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UNIFORM COMMERCIAL CODE

REVISED ARTICLE 9, SECURED TRANSACTIONS (1998)

- A Summary -

The Uniform Commercial Code has eleven substantive articles. Article 9, Secured Transactions, may be the most important of the eleven. Article 9 provides the rules governing any transaction (other than a finance lease) that couples a debt with a creditor's interest in a debtor's personal property. If the debtor defaults, the creditor may repossess and sell the property (generally called collateral) to satisfy the debt. The creditor's interest is called a "security interest." Article 9 also covers certain kinds of sales that look like a grant of a security interest.

The operation of Article 9 appears deceptively simple. There are two key concepts: "attachment" and "perfection." These terms describe the two key events in the creation of a "security interest." Attachment generally occurs when the security interest is effective between the creditor and the debtor, and that usually happens when their agreement provides that it take place. Perfection occurs when the creditor establishes his or her "priority" in relation to other creditors of the debtor in the same collateral. The creditor with "priority" may use the collateral to satisfy the debtor's obligation when the debtor defaults before other creditors subsequent in priority may do so. Perfection occurs usually when a "financing statement" is filed

in the appropriate public record. Generally, the first to file has the first priority, and so on.

Article 9 relies on the public record because it provides the means for creditors to determine if there is any security interest that precedes theirs—a notice function. A subsequent secured creditor cannot complain that his or her grant of credit was made in ignorance of the prior security interests easily found in the public record, and cannot complain of the priority of the prior interests as a result. Every secured creditor has a priority over any unsecured creditor.

The somewhat simple description in the prior paragraphs should not mislead anyone. Article 9 is not simple. There are substantial exceptions to the above-stated perfection rule, for example. Filing is not the only method for perfection. Much depends upon the kind of property that is collateral. Possession of collateral by the secured party is an alternative method of perfection for many kinds of collateral. For some kinds of property, control (a defined term) either perfects the interest or provides a better priority than filing does. There are kinds of transactions for which attachment is perfection. Priority is, also, not always a matter of perfecting a security interest first in time.

The following numbered topics highlight Article 9 as revised in 1998. They are not a treatise on Revised Article 9, but are a schematic summary of its relevant changes.

1. The Scope Issue. The 1998 revision expands the "scope" of Article 9. What this

means literally is that the kinds of property in which a security interest can be taken by a creditor under Article 9 increases over those available in Article 9 before revision. Also, certain kinds of transactions that did not come under Article 9 before, now come under Article 9. These are some of the kinds of collateral that are included in Revised Article 9 that are not in original Article 9: sales of payment intangibles and promissory notes; security interests created by governmental debtors; health insurance receivables; consignments; and commercial tort claims. Nonpossessory, statutory agricultural liens come under Article 9 for determination of perfection and priority, generally the same as security interests come under it for those purposes.

2. Perfection. Filing a financing statement remains the dominant way to perfect a security interest in most kinds of property. It is clearer in Revised Article 9 that filing a financing statement will perfect a security interest, even if there is another method of perfection. "Control" is the method of perfection for letter of credit rights and deposit accounts, as well as for investment property. Control was available only to perfect security interests in investment property under old Article 9. A creditor has control when the debtor cannot transfer the property without the creditor's consent. Possession, as an alternative method to filing a financing statement to perfect a security interest, is the only method for perfecting a security interest in money that is not proceeds of sale from property subject to a security interest. Automatic perfection for a purchase money security interest is increased from ten days in old Article 9 to twenty days in Revised Article 9. Attachment of a purchase money security interest is perfection, at least for the twenty-day period. Then another method of perfection is necessary to continue the perfected security interest.

However, a purchase money security interest in consumer goods remains perfected automatically for the duration of the security interest.

3. Choice of Law. In interstate secured transactions, it is necessary to determine which state's laws apply to perfection, the effect of perfection and the priority of security interests. It is particularly important to know where to file a financing statement. The 1998 revisions to Article 9 make two fundamental changes from old Article 9. In old Article 9, the basic rule chooses the law of the state in which the collateral is found as the law that governs perfection, effect of perfection, and a creditor's priority. In Revised Article 9, the new rule chooses the state that is the location of the debtor. Further, if the debtor is an entity created by registration in a state, the location of the debtor is the location in which the entity is created by registration. If an entity is a corporation, for example, the location of the debtor is the state in which the corporate charter is filed or registered. In old Article 9, the entity that is a debtor is located in the state in which it has its chief executive office. These changes in basic choice of law rules will change the place in which a financing statement is filed in a great many instances from the place it would have been filed under old Article 9. At the same time, the location of the debtor establishes a more certain place to perfect than the old rule does. Collateral shifts location much easier than the debtors do.

4. The Filing System. Improvements in the filing system in the 1998 revisions to Article 9 include a full commitment to centralized filing—one place in every state in which financing statements are filed, and a filing system that escorts filing from the world of filed documents to the world of electronic communications and records.

Under Revised Article 9, the only local filing of financing statements occurs in the real estate records for fixtures. Fixtures are items of personal property that become physically part of the real estate, and are treated as part of the real estate until severed from it. It is anticipated that electronic filing of financing statements will replace the filing of paper. Paper filing of financing statements is already disappearing in many states in 1998, as Revised Article 9 becomes available to them. Revised Article 9 definitions and provisions allow this transition from paper to electronic filing without further revision of the law. Revised Article 9 makes filing office operations more ministerial than old Article 9 did. The office that files financing statements has no responsibility for the accuracy of information on the statements and is fully absolved from any liability for the contents of any statements received and filed. Financing statements may, therefore, be considerably simplified. There is no signature requirement, for example, for a financing statement.

5. Consumer Transactions. Revised Article 9 makes a clearer distinction between transactions in which the debtor is a consumer than prior Article 9 did. Enforcement of a security interest that is included in a consumer transaction is handled differently in certain respects in the 1998 revisions to Article 9 than it was pre-1998. Examples of consumer provisions are: a consumer cannot waive redemption rights in a financing agreement; a consumer buyer of goods who pre-pays in whole or in part, has an enforceable interest in the purchased goods and may obtain the goods as a remedy; a consumer is entitled to disclosure of the amount of any deficiency assessed against him or her, and the method for calculating the deficiency; and, a secured creditor may not accept collateral as partial satisfaction of a consumer obligation, so that choosing strict foreclosure as a remedy means that no deficiency may be

assessed against the debtor. Although it governs more than consumer transactions, the good faith standard becomes the objective standard of commercial reasonableness in the 1998 revisions to Article 9.

6. Default and Enforcement. Article 9 provisions on default and enforcement deal generally with the procedures for obtaining property in which a creditor has a security interest and selling it to satisfy the debt, when the debtor is in default. Normally, the creditor has the right to repossess the property. Revised Article 9 includes new rules dealing with "secondary" obligors (guarantors), new special rules for some of the new kinds of property subject to security interests, new rules for the interests of subordinate creditors with security interests in the same property, and new rules for aspects of enforcement when the debtor is a consumer debtor. These are some of the specific new rules: a secured party (creditor with security interest) is obliged to notify a secondary obligor when there is a default, and a secondary obligor generally cannot waive rights by becoming a secondary obligor; a secured party who repossesses goods and sells them is subject to the usual warranties that are part of any sale; junior secured creditors (subsequent in priority) and lienholders who have filed financing statements, must be notified when a secured party repossesses collateral; and, if a secured party sells collateral at a low price to an insider buyer, the price that the goods should have obtained in a commercially reasonable sale, rather than the actual price, is the price that will be used in calculating the deficiency.

Founded in 1892, the National Conference of Commissioners on Uniform State Laws is a confederation of state commissioners on uniform laws. Its membership comprises more than 300 attorneys, judges, and law professors, who are appointed by each of the 50 states, the District of Columbia, Puerto Rico, and the U.S. Virgin Islands, to draft uniform and model state laws and work toward their enactment.

UNIFORM COMMERCIAL CODE (UCC)

REVISED ARTICLE 9 – SECURED TRANSACTIONS

– Short Summary –

UCC Article 9 – Secured Transactions governs transactions in which a creditor takes a security interest in specific property of a debtor, allowing the creditor to take the property in the event the debtor defaults on the debt. Revised Article 9 in 1998 provides for these changes in Article 9: 1) the scope of Article 9 is expanded to include kinds of property such as deposit accounts, health care receivables and commercial tort claims, that were excluded in original Article 9; 2) perfection of a security interest by control is available not only for investment property, but also deposit accounts and letter of credit rights;

3) the location of the debtor rather than the location of the collateral determines where a security interest perfects; 4) a simplified and unified system of filing financing statements in one place in each state to perfect security interests replaces the original filing system which allowed certain local filing; 5) consumers obtain certain rights that were not available in original Article 9, such as specific disclosure of any deficiency rights the creditor may have; and, 6) new rules for enforcement, such as a requirement that a creditor notify a secondary obligor when repossessing

goods subject to a security interest. UCC Article 9, then, becomes updated and prepared for the next century.

A Few Facts About

REVISED UCC ARTICLE 9, SECURED TRANSACTIONS (1998)

PURPOSE: Updates UCC Article 9, last revised in 1972 and adopted in every state. Article 9 provides a statutory framework that governs secured transactions — transactions which involve the granting of credit secured by personal property.

ORIGIN: Completed by the Uniform Law Commissioners, in conjunction with the American Law Institute, in 1998.

ENDORSED BY: American Bar Association

STATE

ADOPTIONS: Arizona *

Maryland *

Montana * Nebraska *

Nevada *

1999

INTRODUCTIONS: California

Hawaii

Illinois

Indiana

Louisiana

Maine Missouri

Oklahoma

Texas

Vermont

West Virginia

For any further information regarding the Revision of UCC Article 9, Secured Transactions, please contact John McCabe or Katie Robinson at 312-915-0195.

* 1999 Enactment

(6/1/99)

WHY STATES SHOULD ADOPT
UNIFORM COMMERCIAL CODE ARTICLE 9 – SECURED TRANSACTIONS

Trillions of dollars of commercial and consumer credit are granted each year in secured transactions under Article 9 of the Uniform Commercial Code — a manufacturer finances the acquisition of machinery and raw materials, a retailer finances inventory, a consumer finances furniture for a new house. The manufacturer, the retailer, and the consumer all depend upon Article 9 of the Uniform Commercial Code to make it possible for them to obtain the credit they need. Their creditors get assurance, in the form of the collateral that secures the granting of credit, that it will cushion the risk of default in the event the debtor does not pay the debt. Article 9 of the Uniform Commercial Code is absolutely necessary to economic function in the United States. It is the crankshaft for the American economic engine, and it is the envy of the rest of the world, which often struggles with the mechanics of credit granting and enforcement of creditor's rights.

Major revisions to Article 9 were completed in 1998. These revisions bring Article 9 into the 21st Century. There are many reasons that Revised Article 9 should be adopted in every state.

Technology. Paper-based transactions are giving way to electronic transactions. Revised Article 9 makes way for this revolution.

Volume. Article 9 was first proposed in 1951. Its last update was in 1972. Since 1972

the volume of commerce and the volume of credit has increased exponentially. Volume of secured transactions increases proportionately and directly with increase in economic activity in the United States. The filing system revisions are particularly necessary to meet the problem of increased volume.

New Collateral. New kinds of property and transactions have been developed since Article 9 was last amended. The scope of Article 9 expands to keep up and the 1998 revisions meet the needs for collateral into the new millennium. Examples of specific new collateral are deposit accounts and health insurance receivables.

Certainty of Perfection. Uncertainties about where to perfect a security interest under old Article 9 are overcome by the new basic rule in the 1998 revisions that makes the location of the debtor the place where the creditor will perfect the security interest.

New Liens. Statutory, non-possessory liens have proliferated since Article 9 was originally approved. Such liens represent a risk for creditors, and a potential conflict with security interests in collateral, if there is no public notice of their existence. Article 9 includes certain statutory, non-possessory liens for the purposes of providing public notice and setting priorities between creditors.

Clarification of Rules. Over time, provisions of Article 9 have been interpreted by courts, sometimes in conflicting ways. Some decisions deal with issues that were not expressly addressed in original Article 9. The result is ambiguity in the application of some rules. The revisions to Article 9 address and cure the accrued ambiguity

problems.

Consumer Impact. Revised Article 9 addresses consumer issues that were not addressed in original Article 9.

Commitment to Uniformity. Amendments to Article 9 from state to state have created differences that impair interstate transactions. The revisions address specific kinds of secured transactions in oil and gas and agriculture in an effort to re-establish uniformity of law governing these kinds of transactions.

UNIFORM COMMERCIAL CODE, ARTICLE 9, SECURED TRANSACTIONS
THE 1998 REVISIONS
AN INTRODUCTION

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The operation of Article 9 appears deceptively simple. There are two key concepts: "attachment" and "perfection." These terms describe the two key events in the creation of a "security interest." Attachment generally occurs when the security interest is effective between the creditor and the debtor, and that usually happens

when their agreement provides that it takes place. Perfection occurs when the creditor establishes his or her "priority" in relation to other creditors of the debtor in the same collateral. Perfection occurs usually when a "financing statement" is filed in the appropriate public record. Generally, the first to file has the first priority, and so on.

Article 9 relies on the public record because it provides the means for creditors to determine if there is any security interest that precedes theirs—a notice function. A subsequent secured creditor cannot complain that his or her grant of credit was made in ignorance of the prior security interests that the record displays, and cannot complain of the priority of the prior interests as a result. Every secured creditor has a priority over any unsecured creditor.

The somewhat simple description in the prior paragraphs should not mislead anyone. Article 9 is not simple. There are substantial exceptions to the above-stated perfection rule, for example. Filing is not the only method for perfection. Much depends upon the kind of property that is collateral. Possession of collateral by the secured party is an alternative method of perfection for many kinds of collateral. For some kinds of property, control (a defined term) either perfects the interest or provides a better priority than filing does. There are kinds of transactions for which attachment is perfection. Priority is, also, not always a matter of perfecting a security interest first in time.

The following chapters of this backgrounder are meant to suggest and highlight Article 9 as revised in 1998. They are not a treatise on revised Article 9, but are meant

to be a schematic guide to it. Each chapter addresses a specific topic qua issue. What follows in this introduction is an introduction to each of those issues.

1. The Scope Issue. The 1998 revision expands the "scope" of Article 9. What this means literally is that the kinds of property in which a security interest can be taken by a creditor under Article 9 increases over those available in Article 9 before revision. Also, certain kinds of transactions that did not come under Article 9 before, now come under Article 9.

2. Perfection. Although filing a financing statement remains the dominant way to perfect a security interest in most kinds of property, there are expanded property types in which "control" is the operative method of perfection. Specific perfection rules are extended to property that comes under the scope of Article 9 for the first time in the 1998 revisions.

3. Choice of Law. In interstate secured transactions, it is necessary to determine which state's laws apply to perfection, the effect of perfection and the priority of security interests. It is particularly important to know where to file a financing statement. The 1998 revisions to Article 9 change the rules substantially.

4. The Filing System. Improvements in the filing system in the 1998 revisions to Article 9 include a full commitment to centralized filing—one place in every state in which financing statements are filed, and a filing system that escorts filing from the world of filed documents to the world of electronic communications and records.

5. Consumer Transactions. Revised Article 9 makes a clearer distinction between transactions in which the debtor is a consumer than prior Article 9 did. Enforcement of a security interest that is included in a consumer transaction is handled differently

in certain respects in the 1998 revisions to Article 9 than it was pre-1998. Although it governs more than consumer transactions, the good faith standard becomes the objective standard of commercial reasonableness in the 1998 revisions to Article 9.

6. Default and Enforcement. Article 9 provisions on default and enforcement deal generally with the procedures for obtaining property in which a creditor has a security interest and selling it to satisfy the debt, when the debtor is in default. Normally, the creditor has the right to repossess the property. Revised Article 9 includes new rules dealing with "secondary" obligors (guarantors), new special rules for some of the new kinds of property subject to security interests, new rules for the interests of subordinate creditors with security interests in the same property, and new rules for aspects of enforcement when the debtor is a consumer debtor.

SCOPE OF UCC ARTICLE 9

What kinds of property may become collateral under Uniform Commercial Code, Article 9? This is the "scope" question. In the 1998 revision to Uniform Commercial Code, Article 9, scope expands. That is, more kinds of property may be used as collateral and more types of transactions are covered. Also, some kinds of property that may have fallen into a more general category of collateral under pre-1998 Article 9, become defined and subject to specific rules.

SCOPE OF UCC ARTICLE 9 BEFORE THE 1998 REVISIONS

These kinds of property were (and will continue to be in the 1998 revisions to Article 9) subject to Article 9:

1. Tangible personal property. Property that is not real estate, but is tangible in form. Subdivisions of "tangible personal property" include "consumer goods," "equipment,"

"farm products," and "inventory."

2. Fixtures. This category of tangible personal property is separated from other personal property. Fixtures are items of tangible personal property that become so attached to real property that they are treated as part of the real estate. Fixtures begin as personal property, become real estate, but become personal property again when removed from the real estate. Special rules apply to fixtures under Article 9.

3. Documents. These are "documents of title" which, in general, establish that the person in possession has the rights to the goods which are represented in the title document. Bills of lading, dock warrants, dock receipts and warehouse receipts are included.

4. Instruments. An instrument generally is a negotiable instrument that evidences a right to the payment of money. An instrument becomes negotiable when it meets the criteria for negotiability in Article 3 of the Uniform Commercial Code. A note or draft is an example.

5. General Intangibles. Any intangible (meaning not goods) property interest that is not specifically addressed in Article 9. This is a gap-filling concept. Investment property is intangible property, for example, but because it is specifically addressed in Article 9, it is not a general intangible.

6. Chattel Paper. The writings that evidence a debt owed coupled with a security interest in goods or a lease of goods are chattel paper.

7. Accounts. An account is any right to payment for goods sold or leased or for services rendered which is not evidenced by an instrument or chattel paper. A "deposit account" like a bank account is not included.

SPECIFIC EXCLUSIONS FROM UCC ARTICLE 9 BEFORE 1998

These kinds of property or transactions are specifically excluded in the pre-1998
Article 9:

1. Statutory or common law liens.
2. Tort claims.
3. Deposit accounts (except those represented by certificates of deposit).
4. Governmental transfers.
5. Insurance claims or interests.
6. A right represented by a judgment.
7. Creation or transfer of an interest in or a lien on real estate.
8. Federally preempted rights.
9. Set off.
10. Transfer of a claim for wages, salary or compensation.
11. Sale of accounts and chattel paper as part of a sale of the business from which they arose.

12. Assignment of accounts and chattel paper for collection only, and
13. Transfer for performance of a contract or transfer of a single account to satisfy a pre-existing indebtedness.
14. Transfer of interest in a letter of credit, except for proceeds of a written letter of credit.

CHANGES IN THE SCOPE OF UCC ARTICLE 9 IN 1998

The 1998 revision to Article 9 keeps many of the exclusions in pre-1998 Article 9 but makes some significant changes as well. This list of changes tend to fall (though not wholly) into two categories, interests that are no longer excluded and interests that were included under more general categories such as "general intangibles" or "accounts" but that need to be addressed with specific secured transaction rules:

1. Nonpossessory, statutory agricultural liens. These liens were excluded under Article 9 prior to 1998. They are included for purposes of perfection and priority in revised Article 9. Note other nonpossessory statutory liens remain excluded.
2. Sales of payment intangibles and promissory notes. Payment intangibles were a kind of general intangible, now distinguished by the characteristic of a primary monetary obligation. Promissory notes are a kind of instrument. These interests are sold, securitized and pooled. The interests sold are so like security interests that distinguishing these sales transactions from secured transactions is virtually

impossible. The 1998 revision to Article 9 includes these kinds of property.

3. Security interests created by governmental debtors. The general pre-1998 exclusion has been narrowed. Only those governmental transfers that are subject to another statute on establishing and enforcing security interests are excluded. Federal preemption would, also, apply.

4. Health insurance receivables. The general exclusion of insurance proceeds in pre-1998 Article 9 is curbed for these specific kinds of receivables.

5. Consignments. Consignments of goods are included within the scope of Article 9 in the 1998 revisions. A consignment is a delivery of goods by the owner to another person, who sells for the consignor. A consignor is deemed to hold a purchase money security interest as against the consignee's secured creditors in the 1998 revisions to Article 9. Failure to comply with the requirements for a purchase money security interest potentially subjects the goods to the consignee's secured creditors. Before the 1998 revisions, a consignor had to perfect by filing a financing statement even though consignments fell within the scope of Article 2.

6. Commercial tort claims. The general exclusion of tort claims is narrowed so that security interests may be taken in commercial tort claims.

7. Liens on property. Certain liens on real property are included to the extent the lien establishes a right to payment.

8. Deposit accounts. Security interests may be taken in deposit accounts (with some restrictions). A security interest can be taken, therefore, in an ordinary bank account.

9. Supporting obligations. An example is a guarantee of payment or a letter of credit

supporting an obligation to pay money.

PERFECTION OF SECURITY INTERESTS

A security interest is perfected when the secured creditor has met the statutory requirements for notice to unsecured creditors, and most creditors who perfect their interests after the first secured creditor's perfection. There are four basic kinds of perfection: 1) perfection by filing; 2) perfection by possession; 3) perfection by control; and, 4) automatic perfection. All forms of perfection were available in Article 9 before 1998. However, Article 9 assigns a perfection method for each new kind of property within its scope in the 1998 revisions. "Control" as a method of perfection is expanded beyond the single kind of property, investment property, in which a security interest could be perfected by control in the pre-1998 Article 9. Thus "control" takes on new and larger significance after 1998 than it did before 1998.

Automatic perfection is specific to certain kinds of transactions. Purchase money security interests in consumer goods are a kind of security interest that perfects automatically. However, automatic perfection is usually temporary and extinguishes unless another appropriate form of perfection occurs during the temporary period of automatic perfection. There are more kinds of automatic perfection in the 1998 revisions than was the case before 1998.

Unless otherwise noted, conflicting security interests take priority in order of filing or other perfection in time. First in time usually wins, but note that purchase money security interests often provide a creditor priority notwithstanding the time perfection took place.

Each method of perfecting a security interest is discussed as follows:

1. Filing a financing statement. Filing a financing statement in the appropriate place of record maintained by a state will perfect almost every kind of security interest (There are some exceptions.). The 1998 revisions make it clearer that filing will perfect, even if there is another method of perfection available. The old maxim, "When in doubt, file," is even more appropriate after the 1998 revisions. This is the time-honored method of perfection.
2. Possession. A secured creditor may perfect a security interest in a broad range of collateral by taking possession of that collateral. Possession is the only way to perfect a security interest in money, except for proceeds from a sale of property subject to a security interest. The 1998 revisions to Article 9 clarify issues of possession as a method of perfection, but do not change the rules materially. For example, there is a method for a third-party bailee to acknowledge the creditor's interest. Such a method is not expressly provided pre-1998.
3. Control. Control as a method of perfection first applied to investment property in amendments to Article 9 that followed the 1994 revision of Uniform Commercial Code, Article 8. A creditor has control, and a perfected security interest, when the debtor's interest can be transferred by the secured creditor without the debtor's consent. For certain kinds of property, like certificated securities, possession is tantamount to control. The 1998 revisions of Article 9 allow a creditor to perfect a security interest in deposit accounts and letter-of-credit rights by control, as well as in investment property. Control is effectively the only way to perfect a security interest in deposit accounts and letter-of-credit rights. It is possible to perfect an interest in investment property by filing, but perfection by control always has

priority over perfection by filing if there are conflicting security interests, no matter which kind of perfection occurs first in time.

4. Automatic perfection. In some kinds of secured transactions, attachment is perfection. The "purchase money security interest" (PMSI) in consumer goods is such a case of automatic perfection. It arises when credit is extended to purchase goods. Other types of security interests are automatically perfected but only temporarily. An example is a security interest in a certificated security perfected for 20 days even though there is no filing or possession when it is delivered for sale or the like. Generally, a purchase money security interest has priority over security interests perfected before it in time. There are new specific PMSI's in the 1998 revisions, such as a PMSI in computer software and livestock.

Examples of other kinds of security interests that perfect upon attachment are a sale of a payment intangible, a sale of a promissory note, a security interest in a healthcare insurance receivable (all new in 1998), and a broker's security interest in investment property created by the broker (from the 1994 Article 8 revisions). Most of these security interests will, also, have priority over other kinds of security interests that perfect earlier in time.

CHOICE OF LAW RULES

A transaction in which a creditor takes a "security interest" in the collateral of a debtor may involve more than one state. The creditor may be in one state, the debtor in another, and the collateral in another. Further, the collateral may move at some point in the transaction from one state to another. Both the creditor and the debtor may be able to claim more than one place as residence or domicile. Therefore, Article 9 has always had rules that determine which state's law will apply to the perfection,

the effect of perfection and the priority of creditors in collateral.

When perfection requires filing a "financing statement" it is important to identify with certainty the state in which to file the financing statement. It is also important that creditors know with certainty that same state is the state in which they must search the record for financing statements indicating the existence of prior security interests. The state which the "choice of law" rules identify as the state whose law governs perfection, effect of perfection and the priority of creditors in the collateral, is the state in which the financing statement must be filed.

The 1998 revisions to Article 9 both simplify and substantially change the "choice of law" rules, meaning that in some cases different states will be the states in which perfection, the effect of perfection and the priority of creditors will be established than is the case under pre-1998 Article 9. The ultimate result is greater certainty for those who file financing statements and those who search for filed financing statements about which state is the right state.

Major Changes

There are two major changes in the "choice of law" rules:

1. Pre-1998, the basic rule chooses the law of the state in which the collateral is found to govern perfection and the effect of perfection of a security interest. If perfection occurs when a financing statement is filed, then the filing must take place in the state where the collateral is found. In the 1998 revisions, the basic rule chooses the law

of the state in which the debtor is located as the law governing perfection, effect of perfection and the priority of a security interest in collateral. If a filing of a financing statement is required, then the statement must be filed where the debtor is, without regard for the location of the collateral. The location of the debtor is less likely to change than the location of the collateral and reliance on the location of the debtor provides creditors with more certainty about where to file and where to search. (Exceptions to both these rules to be discussed later on.)

2. If the debtor is a registered organization (corporation, limited partnership, limited liability partnership, limited liability company, etc.), pre-1998 treated the state with the chief executive office as the debtor's state. In the 1998 revisions, the debtor's state is the state in which it is a registered organization. Again, the objective of certainty about the place to file and the place to search is better served by the new rule than by the old rule, but the change will probably result in very little change in the actual place of filing in the vast number of cases.

Exceptions and Continuity

There are prominent exceptions to the new general rule in the 1998 revisions to Article 9. In most instances these exceptions mean no practical change in the choice of law rules from pre-1998 Article 9:

1. All possessory (meaning that there is no filing of a financing statement) security interests are perfected under the law of the state in which the collateral is located (where the creditor has possession). The practical effect is to leave the law unchanged for possessory security interests in any kind of collateral.
2. For other kinds of collateral, there are also no effective changes in the "choice of law" rules. These other kinds of collateral include property subject to certificates of

title, and minerals, letter of credit rights and investment property.

3. For deposit accounts, which were not in the scope of pre-1998 Article 9, the location of the bank determines the place for perfection, effect of perfection and non-perfection, and the priority of security interests.

4. For agricultural liens, which were not within the scope of pre-1998 Article 9, the location of the farm products determines the place for perfection, effect of perfection and non-perfection, and the priority of security interests.

5. There are security interests that perfect in the location of the debtor under pre-1998 Article 9. Since the location of the debtor is the fundamental rule in the 1998 revisions, perfection rules effectively do not change for these security interests under the 1998 revisions to Article 9. Included are security interests in accounts, general intangibles and mobile goods (no distinction between mobile and other goods in the 1998 revisions), automatic perfection of a broker in investment property, and automatic perfection of the security interest of a commodity broker in a commodity contract.

Important Differences for Some Collateral

Under the 1998 revisions, the law governing perfection may be different from the law governing effect of perfection and priority of security interests for some kinds of property. These kinds of property include negotiable documents, goods, instruments, money and tangible chattel paper. The effect of perfection and priority of nonpossessory security interests in these kinds of collateral will be determined by the location of the collateral. This means that the place to file or the place where automatic perfection takes place, is the location of the debtor, but the impact of filing may be determined under the law of the state where the collateral is.

THE FILING SYSTEM

The primary and principal method for perfecting a security interest under Uniform Commercial Code, Article 9 is to file a financing statement with the filing authority or authorities in the appropriate state. Before 1998, most states had centralized the filing of financing statements covering most collateral in one state office. A few states continued to have both general central and local filing for all collateral. Many of the states that have centralized filing for most collateral, still continue to have local filing for some kinds of collateral. The result is a very mixed array of filing and search requirements. For filing must facilitate the search of records by subsequent creditors who must be able to find prior security interests. The fundamental objective of uniformity has been substantially impaired by the lack of uniformity just in the filing systems.

The new filing system is designed to forge a uniform system that is simpler and more reasonable to use:

1. Medium neutral. The new system is designed to be medium neutral. This simply means that the filing systems are no longer to be required to file paper only. The systems can convert to any and all forms of electronic communications for filing purposes.
2. Centralized filing. Every state will have a central filing authority. One place to file and one place to search. The only exception is fixture filings, which must continue to be made (and searched) in the real estate records.
3. Simplified financing statement. The statement must name debtor, creditor and

generally describe some collateral. No signature is required. Identity of filer is immaterial.

4. Filing office operations. No discretion resides in the filing office as to sufficiency of a filing. A file cannot be cleared until one year after a termination occurs, extending the availability of the record for one year longer than pre-1998 Article 9.

5. Correction statement. A debtor can file a correction to an improper or falsely filed financing statement.

6. Extended effective dates. Most financing statements lapse after five years from the date of filing. Two kinds of financing statements, those for public-finance transactions and for manufactured-home transactions are initially effective for 30 years.

7. National forms and fees. There is an effort to establish the same forms for filing in every state and to nationalize filing fees. Uniformity, therefore, is intended to go to the administration of filing as well as to the basic law.

CONSUMER TRANSACTIONS

In the 1998 revisions to Uniform Commercial Code, Article 9, there are special provisions for secured transactions in which the debtor is a consumer. A "consumer transaction" is defined to be one in which an individual incurs an obligation primarily for personal, family, or household purposes, a security interest secures the obligation, and the collateral is held or acquired primarily for personal, family, or household purposes. Most consumer secured transactions are consumer-goods transactions, meaning that an individual purchases an item, i.e. a refrigerator, a couch, and finances the purchase. The item, i.e., the refrigerator, the couch, are the collateral. If the consumer debtor defaults on the debt, the item is repossessed. The 1998 revisions make a distinction between a consumer debtor and a consumer

obligor. In Article 9, a "debtor" is defined in terms of an interest in the collateral. An "obligor" is a person obligated to pay the debt. Usually they are the same person, but there are obligors who are not debtors, i.e., a person who guarantees the payment of the debt for the debtor. Most of the special consumer transaction rules pertain to enforcement of a security interest after the debtor defaults on the basic obligation. Some of these rules are as follows:

1. Right to Redeem. A consumer-goods transaction debtor may not waive the right to redeem collateral taken to satisfy the debt, a right which all debtors have. Redemption is the right under Article 9 that collateral be returned to the debtor if the debt is satisfied after a default. Commercial and business debtors are able to waive that right as part of credit acquisition. Consumer debtors will not be able to waive their right.
2. Process Presumption. In an action against a secured creditor for errors in enforcement and collection process, the presumption is that the collateral is worth the debt. In order to establish a deficiency, a creditor must rebut the presumption. These rules do not apply to consumer transactions. The courts will determine the rule to apply in consumer transactions and could choose a different rule.
3. No Dual Status Rule. The 1998 revisions to UCC Article 9 provide that the same collateral may secure a purchase-money security interest and a non-purchase-money security interest. This "dual status" rule is adopted in the 1998 revisions to Article 9, rejecting the opposing "transformation" rule applied in some pre-1998 court cases. Because the "dual status" rule may limit the benefit of purchase money security interests, consumer-goods transactions are excepted from its application. In a consumer-goods transaction, the courts must determine the

appropriate rule to apply.

4. Pre-Payment Rights. Amendments to Article 2 of the Uniform Commercial Code that accompany the 1998 revisions to Article 9 provide greater protection for a consumer buyer of goods who pays in whole or in part before delivery of the goods. The buyer has an enforceable interest under Article 2 that allows the buyer to obtain the goods.

5. FTC Rule 433. A consumer's rights under Federal Trade Commission Rule 433 on preservation of claims and defenses are specifically recognized in the 1998 revisions to Article 9, and will continue even if the required notification in the appropriate record is missing.

6. Deficiency Statement. A consumer-goods debtor or consumer obligor is entitled to a written statement which provides the amount of a deficiency (what is owed after collateral is sold to satisfy the debt) and the calculation which results in that amount.

7. No Partial Satisfaction. A secured party may not accept collateral as partial satisfaction of a consumer obligation.

8. Sufficient Description. A description of consumer goods, a security entitlement, a security account, or a commodity account that is by category only is not a sufficient description when there is a consumer transaction. A security entitlement, a security account and a commodity account are types of investment property under Article 8 of the Uniform Commercial Code.

GOOD FAITH

The 1998 revisions to Article 9 adopt the more "objective" good faith standard: "honesty in fact and observance of reasonable commercial standards of fair dealing."

DEFAULT AND ENFORCEMENT

When a debtor defaults on an obligation secured under Uniform Commercial Code, Article 9, a secured creditor has a right to take the collateral, sell that collateral, and apply the proceeds to pay off the debt. If the proceeds are insufficient to satisfy the debt, there may be a deficiency that the debtor will be obligated to pay. The creditor will be entitled to pursue the deficiency with the creditor's remedies available under other law. If there is a surplus after sale, that surplus will be the debtor's, unless other creditors act to obtain satisfaction of their debts, as well. Strict foreclosure is an alternative to sale. The creditor keeps the collateral in a strict foreclosure. The procedures under Article 9 are generally non-judicial procedures. (Although a creditor may seek enforcement in court.) Usually the secured creditor will repossess the collateral and pursue the available remedies without a court proceeding. Article 9 has its own procedural requirements for creditors. Not following them may mean that a creditor will not obtain a full remedy under Article 9.

The 1998 revisions do not fundamentally change the rules for enforcement of a security interest upon a debtor's default. The revisions provide for problems perceived in enforcement prior to 1998. Some of the important changes are as follows:

1. **Secondary Obligors.** A secured party owes duties to "secondary" obligors on the secured debt. A secondary obligor is liable for a debt only if the primary obligor does not satisfy the debt. A guarantor is an example. There are notifications that must be given to known secondary obligors by secured parties upon default. Contrary to the

law of suretyship, the 1998 revisions generally prohibit waiver of rights by a secondary obligor. A secondary obligor can waive notification of disposition of the collateral, and (in a non-consumer transaction) the right to redeem, but only after the default has actually taken place.

2. Deposit Accounts. The enforcement rights of a depositary bank holding a security interest in a deposit account are expressly provided for. Security interests in deposit accounts under Article 9 were not possible before the 1998 revision.

3. Warranties. A secured party is subject to warranties of title, quiet possession and the like, applicable under other law (usually Uniform Commercial Code, Article 2), including rules for their exclusion or modification when disposing of collateral.

4. Notification of Junior Creditors. A secured party taking collateral and disposing of it upon default, has a broader obligation to notify other secured parties and lienholders who have filed financing statements against the debtor covering the same collateral than is the case under pre-1998 Article 9. There are specific notification requirements and a requirement for notification within a reasonable time (no less than 10 days after the earliest time of disposition of the collateral).

5. Transfer to a Secondary Obligor from Secured Party. A secondary obligor obtains the rights and assumes the duties of a secured party if it takes an assignment of the secured obligation, agrees to assume the secured party's obligations, or is subrogated to the rights of the secured party. This is not a disposition of the collateral by the secured party, but relieves the secured party of further duties and obligations.

6. Transfer of Title to Secured Party. The 1998 revisions make it clear that a transfer of record or legal title to a secured party in order to facilitate a disposition, is not of itself a disposition of the collateral.

7. Strict Foreclosure. A secured party may accept collateral in partial (except in

consumer-goods transactions) or full satisfaction of a debt. Junior claimants rights are accounted for. Acceptance of collateral in satisfaction of a debt is not of itself an unreasonable delay of disposition. Strict foreclosure is permissible if it is commercially reasonable, and unreasonable delay can occur only if the foreclosure itself is not commercially reasonable.

8. Damages for Secured Party's Noncompliance. Secured parties are subject to a "rebuttable presumption" that the collateral value equals the debt if they do not comply with the enforcement procedures and requirements in Article 9 for non-consumer transactions. If there is breach on the part of the secured party, the obligor is credited with the difference between the actual disposition price and the price that would have been paid if the disposition had been conducted in a commercially reasonable manner. The "absolute bar" rule is not mentioned but should be unnecessary (except that it may be selected for consumer transactions).

9. Deficiency Calculation. If there is a procedurally regular disposition that nonetheless fetches a low price, and the disposition is to an insider transferee, the deficiency is calculated on the basis of what the price should have been in a commercially reasonable disposition.

**PREFATORY NOTE TO REVISED ACT-SUMMARY OF REVISIONS
PORTION**

4. Summary of Revisions. Following is a brief summary of some of the more significant revisions of Article 9 that are included in this Article.

a. Scope of Article 9. This Article expands the scope of Article 9 in several respects.

Deposit accounts. Section 9–109 includes within this Article’s scope deposit accounts as original collateral, except in consumer transactions. Former Article 9 dealt with deposit accounts only as proceeds of other collateral.

Sales of payment intangibles and promissory notes. Section 9–109 also includes within the scope of this Article most sales of “payment intangibles” (defined in Section 9–102 as general intangibles under which an account debtor’s principal obligation is monetary) and “promissory notes” (also defined in Section 9–102). Former Article 9 included sales of accounts and chattel paper, but not sales of payment intangibles or promissory notes. In its inclusion of sales of payment intangibles and promissory notes, this Article continues the drafting convention found in former Article 9; it provides that the sale of accounts, chattel paper, payment intangibles, or promissory notes creates a “security interest.” The definition of “account” in Section 9–102 also has been expanded to include various rights to payment that were general intangibles under former Article 9.

Health–care–insurance receivables. Section 9–109 narrows Article 9’s exclusion of transfers of interests in insurance policies by carving out of the exclusion “health–care–insurance receivables” (defined in Section 9–102). A health–care–insurance receivable is included within the definition of “account” in Section 9–102.

Nonpossessory statutory agricultural liens. Section 9-109 also brings nonpossessory statutory agricultural liens within the scope of Article 9.

Consignments. Section 9-109 provides that "true" consignments—bailments for the purpose of sale by the bailee—are security interests covered by Article 9, with certain exceptions. See Section 9-102 (defining "consignment"). Currently, many consignments are subject to Article 9's filing requirements by operation of former Section 2-326.

Supporting obligations and property securing rights to payment. This Article also addresses explicitly (i) obligations, such as guaranties and letters of credit, that support payment or performance of collateral such as accounts, chattel paper, and payment intangibles, and (ii) any property (including real property) that secures a right to payment or performance that is subject to an Article 9 security interest. See Sections 9-203, 9-308.

Commercial tort claims. Section 9-109 expands the scope of Article 9 to include the assignment of commercial tort claims by narrowing the exclusion of tort claims generally. However, this Article continues to exclude tort claims for bodily injury and other non-business tort claims of a natural person. See Section 9-102 (defining

”commercial tort claim”).

Transfers by States and governmental units of States. Section 9–109 narrows the exclusion of transfers by States and their governmental units. It excludes only transfers covered by another statute (other than a statute generally applicable to security interests) to the extent the statute governs the creation, perfection, priority, or enforcement of security interests.

Nonassignable general intangibles, promissory notes, health–care–insurance receivables, and letter–of–credit rights. This Article enables a security interest to attach to letter–of–credit rights, health–care–insurance receivables, promissory notes, and general intangibles, including contracts, permits, licenses, and franchises, notwithstanding a contractual or statutory prohibition against or limitation on assignment. This Article explicitly protects third parties against any adverse effect of the creation or attempted enforcement of the security interest. See Sections 9–408, 9–409.

Subject to Sections 9–408 and 9–409 and two other exceptions (Sections 9–406, concerning accounts, chattel paper, and payment intangibles, and 9–407, concerning interests in leased goods), Section 9–401 establishes a baseline rule that the inclusion of transactions and collateral within the scope of Article 9 has no effect on non–Article 9 law dealing with the alienability or inalienability of property. For

example, if a commercial tort claim is nonassignable under other applicable law, the fact that a security interest in the claim is within the scope of Article 9 does not override the other applicable law's effective prohibition of assignment.

b. Duties of Secured Party. This Article provides for expanded duties of secured parties.

Release of control. Section 9-208 imposes upon a secured party having control of a deposit account, investment property, or a letter-of-credit right the duty to release control when there is no secured obligation and no commitment to give value. Section 9-209 contains analogous provisions when an account debtor has been notified to pay a secured party.

Information. Section 9-210 expands a secured party's duties to provide the debtor with information concerning collateral and the obligations that it secures.

Default and enforcement. Part 6 also includes some additional duties of secured parties in connection with default and enforcement. See, e.g., Section 9-616 (duty to explain calculation of deficiency or surplus in a consumer-goods transaction).

c. Choice of Law. The choice-of-law rules for the law governing perfection, the effect of perfection or nonperfection, and priority are found in Part 3, Subpart 1 (Sections 9-301 through 9-307). See also Section 9-316.

Where to file: Location of debtor. This Article changes the choice-of-law rule governing perfection (i.e., where to file) for most collateral to the law of the jurisdiction where the debtor is located. See Section 9-301. Under former Article 9, the jurisdiction of the debtor's location governed only perfection and priority of a security interest in accounts, general intangibles, mobile goods, and, for purposes of perfection by filing, chattel paper and investment property.

Determining debtor's location. As a baseline rule, Section 9-307 follows former Section 9-103, under which the location of the debtor is the debtor's place of business (or chief executive office, if the debtor has more than one place of business). Section 9-307 contains three major exceptions. First, a "registered organization," such as a corporation or limited liability company, is located in the State under whose law the debtor is organized, c.g., a corporate debtor's State of incorporation. Second, an individual debtor is located at his or her principal residence. Third, there are special rules for determining the location of the United States and registered organizations organized under the law of the United States.

Location of non-U.S. debtors. If, applying the foregoing rules, a debtor is located in

a jurisdiction whose law does not require public notice as a condition of perfection of a nonpossessory security interest, the entity is deemed located in the District of Columbia. See Section 9–307. Thus, to the extent that this Article applies to non–U.S. debtors, perfection could be accomplished in many cases by a domestic filing.

Priority. For tangible collateral such as goods and instruments, Section 9–301 provides that the law applicable to priority and the effect of perfection or nonperfection will remain the law of the jurisdiction where the collateral is located, as under former Section 9–103 (but without the confusing “last event” test). For intangible collateral, such as accounts, the applicable law for priority will be that of the jurisdiction in which the debtor is located.

Possessory security interests; agricultural liens. Perfection, the effect of perfection or nonperfection, and priority of a possessory security interest or an agricultural lien are governed by the law of the jurisdiction where the collateral subject to the security interest or lien is located. See Sections 9–301, 9–302.

Goods covered by certificates of title; deposit accounts; letter–of–credit rights; investment property. This Article includes several refinements to the treatment of choice–of–law matters for goods covered by certificates of title. See Section 9–303. It also provides special choice–of–law rules, similar to those for investment property

under current Articles 8 and 9, for deposit accounts (Section 9–304), investment property (Section 9–305), and letter-of-credit rights (Section 9–306).

Change in applicable law. Section 9–316 addresses perfection following a change in applicable law.

d. Perfection. The rules governing perfection of security interests and agricultural liens are found in Part 3, Subpart 2 (Sections 9–308 through 9–316).

Deposit accounts; letter-of-credit rights. With certain exceptions, this Article provides that a security interest in a deposit account or a letter-of-credit right may be perfected only by the secured party's acquiring "control" of the deposit account or letter-of-credit right. See Sections 9–312, 9–314. Under Section 9–104, a secured party has "control" of a deposit account when, with the consent of the debtor, the secured party obtains the depositary bank's agreement to act on the secured party's instructions (including when the secured party becomes the account holder) or when the secured party is itself the depositary bank. The control requirements are patterned on Section 8–106, which specifies the requirements for control of investment property. Under Section 9–107, "control" of a letter-of-credit right occurs when the issuer or nominated person consents to an assignment of proceeds under Section 5–114.

Electronic chattel paper. Section 9–102 includes a new defined term: “electronic chattel paper.” Electronic chattel paper is a record or records consisting of information stored in an electronic medium (i.e., it is not written). Perfection of a security interest in electronic chattel paper may be by control or filing. See Sections 9–105 (sui generis definition of control of electronic chattel paper), 9–312 (perfection by filing), 9–314 (perfection by control).

Investment property. The perfection requirements for “investment property” (defined in Section 9–102), including perfection by control under Section 9–106, remain substantially unchanged. However, a new provision in Section 9–314 is designed to ensure that a secured party retains control in “repledge” transactions that are typical in the securities markets.

Instruments, agricultural liens, and commercial tort claims. This Article expands the types of collateral in which a security interest may be perfected by filing to include instruments. See Section 9–312. Agricultural liens and security interests in commercial tort claims also are perfected by filing, under this Article. See Sections 9–308, 9–310.

Sales of payment intangibles and promissory notes. Although former Article 9 covered the outright sale of accounts and chattel paper, sales of most other types of

receivables also are financing transactions to which Article 9 should apply. Accordingly, Section 9-102 expands the definition of "account" to include many types of receivables (including "health-care-insurance receivables," defined in Section 9-102) that former Article 9 classified as "general intangibles." It thereby subjects to Article 9's filing system sales of more types of receivables than did former Article 9. Certain sales of payment intangibles—primarily bank loan participation transactions—should not be subject to the Article 9 filing rules. These transactions fall in a residual category of collateral, "payment intangibles" (general intangibles under which the account debtor's principal obligation is monetary), the sale of which is exempt from the filing requirements of Article 9. See Sections 9-102, 9-109, 9-309 (perfection upon attachment). The perfection rules for sales of promissory notes are the same as those for sales of payment intangibles.

Possessory security interests. Several provisions of this Article address aspects of security interests involving a secured party or a third party who is in possession of the collateral. In particular, Section 9-313 resolves a number of uncertainties under former Section 9-305. It provides that a security interest in collateral in the possession of a third party is perfected when the third party acknowledges in an authenticated record that it holds for the secured party's benefit. Section 9-313 also provides that a third party need not so acknowledge and that its acknowledgment does not impose any duties on it, unless it otherwise agrees. A special rule in Section 9-313 provides that if a secured party already is in possession of collateral, its security interest remains perfected by possession if it delivers the collateral to a third party and the collateral is accompanied by instructions to hold it for the secured party or to redeliver it to the secured party. Section 9-313 also clarifies the limited

circumstances under which a security interest in goods covered by a certificate of title may be perfected by the secured party's taking possession.

Automatic perfection. Section 9-309 lists various types of security interests as to which no public-notice step is required for perfection (e.g., purchase-money security interests in consumer goods other than automobiles). This automatic perfection also extends to a transfer of a health-care-insurance receivable to a health-care provider. Those transfers normally will be made by natural persons who receive health-care services; there is little value in requiring filing for perfection in that context. Automatic perfection also applies to security interests created by sales of payment intangibles and promissory notes. Section 9-308 provides that a perfected security interest in collateral supported by a "supporting obligation" (such as an account supported by a guaranty) also is a perfected security interest in the supporting obligation, and that a perfected security interest in an obligation secured by a security interest or lien on property (e.g., a real-property mortgage) also is a perfected security interest in the security interest or lien.

e. Priority; Special Rules for Banks and Deposit Accounts. The rules governing priority of security interests and agricultural liens are found in Part 3, Subpart 3 (Sections 9-317 through 9-342). This Article includes several new priority rules and some special rules relating to banks and deposit accounts (Sections 9-340 through 9-342).

Purchase-money security interests: General; consumer-goods transactions; inventory. Section 9-103 substantially rewrites the definition of purchase-money security interest (PMSI) (although the term is not formally "defined"). The substantive changes, however, apply only to non-consumer-goods transactions. (Consumer transactions and consumer-goods transactions are discussed below in Comment 4.j.) Section 9-103 makes clear that a security interest in collateral may be (to some extent) both a PMSI as well as a non-PMSI, in accord with the "dual status" rule applied by some courts under former Article 9 (thereby rejecting the "transformation" rule). The definition provides an even broader conception of a PMSI in inventory, yielding a result that accords with private agreements entered into in response to the uncertainty under former Article 9. It also treats consignments as purchase-money security interests in inventory. Section 9-324 revises the PMSI priority rules, but for the most part without material change in substance. Section 9-324 also clarifies the priority rules for competing PMSIs in the same collateral.

Purchase-money security interests in livestock; agricultural liens. Section 9-324 provides a special PMSI priority, similar to the inventory PMSI priority rule, for livestock. Section 9-322 (which contains the baseline first-to-file-or-perfect priority rule) also recognizes special non-Article 9 priority rules for agricultural liens, which can override the baseline first-in-time rule.

Purchase-money security interests in software. Section 9-324 contains a new priority rule for a software purchase-money security interest. (Section 9-102 includes a definition of "software.") Under Section 9-103, a software PMSI includes a PMSI in software that is used in goods that are also subject to a PMSI. (Note also that the definition of "chattel paper" has been expanded to include records that evidence a monetary obligation and a security interest in specific goods and software used in the goods.)

Investment property. The priority rules for investment property are substantially similar to the priority rules found in former Section 9-115, which was added in conjunction with the 1994 revisions to UCC Article 8. Under Section 9-328, if a secured party has control of investment property (Sections 8-106, 9-106), its security interest is senior to a security interest perfected in another manner (e.g., by filing). Also under Section 9-328, security interests perfected by control generally rank according to the time that control is obtained or, in the case of a security entitlement or a commodity contract carried in a commodity account, the time when the control arrangement is entered into. This is a change from former Section 9-115, under which the security interests ranked equally. However, as between a securities intermediary's security interest in a security entitlement that it maintains for the debtor and a security interest held by another secured party, the securities intermediary's security interest is senior.

Deposit accounts. This Article's priority rules applicable to deposit accounts are

found in Section 9–327. They are patterned on and are similar to those for investment property in former Section 9–115 and Section 9–328 of this Article. Under Section 9–327, if a secured party has control of a deposit account, its security interest is senior to a security interest perfected in another manner (i.e., as cash proceeds). Also under Section 9–327, security interests perfected by control rank according to the time that control is obtained, but as between a depositary bank’s security interest and one held by another secured party, the depositary bank’s security interest is senior. A corresponding rule in Section 9–340 makes a depositary bank’s right of set-off generally senior to a security interest held by another secured party. However, if the other secured party becomes the depositary bank’s customer with respect to the deposit account, then its security interest is senior to the depositary bank’s security interest and right of set-off. Sections 9–327, 9–340.

Letter-of-credit rights. The priority rules for security interests in letter-of-credit rights are found in Section 9–329. They are somewhat analogous to those for deposit accounts. A security interest perfected by control has priority over one perfected in another manner (i.e., as a supporting obligation for the collateral in which a security interest is perfected). Security interests in a letter-of-credit right perfected by control rank according to the time that control is obtained. However, the rights of a transferee beneficiary or a nominated person are independent and superior to the extent provided in Section 5 114. See Section 9–109(c)(4).

Chattel paper and instruments. Section 9–330 is the successor to former Section

9–308. As under former Section 9–308, differing priority rules apply to purchasers of chattel paper who give new value and take possession (or, in the case of electronic chattel paper, obtain control) of the collateral depending on whether a conflicting security interest in the collateral is claimed merely as proceeds. The principal change relates to the role of knowledge and the effect of an indication of a previous assignment of the collateral. Section 9–330 also affords priority to purchasers of instruments who take possession in good faith and without knowledge that the purchase violates the rights of the competing secured party. In addition, to qualify for priority, purchasers of chattel paper, but not of instruments, must purchase in the ordinary course of business.

Proceeds. Section 9–322 contains new priority rules that clarify when a special priority of a security interest in collateral continues or does not continue with respect to proceeds of the collateral. Other refinements to the priority rules for proceeds are included in Sections 9–324 (purchase–money security interest priority) and 9–330 (priority of certain purchasers of chattel paper and instruments).

Miscellaneous priority provisions. This Article also includes (i) clarifications of selected good–faith–purchase and similar issues (Sections 9–317, 9–331); (ii) new priority rules to deal with the “double debtor” problem arising when a debtor creates a security interest in collateral acquired by the debtor subject to a security interest created by another person (Section 9–325); (iii) new priority rules to deal with the problems created when a change in corporate structure or the like results in a new

entity that has become bound by the original debtor's after-acquired property agreement (Section 9-326); (iv) a provision enabling most transferees of funds from a deposit account or money to take free of a security interest (Section 9-332); (v) substantially rewritten and refined priority rules dealing with accessions and commingled goods (Sections 9-335, 9-336); (vi) revised priority rules for security interests in goods covered by a certificate of title (Section 9-337); and (vii) provisions designed to ensure that security interests in deposit accounts will not extend to most transferees of funds on deposit or payees from deposit accounts and will not otherwise "clog" the payments system (Sections 9-341, 9-342).

Model provisions relating to production-money security interests. Appendix II to this Article contains model definitions and priority rules relating to "production-money security interests" held by secured parties who give new value used in the production of crops. Because no consensus emerged on the wisdom of these provisions during the drafting process, the sponsors make no recommendation on whether these model provisions should be enacted.

f. Proceeds. Section 9-102 contains an expanded definition of "proceeds" of collateral which includes additional rights and property that arise out of collateral, such as distributions on account of collateral and claims arising out of the loss or nonconformity of, defects in, or damage to collateral. The term also includes collections on account of "supporting obligations," such as guarantees.

g. Part 4: Additional Provisions Relating to Third-Party Rights. New Part 4 contains several provisions relating to the relationships between certain third parties and the parties to secured transactions. It contains new Sections 9-401 (replacing former Section 9-311) (alienability of debtor's rights), 9-402 (replacing former Section 9-317) (secured party not obligated on debtor's contracts), 9-403 (replacing former Section 9-206) (agreement not to assert defenses against assignee), 9-404, 9-405, and 9-406 (replacing former Section 9-318) (rights acquired by assignee, modification of assigned contract, discharge of account debtor, restrictions on assignment of account, chattel paper, promissory note, or payment intangible ineffective), 9-407 (replacing some provisions of former Section 2A-303) (restrictions on creation or enforcement of security interest in leasehold interest or lessor's residual interest ineffective). It also contains new Sections 9-408 (restrictions on assignment of promissory notes, health-care-insurance receivables ineffective, and certain general intangibles ineffective) and 9-409 (restrictions on assignment of letter-of-credit rights ineffective), which are discussed above.

h. Filing. Part 5 (formerly Part 4) of Article 9 has been substantially rewritten to simplify the statutory text and to deal with numerous problems of interpretation and implementation that have arisen over the years.

Medium-neutrality. This Article is "medium-neutral"; that is, it makes clear that parties may file and otherwise communicate with a filing office by means of records

communicated and stored in media other than on paper.

Identity of person who files a record; authorization. Part 5 is largely indifferent as to the person who effects a filing. Instead, it addresses whose authorization is necessary for a person to file a record with a filing office. The filing scheme does not contemplate that the identity of a "filer" will be a part of the searchable records. This approach is consistent with, and a necessary aspect of, eliminating signatures or other evidence of authorization from the system (except to the extent that filing offices may choose to employ authentication procedures in connection with electronic communications). As long as the appropriate person authorizes the filing, or, in the case of a termination statement, the debtor is entitled to the termination, it is largely insignificant whether the secured party or another person files any given record.

Section 9-509 collects in one place most of the rules that determine when a record may be filed. In general, the debtor's authorization is required for the filing of an initial financing statement or an amendment that adds collateral. With one further exception, a secured party of record's authorization is required for the filing of other amendments. The exception arises if a secured party has failed to provide a termination statement that is required because there is no outstanding secured obligation or commitment to give value. In that situation, a debtor is authorized to file a termination statement indicating that it has been filed by the debtor.

Financing statement formal requisites. The formal requisites for a financing statement are set out in Section 9–502. A financing statement must provide the name of the debtor and the secured party and an indication of the collateral that it covers. Sections 9–503 and 9–506 address the sufficiency of a name provided on a financing statement and clarify when a debtor’s name is correct and when an incorrect name is insufficient. Section 9–504 addresses the indication of collateral covered. Under Section 9–504, a super–generic description (e.g., “all assets” or “all personal property”) in a financing statement is a sufficient indication of the collateral. (Note, however, that a super–generic description is inadequate for purposes of a security agreement. See Sections 9–108, 9–203.) To facilitate electronic filing, this Article does not require that the debtor’s signature or other authorization appear on a financing statement. Instead, it prohibits the filing of unauthorized financing statements and imposes liability upon those who violate the prohibition. See Sections 9–509, 9–626.

Filing–office operations. Part 5 contains several provisions governing filing operations. First, it prohibits the filing office from rejecting an initial financing statement or other record for a reason other than one of the few that are specified. See Sections 9–520, 9–516. Second, the filing office is obliged to link all subsequent records (e.g., assignments, continuation statements, etc.) to the initial financing statement to which they relate. See Section 9–519. Third, the filing office may delete a financing statement and related records from the files no earlier than one year after lapse (lapse normally is five years after the filing date), and then only if a continuation statement has not been filed. See Sections 9–515, 9–519, 9–522. Thus,

a financing statement and related records would be discovered by a search of the files even after the filing of a termination statement. This approach helps eliminate filing-office discretion and also eases problems associated with multiple secured parties and multiple partial assignments. Fourth, Part 5 mandates performance standards for filing offices. See Sections 9-519, 9-520, 9-523. Fifth, it provides for the promulgation of filing-office rules to deal with details best left out of the statute and requires the filing office to submit periodic reports. See Sections 9-526, 9-527.

Correction of records: Defaulting or missing secured parties and fraudulent filings. In some areas of the country, serious problems have arisen from fraudulent financing statements that are filed against public officials and other persons. This Article addresses the fraud problem by providing the opportunity for a debtor to file a termination statement when a secured party wrongfully refuses or fails to provide a termination statement. See Section 9-509. This opportunity also addresses the problem of secured parties that simply disappear through mergers or liquidations. In addition, Section 9-518 affords a statutory method by which a debtor who believes that a filed record is inaccurate or was wrongfully filed may indicate that fact in the files by filing a correction statement, albeit without affecting the efficacy, if any, of the challenged record.

Extended period of effectiveness for certain financing statements. Section 9-515 contains an exception to the usual rule that financing statements are effective for five years unless a continuation statement is filed to continue the effectiveness for

another five years. Under that section, an initial financing statement filed in connection with a "public-finance transaction" or a "manufactured-home transaction" (terms defined in Section 9-102) is effective for 30 years.

National form of financing statement and related forms. Section 9-521 provides for uniform, national written forms of financing statements and related written records that must be accepted by a filing office that accepts written records.

i. Default and Enforcement. Part 6 of Article 9 extensively revises former Part 5. Provisions relating to enforcement of consumer-goods transactions and consumer transactions are discussed in Comment 4.j.

Debtor, secondary obligor; waiver. Section 9-602 clarifies the identity of persons who have rights and persons to whom a secured party owes specified duties under Part 6. Under that section, the rights and duties are enjoyed by and run to the "debtor," defined in Section 9-102 to mean any person with a non-lien property interest in collateral, and to any "obligor." However, with one exception (Section 9-616, as it relates to a consumer obligor), the rights and duties concerned affect only obligors who are "secondary obligors." "Secondary obligor" is defined in Section 9-102 to include one who is secondarily obligated on the secured obligation, e.g., a guarantor, or one who has a right of recourse against the debtor or another obligor with respect to an obligation secured by collateral. However, under Section 9-628, the secured

party is relieved from any duty or liability to any person unless the secured party knows that the person is a debtor or obligor. Resolving an issue on which courts disagreed under former Article 9, this Article generally prohibits waiver by a secondary obligor of its rights and a secured party's duties under Part 6. See Section 9-602. However, Section 9-624 permits a secondary obligor or debtor to waive the right to notification of disposition of collateral and, in a non-consumer transaction, the right to redeem collateral, if the secondary obligor or debtor agrees to do so after default.

Rights of collection and enforcement of collateral. Section 9-607 explains in greater detail than former 9-502 the rights of a secured party who seeks to collect or enforce collateral, including accounts, chattel paper, and payment intangibles. It also sets forth the enforcement rights of a depository bank holding a security interest in a deposit account maintained with the depository bank. Section 9-607 relates solely to the rights of a secured party vis-a-vis a debtor with respect to collections and enforcement. It does not affect the rights or duties of third parties, such as account debtors on collateral, which are addressed elsewhere (e.g., Section 9-406). Section 9-608 clarifies the manner in which proceeds of collection or enforcement are to be applied.

Disposition of collateral: Warranties of title. Section 9-610 imposes on a secured party who disposes of collateral the warranties of title, quiet possession, and the like that are otherwise applicable under other law. It also provides rules for the exclusion

or modification of those warranties.

Disposition of collateral: Notification, application of proceeds, surplus and deficiency, other effects. Section 9–611 requires a secured party to give notification of a disposition of collateral to other secured parties and lienholders who have filed financing statements against the debtor covering the collateral. (That duty was eliminated by the 1972 revisions to Article 9.) However, that section relieves the secured party from that duty when the secured party undertakes a search of the records and a report of the results is unreasonably delayed. Section 9–613, which applies only to non–consumer transactions, specifies the contents of a sufficient notification of disposition and provides that a notification sent 10 days or more before the earliest time for disposition is sent within a reasonable time. Section 9–615 addresses the application of proceeds of disposition, the entitlement of a debtor to any surplus, and the liability of an obligor for any deficiency. Section 9–619 clarifies the effects of a disposition by a secured party, including the rights of transferees of the collateral.

Rights and duties of secondary obligor. Section 9–618 provides that a secondary obligor obtains the rights and assumes the duties of a secured party if the secondary obligor receives an assignment of a secured obligation, agrees to assume the secured party’s rights and duties upon a transfer to it of collateral, or becomes subrogated to the rights of the secured party with respect to the collateral. The assumption, transfer, or subrogation is not a disposition of collateral under Section 9–610, but it

does relieve the former secured party of further duties. Former Section 9–504(5) did not address whether a secured party was relieved of its duties in this situation.

Transfer of record or legal title. Section 9–619 contains a new provision making clear that a transfer of record or legal title to a secured party is not of itself a disposition under Part 6. This rule applies regardless of the circumstances under which the transfer of title occurs.

Strict foreclosure. Section 9–620, unlike former Section 9–505, permits a secured party to accept collateral in partial satisfaction, as well as full satisfaction, of the obligations secured. This right of strict foreclosure extends to intangible as well as tangible property. Section 9–622 clarifies the effects of an acceptance of collateral on the rights of junior claimants. It rejects the approach taken by some courts—deeming a secured party to have constructively retained collateral in satisfaction of the secured obligations—in the case of a secured party’s unreasonable delay in the disposition of collateral. Instead, unreasonable delay is relevant when determining whether a disposition under Section 9–610 is commercially reasonable.

Effect of noncompliance: “Rebuttable presumption” test. Section 9–626 adopts the “rebuttable presumption” test for the failure of a secured party to proceed in accordance with certain provisions of Part 6. (As discussed in Comment 4.j., the test does not necessarily apply to consumer transactions.) Under this approach, the deficiency claim of a noncomplying secured party is calculated by crediting the

obligor with the greater of the actual net proceeds of a disposition and the amount of net proceeds that would have been realized if the disposition had been conducted in accordance with Part 6 (e.g., in a commercially reasonable manner). Section 9–626 rejects the “absolute bar” test that some courts have imposed; that approach bars a noncomplying secured party from recovering any deficiency, regardless of the loss (if any) the debtor suffered as a consequence of the noncompliance.

“Low-price” dispositions: Calculation of deficiency and surplus. Section 9–615(f) addresses the problem of procedurally regular dispositions that fetch a low price. Subsection (f) provides a special method for calculating a deficiency if the proceeds of a disposition of collateral to a secured party, a person related to the secured party, or a secondary obligor are “significantly below the range of proceeds that a complying disposition to a person other than the secured party, a person related to the secured party, or a secondary obligor would have brought.” (“Person related to” is defined in Section 9–102.) In these situations there is reason to suspect that there may be inadequate incentives to obtain a better price. Consequently, instead of calculating a deficiency (or surplus) based on the actual net proceeds, the deficiency (or surplus) would be calculated based on the proceeds that would have been received in a disposition to person other than the secured party, a person related to the secured party, or a secondary obligor.

j. Consumer Goods, Consumer–Goods Transactions, and Consumer Transactions.
This Article (including the accompanying conforming revisions (see Appendix I))

includes several special rules for "consumer goods," "consumer transactions," and "consumer-goods transactions." Each term is defined in Section 9-102.

(i) Revised Sections 2-502 and 2-716 provide a buyer of consumer goods with enhanced rights to possession of the goods, thereby accelerating the opportunity to achieve "buyer in ordinary course of business" status under Section 1-201.

(ii) Section 9-103(e) (allocation of payments for determining extent of purchase-money status), (f) (purchase-money status not affected by cross-collateralization, refinancing, restructuring, or the like), and (g) (secured party has burden of establishing extent of purchase-money status) do not apply to consumer-goods transactions. Section 9-103 also provides that the limitation of those provisions to transactions other than consumer-goods transactions leaves to the courts the proper rules for consumer-goods transactions and prohibits the courts from drawing inferences from that limitation.

(iii) Section 9-108 provides that in a consumer transaction a description of consumer goods, a security entitlement, securities account, or commodity account by Article 9-defined "type" alone (e.g., "all consumer goods" or "all securities accounts") is not a sufficient collateral description in a security agreement.

(iv) Sections 9-403 and 9-404 make effective the Federal Trade Commission's anti-holder-in-due-course rule (when applicable), 16 C.F.R. Part 433, even in the absence of the required legend.

(v) The 10-day safe-harbor for notification of a disposition provided by Section 9-612 does not apply in a consumer transaction.

(vi) Section 9-613 (contents of notice of disposition) does not apply to a consumer-goods transaction.

(vii) Section 9-614 contains a safe-harbor form of notification, in "plain English," for consumer-goods transactions.

(viii) Section 9-616 requires a secured party in a consumer-goods transaction to provide a debtor with a notification of how it calculated a deficiency at the time it first undertakes to collect a deficiency.

(ix) Section 9-620 prohibits partial strict foreclosure with respect to consumer goods collateral and, unless the debtor agrees to waive the requirement in an authenticated record after default, in certain cases requires the secured party to

dispose of consumer goods collateral which has been repossessed.

(x) Section 9–626 (“rebuttable presumption” rule) does not apply to a consumer transaction. Section 9–626 also provides that its limitation to transactions other than consumer transactions leaves to the courts the proper rules for consumer transactions and prohibits the courts from drawing inferences from that limitation.

k. Good Faith. Section 9–102 contains a new definition of “good faith” that includes not only “honesty in fact” but also “the observance of reasonable commercial standards of fair dealing.” The definition is similar to the ones adopted in connection with other, recently completed revisions of the UCC.

l. Transition Provisions. Part 7 (Sections 9–701 through 9–707) contains transition provisions. Transition from former Article 9 to this Article will be particularly challenging in view of its expanded scope, its modification of choice-of-law rules for perfection and priority, and its expansion of the methods of perfection.

m. Conforming and Related Amendments to Other UCC Articles. Appendix I contains several proposed revisions to the provisions and Comments of other UCC articles. For the most part the revisions are explained in the Comments to the proposed revisions. Cross-references in other UCC articles to sections of Article 9

also have been revised.

Article 1. Revised Section 1-201 contains revisions to the definitions of "buyer in ordinary course of business," "purchaser," and "security interest."

Articles 2 and 2A. Sections 2-210, 2-326, 2-502, 2-716, 2A-303, and 2A-307 have been revised to address the intersection between Articles 2 and 2A and Article 9.

Article 5. New Section 5-118 is patterned on Section 4-210. It provides for a security interest in documents presented under a letter of credit in favor of the issuer and a nominated person on the letter of credit.

Article 8. Revisions to Section 8-106, which deals with "control" of securities and security entitlements, conform it to Section 8-302, which deals with "delivery." Revisions to Section 8-110, which deals with a "securities intermediary's jurisdiction," conform it to the revised treatment of a "commodity intermediary's jurisdiction" in Section 9-305. Sections 8-301 and 8-302 have been revised for clarification. Section 8-510 has been revised to conform it to the revised priority rules of Section 9-328. Several Comments in Article 8 also have been revised.