

Survey of 2008 UCC Article 9 Legislation

When Revised Article 9 took effect in 2001 it largely accomplished the drafters' goal of creating more uniformity in secured transactions. The project's joint sponsors, the National Conference of Commissioners on Uniform State Laws (NCCUSL) and the American Law Institute (ALI), achieved great success at getting the new law enacted in all fifty states without significant non-uniform variations.

Nevertheless, Revised Article 9 was not perfect. It contained some drafting ambiguities that continue to plague the UCC search and filing process. One issue in particular, the lack of standards for sufficiency of an individual debtor name, continues to be a matter of concern for secured parties. Practical experience has also exposed problems the drafters could not anticipate during the revision process, such as the large volume of bogus lien filings or the increase of privacy and identity theft concerns. Article 9 restricts the ability of filing offices to deal with those issues. Many filing officers want authority to reject clearly bogus UCC filings or records submitted with social security numbers.

Some states have now started legislative initiatives to address these issues. Texas led the way in 2007 when the legislature passed non-uniform amendments to the debtor name

provisions in § 9-503(a). Several more states introduced non-uniform Article 9 legislation in 2008. This article reports on some of the more significant 2008 legislative developments and explains the impact these initiatives have on best practices for UCC search and filing.

RECENT LEGISLATION

Tennessee

Tennessee Senate Bill 3732 contains amendments to the debtor name sufficiency provisions of § 47-9-503(a). The Tennessee Governor signed SB 3732 on March 26th and it takes effect on May 1, 2008.

The bill appears largely based on the 2007 Texas legislation that addressed ambiguities surrounding the sufficiency of registered organization and individual debtor names. Under UCC § 9-503(a), a registered organization name is sufficient only if the financing statement provides the name of the debtor indicated on the public record that shows the debtor to have been organized. However, the UCC does not define "public record."

Last year, Texas amended its version of § 9-503(a) to clarify that the source of a registered organization name is the *formation documents filed of public record*. Tennessee adopted the

Texas language verbatim. As purely a clarification of § 9-503(a)(1), SB 3732 has no impact on registered organization name due diligence best practices. The prudent filer should already be using the name on the articles or equivalent formation documents as the source of a registered organization name.

The same cannot be said about the new standard created by SB 3732 for sufficiency of individual debtor names. The 2007 Texas legislation carved out a safe harbor for individual names if the financing statement provides the name on the driver's license or state-issued identification certificate. Tennessee used the Texas law as a starting point, but took the safe harbor concept much farther. Instead of specifying a single safe harbor document, SB 3732 establishes multiple options for a sufficient individual debtor name. The financing statement sufficiently provides the name of an individual debtor only if it provides the name shown on any of the several safe harbor documents specified in the statute. These documents include the driver's license, state-issued identification card, birth certificate, passport, social security card or military identification card.

While SB 3732 makes it far easier for filers to provide the correct debtor name, it comes at the cost of added risk for UCC searchers. This bill will have a substantial impact on due diligence practices. Prospective lenders must now ask the debtor for each of the safe harbor documents and then conduct a UCC search on every name variation disclosed.

Nebraska

Nebraska also amended Article 9 to provide more certainty for secured parties that file UCC records against individual debtors. However, Legislative Bill 851 does not create a safe harbor. Instead, the bill amends UCC § 9-506(c) so that a financing statement is sufficient in the case of a debtor who is an individual if a search on the debtor's correct last name would disclose the record. The effect of this bill is that first and middle names no longer have any impact on the sufficiency of a financing statement.

As with the Tennessee legislation, LB 851 shifts risk from the UCC filer to subsequent searchers. The bill has a substantial impact on due diligence practices for searchers. Any financing statement that matches the last name of the debtor is potentially effective and must be reviewed as part of a diligent search. In some cases a prudent lender will need to review a large number of records. For example, a UCC search of the individual last name "Johnson" on the Nebraska Secretary of State's web site produces 2671 unique active records. Each must be reviewed as part of a diligent search on a debtor with the same last name.

The Nebraska Governor signed the bill on March 14, 2008. The law was scheduled to take effect in mid-July 2008, but the legislature passed a temporary repeal of LB851 on the last day of the legislative session. The governor signed the repeal on April 21, 2008. Unless

fully repealed next year, LB851 will take effect on September 2, 2009.

The reason for delaying the effective date was to give NCCUSL time to create a uniform legislative solution. The Nebraska legislature could repeal or further delay LB851 if it is satisfied with NCCUSL's progress.

While the effective date of LB851 is delayed, searchers should still consider following the best practices described above. An individual debtor name with errors or omissions may make the financing statement seriously misleading under current law, but it could suddenly become sufficient when LB851 takes effect. It is not clear whether the new law will have any retroactive effect. The courts will ultimately make that decision. To avoid the risk of unpleasant priority surprises down the road, searchers should review all financing statements with a matching last name.

Colorado

In 2008, Colorado enacted HB08-1266. This bill includes a number of amendments to Article 9. Some consist of minor changes to correct some non-uniform text. It also removes a statutory provision that requires the Secretary of State to accept UCC records submitted on paper. At some point after the bill takes effect, the Secretary of State intends to mandate electronic filing of all UCC records. That won't happen for at least two years, because the filing office must first make a major upgrade to its UCC

indexing and retrieval system. The bill also clarifies that the debtor, secured party and the party that filed a UCC record all have the authority to file a correction statement under §9-518. The Governor signed the bill on March 31st. It will take effect ninety days after adjournment of the legislative session.

The Colorado legislation has no immediate impact on UCC search or filing practices. However, UCC filers should prepare to deal with mandatory electronic filing. Colorado is not the only state interested in creating a purely electronic filing system. Some other jurisdictions may require electronic UCC filing within the next two to four years.

Kansas

Senate Bill 449 eliminates the national UCC form safe harbor from § 9-521. When the bill takes effect, the filing office can reject UCC records under § 9-516(b) if submitted on forms not approved by the Secretary of State. The purpose of this legislation is to reduce the temptation for UCC filers to submit social security numbers. The 1998 versions of the national forms embedded in § 9-521 include a field for the debtor's social security number. The filing office does not want to collect this information, but many filers provide it because of the form design. The International Association of Commercial Administrators ("IACA") redesigned the national forms in 2002. The 2002 versions removed the "SSN or FEIN" label, making filers less likely to provide the

information. The Secretary of State now has flexibility to approve only the 2002 versions of the national forms.

While SB449 addresses an important issue, it eliminates the safe harbor for national forms in § 9-521. The secretary of state has the option of approving the IACA forms, but is not required to do so.

The bill has passed the legislature but has not yet been signed by the governor. Assuming the law will take effect, UCC filers will need to use the form approved by the Kansas Secretary of State. In all likelihood that will be the 2002 version of the IACA forms. Filers can find the 2002 version of the national forms at www.iaca.org.

Alaska

Alaska House Bill 295 has passed the legislature. It contains an amendment to § 9-516(b) that permits the filing office to reject a UCC record if it is not on a form approved by filing office regulation. The bill also repeals the national UCC form safe harbor in § 9-521. As with Kansas SB 449, the purpose is to give the filing office the ability to accept revised national forms developed by IACA. If the governor signs the bill UCC filers should be prepared to use only the 2002 version of the national forms.

PENDING LEGISLATION

Michigan

On March 26, 2008, the Michigan Legislature introduced Senate Bill 1236 to amend provisions of Article 9. The bill would give the secretary of state much broader power to reject UCC filings. The legislation appears to be an attempt to address the problem of bogus lien filing, but could have an impact on legitimate UCC records. Under SB 1236, the filing office can reject records if it determines the record is not required by Article 9, is materially false or filed for an improper purpose. Additionally, the bill provides that an individual debtor cannot be designated as a transmitting utility. Transmitting utility records that already provide an individual debtor name cannot be continued under the proposed law. Bogus lien filers often indicate the debtor is a transmitting utility to ensure the record does not lapse and is more difficult to remove from the UCC index. An exception to the transmitting utility restrictions would occur if the record was filed through a service company.

The Michigan bill also would amend § 9-521 to repeal the national form safe harbor. Instead, the filing office would be required to accept forms approved by NCCUSL. This appears to be a drafting error, because the responsibility for designing the national forms lies with IACA. The legislature has not taken any action on this bill since it was introduced.

Federal

Although not technically UCC legislation, S. 2394 would have an impact on federal tax lien records currently filed with the state filing offices. The bill, co-sponsored by Senators Coleman and Collins, was introduced in late 2007 and would create a national federal tax lien registry. The registry would be maintained by the Secretary of the Treasury. The bill requires the Secretary to make the registry available over the Internet and it must be searchable by the public at no cost. This legislation is currently before the Senate Committee on Finance.

THE NEXT STEPS

NCCUSL and ALI are aware of the current trends in Article 9 legislation and the threat this poses to national uniformity. In response, NCCUSL and ALI appointed a joint review committee to analyze the unresolved Article 9 issues. The committee is expected to complete its work and make recommendations in the summer of 2008. Depending on the recommendations, NCCUSL and ALI may appoint a drafting committee to devise a uniform legislative solution. Due to the complexities involved, the drafting of a national uniform law requires a slow and deliberate approach. Consequently, uniform legislation may not be available to the states until 2009 or later.

What remains to be seen is whether the states will be patient while the NCCUSL/ALI

committees complete their work. Unless the committees work quickly on the most serious issues, more states will be tempted to enact their own non-uniform solutions.

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