor's general checking account at the Bank.

19. That the Debtor argued that the GBSA did not place the Bank in the position of a secured creditor in regard to the note at bar; and that, accordingly, the withdrawal of funds by the Bank was not authorized by 11 U.S.C. sec. 553 (1982).

20. That the Bank joined issue regarding its secured status under the GBSA.

21. That the Bank's secured status is a question of Wisconsin state law. See In re Taddeo, 9 B.R. 299, 305 (Bankr. E.D.N.Y. 1981), aff'd, 15 B.R. 273 (E.D.N.Y. 1981), aff'd., 685 F.2d 24 (2nd Cir. 1982).

22. That Wis. Stat. sec. 409.204 provides, in pertinent part:

> (3) Obligations covered by a security agreement may include future advances or other value whether or not the [secured party has bound itself to make future advances].

23. That, under sec. 409.204(3),

> [a] "floating lien" security agreement will be effective according to its own terms, but only if those terms or the course of dealing of the parties evidence that the real intent of the parties was that their subsequent transactions be covered by the terms of the security agreement.

John Miller Supply Co., Inc. v. Western State Bank, 55 Wis. 2d 385, 395, 199 N.W.2d 161, 165 (Sup. 1972) (interpreting former Wis. Stats. sec. 409.204(5), which has been recodified--with cosmetic changes--as Wis. Stats. sec. 409.204(3)).

24. That the first part of the John Miller test, whether the security agreement would, by its terms, relate to the future advance in question, is met. See Finding 6.

25. That the two-pronged, second part of the John Miller test, whether the terms of the security agreement or the parties' course of dealing evidences a real intent[1] that subsequent transactions be covered, is an objective[2] inquiry which protects debtors against overreaching creditors' habitual use of general future advance clauses. See B. Clark, The Law of Secured Transactions Under the Uniform Commercial Code 10-9 & 10-10 (1980)("The accounts and inventory lender's future advance clause is part and parcel of the floating lien. Both debtor and secured party expect it. If the language of the security agreement expressly covers the extension

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1 In re Zwicker, 8 U.C.C. Rep. Serv. 924, 1970-3 Bankr. L.Rep. (CCH) para. 64,072 (Bankr. W.D.Wis. 1971), is superseded to the extent that it permits a security agreement to cover future advances by the parties' "assent", id. 8 U.C.C. Rep. Serv. at 926.

2 In re Zwicker, supra note 1, and In re Glawe, 6 U.C.C. Rep. Serv. 876 (Bankr. E.D.Wis. 1969), are superseded to the extent that they permit inquiry into the subjective understanding of the parties.

of credit, the future advance should be upheld. . . Conversely, if one-shot financing of equipment or consumer goods is involved, the burden on the secured party to describe the advance in the security agreement should increase").

26. That neither the GBSA nor the purchase note and related guarantees evidence that subsequent transactions were contemplated or negotiated. Cf., eg., John Miller, supra Finding 23, 55 Wis.2d at 387, 199 N.W.2d at 161 (litigated instrument was a "General Revolving Loan and Security Agreement").

27. That, accordingly, the first prong of the second part of the John Miller test is not met.

28. That a "course of dealing is a sequence of previous conduct between the parties to a particular transaction which is fairly to be regarded as establishing a common basis of understanding for interpreting their expressions and other conduct." Wis. Stat. sec. 401.205(1).

29. That the Court is sympathetic to the argument that, in the commercial setting, both parties should consider and intend a series of loans beginning within months of the execution of a GBSA to be covered by that GBSA. However, when the GBSA is entered into during an isolated and distinct purchase transaction which

occurred almost a half a year before the first of a series of operating and related loans, there is no course of dealing which demonstrates a real intent between the parties that the GBSA apply to subsequent loans.

30. That, accordingly, the second prong of the second part of the John Miller test is not met.

CONCLUSIONS OF LAW

1. That the GBSA would be effective according to its own terms.

2. That neither the terms of the GBSA nor the course of dealing of the parties evidence that the real intent of the parties was that their subsequent transactions be covered by the terms of the GBSA.

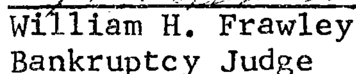
3. That the GBSA is ineffective in regard to the note at bar.

ORDER

IT IS ORDERED THAT the Citizens National Bank of Stevens Point reinstate $20,212.69 to the Debtor-in-possession, Reorowicz Construction Company, Inc.

Dated: March 1, 1984.

BY THE COURT:



William H. Frawley
Bankruptcy Judge