

**UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF ALASKA**

In re:

RUSSELL A. SHANGIN and PATRICIA
A. SHANGIN,

Debtors.

Case No. A97-00723-DMD
Chapter 7

**Filed On
10/2/07**

MEMORANDUM ON PROOF OF CLAIM NO. 18

Creditor ADF Inc. filed Proof of Claim No. 18 as a secured claim for \$115,839.07. ADF says its claim is secured by the debtor's "EXXON Valdez claim proceeds." The trustee has objected to Claim No. 18 on the grounds that, under the version of the Uniform Commercial Code in effect at the time the debtor's bankruptcy was filed, no security interest could be created in commercial tort claims. The trustee contends ADF's claim should therefore be treated as a general unsecured claim.

I have reviewed the trustee's objection and ADF's response. For the reasons stated below, I conclude that the trustee's objection should be overruled.

1. Procedural Sufficiency of Trustee's Objection

The trustee is attacking the validity of ADF's asserted lien. As noted in ADF's reply and by its counsel at the hearing, this is a matter which typically requires the filing of an adversary proceeding.¹ However, where the record in a contested matter is developed to essentially the same extent as it would have been in an adversary proceeding, this

¹ Fed. R. Bankr. P. 3007, 7001(2).

requirement can be circumvented.² The trustee's objection to ADF's claim raises a purely legal issue. This issue has been fully briefed by ADF's counsel, who advised the court at the hearing that he was ready to proceed on the merits. Under the circumstances, I feel the need for resolving this claim objection by way of a more formal adversary proceeding is unnecessary.³ The trustee's objection does not fail on procedural grounds.

2. Assignment of the Debtor's EVOS Proceeds

In August, 1995, debtor Russell Shangin and ADF entered into an agreement regarding Shangin's repayment of a \$130,000.00 obligation. As security for this debt, Shangin agreed to provide any documents necessary to assign to ADF his "right to receive proceeds of any judgment, award, or settlement entered against Exxon Shipping Company, Exxon Company, U.S.A. or any related entity."⁴ Contemporaneously with the agreement, Shangin executed an assignment which specified:

1. For valuable consideration, Assignor hereby assigns and transfers to ADF all of his right, title and interest in the first One Hundred Thirty Thousand Dollars (\$130,000) less any payments made pursuant to the "AGREEMENT" and "DELIVERY AGREEMENT" between Assignor and ADF, Inc. dated June 7, 1995, payable by Exxon Corporation, or any of its affiliates, ("Payor") under the terms of any

² *Ruvacalba v. Munoz (In re Munoz)*, 287 B.R. 546, 551 (B.A.P. 9th Cir. 2002).

³ *Trust Corp. of Montana v. Patterson (In re Copper King Inn, Inc.)*, 918 F.2d 1404, 1406-07 (9th Cir. 1990) (technical shortcomings, including lack of adversary proceeding, would be overlooked and court found no material prejudice to a creditor where claim objection was resolved after extensive hearing and briefing).

⁴ See Agreement, attached to Proof of Claim No. 18, filed Nov. 21, 1997, at p. 2.

judgment, ruling, determination, compromise or settlement, for losses, expenses and damages of any kind or nature, whether direct or consequential, arising out of the incident described as follows: Exxon Valdez oil spill, including, without limitation, all amounts received or receivable by Assignor pursuant to that certain litigation filed in U.S. District Court, District of Alaska, cause no. A90-095 Civil (consolidated) in re: The Exxon Valdez.

. . . .

3. Assignor hereby authorizes Payor to pay ADF, directly, the full amount of any amounts assigned hereby to which Assignor is or becomes entitled.⁵

Shangin executed two UCC-1 financing statements, one for Alaska and the other for Washington, covering his right, title and interest in the Exxon litigation. He also signed two notices of assignment of his Exxon claim, one directed to Keller Rohrback and the other to Exxon Corporation, advising that he had assigned to ADF his interest in the first \$130,000.00 which might be payable to him in the Exxon litigation. Keller Rohrback received notice of the assignment on June 21, 1996.⁶

The Shangins filed a chapter 11 petition on July 29, 1997. Their case was converted to chapter 13 on December 2, 1997, and subsequently converted to chapter 7 on July 6, 1998. The only significant asset in this bankruptcy estate is the debtors' interest in the Exxon litigation, which is, undisputedly, a commercial tort claim.

⁵ See Assignment, p. 1, attached to Proof of Claim No. 18.

⁶ See Letter to Mr. Davis from Exxon Qualified Settlement Fund, dated July 15, 2003, attached to Creditor's Resp. in Opp'n to Claim Obj. (Proof of Claim No. 18), filed Aug. 13, 2007 (Docket No. 214).

At the time Shangin executed the assignment to ADF, both the Alaska and Washington Uniform Commercial Codes (“UCC”) provided that the provisions of Article 9, governing security interests, did not apply to “a transfer in whole or in part of a claim arising out of tort.”⁷ The trustee argues that this exclusion prohibits the creation of a security interest in a tort claim. He relies on a recent Ninth Circuit decision, *Fifteenth RMA Partners, L.P. v. Pacific/West Communication Group, Inc. (In re Pacific/West Communication Group, Inc.)*,⁸ to support this contention. In that case, the issue was whether a creditor’s security interest in a debtor’s general intangibles and all proceeds thereof would attach to the proceeds of a commercial tort claim.⁹ The California Commercial Code in effect at the time the security interest was created contained the same tort claim exclusion as the Alaska and Washington UCCs.¹⁰ The court interpreted this to mean that the UCC prohibited an individual from granting a security interest in a pending tort claim.¹¹ The court further reasoned that, since tort claims could not be offered as collateral, neither could the proceeds of tort claims serve as collateral under Cal. Comm. Code § 9306.¹²

In reaching its decision, the Ninth Circuit examined several cases which held that a broad security interest in proceeds, claims or general intangibles would not attach the

⁷ AS 45.09.104(11) (The Michie Co. 1994); Wash. Rev. Code § 62A.9-104(k) (West 1995). This exclusion has since been amended to extend Article 9 coverage to security interests in commercial tort claims. See AS 45.29.109(d)(12) (West 2007); Wash. Rev. Code § 62A.9A-109(d)(12) (West 2007).

⁸ 301 F.3d 1150 (9th Cir. 2002).

⁹ *Id.* at 1151.

¹⁰ *Id.*, at 1152, *citing* Cal. Comm. Code § 9104(k) (1997).

¹¹ *Pacific/West*, 301 F.3d at 1152.

¹² *Id.* at 1154-55.

proceeds of a debtor's tort claim.¹³ *Pacific/West*, and the cases cited by the Ninth Circuit, are all distinguishable on their facts. ADF doesn't claim a broad security interest in Shangin's general intangibles or all of Shangin's claims and causes of action. Rather, ADF has been assigned a specific interest in Shangin's Exxon claim. The UCC in effect at the time ADF's assignment was created may have excluded this transaction from Article 9,¹⁴ but it did not prohibit the transaction altogether.

The UCC provides that the common law applies where the UCC's provisions do not.¹⁵ Even before the UCC was amended to extend Article 9 security interests to commercial tort claims, there was a "substantial body of state law permitting the consensual assignment of many types of tort causes of action," including for security purposes.¹⁶ Commercial tort claims could be assigned under both Alaska and Washington common law at the time Shangin executed the ADF assignments.¹⁷ There is no special format required to

¹³ See *Israel Disc. Bank., Ltd. v. Gottesman (In re Ore Cargo, Inc.)*, 544 F.2d 80 (2d. Cir. 1976) (standard security agreement which granted interest in a debtor's "credits, claims, demands and any other property" did not create security interest in a commercial tort claim that creditor didn't know existed); *Corcoran v. Land O'Lakes, Inc.*, 39 F.Supp.2d 1139 (N.D. Iowa 1999) (security interest in general intangibles didn't encumber tort claim or its proceeds because of exclusion of such claims from UCC coverage); *Ins. Co. of N. Am. v. Della Indus., Inc.*, 998 F.Supp.159 (D. Conn. 1998) (same); *Barclay's Bus. Credit, Inc. v. Four Winds Plaza P'ship*, 938 F.Supp. 304 (D.V.I. 1996) (security interest in general intangibles doesn't cover tort claim or proceeds from settlement of such claim, because tort claims are excluded from UCC's coverage).

¹⁴ Tort claims were excluded from Article 9 because, at the time the UCC was initially drafted, they were considered to be "noncommercial assets inappropriate for inclusion as collateral within the scope of a commercial financing statute." Harold R. Weinberg, *They Came From "Beyond the Pale": Security Interests in Tort Claims*, 83 Ky. L.J. 443, 444 (1995). Mr. Weinberg served as a Special Advisor to the Permanent Editorial Board Study Group on Article Nine of the Uniform Commercial Code. *Id.* at 483 [FN a].

¹⁵ *State v. McKinnon*, 667 P.2d 1239, 1243 (Alaska 1983), citing AS 45.01.103 (1983).

¹⁶ Harold R. Weinberg, *Tort Claims as Collateral: Impact on Consumer Finance*, 49 Consumer Fin. L.Q. Rep. 155, 157 (1995).

¹⁷ *Andersen v. Edwards*, 625 P.2d 282, 290 (Alaska 1981); *Cooper v. Runnels*, 291 P.2d 657, 658 (Wash. 1955).

make such an assignment, so long as the intent of the parties is clear.¹⁸ Shangin's assignment to ADF is very specific. Further, ADF gave notice of the assignment to Exxon and the EQSF administrator, and recorded UCC-1 notices of the assignment as well.¹⁹

I conclude that ADF has a valid and enforceable assignment of the first \$130,000.00 from Shangin's Exxon litigation claim. The trustee's objection to ADF's claim will therefore be overruled. An order will be entered consistent with this memorandum.

DATED: October 1, 2007

BY THE COURT

/s/ Donald MacDonald IV
DONALD MacDONALD IV
United States Bankruptcy Judge

Serve: G. Spraker, Esq. (for trustee)
J. Davis, Esq. (for Tim Shaffer)
U. S. Trustee

10/02/07

¹⁸ *Andersen*, 625 P.2d at 290.

¹⁹ *See, e.g., Fugate v. Carter County Bank (In re Webb)*, 187 B.R. 221, 228 (Bankr. E.D. Tenn. 1995) (assignment of tort claim was excluded from UCC, so there was no requirement to record the assignment, but notice of the assignment must be given to the obligor to be effective against a bankruptcy trustee).