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Twenty Questions about Filing under Revised Article 9: The Rules of the Game under New Part 5

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TWENTY QUESTIONS ABOUT FILING UNDER REVISED ARTICLE 9: THE RULES OF THE GAME UNDER NEW PART 5

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Article 9's filing provisions have been significantly rewritten. Under Revised Article 9, for most transactions, filing should be as simple as child's play. The new provisions are intended to place virtually all filings in a single statewide office, facilitate electronic filing, foster nationwide utilization of well-designed user-friendly uniform paper forms, and make filing office practices more efficient, transparent, and uniform. This article presents the key concepts, structure, and terminology of new Part 5 in the format of a series of fact situations. The hypotheticals are intended to present the rules and principles systematically but in a working context. Except as otherwise indicated, all references are to Revised Article 9.

Q1. Debtor's name, as shown in its corporate charter, is "The Best Lawyers in the World, Inc." The financing statement filed provided the debtor's name as "Best Lawyers in the World." Has Debtor's correct name been provided? Is the financing statement sufficient?

A1. Section 9-502(a)(1) provides that a financing statement is not sufficient if it fails to provide the name of the debtor. Section 9-503 provides specific rules elaborating on how a debtor's name is sufficiently provided. In this case, Debtor is a corporation and most likely fits within the newly defined category of "registered organization."[1] Section 9-503(a)(1) states that the financing statement sufficiently provides the name of a debtor that is a registered organization only if it provides the name indicated on the public record of the debtor's jurisdiction of organization. Thus, the debtor's correct name has not been provided, and the case presents the issue

* Mr. Sigman was a member of the Drafting Committee to revise Article 9. The views expressed herein, however, are solely his. These questions are based on problems used at a Financial Lawyers Conference seminar. The author wishes to thank Steven L. Harris for his assistance in preparing the questions and helpful suggestions concerning the answers. Errors, however, are solely the author's.

1. *See* R. § 9-102(a)(70).

of an error in the debtor name.

Section 9-506(a), continuing the rule under Former section 9-402(8), states: "A financing statement substantially satisfying the requirements of this part is effective, even if it has minor errors or omissions, unless the errors or omissions make the financing statement seriously misleading." The text adds a reference to "omissions" for the sake of completeness, but this is unlikely to alter any result that would have been reached under the former language, as an omission is a form of error. Supplementing the general rule of condemning errors that are seriously misleading, in a provision specifically addressing errors in the debtor name, section 9-506(b) states: "Except as otherwise provided in subsection (c), a financing statement that fails sufficiently to provide the name of the debtor in accordance with Section 9-503(a) is seriously misleading." This per se rule is new and might produce a different result in some instances.

The financing statement in this case most likely will be sufficient by virtue of the section 9-506(c) safe harbor rule. Section 9-506(c) provides that an erroneous debtor name does not make the financing statement seriously misleading "[i]f a search of the records of the filing office under the debtor's correct name, using the filing office's standard search logic, if any, would disclose" the financing statement. Many, if not most, of the statewide filing offices use a search logic with respect to names of organizations (much less uniformity exists with respect to names of individuals) that ignores organizational endings such as "Inc." and ignores "The" when it is the first word of an organization's name. It should be noted that the safe harbor entails use of the search logic, if any, used by the filing office. The fact that a wider search logic used by a private search service might have disclosed an erroneous filing does not bring that financing statement within the safe harbor. Note also that a filing office may modify its search logic from time to time; this might have the effect of rendering undiscoverable (under a search using the correct name) a filing providing an erroneous name that was previously discoverable.

The statutory safe harbor rule reflects a balance between the need for some flexibility to allow for human error on the part of filers (which precludes adoption of a rule requiring absolute perfection in the presentation of the debtor name, particularly for names of individuals and organizations other than registered organizations, for neither of which is there a publicly available official record that might enable a filer to assure itself of absolute accuracy) and the avoidance of a rule that would cast an altogether inappropriate burden on

searchers to have to try to divine potential errors and make searches under not only the correct name but also "foreseeable" or "likely" errors that a filer might have made, although some courts, under prior law, have indicated a misguided willingness to follow such an approach.[2] Using the objective rule of discoverability upon a search under the correct name also offers the benefit of lessening the need for litigation.

Q2. Secured party's name, as shown in its corporate charter, is "The First National City Bank of Oxnard, N.A." It is frequently referred to in the financial world as "Citybank." The filed financing statement provides the secured party's name as "Citybank." Is the financing statement sufficient?

A2. Under section 9-502, one of the three elements of sufficiency of a financing statement is "the name of the secured party or a representative of the secured party."[3] Section 9-503's specific rules about name sufficiency, e.g., providing the name of a registered organization "indicated on the public record of the debtor's jurisdiction of organization,"[4] are applicable only to debtor names. "Citybank," however, is so far from the correct name of the secured party that even without that rule, it is clear that the correct name has not been provided. The effect of this error, however, unlike the debtor name error discussed in Question 1, is not governed by sections 9-506(b) and (c), but rather by section 9-506(a). This provision, intended to provide a margin for error, makes clear that information provided on the financing statement need not be perfect and that an error does not ipso facto render a filing insufficient. It sets as an outer boundary to this permissiveness the "seriously misleading" rule.

This rule, of course, varies in its meaning depending on the context, i.e., the nature of the information that is erroneous. Before dealing with the secured party name error presented in this Question, it may be useful to consider the different types of information that might be erroneous. I would divide them into four categories.

The first category is the debtor's name—already considered in Question 1 and governed by the specific rules of subsections (b) and (c) of section 9-506. Since this item of information is the key to

2. See, as examples of the approach rejected by Revised Article 9, *In re Mines Tire Co.*, 194 B.R. 23, 26 (Bankr. W.D.N.Y. 1996); and *Corporate Financers, Inc. v. Voyageur Trading Co.*, 519 N.W.2d 238, 243 (Minn. Ct. App. 1994).

3. *See* R. § 9-502(a)(2).

4. *Id.* § 9-503(a)(1).

discoverability of the filing, these subsections reflect the crucial nature of the information and focus on discoverability in setting the boundaries for permissible error. The second category, at the other extreme, comprises the items of information that are not even elements of sufficiency under section 9-502. This category includes items such as addresses of the parties and the jurisdiction of organization of the debtor. While these are useful items of information, section 9-520(c) provides that even if these items are completely missing, the financing statement is nevertheless effective if it is filed (although the filing office is supposed to reject a tendered filing that fails to provide this information[5]). This point is discussed in greater depth in connection with subsequent questions. The point for present purposes is that since the statute declares effective a filed financing statement where such an item is totally absent, the further impact of that rule is to render effective a financing statement where that item is provided but is erroneous, leaving no room for an inquiry under section 9-506(a). Thus, with respect to this category of information, the seriously misleading rule simply is not applicable or, put otherwise, cannot be failed. The third category, indication of collateral, is one of the elements of sufficiency.[6] It is discussed in depth four paragraphs below. For purposes of the present analysis, the seriously misleading rule is effectively displaced by section 9-108 or, put otherwise, the standard in that section of "reasonable identification" provides the context for what is "seriously misleading" when the category of information that is under scrutiny is the collateral indication. The fourth category, the secured party's name, is the type presented by this Question.

In considering the effect of an error in the secured party name, both the definition of "secured party" and other provisions of Part 5 dealing with the secured party should be borne in mind. The term "secured party" is defined to include "a trustee, indenture trustee, agent, collateral agent, or other representative in whose favor a security interest . . . is created or provided for."[7] Also, the name requirement provision[8] is expanded to encompass a "representative" (whether or not the representative capacity is indicated on the financing statement[9]). These provisions make clear that the true

5. *See id.* §§ 9-516(b)(4), (b)(5)(a), (b)(5)(C)(ii), 9-520(a).
6. *See id.* § 9-502(a)(3).
7. *Id.* § 9-102(a)(72)(E).
8. *See id.* § 9-502(a)(2).
9. *See id.* § 9-503(d).

identity of the person who actually extended credit or the person in whose favor a security interest was granted need not be disclosed of record.[10] Moreover, putting onto the public record the name of an assignee of a secured party has never been mandatory and is not an element of continued perfection.[11] These provisions suggest that great liberality should be employed in determining the consequences of an error in the secured party's name. Cases under Former Article 9 recognized that the secured party's name carries far less weight than that of the debtor, since the latter, not the former, is the key to the index.[12] Further, and more generally, it should be kept in mind that the function of the filing system is not to give detailed information which can be relied on without inquiry of the debtor supplemented by such further investigation as a prospective secured party may deem appropriate under the circumstances. Other rules in Part 5 are based on this premise.[13]

Since an error in the secured party name can never preclude discovery of the financing statement because the index is based on debtor names, it would be an extraordinarily rare case where an error in the secured party name could fail the seriously misleading test. Perhaps a name might be so egregiously wrong and the error of such a nature that there would be a strong probability that most reasonable searchers, despite discovery of the filing, would somehow nevertheless be seriously misled by the error (e.g., despite discovering the financing statement they would be hampered significantly in investigating it by reason of the error, posing a substantial risk of debtor or secured party misconduct). The reasoning that virtually any erroneous secured party name is nevertheless sufficient does not, however, compel the conclusion that complete omission of any name would be acceptable, for this would open the door to possible manipulation by the debtor. An erroneous name does not present this risk, and the secured party claiming to be the one entitled to base perfected status on that particular filing would, of course, have to

10. This rule is in accord with *In re Cushman Bakery*, 526 F.2d 23, 30 (1st Cir. 1975) (approving use of nominee). *See also In re* Fried Furniture Corp., 293 F. Supp. 92, 93 (E.D.N.Y. 1968) (agent); *In re* Industrial Packaging Prods. Co. v. Fort Pitt Packaging Int'l, Inc., 161 A.2d 19, 21 (Pa. 1960) (agent). In addition, see R. § 9-511, which introduced explicitly the concept of "secured party of record."

11. *See* R. §§ 9-310(c), 9-514 (continuing the rules under Former sections 9-302(2) and 9-405).

12. *See, e.g.*, Unsecured Creditors Comm. v. Marepcon Fin. Corp (*In re* Bumper Sales, Inc.), 907 F.2d 1430, 1435 (4th Cir. 1990); Scot Lad Foods, Inc. v. First Bank & Trust Co., 546 N.E.2d 1168, 1170 (Ill. App. Ct. 1989).

13. *See, e.g.*, R. § 9-507(b) (discussed in Question 3).

present a credible story linking it to the erroneous name.

This liberal approach, however, would not preclude application of an equitable estoppel in an appropriate case where the secured party name error actually resulted in prejudice to a particular searcher that reasonably relied to its detriment on the error and would be harmed unfairly if the filer who committed the error were allowed to assert its priority.[14] This approach, supplemented by estoppel when appropriate, would visit consequences on the party who committed the error only when required to prevent unfairness, but would not render the filing ineffective for all purposes. While a more stringent approach might stimulate filers to exert greater effort to avoid secured party name errors, filers who commit secured party name errors should not, as a matter of course, be penalized by rendering their filings ineffective for all purposes. Even an across-the-board rule that does not require the existence of a searcher who was actually harmed would, nevertheless, not avoid litigation, since the inquiry into the "seriously misleading" nature of the error would still be necessary. Moreover, employing a rule that imposes a penalty is not the approach taken generally by the Uniform Commercial Code.[15] Fortunately, most secured parties are likely to get their own names right.

Although not presented by this Question, it is appropriate to complete the analysis of section 9-506(a) by including here a brief discussion of errors in the indication of collateral. Like the secured party name error, a collateral indication error cannot preclude discovery of the financing statement. Again, however, since section 9-506(a)'s language does not explicitly limit that rule to debtor name errors, courts might apply the general "seriously misleading" rule to errors in the indication of the collateral. In my view, a sound methodology would begin with section 9-504, which deals directly with the sufficiency of the indication of collateral in a financing statement. That section provides that an indication is sufficient if it provides "(1) a description of the collateral pursuant to Section 9-108; or (2) an indication that the financing statement covers all assets or all personal property." Except for use of the blanket "all assets" indication, this provision, therefore, directs us to section 9-108, which provides that a description is sufficient if, except as otherwise provided in other subsections, it "reasonably identifies what is

14. *See id.* § 9-338 (providing an analogous rule) (discussed in Question 13).
15. *See* U.C.C. § 1-106(1).

described."[16] Thus, with respect to collateral description, the statute directs that the focus of analysis be on whether the description meets the "reasonably identifies" test. In my view, if the description fails to meet that test, a court should not even consider an argument that, despite such insufficiency, the financing statement nevertheless may be effective because the error or omission did not make the financing statement "seriously misleading." "Reasonable identification" is the standard provided by the statute for this category of information. This methodology easily accommodates the classic erroneous serial number cases. A court should have no difficulty finding that "1996 Bronco VIN 123456789" reasonably identifies the 1996 Bronco whose VIN is 123457689. Thus, there should be no occasion for application of the "seriously misleading" test as such to collateral indication questions.

This Question presents a case involving a trade name used by a secured party. Section 9-503(c), dealing with the debtor's trade name, provides that a trade name is neither necessary nor sufficient. Although this was the rule under Former Article 9 as well,[17] some courts have gotten this wrong.[18] The intended effect of the debtor trade name rule is to push secured parties to do what due diligence and good business practice would dictate anyway: confirm the debtor-supplied information by examining public records to be sure they know who the debtor is, what its status is, whether there are peculiarities in its articles, etc.

Q3. The facts are as in Question 2. Three years after the financing statement was filed, the debtor approached Lender for a loan to be secured by certain equipment. Lender discovered Citybank's filed financing statement by a search under the debtor's name and tried to contact Citybank, by writing to the mailing address provided in the financing statement, to determine whether the particular equipment was actually encumbered. Lender was unable to do so because the mailing address provided in the financing statement was a post office box that was no longer operative (Lender's letter to Citybank was returned marked "Addressee Unknown") and there was no listing in the telephone book under "Citybank." Lender makes the secured loan and files a sufficient financing statement,

16. R. § 9-108(a).

17. *See* U.C.C. § 9-402(7).

18. *See, e.g.*, National Bank v. West Texas Wholesale Supply Co. (*In re* McBee), 714 F.2d 1316, 1321 (5th Cir. 1983); Brushwood v. Citizens Bank (*In re* Glasco, Inc.), 642 F.2d 793, 796 (5th Cir. Unit B 1981).

thereby perfecting its security interest. Which security interest, Citybank's or Lender's, has priority?

A3. If both financing statements are sufficient, the 'first to file or perfect' rule[19] would dictate that Citybank's security interest has priority. With respect to the name error, assume that, pursuant to the analysis under Question 2, Citybank's financing statement is found to be sufficient.

This brings us to the matter of the address provided in the financing statement. The address provided was Citybank's mailing address at the time of filing; it became no longer useful only sometime after the filing. Thus, there was no error. The applicable rule is found in section 9-507(b), which states: "Except as otherwise provided in subsection (c) and Section 9-508 [both of which deal with the debtor name], a financing statement is not rendered ineffective if, after the financing statement is filed, the information provided in the financing statement becomes seriously misleading under Section 9-506." The same result should obtain, however, even were we dealing with an error. The secured party's address is not an element of sufficiency under section 9-502. Failure to provide an address for the secured party is a ground for rejection under section 9-516(b)(4), but if the financing statement is nevertheless accepted by the filing office, it is effective.[20] Since a filed financing statement that lacks a secured party address would be effective, a filed financing statement with an erroneous address or an address that was correct when filed but is no longer correct must surely remain effective. (The answer to this Question, however, is provided by section 9-507(b) and is not dependent on logical extrapolation (as is the case with an erroneous address).) Furthermore, when considering the effect of a secured party address error, it must be borne in mind that a searcher has no statutorily protected right to communicate with a secured party. The duty of a secured party to respond to inquiries is provided in section 9-210 and runs only to the debtor.[21]

Q4. Which, if any, of the following indications of collateral on a financing statement is sufficient: (i) "all of Debtor's equipment," (ii) "all of Debtor's assets," (iii) "all of Debtor's assets except for equipment"?

19. *See* R. § 9-322(a)(1).

20. *See id.* § 9-520(c).

21. See also the discussion in Question 11 of the effect of an incorrect secured party address in the context of a purchase money security interest notification.

A4. All three are sufficient. Analysis begins with section 9-502(a)(3), which provides that a financing statement is sufficient if it "indicates the collateral covered by the financing statement." Section 9-504 provides that an indication is sufficient if it (1) is a description sufficient under section 9-108 ("whether or not it is specific, if it reasonably identifies what is described"[22]) or (2) indicates that all personal property or all assets are covered. The first of these alternatives, generally speaking, carries forward prior law (this is true in principle, but section 9-108 does change the notion of description somewhat). The second alternative changes the law in those states where there is caselaw (probably the majority of these) to the effect that an "all assets" description is inadequate, on the basis that "everything" does not describe anything or on the basis that "everything" does not describe the collateral by "item" or "type" (as required by Former section 9-402).[23] It should be noted that an "all assets" description is not a sufficient description, as a matter of law, under section 9-108(c), for purposes of a security agreement, despite its sufficiency in a financing statement. As to the three indications posited in Question 4: (i) section 9-108(b)(3) expressly renders sufficient identification by a collateral type defined in the UCC; (ii) and (iii) are both sufficient by virtue of section 9-504(2); (iii) is simply a lesser included example of (ii).

Q5. A financing statement filed in January 2002 provided the following collateral indication: "green 1998 4-door Audi A4." Assume there is no applicable certificate of title statute. (i) Is this indication sufficient to perfect a security interest in a blue 1998 4-door Audi A4 bought by Debtor in February 2002? (ii) Would the result in part (i) be different if the 1998 4-door Audi A4 owned by Debtor at the time of the filing of the financing statement had been green then but was painted blue after the filing? (iii) Would the result in part (i) be different if Debtor is (a) an individual who has never owned more than one car at a time and that since October 2001, when he bought it, his only car was a blue 4-door Audi A4, or (b) a dealer who at all times has an inventory of at least a dozen Audis of various models and colors?

A5. (i) In the absence of more facts (see part (iii) below), this indication does not appear to describe ("reasonably identify") the blue car bought by Debtor after the filing. This Question illustrates

22. R. § 9-108(a).

23. *See, e.g.*, Johnson v. First Nat'l Bank (*In re* Fuqua), 461 F.2d 1186 (10th Cir. 1972).

the risk of being too specific; better be very sure you have it right if such specificity is required by the debtor. There are, of course, the VIN number cases that have excused a single-digit error on the ground that a vehicle otherwise matching the description and having a VIN number almost identical to that provided in the financing statement is adequately described.[24] On the basis of those cases, the secured party might argue that the posited description is adequate on the basis of correct year, make, model, and style, with only color being incorrect—i.e., that it does "reasonably identify" the collateral.

(ii) Yes, the result would be different. The indication did describe Debtor's car correctly at the time the financing statement was filed, albeit perhaps with atypical specificity (putting aside the use of VIN numbers and other descriptive elements often required under certificate of title laws). The financing statement was sufficient. The secured party always has the burden of proof to identify that it is seeking to enforce against its collateral, so in this case the secured party would have to prove that the now-blue car was in fact the green car with a post-filing paint job. Section 9-507(b) makes clear that the secured party has no duty to monitor with respect to the car's color and has no duty to amend its financing statement due to the post-filing change of car color.

(iii) This part of the Question presents the issue, alluded to in part (i), of whether, at least within reasonable limits, surrounding facts peculiar to the case may permit a seemingly insufficient description to reasonably identify the collateral. If external facts are to be considered, assumption (a) certainly presents a much stronger case for sufficiency than assumption (b). In light of the different purposes served by the collateral description in the security agreement (which conveys property rights, and which like all contracts, is subject to extrinsic evidence of the parties' intention) and in the financing statement (which serves only as a warning bell and is, in most circumstances, not relied on without further investigation), a looser approach to reading collateral descriptions in financing statements is justified. Nothing in the text suggests an intent to change existing law. Estoppel may be the appropriate method to safeguard against undesirable results in a particular case, without the necessity to have a stringent approach that renders the financing statement ineffective for all purposes. Care, however, must be taken to avoid opening an avenue for after-the-fact manipulation of results

24. *See, e.g.*, Bank of N. Am. v. Bank of Nutley, 227 A.2d 535 (N.J. Super. Ct. 1967).

by the debtor.[25]

Q6. Debtor applies for a loan. Bank, advised by its counsel that pre-filing is advantageous, files the national standard written (unsigned) form financing statement covering Debtor's inventory and accounts. (i) Debtor is traveling while Bank is considering the loan application and preparing the security agreement. Bank's loan officer calls Debtor to discuss the terms of the loan; Debtor approves Bank's filing of a financing statement during the telephone conversation. Is the filed financing statement effective? (ii) Same facts as part (i) except that Debtor subsequently signs a security agreement covering inventory and accounts; the security agreement makes no mention of filing a financing statement. Is the filing effective? (iii) Same facts as part (ii) except that the security agreement (still silent regarding filing a financing statement) covers only inventory. (iv) Same facts as part (ii) except that Debtor finds a better deal elsewhere, never draws on the loan, and demands that Bank file a termination statement. Is Debtor entitled to the termination statement? What can Debtor do if Bank refuses to provide the termination statement?

A6. Before addressing the issues presented by this Question, it is appropriate to discuss a significant change in practice that will obtain under the new law—under Revised Article 9, there is no requirement that the debtor sign a financing statement.[26] Now, as before, the vital element is authorization for the filing.[27] This was implicit under prior law and is now made explicit.[28] There is no need, however, that evidence of authorization be placed on the public record. The new approach makes clear that the filing office has no role to play with respect to authorization.[29] The sole grounds for refusal to accept a tendered filing, set forth in section 9-516(b), have nothing to do with the matter of authorization. Given the facts that: (1) a filing office has no means of verifying the authenticity of a purported debtor signature (so the signature requirement could not effectively guarantee the "integrity" of the public record); (2) the presence of the signature requirement had not deterred abuse (usually politically motivated) by filers of so-called "bogus filings"; (3) the presence of the signature requirement had resulted in inefficiency (and sometimes error, arbitrariness, added cost, and

25. See the discussion in Question 2 concerning collateral description errors.
26. *See* R. § 9-502 cmt. 3; *cf.* U.C.C. § 9-402(1).
27. *See* R. § 9-502 cmt. 3.
28. *See id.* § 9-510(a).
29. *See id.* § 9-509 cmt. 2.

delay) in the intake process of certain filing offices (often flowing from unawareness of the meaning of "signed," defined in unchanged section 1-201(39), which does not require a blue-ink manually applied name); and (4) the extra burden on electronic filing that some might have been tempted to impose were an electronic or "digital" signature to be required, the Drafting Committee simply eliminated the requirement that evidence of authorization of the filing be part of the public record. The requirement that the debtor authorize the filing of the financing statement, of course, continues. Section 9-509(a)(1) provides that a person may file an initial financing statement (or an amendment that adds collateral) only if the debtor authorizes the filing in an authenticated record. Thus, the statute now makes explicit the same result as would have obtained under Former Article 9 in the case of the filing of a financing statement on which the debtor's "signature" was forged—despite having been accepted by the filing office and become part of the public record, the financing statement would not have been effective for any purpose. Deletion of the signature requirement, along with the adoption of medium-neutral language that does not imply a paper filing, also facilitates electronic filing (although electronic filing was possible, and in fact used, under Former Article 9[30]).

The Question presents the issue of effectiveness of a filed financing statement. Section 9-510(a) provides: "A filed record is effective only to the extent that it was filed by a person that may file it under Section 9-509." Section 9-509(a)(1) provides that a person may file an initial financing statement only if "the debtor authorizes the filing in an authenticated record." In part (i), the debtor authorized the filing, but did not do so in an authenticated record. Section 9-102(a)(69) defines "record" to mean "information that is inscribed on a tangible medium or which is stored in an electronic or other medium and is retrievable in perceivable form." The telephone call does not qualify as a record.[31] Debtor's unrecorded telephonic consent would not, at least in the absence of more facts, fall within section 9-102(a)(7)'s definition of "authenticate." "Signing" would, under unchanged section 1-201(39), require a "writing," apparently

30. *See* PEB COMMENTARY NO. 15, ELECTRONIC FILING UNDER ARTICLE 9 (1996).

31. A tape recording of the telephone call, however, might well qualify. *See* Londono v. City of Gainesville, 768 F.2d 1223, 1227-28 n.4 (11th Cir. 1985) (tape recording as a writing satisfying the statute of frauds); Ellis Canning Co. v. Bernstein, 348 F. Supp. 1212, 1228 (D. Colo. 1972); Swink & Co. v. Carroll McEntee & McGinley, Inc., 584 S.W.2d 393, 399 (Ark. 1979); *see also* PEB COMMENTARY NO. 15, *supra* note 30 (concerning electronic filing under Former Article 9).

absent here, and there does not appear to have been any symbol that Debtor might have adopted with the present intent to identify itself and adopt or accept a record.

(ii) Section 9-509(b) provides: "By authenticating ... a security agreement, a debtor ... authorizes the filing of an initial financing statement, and an amendment, covering: (1) the collateral described in the security agreement...." Two further points are raised by this part of the Question. First, nothing in the statute requires that the requisite authorization, in the requisite form, exist at the moment of presentation of the financing statement for filing—the familiar concept of ratification serves to make the financing statement fully effective from the time of filing (for purposes of all applicable rules, such as the priority rule based on time of filing). Second, the rule of section 9-509(b) is not contingent on the express mention of authorization in the security agreement—the statute makes authorization an automatic consequence of the debtor's authentication of a security agreement.

(iii) This part of the Question brings out the point that such automatic authorization extends only to the collateral covered in the security agreement. Thus, there was neither automatic authorization nor authorization evidenced by an authenticated record with respect to a filing covering accounts. The filing, of course, is authorized and effective with respect to inventory and proceeds thereof.[32] It must be kept in mind that a financing statement is not a "document" (even when embodied in a paper record) that stands or falls in its entirety; the financing statement is an aggregation of data meeting the sufficiency requirements of section 9-502. "Financing statement" is defined in section 9-102(a)(39) simply as a record, and there are no requirements of form that go to sufficiency or effectiveness.

(iv) This part of the Question presents the issue of when a person named as a debtor on a filed financing statement is entitled to obtain a termination statement from the secured party. Since the collateral is inventory, it is not consumer goods, and the parties' rights and obligation are governed by section 9-513(c), not subsection (a). The secured party is obligated, within twenty days after the secured party receives an authenticated demand from the debtor, to send the debtor or file directly a termination statement when there is neither an outstanding secured obligation nor a commitment to give value.[33]

32. *See* R. § 9-509(b).
33. *See id.* § 9-513(c)(1).

If the secured party fails to fulfill that obligation, the debtor may file a termination statement itself.[34] Section 9-510(a) provides that a filing is effective to the extent it was filed by a person entitled to file it under section 9-509. Section 9-509(d)(2) provides that a person (including the debtor) may file a termination statement for a financing statement as to which the secured party failed to perform the obligation imposed under section 9-513, provided (as conditions to the effectiveness of the termination statement) that the debtor authorizes the filing and that the termination statement indicates that the debtor authorized it to be filed. The latter proviso enables subsequent searchers to discern that the debtor has filed the termination statement claiming entitlement to do so pursuant to this section—additional information that will no doubt provoke further inquiry by a prudent searcher. Unless circumstances suggest a contrary course, a prudent searcher will, in all events, likely investigate all filed financing statements, even those whose effectiveness appears to be terminated by filed termination statements. In addition to the right to file an effective termination statement, if the debtor has been harmed by the secured party's failure to perform its section 9-513 obligation, the debtor is entitled to compensatory damages under section 9-625(b) and statutory damages under section 9-625(e)(4).

Q7. Bank *A*, which acts in California through Straw Man, is considering Debtor's application for a secured inventory loan. Bank *A* will provide the funds advanced and ultimately will reap the income or suffer any loss that is produced by the loan, but the security agreement and other loan documents run in favor of Straw Man, which will administer the loan. In preparation for the loan, a financing statement is filed. (a) Which, if any, of the following financing statements is sufficient? (i) financing statement identifying "Bank *A*" as secured party. (ii) financing statement identifying "Straw Man" as secured party. (iii) financing statement identifying secured party as "Straw Man acting as agent for Bank *A*." (iv) financing statement identifying secured party as "Straw Man, as Agent." (b) With respect to each of the financing statements listed in part (a), assuming it was filed, who may file an amendment?

A7. Section 9-502 requires for sufficiency that a financing statement provide the "name of the secured party or a representative of the secured party."[35] The definition of "secured party" includes "a

34. *See id.* § 9-509(d)(2).
35. *Id.* § 9-502(a)(2).

trustee, indenture trustee, agent, collateral agent, or other representative in whose favor a security interest ... is created or provided for."[36] Thus, the secured party is the person in whose favor the security agreement provides for a security interest, whether that person is the actual creditor or an agent for the actual creditor. Therefore, in part (i), the financing statement identifying Bank *A* would not appear to be sufficient because the security agreement did not run in its favor. It might be argued, however, that under the law of agency, extrinsic to Article 9, but incorporated under section 1-103, Bank *A* is nevertheless the secured party, as Straw Man's undisclosed principal. This approach does not fit the statutory construct neatly, however, and might have unintended consequences. Perhaps this might better be dealt with as a name error.[37]

In part (ii), however, the financing statement identifying Straw Man is sufficient, whether Straw Man or Bank *A* is the grantee of the security interest under the loan documents. If Straw Man is the grantee, it is obviously the secured party. If Bank *A* is the grantee, identification on the financing statement of Straw Man is nevertheless sufficient because Straw Man is Bank *A*'s representative. Section 9-503(d) provides: "Failure to indicate the representative capacity of a secured party or representative of a secured party does not affect the sufficiency of a financing statement."

The financing statements in parts (iii) and (iv) are clearly sufficient under all hypotheses—nothing in Article 9 requires disclosure of either representative capacity or the identity of the principal.[38]

Part (b) of the question introduces the subject of amendments. This term embraces all filings subsequent to the initial financing statement, all of which in some fashion alter the state of the record.[39] Again, we must look to section 9-509 to determine who may file an amendment, since under section 9-510 a filed record is effective only to the extent it is filed by someone entitled to file it.[40] Assuming that this Question does not involve an amendment that either adds collateral or a debtor not previously covered (which would require authorization by the debtor),[41] and also does not involve a

36. *Id.* § 9-102(a)(72)(E).
37. See the discussion in Question 2.
38. *See* R. § 9-503(d).
39. *See id.* § 9-512.
40. *See id.* § 9-510(a).
41. *See id.* § 9-509(a).

termination statement filed by the debtor after failure by a secured party to file a termination statement when obligated to do so, other types of amendments are effective, pursuant to section 9-509(d), only if the "secured party of record" authorizes the filing.

This concept is dealt with in section 9-511, which provides that the secured party of record is the person named as the secured party or the representative of the secured party in the initial financing statement (as may be subsequently modified by filed amendment, including amendments that assign of record the power to affect the record[42]). Thus, under section 9-509(c), it is the person identified on the record as the secured party or its representative that is the person who may authorize (and, thus, render effective) subsequent filings. An example of the significance of the distinction between the secured party and the secured party of record is found in the provision concerning the obligation of the secured party to provide a termination statement under section 9-513. The secured party is the person obligated, but the obligation is stated in terms of "caus[ing] the secured party of record" to send or file the termination statement,[43] since the secured party of record, not the secured party, is the only one with the power to authorize the filing of the termination statement. This illustration also makes the point that a secured party who elects to act by means of a third party secured party of record should select its agent prudently. In the problems posed, Bank *A* is the secured party of record in part (i) and Straw Man is the secured party of record in parts (ii)-(iv).

Q8. Bank *A* and Bank *B* made a $1,000,000 loan to Debtor, secured pursuant to a security agreement providing for a security interest in favor of both banks; each bank advanced half the loan funds. (a) Are both banks' security interests perfected if (i) the filed financing statement identified the secured party as "Bank *A*"? (ii) the filed financing statement identified as secured parties "Bank *A*" and "Bank *B*"? (b) Bank *A* agrees to release its security interest in some of the collateral and Bank *A* files an amendment deleting that collateral. Under each alternative, what consequence to Bank *B*?

A8. In part (a), under the facts of alternative (i), the security interests of both banks are perfected, for the reasons discussed in Question 7, assuming that between them the banks have agreed (however informally) that Bank *A* will serve as Bank *B*'s

42. *See id.* § 9-514(b).
43. *See id.* § 9-513(c).

representative for purposes of the public record. Ordinary agency principles will govern their relationship. Agency for all purposes is not required; agency for the limited purpose of dealing with the public record is sufficient. Based on the statutory provisions discussed in Question 7, the identification of Bank *A* is sufficient to perfect for Bank *B* as well.

Under the facts of alternative (ii), each of the banks has been identified in its own right and clearly the financing statement has satisfied section 9-502(a)(2). Section 9-503(e) expressly validates the provision of more than one secured party name on a financing statement.

Turning to part (b), under alternative (i), Bank *A* has effectively released its security interest in the collateral described in the amendment and terminated the effectiveness of the financing statement to perfect that interest. As Bank *A* is the sole secured party of record, Bank *A*'s filing of the amendment also has the effect of terminating the effectiveness of the financing statement to perfect the security interest of Bank *B* in the deleted collateral.[44] Bank *A* had the statutory authority effectively to file the termination statement and thereby change the legal effect of the public record, even if it lacked actual authority under ordinary agency law. This again points up the need for caution in selecting a representative to act as secured party of record.

Under the facts of alternative (ii), however, both Bank *A* and Bank *B* are secured parties of record (and presumably there has been no agency agreement between them). Section 9-509(d) permits each of multiple secured parties of record to authorize the filing of an amendment (precluding filing offices from requiring all secured parties of record to join in an amendment). The filing by Bank *A*, however, does not affect Bank *B*'s security interest because, under section 9-510(b), "[a] record authorized by one secured party of record does not affect the financing statement with respect to another secured party of record." Thus, in the absence of off-record authorization from Bank *B* empowering Bank *A* to affect the record in its behalf, Bank *B* will not be affected by Bank *A*'s filing.

Q9. Lender, holding a security interest, presents for filing a financing statement that fails to provide a name for the secured party.

44. Had Bank *B* also been a secured party of record, the filing of the amendment would not have affected the financing statement with respect to Bank *B*. *See id.* § 9-510(b). This is illustrated in alternative (ii), discussed below.

(i) Assuming it complies with its statutory obligations, will the filing office reject the financing statement? (ii) If the filing office rejects the tendered financing statement, is the security interest perfected? (iii) If the filing office accepts the tendered financing statement, is the security interest perfected?

A9. Section 9-516(a) continues the former rule[45] to the effect that filing occurs if a record is communicated to the filing office with a tender of the filing fee or acceptance of the record by the filing office; however, subsection (b) provides that filing does not occur if the filing office refuses to accept a record for any of the enumerated reasons. This section must be read together with section 9-520(a), which requires the filing office to refuse acceptance for, and only for, the reasons enumerated in section 9-516.

Subsection (b)(4) states as a ground for rejection the failure of an initial financing statement to provide a name for the secured party of record. Thus, the filing office is obliged to refuse to accept the tendered financing statement. If it properly rejects the financing statement, filing has not occurred and the security interest is not perfected. If the filing office improperly accepts the tendered financing statement, filing does occur, pursuant to section 9-516(a). The financing statement, however, even though it is filed, is not effective and, thus, does not perfect the security interest, because it is not sufficient under section 9-502, which makes a secured party name an element of sufficiency.[46]

Q10. Same facts as Question 9 except that the item lacking in the tendered financing statement is a mailing address for the debtor. Same questions as Question 9.

A10. The answers to parts (i) and (ii) are the same as in Question 9. Section 9-516(b)(5)(A) lists failure to provide a mailing address for the debtor as a ground for rejection. Thus, the filing office is obliged to reject the financing statement and if it does reject, filing does not occur. If, however, the financing statement is improperly accepted, filing does occur and, in this case, it is effective to perfect. This is because under section 9-520(c), a filed financing statement that satisfies the sufficiency elements of section 9-502(a) is effective "even if the filing office is required to refuse to accept it for filing."

This important rule effectuates the policy of making effective filings that, albeit intended to be kept off the record by the rejection

45. *See* U.C.C. § 9-403(1).
46. *See* R. § 9-502(a)(2).

screen mandated on the filing office, nevertheless actually do get on the record and, having at least met the requirements of sufficiency, can perform the Article 9 function of giving notice to searchers. Information such as the debtor's mailing address may be helpful in distinguishing between debtors having the same name, but that information is not a search criterion that might preclude discovery of the financing statement. There is, of course, a balancing of competing interests reflected in this approach. In the case of a very common individual debtor name, against which there might, in a populous state, be hundreds of filings, having distinguishing additional items of information would be a helpful screen to lessen the burden of investigation. On the other hand, making the presence and correctness of this information a condition to effectiveness of the filing would impose a substantial risk of loss on secured parties whose filings are nevertheless discoverable in instances where no prejudice at all is suffered by a searcher and where nonreliance creditors would derive a windfall benefit. The relative unimportance of the debtor's address is also demonstrated by the fact that the obligation to correct on the record post-filing changes in information is limited to situations involving the debtor's name.[47]

Q11. Bank holds a security interest in Debtor's existing and after-acquired inventory. Bank's filed financing statement provides an erroneous address for itself. Subsequent to the Bank's filing, Seller, intending to sell inventory to Debtor on secured credit, retained a security interest and timely filed its own financing statement, searched the files, and sent a notification under section 9-324(b) to Bank at the address provided in Bank's financing statement. The notification never reached Bank. (i) Is Bank's security interest perfected? (ii) Does Bank's security interest have priority over that of Seller? (iii) Would the results in parts (i) and (ii) be different if the error were in Bank's name rather than its address?

A11. Part (i) differs from Question 10, where the financing statement lacked a debtor address; here, the problem is with the secured party's address and it is not lacking but rather is erroneous. The filing office cannot serve as a screening device with respect to this problem since it has no way of knowing whether a given address is correct or incorrect. Addresses (of either debtor or secured party) are not elements of sufficiency under section 9-502; they are, however,

47. *See id.* § 9-507(b)-(c).

elements that if lacking would constitute grounds for rejection.[48] Even were the error rule of section 9-506 applicable to items that are not elements of sufficiency,[49] addresses are not search criteria, so it is hard to imagine a case where an address error can be "seriously misleading" in such a general sense that the consequence should be ineffectiveness for all purposes. This does not mean, however, that the error may never have consequences, merely that the error will not render the financing statement ineffective to perfect. Under appropriate circumstances, an estoppel might be justified to protect a particular searcher who was misled and is deserving of protection. Bank's security interest is perfected.

Under the 'first to file or perfect' rule, Bank would have priority. Seller, however, asserts purchase money superpriority. Under section 9-324(b), not only must Seller send its notification to Bank, but Bank must also receive it.[50] In this case, Bank did not physically receive the notification because it had provided an incorrect address for itself. Seller did "send" the notification in that, under section 9-102(a)(74)(A), using "any address reasonable under the circumstances" satisfies the definition. It certainly was reasonable for the Seller to rely on the address provided on the public record by Bank. Bank "received" the notification because, under section 1-201(26)(b), a person receives a notification when it is duly delivered at any "place held out by him as the place for receipt of such communications."[51]

Part (iii), where Bank's name rather than address was incorrect, differs from Question 9, where the secured party's name was altogether lacking; here, it was provided but was incorrect. Again, the filing office cannot in such circumstances perform a screening function, so the financing statement gets on the record despite the name error. Unlike part (i), however, the secured party name is an element of sufficiency under section 9-502(a)(2). Section 9-503, which offers some guidance in connection with debtor names, is not applicable. Thus, we might fall back on section 9-506—the "seriously misleading" rule.[52] An easier solution is available, however. Although Bank's error prevented physical receipt of the notification sent by Seller, it is most likely that Seller, as in part (ii), did satisfy the

48. *See id.* § 9-516(b)(4), (b)(5)(A).
49. See the discussion in Question 2.
50. *See* R. § 9-324(b)(2)-(3).
51. *See id.* § 9-516 cmt. 5.
52. See the discussion in Question 2.

requirements of section 9-324. Even if the name error for some reason does not fit neatly within the "send" and "receive" definitions discussed above, however, a court would likely estop Bank from asserting its priority vis-à-vis Seller, who was prejudiced by Bank's error.

Q12. Secured party filed a financing statement on a nonstandard written form. In the space for the debtor's name, the secured party typed "Elton John." Elton John is the debtor's correct name. (i) Assuming it complies with its statutory obligation, will the filing office refuse to accept the financing statement? (ii) If the filing office rejects the financing statement, is the security interest perfected? (iii) If the filing office accepts the financing statement, is the security interest perfected?

A12. The filing office will refuse to accept the financing statement on either of two grounds: section 9-516(b)(5)(B) requires that the financing statement "indicate whether the debtor is an individual or an organization" or, if it does indicate that the debtor is an individual, section 9-516(b)(3)(C) requires that such a financing statement identify the debtor's last name.

These, and the other refusal criteria specified in section 9-516, are designed to make the filing office intake and indexing tasks more efficient, make the database more accessible, and allocate to filers, not filing office personnel, the task of providing the required data in a way that facilitates those goals. Search logic for organization names differs from that for individual names, and individual names are searched under the last name. Designation of the nature of this data should be the responsibility of the filer, and the filing office personnel should not be required (or permitted) to make determinations of this sort. Electronic filing produces these results automatically. With a view to achieving these results even when written (paper) forms are used, national standard forms satisfying the requirements of Revised Article 9 were developed and put into the statute. Relying on practicality rather than coercion to encourage their use, the statute does not make their use mandatory. Section 9-521, however, does prohibit filing offices from refusing to accept them on the basis of form.[53]

Returning to the problem presented in Question 12, the national

53. The predecessor transition period forms, on which the statutory forms were based, are explained in detail in Harry C. Sigman, *Putting Uniformity into—and Improving the Operation of—the Uniform Commercial Code: The New National Financing Statement Form*, 51 BUS. LAW. 721 (1996).

standard written form would have satisfied both of the above-mentioned requirements as it provides separate debtor name boxes for individuals and organizations, and it provides separate boxes for an individual's first and last names. Thus, filling in that form automatically would have complied with these requirements. A nonstandard form was used, however. If the filing office properly refuses to accept the financing statement, filing does not occur and the security interest is not perfected. If the filing office improperly accepts the financing statement, filing has occurred and, if the financing statement is otherwise sufficient, it is effective under section 9-520(c). If the financing statement was indexed under Elton, rather than under John, however, it would obviously be undiscoverable. That is the reason section 9-516 requires the filing office to refuse to accept the tendered financing statement when the filer fails to specify the last name of an individual debtor.[54]

Q13. *D* Corp., a California corporation, gave a security interest in its existing and after-acquired inventory and accounts to Financer. Financer presents for filing a financing statement that indicates Nevada as *D* Corp.'s state of organization. (i) The Nevada filing office rejects because it knows, from the corporate identification number given on the financing statement, that the information about the debtor's state of organization is incorrect. Is the financing statement effective to perfect Financer's security interest? (ii) The California filing office rejects because the financing statement indicates that *D* Corp. was organized in Nevada. Is the financing statement effective to perfect Financer's security interest? (iii) The California filing office accepts and files the financing statement. *D* Corp. approaches Bank for financing and Bank sends the California filing office a search request. In response thereto, the listing shows Financer's financing statement. Bank, however, ignores that financing statement because it is looking for filings against the *D* Corp. that is a California corporation, not corporations organized elsewhere that happen to have the same name. Bank takes a security interest in *D* Corp.'s existing and after-acquired inventory and accounts, files an effective financing statement in California, and advances funds. Which security interest, Financer's or Bank's, has priority as to the inventory?

A13. (i) The refusal by the Nevada filing office to accept Financer's financing statement was not authorized under the statute;

54. See Question 14 for a discussion of misindexing.

it was not based on any of the grounds for refusal enumerated in section 9-516(b). Nothing in the Code authorizes the filing office to inquire into or consider the accuracy or correctness of any information provided in a record presented for filing.[55] Section 9-520(a) makes clear that a filing office may not refuse to accept a record on any ground other than those enumerated in section 9-516(b). Financer's financing statement was communicated to the Nevada filing office and the filing fee was tendered, so, despite the wrongful rejection, the financing statement is effective as a filed record.[56] It will probably do Financer no good, however, because, under section 9-301(1), the debtor's location is the proper state in which to file, and, under section 9-307(e), the location of a registered organization is the state in which it is organized.

(ii) Turning to the rejection by the California filing office, the analysis presented above indicates the wrongfulness of the rejection and the consequent filing notwithstanding the wrongful rejection. Now, however, the filing is in the right state. Thus, the financing statement is effective to perfect Financer's security interest.

(iii) The erroneousness of the information about the state of organization does not render the financing statement undiscoverable. In fact, it was reported by the California filing office in response to a search request. Because this case involves information described in section 9-516(b)(5) that was incorrect at the time the financing statement was filed, section 9-520(c) makes section 9-338 applicable. Under section 9-338(1), Financer's security interest is subordinate to that of Bank to the extent that Bank gave value in reasonable reliance upon the incorrect information. It is likely that a court would find Bank behaved reasonably in not investigating Financer's financing statement, especially if *D* Corp. is a common name and there might well be numerous filings listed against *D* Corps. that are organized elsewhere than in California. Since the vulnerability of the filing secured party is already very limited—no risk of ineffectiveness, just of subordination, and then only to a very small class of persons who actually searched the public record, actually found the financing statement, and actually relied on the erroneous information—the courts ought not erect much of an additional barrier by a rigorous application of the reasonableness of the reliance. Section 9-338 is a rule designed to protect reliance competitors who are actually

55. *See* R. § 9-516 cmt. 3.
56. *See id.* § 9-516(d).

prejudiced by the secured party's error, while at the same time not placing an undue burden on all transactions (and inappropriate risk of loss on all secured parties), since this particular category of information (while helpful to searchers in some contexts) is rarely likely to be pivotal.

Q14. Bank obtained a security interest and filed a financing statement correctly identifying "Weise, Steven O." as the debtor. The filing office, however, misindexes it under "Weiss, Steven O." (i) Is Bank's security interest perfected? (ii) In response to a later search request from Financer under the debtor's correct name, the filing office reports that no financing statements are on file against that debtor. Financer perfects a security interest and advances funds. Which security interest, Bank's or Financer's, has priority? What, if anything, could the losing party have done to avoid the loss?

A14. Bank's security interest is perfected. Section 9-517, carrying forward the rule under Former section 9-401, provides that the "failure of a filing office to index a record correctly does not affect the effectiveness of the record." Bank's security interest has priority under the 'first to file or perfect' rule. Financer could have done nothing more, in terms of the public record, than it did; it searched under the correct debtor name. Bank, of course, could have discovered the misindexing by conducting a post-filing search, a practice followed by some secured parties. The statute does not require this, however, because errors are relatively rare and it would make no sense to require, by putting the opposite rule into effect, every filing of a financing statement to be followed by a post-filing search. Besides adding to the cost of every secured financing, this inundation would require the reallocation of scarce filing office resources and would likely impede prompt and accurate filing office intake processing, indexing, and searching. The advent of free remote access electronic searching of computerized indices might suggest reconsideration of this rule.

Q15. The filing office received in the mail a financing statement naming Duncan as debtor and Firstbank as secured party, covering Duncan's inventory and accounts. In the course of processing the financing statement in the filing office, the financing statement is accidentally stapled to another financing statement naming someone else as debtor. Consequently, Firstbank's financing statement is never fully processed and never entered into the index. (i) Is Firstbank's financing statement effective? (ii) In response to Credit Union's search request under Duncan's correct name, the

filing office reports that there are no financing statements on file naming Duncan as debtor. Credit Union obtains a security interest in Duncan's inventory and accounts, files an effective financing statement, and advances funds. Which security interest, Firstbank's or Credit Union's, has priority? What, if anything, could the losing party have done to avoid the loss?

A15. Firstbank, as in Question 14, made an effective filing and its security interest was perfected and has priority under the 'first to file or perfect' rule. Assume that Firstbank's check was processed and that Firstbank did not request an acknowledgement of the filing; it would have had no reason to even suspect the existence of a problem. Nothing obliges a filer to request an acknowledgement. Under section 9-523(b), the filing office is required to acknowledge all filings presented other than by means of a written record (e.g., electronically), but under subsection (a), an acknowledgment of the filing of a written record is required only if it is requested by the filer. If Firstbank had requested and failed to receive an acknowledgement of its filing, one might argue that it was put on notice that something went awry and it should have followed up. On the other hand, particularly in the case, for example, of a small seller who only occasionally sells on a secured basis and acts without counsel, a failure to discover the error for lack of an effective follow-up system should not ordinarily result in loss of perfection. Nothing in the Code expressly requires such due diligence, and adoption of a rule of automatic subordination for failure to follow up on each failure to receive a requested acknowledgement would be counterproductive. Even an institutional lender might not be expected to track all filings for which it does not receive a notification of rejection, particularly since under section 9-520(b) filing offices are now expressly obliged to promptly communicate the "fact of and reason for the refusal." In this case, we did not have a refusal to accept but rather something more akin to a misindexing, although likely in this case the financing statement never got indexed at all. Generally, Part 5 puts the risk of loss due to filing office error on the later party, rather than on the secured party who properly communicates a sufficient record to the filing office, and courts should be extremely cautious about using estoppel to undermine the certainty and efficiency provided by this approach. There was nothing Credit Union could have done to avoid the loss.

Q16. The filing office received a financing statement in written form, with debtor *A*'s name correctly presented but debtor *B*'s name

scribbled illegibly. Is the financing statement effective with respect to either, both, or neither debtor? Does the answer depend on what the filing office does with it? What is the filing office supposed to do with it?

A16. Section 9-503(e) states that a financing statement may provide the name of more than one debtor, and section 9-520(d) states that, in such a case, Part 5 "applies as to each debtor separately." As to *A* there is no problem; therefore, the filing office may not refuse to accept the financing statement as to *A*, and the financing statement is effective as to *A*. As to *B*, the illegibility constitutes a ground for refusal to accept. Section 9-516(c)(1) provides that "a record does not provide information if the filing office is unable to read or decipher the information." Thus, no debtor name was provided as to *B*, requiring rejection[57] and precluding an effective filing as to *B*. Thus, the financing statement should be accepted as to *A* and rejected as to *B*.

The foregoing answers as to effectiveness do not depend on what the filing office does. If it improperly rejects the financing statement as to *A*, it is nevertheless effective, and if the filing office improperly accepts the financing statement as to *B* (hard to imagine because it would be impossible to index a name that is illegible), the financing statement would still be ineffective—unless the filing office, treating the name as legible enough to index it, came up with a name so close that, treated as an erroneous name under the rules discussed in Question 1 above, it was not "seriously misleading."

Q17. Lender filed a financing statement on July 24, 2001. Four years later, on July 24, 2005, Lender filed a continuation statement. (a) When does the effectiveness of the financing statement lapse? Does the answer depend on what the filing office does with the continuation statement? What is the filing office supposed to do with it? (b) Would any of the foregoing answers be different if Lender had filed the continuation statement on July 31, 2006?

A17. The effectiveness of the financing statement lapses on July 24, 2006. The continuation statement was filed prematurely, prior to the commencement of the permitted filing period. Section 9-515(d), continuing the rule under prior law,[58] states: "A continuation statement may be filed only within six months before the expiration of the five-year period . . . ." Section 9-515(e) provides that

57. *See id.* § 9-516(b)(3)(A).
58. *See* U.C.C. § 9-403(3).

effectiveness of an initial financing statement continues "upon timely filing of a continuation statement," and section 9-515(c) provides that the "effectiveness of a filed financing statement lapses on the expiration of the period of its effectiveness unless before the lapse a continuation statement is filed pursuant to subsection (d)." Thus, even if the filing office accepts the continuation statement, it is not effective to extend the duration of the effectiveness of the financing statement. Section 9-516(b)(7) obliges the filing office to refuse to accept a continuation statement "not filed within the six-month period prescribed by Section 9-515(d)."

(b) The statutory provisions make no distinction between premature and tardy presentations of continuation statements; both are required to be rejected and neither is effective even if accepted.

It should be noted that receipt by the filing office of a timely filed continuation statement is one of the few circumstances when the filing of an amendment triggers filing office action other than simply adding the filed record to the files. On receipt of other types of amendments, the filing office simply adds the amendment to the public record (in some cases also adding information, such as, for example, adding an additional secured party name by reason of a partial assignment, or adding (but not substituting) a changed debtor name), but does not delete anything from the public record and otherwise takes no action. In the case of a timely filed continuation statement, the filing office takes action based on the filing—it extends the lapse date, thereby deferring any purge program that would otherwise delete the financing statement.

Section 9-522(a) requires the filing office to "maintain a record of the information provided in a filed financing statement for at least one year after the effectiveness of the financing statement has lapsed ... with respect to all secured parties of record." Section 9-519(g) prohibits the filing office from removing "a debtor's name from the index until one year after the effectiveness of a financing statement naming the debtor lapses ... with respect to all secured parties of record." Thus, it is lapse that triggers the possibility of deletion (and, thus, discoverability) and the continuation statement defers lapse.

The overall filing system provided for under Revised Article 9, despite the deletion of the requirement of signatures on filings and because of a more limited and more clearly defined role of the filing office, results in a more efficient, reliable, and uniform system in which searchers get more information and the interests of all users are better-served.

As is the case with all tendered records, the filing office has no way of knowing in whose behalf a record is tendered, whether the filing is authorized, and whether it was tendered by mistake. In the case of a wrongfully accepted (or mistakenly filed) continuation statement, the worst that can happen is that a financing statement that actually lapsed appears to have been continued, thus deferring the potential deletion date—it continues to be discoverable. Contrast this situation with a termination statement tendered by mistake or by a miscreant debtor. Under former law, the filing office would have, immediately upon receipt of the termination statement, deleted the financing statement from its active files and ceased reporting it to searchers.[59] While this should not (except perhaps in the case of a termination sent by the secured party by mistake[60]) result in the de-perfection of the security interest, it would at the very least have resulted in litigation with any subsequent filers (or a trustee in bankruptcy). Under Revised Article 9, the filing office does not delete anything from the public record upon receipt of a termination statement; instead, that filing is simply added to the record and reported to subsequent searchers. Under Revised Article 9, the filing office is taken out of the business of making determinations concerning the effect of a filing, and searchers get more information.

Q18. On November 19, 2001, Debtor and Financer entered into a written agreement for the sale of all Debtor's existing and future accounts. A financing statement was filed on that day, but no continuation statement was filed subsequently. On November 1, 2006, LC, a creditor of Debtor, acquired a judicial lien on two of the sold accounts. (i) On November 1, 2006, who has the senior claim to the two accounts, LC or Financer? (ii) On November 15, 2006, the account debtor on Account #1 paid to Financer the amount due on the account. Who has the senior claim to the payment, LC or Financer? (iii) On December 1, 2006, who has the senior claim to Account #2, LC or Financer? (iv) On December 12, 2006, the account debtor on Account #2 paid to Financer the amount due on the account. Who has the senior claim to the payment, LC or Financer?

A18. (i) On November 1, 2006, Financer, not Debtor, owned the accounts. Nevertheless, Article 9 is applicable pursuant to section 9-109(a)(3), and the definition of "security interest" in section

59. UCC section 9-407(2) provided for reporting of "presently effective" financing statements. *Cf.* R. § 9-523.

60. *See, e.g.*, Crestar Bank v. Neal (*In re* Kitchin Equip. Co.), 960 F.2d 1242 (4th Cir. 1992).

1-201(37) includes the interest of a buyer of accounts. Section 9-318(a), in an effort to make clear that *Octagon Gas Systems, Inc. v. Rimmer*,[61] does not take the desired approach,[62] expressly states that the seller of accounts does not retain any legal or equitable interest in the sold accounts. Section 9-318(b), however, provides:

> For purposes of determining the rights of creditors of, and purchasers for value of an account or chattel paper from, a debtor that has sold an account or chattel paper, while the buyer's security interest is unperfected, the debtor is deemed to have rights and title to the account or chattel paper identical to those the debtor sold.

On November 1, 2006, Financer's interest was perfected by a still effective filing. On that date, therefore, Debtor had no interest in the accounts and the levy caught nothing. Financer has the senior claim.

(ii) On November 15, 2006, Financer was still perfected and it had priority in the payment, the proceeds of the account as to which it had priority on that date as well. Since Debtor had no interest in the payment, the levy didn't catch that either. (iii) On December 1, 2006, the effectiveness of Financer's financing statement has lapsed. The consequences of lapse are provided in section 9-515(c). Retroactive effect of lapse is not provided vis-à-vis anyone other than a purchaser. Hence, even on December 1, 2006, despite the lapse, Financer prevails over LC, whose claim is based on a pre-lapse levy. This answer might vary depending on the nature of a judicial lien in a particular state—if under local law it is effective as a continuing levy, i.e., treated as a fresh levy each day, LC would prevail, although not based on retroactivity of the lapse, but rather on the basis that it levied after lapse; on that basis, LC would prevail under section 9-317(a)(2). (iv) Same answer as part (iii), assuming that under the local law of the state in question LC's judicial lien on the account reaches the payment by the account debtor.

Q19. On November 19, 2001, Debtor and Financer entered into a written agreement for the sale of all Debtor's existing and future accounts. A financing statement was filed on that day, but no continuation statement was filed subsequently. On November 1, 2006, Factor bought two of the sold accounts from Debtor and filed a financing statement against Debtor covering the two accounts. (i) On November 1, 2006, who has the senior claim to the two accounts, Financer or Factor? (ii) On November 15, 2006, the account debtor on Account #1 paid to Financer the amount due on the account. Who

61. 995 F.2d 948 (10th Cir. 1993).

62. *See* PEB COMMENTARY NO. 14, ELECTRONIC FILING UNDER ARTICLE 9 (1996).

has the senior claim to the payment, Financer or Factor? (iii) On December 1, 2006, who has the senior claim to Account #2, Financer or Factor? (iv) On December 1, 2006, who has the senior claim to the November 15 payment made on Account #1, Financer or Factor? (v) On December 12, 2006, the account debtor on Account #2 paid to Financer the amount due on the account. Who has the senior claim to the payment, Financer or Factor?

A19. - (i) Same analysis as for part (i) of Question 18. As Debtor had nothing to sell to Factor, Financer has the senior—only—claim to the two accounts. (ii) Again, same analysis as for part (ii) of Question 18. Financer owned the account free of any interest therein of Debtor, who had thus sold nothing to Factor. The same, therefore, holds true for the payment on the account.

(iii) At this point in time, Financer's security interest in Account #2 has lapsed. Thus, under section 9-318(b), Debtor is deemed to have rights identical to those it had previously sold, meaning ownership of Account #2, including the power to sell it again. Section 9-515(c) provides that the effect of the lapse of the effectiveness of Financer's financing statement is retroactive as against a purchaser for value; that is, Financer's security interest not only became unperfected on the lapse date but is "deemed never to have been perfected" as against Factor.

(iv) The fact that the effectiveness of Financer's financing statement has lapsed after it collected and applied the payment on Account #1 should make no difference. That payment has discharged both Financer's security interest and that of subordinate interests therein and from that moment on ceased to be collateral as to which Article 9 was applicable. The subsequent loss of perfection, even if retroactive as to property that continued to be collateral, should not enable Factor to force the disgorgement of payments received by Financer at a time when Financer was perfected.

(v) Even if Financer is at this point in time junior with respect to Account #2 (as concluded in part (iii)), Financer might nevertheless prevail with respect to the payment on that account from the account debtor. Presumably the account debtor paid the amount due on the account by means of a check, a negotiable instrument. Under section 9-331, successor provision to Former section 9-309, Article 9 does not limit the rights of a holder in due course of a negotiable instrument, and the filing of a financing statement does

not give notice of a claim to such a holder.[63] Factor's filed financing statement does not of itself constitute notice to Financer sufficient to deprive it of holder in due course status. The definition of good faith, found in section 9-102(a)(43), now includes, in addition to honesty in fact, the objective component of "the observance of reasonable commercial standards of fair dealing." There would not appear to be any question of Financer's good faith, as there is certainly no practice in the industry to continuously search for subsequent filers when simply collecting out accounts previously purchased.

Moreover, under a new provision, section 9-330(d), Financer may prevail as to the check even if it is not a holder in due course (for example, if it had notice or knowledge of a security interest in the account taken subsequent to its purchase of the account), provided it gave value and took possession of the check in good faith (same standard as required for holder in due course status) "and without knowledge that the purchase violates the rights of the secured party." In this case, factual determinations would have to be made. Even if Financer knew of Factor's acquisition of Account #2 (as contrasted with the taking by a lender of a security interest), it would not necessarily have knowledge of a violation of Factor's rights; although Factor bought the accounts, it apparently allowed the Debtor to continue to collect, and possibly to use, the proceeds.

Q20. Debtor signed a security agreement in favor of Bank. Sometime later, Debtor discovered that the financing statement filed by Bank in connection with the transaction covers tax refunds. In the honestly held belief that the security agreement did not cover tax refunds, Debtor filed a correction statement that properly identified the financing statement to which it related, indicated that it was a correction statement, provided the basis for Debtor's belief that the financing statement is inaccurate, and indicated that the indication of collateral in the financing statement should be amended to delete the reference to tax refunds. Is Bank's security interest perfected with respect to a tax refund received by Debtor shortly thereafter? Does the answer depend on the description of collateral set forth in the security agreement?

A20. The correction statement appears to be sufficient under section 9-518(b). Debtor had a right to file it under section 9-518(a). Under section 9-518(c), however, the "filing of a correction statement does not affect the effectiveness of an initial financing statement."

63. *See* R. § 9-331(a), (c).

Thus, if Bank has a security interest in the tax refund, the financing statement is effective to perfect. Whether Bank is entitled to file the financing statement covering tax refunds depends on whether Debtor had authorized the filing. This might be automatic by virtue of coverage of tax refunds in the security agreement or it might derive from some other record authenticated by Debtor. Even a financing statement the filing of which is authorized, however, does not expand the scope of collateral covered by a security interest. Whether Bank has a security interest in the tax refund depends on the collateral description in the security agreement,[64] not on the indication of collateral in the financing statement.

64. *See id.* § 9-203(b).