**Secured Transactions: After-Acquired Property and Future Advances**

Welcome to this podcast on After-Acquired Property and Future Advances brought to you by CALI. I am Professor Jennifer S. Martin. The topic of this podcast is the use of after-acquired property clauses and future advances given by secured creditors. This topic primarily requires a careful reading of UCC § 9-204 and a basic understanding of how a secured party attaches its security interest in the first place.

Recall that § 9-203 lists three formalities for creating a security interest enforceable against the debtor: first, value given by the creditor; second, the debtor having rights in the collateral; and third, an authenticated security agreement or other validating device such as possession of the collateral. We might imagine that the creation of the security interest attaches a sort of invisible string between the debtor’s obligation to pay the creditor and the collateral. But issues can arise with respect to exactly what the collateral is and what obligations are covered. What collateral is the string attached to? And, what obligations are on the other end of the string?

Some of these issues involve after acquired property clauses and future advances. Let’s look at after acquired property clauses first. You might think of after acquired property as the creditor taking a type of continuing or floating lien on the specified collateral of the debtor as stated in the security agreement. Recall that Article 9 defines a security agreement simply as any agreement that creates or provides for a security interest. In order to know what collateral is covered by the security agreement we would have to know what it says. Typically this will be a simple matter of reading the document and looking for identification of the collateral. Oftentimes, a secured creditor will identify the collateral in a general way such as by category (like computers) or the type of collateral under Article 9 (such as equipment). An example might be helpful here.

Suppose I want to buy a clarinet for my young son Marshall. Music City, the seller of the clarinet, might agree to sell me the clarinet on credit with me signing a security agreement granting Music City a security interest in the clarinet to secure payment of $50 per month over three years for the clarinet. We could read the security agreement to determine that the clarinet is the collateral. But what if, instead, the security agreement granted Music City a security interest in my musical instruments? I only own the clarinet for Marshall right now, but what if my other son Leeland comes home from school tomorrow and says he needs a violin for his class? If I purchase the violin, would it be subject to the security interest of Music City? Of course, it depends.

When we look at security agreements, ordinarily we consider the personal property at the time the debtor signs the security agreement. A big exception to this is that § 9-204 allows a security agreement to provide for a security interest in after-acquired property, but the agreement simply must so state. Basically when a security agreement includes an after-acquired property clause, the language is valid for the collateral the debtor owns at the time the value is given and property acquired in the future that is of the kind of collateral specified in the agreement.

So with respect to Music City, we would conclude that the collateral subject to the security agreement that described the collateral as “my musical instruments” would include the musical instruments that I own at the time the security agreement is signed. That would just be the clarinet. If Music City wants its security interest to extend to any musical instruments that I might buy in the future, § 9-204 tells us that’s possible.

Let’s suppose the security agreement instead provides that I grant Music City a security interest in musical instruments, now owned and hereafter acquired. Now, in accordance with § 9-204, Music City would have a security interest in the clarinet that I own today and a violin that I buy for Leeland later this week. As it turns out, though, after acquired property clauses are not always effective. Here, the violin and the clarinet are consumer goods because they are used for family or household purposes. Article 9 contains two important limitations on after-acquired property clauses. First, a security interest would not attach using an after acquired property clause for consumer goods, other than accessions given as additional security, unless the debtor acquires rights to the consumer goods within ten days after the secured party gives value. Second, an after-acquired property clause does not attach to commercial tort claims that are later acquired. In our case with Music City, the after-acquired property clause would only reach musical instruments that I purchase within ten days after Music City gave value. Here, I purchased the violin for Leeland in the first week, so it would be covered by the security interest. But, if I purchase a trumpet next month because one of the boys decides to take up that instrument, it would not be covered by the security interest of Music City because it was purchased more than ten days after it gave value.

One last note about after-acquired property. Notice that we really need to use an after-acquired property clause in a security agreement in order to make all this work. If a security agreement does not provide for after-acquired property then the creditor is limited to what the security interest initially attaches to. That is true with one big exception with respect to when a security agreement provides that the collateral is inventory. Most courts hold that inventory that is after-acquired is included in the security interest whether or not specifically stated in the security agreement. That said, creditors often use after-acquired property clauses even for inventory, even though it might not be required. Remember, secured creditors like to get this right and be clear in their agreements as to the collateral covered.

Let’s turn to future advances now. Future advances don’t work on the collateral side of the agreement but rather on the obligation side of the security interest. Section 9-204 also provides that a security agreement may provide that the collateral secures future advances as well as the value given at the time of the initial attachment. This is true whether or not the advances are given pursuant to a firm commitment. Basically, sometimes creditors have a debtor sign a security agreement that covers all obligations to the creditor that may come into existence at any point in time. That way, if a secured creditor later does lend additional money to the debtor, the future-advance clause will make sure that the collateral given is tied to the later advance as well. The Code gives the parties wide discretion in terms of using a future advance clause, whether or not the clause is part of a firm commitment to lend by the lender.

At this point, you should be able to identify and describe when a secured creditor would want to use an after-acquired property clause in a security agreement to enable the creditor to reach collateral acquired by a debtor in the future. You should also be able to identify when the limitations on the use of after-acquired property clauses arise. Finally, you should be able to describe the process by which a creditor might be able to have the security interest cover obligations that might come into existence in the future as a future advance.

I hope you’ve enjoyed this podcast on After-Acquired Property and Future Advances.

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