

# Deposit Accounts as Original Collateral in Commercial Transactions

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Revised Article 9, which became effective July 1, 2001, makes it easier to take a security interest in deposit accounts in commercial transactions. As opposed to old Article 9, a lender may obtain a perfected security interest in a deposit account in a commercial (not consumer) transaction, even if the depositor is entitled to withdraw funds from the account, and the perfected security interest will defeat a competing secured creditor who claims the funds in the account as proceeds of other collateral.

The Old Rules. Deposit accounts were excluded from the scope of old Article 9. There was no clear statutory direction, and secured creditors looked to common law (case law) for how to perfect a lien on deposit accounts. Generally, the account had to be frozen; the depositor could not have access to it. If the deposit account was not held by the lender, the lender entered into a "bailee" agreement with the depository bank, which essentially made the depository bank hold the account for the lender. Under the old rules, a lender probably could not perfect a lien in a deposit account from which the depositor could withdraw funds.

The New Rules. New Article 9 changes the treatment of deposit accounts. There are now clear rules for a lender to take and perfect a security interest in deposit accounts in commercial transactions, even if the depositor has access to withdraw funds. Generally, the rules are as follows:

1. The lender should take a security agreement which includes "deposit accounts" as collateral. A deposit account is defined as a demand, time, savings, passbook or similar account maintained with a bank. A "bank" means an organization that is engaged in the business of banking; it includes savings banks, savings and loan associations, credit unions and trust companies.
2. The lender should perfect the security interest by obtaining "control." "Control" is a matter of definition and is accomplished by a lender in one of three ways:
  - a) By having the account held in the lender's name at the depository bank;
  - b) By the lender being the depository bank; or
  - c) By the lender obtaining a "Control Agreement" with the depository bank.
3. **Filing a financing statement does not accomplish perfection as to deposit accounts.**

Control Agreements. A "Control Agreement" is an agreement between the depository bank, the secured lender and the depositor (all three must sign it) that obligates the depository bank to send the funds to the secured lender when the secured lender asks for them, without the need for the depositor's further consent. There is a new Wisconsin Banker's Association/FIPCO form for this - the WBA 421 DACA ("Depository Account Control Agreement").

Priority. A secured lender who is perfected by having control of a commercial deposit account has priority over a conflicting security interest that is not perfected by control. Therefore, the secured lender who has control defeats the lender who claims a security interest only by virtue of the funds being proceeds of other collateral. If there are competing creditors who are perfected by control: (i) the lender who has the account in its name (2(a) above) has the first priority; (ii) the depository bank (2(b) above) has next priority; and (iii) the lender with a Control Agreement (2(c) above) takes third priority. Because the depository lender has a better priority than a lender with a Control Agreement, the lender who obtains perfection by a Control Agreement should also obtain a subordination agreement from the depository bank. (If using the WBA/FIPCO form, make sure the box in section 4 is checked to obtain that subordination.)

Default. Upon the occurrence of a default (or if agreed to, at an earlier time), the lender who holds the deposit account may apply the balance in the deposit account to the secured obligation. The lender who has perfected by one of the other methods of control may instruct the depository bank to pay the balance in the account to it.

Caveats. These rules do not apply to deposit accounts evidenced by negotiable instruments, which by definition are not deposit accounts. These rules also do not apply to consumer transactions; the scope provisions of new Article 9 continue to exclude deposit accounts in consumer transactions.

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