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Article 6: Bulk Transfers

By EDWARD L. KIMBALL*

About the turn of the century attention came to be focussed on the widespread practice of many hard-pressed or scheming merchants to dispose quietly of their whole stock of goods to a single buyer and disappear, or at least divest themselves of the proceeds to the detriment of their creditors.¹ Creditors then, as a group, undertook to push for the enactment of preventive legislation. Through "one of the most highly organized, and thoroughly efficient, nation-wide lobbying campaigns ever conducted in the interests of one economic group"² the National Association of Credit Men was successful over a period of about ten years in obtaining the enactment everywhere in the United States of some form of legislation regulating "bulk sales."³ At the outset a few of the statutes were declared unconstitutional as denials of equal protection and as arbitrary restrictions on the right to contract, but it soon became universally established that this sort of regulation of bulk sales is constitutional.⁴

In the majority of states the bulk sales law undertakes to protect creditors by putting the burden upon the purchaser of goods in bulk to see that the seller's creditors have sufficient notice of the impending sale to take appropriate steps under local law to prevent its consummation or to impound the proceeds if they think that necessary or desirable. In some states the law goes even further and imposes upon the buyer the duty also of seeing that the sale proceeds are actually applied to the seller's debts.

There can be no doubt that bulk transfer laws create delay and red tape, and set a trap for the unwary buyer, but the legislatures have in every case decided that these drawbacks are outweighed by the benefits of such statutes.

In the following pages the Montana bulk sales statute⁵ will be analyzed and the Uniform Commercial Code article on bulk transfers⁶ compared with it.

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¹Billig, *Bulk Sales Laws: A Study in Economic Adjustment*, 77 U. PA. L. REV. 72 (1928); GLENN, *FRAUDULENT CONVEYANCES AND PREFERENCES* § 309 (rev. ed. 1940). The related problem of sale by merchants to a friend at less than value, payment of this sum to creditors under a composition agreement in full satisfaction of claims, with the intent later to reenter the business through the back door (a practice referred to in the comment to section 6-101 of the UNIFORM COMMERCIAL CODE) is one which is covered by fraudulent conveyances acts, not by bulk transfer legislation.

²Billig, *supra* note 1, at 81.

³*Id.* at 72-74; 3 NEW YORK LAW REVISION COMMISSION, *STUDY OF THE UNIFORM COMMERCIAL CODE 1727* (1955) (hereinafter cited NYLRC, UCC STUDY).

⁴*E.g.*, the New York statute enacted in 1902 was held unconstitutional in 1905, but a similar statute was upheld in 1916. The Montana statute, enacted in 1907, was upheld in *Wheeler & Motter Merc. Co. v. Moon*, 49 Mont. 307, 314, 141 Pac. 665, 668 (1914), against constitutional attack.

⁵REVISED CODES OF MONTANA, 1947, §§ 18-201 to -205. (Hereinafter REVISED CODES OF MONTANA are cited R.C.M.)

⁶UNIFORM COMMERCIAL CODE §§ 6-101 to -111 (hereinafter cited UCC).

Transfers Covered

The Montana statute governs sales; it uses such terms as *sale in bulk*, *vendor*, and *every person who shall bargain for or purchase, in bulk, for cash or on credit*. There is no regulation of bulk mortgages.⁷ This is emphasized by the fact that where the statute originally referred to *sale or transfer* it was reframed to omit reference to transfers other than sales. The only kind of bulk sale which is specifically exempt from regulation is one made by "executors, administrators, receivers, or any public officer acting under judicial process."⁸

Article 6 of the Uniform Commercial Code is entitled *Bulk Transfers* and is broad enough to encompass all of the many kinds of transfers in addition to sales, subject, however, to a number of important exceptions.⁹ As in Montana, judicial sales are specifically excepted. Sales in the process of judicial or administrative proceedings for dissolution or reorganization of a corporation, where notice is given the creditors, are likewise specially exempted by the Code; such sales are not clearly excepted from the Montana statute but might very well be excluded by judicial construction of the act in light of its purposes. Transfers made to give security are exempted; this provision would serve to repeal the bulk mortgage statutes which some states have enacted, but Montana has no such statute. The Code exempts general assignments and transfers in settlement of a lien or other security interest; these transfers are likewise outside the Montana act. Sales of property which is exempt from execution under state law are excepted from regulation by article 6. There is no such specific exception in the Montana law, but most courts hold sales of exempt property to be outside the statute.¹⁰ On the other hand the proceeds of sales of exempt property are not themselves exempt, so exclusion of such sales does permit the seller to conceal his receipt of what may be substantial funds.

There are two more kinds of bulk transfers which the Code excepts from regulation by article 6. Adoption of these exceptions would substantially affect existing Montana law. The Code excepts transfers to a person with an established business in the state who gives public notice that he has obligated himself to pay the debts of the transferor in full and is still solvent after taking on that obligation. This is one of the key provisions of article 6 because it permits the transaction which qualifies to proceed without delay and with a minimum of red tape. The other exception is of transfers to a new business enterprise organized to take over and continue the business which gives public notice that it has assumed the transferor's debts, provided that the transferor receives as consideration only an interest in the new enterprise subordinate to the claims of creditors. In both cases these sales would be covered by the Montana bulk sales act, but the Code excludes them on the reasoning that the creditors are adequately protected

⁷The majority of courts have held bulk mortgages not included within a bulk sales statute unless specifically mentioned. 1 GLENN, *FRAUDULENT CONVEYANCES AND PREFERENCES* § 310 (rev. ed. 1940).

⁸R.C.M. 1947, § 18-205.

⁹The eight exceptions discussed below are subdivisions of UCC § 6-103.

¹⁰3 NYLRC, *UCC STUDY* 1744 (1955). This would accord with the usual view that exempt property is not susceptible of fraudulent alienation because there is no prejudice to creditors in its sale. 1 GLENN, *FRAUDULENT CONVEYANCES AND PREFERENCES* § 172 (rev. ed. 1940).

by the addition of another party responsible to pay their claims. These seem to be desirable changes in the law. There is, however, no specification what form the public notice should take.

Businesses Included

The Montana statute does not delineate the businesses to be included. The original statute defined a bulk sale in part as a sale "of goods, wares or merchandise," indicating its principal concern with merchandising businesses.¹¹ In *Farrat v. Adamson*¹² the Montana court held a sale of pool hall fixtures not covered by the bulk sales statute. The court did not base its decision on the ground that a pool hall is not the kind of business which the statute covers, but on the ground that the fixtures are not "goods, wares or merchandise" within the meaning of the statute. In 1931 when the statute was amended to relate to sales in bulk of merchandise or fixtures or personal property used in the vendor's business it was clearly broad enough to encompass any business enterprise.¹³

The Code regulates the bulk sales only of those businesses whose principal activity is the sale of merchandise from stock, including enterprises which manufacture what they sell.¹⁴ The accompanying comment justifies this limitation on the ground that only in merchandising businesses is it likely that unsecured credit was extended on the faith of a stock of merchandise. The limitation runs hand in hand with concern of the Code with bulk transfer of inventory as distinguished from fixtures and business personalty. Thus limiting the businesses included will tend to avoid the large amount of litigation there has been in the past about whether a business was covered, but may deprive deserving creditors of needed protection.

Property Included

As pointed out in the preceding section, the Montana statute which was originally concerned with sale of merchandise now concerns the sale of "goods, wares, merchandise or trade fixtures, or personal property of the vendor's business."¹⁵ The *Farrat* case should no longer be good law, because sale of fixtures separately is covered by the amended statute. Conceivably the term *personal property of the vendor's business* could include such items as investment securities or negotiable instruments or other things in action, but it probably would be held not to include them—the statute is directed at the sale of more tangible property.

The Code deals with bulk transfers of "materials, supplies, merchandise or other inventory."¹⁶ The transfer of equipment (which is defined in another article of the Code as "goods . . . used or bought for use primarily in business"¹⁷) may be a bulk transfer under the Code only if made in connection with a bulk transfer of inventory.¹⁸ In common usage *equipment* has a more limited meaning, but as defined in the Code, "roughly speaking,

¹¹Laws of Montana 1907, ch. 145, § 4, at 375.

¹²53 Mont. 172, 179, 163 Pac. 112, 114 (1917).

¹³R.C.M. 1947, § 18-204. The disjunctive seems to be precisely used there, even though the conjunctive is used in section 18-201.

¹⁴UCC § 6-102. 1 GLENN, FRAUDULENT CONVEYANCES AND PREFERENCES § 311 (rev. ed. 1940), is critical of statutes which are so limited.

¹⁵R.C.M. 1947, § 18-204.

¹⁶UCC § 6-102.

¹⁷UCC § 9-109(2).

¹⁸UCC § 6-102. It has been suggested that a sale of fixtures could probably be "in connection with" a bulk transfer of inventory even though to a different person.

it includes all tangible chattels, both real and personal, which are used in any of the included businesses except those specifically excepted."¹⁹ As the comment, too, points out, the Code is concerned only with transfers of goods, not things in action.

Quantitative and Qualitative Requirements

The original Montana statute designated as a bulk sale one of "an entire stock of goods. . . out of the usual or ordinary course of business."²⁰ In 1921 it took its present form, designating as a bulk sale a sale of "an entire stock of a particular character of goods, wares, merchandise or trade fixtures, or personal property of the vendor's business."²¹ There need therefore not be a sale of any particular proportion of the vendor's inventory or other property to constitute a bulk sale so long as there is a sale of all of a particular class. What constitutes a "particular character" of things has not been in issue in the cases.

Under the Code a bulk transfer is "any transfer in bulk and not in the ordinary course of the transferor's business of a major part of the. . . merchandise."²² The transfer of a "substantial part" of the equipment of a business is also a bulk transfer if made in connection with a bulk transfer of merchandise.²³ There is serious question whether *in bulk* has any special meaning in the definition. It could refer to sale in a mass without itemization,²⁴ but it has also been alleged to refer to a quantitative requirement and to apply to a situation where there are several successive sales within a limited time to determine whether the statute should affect them.²⁵ Perhaps it has no real meaning. The phrase *not in the ordinary course of the transferor's business* refers, in the majority view, to the transferor's personal method of doing business, not to trade custom.²⁶ The limitation *major part* means more than half; it is to be contrasted with the term *substantial*, used with reference to transfer of equipment.²⁷ In regard to the foregoing requirements the Code is substantially different from the Montana bulk sales act.

Creditors Benefited

The Montana law seems to permit only business creditors to take advantage of the statute, contrary to what is "consistently held, under all the statutes."²⁸ It relates in terms to "creditors of the vendor holding claims due or owing, or which shall become due or owing, for or on account of goods, wares, merchandise and trade fixtures, and personal property used in the business of the vendor purchased upon credit, and . . . for or on

¹⁹Miller, *The Effect of the Bulk Sales Article on Existing Commercial Practices*, 16 LAW & CONTEMP. PROB. 267, 272 (1951); accord, 3 NYLRC, UCC STUDY 1739 (1955). Though *fixtures* generally has a narrow technical meaning, the New York courts have construed it to include all such things as are customarily and necessarily employed in the merchandising operation; thus the broad meaning which the Code gives to *equipment* is not without precedent. 3 NYLRC, UCC STUDY 1739 (1955).

²⁰Laws of Montana 1907, ch. 145, § 4, at 375.

²¹R.C.M. 1947, § 18-204.

²²UCC § 6-102.

²³*Ibid.*

²⁴Feldstein v. Fusco, 205 App. Div. 806, 201 N.Y. Supp. 4 (1923), *rev'd on other grounds*, 238 N.Y. 58, 143 N.E. 790 (1924).

²⁵Miller, *Bulk Sales Laws: Meaning to be Attached to the Quantitative and Qualitative Requirements Phrases of the Statutes*, 1954 WASH. U.L.Q. 283, 298.

²⁶*Id.* at 312, 325.

²⁷HAWKLAND, SALES AND BULK SALES 166 (1958).

²⁸3 NYLRC, UCC STUDY 1730 (1955).

account of money borrowed by the vendor and used in the business.’²⁹ This is much more explicit than the original version, which referred in its major provision to “all the creditors of said vendor.”³⁰ Even then the Montana court said in dictum, “[I]t seems clear that it was intended only to protect creditors incident to the conduct of the business. . . . It is a matter of common knowledge that the main purpose of the law is to protect the wholesaler. . . . It applies to known existing obligations to creditors of the business. . . . it applies only to claims arising *ex contractu*.’³¹ Under the present law, since 1931, those statements should be true a fortiori. Obviously tort creditors would not be protected.³² Under the statute the creditors benefited will ordinarily have liquidated claims, but apparently they need not be either matured nor liquidated. Contingent claims would seem to be excluded by limitation to “claims due or owing, or which shall become due or owing.” It appears that a creditor who has acquired a business claim by assignment prior to the transfer should be able to take advantage of the statute.

Under the Code there is no other express limitation on the creditors who can take advantage of the statute than that their claims must be based upon events occurring before the bulk transfer (that is, before payment or possession by the transferee).³³ The claims may thus be unmatured and unliquidated, but it is uncertain whether they may be contingent.³⁴ It is likewise uncertain whether a post-transfer assignee of an otherwise in-cludible claim may benefit from the statute.³⁵

Duty of the Transferee

The vendee in a Montana bulk sale is now under a statutory duty to demand a sworn statement from the vendor which includes a list of the affected creditors, their addresses and the amount of their claims; a detailed inventory of the property to be sold; and the correct sale price.³⁶ The vendee must then give the listed creditors notice of the impending sale, describing the property generally and by location and by the name of the owner, either personally or by registered mail at least ten days prior to his making any payment or giving any note.³⁷ Finally the vendee must see that the purchase money is applied *pro rata*³⁸ to the claims of the creditors

²⁹R.C.M. 1947, § 18-201.

³⁰Laws of Montana 1907, ch. 145, § 1, at 373. However, in the same section the statute requires the vendor to state “that there are no creditors holding claims due, or which shall become due for or on account of goods, wares, or merchandise purchased upon credit or on account of money borrowed to carry on the business of which said goods are a part, other than as set forth.”

³¹Harrison v. Riddell, 64 Mont. 466, 477-78, 210 Pac. 460, 463 (1922). The court actually held only that an unliquidated chose in action arising in tort for negligence is not within the bulk sales act.

³²*Ibid.* This accords with the majority view under statutes referring to “all the creditors.” 3 NYLRC, UCC STUDY 1730 (1955); 1 GLENN, FRAUDULENT CONVEYANCES AND PREFERENCES §§ 314, 315 (rev. ed. 1940).

³³UCC § 6-109.

³⁴3 NYLRC, UCC STUDY 1753 (1955). *But see* Billig, *Article 6—Order Out of Chaos; A Bulk Transfers Article Emerges*, 1952 Wis. L. Rev. 312, 330: “It would appear to the present writer that tort claimants and holders of contingent claims are also within the meaning of the term ‘creditors of the transferor,’ as that term is used in the section.”

³⁵3 NYLRC, UCC STUDY 1754 (1955).

³⁶R.C.M. 1947, § 18-201.

³⁷*Ibid.*

³⁸The original statute required payment “share and share alike,” but in 1915 this was changed to “*pro rata*.”

listed by the vendor and of the creditors who were not listed but gave written notice of their claim.³⁹ Note that there is no requirement that the vendor's statement be retained or distributed or exhibited; that service, if not personal, must be by registered mail instead of by certified mail as permitted in some other statutes;⁴⁰ and that there is no time limitation upon payment to the creditors nor upon an unlisted creditor's making claim.

The Code is basically the same with regard to the transferee's duty, yet differs in many details. He must demand from the transferor a sworn list of all creditors, with their addresses and the amounts of their claims, if known, and also a list of persons asserting claims against him which the transferor disputes.⁴¹ Responsibility for correctness of this list is solely on the transferor. Responsibility is then on both parties to prepare a schedule of the property "sufficient to identify it."⁴² The transferee must give notice personally or by registered mail to all listed persons and also any other persons asserting claims whom the transferee knows ten days prior to his making payment or taking possession.⁴³ The notice may simply name the parties to the bulk transfer and give their addresses provided the transferee can also state that debts of the transferor will be paid in full as they fall due.⁴⁴ If the transferee is not sure the debts will be paid his notice must include much additional information—location and description of the property, transferor's total indebtedness, place where the inventory and list of creditors may be inspected, and other details if the transfer is to pay existing debts or is for new consideration.⁴⁵ It is not clear who must determine whether or not the debts of the transferor will be paid, so as to permit use of the short form notice.⁴⁶ Though the reference to the transferee's being in doubt about the debts being paid indicates that the transferee cannot rely wholly on the transferor's statement, how doubtful must he be? And how does one go about proving he was in doubt?

The Code includes as an optional provision the requirement that the transferee assure that the consideration be paid to the transferor's creditors—both those listed and those making written claim within thirty days of the mailing of notice.⁴⁷ This provision is similar to existing Montana law and would apply only where new consideration is given for the transfer (that is, the sale situation).⁴⁸ Finally the Code makes the additional requirement that the transferee either file the list and inventory in a designated public office or keep it in his own possession and open to creditors for a period of six months.⁴⁹ But there is no time designated within which the filing must be done.

³⁹R.C.M. 1947, § 18-202.

⁴⁰In 1959 the Montana legislature amended sections 23-1813 (transmittal of election returns), 93-1509 (summoning of jurors) and 84-710 (notification of changed property assessment) to permit use of less expensive certified mail instead of registered mail. The change seems a sensible one.

⁴¹UCC § 6-104.

⁴²*Ibid.*

⁴³UCC §§ 6-105, -107.

⁴⁴UCC § 6-107.

⁴⁵*Ibid.*

⁴⁶3 NYLRC, UCC STUDY 1751 (1955).

⁴⁷UCC § 6-106.

⁴⁸This sort of provision is now present in the statutes of several states, notably Pennsylvania. The majority of states, following New York, have not thought it desirable.

⁴⁹UCC § 6-104.

Consequence of Violation of Transferee's Duty

Under Montana law a bulk sale where the vendee has not complied with the statute is "fraudulent and void" as to the business creditors intended to be protected.⁵⁰ The vendee in such case is a trustee of the property and must deliver it up or account for its value to a demanding creditor.⁵¹ It is probably true, however, that the sale is not truly void (in the sense of being ineffective even between the parties) and that a bona fide purchaser from the vendee for value without notice of the vendee's non-compliance with the statute will, under general principles, take good title.

The Code specifies that noncompliance will render the transfer "ineffective against any creditor of the transferor."⁵² It is said to be implicit in the Code that to this could be added: "whose debt is not paid as matured."⁵³ Likewise a failure to notify some of the creditors can be cured by paying them off.⁵⁴ The non-complying transferee will in all probability be considered a receiver of the property and may also be personally liable to creditors.⁵⁵ There is specific provision that the bona fide purchaser for value and without notice from the transferee takes good title.⁵⁶

Sales at Auction

Auction sales present peculiar difficulty. In all probability the Montana bulk sales law does not cover the sale by auction; it is simply not geared to that problem.⁵⁷ The Code, however, has stopped this loophole by making the auctioneer who is aware that he is conducting a bulk sale assume the responsibilities which in ordinary bulk transfers are imposed on the transferee.⁵⁸ If the auctioneer knows the auction is disposing of a major part of the seller's inventory and fails to give the proper notice to creditors or fails to see that the proceeds are applied to their claims (where this optional provision is adopted), he is personally liable to the creditors as a class up to the amount of the net proceeds of the auction.

Penalty for Perjury

The Montana bulk sales statute makes falsification by the vendor in the statement which he is required to give to the vendee an offense punishable by imprisonment of one to five years or by a fine not exceeding

⁵⁰R.C.M. 1947, § 18-202.

⁵¹Wheeler & Motter Merc. Co. v. Moon, 49 Mont. 307, 317, 141 Pac. 665 (1914).

⁵²UCC § 6-104.

⁵³HAWKLAND, SALES AND BULK SALES 173 (1958).

⁵⁴*Ibid.*

⁵⁵3 NYLRC, UCC STUDY 1744-46 (1955).

⁵⁶UCC § 6-110.

⁵⁷States in a similar position with respect to auction sales, New York for example, have held bulk sales laws inapplicable to auctions. 3 NYLRC, UCC STUDY 1731, 1751 (1955). By a 1955 enactment it was made unlawful in Montana to sell new merchandise at public auction without license (R.C.M. 1947, § 66-222), unless it is a sale by an individual who maintains an established retail sales outlet and an inventory of goods in the county (R.C.M. 1947, § 66-229). This would seem to require a license for one who wished to sell all his merchandise at auction, but not for one who wished to sell only a major part of inventory or who wished to sell his equipment or other personalty used in the business. Application for a license must be filed with the county treasurer ten days before the auction (R.C.M. 1947, § 66-223), giving constructive notice to creditors. The defects in this statute as protection for creditors are not only that notice is merely constructive but that the threat of punishment for a misdemeanor against the seller is likely insufficient deterrent to a debtor who wants to sell and abscond.

⁵⁸UCC § 6-108.

\$1000.⁵⁰ The Code specifies no penalty for falsification in the sworn statement. Such falsification is perjury, so under the general Montana law it would be punishable by imprisonment for one to fourteen years.⁵⁰

Statute of Limitation

It is uncertain what time limitation is applicable to actions relying on the "fraudulent and void" character of a non-complying transfer under the Montana bulk sales act.⁶¹ The Code, however, has specified that no action under its bulk transfer article (as, for example, an action against an auctioneer on his personal liability) may be brought nor any levy be made on the property more than six months from the time the transferee takes possession, or more than six months from discovery of the transfer if it has been concealed.⁶²

Conflict of Laws Rule

In several cases the Montana court has evidenced an awareness of its power to control transactions involving chattels within the state and a readiness to do so.⁶³ The Code makes all bulk transfers of goods located within the state subject to the state's internal law (i.e., article 6).⁶⁴ It would appear that implicit in this provision is recognition of a policy that the law of the situs of goods involved in bulk transfer should be controlling, but some doubt is cast on this by section 1-105 of the Code, and particularly the accompanying comment, which suggests the propriety of the broadest possible application of the Code because of its superior merit and in furtherance of a policy of uniformity, even though this may mean rejection of the law of the situs.

Conclusion

The Uniform Commercial Code does not make any basically new approach to bulk sales problems. It is much more detailed than the Montana law and thus avoids some of the vagueness of that law, but its greater particularity opens new areas of uncertainty. The avenues by which a simple, above-board transaction can be completed with a minimum of red tape are welcome. The provision for the auction situation is a wise addition. In all, the Code bulk transfers article is in many, but not all respects superior to the existing Montana law.

⁵⁰R.C.M. 1947, § 18-203.

⁶⁰R.C.M. 1947, § 94-3811.

⁶¹UCC § 6-111. In addition to uncertainty which limitation applies there is the problem of different limitations for different remedies as illustrated in the fraudulent conveyances field in *Lind v. Johnson Co.*, 204 Minn. 30, 282 N.W. 661 (1938), and *Brasie v. Minneapolis Brewing Co.*, 87 Minn. 456, 92 N.W. 340 (1902).

⁶²In *Wheeler & Motter Merc. Co. v. Moon*, 49 Mont. 307, 141 Pac. 665 (1914), after judgment was secured and execution issued thereon was returned unsatisfied "an *alias* execution was issued and served upon L. T. Moon [the vendee] as garnishee." In *Ferrat v. Adamson*, 53 Mont. 172, 163 Pac. 112 (1917), after judgment was secured execution issued thereon was used by the constable to levy on the goods in the hands of the vendee. In *Harrison v. Riddell*, 64 Mont. 466, 210 Pac. 460 (1922), after judgment was secured and execution issued thereon was returned unsatisfied "this action was instituted in equity, in the nature of a creditor's bill, to subject the property of the defendant corporation [vendee] to payment of the plaintiff's judgment." These are remedies suggested by the Montana cases. See 3 NYLRC, UCC STUDY 1745 (1955), for mention of other possible procedures.

⁶³*Mieyr v. Federal Surety Co.*, 97 Mont. 503, 34 P.2d 982 (1934); cf. *In re Perry's Estate*, 121 Mont. 280, 192 P.2d 532 (1948).

⁶⁴UCC § 6-102.