Applying Old Article 9 law, the court in *Van Diest Supply Co. v. Shelby County State Bank* (2005 WL 2417066, 7th Cir. 2005) held that a purchase money secured creditor had to identify the proceeds from the sale of its products to prevail over a secured party who factored the accounts of the debtor.

Van Diest was one of a number of creditors that sold the same product to Hennings Feed and Crop Care. In 1983, to secure payment, Van Diest perfected a purchase money security interest. Hennings did not segregate its inventory by supplier or track inventory by supplier. As a result, Hennings had no idea how much inventory it had on hand on any given day from a particular vendor.

In May 1998, Shelby County provided a $4 million line of credit to Hennings secured by a security interest in Hennings’ accounts receivable. Shelby County collected the receivables, and from May 1986 to as late as January 1999 it purchased Hennings’ receivables.

Hennings defaulted on a payment due Van Diest in June 1999. In August 1999, Hennings filed a voluntary petition in bankruptcy. At that point, Van Diest demanded that Shelby County turn over funds that Shelby County had collected from payments made by Hennings’ account debtors. When Shelby County refused, Van Diest sued for conversion. At issue were payments made by Hennings’ customers directly to Shelby.

The court first established that Van Diest could prevail only if the proceeds from the sale of the inventory Van Diest supplied to Hennings were identifiable. At the same time, the court noted that the UCC did not define “identifiable.”

In holding for Shelby County, the court concluded that Van Diest had not borne its burden of proof—identifying the proceeds from the sale of the inventory it supplied. The court noted that Van Diest had admitted it could not specify the amount of its pro rata share of Hennings’ commingled inventory.

Van Diest’s efforts to use the pro rata method failed because it could not, on any given day, establish the proportion of Hennings’ inventory attributable to inventory it sold to Hennings. Had it been able to do so, it could then have presented evidence of increases or decreases in Hennings’ inventory over time as Hennings purchased more inventory from its suppliers and sold inventory to customers. The ruling in favor of Shelby thus stemmed from the court’s observation that, on any given day in 1998 and 1999, Hennings did not know how much inventory it had in its warehouse from any supplier.

**What’s the point?** Section 9-315 of Revised Article 9 continues the requirement that proceeds be identifiable in order to be claimed by a secured party when they have been commingled. And it expressly recognizes that equitable principles that permit various methods of proof (including the lowest intermediate balance test) may be applied in establishing the identity of proceeds.

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