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Lender Alert

August 2013

Attention Secured Lenders: The 2010 Amendments to Article 9 are Beginning to Take Effect

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Article 9 of the Uniform Commercial Code, which governs security interests in transactions secured by personal property, is currently undergoing its first revision since 1998. The 2010 Amendments to Article 9 (the "2010 Amendments"), which are the result of a joint effort by the Uniform Law Commission and the American Law Institute, were drafted to address filing issues and other matters that have arisen since the substantial overhaul of Article 9 in 1998. The following is a summary of a few of the key provisions of the 2010 Amendments.

1. Individual Debtor's Name

Perhaps the most important change brought about by the 2010 Amendments relates to the method of identifying an individual debtor's name on a UCC financing statement. Pursuant to the pre-2010 Amendments version of Section 9-503(a), a financing statement sufficiently identifies an individual debtor's name if it provides the "individual" name of the debtor.

However, Section 9-503 provides no guidance regarding the basis for determining a debtor's individual's name. This lack of guidance has caused concern amongst both filers and searchers.

Pursuant to current Section 9-506(a), a financing statement is not effective if errors or omissions contained therein make the financing statement seriously misleading. A financing statement that fails to sufficiently provide the name of the debtor in accordance with Section 9-503(a) is "seriously misleading," unless a search of the records of the filing office under the debtor's correct name would disclose the financing statement (Section 9-506(b) and (c)). Therefore, it is essential for a filer to know the individual debtor's correct name in order to ensure that its financing statement is effective.

Further, the lack of guidance regarding the method of determining a debtor's "individual" name have left many searchers wondering whether their search results accurately reflect all of the effective financing statements filed on the individual debtor. Unfortunately, since the enactment of the 1998 Amendments, courts have been unable to provide clarity on this issue.

As a result, the drafters of the 2010 Amendments have attempted to clarify the method of identifying an individual debtor's name by offering two alternative approaches. "Alternative A," which is known as the "only if" option, provides that, if the debtor holds an unexpired driver's license (or a non-driver identification card accepted as an alternative to a driver's license by the applicable jurisdiction) issued by the state where the financing statement is filed (ordinarily the State where the debtor maintains the debtor's principal residence), the debtor's name as it appears on the driver's license or identification card is the name *required* to be used on the financing statement. Under Alternative A, a filer must include the individual debtor's name on the financing statement *exactly* as it appears on the unexpired driver's license or identification card, regardless of whether the name in the driver's license or identification card contains an error. Under "Alternative A," if the debtor does not have an unexpired driver's license or identification card, a filer may list either the debtor's actual name or the debtor's surname and first personal name on the financing statement.

In States that adopt "Alternative A," if an individual debtor has an unexpired driver's license or identification card, the burden on searchers will be reduced because the searcher will only need to conduct one search under the name that appears on the driver's license or identification card. If, however, an individual debtor does not have an unexpired driver's license or identification card, a searcher should search all variations of the debtor's actual name and surname and first personal name.

"Alternative B," which is known as the "Safe Harbor Approach," provides that a filer may list the debtor's driver's license or identification card name, the debtor's actual name or the debtor's surname and first personal name on the financing statement. Unlike "Alternative A," Alternative B will not reduce the burden on searchers because, in call cases, searchers should search all variations of the debtor's name that would satisfy the three safe harbor categories identified above to ensure that their search discloses all effective financing statements.

The "only if" option has been the preference of most States that have enacted the 2010 Amendments. As of July 2, 2013, 39 jurisdictions (including the District of Columbia and Puerto Rico) have enacted Alternative A. On the other hand, only 7 jurisdictions have enacted Alternative B.

California, which is among a handful of jurisdictions with legislation still pending, is expected to enact the 2010

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Amendments effective July 1, 2014. The current bill to enact the 2010 Amendments in California, AB 502, was amended in the California Senate on June 24, 2013, to create a non-uniform rule for the sufficiency of individual debtor names in § 9-503(a). The current bill, as amended, is essentially "Alternative B" without the driver's license option.

2. Filing Against Registered Organizations

Pursuant to the pre-2010 version of Section 9-503(a), a financing statement sufficiently provides the name of the debtor if the debtor is a "registered organization" only if the financing statement provides the name of the debtor indicated on the public record of the debtor's jurisdiction of organization which shows the debtor to have been organized. However, since some jurisdictions provide more than one public record, in some cases with multiple variations of the name of the "registered organization," there was uncertainty about which public record was sufficient.

To offer clarity, the drafters of the 2010 Amendments created a new definition of "public organic record," which is defined to include "a record consisting of the record initially filed with or issued by a State or the United States to form or organize an organization." Thus, the articles of incorporation for a corporation, or articles of organization for a limited liability company, would qualify as a "public organic record." Records which are not initially filed with or issued to organize an organization, such as a certificate of good standing or a state-created database, will not qualify as a "public organic record," and should not be relied upon to determine the name of a "registered organization" because the name reflected in such a record may not match the name listed in the "public organic record." As discussed above with respect to individual debtors, not knowing the correct name of a debtor can result in serious consequences for both filers and searchers.

Further, the 2010 Amendments revise the definition of "registered organization" to make clear that an organization is a registered organization if it is formed or organized under the law of a state by the filing of a public organic record. In addition, the definition of "registered organization" now includes business trusts.

3. Change in Debtor's Location

The 2010 Amendments add new subsections (h) and (i) to Section 9-316, which are drafted to address perfection issues arising with respect to after-acquired property acquired by a debtor after a change in the debtor's location. Section 9-307 provides that a "registered organization" is located in the State of its organization and an individual is located in the State of the individual's principal residence.

Currently, Article 9 provides that perfection by filing continues four months after the jurisdiction in which the debtor is located changes. However, this grace period applies only with respect to collateral owned by the debtor at the time of the change. New subsection (h) fills this gap with respect to after acquired property by providing that a secured party will remain perfected with respect to collateral acquired by the debtor before and within four months after a change in location. Accordingly, a secured party considering making an advance, in reliance on after acquired property, when the debtor has recently relocated should search the debtor's previous jurisdiction to ensure that no financing statements prime its lien under this new provision.

In addition, new subsection (i) to Section 9-306 provides a similar four month grace period for a new debtor that becomes bound as debtor by a security agreement entered into by the original debtor, where the new debtor and original debtor are located in different jurisdictions. Thus, new subsection (i) provides that a secured party has a perfected security interest in the collateral of a successor by merger that such successor acquired before, and within four months after, the successor became bound by the security agreement.

4. Status of 2010 Amendments

In most the jurisdictions that have enacted them, the 2010 Amendments became effective as of July 1, 2013. While it was the drafters' goal to have a uniform effective date, as of the date of this writing, Alabama, Arizona, California, New York, Oklahoma, Vermont, and the Virgin Islands have yet to enact the 2010 Amendments.

Included in the 2010 Amendments are transition provisions which are set forth in the new Part 8 of Article 9. The following are important transitional rules set forth in Part 8:

- Security interests that are perfected before the effective date, which are no longer effective as a result of the 2010 Amendments, must be properly perfected in accordance with the 2010 Amendments within one year after the effective date.

- If the 2010 Amendments would render a previously effective financing statement ineffective, such financing statement will not become ineffective until it expires on its own or June 30, 2018, whichever is earlier. This transition rule addresses the problems arising from new Section 9-503

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(discussed above), concerning the name of the debtor that must be provided for a financing statement to be sufficient.

5. Conclusion

In sum, while the 2010 Amendments represent the refinement of Article 9, and not a substantial overhaul, the amendments contain a few significant changes to filing and perfection provisions. Accordingly, now that they are effective in most jurisdictions, lenders and other secured parties should begin becoming familiar with the 2010 Amendments.

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