The 2010 Amendments to Article 9 of the Uniform Commercial Code: What Does It All Mean?

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On July 1, 2013, the 2010 amendments to Article 9 of the Uniform Commercial Code (UCC) went into effect in Ohio. As of October 7, 2013, the amendments (in some form) are effective in all but six states, and all but three states (Arizona, Oklahoma and Vermont) have enacted some version of the amendments.

For the most part these amendments are an effort to address certain concerns that have arisen over the decade of practice under the much more substantive 2001 amendments. However, there are certain changes that every banker should be aware of to ensure and maintain perfection of a bank's security interest in personal property collateral.

What's in a Name?

1. The Driver's License Rule

The driver's license rule is one of the two more noteworthy changes to Article 9. It addresses how (by what name) an individual debtor is identified on a financing statement. When the Uniform Law Commission released the proposed changes in 2010, they provided two alternatives for states to consider. The majority of states, including Ohio, opted for Alternative A (the "only if" approach), which utilizes the name of the debtor as indicated on his/her state issued, unexpired driver's license or identification card. "The individual name of the debtor or the surname and first personal name" were left as a secondary option, but only if an individual has no driver's license or state issued identification card. See UCC §9-503. The Official Comments to Article 9 state specifically that the article does not determine the "individual name," nor which elements of a debtor's name make up the surname. It provides no guidance, for example, when a last name is hyphenated. Under Alternative A, where an individual has more than one unexpired driver's license, the most recent license should be used.

Alternative B is known as the "safe harbor" approach. It allows a secured party to use any of the three alternatives described in Alternative A, without favoring or insisting on the use of any one exclusively. This means a secured party filing in an Alternative B state can file a financing statement using the individual's driver's license or identification card, his/her "individual name," or his/her "surname and first personal name." At the time this article was written, only eight states had enacted Alternative B (Alaska, Colorado, Connecticut, Delaware, New Hampshire, Oregon, Washington and Wyoming).

If a current financing statement is made "seriously misleading" by applying the new identification rules (for instance the name used is not the name on the debtor's driver's license in an Alternative A state), you don't need to correct the filing until such time as the financing statement would have become ineffective had the amendments not taken effect. *UCC §9-801, Official Comment*.

To summarize – if a financing statement was filed using the incorrect individual debtor name in 2012, prior to the effective date of the 2010 amendments, that filing remains effective until 2017 without any amendment. However, any continuation filed would require that the debtor's name be amended in order to maintain effectiveness.

2. 'Public Organic Record'

The 2010 amendments also provide guidance on a registered organization's name for purposes of filing a financing statement. The amendments use a new term, "public organic record," to describe which name is correct. "Public organic record" is defined to include records available to the public for inspection. This consists of either the record initially filed with or issued by the state or federal government to form or organize an organization, and any record filed which amends or restates the initial record, or any state or federal legislation that does the same. Secured parties are required to use "the public record most recently filed with or issued or enacted by the registered organization's jurisdiction that purports to state, amend or restate the registered organization's name." UCC §9-503(a)(1). Generally, this information can be found in the incorporation/organizational documents maintained by the secretary of state in the jurisdictional state.

3. Trusts

When a trust is a registered organization (ex. business trusts in Massachusetts), the rule for registered entities (described above) applies. However, the majority of trusts are unregistered and/or testamentary and do not maintain a public organic record. A new Official Comment to UCC §9-503 (comment 2b) explains that if a trust's organic record (undefined term) specifies the name of the trust, the name of the trust should be used as the debtor's name. If the organic record does not specify a name, the name required for the financing statement is the settlor, or in the case of a testamentary trust, the testator. If the settlor's or testator's name is used, the financing statement must also include: (a) express notice that the collateral is being held in a trust and (b) some description of the trust at issue in order to distinguish it from other trusts which might be administered by the settler or testator. If "organic record" can be read to mean a document organizing a trust, even though not filed of public record, a trust indenture can be used to determine the name of a trust.

Change in the Jurisdiction of the Debtor

The other more substantive change in the amendments involves maintaining perfection when a debtor changes jurisdictions. Imagine the following scenario: In July 2013, a company located in State A enters into a loan agreement with a bank. In exchange for a loan, the company grants the bank a security interest in all of the company's personal property and assets and the products and proceeds thereof.[1] The bank files a financing statement to protect and perfect its interests. In November 2013, the company reincorporates in State B, a neighboring state. The company does not move its physical location or the collateral from State A, but it is now incorporated in State B. Prior to the 2010 amendments, when the company reincorporated in State B, the bank's financing statement in State A would have immediately lost perfection in all after-acquired collateral obtained after the move. The failure to simultaneously file (at the time of reincorporation) a financing statement in State B would have limited the bank's perfected security interest to collateral owned by the company up to the point of reincorporation, but nothing acquired thereafter.

The amendments provide a grace period (the lesser of four months or the time prior to a financing statement's expiration date) for the bank to discover that the company has reincorporated and file a new financing statement in State B. If a financing statement is properly filed in State B, within the grace period, the bank maintains its perfection on both the presently owned and after-acquired collateral of the company. However, if a financing statement is not filed within the grace period, the bank's security interest becomes unperfected and is deemed "never to have been perfected as against a purchaser of the collateral for value." UCC §9-316(h).

A similar grace period is also now applicable to after-acquired collateral in a merger scenario. If a corporate debtor incorporated in State A merges into another entity (the "survivor") incorporated in State B, the bank's original financing statement in State A will protect the bank's security interest in the survivor's property, including after-acquired collateral, for the same grace period described above, if a bank files a new financing statement in State B with the survivor as the debtor within the grace period. As with "reincorporation," if a financing statement is not filed in State B before the end of the grace period, the bank's original security interest will become unperfected and be deemed never to have been perfected as against a purchaser for value.

Other Changes

1. The Process

Along with the amendments, the original filing form (UCC-1) and amendment form (UCC-3) have been updated. The new forms no longer include space to provide the type or jurisdiction of the organization or the organizational identification number. This information is no longer considered useful in practice and adds cost and delay to the filing process. The Ohio Secretary of State's Office no longer accepts any financing statement/amendment filings using the old forms.

2. Information Statements

The term "correction statement" in Article 9 has been changed to the more accurate "information statement." UCC §9-518. Information statements can now be filed by debtors and/or secured parties when either believes that a financing statement or amendment was incorrectly filed or is inaccurate. Filing an

information statement does not correct errors. Before the amendment, only debtors could file correction statements. Secured creditors advocated to enlarge this concept so that if a third party erroneously modified a secured creditor's filings, the secured creditor had a way to address such issues (ex. a third party attempting to modify its own financing statement enters the incorrect file number and instead changes the secured creditor's number). Information statements are not required and secured creditors will not be penalized for not filing them, even if a secured creditor is aware of the inaccuracy in the record.

Practice Points

What does all of this mean to you as a secured creditor hoping to obtain or maintain perfection of your security interests in borrower collateral? Here are a few suggestions for ways to best protect your collateral interests in light of the above changes.

1. Ask for information early and often. Whether beginning a borrowing relationship or restructuring a troubled loan, ask your borrower for all of the information that you will need. If working with an individual debtor, request a copy of their most current, unexpired driver's license. If your borrower is a registered entity, ask for the public organic record. With a trust, ask for the trust indenture and any other writing indicating the name and location of your debtor. Also, if while entering into a new lending relationship you discover that a registered organization has been incorporated/organized in a particular state for less than four months, ask about its previous location. This will allow you to confirm that no other creditors hold a lien on your collateral – in the current or previous jurisdiction.

2. Require borrowers to provide periodic updates of necessary information. In addition to requiring periodic financial reporting as a condition in your loan documentation, consider requiring updated name and location information at the same time. More than once we've seen scenarios where the bank requests information at the beginning of a relationship but that information is never updated. The borrower merges into another entity and any safe harbor protections are long gone before the bank is aware. This is especially important as/when continuation statements are filed for older financing statements.

3. If there is a question concerning the proper name, file financing statements for both. This scenario is most likely to arise where either: (a) an individual goes by a name that is not his given name (Ex. "Drew" short for "Andrew." His current driver's license says Drew but it will be renewed in six months. You know his given name is Andrew.). Or, (b) you are unsure of the name of a trust. In the first example, we suggest filing both ways – in the name of Andrew and Drew. In the second scenario, filing under the name of the trust and the name of the settler/testator is the best way to protect your interests. Just remember that, if filing in the name of the settlor or testator, there must be some indication on the financing statement that the collateral is being held in a trust and also some information differentiating the debtor trust from other trusts that might have the same settlor/testator (ex. the date the trust was formed).

4. If you have questions – ask them. It is so much easier to confirm at the outset that your collateral interest is perfected, than it is to try and pick up the pieces when you discover it isn't and there isn't sufficient collateral to go around. Talk to your internal legal department or give us a call. We are happy to assist in any way we can.

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[1] Though sufficient to perfect a blanket interest in Debtor's personal property in a financing statement, it is not sufficient to describe collateral in a security agreement as "all personal property and assets of the Debtor and all products and proceeds thereof." Instead, we recommend use of collateral terms and definitions used in the UCC. See UCC §9-108; UCC § 9-504.