

Delaware Transactional & Corporate Law *Update*

The Proposed 2010 Revisions to UCC Article 9

by Norman M. Powell



Introduction. The current version of Article 9 (“Current Article 9”) of the Uniform Commercial Code (“UCC”), as promulgated in 1998 by the Uniform Law Commissioners (“ULC”) and The American Law Institute (“ALI”), has been enacted in all fifty states, the District of Columbia, and the U.S. Virgin Islands, and generally took effect on July 1, 2001. From 2008 to 2010, a committee (the “Review Committee”) convened by the ULC and the ALI considered certain issues, ultimately recommending amendments to the official text of, and official comments to, Current Article 9 (the “2010 Amendments”). While most are unremarkable and simply clarify existing text, some are noteworthy. This article provides a summary and brief discussion of the 2010 Amendments. To the extent feasible, related provisions are discussed together regardless of their juxtaposition in the code. Unless otherwise noted, all citations in this article are to Current Article 9.

Summary. The 2010 Amendments were approved by the National Conference of Commissioners on Uniform State Laws at its 2010 annual meeting, and are now (or will shortly be) available for consideration and adoption. They include provisions that clarify, rather

than change, what was intended by Current Article 9, as well as substantive changes reflecting emerged and emerging thought. Perhaps the most significant change is the offering of two alternative approaches to the vagaries of determining individual debtors’ names. Alternative A, the so-called “only if” approach, would require that such names be rendered as they appear on a driver’s license or other specified document. Alternative B, the so-called “safe harbor” approach, would merely create a safe harbor for financing statements naming debtors thus. Other debtor name changes are relevant where collateral is held by the personal representative of a decedent, and where collateral is held in a trust. The classification of certain entities as “registered organizations” is clarified, as is the record to be consulted to determine a registered organization’s name. The current “four month rule” that continues perfection following a change in a debtor’s location would be changed to provide not merely that a secured party’s perfected security interest continues for four months following a change in its debtor’s location (or, similarly, for four months following a new debtor becoming bound under an existing security agreement), but that such secured party is generally perfected in collateral acquired

by its debtor within four months thereafter. The much-misunderstood “correction statement,” which has no legal effect and can be filed only by a debtor, would be renamed an “information statement,” would continue to have no legal effect, but could be filed by either a debtor or a secured party. The proposed changes would eliminate the requirement that financing statements indicate a debtor’s type of organization, jurisdiction of organization, and organizational identification number, based on the judgment that the burden of providing such information outweighs the resulting benefits. These and the other revisions are discussed in more detail below.

Proposed Changes to Part 1: General Provisions.

Section 9-102(a)(7) – “authenticate”: The 2010 Amendments begin with revisions to certain definitions. Section 9-102(a)(7) is revised such that the definition of “authenticate” more closely resembles the definitions of “sign” in revised UCC Articles 1 and 7. Recall that Current Article 9, intending to be medium-neutral, largely did away with

Meet the Author:



Norman M. Powell writes and speaks regularly at conferences and training programs on topics including alternative entities and secured transactions, and serves on the Commercial Financial Services, Legal Opinions, and Uniform Commercial Code Committees of the Business Law Section of the American Bar Association.

npowell@ycst.com
302.571.6629

anachronistic terms that suggested any requirement for paper documents and manual signatures affixed by humans wielding pens. This amendment is intended to bring to Article 9 the further-refined thinking of the years since the text of Current Article 9 was finalized in 1998.

Section 9-102(a)(10) – “certificate of title”: Section 9-102(a)(10)’s definition of “certificate of title” is revised to comport with the emerging practice in many jurisdictions of maintaining non-paper electronic records evidencing both ownership and security interests. Conforming changes appear in Section 9-311 (Perfection of Security Interests in Property Subject to Certain Statutes, Regulations, and Treaties). The 2010 Amendments include a new sentence in Official Comment 5b to Section 9-102, noting that when electronic chattel paper is converted to tangible form (“papered-out,” in industry parlance), tangible chattel paper results. In a similar vein, Official Comment 3 to Section 9-330 is modified to more clearly state that a secured party may achieve priority with respect to “hybrid” chattel paper (that is, chattel paper that is partly tangible and partly electronic chattel paper) under Section 9-330(a) or (b), and to clarify how a secured party can retain its priority when tangible chattel paper is converted to electronic chattel paper and vice versa.

Official Comment 5d to Section 9-102 – Assignment of Lessor Rights as Chattel Paper: Rejecting the holding in *In re Commercial Money Center, Inc.*, 350 B.R. 465 (B.A.P. 9th Cir. 2006), the 2010 Amendments provide in their changes to Official Comment 5d to Section 9-102 that if a lessor’s rights under a lease constitute chattel paper, an assignment of the lessor’s right to payment under the lease, even if the assignment excludes any other rights, would also be an assignment of chattel paper.

Section 9-102(a)(68) – “public organic record”: Section 9-102(a)(68) is new, and brings specificity to the question of just what public record should be consulted to determine a registered organization’s name. The new term “public organic record” generally means the document filed with or issued by the relevant state or the United States to form or organize a registered organization. Revi-

sions to the accompanying Official Comment 11 explicitly indicate that a certificate of good standing is not a public organic record and, thus, not an appropriate referent for determining a registered organization’s name. Similarly, the definition of “Registered organization” in (what will be renumbered as) Section 9-102(a)(71) is amended to clarify that the term includes organizations (i) formed or organized, (ii) by (a) the filing or issuance of a public organic record, or (b) by legislative enactment, even if such organizations are created without the need for a public organic record. These latter two provisions work in concert with revisions to Section 9-503 (discussed below).

Section 9-105 – Control of Electronic Chattel Paper: Section 9-105 is revised to provide a general test, and a safe harbor, for achieving perfection by control of electronic chattel paper. The language derives from the Uniform

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organized under federal
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Electronic Transactions Act, and defers to emerging systems that reliably establish the secured party as the assignee of the chattel paper, contemplating continued innovation in this field generally.

Proposed Changes to Part 3: Perfection and Priority.

Section 9-301 – Law Governing Perfection and Priority: The 2010 Amendments include revision and augmentation of Official Comment 5b to Section 9-301 to clarify certain matters relevant to fixture filings and non-fixture filings against collateral of transmitting utilities. A security interest in most

types of collateral, including fixtures, of a transmitting utility can be perfected by a central filing in the jurisdiction where the transmitting utility is located. But a fixture filing is effective to perfect a security interest only in fixtures of a transmitting utility located in the jurisdiction in which such fixture filing is made, with the consequence that multiple such filings may be required.

Section 9-307 – Location of Debtor: It is in Section 9-307 that Current Article 9 provides the rules for determining a debtor’s location, and thus the place in which one must generally file a financing statement naming that debtor for such financing statement to be effective.¹ Its subsection (f) addresses the location of registered organizations organized under federal law. Subparagraph (f)(2) currently provides that where a location is designated in accordance with federal law, such location constitutes the organization’s location for filing purposes. Alas, this succinct and seemingly clear provision has given rise to considerable consternation. In the parlance of many federal laws (e.g., the National Bank Act), what’s designated is actually denominated a “main office” or “home office”, not a location. In its initial enactment of Current Article 9, Delaware added to Section 9-307(f) non-uniform language to the effect that designating a main office or home office constitutes designation of a location. Revised versions of the Official Comments to Current Article 9 offered the same assurance,² but of course lacked the force of law. The 2010 Amendments would remove any doubt that such designations are, in fact, designations of a location for filing purposes.

Section 9-316 – Effect of Change in Governing Law: The 2010 Amendments significantly alter the effect of a change in governing law. Under Current Article 9 Section 316, perfection of security interests that have attached prior to a change in the debtor’s location continues for four months after such change. The 2010 Amendments add a new subsection 316(h) pursuant to which a secured party would also enjoy perfection of security interests that attach within four months *after* a change in the debtor’s location, provided it has already taken steps pursuant to which it would have been perfected absent the change in location. To illustrate, assume D is located in Florida and SP has

properly perfected its security interest in D's inventory and accounts receivable by filing a financing statement in Florida. Thereafter, D's location changes to Delaware. Under Current Article 9, SP remains perfected, for four months following the change in location, in any inventory and accounts receivable in which it was perfected *before* the



change. Under the 2010 Amendment, this remains so, but SP is *also* perfected in any (newly acquired) inventory and (newly arising) accounts receivable to which its security interest first attaches during the four months *after* the change in location. Such perfection continues until the end of this four-month period.

Similarly, a new subsection 316(i) provides for perfection of security interests that attach within four months after a new debtor becomes bound by an existing security agreement. Returning to our example, let's suppose that upon its "relocation" to Delaware "old D" is succeeded by "new D" as the debtor bound by the existing security agreement in favor of SP. Let us further suppose that "new D" enters into a financing transaction in which it grants SP2 a security interest in all of its inventory and accounts receivable, and that SP2 promptly perfects its security interest by filing in Delaware a financing statement naming "new D" as debtor. As between SP and SP2, both of whom have perfected security interests in inventory acquired and accounts receivable arising within the four months immediately following the change in location, who has greater priority? Current Article 9 Section 326 generally provides

that, with respect to collateral in which the original debtor never held an interest, the security interest perfected by filing against the original debtor is subordinate to the security interest perfected by filing against the new debtor. The 2010 Amendments preserve and extend this result to the circumstances contemplated by new subsection 316(i). Thus, in our example, SP is subordinate to SP2 with respect to collateral in which "old D" never held an interest. A modest revision to Official Comment 2 to Section 9-326 clarifies the interplay between that section and Section 9-508 regarding subordination of certain security interests created by a new debtor.

Section 9-317 – Interests That Take Priority Over or Take Free of Security Interest or Agricultural Lien: In what is viewed as a clarification, the language of Section 9-317 is expanded to explicitly cover buyers of all types of collateral not susceptible to perfection by possession. Thus, a licensee of a general intangible, and a buyer (other than a secured party) of any collateral other than tangible chattel paper, tangible documents, good, instruments, or certificated securities takes free of a security interest if he gives value without knowledge of, and before perfection of, such interest.

Section 9-322 – Priorities Among Conflicting Security Interests in and Agricultural Liens on Same Collateral: In another clarification, Official Comment 4 to Section 9-322 has been augmented to include an explicit statement to the effect that a financing statement filed without authorization, but later authorized or ratified, thereupon becomes effective, but nevertheless enjoys priority from its time of filing. Official Comment 8 to the same section has been augmented to complete the explanation of certain priority rules applicable to proceeds: specifically, that where two security interests in the same original collateral are entitled to priority in proceeds under Section 9-322(c)(2), the security interest having priority in the original collateral has priority in the proceeds.

Proposed Changes to Part 4: Rights of Third Parties. Current Article 9 Section 406 is a broad override of contractual restrictions on assignability of receivables. Current Article 9 Section 408 is a narrow such override. The two differ on whether an assignee

may enforce the assigned receivable against the account debtor or another obligor. The 2010 Amendments address the allocation of transactions between the broad override of Section 9-406 and the narrow override of Section 9-408, and have relevance where collateral is the right to payment of a loan. As they appear in Current Article 9, Sections 406 and 408 differ on whether an assignee may enforce the assigned receivable against the account debtor or another obligor notwithstanding a contractual restriction on assignability. If the right to payment is evidenced by chattel paper, it is clear the assignee can enforce the right despite any contractual restriction. But if the right to payment is evidenced by an instrument, or is a payment intangible, the assignee can enforce despite contractual restriction if the assignment is made for security, but not if the assignment is a sale. Experience has revealed uncertainty in determining whether foreclosure should be regarded as a "sale" or an assignment "for security." The 2010 Amendments clarify applicability of 9-406, and explicitly provide that a buyer at a foreclosure sale, as well as the assignee in a strict foreclosure under 9-620, can enforce the right notwithstanding any contractual restriction.

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Proposed Changes to Part 5: Filing. Perhaps the greatest and most significant of the 2010 Amendments appear in Section 9-503 (Name of Debtor and Secured Party). These changes are relevant to filings against registered organizations, filings where collateral is being administered by the personal representative of a decedent, filings where collateral is held in a trust that is not a registered organization, and, most significant of all, filings against individual debtors. With different variations in each context, it has proven challenging to determine exactly what a given debtor's name is, and likewise chal-

lenging to make other determinations antecedent to filling out financing statements and tendering them for filing. In addition to the changes discussed below, consistent changes appear in Official Comment 2 to Section 9-506 (Effect of Errors or Omissions).



Registered Organizations: It has proven unclear to some just which public record is relevant to determining the name of a registered organization. Many quickly came to the view that good standing certificates were not the appropriate source of such information, but uncertainty remained as to which filed, or issued, formation document should be consulted.³ As revised by the 2010 Amendments, Section 9-503 refers to the “public organic record,” the newly defined term appearing at new subsection 9-102(a)(68),⁴ which means a record filed with the relevant state or the United States, and includes a charter issued by such state or the United States. Helpfully, it explicitly notes that a certificate of good standing or an index of domestic entities is irrelevant.⁵ Moving beyond the challenge of determining a registered organization’s name, the 2010 Amendments revisit the threshold question of what organizations fit the subcategory of registered organization. “Registered organization” includes an organization created without a public record but that is “formed” only when a public filing has been made. For example, a Delaware statutory trust is “created” by its governing instrument,⁶ but is “formed at the time of the filing of the initial certificate of trust in the office of the Secretary of State”⁷ Similarly, the 2010 Amendments clarify that a Massachusetts business trust is a registered organization.⁸

Decedents and Their Estates, Trusts and Trustees: The 2010 Amendments respond

to some extent to difficulties experienced by those endeavoring to determine, in contexts involving decedents and their estates, and trusts and trustees acting with respect to property held in trust, the exact identity of the “debtor”, which is to say the person possessed of the requisite rights to meet the statutory definition of “debtor” in Section 9-102(a)(28). In the former context, the 2010 Amendments eliminate the requirement that a filing indicate whether, in fact, the debtor is “a decedent’s estate,”⁹ and instead simply require indication that the collateral is “being administered by the personal representative of the decedent.” In the latter context, the 2010 Amendments eliminate the requirement that a filing indicate whether, in fact, the debtor is “a trust” or, alternatively, is “a trustee acting with respect to property held in trust,” and instead simply require indication that “the collateral is held in a trust.” In both contexts, special transition rules provide, in effect, that financing statements filed prior to the effective date of the 2010 Amendments and meeting the then-current requirements (that is, the requirements of Current Article 9) in this regard will not cease to be effective by reason of their failure to provide the simpler (yet arguably different) indication required by the 2010 Amendments. The reader is cautioned, however, that although the challenge of determining the precise identity of the “debtor” need no longer be met as a precondition to properly filling out a financing statement, it remains vitally important inasmuch as the financing statement, to be effective, must generally be filed in the jurisdiction in which the debtor is located within the meaning of Section 9-307. Finally, it should be noted that the 2010 Revisions clarify that these special rules applicable to property held in a trust don’t apply where collateral is held by a trust that is itself a registered organization – in such cases, the ordinary rules for filing against registered organization debtors should be followed.

Individual Debtor Names: The issue that presented the greatest challenge to the Review Committee was that of individual debtor names. Under Current Article 9, when the debtor is an individual, a financing statement is sufficient only if it provides the “name of the debtor.” The simplicity of this requirement belies the challenge of its application. American law provides indi-

viduals nearly unlimited freedom to change their names, often with little or no formality or documentation. Consider, for example, the name changes that commonly accompany marriage and divorce, and the insidious spread of informality by which many a Thomas is known far and wide as Tom and many an Elizabeth as Liz (or, if personal preference so dictates, Beth), to say nothing of Stefani Joanne Angelina Germanotta (or is her name now “Lady Gaga?” And if so, is that a first name and surname, or something else?). While the Review Committee generally came to share the view that the simplicity of requiring the “name of the debtor,” while appealing, presupposed that one could determine a debtor’s name with greater certainty and ease than experience suggests one actually could, it found no panacea, and instead offers in the 2010 Amendments two alternative approaches. Alternative A – the



“only if” approach – requires use of the name that appears on the debtor’s driver’s license or other specified document (e.g., an identification card issued by his or her state of residence) or, if the debtor has no such document, the debtor’s surname and first personal name. Alternative B – the “safe harbor” approach – retains the current “name of the debtor” approach, but also provides a “safe harbor” for using the name designated by statute (viz., the name appearing on the debtor’s driver’s license or state-issued identification card). These alternatives strike different balances in the allocation of risks and protections among filers and searchers. The “only if” approach appears very simple – if only the name on the relevant identification document will suffice, searchers need only conduct searches in such name. But this