Publicity in secured transactions law: Towards a European public notice filing system for non-possessory security rights in movable assets?
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Chapter 6

Examination of the Art. 9 UCC notice filing system
1. Introduction

Part I of this thesis examined the need for public information on non-possessory security interests by mapping the problems and risks that exist for several types of parties involved in and exposed to secured transactions in a system where public filing is not available (a 'non-public filing system'). The outcome of this examination was that the absence of a public filing system entails several legal risks for these parties.

First, it exposes first and second-in-time secured lenders, secured trade creditors, and attaching unsecured creditors to the risk of 'proprietary conflicts', i.e. conflicts where parties fight for the same asset or for competing proprietary positions therein. This is undesirable from the perspective of various parties investigated in this thesis, since at least one of the parties involved in such a proprietary conflict will always lose and incur costs. Moreover, to the extent that this risk materializes in practice and lenders pass on these costs to their borrowers (i.e. 'debtors') in the form of one or more credit surcharges, these debtors pay a higher interest rate for their loans, i.e. incur costs they would not have incurred had publicity – in the abstract – been available. Another important consequence of the absence of 'publicity' is that the moment at which security interests take effect (against third parties) can be antedated fraudulently. This entails a risk for all (secured and unsecured) creditors of the debtor except the perpetrator of the fraud itself, since the latter, by committing such fraud, feathers its nest at the expense of the debtor's other creditors. This equally causes the parties investigated in this thesis to incur costs and sustain damage, which would have been avoided had publicity been available.

Whether promotion of publicity in the form of a public notice filing system is in the interests of these parties depends on a variety of (political or non-political) reasons. This thesis proceeds from the proposition that it is worthwhile to strive for public filing if it effectively addresses the above-mentioned legal risks and does so in a manner that is cost-efficient for the parties concerned, i.e. in accordance with a cost-benefit analysis. This chapter will conduct this analysis for the notice filing system that is often cited as the prime example for future European secured transactions law: the Art. 9 UCC notice filing system.

1 Cf. 'Publicity of Security Rights' (London: EBRD, 2004), p. 4: "The development of a publicity system is essentially an economic exercise, not a legal one, where the ultimate objective is the reduction of risk" and 'Secured Transactions Systems and Collateral Registries' (Washington DC: IFC, 2010), p. 47: "To reduce the risk of lending to an acceptable level, a secured creditor must have confidence in the collateral on which the creditor relies. That confidence requires that the secured creditor have notice of all claims against the collateral that may impair the secured creditor's priority (...)."

2 This is only not so if the creation of undisclosed non-possessory security is subject to a requirement to ensure date-certainty, as in the Netherlands, for instance. See supra Chapter 3, subsections 2.2.3 -2.2.4.

3 The ultimate aim of this approach is to assess whether it is likely that the adoption of a public filing system on a European scale will be economically efficient for the parties that are typically involved in secured transactions and operate within the borders of the European Union; see supra Chapter 2, subsection D.2.
1. Introduction

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First, it exposes first and second-in-time secured lenders, secured trade creditors, and attaching unsecured creditors to the risk of ‘proprietary conflicts’, i.e. conflicts where parties fight for the same asset or for competing proprietary positions therein. This is undesirable from the perspective of various parties investigated in this thesis, since at least one of the parties involved in such a proprietary conflict will always lose and incur costs.1 Moreover, to the extent that this risk materializes in practice and lenders pass on these costs to their borrowers (i.e. ‘debtors’) in the form of one or more credit surcharges, these debtors pay a higher interest rate for their loans, i.e. incur costs they would not have incurred had publicity – in the abstract – been available. Another important consequence of the absence of ‘publicity’ is that the moment at which security interests take effect (against third parties) can be antedated fraudulently.2 This entails a risk for all (secured and unsecured) creditors of the debtor except the perpetrator of the fraud itself, since the latter, by committing such fraud, feathers its nest at the expense of the debtor’s other creditors. This equally causes the parties investigated in this thesis to incur costs and sustain damage, which would had been avoided had publicity been available.

Whether promotion of publicity in the form of a public notice filing system is in the interests of these parties depends on a variety of (political or non-political) reasons. This thesis proceeds from the proposition that it is worthwhile to strive for public filing if it effectively addresses the above-mentioned legal risks and does so in a manner that is cost-efficient for the parties concerned, i.e. in accordance with a cost-benefit analysis.3 This chapter will conduct this analysis for the notice filing system that is often cited as the prime example for future European secured transactions law: the Art. 9 UCC notice filing

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3 The ultimate aim of this approach is to assess whether it is likely that the adoption of a public filing system on a European scale will be economically efficient for the parties that are typically involved in secured transactions and operate within the borders of the European Union; see supra Chapter 2, subsection D.2.
system. It will first evaluate whether Art. 9 UCC offers an effective solution for the problems that exist in a non-public filing system. At the same time, it will consider whether it is likely that Art. 9 UCC does so at lower cost than the investigated parties would incur in a non-public filing system. The cost-efficiency aspects of the filing system will be addressed in mere conceptual terms and will be mapped on the basis of several ‘deciding factors’, e.g. the direct costs that are incurred to make use of the filing system (such as search and filing fees), but also the indirect costs such as its user-friendliness and effort that parties must make in order to use it. This includes the difficulties in practice of needing to check and monitor the filing system, as well as the time required for updating and the risk of potential errors.

To the extent that the EU may feel inclined to adopt a filing system for considerations of efficiency, the outcome of this analysis will enable the EU to make an informed decision about whether or not to adopt a European public notice filing system at all. If the EU were to adopt such a system, the outcome may be helpful for designing a filing system as efficiently as possible. This will be dealt with in Chapter 7.

2. The Art. 9 UCC approach to proprietary conflicts

2.1. Basics and positive aspects of the Art. 9 UCC approach

Art. 9 UCC settles several types of ‘proprietary conflicts’, i.e. conflicts where parties fight for the same (proprietary position in the) asset. Art. 9 UCC not only settles, but also, to the extent that the investigated parties (can) publicize a notice of their interest in the public filing system, prevents these conflicts. This applies to proprietary conflicts involving first-in-time secured lenders and – in some U.S. states – to proprietary conflicts involving first-in-time judicial lien creditors.

Art. 9 UCC allows secured lenders to file a financing statement of their security interest and induces them to do so by stipulating that a security interest has no effect against several types of second-in-time parties if such a notice has not been filed and has not been otherwise ‘perfected’ either. These ‘successors’ – comprising second-in-time secured lenders, secured sellers, judicial lien creditors and buyers outside the ordinary

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4 When analyzing Art. 9 UCC, I will not discuss each and every amendment that has been adopted over time in various states, but will rather concentrate on a limited number of striking examples to illustrate its downsides and shortcomings. Accordingly, I will not exhaustively discuss all potential pitfalls that may be encountered under Art. 9 UCC. My analysis aims to provide a general insight into the operation of Art. 9 UCC, which I consider relevant for the purposes of the subject of this thesis.

5 In other words, it will ask: does Art. 9 UCC actually solve these problems, i.e. does it mitigate these risks? See supra Chapter 1, subsection D.2.1.

6 See supra Chapter 1, subsection D.2.2.

7 Cf. ‘Secured Transactions Systems and Collateral Registries’ (Washington DC: IFC, 2010), p. 70: “Since the costs of registration constitute a burden on secured transactions, they should be minimized. Such costs include both the costs of preparation and presentation of notices and the fees paid for registration and searching.”

8 See supra Chapter 5, section 4.
course of business – are induced to check the filing system because they are charged with constructive notice of filings made.9

“(…) the filing system is designed to allow earlier parties to communicate with later parties about the possible existence of security interests.”10

To the extent that these successors are secured lenders, they are induced to also file a financing statement themselves (or otherwise perfect their interest), since Art. 9 UCC is based on a pure ‘race statute’, which means that whoever files first wins, irrespective of the parties’ knowledge.11 By settling priority conflicts primarily on the ‘easily determinable fact’12 of filing, Art. 9 UCC avoids conflicts about who perfected first, which is cost-efficient for the parties concerned. At the same time, it prevents the debtor from withholding (the correct) information as to whether prior security interests have been created, as might be the case in a non-public filing system, thereby mitigating the risk of proprietary conflicts.13 However, because a filing is no more than a warning about the possible existence of security, proprietary conflicts are not prevented solely on the basis of the filing system; this is why it is called a ‘notice filing system’. If second-in-time parties come across a filed notice, they will need to ask the secured party on file to what extent this ‘notice’ represents the actual state of affairs.14

9 A similar mechanism applies to first-in-time PMSIs on inventory collateral: vis-à-vis first-on-file lenders the PMSI will have the status of ‘super priority’, but only if the purchase money lender achieves perfection e.g. by filing before the debtor receives possession of the inventory collateral and the purchase money lender has notified the first-on-file lender that it has or expects to acquire a PMSI (§ 9-342(b)). See supra Chapter 5, subsection 4.3.2.

10 Livingston 2007, p. 156. Cf. LoPucki 2007, p. 283: “The function of the Article 9 filing system is to provide notice of priority conflicts to those who consider taking subsequent ones (hereafter “searchers”).” See also Fredrickson 2007, p. 1: “Before taking a security interest in the debtor’s property, most lenders want to know that no other party can claim active security interest in the property in question. The Article 9 filing system exists to provide this assurance.”

11 Hence, even if the first-to-file had knowledge of an earlier security interest. See § 9-322(a)(1) UCC, which is discussed in more detail in Chapter 5, subsection 4.3.1.

12 Cf. Baird & Jackson 1982, p. 185: “A debtor will be deterred from misbehaving, since a filing system deprives him of the possibility of gaining from such misbehavior”, and: “A filing system places fewer restrictions on the use of collateral than does a possession-based solution to the ostensible ownership problem, yet it still provides information that allows a creditor to avoid the uncertainty caused by the possibility of debtor misbehavior.”

13 As discussed in subsection 1.3.2 of Chapter 5, a financing statement can (and will often) be filed in advance of any finance transaction. A warning therefore does not mean that security is actually in place or that the assets concerned may not be available to serve as security. Similarly, a valid security interest that is still on record as such may have ceased to exist because the secured claim has been discharged without the release of the properly recorded security. Cf. Adler, Baird & Jackson 2007, p. 15: “The financing statement is intended only to give others notice that a creditor may have a security interest. If they need details, they must look elsewhere.” See also Sigman 1999b, p. 865: “(…) the function of the filing system is not to give detailed information which can be relied on without inquiry of the debtor supplemented by such further investigation as a prospective secured party may deem appropriate under the circumstance”, Livingston 2007, p. 112: “The goal of filing was merely to put third parties on notice that security interests might exist as opposed to providing detailed information about the nature and extent of the secured party’s financing arrangement with the debtor. It was then up to interested third parties to seek out further
This inquiry can be made on the basis of the filed financing statement, which contains, besides the debtor’s name and an indication of the collateral, the name and address of the purported secured party.\(^{16}\) At the debtor’s request, secured parties on file have a duty to provide the debtor with exact information regarding the collateral and the obligation(s) secured.\(^{16}\) The debtor can pass on this information to the parties that made the request for ‘further information’.\(^{17}\)

By making ‘further inquiry’, second-in-time parties can establish the exact scope and extent of an alleged proprietary claim and act appropriately on this information, \(i.e.\) make informed decisions. Depending on whether prospective parties are lenders, buyers outside the ordinary course of business or judicial lien creditors, such decisions may take different forms.

If a second-in-time \textit{lender} is satisfied that a prior security interest does indeed exist, it may choose to accept that its position will be subordinated. Alternatively, if it wants to grant the debtor a secured loan only on a first priority-basis, it may want to work out a satisfactory arrangement with the first-in-time secured lender.\(^{18}\) In that case, it will have filed a financing statement itself\(^{19}\) and will ask the first-in-time secured lender to release (part of) the collateral and terminate or amend its financing statement accordingly.\(^{20}\) If the lender on file is not willing to facilitate this, the second-in-time lender may try to see if certain collateral may nonetheless be available to it (and advance its loan against that collateral), or decide to refrain from providing the requested financing altogether.\(^{21}\)

A similar mechanism applies to prospective \textit{buyers} operating outside the (seller’s) ordinary course of business, the only difference being that buyers cannot \textit{file} their own interest in the public filing system: they are charged with constructive knowledge of

\(^{15}\) See supra Chapter 5, subsection 3.3.1 and § 9-502(a) UCC.

\(^{16}\) This information has to be provided to the debtor within 14 days after the date of receipt of the request; see § 9-210(b)-(e) UCC. See supra Chapter 5, subsection 3.7.5.

\(^{17}\) We will see in subsection 2.4.1 that there is no legal \textit{duty} for the debtor to cooperate in this respect, nor is there an obligation for secured parties to respond to a request for credit information from \textit{third parties}.


\(^{19}\) This is because Art. 9 UCC is based on a pure ‘race statute’, which means that whoever files first wins, irrespective of the parties’ knowledge; see supra footnote 11.

\(^{20}\) Alternatively, the second-in-time lender may request an estoppel letter whereby the first-in-time lender disclaims an interest in certain collateral. Hodnefield; see infra footnote 40.

existing filings (§ 9-507(a)). Consequently, if buyers are satisfied that a prior security interest does indeed exist, in order to acquire an asset free from a prior encumbrance they will have to insist that the secured lender on file terminates the financing statement or amends it to exclude the purchased collateral and provide a release of the purchased collateral from the security interest. If the secured lender on file is not willing to cooperate, then to be safe, the buyer will have to refrain from the transaction.

In theory, this mechanism equally applies to judicial lien creditors (although these creditors can only file their attachment claim in some states). If a secured lender perfects its security interest or files a financing statement and the debtor has authenticated a security agreement before an unsecured creditor acquires a lien on the debtor’s property by attachment, levy, or the like, the former will win. Judicial lien creditors are therefore charged with constructive notice of filed notices. Unlike buyers or secured lenders, however, judicial lien creditors will have no leverage to ask the debtor or the secured lender on file for further information. Attaching unsecured creditors will therefore only have the filing system as a source of information, for whatever that is worth. Subsection 2.2.2 will deal with this subject.

In some states, not only secured lenders but also judicial lien creditors are allowed to file their judgment in the Art. 9 UCC filing system. In this case, the filing procedure is slightly different from that for perfecting a security interest in property under the UCC: instead of a financing statement, ‘notice of judgment lien’ has to be filed in the UCC filing office. Once the judgment creditor has received payment, the debtor can ask the creditor to file an ‘acknowledgment of satisfaction of judgment’. If a state allows the creation of a lien by filing it in the records (such as California; see supra Chapter 5, subsection 4.1.3), the filing mostly constitutes constructive notice to prospective lenders and buyers at penalty of losing or not obtaining their interest or priority position vis-à-vis a lien creditor. Accordingly, in these states the risk of proprietary conflicts between judicial lien creditors, i.e. seizing unsecured creditors (amongst themselves), and prospective secured lenders and buyers acting outside the ordinary course of business is mitigated.

By providing the above-mentioned rules, Art. 9 UCC prevents both first-in-time and second-in-time secured lenders and buyers from obtaining a different (worse) proprietary position than stipulated or anticipated. As a result, it provides an effective solution to the risk of proprietary conflicts for these parties. That Art. 9 UCC is far from perfect, however, will be addressed in the next subsections. First, it will be made clear that Art. 9 UCC does not mitigate proprietary conflicts between several of the other types of investigated parties (subsection 2.2). Second, it will be shown that insofar as Art. 9 UCC does not mitigate proprietary conflicts between several of the other types of investigated parties (subsection 2.2). Second, it will be shown that insofar as

22 See supra Chapter 5, subsection 4.5.2. and 4.5.3.
23 This mechanism does not apply to buyers in the ordinary course of business. See supra Chapter 5, subsection 4.5.1.
24 See § 9-102(a)(52) UCC. The same applies in bankruptcy: the trustee in bankruptcy can avoid unperfected security interests, after which the collateral becomes part of the bankruptcy estate and can be liquidated by the trustee for the benefit of the general unsecured creditors; see § 544(a)(1) BC. See supra Chapter 5, subsections 4.1.2-4.2.3.
prevents proprietary conflicts, it is doubtful whether it does so at a lower cost than the investigated parties would incur in a non-public filing system, i.e. in a manner that is cost-efficient for the parties concerned. This is largely attributable to the practical process of filing and searching financing statements (subsection 2.3), but can also be ascribed to other limitations of the Art. 9 UCC notice filing system (subsections 2.4-2.5).

2.2. Shortcomings in Art. 9 UCC's basic structure and rules
2.2.1. The 'Untraceables'
Under Art. 9 UCC, some types of proprietary conflicts are not prevented at all, simply because not all proprietary interests are public, or only become public after a certain period of time. This applies to proprietary conflicts involving purchase money lenders and purchase money sellers and – in some states – to proprietary conflicts involving judicial lien creditors. I will elaborate on both issues.

Art. 9 UCC affords PMSIs ‘super-priority’ as soon as they come into existence, i.e. even when a notice of their existence has not (yet) been filed. To obtain this status, purchase money lenders and sellers have to perfect their PMSI within 20 days after the debtor receives possession of the assets.25 Hence, unlike ordinary security interests, purchase money lenders and sellers are offered a grace period: as long as the financing statement is filed within 20 days, the PMSI is perfected as from the moment the debtor had received possession of the collateral (and thus with retroactive effect).26 Unless one already regards the publicly known fact that PSMIs may exist and have priority as a manifestation of publicity, the outcome of this is that the risk of proprietary conflicts between PMSI lenders and sellers and prospective secured lenders is not mitigated under Art. 9 UCC. A similar rule applies in respect of judicial lien creditors27 and buyers28 that attempt to respectively seize or buy PMSI goods: the PMSI will be untraceable until the moment it is registered, which is may be as long as 20 days after its creation. As a result, second-in-time ordinary secured lenders, judicial lien creditors and buyers may always be faced with a PSMI the existence of which they were not aware of.

25 § 9-317(e) UCC.
26 The rationale for the ‘super-priority’ is manifold and it is granted even if the purchase money lender or seller knows that a conflicting security interest has been created or that a conflicting financing statement covering the same collateral has been filed by another lender. Further details of these rules are provided in Chapter 5, subsection 2.3.
27 A purchase money lender takes priority over the rights of a judicial lien creditor if the former files a financing statement with respect to the PMSI before or within 20 days after the debtor receives delivery of the collateral and the judicial lien has arisen between the time the security interest attaches and the time of filing (§ 9-317(e) UCC). For an example see infra Chapter 5, subsection 4.2.4.
28 The 20-day grace period that purchase money lenders have as against judicial lien creditors is similarly applicable as against these buyers (§ 9-317(e) UCC); see previous footnote and Chapter 5, subsection 4.5.4.
This risk is solved in relation to ordinary secured lenders, in the context of inventory financing. Here, the risk of proprietary conflicts between purchase money lenders and sellers vis-à-vis prospective secured lenders is addressed, by requiring two things of the purchase money lenders and sellers. First, they will only achieve super-priority over earlier-filed ordinary security interests if they perfect — i.e. file — before the debtor receives possession of the inventory. In other words, there is no 20-day grace period. Second, purchase money lenders and sellers must notify earlier-filed lenders that they have or expect to acquire a PMSI in the described inventory.

As regards the issue of judicial lien creditors, in most U.S. states they cannot file their judgment, with the result that proprietary conflicts between the parties, i.e. first-in-time judicial lien creditors and later-in-time secured lenders and judicial lien creditors, are not prevented. Under Art. 9 UCC, both conflicts are decided in favor of the first-in-time judicial lien creditor. Hence, secured lenders may take a security interest in assets that have already been attached by unsecured creditors. Although not examined in detail in this thesis, similar observations may apply in the context of proprietary conflicts between the first-in-time judicial lien creditors and buyers outside the ordinary course of business.

In addition to the aforementioned 'untraceable' interests, it could be argued that possessory security interests are untraceable also, as a result of which proprietary conflicts between secured lenders that have perfected their security interest by taking possession of the debtor’s assets and successors are not prevented. After all, when a

29 See supra Chapter 5, subsection 4.3.2.
30 § 9-324(a) UCC. Purchase money lenders and sellers therefore have to search the files to know whom, i.e. which inventory lender, they have to notify. Although a PMSI notification is supposed to be able to encompass multiple transactions, this must be received before, but not more than five years before, the debtor receives possession of the inventory (§ 9-324(b)(3) UCC). This means that the notification is good for five years. See Official Comment 3 to § 9-324 UCC and Sigman 2004, p. 74. If the inventory lender has not received notification (or if the other security interest does not qualify as a PMSI), any advance made in normal circumstances will have priority under the basic priority rule of § 9-322 UCC. Inventory lenders are thus enabled to consciously decide to not make other advances when they receive this notification. At the same time, such fraud is prevented without the need for inventory lenders to search the filing system. See e.g. Official Comment 4 to § 9-324 UCC, Harris & Mooney 2006, p. 251, LoPucki & Warren 2012, p. 477 and White & Summers 2002, § 33-4 on this rule.
31 First, only if a secured lender perfects its security interest or files a financing statement and the debtor has authenticated a security agreement before a secured creditor acquires a lien on the debtor’s property by attachment, levy, or the like — i.e. before the latter becomes a ‘judicial lien creditor’ — the former will win; see § 9-102(a)(52) UCC. Second, judicial lien creditors have priority according to the prior tempore rule: a creditor who became a judicial lien creditor before another creditor, has priority over the latter. See supra Chapter 5, subsection 4.1.3.
32 As explained in Chapter 5, subsections 4.1.2-4.1.3, creation of a lien differs from state to state: it can be created by taking possession of the debtor’s property, by execution, by delivering the writ of execution to the sheriff and, in a growing number of states, by filing a financing statement with the UCC filing office. In states where judicial lien creditors can file their judgment this risk is mitigated; see also subsection 2.1 of this Chapter. See also on this subject Stürner 2008, p. 171.
33 Chapter 5, subsection 4.9 already indicated that it was beyond the scope of this thesis to describe all the different ways a buyer of the debtor can come into conflict with debtor’s judicial lien creditors. It did indicate, however, that if a state allows judgment creditors to file their lien in the public records, the filing mostly constitutes constructive notice to potential buyers, lenders and subsequent judicial lien creditors.
security interest is perfected by taking possession, a financing statement will not be filed and, accordingly, not be found by checking the filing system. In Chapter 2 I already addressed the issue that ‘possession’, when considered purely in the abstract, can indeed signify many relationships and might be (too) ambiguous for the purpose of giving notice. However, to the extent that possessory security interests are still used, disposssession will nonetheless serve the function of giving notice that the assets might be encumbered, as it signifies that another party holds the assets. In addition to checking the filing system, searchers should therefore always verify whether a lender has taken possession of the collateral. This attracts costs.\footnote{34}

2.2.2. Provision of information is mainly based on leverage

What might also be called an ‘imperfection’ in Art. 9 UCC’s basic structure is the fact that the Art. 9 UCC notice filing system is largely based on leverage and economic compulsion. Since there is no obligation for lenders on file to respond to information requests by third parties, the exact scope and extent of any proprietary rights they purportedly hold can be established only through the debtor.\footnote{35} In practice, secured parties generally cooperate voluntarily and respond promptly to requests for information. However, they have no obligation to respond to anything other than a request by the debtor and, moreover, there is no legal duty for the debtor to cooperate. Since most debtors have an interest in obtaining new loans or selling their assets, they will want to satisfy prospective lenders and buyers that the collateral is free of security. They will therefore want to facilitate as far as possible the removal or amendment of an erroneous filing. Vis-à-vis enforcing unsecured creditors, this is clearly different. Debtors would be more likely to have the opposite interest of pretending that in fact the assets are encumbered and therefore not available for recovery, and will be incentivized to withhold information showing that the assets are unencumbered.\footnote{36} Thus, the Art. 9 UCC filing system is the gateway to further information concerning the debtor’s assets, but not for everyone. If there is a filing on file with respect to the debtor’s assets, enforcing unsecured creditors will be warned about the possible encumbrance of these assets, but

\footnote{34}{Because the basic priority rule is that ‘the first to file or perfect’ wins (§ 9-322(a)(1) UCC), this ‘off record’ step of checking whether the debtor has the goods in its possession would ideally be conducted right after the creditor has filed its financing statement. The risk of an earlier perfected competing security interest would simply remain if the collateral were inspected at a later time.}

\footnote{35}{With regard to the fact that only debtors can make this kind of requests, Official Comment 3 to § 9-210 UCC provides the following information: “Because creditors of and prospective purchasers from a debtor may have legitimate needs for more detailed information, it is necessary to provide a procedure under which the secured party will be required to provide information. On the other hand, the secured party should not be under a duty to disclose any details of the debtor’s financial affairs to any casual inquirer or competitor who may inquire. For this reason, this section gives the right to request information to the debtor only. The debtor may submit a request in connection with negotiations with subsequent creditors and purchasers, as well as for the purpose of determining the status of its credit relationship or demonstrating which of its assets are free of a security interest.”}

\footnote{36}{However, in most states and federal courts a judgment creditor can force a debtor (or its representative) to answer questions about its assets and financial condition under oath. It is beyond the scope of this thesis to elaborate on this. I am indebted to Professor Mooney Jr. for providing me with this information, for which however I myself take full responsibility.}
no more than that. This means that the risk of proprietary conflicts between existing lenders and enforcing unsecured creditors is not mitigated by Art. 9 UCC. It is therefore likely that enforcing unsecured creditors will continue to take enforcing measures no matter whether there is a filing on file. They will probably just give it a shot, because another purpose of attaching legal assets is to put the debtor under pressure. That the aim of Art. 9 UCC is not to inform unsecured creditors about whether or not to levy, but only to facilitate the process of determining priorities among ‘purchasers’, is a broadly shared view.

2.3. Shortcomings in the process of searching the filing system

Various shortcomings and deficiencies in the way Art. 9 UCC has been implemented keep it from being fully effective in its goal to prevent proprietary conflicts. In particular the process of filing and searching financing statements shows weaknesses.

2.3.1. Difficulties in determining where to search and file

The first main problem in the practical process of filing and searching for financing statements is that it is difficult to determine where to file and search, i.e. in which filing office. As I mentioned earlier, the filing and searching take place in one of the many filing offices located in the United States. Although Art. 9 UCC and other legislation aim to guide lenders and other creditors to the correct filing office in which to file, it turns out that finding the correct filing office is not actually so easy.

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37 LoPucki, Abraham & Delahaye 2013, p. 1803: “In the American system, this creditor [i.e. an unsecured creditor that is considering whether to take legal action against its debtor, D[UYH] would have the right to only the names of persons who might have security interests in general categories of property those interests might encumber.”

38 Another reason why unsecured creditors may want to attach the assets despite a filing, is the fact that they will trump the lender on file by obtaining the status of ‘judicial lien creditor’ before the lender has authenticated the security agreement with the debtor. See supra Chapter 5, subsection 4.2.2.

39 LoPucki, Abraham & Delahaye 2013, p. 1860: “(…) the English view their system as serving the public. The Americans view their system as serving only debtors and secured creditors. As a result, the English make more information available to a wider range of users than do Americans.” See also p. 97: “The key policy choice remaining is between the American view — that security agreements should be private because the filing system exists only for the benefit of secured creditors and their debtors — and the English view that security agreements should be public because the filing system exists for the benefit of everyone affected by security interests.” Cf. Baird on the Art. 9 UCC notice filing system: “In short, the Code’s notice filing system addresses principally only one kind of ostensible ownership problem — the one arising from competition between secured creditors.” Baird 1983, p. 66.

40 I am especially indebted to Paul Hodnefield (Associate General Counsel at Corporation Service Company; a specialist in Article 9 UCC searching and filing issues), who was most helpful in assisting me to obtain the information provided in this chapter and for which I naturally assume full responsibility.

41 In the United States as a whole there are more than 4,000 filing offices. Most of these filing offices are ‘local filing offices’, dedicated to specific types of collateral or to specific types of liens. Each state has only one UCC filing office covering a broad range of collateral security rights on personal property and fixtures; see supra Chapter 5, subsection 3.3.3 and LoPucki 1992, p. 10.

42 See § 9-109(c) UCC, which states that Art. 9 UCC does not apply to the extent that a statute, regulation, or treaty of the United States preempts it. See in particular section (c)(2); “This article does not apply to the extent that: (…) another statute of this State expressly governs the creation, perfection, priority, or enforcement of a security interest created by this State or a governmental unit of this State (…)”
2.3.1.1. Many different types of filing offices

The first obstacle in determining where to file or search is the fact that there are many different types of filing offices. Several scholars have drawn attention to this variety of filing systems, and regard it as a serious problem:

“The task of a lender who would search for messages relating to the collateral, lend money, and leave a message of its own is vastly complicated by the fact that there is not just one message center, but many.”

In the U.S. a distinction is made between UCC filing offices (‘central filing offices’), which cover a broad range of collateral security rights on personal property and fixtures, on the one hand, and many other types of filing offices (‘local’ or ‘non-UCC filing’ offices), on the other hand. Non-UCC filing offices are created by different statutes and are dedicated to particular types of collateral or to specific types of liens.

Most states maintain UCC filing systems for security in personal property and fixtures, with Louisiana and Georgia the only exceptions to the rule. These two states have organized their UCC filing office on a per county or per parish basis, but have nonetheless facilitated a statewide search of such local filings. In addition, all 50 states maintain certificate of title systems with respect to security rights in automobiles, i.e. cars. Many of these states also have separate certificate of title systems for boats and/or mobile homes. Furthermore, different types of filing offices are maintained at the county level. The main example of this is the real estate offices, where mortgages and fixture filings are filed. Besides these (‘local’) real estate offices, counties have often implemented filing systems for several types of tax liens and money judgments. Finally, the federal government has separate filing systems for copyrights, trademarks, patents, and ship and aircraft mortgages.

While some types of collateral are covered exclusively by the UCC filing offices, other types of collateral may be covered by both UCC and non-UCC filing offices. Unhelpfully, the relevant definitions marking the determinative distinctions are far from intuitive.

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43 LoPucki & Warren 2012, p. 285. Cf. Lecture(s) Secured Transactions Law by Prof. R. Mann, Spring 2010 (Columbia University, New York), LoPucki 2009, p. 283 and LoPucki 1995, p. 579: “The Article 9 filing system is a mess. Filings are spread among 4,300 filing offices, each of which imposes its own procedures and requirements. The legal instructions for filing that are standardized in Article 9 are overly complex and ambiguous, frequently making it difficult or impossible to determine in advance the appropriate system in which to file.”
46 A ‘county’ is a geographic division of a state with some form of administrative authority. There are about 3,000 counties in the U.S.; Lecture(s) on Secured Transactions Law by Prof. R. Mann, Spring 2010 (Columbia University, New York).
47 See supra Chapter 5, subsection 3.3.3.2 and § 9-501(a)(1), (2) UCC.
49 The U.S. ratified the Cape Town Convention for security interests in airframes, helicopters, and aircraft engines in 2004 and is still considering whether to ratify the Protocol on Matters Specific to Railway Rolling Stock.
Depending on the context, for example, a car may qualify as ‘equipment’ or as a ‘motor vehicle’, an ‘aircraft’ may in fact be an ‘aircraft part’, and a ‘ship’ may qualify as a ‘boat’.50 While filing in the wrong filing office will render a secured party unperfected (i.e. unenforceable) against prospective parties,51 searching in the wrong filing office may entail the risk that a financing statement of another secured party is filed in another (type of) filing office.52 Hence, from the perspective of both first- and second-in-time lenders, finding the right (type of) filing office is of vital importance to avoid the loss of priority.

Research conducted in 2010 showed that 15% of secured creditors filed their security interest in the wrong filing system and, at the same time, failed to file it in the right filing system. Although this research focused on security interests in trademarks, one of the findings was that when “[e]xtrapolating this data to the entire population, one would expect that approximately (...) 15% of the population were unperfected.”53

In addition to the loss of priority in itself, filing and searching multiple times in order to circumvent the uncertainty that one might file or search in the wrong place, involves repeated filing and searching costs.

2.3.1.2. Difficulties in determining the state in which to search or file (which UCC filing office)

Once it has been found that a transaction is subject to Art. 9 UCC and that the designated filing office is a UCC filing office, the next step is to determine which is the required UCC filing office, i.e. in which state. Non-possessory security rights have to be filed in the UCC filing office of the state where the debtor is located. For registered organizations,54 ‘incorporation-based’ filing is prescribed: filing must take place in the UCC filing office of the state where the debtor is incorporated.55 Determining the debtor’s state of incorporation is relatively easy: each state has a business entity database that will indicate the state of origin, i.e. of incorporation, of every company that is included in the database. This means that it will show whether a particular debtor is a domestic organization or whether it is

51 Cf. LoPucki & Warren 2012, pp. 285-286: “If the secured creditor leaves its message in the wrong office, the message almost certainly will be ineffective. (...). The statutes that create each of these systems specify, with differing degrees of clarity, the circumstances in which a message should be filed in that system.”
52 Cf. LoPucki & Warren 2012, p. 285: “If the later lender searches only in the wrong office, it will miss whatever messages were left in the right office.”
53 Ferguson 2009, p. 213.
54 I remind the reader that ‘registered organizations’ ordinarily include corporations, limited partnerships, limited liability companies and statutory trusts (§ 9-102(a)(71) UCC); see supra Chapter 5, footnote 251 for a detailed definition.
55 Incorporation-based filing was adopted in 2001, mainly because – in Sigman’s words – it ‘facilitates the use of a clear objectively verifiable test’. Sigman 1999a, p. 65. See supra Chapter 5, subsection 3.3.3.1 and § 9-307 UCC.
formed under the law of another state. Most states provide this information both by telephone and online within 24 hours.56

Determining the debtor’s location was much more difficult under the rules in force prior to the 2001 amendments. Back then, security interests in tangible collateral had to be filed in the UCC filing office of the state where the collateral was located, whereas security in certain mobile goods and intangible collateral had to be filed in the UCC filing office of the state where the debtor was located, i.e. former Art. 9 UCC operated under a split approach.57 Since the burden of proof lies with the filing party, the former rule entailed that lenders had to prove not only that tangible collateral was located in a particular state at the time of filing, but also for how long that had been the situation. This resulted in the habit of filers photographing the collateral, in addition to safekeeping other written evidence concerning the state and location of the assets concerned.58 With regard to certain mobile goods and intangible collateral, matters were at least as complicated, because ‘the debtor’s location’ referred to either the debtor’s ‘place of business’ or – if the debtor had more than one place of business – its ‘chief executive office’; notions that are, as I will explain below in the context of non-registered organizations, predominantly subjective. At that time, there was so much uncertainty that leading scholars advised secured parties to “file everywhere possibly required.”59 Fortunately, in 2001 this rule was replaced by a rule that defined the debtor’s location as the place where the debtor was incorporated, i.e. a ‘one-stop shop’ rule.60

While it is relatively easy to establish the debtor’s state of incorporation in the case of registered organizations, there is still much uncertainty with regard to entities that are not formed or organized by the filing of a record with, or the issuance of a record by, a State or the United States, i.e. non-registered organizations.61 Because these types of entities are not incorporated, filing and searching has to take place in the filing office of the state where the debtor is located. However, ‘location’ refers either to the debtor’s ‘place of business’ or – if the debtor has more than one place of business – to its ‘chief executive office’.62 The debtor’s ‘place of business’ is ‘a place where the debtor conducts its affairs’.63

56 It is therefore not necessary to check the business entity index of every state. It is fairly easy to check these records, but for convenience purposes some law firms and financial institutions outsource this to private service companies. Hodnefield, see supra footnote 40. Compare LoPucki 1995, p. 599: “For the vast majority of creditors, discovering the debtor’s correct name and state of incorporation will present no problem. The corporate debtor will know that information and relay it to the creditor. The creditor can verify the information either by searching the public record or obtaining a credit report.” See also pp. 604-605.
57 See § 9-103(1), (3) (1972) UCC and § 9-401 (1972) UCC. For more information, see e.g. Penney 1990, pp. 1417-1418.
59 See LoPucki 1995, pp. 579-580; especially footnote 3, for further references. LoPucki points out that since making and maintaining filings attracts costs and since filing errors were rarely fatal and tended to remain unchallenged anyway, most secured parties did not follow this advice. LoPucki 1995, pp. 579-580.
60 This revision was recommended by the Permanent Editorial Board for the Uniform Commercial Code (“PEB”) in 1992. More information on these recommendations can be found in the PEB Report 1992, p. 78.
61 See Official Comment 11 to § 9-102(a) UCC. Examples are general partnerships, joint ventures and sole proprietorships. See supra Chapter 5, footnote 261.
62 § 9-307(b)(2), (3) UCC.
63 See § 9-307(a) UCC. Official Comment 2 to this section adds that “(…) every organization, even eleemosynary institutions and other organizations that do not conduct ‘for profit’ business activities, has a “place of business.”” White &
Although this term is not defined in the UCC, the debtor’s ‘chief executive office’ is the place from which it manages the main part of its business operations or other affairs, developed under case law as the ‘nerve center’. According to the Official Comment, this is the place where persons would normally look for credit information, and is the appropriate place for filing. It will come as no surprise that the application of both these notions creates much uncertainty as to where to file. Although – according to the Official Comment – it is supposed to be relatively easy to determine which of the debtor’s offices is the chief executive office, it can hardly be a coincidence that the same Official Comment recommends perfecting under the law of each possible jurisdiction in case of doubt. This leads to repeated filing and searching practices, with corresponding unnecessary costs as a result. However, since only a small number of entities qualify as a 'non-registered organization', this issue is not a tremendous burden on the search and file process. Generally, just one or two additional filings or searches will be sufficient to cover any doubt.

Summers indicate that this is the place where e.g. the CEO goes to work. Regarding the transition from debtor-based filing to incorporation-based filing for registered organizations, they say, with relief: “The messy, practical question about where the CEO goes to work and whether that is the chief office will not be relevant.” White & Summers 2002, § 31-16.


See Official Comment 2 to § 9-307 UCC. LoPucki clarifies this by saying that “[t]he nerve center of a business may be virtually anywhere the chief executive officer works.” LoPucki 1995, p. 594, footnote 58.

Compare LoPucki 1995, p. 595: “Designating the chief executive office as the proper place to file is unworkable because creditors may have no practical means of determining where that is.” For an analysis of all the different problems that may arise in determining the debtor’s chief executive office, see LoPucki 1995, p. 595 et seq.

See Official Comment to § 9-307 UCC.

See e.g. LoPucki 1995, p. 597: “Once the location of a debtor is in doubt, the scope of the inquiry the creditor must make to determine that location is enormous. In determining the location of a debtor for this purpose, the courts have considered where the debtor kept its financial records, where the board of directors met, where the debtor’s top management must often worked, whether the business location was temporary or permanent, and numerous other factors.” Attempting to assess the exact amount of these costs falls outside the scope of this thesis, but according to LoPucki they are substantial: “The true costs of a second filing are far from trivial.” LoPucki 1995, p. 597.

Hodnefield, see supra footnote 40.
2.3.2. Difficulties in searching and filing under the debtor’s name

Once the (type of) filing office and the correct state in which to file have been determined, financing statements relating to a particular debtor have to actually be found and identified when filing or conducting a search. There are several things that can go wrong in the filing and searching process. Most of the difficulties relate to stating the debtor’s name.70

2.3.2.1. Problems in ascertaining the debtor’s correct name

The importance of ascertaining the debtor’s correct name and stating that name accurately on the financing statement is evident: if any errors are made by the filer, searchers will both take the lack of any hits resulting from their search as justifying the conclusion that they have priority because no security rights exist. The same applies if the filer has used the correct name, but the filer misspelled the name in its search request.71 It is for this reason that Art. 9 UCC stipulates that a financing statement is sufficient only if it provides the name of the debtor (§ 9-502(a)(1) UCC).

Over the years it became clear that the question of what constitutes ‘the name of the debtor’ is not always easy to answer.72 Art. 9 (1972) UCC provided: “A financing statement sufficiently shows the name of the debtor if it gives the individual, partnership or corporate name of the debtor, whether or not it adds other trade names or the names of partners.” 73 What constituted ‘partnership name’ and ‘corporate name’, however, was not further explained. This created much ambiguity as to which name should be used, both when filing and searching, most importantly because most debtors have more than one name – e.g. legal names, nicknames, trade names. Debtors do little to remove any such unclarity or ambiguity:

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70 Cf. Tu 2010, p. 135: “The issue of the debtor-name sufficiency has plagued filers, searchers, and courts since the inception of Revised Article 9”, Livingston 2011, p. 176: “The key to perfection is getting the debtor’s name right on the financing statement, and that task can sometimes prove more difficult than would first appear” and LoPucki 2007, p. 281: “Errors in debtor’s names have plagued the Article 9 filing system since its inception.” Besides Tu, Livingston and LoPucki, many other scholars have described the problem of stating the debtor’s name; see e.g. Penney 1990, Livingston 2007, p. 146 and Official Comment 2 to § 9-503.

71 Cf. Fredrickson 2007, p. 44, LoPucki 2007, p. 283: “If the debtor’s name is spelled incorrectly in either the financing statement or the search request, the communication can fail, leaving both filer and searcher with the belief that its interest has priority” and Burton 2012, p. 313: “As the name is typically entered manually, the accuracy of the entry of the debtor’s name by the original secured party is crucial to a subsequent lender being able to locate it” and p. 315: “(…) when a searcher types in the correct name of the debtor, the financing statement may not be located, creating the false impression that no one has rights in the collateral other than the debtor himself. Relying on the lack of financing statements located, the searcher would be more likely to extend credit to the debtor, mistakenly believing that in the event of default, the searcher would be able to collect first.” (footnotes omitted)

72 Cf. Burton 2012, p. 314: “At first glance, it would appear that entering a debtor’s name correctly on a financing statement would be a simple requirement for a secured party to fulfill; however, in many circumstances this can be an arduous undertaking.”

73 § 9-402(7) (1972) UCC.
"Debtors use ‘trade names’ without designating them as such; misspell their own corporate names on letterheads, checks and directories; and exchange abbreviations for the words abbreviated at will."

Apart from the question of the correct name to use on the financing statement, Art. 9 (1972) UCC also gave no express guidance on who was to bear the consequences if the wrong (type of) name was used, or if the right name was not spelled accurately. It provided that ‘(…) [a] financing statement substantially complying with the requirements of this section is effective even though it contains minor errors which are not seriously misleading.’

When courts tried to apply this rule in resolving disputes between a filer and a searcher, they more or less got stuck: after all, when does a financing statement satisfy the requirements substantially and when is a mistake in the debtor’s name serious enough to render the financing statement seriously misleading? Before long, courts began to apply the ‘reasonably diligent searcher’ standard. Pursuant to this standard, in order to determine if a minor error was seriously misleading, courts had to judge whether the searcher concerned could have found the financing statement if it had conducted a ‘reasonably diligent search’. Searching under various debtor name alternatives formed part of the exercise. As a result, filers were spared; not only did courts take the liberty of condoning the use of different types of names, they sometimes also held names to be valid despite misspelling. For filers, therefore, ‘being close was often good enough’. Moreover, judges were not always consistent as to whether it was sufficient to state the debtor’s legal name, its trade name, or both. Consequently, searchers persistently ran the risk that a search would not produce all the security interests that existed for any given collateral,

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75 § 9-402(8) (1972) UCC.
76 Burton 2012, p. 316. See also on this subject: Livingston 2007, p. 120 et seq.
77 Courts were induced to do so by the Official Comment 9 to § 9-402 (1972) UCC: ‘[Art. 9 UCC] is designed to discourage the fanatical and impossibly refined reading of such statutory [filing] requirements in which courts have occasionally indulged themselves.’ Compare on this subject Penney 1990, p. 1416 and p. 1424: ‘By adopting U.C.C. Section 9-402(8), the drafters sought to avoid the harshness that appeared to result when only a very minor error was present in the financing statement.’
78 See Livingston 2007, p. 124: ‘Both the “reasonably diligent searcher” standard and the “close enough” standard allowed judges to second-guess what searchers should or should not have been able to discover had they tried hard enough.’
81 See Harris & Mooney 2006, pp. 165-166 and Livingston 2007, pp. 120-123, also for further references to case law under Art. 9 (1972) UCC relating to this matter. This was despite the fact that Official Comment 7 to § 9-402 (1972) UCC actually pointed out that stating the trade name alone was not sufficient: ‘Trade names are deemed to be too uncertain and too likely not to be known to the secured party or person searching the record, to form the basis for a filing system.’

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In the 1990s, the Art. 9 UCC drafters – the NCCUSL and the ALI – took action to remedy the imbalance that placed a heavy burden on searchers. A study committee was appointed to verify whether Art. 9 UCC was in need of revision, which resulted in an amendment of Art. 9 UCC enacted in 2001.85 Most importantly, this amendment elaborated on what constituted the debtor’s ‘name’ for filing and searching purposes. With regard to registered organizations, it stipulated that a financing statement sufficiently provides the debtor’s name if it is the name indicated on the public record of the debtor’s jurisdiction of organization which shows the debtor to have been organized.86 Secondly, the ‘substantial compliance test’, which the courts had reduced to the ‘reasonably diligent searcher’ standard, was fundamentally changed: as of 2001, the ultimate test became not whether the searcher had been ‘reasonably diligent’ enough to actually find the financing statement, but whether a ‘hypothetical search’ under the debtor’s correct name, using the filing office’s ‘SSL’, would have produced the financing statement (§ 9-506(e) UCC).87 Hence, if a secured party had entered the wrong name, but this search did actually uncover the debtor’s exact, correct name.88 Henceforth, due to the adoption of an objective and predictable debtor name standard, the onus was on the debtor to correctly disclose such names to the filing office.89

Clarity as to how to correctly state the name of a registered organization put an end to carelessness or arbitrariness on the part of the filer, because the proper name

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82 Cf. Burton 2012, p. 316: “The “reasonably diligent searcher” standard was rightly criticized since it unduly burdened searchers and it created problematic litigation in which each case had to be addressed flexibly based on idiosyncratic facts.” Cf. Penney 1990, p. 1417.

83 LoPucki 2007, p. 284.

84 See Alces 1995, pp. 689-691, reporting on a study of 100 legal bills generated by law firm Bingham, Dana & Gould, conducted by attorney Meredith Jackson.


86 See § 9-503(a)(1)(2001) UCC and § 9-102(a)(70) UCC. The amendment also stipulated what the correct name was for estates and trusts (§ 9-503(a)(2) and (3) (2001) UCC), and that ‘in other cases’ the individual or organizational name had to be used (§ 9-503(a)(4)(A) (2001) UCC).

87 This rule also entails that a financing statement that is seriously misleading is ineffective, even if it is disclosed by (i) using a search logic other than that of the filing office to search the official records, or (ii) using the filing office’s standard search logic to search a database other than that of the filing office; see Official Comment 2 to § 9-506 UCC. See also on this subject Sigman 1999b, p. 862, Harris, Kilborn & Livingston 2012, pp. 464-465 and Burton 2012, p. 317.

88 Cf. Harris, Kilborn & Livingston 2012, p. 465: “(…) the thought is, “[w]ell, the searcher can find you.””
was now found in the prescribed documents and no longer depended on the name given
to the lenders by the debtor itself (or whatever name it used on its stationery).89 Since the
same revision had adopted ‘incorporation-based’ filing for registered organizations – see
supra subsection 2.2.1.2. – creditors now also had easy access to the files that showed the
debtor’s exact, correct name.90 Henceforth, due to the adoption of an objective and
computerized ‘single search standard’ (or ‘single search safety net’), the measure was no
longer the subjective view of the courts, but the filing system of any given state.91 This
change in the law improved legal certainty and eased the pressure both on searchers and
on courts, which no longer needed to develop a standard with which a searcher had to
comply. Because searchers were relieved of the obligation to conduct multiple searches,
they saved costs.92

Although this was a great improvement in comparison with former law, it soon
became clear that the new name requirements were still somewhat imprecise. While the
individual name standard generated the most controversy, it was also unclear in relation
to registered debtors what documents would qualify to identify the debtor’s name. The
problem was that ‘public record of the debtor’s jurisdiction of organization which shows
the debtor to have been organized’93 could indicate several different types of documents,
such as public records from the state business-entity index94 or state certificates of good
standing.95 See Tu:

“Because the appropriate public record is not specified, the name of a registered organization as set
forth on any number of different public records could arguably comply with this standard.”96

Uncertainty about what documents had to be used made lenders nervous – and rightly so,
given that the names as set forth on the various types of documents often do not match.97

establish an objective procedure for determining whether a given financing statement is sufficient.”
90 Corporate filings were, in other words, migrated to the state of incorporation; see § 9-301(1) and 9-
307(e) (2001) UCC. Cf. LoPucki 2007, pp. 285-286: “That change put the public record showing the debtor’s exact,
correct name in the hands of the filing officer who would receive filings and search requests regarding that debtor.”
91 See Burton 2012, p. 317: “The 1998 revision of Article 9 effectively proposed to take control away from judges and
put that control into the hands of a state’s filing and searching system.” See also on this subject Livingston 2007, pp.
125-126.
92 Penney 1990, pp. 1425 and 1442.
93 See supra footnote 86 of this chapter.
94 Tu 2010, p. 98 explains: “A business-entity index will typically contain the name of all entities organized in the state
and allow the public search for the status of an organization or the availability of a business name.”
95 Tu 2010, pp. 98-99 explains: “(…) a certificate of good standing is typically available to the public and can show that
a particular entity is properly organized in the state.”
96 Tu 2010, p. 86. On p. 131 Tu states: “(…) multiple public records can satisfy it”. Cf. Hodnefield 2007b, p. 3
and Sigman 2011, p. 482: “While filing a financing statement against the name stated in the charter to be the
organization’s name surely satisfies current law, concerns were expressed whether the name “indicated” on one of those other
forms of public record might also satisfy Article 9.”
97 See Hodnefield 2007b, p. 3: “Every state maintains a business entity index. The filing office generally makes some or
all of the data available to the public, often for free over the Internet. The purpose of putting this information online is to give
Consequently, after 2001, lenders often continued to file and search under each possible name of the debtor, or accepted the risk of not being secured. As of 2007, many states began to adopt state-specific amendments to address the lack of a clear debtor-name standard. Due to the adoption of divergent standards, poor quality of the amendments or misunderstanding of the amended rules, courts remained inconsistent in applying the newly adopted search standards, in the case of both individual and corporate names.

It was not until 2010 that this uncertainty was eliminated by changing ‘public record’ to ‘public organic record’. This is the record that was initially filed with or issued by a State or the United States to form or organize an organization. i.e. a...
business’s ‘birth certificate’. This amendment removed any doubt as to whether the originally (and publicly) filed articles of incorporation (as amended) or equivalent formation documents could and should be used to establish the corporate debtor’s name. It thus appears that Art. 9 UCC has slowly found the way to overcome the difficulties resulting from uncertain and non-uniform name standards.

At present, the 2010 amendments have been enacted in all states. However, not everyone was happy about the 2010 amendments. Sigman, for example, argues that the text of Revised Art. 9 (2001) UCC “is manageable and has been quite successful for over five decades, and, thus, that no change at all is absolutely required.” With regard to the rise in state-specific amendments starting from 2007, Sigman’s attitude is highly critical: “Had this provision simply remained a Texas aberration (…), it would have done little harm nationally. However, enthusiastic proselytizing efforts soon began to cause the spread of the disease.”

At the same time, it appears that courts are becoming increasingly consistent in applying the new law and less forgiving of errors made by filers:

“Though a few pockets of resistance to the new regime remain, the days of latitude for the filing party are largely over. (…) various courts have treated the debtor name issue more or less consistently, regardless of whether the debtor is an individual or a registered organization.”

Nonetheless, this system is far from perfect. For example, the rule that assists with the identification of the debtor’s correct name in the case of registered organizations applies, by its very nature, only to registered organizations. With regard to non-registered organizations, the (legal) name that must be provided or searched for on the financing statement is still the organizational name, with no further guidance given on what that name means or where to find it. Furthermore, even in the case of registered organizations, there are still filers today who, despite having found the correct debtor name by reference to its public organic record, also insert the debtor’s trade name on the self-same file. Such an attempt to be even more transparent and accommodating toward future searchers – which is in fact encouraged by Art. 9 UCC – may well backfire if the correct debtor name and the trade name are inserted in the same field of the financing statement, and thus prove counterproductive. Hodnefield has warned that this could render the financing statement seriously misleading. Only if those names are indicated as

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105 I reiterate from subsection 2.3.1.2, especially footnote 56, that in most states these articles are available online or from the filing office within 24 hours.
108 Livingston 2007, p. 129.
109 § 9-503(a)(5)-(6) UCC. Non-registered organizations may have multiple organizational names; see Livingston 2007, p. 151.
two separate debtors would filers be safe.\textsuperscript{110} In sum, it must be said that many complications regarding the correct debtor name continue to exist.\textsuperscript{111}

Although problems with individual names create by far the most difficulties,\textsuperscript{112} many scholars appear to agree that “[t]he number of errors [in the debtor’s name, made by filers] is astonishingly high”.\textsuperscript{113} Research conducted in 2006 in Vermont showed that no less than 63\% of all searched filings for registered debtors involved filers inserting a wrong or misspelled name. About 30\% of the errors made were so minor that they still passed the standard search logic. However, a further 30\% did not pass, and resulted in the security being unperfected for purposes of § 9-506 UCC, i.e. about 20\% of the total. The same research shows that there are strong indications that these results are not dissimilar from other States.\textsuperscript{114} More recent research, conducted in the same state in 2010, does not show a significant variation from these results; in this research, 17\% of the filings were found to be ineffective due to debtor name errors, broken down as follows: 11\% were ineffective due to the use of the registered organization’s trade name and 6\% were ineffective due to typographical errors in the debtor’s name.\textsuperscript{115}

2.3.2.2. Difficulties in using a filing office’s SSL (and determining which SSL applies)

One might have thought that if there were no difficulties in determining the debtor’s correct name for either filers or searchers, and if there were also no ambiguity about who bears the risk of errors, life would be relatively easy.

After all, if filers file under the debtor’s correct name, they know they are safe. Searchers, in turn, would just have to search under the debtor’s correct name, using the search logic of the right filing office. There would then be only two possible outcomes under Art. 9 UCC (2010). The first possibility is that no financing statement will show up. In this case, searchers may assume they are first on file: there will either be no financing statement on file, or if there is, it will have no effect against them because it was filed under a misspelled name and the mistake did not pass the filing office’s SSL.\textsuperscript{116} The second possibility is that a financing statement does show up. In this case, searchers will have to contact the secured party on file to ascertain the extent of their alleged right.

\begin{itemize}
\item \textsuperscript{110} Hodnefield 2011, pp. 1-2.
\item \textsuperscript{111} Cf. LoPucki, Abraham & Delahaye 2013, p. 17: “With difficulty, the filer can search the company records to discover the debtor’s name and computer search logic may or may not save filers or searchers from minor errors in punctuation and abbreviation.”
\item \textsuperscript{112} For an overview of the various problems that arise in individual debtor names, see e.g. Fredrickson 2007. It is worth noting that the number of filings against individual debtors exceeds the number of filings against corporate debtors; see Sigman 2011, p. 465.
\item \textsuperscript{113} LoPucki 2007, p. 289.
\item \textsuperscript{114} Ernst 2006. In this report, the author says that his firm’s “experience in analyzing debtor name errors in other states leads us to think that these figures are roughly applicable in any state.” This research shows that these data are in any event comparable to those of the (densely populated) state of Florida. See also Fredrickson 2007, footnote 6.
\item \textsuperscript{115} Soderstrom 2010, p. 6-9. In addition, 10\% of the total number investigated was wrongly indexed, i.e. effective but not findable for searchers; this will be discussed in more detail in subsection 2.3.3.1.
\item \textsuperscript{116} It makes sense to place the burden of getting the name right on the filing party. After all: “(…) the secured party has the means by which to find out the debtor’s correct name before filing whereas searchers can only guess at various possible spellings or variations of the debtor’s name that might exist in filed financing statements.” Livingston 2007, p. 128.
\end{itemize}
The reality is, however, more complicated. The next obstacle in the filing and search process is formed by the issue of the ‘search logics’. As I observed earlier, when a searcher conducts a search, the filing office concerned will impose its own rules that determine what search string must be used to ensure that filings are found. This is known as the ‘search logic’.\footnote{Cf. Soderstrom 2010, p. 5: “The search logic is the standard protocol employed to determine what the program will consider to be an equivalent name” and LoPucki 2007, p. 292: “The “search logic” of a database program is the set of instructions that determine what strings of characters the program will treat as equivalent.”} Each state has its own official standard search logic (‘SSL’): this is the search logic that will be applied in a conflict between a filer and a searcher when a filer has made an error in stating the debtor’s name. I reiterate that the filing party will win the conflict if, despite the minor error, the financing statement is disclosed when a search is made using the filing office’s SSL (§ 9-506(c) UCC).\footnote{See supra subsection 2.3.2.1.} The aim of introducing this ‘single search test’ was to facilitate the filing and search process: not only does it give filers some leeway for making minor errors in stating the debtor’s name, it also serves as an objectified benchmark on which both filers and searchers can rely. However, the introduction of the ‘single search standard’ has increased the burden on searchers, since an inevitable consequence of adopting this rule is that every UCC filing office provides a set of instructions on the operation of its own standard search logic. An example from the Ohio Secretary of State’s website:

“(…) when searching the database, you should keep these rules in mind and use them as a guideline(s) for your search criteria. Remove all occurrences of double quotes (“), commas (,), pound signs (#), Parentheses (()), and periods (.). Remove any hyphens (-) and concatenate (world-wide becomes worldwide). Remove “the” when it is the first word. Consecutive single characters followed by a space, or punctuation are concatenated into one word and should be searched that way (G.P.R. FOUNDATION becomes GPR FOUNDATION). Two (2) or more characters preceded or followed by a period, the period will be replaced with a space (corp.com becomes corp.com). Use of these stripped words, symbols and characters in your search will give you inaccurate results. For example, if you are looking for B-B CONSTRUCTION COMPANY, LLC., type BB CONSTRUCTION. The search will also find variations such as THE B & B CONSTRUCTION, INC., B.B. CONSTRUCTION, LTD and B B CONSTRUCTION.”\footnote{This is an example of a set of instructions on how to conduct a search for business names in their Corporation Database. See: <www2.sos.state.oh.us/pls/bsqry/Fp?Fp=100:1> (last visited February 5, 2014). Most systems inform users as to the particular search logic employed, but in some systems this information is only available to system managers; see LoPucki & Warren 2012, p. 299.}

Hence, in addition to the question of what constitutes the debtor’s correct name, searchers need to determine the right equivalent of this name for their search. There are several reasons why this is not so easy to determine.

The first reason is that the various search logics differ from one filing office to another.\footnote{See e.g. Michelson Hillinger, Leipold & Livingston 2004, p. 678, Hodnefield and Burton 2012, p. 318.} This is largely because Art. 9 UCC leaves it up to the individual states to adopt their own search rules. Although many UCC filing offices have adopted a variant of the
standard search logic of the Model Administrative Rules (‘MARS (SSL)’), this harmonization attempt has led nowhere.\footnote{The IACA promulgated the MARS in 2007 in an attempt to align the file-and-search process. In addition to the SSL, the MARS contains e.g. general provisions, rules for acceptance and refusal of records by filing officers, rules on how filing officers should store, index and retrieve information relating to financing statements, rules on how filing officers should deal with search requests etc. The MARS rules can be found on: <www.iaca.org/secured-transactions/model-administrative-rules> (last visited February 5, 2014). See also on this subject Livingston 2007, p. 159 et seq.} Since the MARS SSL offers nothing more than ‘model rules’ to guide states, without enforcement powers, some states have adopted the MARS SSL in its entirety, some have adopted only bits and pieces, and a few have not adopted it at all.\footnote{Paul Hodnefield, see supra footnote 40. § 9-526(a) and (b) UCC do actually encourage states to e.g. align their SSL with the MARS SSL. At the same time, Official Comment 3 to § 9-526(a) UCC provides: “Although uniformity is an important desideratum, subsection (a) affords considerable flexibility in the adoption of filing office rules”. The reason for not adopting the MARS rules is often explained by states’ budget constraints. Harris, Kilborn & Livingston 2012, p. 477.} As a result, principal differences have persisted between the SSLs of the various UCC filing offices.

Although the differences might seem small at first glance, it is precisely the subtlety of these differences that makes them difficult for searchers to recognize. Moreover, the subtlety increases the risk that searchers will assume that they all operate in the same way. In addition to differing from one filing office to another, SSLs are generally too narrow to pick up all name variations. This adds up to making any uncertainty about the operation of a filing office’s SSL disastrous to the search process. After all: even if filers use the exact correct name in an official search, but combine it with e.g. the debtor’s trade name, they may still miss the boat because the name is not returned during a search.\footnote{Hodnefield 2007a, p. 2: “The comment is pretty clear in saying we do not expect you to know whether there are filings out there against your debtor, you also will do a non-standardized search because that will produce a greater range of hits and reduce the likelihood of missing something that could affect the outcome of your search.”} Although the SSL is the only relevant standard for determining whether the financing statement is effective,\footnote{Cf. Hodnefield 2007a, p. 2: “In addition to the ambiguity stemming from the undefined term “debtor’s correct name”, the safe harbor lacks uniform application between jurisdictions because it is dependent on the standard search logic of a filing office, which may differ from state to state” and Livingston 2007, p. 146: “As a result of the uncertainty surrounding multiple-named debtors and varying filing office search logic, Article 9 loses some of its heralded uniformity and predictability”.} the foregoing prompts searchers to adopt a typical
search behavior. They often first conduct a so-called ‘unofficial search’ under (variations of) the debtor’s correct name in unofficial databases of filing offices or in private unofficial databases created for that very purpose in various states. Because these unofficial searches are based on broader and more comprehensive search logics, they tend to produce more hits of filed financing statements. With this small quantity of hits, searchers subsequently conduct an official search, to guarantee an outcome that is as certain as possible.

The distinction between these search methods is often referred to as ‘standardized v. non-standardized search’ or ‘certified v. uncertified search’. In the Arizona UCC filing office, for example, searchers can choose between a ‘Revised Article 9 search’, which is a search according to the MARS rules, and a ‘wildcard search’, which is a search under all variations of the entered name. The Colorado filing system also has several search options, such as a ‘standard search’ (the default search), an ‘advanced search’ and a ‘master list search’.

filing office to search the official records, or (ii) using the filing office’s standard search logic to search a database other than that of the filing office. Cf. Hodnefield 2007a, p. 2: “The relevant standard for determining the sufficiency of a debtor name is, therefore, not a diligent searcher’s logic, nor a private organization’s standard search logic. All that matters is the filing office’s SSL.” Cf. Livingston: “The comment is pretty clear in saying we do not expect you to be using unorthodox search methods or unofficial databases. You have a right to enter a name into the official Secretary of State’s database and see what that produces.” Michelson Hillinger, Leipold & Livingston 2004, p. 681.

These unofficial databases emerged in the 1980s. Although their number has diminished since the adoption of Revised Article 9, they still exist. See e.g. LoPucki 2007, pp. 290-291 and 311.

See Harris, Kilborn & Livingston 2012, pp. 466-467 and 471. Cf. Kettering 2012, p. 911: “A filing office might offer more than one search procedure, raising the question of which is the “standard”, and an official designation would settle the issue. For that reason, no doubt, some filing offices that have enabled online searching have designated a particular search mode as being the “standard”.”

128 See <www.sos.state.co.us/pubs/UCC/FAQs/searching.html> (last visited February 5, 2014) and Burton 2012, pp. 325-327 for explanations and examples of these various search methods. Another example from practice: “I will do the search or have the search done, and then I will pay extra to have the Secretary of State, the only filing place in Connecticut, do its own search. Then, I will give them all sorts of possibilities: in the case of “Smith”, three or four spellings; in the case of “Erwin”, with an “i” or with an “e”. I will pay the Secretary of State and get a certificate from them. If they screw up, I have at least covered myself with the lender I am searching for by doing my own search.” This comment was made by an audience member at the second panel of the DePaul Business and Commercial Law Journal Symposium, ‘Emerging Trends in Commercial Law: Surviving Tomorrow’s Challenges’, held on April 15, 2004. In edited form, this is: Michelson Hillinger, Leipold & Livingston 2004, in which the quotation can be found on p. 680. Cf Harris, Kilborn & Livingston 2012, p. 467: “(...) if you really want to know whether there are filings out there against your debtor, you also will do a non-standardized search because that will produce a greater range of hits and reduce the likelihood of missing something that could affect the outcome of your search” and Harris & Mooney 2011, p. 166. I verified whether this is still a common practice for conducting searches in 2012, by asking Hodnefield, and he confirmed this. Hodnefield adds, however, that although filing offices intended that users should search for name variations using the unofficial search logic and
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Filing offices also sometimes change their SSL. Consequently, searchers that think they know the operation of a filing office’s SSL may be wrong.

Searchers that are aware of these risks may choose to conduct multiple searches, hire agencies to conduct searches for them, take out insurance to cover priority losses or a combination of these measures. Some even decide to forego reliance on the filing system altogether. Besides incurring the necessary search or insurance costs, searchers risk subordination, i.e. the loss of priority.

‘UCC insurance’ is a relatively new form of insurance that is modeled after traditional real estate title insurance. UCC insurance can cover a diversity of risks: from inaccuracy of the security agreement to errors in names of the debtor on the financing statement, filing in the wrong location, mistakes made by the filing officer, and much more.133

then order official searches for each of the disclosed variations, many users simply search with the unofficial logic for due diligence purposes, without the follow-up official searches.

129 On August 12, 2004, for example, the California UCC filing office changed its SSL completely. Ernst 2004, p. 5, footnote 13. Cf. Sigman 1999b, p. 862: “(...) a filing office may modify its search logic from time to time; this might have the effect of rendering undiscoverable (under a search using the correct name) a filing providing an erroneous name that was previously discoverable” and Hodnefield 2007a, p. 2: “Even if a jurisdiction uses IACA standard search logic, there is no guarantee the debtor name sufficient under § 9-506(c) will remain sufficient. Filing offices do occasionally change their search logic. It has happened in several states since RA9 took effect. If updated search logic fails to disclose the financing statement it becomes seriously misleading.” See also Livingston 2007, p. 138, Hodnefield 2007a, p. 2 and Kettering 2012, p. 912, especially footnote 19.

130 See for example National Corporate Research’s website: “Conducting UCC, lien, litigation and court searches is never as easy as it seems because every state has different state and local requirements that determine where and how to search. The experienced service specialists at National Corporate Research, Ltd. (NCR) can help take the guesswork out of search projects so that you can better manage costs, save time and obtain exactly what you need, when you need it.” <www.nationalcorp.com/ncri/solutions/UCC-and-Related-Services/UCC-Lien-Searches-and-Document-Retrieval> (last visited February 5, 2014).

131 De La Campa et al. seem to believe that this practice is a solution rather than a problem: “(...) in the United States and Canada, the problem of decentralization of registries is mitigated through the compilation of the information by private companies which sell multi-state searches to potential secured creditors and buyers of movables.” De La Campa et al., ‘Making Security Interests Public: Registration Mechanisms in 35 Jurisdictions’ (Washington DC: IFC, 2012), p. 15.

132 See Alces 1995, p. 707, especially footnote 101. LoPucki & Warren also describe a conversation between Mann and the vice-president of a bank, in which the vice-president explains that searching is done fairly frequently after the loan is granted. The vice-president explains that this is mainly done in relation to small loans, and when the search is expected to take a long time. He adds to this: “Usually, in those situations we are comfortable with the customer. We are comfortable that the fact that we would make this unsecured and probably we’re just taking this as a matter of control.” LoPucki & Warren 2012, p. 282.

133 See also UCCPlus’s website: “UCCPlus insures the commercial lender’s security interest in Article 8 and Article 9 collateral for validity, enforceability, attachment, perfection and priority. Policies protect against fraud, forgery, documentation defects and search office errors and omissions. Policies include UCC search and filing functions and provide for defense costs if
Generally, there are two types of UCC insurance. On the one hand, it can focus on the interest of the lender by insuring attachment, perfection and priority of its security interest (this is often referred to by the term ‘Lender’s Policy’). On the other hand, insurance can take account of the position of the buyer, by insuring that the purchased collateral is free of any security interest or other liens (this is often referred to as ‘Buyer’s Policy’).

Consequences for filers

That filing parties may also suffer from ambiguity of a certain filing office’s SSL seems unlikely because, as a rule, filers bear the responsibility for stating the debtor’s name correctly. In other words, filers should simply ensure that they make no mistakes. However, filers might also be under the mistaken impression that their financing statement is effective, due to a wrongly interpreted SSL:

“(...) a significant number of UCC filers believe that certain errors in the debtor name really don’t matter. Why worry? After all, the debtor name is sufficient if it shows up on a filing office search of the correct name. Filing office standard search logic generally ignores spacing, punctuation and, for organizations, ending “noise words,” doesn’t it?”

Filers could therefore also be misinterpreting a filing office’s SSL. They can mitigate this risk by conducting a search after they have made a filing, thus testing whether the SSL worked as they assumed when making the filing. Here too, however, the principle

the insured lender suffers a loss under the insuring provisions of the policy”, at <www.uccplus.com/index.asp> (last visited February 5, 2014).

134 See for example First American Title, that provides the ‘EAGLE9® UCC Lender’s Insurance Policy’ to filers: “Even the simplest UCC search or filing error may impede a lender’s ability to foreclose on reliance collateral in order to satisfy debts. Our lender’s policy insures the attachment, perfection and priority of the secured party’s security interest in personal property collateral. The lender’s policy also provides full ownership insurance for pledged or acquired equity, effective risk management for factual or legal uncertainty, and significant utility and cost savings in multi-jurisdictional practice.” <www.firstam.com/title/ucc/products/eagle9-ucc-insurance-policies/eagle9-ucc-lenders-insurance-policy.html> (last visited February 5, 2014).


136 Hodnefield 2007a, p. 1. In re Tyringham Holdings, Inc., 354 B.R. 363 (Bankr. E.D. Va. 2006) is an illustration of a case where a secured party omitted the noise word ‘Inc’, while the filing office where the financing statement was filed had not adopted the MARS SSL. The filing office’s SSL therefore did not treat ‘Inc.’ as a noise word, i.e. the omission of ‘Inc.’ was an outright error. Consequently, a search under the debtor’s correct name failed to disclose the secured party’s financing statement. For an analysis of this case, see e.g. Hodnefield 2007a, pp. 1-2 and Harris, Kilborn & Livingston 2012, pp. 466 and 472.

137 See supra Chapter 5, subsection 4.3.1, where I mentioned that the order of conduct should ideally be: (1) file, (2) search, (3) establish that you have priority, (4) grant the loan. Cf. Harris, Kilborn & Livingston
applies that filers that are familiar with the operation of a particular SSL could lose out if the filing office changed its SSL.138 This is because a financing statement that was disclosed despite a misspelling prior to the change may not be disclosed by the new SSL. As a result, the financing statement may become seriously misleading — i.e. ineffective139 — after all.140

Although courts have not yet had a chance to express their views, filers should not expect to receive great sympathy. Courts are becoming increasingly consistent in applying the new law and less forgiving of errors made by filers. Secured parties should therefore never rely on any assumed margin resulting from an applicable search logic to compensate for a misspelled name that does not satisfy § 9-503(a) UCC.141

In view of this need for precision, filers also take out insurance to cover the risk that they did not file properly142 or hire agencies to file for them.143

2.3.2.3. Difficulties in identifying the debtor

After the phase of searching and finding financing statements, searchers arrive at the phase of identifying the right one.144 If a search produces more than one financing statement,
searching parties must make further inquiry to verify or exclude the ones that do not indicate the debtor they are dealing with. However, identification of the debtor can be a tough job.

That searchers would have to identify a debtor on a list of financing statements covering the same or similar names – often referred to as the ‘common name overload’-problem – may be the first problem that comes to mind. While this is indeed a problem in relation to individual names, it is not so (anymore) in relation to corporate debtors. Most states have separate data fields for individual names and corporate names, so there is no room for confusion about whether searchers are dealing with an individual named ‘Smith’ or a corporate debtor named ‘Smith LLC’. Even within the category of registered organizations, states do not allow unaffiliated organizations to use the same or substantially similar names.

The design of a filing office’s search system could, however, have an impact on the search process – by producing arbitrary and confusing ‘results’ – in another way. Because IACA offered its MARS SSL without a corresponding computer program, each filing office was left to implement the SSL in its own computer system. As a result, when it comes to searching and locating financing statements, filing offices are technically designed in very different ways:

The purpose of the debtor name requirement, as discussed in the previous subsection, is to allow retrieval of the document, not to identify the debtor.

See e.g. Livingston 2004, p. 74 on this problem with regard to individual names: “Where the debtor has an extremely common name (e.g., Smith) and lives in a populous jurisdiction (e.g., California), a search under the debtor’s last name (or the debtor’s last name plus first initial) might produce hundreds of financing statements to sort through.” Research on the extent of this problem is beyond the scope of this thesis.

Hodnefield, see supra footnote 40. See for example the New Hampshire UCC filing office’s website (Corporate Divisions): “The Secretary of State will not register a name that is not distinguishable from a name that is registered.” <www.sos.nh.gov/corporate/soskb/csearch.asp> (last visited February 5, 2014). Cf. LoPucki 1995, p. 599: “Because no state permits the formation of two corporations with the same name, the correct name and state of incorporation identify a corporation in a way that distinguishes it from all other entities for which the correct name and state of incorporation are given” and LoPucki 2007, pp. 288-289: “Each of those governments permits only one corporation to have any particular name. If, for example, the state of Ohio has already chartered a corporation by the name “Magnetics Corporation,” that state will not incorporate another.”

Hodnefield 2010, pp. 1-2: “MAR’s merely provides a filing office with the recommended name normalization steps. The rules did not offer model computer programming code. Filing offices use a wide variety of computer hardware, software and operating systems.” Cf. LoPucki & Warren 2012, pp. 299-300.
The Florida filing office, for example, uses an alphabetical index. If one searches in this system under the name ‘Hamwijk’, the system searches for all names beginning with the letter ‘H’ and then progresses to the next letter. If the name is found, it is displayed on the first search page along with 19 other names (the total number of names on a page is 20). For both filers and searchers, this creates uncertainty as to whether a (misspelled) financing statement falls within the ‘safe harbors’ of § 9-506 UCC. After all, what qualifies as a ‘search’? The extent to which searchers will be expected to be more diligent in their efforts depends on how courts will look at this.

By way of example, I refer to In re Summit Staffing, in which it was held that although a searcher did not have to meet the standard of being a reasonably diligent searcher in trying to find the financing statement – see supra subsection 2.3.2.1 – a searcher does have to use reasonable diligence in examining the search results. What this meant in the case concerned was that the searcher had to check preceding and successive names on the alphabetical list by scrolling back and forth. Four years later in In re John’s Bean Farm, this rule was somewhat qualified by the judgment that there is a limit to the number of pages the searcher should discover: one click on the ‘previous button’ is sufficient to qualify as a reasonable diligent searcher.

2.3.2.4. The influence of courts on the file and search process

Realizing a foolproof filing and search mechanism is difficult enough in itself, but the task becomes even more challenging if courts interpret the rules rather loosely. The Spearing...
Tool case\textsuperscript{155} is an example where limits were pushed. It showed that a well-considered and adequately designed ‘single search mechanism’ can easily be rendered completely useless. It was not without reason that this case was called ‘The Spearing Tool Filing System Disaster’\textsuperscript{156}

In summary, Spearing Tool and Manufacturing Co., Inc. (‘Spearing Tool’) entered into a series of secured loan transactions with Crestmark Bank (‘Bank’). The Bank obtained a security interest in all of Spearing Tool’s assets and perfected its security interest, by filing under the debtor’s exact registered corporate name in the Michigan UCC filing office. As Spearing Tool defaulted on payment of several tax obligations, the IRS filed two notices of federal tax liens against Spearing Tool in the appropriate, i.e. Michigan, UCC filing office. However, it perfected these tax liens by filing under a slight variation of the debtor’s correct name (‘Spearing Tool & MFG. Company Inc.’ rather than ‘Spearing Tool and Manufacturing Co., Inc.’). When Spearing Tool was declared bankrupt, both the Bank and the IRS claimed priority with regard to (part of) the debtor’s assets. The Bank claimed priority on the basis of the fact that it filed under the debtor’s correct name and that it did so earlier in time than the IRS. It had periodically searched for prior tax liens, but the IRS tax liens had not showed up (the Michigan UCC filing office’s search logic had been too narrow to produce the tax lien despite the error made by the IRS). The IRS, in turn, claimed priority on the basis of 26 U.S.C. § 6323(d). This section provides that a filed tax lien has priority over disbursements made by a prior secured lender more than 45 days after the filing.\textsuperscript{157}

The District Court of Appeal for the 6\textsuperscript{th} Circuit ruled – upholding the ruling of the District Court – that the reasonably diligent search test of federal law applied. At the same time, however, it ruled that a ‘single search’ in the exact, correct name of the debtor was not reasonable and diligent. Hence, it decided that a tax lien was valid even though the IRS had not stated the debtor’s exact, correct name. It explained the reasons for its ruling by referring to the search instructions of the Michigan UCC filing office which recommended e.g. to search by using abbreviations. Moreover, it used policy considerations: “A requirement that tax liens identify a taxpayer with absolute precision would be unduly burdensome to the government’s tax-collection efforts.” And “(…) while we understand that a requirement that the IRS comply with UCC Article 9 would spare banks considerable inconvenience, we conclude from Supreme-Court precedent that the federal government’s interest in prompt, effective tax collection trumps the banks’ convenience in loan collection.”\textsuperscript{158}

Given that most states use the same filing index for tax liens and Article 9 filings – i.e. searchers will automatically search for both types of liens – the effect of this case was to reinforce the reasonably diligent search test as effective under Art. 9 UCC.\textsuperscript{159}


\textsuperscript{156} LoPucki 2007, p. 281.


\textsuperscript{159} See supra subsection 2.3.2.1. Cf. LoPucki 2007, pp. 287: “That simultaneous search must include the steps necessary to find tax liens as well as the steps necessary to find Article 9 filings. Thus, by imposing the reasonably diligent search requirement on those searching for tax liens, Spearing Tool imposed it on all searchers. The effect was to resurrect the reasonably diligent search requirement for Article 9 searching” and Molen & Baxter 2005: “Creditors should (…) conduct federal tax lien searches under the current legal name of the entity, prior legal names, trade names and other names of which they have knowledge, as well as other name variations that come to the mind of the imaginative searcher.” Cf. Livingston 2007, pp. 139 and 141.
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This was a significant setback for the newly adopted single search test, and in fact turned the clock back several years.\footnote{160}

2.3.2.5. Concluding remarks & future developments

The above shows that: ‘[s]earchers (…) cannot fully rely on the notice-filing system promulgated under Revised Article 9 to actually give notice of a prior security interest in a potential debtor’s property’ and that ‘(…) subsequent creditors, like filers of initial financing statements, often enter into secured transactions with an abundance of uncertainty regarding the effectiveness and relative priority of a particular security interest.’\footnote{161} Although discovering a corporate debtor’s exact name presents no problem for the vast majority of creditors,\footnote{162} the filing and search process remains cumbersome. Creditors have to put considerable effort into mastering search logic(s), filing under and collecting tips on multiple name variations, identifying the right debtor, etc.\footnote{163} This is partly because the UCC filing system does not employ state-of-the-art technology.\footnote{164} The remainder of the cause, however, lies in the policy choice of employing a name-based system:

‘(…) no matter how a state designs its system, if creditors are given the responsibility of recording the name of the debtor on the financing statements themselves, errors and eventual litigation will follow.’\footnote{165}

This affects the legal position of the parties investigated in this thesis on a daily basis, in their capacity as both filer and searcher. In an attempt to avoid mistakes in searching and identifying the debtor, in 1995 LoPucki recommended that the UCC filing office should be linked to the corporate records. In such a system, searchers would simply be able to pick the correct name from a list of existing (i.e. incorporated) entities rather than attempting to reproduce the debtor’s correct name themselves.\footnote{166} A system like this gives less margin for misspellings or mistakes in entering the wrong type of name, because it makes the use of SSL unnecessary: one only needs to point-and-click on the correct name.\footnote{167}


\footnote{161} Tu 2010, p. 108.

\footnote{162} After all, since as all states have implemented the 2010 amendments, a registered debtor’s name is determined by checking the business’s ‘birth certificate’ online or by telephone. Uncertainty will continue to exist, however, with regard to non-registered organizations. See supra subsection 2.3.1.2.

\footnote{163} Cf. LoPucki 2007, p. 286 and Dalhuisen II 2013, p. 471.

\footnote{164} LoPucki, Abraham & Delahaye 2013, p. 1860.

\footnote{165} Burton 2012, p. 327.

\footnote{166} See LoPucki 1995, e.g. on p. 603: “Each time a UCC filing would be made against a corporate debtor, the computer would match the name of the debtor to the names of the corporations formed under the laws of the state. If there were no match, the filing would be erroneous. The system could notify the filer of that fact. If there were a match, the system could display a list of filings against the debtor (…) .”

Adopting such a system would have been a logical step after the introduction of incorporation-based filing in 2001, since of that moment, the filing offices in which the financing statements are filed also contained the articles of incorporation, *i.e.* documents that show the only correct name of the debtor.\(^{168}\) In addition to limiting mistakes made in the search process, it could have paved the way for facilitating further exchange of information between the debtor and its secured creditors. For example, if corporate records were linked to UCC filings, secured creditors would be alerted to the fact that their debtor intended to merge, which would reduce the need to perform periodic update searches.\(^{169}\) However, now, almost twenty years later, there are only on or two ('commercially unimportant') states that have adopted this system.\(^{170}\)

An example is the State of Maine. On the website of Maine’s Secretary of State, *filers* can file a ‘Standard UCC Lien’ by selecting the option to ‘File a Financing Statement - Form UCC-1’. Filing parties can select the ‘Registered Organization’ box, and then enter a full or partial debtor name in a search field to verify whether the entry is a registered Maine organization. If a creditor enters *e.g.* ‘Smith LLC’, 21 companies containing the words ‘Smith LLC’ will be shown. All these companies are specified by a unique ‘organization (charter) number’.\(^{171}\) After a point-and-click of the correct debtor, the filer has to complete the debtor’s address information (*i.e.* enter *e.g.* the debtor’s address, city, state or province and zip code). It then has to indicate whether it itself is an ‘Individual’ or an ‘Organization’ and complete its own address information. Finally, the filer can add collateral by describing it manually or by clicking ‘Choose Collateral from Library’, which means that several categories of collateral (*e.g.* equipment, farm products) can be ticked. The process is completed by reviewing the Transaction Information, and paying $10.00 (for each filing) by credit card or otherwise.

On the same website, *searchers* can request an ‘Official UCC Debtor Search’ with or without copies of the filings associated with the search. Searchers are not, however, offered the point-and-click option. If they select a ‘Standard Search Response’ of an ‘Organization’, searchers have to enter the organization’s name manually. After the debtor’s name has been entered, searchers are not shown a list of organizations registered in Maine. The website even states explicitly that if no results are found for the requested search, searchers will still be charged for the search.\(^{172}\) Given that the list of organizations registered in Maine is shown in the filing process (see above), I assume that searchers will normally copy-and-paste the name from the menu in the filing process, and use this name in the ‘Official UCC Debtor Search’, to avoid errors in their search.

The reason that only one or two states have adopted the point-and-click system is that in many states the Internal Revenue Service also uses the Art. 9 UCC filing offices to file tax liens. However, tax liens are not filed in the filing office of the state where the debtor is incorporated, but in the filing office of the state where the debtor has its chief executive

\(^{168}\) Burton 2012, p. 327.

\(^{169}\) This idea came from Harris & Mooney. 1995, pp. 669-670: “An incorporation-based choice-of-law rule might facilitate the transmission of relevant information to secured parties and thereby obviate the need for periodic searches (…).” More details about what secured parties have to do to maintain perfection will be given in subsection 2.3.

\(^{170}\) LoPucki, Abraham & Delahaye 2013, p. 1797.

\(^{171}\) See <www.maine.gov/sos/ccc/ucconline> (last visited February 5, 2014). See also on this subject LoPucki, Abraham & Delahaye 2013, p. 1796, footnote 56.

\(^{172}\) See <www.maine.gov/sos/ccc/ucconline> (last visited February 5, 2014).
Adopting a point-and-click system would therefore not add much, as a search in such a system would still not produce a comprehensive result with respect to all existing filings against the debtor’s property. Searchers would still have to search the filing office in the state of the debtor’s chief executive office to find tax liens against the debtor.

The 2010 amendments deleted the requirement that financing statements must include organizational identification numbers. The drafters also decided that the financing statement sufficiently provides the debtor’s name if it provides the debtor’s name indicated on the ‘public organic record most recently filed’. As a result, this particular name does not necessarily match the name reflected in the computerized record of the UCC filing office. This would seem to represent an insurmountable obstacle to further development of point-and-click systems.

2.3.3. Other challenges: logistical and technical

In addition to the practical problems described above, Art. 9 UCC also has to cope with several logistical challenges that may cause financing statements to be untraceable. These difficulties are not connected with the way financing statements are filed or searched, but rather with the way they are stored by the filing office. Filings that are accepted by the filing office, may be untraceable because they are not indexed properly, not yet indexed at all or lost.

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173 See Title 26 (Internal Revenue Code) of the United States Code (U.S.C.), § 6323(f)(1): “The notice referred to in subsection (a) shall be filed (...) in the case of personal property, whether tangible or intangible, in one office within the State (...) in which the property subject to the lien is situated (...),” 26 USC § 6323(f)(2): “For purposes of paragraphs (1) (...) property shall be deemed to be situated (...) in the case of personal property, whether tangible or intangible, at the residence of the taxpaye at the time the notice of lien is filed” and 26 USC § 6323(f)(2)(B): “(...) the residence of a corporation or partnership shall be deemed to be the place at which the principal executive office of the business is located (...).”

174 LoPucki 2007, pp. 308-309 and Burton 2012, p. 328. Some scholars argue that a point-and-click system would also be inconvenient, because it would prevent creditors from filing in multiple states. In a point-and-click system, parties can only file in the state of incorporation, and not in the state where the collateral is located. Also Hodnefield, see supra footnote 40. According to Burton, multiple filing could be useful, as it would alert searchers – even those who search in the wrong UCC filing office – that a security interest exists: “The elimination of the ability to do this may cause an upheaval in the world of secured transactions, and might prevent filers from wanting to support a change to the system.” Burton 2012, p. 328.

175 This was § 9-516 (b)(5)(C)(iii) (2001) UCC.

176 § 9-503(a)(1)(2010) UCC.

177 LoPucki, Abraham & Delahaye 2013, p. 1796-1797. Remarkably, in the 2010 amendments the drafters did not remove the Official Comment that recommends adopting such point-and-click systems. See Official Comment 4 to § 9-307 UCC: “Determining the registered organization-debtor’s location by reference to the jurisdiction of organization could provide some important side benefits for the filing system. A jurisdiction could structure its filing system so that it would be impossible to make a mistake in a registered organization-debtor’s name on a financing statement. For example, a filer would be informed if a filed record designated an incorrect corporate name for the debtor. Linking filing to the jurisdiction of organization also could reduce pressure on the system imposed by transactions in which registered organizations cease to exist – as a consequence of merger or consolidation, for example. The jurisdiction of organization might prohibit such transactions unless steps were taken to ensure that existing filings were refiled against a successor or terminated by the secured party.”

Although the UCC filing offices have been engaged in the process of modernization, some filing offices still use filing officers to index financing statements manually. Consequently, financing statements may be indexed incorrectly, e.g. by indexing under a different name, a wrong file number, or may even get lost. In both cases, the financing statement is inaccessible to any potential creditor, even if the search is conducted in the right place. Art. 9 UCC imposes the risk of filing-office error on those who search the files rather than on those who file. Searchers have the responsibility of taking out title insurance to cover the risk that filings might be lost or indexed incorrectly. The state (or the filing officer who made the mistake) cannot be sued, due to rules of sovereign immunity.

From inquiries made it follows that it is not uncommon for filing officers to make an error in stating the file number on an amendment form, as a result of which the filing office indexes it in association with an unrelated financing statement. In line with this, research conducted by Soderstrom in 2010 showed that 10% of the total number of investigated filings turned out to be wrongly indexed. This research did not look at the number of filings that were lost. Hence, if searchers do not take out insurance, there is at least a 10% chance that the filing they are looking for is untraceable but nevertheless effective.

Another risk resulting from the fact that some filing offices still store financing statements manually is that filings may be indexed late. Although the indexing should be completed within two days of receipt by the officer (§ 9-519(h) UCC), filing offices are traditionally a few weeks behind in indexing new filings. As a result, filings are often untraceable for a short period of time. This is what generally happens:

“The filing officer dates and numbers an electronic filing or stamps a paper filing to uniquely identify the record and document the date and time of its filing. The financing statement is effective as of that moment, even though it may take a few days, or even weeks, for the filing officer to add it to the official index. Thus, at any given time, there will be filed and effective financing statements that will only be entered into the index at some point in the future.”

180 Wrongly indexed or lost filings are effective according to § 9-516 UCC, which provides that ‘communication of a record to a filing office and tender of the filing fee or acceptance of the record by the filing office constitutes filing’ and § 9-517 UCC, which states that the failure of the filing office to index a record correctly does not impair the effectiveness of the filed record. See also on this subject Picker 2009, p. 135.
181 See for example First American Title, which provides ‘The Insured Search’ insurance to searchers: “The Insured Search insures against filing office error including mis-indexing and incorrect rejection. For the first time, full UCC search services are combined with indemnity insurance, all at a price competitive with uninsured UCC search and filing products.”
182 Soderstrom 2010, pp. 6-9.
183 LoPucki & Warren 2012, p. 384. In extreme cases, filing offices can be more than four months behind: “When such delays occur, the filing officers invariably blame their legislatures for not appropriating sufficient funds for the filing offices to carry the workload. No one can prove the filing officer wrong and no penalty is imposed for violating U.C.C. § 9-519(h) (…)”
statements that searchers cannot discover through the index. Because in many filing systems the not-yet-processed documents were kept in an in-basket on someone’s desk, these unindexed and therefore undiscoverable records have become known as the basket. Filing officers running small systems sometimes conduct or permit hand-searching of the basket in connection with a search of the index. But in a large system, there may be no way to discover financing statements in the basket except to wait for the filing officer to discover them.”

Searching ‘the basket’ is not, however, always possible: filing officers are only authorized to respond to search requests with regard to filings that are indexed (§ 9-523(c) UCC). Additionally, financing statements that are not yet indexed are nevertheless effective. Hence, also in relation to not-yet-indexed financing statements, Art. 9 UCC has chosen to impose the risk on searchers, and searchers can only mitigate this risk by taking out insurance.

The option of presenting filings in physical form also creates the risk of wrongfully rejected filings, i.e. rejection by the filing officer for reasons other than those sanctioned by Art. 9 UCC. If this occurs, filings will not appear in the public filing system during a search. Instead, they will be returned to the filer stamped with the date and time of the attempt to file. The Art. 9 UCC drafters decided to protect filers against such improper actions by the filing officer, but only to a limited extent: the non-filing is effective to perfect the underlying security interest only against lien creditors and the trustee(s) in bankruptcy. However, it has no effect whatsoever against purchasers of the collateral that gave value and acted in reasonable reliance upon the absence of the record from the files. Protecting filers only against prospective judicial lien creditors (and the trustee in bankruptcy) is motivated by the belief of the Art. 9 UCC drafters that judicial lien creditors would not in any way be harmed if financing statements do not appear in the filing system, since they simply do not search the filing system. Hence, the drafters chose to protect third parties that do rely on the filing system, such as prospective buyers and lenders. What this boils down to is that lien creditors, as a consequence of these rules, may be potentially misled and lose out if, and to the extent

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185 § 9-517: “The failure of the filing office to index a record correctly does not affect the effectiveness of the filed record.” See on this subject also Sigman 1999a, p. 70.
186 Cf. footnote 133.
187 § 9-520(b) UCC. Cf. LoPucki & Warren 2012, p. 315. Filing officers are only permitted to reject financing statements if the filing fee is not tendered, or if crucial information is indecipherable or simply absent (§ 9-516 UCC.) This information includes the name of the debtor, the name of the secured party (or its representative), the mailing address of the secured party (or its representative), the mailing address of the debtor and an indication of whether the name of the debtor is the name of an individual or an organization. See §§ 9-502(a)(1) UCC, 9-502(a)(2) UCC, 9-516(b)(4) UCC, 9-516(b)(5)(A) UCC, 9-516(b)(5)(B) UCC, 9-520(a) UCC. Thus, for the most part, the bases for rejection are limited to those that prevent the filing office from dealing with the financing statement that it receives. See Official Comment 2 to § 9-520 UCC. Cf. Harris & Mooney 2006, pp. 174-175 and Picker 2009, pp. 109-110 on this subject.
188 § 9-516(d) UCC. This partial effectiveness is often referred to as a ‘lien perfected’ financing statement.
189 § 9-516(d) UCC. In common parlance, the filing is not ‘purchaser perfected’. In the UCC, ‘purchasers’ includes secured parties and buyers, but not lien creditors, see § 1-201(b)(29) and (30) UCC.
190 LoPucki & Warren argue that this was a matter of faith, not empirical reality. LoPucki & Warren 2012, p. 315.
that, they would actually search. They can only mitigate this risk\textsuperscript{191} by taking out insurance.\textsuperscript{192}

### 2.4. Challenges in ‘making further inquiry’

If a financing statement is filed under the debtor’s exact, correct name and it is searched for under that name in the right filing office (using the filing office’s SSL), the financing statement will most typically show up. If the debtor is then also identified, the aim of ‘providing notice’ to third parties can considered to be fulfilled. We then come to the phase of ‘making further inquiry’. Since Art. 9 UCC is based on notice filing – indicating no more than that the lender on file may have the benefit of security – every searcher who needs substantive answers is expected to inquire outside the filing system. I already explained in subsection 2.2.2 that unsecured creditors that attempt to attach the assets will not have the leverage to ask the debtor for further information, as a result of which proprietary conflicts between them and prior secured parties are not be prevented. This is clearly different in relation to second-in-time lenders and buyers: since they are the ones that keep the debtor’s business running, they do have leverage to ask for further information and, moreover, removal of existing financing statements.\textsuperscript{193} Such will usually be obtained by making an informal request to the lender(s) on file.\textsuperscript{194} or – if the first-in-time lender refuses to provide the information informally – by making a formal § 9-210 request.\textsuperscript{195} In addition, the debtor will cooperate with termination or amendment of existing filings. This process is in practice, however, often cumbersome and time-consuming. This is mainly because there may be (too) many notices in the filing system with respect to one and the same debtor and, moreover, the process of having a filing terminated or corrected is rather complicated. I will elaborate on both issues in the next three subsections.

\textsuperscript{191} I already noted in Chapter 5 (subsection 3.6) that this risk will probably not materialize very often in practice. After all, the filing officer is obliged to communicate the refusal and the reason therefore to the filer and, in addition, has to give notice of the time the financing statement would have been filed had the filing officer accepted it (§ 9-520(b) UCC). This has to be done not later than two days after the filing office receives the record. Customarily, the filer will correct the error and try again. The same applies when a financing statement is filed electronically: it cannot be electronically submitted if the financing statement omits the data mentioned in § 9-516(b) UCC, because the filing office is required under § 9-520(a) UCC to refuse to accept records that omit that information. The absence of an indication of the collateral may be an exception, because this is not a statutory reason for rejection. However, most, if not all, electronic filing systems will require an indication of the collateral. E.g. Hodnefield, see supra footnote 40.

\textsuperscript{192} Cf. footnote 133.

\textsuperscript{193} Put differently: if the debtor does not cooperate, lenders that want to have a first-priority security will simply refuse to grant the loan and buyers will refuse to purchase the assets.

\textsuperscript{194} Most (first-in-time) lenders will respond to this request, simply because they have a business relationship with the debtor.

\textsuperscript{195} The debtor can ask its lender for a ‘request for accounting’ (§ 9-210(a)(2) UCC), a ‘request regarding a list of collateral’ (§ 9-210(a)(3) UCC) or a ‘request regarding a statement of account’ (§ 9-210(a)(4) UCC). Lenders have to respond to such a formal request within 14 days after receipt with an authenticated record including the information (§ 9-210(b)-(e) UCC). See supra Chapter 5, subsection 3.7.5.
2.4.1. Difficulties in identifying the correct secured lender

The main reason for the fact that there may be many notices in the filing system with respect to the same debtor lies in its very nature: a notice filing system. Since a financing statement serves the purpose of warning potential creditors of the possible existence of security interests in the debtor’s property, filing can be – and often is – performed ahead of the actual execution of a secured transaction. Accordingly, filing is relatively easy: filing officers do not check whether the filer is authorized to file financing statements (the debtor is not, for example, required to sign the financing statement). Nor is evidence of authorization recorded in the filing system. In fact, the signing of the security agreement by the debtor operates as an ipso facto authorization of the filing of a financing statement (or an amendment thereof) covering the collateral described in the security agreement.

Along with the possibility of filing at an early stage, this convenience opened the door for ‘bogus filings’ to be filed: financing statements that are filed without prior authorization by the debtor. Over the years, the Art. 9 UCC filing system has suffered from pollution by three types of bogus filings being made: harassment filings, strawman filings and authentication filings.

Harassment filings falsely indicate that a particular person or business has given security to the filer or purported secured party (thereby also often falsely indicating that it owes large sums of money) with the intent to obstruct the former from obtaining future credit. With similar motives, there is the phenomenon of ‘strawman filings’ being made by U.S. citizens who are convinced that the federal government has created a so-called ‘strawman account’ at the U.S. Treasury Department, representing the interest that has been created by the purported debtor and the purported debtor has not authorized the filing of the financing statement.

Authentication filings are filed, even if they are blatantly fraudulent. If a financing statement is submitted with all of the required information, the financing statement serves the purpose of warning potential creditors of the possible existence of security interests in the debtor’s property. In fact, the original text of Article 9 prohibits states from rejecting financing statements unless specific grounds exist for this action. Even then, the reasons for rejection are limited to ministerial issues, such as failure to pay the proper fee, incomplete forms, or illegible writing.” Cf. Sigman 1999a, p. 69 on this topic.

While inclusion of such filings in the public record may be intellectually distressing to some, it is necessary to provide documentation of the existence of security interests in the debtor’s property. The requirement to sign the financing statement and the requirement to have evidence of authorization in the public record were eliminated in 2001 to accommodate electronic filings.

Such filings are often based on a sense of injustice and therefore undertaken against public officials, such as judges and police officers but also against corporations and banks; see ‘Final Report and Recommendations, For the National Association of Secretaries of State (NASS) and International Association of Commercial Administrators (IACA), Joint Task Force, “Bogus” UCC Documents’ (2006), p. 3 and ‘State Strategies to Subvert Fraudulent Uniform Commercial Code (UCC) Filings – A Report for State Business Filing Agencies’ (Washington DC: NASS, 2012), pp. 4-5. Sigman describes these filings as “(…) filings made for the purpose of injuring the purported debtor by giving the impression that a security interest does or may exist with respect to assets of the purported debtor in circumstances where there is no obligation to be secured, no security interest has been created by the purported debtor and the purported debtor has not authorized the filing of the financing statement.” See Sigman 2011, p. 489, especially footnote 108.

196 This possibility of filing a financing statement at an early stage, i.e. even before the loan has been granted, is expressly provided by § 9-502(d) UCC: “A financing statement may be filed before a security agreement is made or a security interest otherwise attaches.” See on this subject also Livingston 2007, p. 117, footnote 26.

197 See Official Comment 3 to § 9-502 UCC and ‘State Strategies to Subvert Fraudulent Uniform Commercial Code (UCC) Filings – A Report for State Business Filing Agencies’ (Washington DC: NASS, 2012), p. 6 about this: “The office does not have the authority to verify the accuracy or the validity of documents when they are filed, even if they are blatantly fraudulent. If a financing statement is submitted with all of the required information, the Secretary of State must record the document. In fact, the original text of Article 9 prohibits states from rejecting financing statements unless specific grounds exist for this action. Even then, the reasons for rejection are limited to ministerial issues, such as failure to pay the proper fee, incomplete forms, or illegible writing.” Cf. Sigman 1999a, p. 69 on this topic.

198 See §§ 9-509(b)(1), (2) UCC, 9-315(a)(2) UCC, 9-516 (a) and 9-520(a). See on this subject e.g. Moringiello 2001, p. 144, Harris & Mooney 2006, p. 172, Sigman 1999, pp. 68-69, Sigman 2004, p. 77 and Harris & Mooney 2006, p. 172. The requirement to sign the financing statement and the requirement to place evidence of authorization in the public records were eliminated in 2001 to accommodate electronic filings.

199 Such filings are often based on a sense of injustice and therefore undertaken against public officials, such as judges and police officers but also against corporations and banks; see ‘Final Report and Recommendations, For the National Association of Secretaries of State (NASS) and International Association of Commercial Administrators (IACA), Joint Task Force, “Bogus” UCC Documents’ (2006), p. 3 and ‘State Strategies to Subvert Fraudulent Uniform Commercial Code (UCC) Filings – A Report for State Business Filing Agencies’ (Washington DC: NASS, 2012), pp. 4-5. Sigman describes these filings as “(…) filings made for the purpose of injuring the purported debtor by giving the impression that a security interest does or may exist with respect to assets of the purported debtor in circumstances where there is no obligation to be secured, no security interest has been created by the purported debtor and the purported debtor has not authorized the filing of the financing statement.” See Sigman 2011, p. 489, especially footnote 108.
monetary worth of each U.S. citizen. These citizens believe that the monetary worth of their account – supposedly between $ 600,000 and $ 3 million – can be ‘claimed back’ by securing an interest in, and filing a financing statement with respect to, this account. Strawman filings therefore generally indicate the same name for the debtor and the secured creditor. It is not rare for these filings to be brightened up with blood-drenched fingerprints. Besides (quite literally) contaminating the public records, strawman filings are said to be used to defraud third parties into providing value for worthless, i.e. nonexistent, assets.200 Finally, ‘authentication filings’ refer to fraudulent financing instruments submitted together with bogus UCC filings, with the aim of misleading third parties about the authenticity of the underlying documents.201

At the same time, Art. 9 UCC is based on an ‘open drawer’202 model, which means that filings are not removed until a certain period of time has passed.203 As a result of all this, there are many filings in the records that do not represent an active underlying credit relationship.

As both bogus filings and otherwise ‘empty’ filings give ‘notice’ of security that is not in place, they prevent the debtor from easily selling its assets or obtaining secured finance from other lenders.204 These filings also affect second-in-time lenders and buyers outside the ordinary course of business, as they may be delayed in advancing loans and buying their assets.

2.4.2. Art. 9 UCC and state-level solutions to incorrect (‘empty’) and bogus filings

Art. 9 UCC offers two options to the debtor to rectify incorrect (‘empty’) filings. If the debtor has paid and discharged all of the secured liabilities, the debtor can demand its secured lender to file a ‘termination statement’ with respect to a filing that was originally authorized. Upon filing of the termination statement – which has to be done within 20 days after the debtor has requested this by means of an authenticated demand – the

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200 See ‘Final Report and Recommendations, For the National Association of Secretaries of State (NASS) and International Association of Commercial Administrators (IACA), Joint Task Force, “Bogus” UCC Documents’ (2006), p. 3 and ‘State Strategies to Subvert Fraudulent Uniform Commercial Code (UCC) Filings – A Report for State Business Filing Agencies’ (Washington DC: NASS, 2012), p. 5. For a different view, see Sigman 2011, p. 489: “While [this, D]YH] category does not reflect a legitimate transaction, it also does no harm to anyone as the purported debtor is the person who has made the filing (this is often done in the mistaken belief that it somehow shields the filer’s assets from availability to creditors; many of these filings are made by “Freemen” or “Sovereign anti-government groups”). While inclusion of such filings in the public record may be intellectually distressing to some, it harms no third party and simply provides additional revenue to the filing office.”


202 Expression taken from Moringiello 2001, p. 146.

203 This is usually 5 years.

204 Although they do not result in perfection (§ 9-510(a) UCC), i.e. seem harmless, this also applies to bogus filings. Cf. Moringiello 2001, p. 140 and Sigman 2011, p. 489: “Even though the filing of a financing statement does not create a security interest, and it was not authorized by the purported debtor, has no legal effect on the purported debtor’s assets, the existence of the filed financing statement on the public record may harm the purported debtor by injuring his credit—it might well delay that person’s access to credit.”
financing statement ceases to be effective.\textsuperscript{205} If the secured lender fails to send the debtor or the filing office a termination statement,\textsuperscript{206} the debtor can authorize and file a termination statement itself.\textsuperscript{207} The debtor can also undertake this action with respect to financing statements that it did not authorize to be filed, \textit{i.e.} bogus filings.\textsuperscript{208} In addition to the possibility of asking for – or filing – a termination statement, the debtor can file an ‘information statement’, which sets forth the reasons why the debtor believes that the financing statement was inaccurate or wrongfully filed,\textsuperscript{209} and why it should be rectified.\textsuperscript{210, 211}

Not only are these rules impracticable or even inadequate for various reasons, the need for such rules is prompted by the very way in which Art. 9 UCC is set up. For example, under Art. 9 UCC termination will only take place by or at the instigation of the debtor. Secured parties do not have a statutory duty to file termination statements in certain specific circumstances, such as having lost interest in the collateral as a result of full discharge of the secured liabilities; they only need to act once having received a demand from the debtor. As a result, debtors will always have to make the effort to keep their records up to date, which may take time and which implies costs.\textsuperscript{212} Furthermore, the possibility of the debtor filing a termination statement itself in certain specific

\textsuperscript{205} Hence, the financing statement is not removed from the filing system, but terminated by a document – the termination statement – that indicates that the financing statement to which it relates is no longer effective; see §§ 9-102(a)(80)(B)(2010), 9-513(c)(1), (d) UCC.

\textsuperscript{206} The secured party may refuse or fail to provide a termination statement because it has disappeared through a merger or liquidation; see Official Comment 4h to § 9-101 UCC.

\textsuperscript{207} §§ 9-510(a), 9-509(d)(2) UCC. This termination statement should indicate the initial financing statement file number and will be effective only if it indicates that the debtor authorized it to be filed. See section 9 on the UCC Amendment statement as provided in Chapter 5 subsection 3.4.2: “If this is an Amendment authorized by a DEBTOR, check here and provide name of authorizing Debtor (…)”. See infra footnote 213 of this chapter.

\textsuperscript{208} §§ 9-513(c)(1), (d) UCC. If the debtor does not know the address of the named secured party, because there is no relationship with this party whatsoever, according to § 1-202(e) UCC the putative secured party is deemed to have received a notification if it is delivered to the address shown in the financing statement. Official Comment 3 to § 9-513 UCC.

\textsuperscript{209} The filing of an ‘information statement’ does not even affect the effectiveness of an initial financing statement or other filed record at all, since its only purpose is to provide public notice that the validity of the financing statement is in dispute (§ 9-518(e) UCC).

\textsuperscript{210} § 9-518(a) UCC. See also on this subject Sigman 1999a, p. 69 and Frisch 2011, p. 1025. Furthermore, parties that submit a bogus filing, or that fail to file (or send the debtor) a termination statement, become liable for ‘actual damages’, referring to e.g. loss resulting from the debtor’s inability to obtain, or increased costs of, alternative financing. These parties also risk a $500 penalty for each bogus filing and/or refusal to file (or send) a termination statement. § 9-625(b) and (e)(3) and (4) UCC. In addition, competing creditors (including senior creditors) holding a security interest or other type of lien may seek to recover damages. See § 9-625(e)(1) UCC and Official Comment 3 to § 9-625 UCC. See also on this subject Harris & Mooney 2006, p. 95 et seq. and LoPucki & Warren 2012, p. 375.

\textsuperscript{211} Under former Art. 9 (2001) UCC, only the secured party could file a termination statement. Moreover, the information statement was called a ‘correction statement’. As this term was found to be somewhat misleading, because it did not result in removal of the filing, it was changed to ‘information statement’.

\textsuperscript{212} Most debtors will not be aware that a bogus filing has been filed until they enter into a relationship with a subsequent lender or intend to sell their assets not in the ordinary course of business.
circumstances, offers no definitive solution to the problem if for whatever reason the first in time lender refused to authorize the filing of a termination statement. One needs to bear in mind that the very nature of Art. 9 UCC as a notice filing system implies, that searchers are only put on notice of possible facts, but will always need to inquire further to learn more detail. Just like a financing statement only serves to alert searchers that security may be in place, a termination statement only alerts them that a prior financing statement may have lost its significance: in both instances further inquiry is required to establish the actual situation. Accordingly, the filing of a termination statement does not obviate the need to satisfy prospective lenders (and buyers outside the ordinary course of business) that such a termination statement was indeed properly authorized by the secured lender on file or by the debtor if the secured lender did not respond within the prescribed 20 days period. In view of the fact that a practice has even developed of filing bogus termination statements, this is not always an easy task, to put it mildly. Debtors have been demonstrated to file bogus, i.e. fake, termination statements to fraudulently clear the record, but this also appears to occur accidentally, when a filer has mistakenly stated a file number that relates to another (i.e. unrelated) financing statement. In an attempt to address this problem, the 2010 amendments to Art. 9 UCC adopted a rule that allows secured parties of record – in addition to the debtor itself – to file an ‘information statement’ with regard to amendments (i.e. termination statements) that they believe have been filed without proper authorization. Apart from the question of whether these remedies are adequate at all, they clearly illustrate the downside of the merely ministerial role of filing officers. Apparently, bogus filings take the form not only of financing statements – harming the debtor – but also of termination statements, which may cause second-in-time lenders to obtain a lower ranking than expected. A more fundamental objection to these Art. 9 UCC solutions, however, is the fact that correction of erroneous

213 Debtors will typically be asked by the subsequent lender to show that it had the authority to file a termination statement itself because the secured party of record failed to file or send it as required by § 9-513(a) or (c) UCC. Not only will at least 20 days have passed, the question will also be raised why the secured party of record did not file a termination statement or authorize such statement to be filed. This requires further due diligence to be conducted by the subsequent lender.  
214 All amendments – including termination statements – become part of the financing statement to which they relate. They must therefore identify the initial financing statement by stating the same ‘file number’ (§ 9-102(a)(80)(A) UCC). Debtors do generally have access to the initial financing statement file number, given that file numbers are assigned by the filing office, and are therefore a matter of public record. In fact, filing offices are required by law to maintain and provide this file number to interested parties. This is often done without any charge. In case of such fraud, debtors put the name of the secured party as the authorizing party. Hodnefield; see infra footnote 40.  
215 See supra subsection 2.3.3 of this chapter.  
216 § 9-518 UCC. They do not, however, have a legal duty to do so.  
217 Since unauthorized termination statements are not effective, they cannot compromise a first-on-file secured lender’s position. I found many lawyer’s office websites warning second-in-time secured parties see <www.herrick.com/sitecontent.cfm?pageID=29&itemID=12837> (last visited February 5, 2014) and <www.jaburgwilk.com/articles/better-safe-than-sorry-ucc-termination-statements.aspx> (last visited February 5, 2014).
filings always takes place by the filing of additional documents, rather than those filings being rejected or removed. The Art. 9 UCC solutions, in other words, contribute to pollution of the filing system rather than helping it to stay unpolluted.

Many states have therefore adopted their own legislative approaches, including variations of the Art. 9 UCC rules, to combat these problems more effectively.\(^{218}\) In addition to the imposition of more comprehensive civil and criminal penalties on bogus filers,\(^{219}\) many states provide the debtor with the remedy of ‘expedited judicial relief’. This is a procedure by which the debtor can go to court to ask for an order for removal of the bogus filing from the records.\(^{220}\) Partly in the light of a growing number of bogus filings, many of these state level solutions are – increasingly – aimed at giving filing officers more powers and discretion to refuse to accept filings that are clearly fraudulent.\(^{221}\) Besides being more efficient, these solutions keep the record clean. Other rules give filing officers the authority to take ‘corrective action’ with regard to those clearly fraudulent filings, mostly consisting of removal of the alleged bogus document.\(^{222}\) Despite these measures, the bogus filing problem is anything but reduced. A recently conducted study even speaks of a ‘dramatic increase in the number of fraudulent UCC filings’ in recent years.\(^{223}\) As

\(^{218}\) State Strategies Report, NASS (2012), p. 3 and 7. This seems to be encouraged by the Art. 9 UCC drafters. See Official Comment 3 to § 9-518 UCC: “A summary judicial procedure for correcting the public record and criminal penalties for those who misuse the filing and recording systems are likely to be more effective and put less strain on the filing system than provisions authorizing or requiring action by filing and recording offices.” Cf. Harris & Mooney 2006, p. 173. Furthermore, these issues are addressed at federal level. See for example: Title 18, USC 15.21: False Lien, against Federal Employee and Title 18, USC 15.41: Mail Fraud.

\(^{219}\) Many states authorize victims to seek civil damages, such as attorney’s fees. In addition, in several states bogus filing is regarded as an outright felony that is subject to criminal sanction by fine. Examples of ‘state criminal and civil penalties’ provided by different states are described in State Strategies Report, NASS (2012), pp. 6, 10 and 20-22.

\(^{220}\) For examples of this ‘state post-filing expedited judicial relief’ in several states, see State Strategies Report, NASS (2012), pp. 9 and 18-19.

\(^{221}\) For an example of such a (non-uniform) rejection provision in Texas, see § 405.022 of the Texas Government Code: “If the secretary of state believes in good faith that a document filed with the secretary of state to create a lien is fraudulent, the secretary of state shall: (1) request the assistance of the attorney general to determine whether the document is fraudulent before filing or recording the document; (2) request that the prospective filer provide to the secretary of state additional documentation supporting the existence of the lien, such as a contract or other document that contains the alleged debtor or obligor's signature; and (3) forward any additional documentation received to the attorney general.” (Effective Sept. 1, 2005). See <www.iaca.org/iaca/wp-content/uploads/Bogus_Filing_Task_Force_Presentation.pdf> (last visited February 5, 2014). Cf. Moriniglio 2001, p. 136 and ‘State Strategies to Subvert Fraudulent Uniform Commercial Code (UCC) Filings – A Report for State Business Filing Agencies’ (Washington DC: NASS, 2012) (‘State Strategies Report, NASS (2012)’), pp. 7-8. More examples of such ‘state pre-filing administrative remedies’ can be found on pp. 12-14 of the report.

\(^{222}\) State Strategies Report, NASS (2012), p. 9. Examples of such ‘state post-filing administrative remedies’ in several states can be found on pp. 15-17 of the report.

\(^{223}\) State Strategies Report, NASS (2012), p. 3. On p. 4 this is further explained: “Bogus UCC filings have become more common in recent years due to the explosion in the number of people who identify with an anti-government belief system called the sovereign citizen movement, a loose network of individuals living across the U.S. who believe that the government is illegitimate. The Federal Bureau of Investigation (FBI) has designated sovereign citizens as a domestic terrorist movement, and a growing threat to law enforcement. By some estimates, there are as many as 300,000 sovereigns in the United States, and their numbers are likely to increase. For many of these individuals, paper-based tactics are used to strike
long as the bogus filing problem persists, debtors (and filing officers) will continue to be forced to pursue legal actions to have those bogus filings removed and claim civil damages.\textsuperscript{224} Moreover, a key objective of Art. 9 UCC – \textit{i.e.} that the debtor is deterred from misbehavior – is not necessarily achieved.\textsuperscript{225} By filing a (bogus) termination statement, debtors can – almost just like in a non-public filing system – try to make second-in-time creditors and buyers outside the ordinary course believe that their record is clean, while in fact it is not. They will not succeed in that attempt if the prospective lender or buyer takes its responsibility to conduct due diligence seriously, but it is no rare exception that the latter does not and decides to place reliance on the filing instead.

\subsection*{2.4.3. Remedies if the party on file fails to provide information}

Another question is what happens if the lender on file – which is not fake – \textit{refuses} to provide further information or to terminate existing filings, despite a request by the debtor. On the basis of § 9-625(b) UCC, the lender on file is liable for loss resulting from the debtor’s inability to obtain, or increased costs of, alternative financing. In addition, the lender will be have to pay the debtor $500 (§ 9-625(c)(4) UCC). Both are not adequate remedies, not only because the debtor will have to prove loss, but mainly because any such remedy will always be after the fact and meanwhile the debtor will have been blocked in obtaining the new funding that he was looking for. In addition, $500 is a token amount only. A somewhat more adequate remedy is provided by § 9-625(g) UCC. Under this rule, if the debtor sent a list of collateral it believes to be accurate and the secured lender fails to correct or confirm the list, it may claim a security interest only as shown in the list or statement included in the request as against a person that is reasonably misled by the failure (§ 9-625(g) UCC).

\footnotesize
\textit{back at government interference in their lives. Numerous websites sell how-to kits or offer to train subscribers on how to perpetuate filing schemes in exchange for large fees.}”


\textsuperscript{225} After all, the idea of the filing system is that the reference point is the filing system, and not the debtor. See for example LoPucki & Warren 2012, p. 317-318. Cf. Baird & Jackson 1982, p. 185: “A debtor will be deterred from misbehaving, since a filing system deprives him of the possibility of gaining from such misbehavior”, and: “A filing system places fewer restrictions on the use of collateral than does a possession-based solution to the ostensible ownership problem, yet it still provides information that allows a creditor to avoid the uncertainty caused by the possibility of debtor misbehavior.” But precisely in case of bogus termination statements the debtor will have (be it fraudulently) influenced the filing and may gain from its deception if the searching subsequent lender decides to place reliance on the filing and not to conduct full due diligence.
2.5. Other downside of the UCC filing system: continuing monitoring required

In addition to the practical and logistic obstacles that frustrate the filing and search process, there are other limitations to the Art. 9 UCC filing system, which create uncertainty and generate costs for both first-in-time secured parties and prospective third parties. An important limitation of the Art. 9 UCC filing system is that it functions in such a way that financing statements may lapse or that information relating to financing statements may become incorrect or may change after the filing process has been completed. Depending on how the conflict of interests works out – i.e. for the benefit of first-in-time lenders or prospective third parties – this may have consequences for the actors involved, which will have to put in effort and incur expense to mitigate such consequences.

The first risk that secured lenders run is through the simple passing of time: a filed financing statement just does not remain perfected forever. It is generally effective for a period of five years from the date of filing.\footnote{§ § 9-515(b), 9-102(a)(54) and (67) UCC.} Subsequently, the financing statement ‘lapses’, i.e. it ceases to be effective with the result that any perfected security interest becomes unperfected, unless it is perfected otherwise. Moreover, after five years the security interest is deemed never to have been perfected against ‘purchasers’ of the collateral for value (§ 9-515(c) UCC).\footnote{Let me briefly explain the consequences of this rule. If two secured lenders have a security interest and both are perfected by filing, the first filed security interest has priority over the second (§ 9-322(a)(1) UCC). On lapse of the first-in-time financing statement, the second-in-time secured lender – the ‘purchaser for value’ – will gain priority over the former. After all, the first-in-time security interest becomes unperfected and ‘is deemed never to have been perfected’ against the later one (§ 9-515(c) UCC). This same effect applies to a prospective buyer, who also qualifies as a ‘purchaser for value’: when the financing statement of a secured lender lapses, a buyer can receive clean title to goods, even though it has bought the goods within the 5-year period when the filing was still on file. In both cases, this rule leads to protection of the prospective ‘purchaser’ irrespective of the moment of its ‘purchase’. Even when the purchaser was aware of the registration, it will still take priority over the original secured party whose filing lapsed, but also as against another secured party that has filed between lapse and (re)registration.}

With regard to judicial lien creditors (or a trustee in bankruptcy on their behalf), this rule works out differently. If a creditor acquires a judicial lien on the collateral of the debtor (or if the bankruptcy trustee files for bankruptcy of the debtor) in which a security interest is perfected by filing, the secured party will still trump the judicial lien creditor if the financing statement lapses. If the judicial lien creditor levies after lapse of the financing statement, the second-in-time secured lender – the ‘purchaser for value’ – will gain priority over the former.

\footnote{See supra Chapter 5, section 4.}

234 It is not uncommon that lawyers are sued and held liable for malpractice if – five years after perfection of the security interest – the financing statement just does not remain perfected forever. It is generally effective for a period of five years from the date of filing.\footnote{It is therefore critical to keep the files updated. Secured parties put in great effort and expense to achieve this. They are normally assisted by lawyers with the (continued) }
There are two things secured creditors can do to avoid loss of priority over competing secured lenders and buyers (‘purchasers for value’). First, they can make sure they are ‘perfected otherwise’, for example by taking possession of the collateral before the financing statement lapses. Second – and this is a more commonly used method – they can file a ‘continuation statement’. A continuation statement may be filed only within six months before expiration of the five-year period. Upon timely filing of the continuation statement, the effectiveness of the initial financing statement continues for a period of five years (commencing on the day on which the financing statement would have become ineffective in the absence of the continuation statement). It is therefore of paramount importance to keep the files updated. Secured parties put in great effort and expense to achieve this. They are normally assisted by lawyers with the (continued) perfection of security interests. Use is also made of ‘service companies’, which offer services to keep track of filings by alerting lenders (and their lawyers) when these filings are approaching their lapse date (often called ‘Online Portfolio Management’). Some UCC filing offices include similar tracking features. In addition, lenders take out UCC insurance to insure continued perfection and ‘gap coverage’.

The remainder of this subsection will address other risks lenders are exposed to, not as a result of the mere lapse of time, but by actions of the debtor that lenders have to deal with, as a result of which continued monitoring of the filing system is necessary.

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220 Official Comment 3 to § 9-515 UCC. See also on this subject LoPucki & Warren 2012, p. 388.

221 § 9-515(c) UCC. See § 9-102(a)(27) UCC for the definition of a continuation statement: “Continuation statement” means an amendment of a financing statement which: (A) identifies, by its file number, the initial financing statement to which it relates; and (B) indicates that it is a continuation statement for, or that it is filed to continue the effectiveness of, the identified financing statement.”

222 § 9-515(d) UCC. It is possible to file succeeding continuation statements (§§ 9-515(c)-(e) UCC).

223 § 9-515(e) UCC. See supra Chapter 5, subsection 3.4.1.1. Hence, a secured party cannot maintain the priority of an initial filing by filing a completely new financing statement; this filing must be sustained by means of a continuation statement. LoPucki & Warren indicate that this rule was probably created to guard against the forgery of backdated financing statements. The American courts are usually very strict concerning the treatment of continuation statements: they are held to be ineffective if they are filed too late or too early, even if no party was prejudiced by the error. See LoPucki & Warren 2012, pp. 385-389, also for illustrative case law.

224 It is not uncommon that lawyers are sued and held liable for malpractice if – five years after perfection – they fail to raise the alarm and the financing statement lapses. See LoPucki & Warren 2012, pp. 388-389.

225 For more information on such service companies, see supra Chapter 5, subsection 3.5.3.

226 See for example the website of First American Title, which provides ‘The Insured Filing’ to filers: “This policy provides gap coverage against intervening liens, perfection insurance for registered organizations (…)” <http://www.firstam.com/title/ucc/products/search-and-filing/the-insured-filing.html> (last visited February 5, 2014).
2.5.1. The debtor may change its name

One of the main risks threatening lenders is that of a debtor changing its name. A name change can take place through an ordinary name change, but it can also take place fraudulently:

"Notwithstanding the incentives to behave, sometimes debtors run amok, drastically changing their names and not telling the secured party." 237

If a debtor changes its name and does not reveal the old name and address to the searcher, first- and second-in-time secured lenders (who are not aware of one another’s existence) may both believe they are the ‘first to perfect’. 238 Art. 9 UCC allocates this risk as follows. In principle, a financing statement that fails to provide sufficient detail as to the name of the debtor is seriously misleading. 239 Hence, in principle, the first-in-time lender has the burden of tracking down name changes to avoid the risk of being subordinated to a prospective third party. Then again: the first-in-time lender is offered a four-month grace period during which its (‘seriously misleading’) financing statement remains effective to perfect collateral. A financing statement with regard to collateral that the debtor has acquired four months after the filing has become seriously misleading, is not effective unless an amendment to the financing statement that stops it being seriously misleading is filed within four months after that moment. 240 In other words, the secured party on file (in U.S. jargon: ‘the secured party of record’) must amend its financing statement to reflect a debtor’s name change within four months: failure to do so will result in that creditor being unperfected in respect of the collateral concerned.

LoPucki & Warren point out that this entails that if a secured party has financed the purchase of a specific item of collateral (such as a boat), it does not have much reason to worry about later changes in the debtor’s name, since the collateral has already been acquired by the debtor and the security vested. However, if a secured party is financing the debtor’s inventory on a rolling basis, it should be concerned about changes in the debtor’s name. After all, in the latter case the secured party’s filing will not be effective against inventory that the debtor acquires more than four months after it has changed its name. 241 According to Livingston, the drafters decided to make this distinction because

LoPucki & Warren 2012, p. 398 and Livingston 2011, p. 185. This is why in practice security agreements often provide for an obligation on the part of the debtor to inform the security holder of any changes (such as name, principal place of business) that will be made or have occurred that may affect the effectiveness of filings. If the debtor fails to do so, a breach of contract takes place, resulting in civil liability. In addition, an undisclosed name change often gives the lender the power to accelerate the loan. Livingston 2011, p. 186 and LoPucki & Warren 2012, pp. 398-399.
inventory lenders – unlike equipment lenders – monitor their debtors closely anyway to make sure they maintain adequate collateral; tracking debtors’ name changes would not require very much more of them.\textsuperscript{242} White & Summers provide a very useful example in this respect: “Suppose a debtor partnership named Jupiter gave a perfected security interest in its equipment and inventory to Bank on October 31. Jupiter changes its name to Zeus on November 1. Five months later Zeus still owns the original equipment, but all of its inventory held on April 1 was acquired in March. During the period October 31 to April 1, Bank has filed no new financing statement in the debtor’s new name, Zeus. If Bank perfected “Yes” as to the equipment, “No” as to the inventory. Had Bank filed an amendment under “Zeus” within four months of the November 1\textsuperscript{st} name change, it would have enjoyed continued perfection as to the inventory as well.”\textsuperscript{243}

Evidently, such name-change rule (also) holds a risk for searchers: if the debtor has changed its name, a search under the debtor’s current, correct name will uncover no filings, whereas an effective filing in the debtor’s former name may still exist in the filing system with respect to both existing and after-acquired property. Searchers should therefore always trace back name changes and search the filing system under the relevant former and new names of the debtor.

As a consequence of this rule and irrespective of what type of debtor they are dealing with, monitoring costs are unavoidable for both the secured party of record and (searching) prospective ‘purchasers’. It will probably depend on the amount of the financial interest at stake and the degree of confidence in the debtor, whether or not they may want to check if the debtor recently changed its name.\textsuperscript{244} In the case of registered debtors, lenders would have to periodically check the Secretary of State’s corporate charter files for corporate name changes. In the case of non-registered debtors, lenders would have to use other sources and keep an eye on any change of e.g. letterhead used by the debtor:

“The secured party should try to have in place certain monitoring systems, under which the creditor keeps track of the name that the debtor is using on its checks to the secured party, on its letterhead, and in its advertising. In addition, the secured party should run a routine check every four months in the state’s corporate registry, which should reveal whether or not the debtor has changed its legal name. If a name change has occurred, the secured party should immediately refile using the new name. Finally, if the creditor does not learn of the name change despite its best efforts and the debtor goes into bankruptcy, it can always argue the equities in its favor and beg the court for constructive trust.”\textsuperscript{245}

Hence, both secured parties of record and prospective ‘purchasers’ must instead keep an eye on name changes to maintain their ranking. Besides uncertainty, this generates costs.

\begin{footnotes}
\item[242] Livingston 2011, p. 185.
\item[244] LoPucki & Warren 2012, p. 398.
\item[245] Livingston 2011, p. 187.
\end{footnotes}
Chapter 6

2.5.2. The debtor may change its identity
Another potential risk for secured creditors occurs if the debtor merges with another company.246 If, as a result of this change in business structure the debtor’s name is also changed, Art. 9 UCC applies the same four-month rule described above. The financing statement is not effective to perfect a security interest in collateral acquired by the new debtor more than four months after the new debtor becomes bound under § 9-203(d) UCC, unless an initial financing statement providing the name of the new debtor is filed before the expiration of that time.247 Thus, if the debtor’s name has not been changed after a merger, the lender of record is always safe; if the debtor’s name has changed, the lender of record is only safe for four months after the change.248 This means that secured parties of record and prospective third parties should keep track of changes in their debtors’ business structure. In addition, secured parties of record should complement their existing filings accordingly.249

2.5.3. The debtor may change the use of its collateral
In addition to the risks stated above, lenders have to take account of the risk that debtors may change the use of their collateral, as a result of which the description of the collateral in the financing statement becomes inaccurate. Some of these changes in use of the collateral will render a financing statement ineffective.250 Generally, this is the case if the perfection method used for the initial filing is not a valid filing perfection method for the ‘differently used’ type of collateral.

This is the case, for example, if an inventory car – which is generally perfected by filing – is used as a non-inventory car. To remain perfected, the secured party of record should re-perfect its security interest by obtaining a notation on the certificate of title.251

246 See supra Chapter 5, subsection 2.1.3: as a primary rule, the security agreement entered into by the original debtor automatically binds the successor i.e. the new debtor (§ 9-203(d) UCC). Cf. LoPucki 1992, p. 8.
247 § 9-508(b) (1) and (2) UCC.
248 § 9-508(a) UCC. No special authorization is needed for this type of amendment filing; § 9-509(b) and (d) UCC. See also Official Comment 4 to § 9-508 UCC, Picker 2009, pp. 338-357, Harris & Mooney 2006, p. 497 and Dalhuizen II 2013, p. 471.
249 LoPucki 1995 provides useful background information on how reincorporation takes place, see p. 614: “For the reincorporation to be effective under corporate law, the surviving entity must file the articles of merger in the corporate records of both the source and destination states. A search of the public filings in either will reveal the fact of reincorporation, the date of reincorporation, and the name of each non-surviving entity against which there may be valid filings.” Cf. LoPucki & Warren 2012, p. 417: “The merger will be a matter of public record, generally in both the original and the destination states. Because articles of merger must be filed in the states of incorporation of each of the merging entities, the secured creditor can discover a merger by monitoring the record of its debtor’s incorporation in the original state.”
250 LoPucki & Warren 2012, p. 401: “(. . .) in some circumstances, a change in the use a debtor makes of collateral can deprive the secured creditor of perfection.” Cf. White & Summers 2002 § 31-14 on this topic.
251 § 9-311(b) UCC; see supra Chapter 5, subsection 3.2.2.
If both types of collateral are covered by the same perfection method – for example if inventory is used as equipment – Art. 9 UCC strikes the balance in favor of the first-in-time secured lender of record. This means that the secured lender of record has no duty to correct information in a filed financing statement: even if the financing statement becomes seriously misleading, it will remain effective.\textsuperscript{252} Hence, in this case, searchers have to take into account the risk that the collateral at stake (which is now used as equipment) is actually covered by a financing statement of another lender. As a result of these rules, not only does the lender of record need to monitor the debtor’s use of the collateral; prospective lenders must also take account of the risk that there might (recently) have been a change in use of (part of the) debtor’s collateral, as a result of which the collateral is covered by a (still) effective financing statement of another lender.

2.5.4. The debtor may exchange the collateral for other collateral or cash (proceeds)

Besides name or identity changes, debtors may exchange their collateral for cash or for other collateral. Depending on the circumstances, these assets qualify as after-acquired property\textsuperscript{253} or proceeds.\textsuperscript{254} This subsection will address what a secured party must do to be perfected and to stay perfected in these assets, without having to file (a) new financing statement(s) after the initial financing statement.\textsuperscript{255} If secured lenders do not take this further action, they risk losing their perfected status, and accordingly their ranking.

2.5.4.1. When collateral is exchanged for other collateral (‘barter trades’)

Transactions by which goods are directly exchanged for other (types of) goods without the use of cash are often referred to as ‘barter trades’. Three types of barter will be discussed in this subsection. The first is that in which the proceeds received by the debtor fall within the description of the collateral in the financing statement that has already been filed, because the description is broad enough to cover both the original collateral and the collateral that has replaced the original collateral. In this case, no additional financing

\textsuperscript{252} § 9-507(b) UCC.

\textsuperscript{253} A financing statement is effective to cover after-acquired property of the type indicated, regardless of whether an after-acquired property clause is adopted in the security agreement. In other words, the after-acquired secured party’s priority against other Art. 9 UCC secured creditors dates from the time of filing. See supra Chapter 5, subsection 2.1.4. Cf. LoPucki & Warren 2012, pp. 524-525 and see supra Chapter 5, subsection 3.3.1.3.

\textsuperscript{254} Secured lenders have an automatic right to proceeds, even when the security agreement is silent on this. The only condition is that the proceeds are ‘identifiable’ (§ 9-315(a)(2) UCC). This follows from § 9-203(f) UCC, in conjunction with § 9-102(a)(12) UCC and § 9-315(a)(2) UCC. § 9-203(f) UCC: “The attachment of a security interest in collateral gives the secured party the rights to proceeds provided by Section 9-315 (…)”; § 9-102(a)(12) UCC: “‘Collateral’ (…) includes (…) proceeds to which a security interest attaches (…)”, and § 9-315(a)(2) UCC: “(…) a security interest attaches to any identifiable proceeds of collateral.” Furthermore, the security interest will attach to any ‘supporting obligation’, such as a guarantee (§ 9-203(f) UCC). See also § 9-102(a)(78) UCC. See supra Chapter 5, subsection 2.2.2.

\textsuperscript{255} The three situations and the illustrative examples described in subsections 2.4.5.1-2.4.5.3 are taken from LoPucki & Warren 2012, pp. 402-407.
statement is necessary: the security interest attaches to the replacement collateral simply on the basis of the description (§ 9-203(f) UCC). The searcher will take cognizance of what is encumbered.

Example: in the security agreement the collateral is described as ‘Coyote Loader, serial number 8203G45’, the financing statement describes the collateral only as ‘loader’ and the Coyote Loader, serial number 8203G45 is replaced by a Caterpillar Loader.256

The second type of barter is that in which proceeds received by the debtor are not covered by the description in the financing statement, but do qualify as property in which a security interest could be perfected by filing in the same office where the secured creditor’s financing statement has already been filed.

Example: the initial financing statement covers only inventory but the debtor exchanges part of its inventory for a piece of equipment. For the equipment to be covered by the financing statement, a filing in the same filing office would be required.257

In this situation, the secured lender’s interest remains perfected without the need to file a new financing statement. This rule is referred to as the ‘same office’ rule. Here, a searcher cannot rely on the description of collateral in any financing statement unless it knows that the debtor acquired the collateral in question in a barter transaction.258

Thirdly, barter could involve collateral being replaced by non-cash proceeds of a type that requires filing in a different office than the office in which the original collateral was perfected.

Example: the original financing statement covers equipment but the debtor exchanges part of its equipment for automobiles. For the automobiles to be covered by the financing statement, a filing in the Department of Motor Vehicles office would be required.259

In this situation, the secured party’s interest does not automatically remain continuously260 perfected: it must refile a financing statement in the correct filing office in order to be perfected in these proceeds, and it must do so within 20 days from the time the debtor

256 These assets qualify as identifiable proceeds on the basis of § 9-203(f) UCC. LoPucki & Warren discuss this example by reference to ‘type 0 barter’; see LoPucki & Warren 2012, p. 402.
257 LoPucki & Warren discuss this example by reference to ‘type 1 barter’; see LoPucki & Warren 2012, pp. 402-403. Cf. White & Summers 2002, § 31-17(b); illustrative case law can be found in footnote 8.
258 § 9-315(d)(1)(B) UCC. LoPucki & Warren discuss this example by reference to ‘type 1 barter’; see LoPucki & Warren 2012, p. 403. See also Official Comment 5 to § 9-315 UCC.
259 LoPucki & Warren discuss this example by reference to ‘type 2 barter’; see LoPucki & Warren 2012, p. 403.
260 This means that the perfection relates back to the time when the creditor first became perfected.
receives the proceeds.\textsuperscript{261} Hence, here, the burden of monitoring the debtor is on the secured lender of record, rather than on the searcher.\textsuperscript{262}

2.5.4.2. When collateral is exchanged for cash and the cash is used to buy new collateral

When the debtor exchanges (e.g. sells) collateral for cash and uses the cash to buy new collateral, the creditor’s security interest will cover the newly bought property as ‘proceeds of proceeds’.\textsuperscript{263} As to the question of what should be done to maintain perfection over these proceeds, the same three situations as described above can be distinguished.

If the new collateral falls within the description of the collateral on the financing statement that has already been filed – the first situation – the security interest covers both the original collateral and the replacement collateral because the description is broad enough.

Example: if the debtor sold the Coyote Loader for cash and bought a new Caterpillar Loader for that cash. The security interest automatically attaches to the Caterpillar Loader as ‘proceeds’ of the Coyote Loader; see § 9-315(d)(3) UCC. Refiling is not necessary to maintain perfection.\textsuperscript{264}

If, however, the debtor sells part of its inventory and uses the cash to buy equipment – we now come to the second of the three situations described above – Art. 9 UCC requires the secured party to file a financing statement to cover the equipment in order to stay continuously perfected.\textsuperscript{265} This has to be done within 20 days of the debtor’s receipt of the equipment. If the secured party files the financing statement later, perfection takes place from that moment.\textsuperscript{266}

The same applies for the third situation, in which the debtor uses the cash from the sale to acquire collateral that requires filing in a different filing office.

Take again the example where the debtor sold its Coyote Loader, but now suppose that the debtor uses the cash to buy an automobile. To be continuously perfected, the secured creditor has to perfect the automobile on the certificate of title within 20 days of the debtor’s receipt of the automobile; see § 9-315(d)(3) UCC.\textsuperscript{267}

\textsuperscript{261} § 9-315(d)(3) UCC. The secured party does not need any additional authorization for this refiling; § 9-509(b)(2) UCC. Cf. LoPucki & Warren 2012, p. 410.

\textsuperscript{262} According to Picker, the purpose of this rule seems to be to reduce the secured party’s burden of monitoring the debtor to once every twenty days. Picker 2009, pp. 264-265.

\textsuperscript{263} § 9-102(a)(12) UCC and (64) UCC, LoPucki & Warren 2012, p. 406 and supra Chapter 5, subsection 2.2.2.

\textsuperscript{264} LoPucki & Warren discuss this example by reference to ‘type 0 change’; see LoPucki & Warren 2012, p. 406.

\textsuperscript{265} § 9-315(d)(3) UCC.

\textsuperscript{266} LoPucki & Warren discuss this example by reference to ‘type 1 change’; see LoPucki & Warren 2012, p. 406. See also Official Comment 5 to § 9-315 UCC.

\textsuperscript{267} LoPucki & Warren discuss this example by reference to ‘type 2 change’; see LoPucki & Warren 2012, pp. 406-407.
2.5.4.3. When collateral is exchanged for cash proceeds and the debtor keeps the cash
Another possibility is that the debtor simply keeps the cash proceeds and, instead of investing it in other property, deposits the cash in a bank account. In that case, Art. 9 UCC dictates that the secured party will be continuously and perpetually – i.e. for as long as the money is stored in the account – perfected in identifiable cash proceeds.270

2.5.4.4. Concluding remarks
Secured lenders have a considerable degree of protection when it comes to extending security interests to proceeds. They nonetheless have to devote resources to making sure that those security interests are also (continuously) perfected in those proceeds. They should mainly be concerned about transactions in which the debtor exchanges the collateral (whether or not directly) for a different type of collateral, especially when that collateral requires filing in a different filing office. As a result, close and continuous monitoring to discover the exchange (and to refile in time) is essential. The form and substance of such monitoring may differ from lender to lender and may depend on, among other things, the nature of the collateral, the level of trust in the debtor etc. Some lenders do not monitor at all; others physically visit the debtor’s premises often, on an irregular and unpredictable schedule.271 These rules have implications for searchers as well: the ‘same office’ rule, for example, results in a financing statement covering property that is not described, which means that the searcher cannot rely on the description of collateral in any financing statement.

2.5.5. The debtor may relocate its business – or transfer the collateral – to another state
Another potential risk for secured lenders is that the debtor moves its business to another state. As a result, they may lose their perfected status.

A debtor that is a non-registered organization may relocate by (physically) moving its place of business or its chief executive office. A debtor that is a registered organization cannot simply ‘move’ its location; it can only reincorporate in another state.272 Security agreements usually do not allow reincorporation by changing the state in which a registered organization is organized without informing the lender beforehand.273

268 § 9-102(a)(9) UCC: “‘Cash proceeds’ means proceeds that are money, checks, deposit accounts, or the like.”
269 When proceeds are ‘identifiable’ was discussed in Chapter 5: subsection 2.2.2, especially footnote 166.
271 Loan documents will for that purpose provide that the secured lender has the right to inspect the debtor’s premises, to inspect the collateral for the purpose of protecting the lender’s security interest.
272 § 9-307(b)(2) and (3) UCC.
When a non-registered organization moves to another state, the secured lender has four months to re-perfect a security interest that attached prior to the debtor’s relocation.\(^\text{274}\) If the debtor is a registered organization, the secured party has one year to refile in the destination state.\(^\text{275}\) If these grace periods lapse without a re-perfection taking place, the security interests become ‘retroactively unperfected’ – i.e. they become unperfected and are deemed never to have been perfected – as against a purchaser of the collateral for value.\(^\text{276}\)

Example: a debtor is incorporated in Pennsylvania and Secured Lender 1 perfects a security interest in the debtor’s equipment by filing in Pennsylvania. Subsequently, Secured Lender 2 perfects its security interest in the same equipment by filing a financing statement in Pennsylvania. Next, the debtor reincorporates in Delaware by merging with a company in Delaware. Under § 9-322(a)(1) UCC, Secured Lender 2 is subordinate to Secured Lender 1. Within a year after the merger (§ 9-316(a)(3) UCC), Secured Lender 2 reperfects by filing in Delaware, but Secured Lender 1 fails to do so. According to § 9-316(b) UCC, Secured Lender 1’s security interest is ‘deemed never to have been perfected’ against Secured Lender 2: the purchaser for value. Consequently, Secured Lender 2’s security interest has priority (§ 9-322(a)(2) UCC).\(^\text{277}\)

With the adoption of the 2010 amendments, this rule of continued perfection was extended to security interests that attach to property acquired by the debtor within four months after its relocation. To remain continuously perfected after these four months, the lender will have to refile before expiration of the four-month period.\(^\text{278}\)

Before this amendment, the four-month period for perfection only applied to property owned by the debtor at the time of the relocation. Hence, after-acquired property was only perfected when the secured party took specific action by filing a financing statement in the new state.\(^\text{279}\)

A similar rule applies with respect to security interests that attach within four months after the debtor’s merger into another company. A lender will remain perfected in collateral that its debtor acquired before, and within four months after, the merger from which a ‘new debtor’ emerged as the surviving entity. Here too, in order to continue to be

\(^{274}\) § 9-316(a)(2) UCC. See also Official Comment 2 to § 9-316 UCC; see especially examples 1-4. Cf. Sigman 1999a, pp. 65-66.

\(^{275}\) § 9-316(a)(3) UCC.

\(^{276}\) § 9-316(b) UCC. The drafters assumed that these grace periods are long enough to discover such a change of location. See Official Comment 2 to § 9-316 UCC; see especially examples 1 and 2. No further explanation is given why these grace periods differ depending on whether a non-registered or registered debtor is at stake.

\(^{277}\) Example taken from Official Comment 2 to § 9-316 UCC; see especially examples 4 and 6. The same applies when Secured Lender 2 is a buyer. See Official Comment 2 to § 9-316 UCC, example 5. Compare § 9-515 UCC, as discussed in Chapter 5, subsection 2.5.1, which takes the same approach with respect to lapse of the financing statement. Cf. White & Summers 2002, § 31-16.

\(^{278}\) § 9-316(b) UCC.

\(^{279}\) See e.g. Official Comment 7 to § 9-316 UCC, example 9, Frisch 2011, pp. 1021-1022 and Harris, Kilborn & Livingston 2012, p. 486.
perfected with regard to this collateral after these four months, the lender will have to refile in the destination state before expiration of the four-month period. If the lender does not refile, the security interest will become unperfected at the end of the four-month period and will be deemed never to have been perfected as against a purchaser for value.

If the debtor transfers (part of) its collateral to a debtor located in another state, the financing statement first filed against the first debtor will not be found. After all, the searcher is dealing with the (prospective) debtor located in a different state than where the financing statement was filed. Under Art 9 UCC, the earlier filer has a grace period of one year to re-perfect its security interest in the other state. If it does so, it remains continuously perfected, also vis-à-vis a competitor that filed against (this part of) the debtor’s collateral in the destination state.

2.5.6. Final remarks
To conclude, first-in-time secured lenders are forced to implement policies to monitor e.g. changes in the debtor’s location, name or identity and the collateral, in order to protect themselves against loss. Filings should be made in the new state (and sometimes under the new entity) as soon as such changes take place. Second-in-time (i.e. searching) lenders, in turn, need to ascertain whether the debtor has recently e.g. changed its location, identity or name, or whether it has recently bought collateral from a debtor located in another state. Should this be the case, they must search for filings in another state, under a different name and so on. Besides uncertainty, this generates costs for the parties using and relying on the filing system.

3. The Art. 9 UCC approach to fraudulent antedating
The previous section discussed the extent to which Art. 9 UCC adequately addresses the risk of ‘proprietary conflicts’, i.e. conflicts where parties fight for the same (proprietary position in the) asset. It reported on both the ‘effectiveness’ of the Art. 9 UCC approach and on ‘cost-efficiency’ aspects for the parties using and relying on the Art. 9 UCC filing system.

This section will now discuss whether Art. 9 UCC mitigates the second main risk faced by the investigated parties operating in a non-public filing system: the risk that the...
creation and effectiveness of a security interest can be fraudulently antedated to the detriment of the debtor's secured and unsecured creditors.285

3.1. Basics and positive aspects of the Art. 9 UCC solution
Under Art. 9 UCC, the antedating of security is primarily prevented by the fact that security rights do not have third party effect until a notice of their possible existence has been filed in the public filing system. The moment from which a security right can be invoked against prospective third parties is thus objectively verifiable.286 In addition to being objectively verifiable, this moment cannot be manipulated in any way, given that entries in the filing system cannot be altered. Generally, it is only permissible to add or delete collateral covered by, or otherwise amend the information provided in, a financing statement by submitting an additional filing: an ‘amendment’.287 Such filing will not cause any change whatsoever to the date in the (former) filing to which the amendment relates – not even retroactively.288 Although legal literature on the subject does not give much attention to this aspect of the Art. 9 UCC filing system,289 it is described to some extent, mostly in the context of competing secured lenders in reference to the filing system’s possibility of producing ‘a fixed moment in time’:

“In order to have a right that is enforceable against third parties and to determine the ranking with competing entitlements, it is sufficient that there is a fixed point in time that allows, without discussion, to establish the creation of a security right.”290

285 See supra Chapter 4; section 6.
286 The ‘A Guide to Movables Registries’ (Manila: ADB, 2002), p. 7 also describes this as the second important function of registering security rights: “[Registration in a movables registry] (…) provides a coherent framework for ordering priorities among competing claimants to the same item of charged collateral by adopting an objective public act—registration—to establish the effective priority date of a charge.”
287 §§ 9-512(a) and 9-509(a) UCC.
288 Unless otherwise provided in § 9-515 UCC. See §§ 9-512(b) UCC and 9-515 UCC.
289 According to LoPucki this function of the filing system is (no more than) a ‘by-product’. He argues that “[t]he filing system certainly serves these goals as well, but they are considerably less important and are subsumed in the goal I [i.e. LoPucki’s] attribute to the system (…)”, which is the function of communicating the existence of prior security interests to those who will take subject to them. See LoPucki 1995, p. 582, especially footnote 19. Cf. Plank 2013, p. 448.
290 Dirix 2004, p. 85; see also on p. 93. Cf. ‘Model Law on Secured Transactions’ (London: EBRD, 2004), p. 13: “Once a system of publicity is in place, it provides a convenient and simple means to determine the chronological ranking order of charges and also of other rights that are included on the charges register. The time of registration (actual entry in the register) will usually be used as the determining factor for deciding the chronological order of ranking.” Cf. ‘The UNCITRAL Legislative Guide on Secured Transactions’ (Vienna: UNCITRAL, 2010), p. 149, mentioning this as one of the three goals of a public filing system: “(…) registration contributes to the efficient and fair ordering of priority by establishing an objectively verifiable temporal reference for applying priority rules based on the time of registration.” Compare Harris & Mooney, who argue that Art. 9 UCC’s priority rules based on the time of filing reduce evidentiary costs and disputes on priority, since the public office filing system “memorializes” the time of filing and constitutes a visible and (generally) reliable “scoreboard”. Harris & Mooney 2011, p. 159. See also Sigman 2004, p. 59 about notice filing: “(…) establishes an objective marker, a date certainly not subject to private manipulation, which can be, and in most cases is, used as a priority determinant.”
As I said earlier, I do not so much consider the possibility of creating such a fixed moment in time as a way to easily determine priorities, but rather as a way to prevent fraudulent attempts by creditors seeking to obtain security by means of bogus proprietary transactions or manipulation of the precise moment in time at which proprietary transactions are said to have taken place, resulting in a decrease of the pool of available assets. In the case of such fraud, unsecured creditors are harmed because the debtor’s estate is manipulated and their recovery unduly diluted. Secured creditors may likewise be harmed since the integrity of their security may be unjustly compromised and they may lose their priority rank.291

There is yet a separate feature of Art. 9 UCC that contributes to the prevention of antedating, or that at least seems to be doing so. This is the rule of § 9-322(a)(1) UCC, granting priority on the basis of the ‘Filing Priority Principle’.292 This rule permits a creditor to file a create a financing statement with regard to the assets concerned, even though the security interest to which such filing relates has not yet been created.293

Example: If Lender A files a financing statement on January 1 but neither grants a loan nor signs a security agreement, the security interest is deemed unperfected simply because it has not attached yet (see § 9-308(a) UCC). If Lender B subsequently files a financing statement on January 7 against the same collateral, and grants a loan at the same time, it will be perfected. However, if Lender A then grants the debtor a loan on January 15 and has the corresponding security agreement signed on that date, it will take priority over Lender B, even though the latter’s loan was made earlier and was perfected at the time the loan was made. Hence, Lender A has priority because it ‘filed or perfected’ (i.e. it filed on January 1) before Lender B did (i.e. Lender B filed and perfected on January 7). It makes no difference whether Lender A knew of Lender B’s security interest when Lender A advanced its loan.294

The example shows that Art. 9 UCC affords prospective secured lenders the possibility to lay claim on (part of) the debtor’s assets and ‘fix’ their priority even though the security concerned has not yet come into existence. As long as a lender has filed its notice prior to others (and provided that the description of the collateral in the notice is formulated broadly enough), this lender will trump subsequent secured lenders with respect to

291 See supra Chapter 4; subsection 3.2.
292 Phrase taken from Plank 2013, p. 439 et seq.
293 See Plank 2013, p. 443: “The Filing Priority Principle favors a subsequent transferee that provides notice of a potential interest in a property item by filing such notice pursuant to an established filing or recordation regime over an earlier transferee that acquired its interest after the filing but before the subsequent transferee completes the steps necessary to acquire its interest. (...) the most prominent and innovative application of the Filing Priority Principle is the relatively new (...) first-to-file-or-perfect rule for competing perfected security interests of UCC section 9-322(a)(1) (...)” See furthermore on p. 444: “To facilitate the operation of the notice filing system adopted by Article 9, the first-to-file-or-perfect rule permits a person that has not yet obtained an interest in a property item to create a conditional superior interest in that property item by filing a financing statement that provides relatively accessible notice to subsequent persons of that person’s potential property interest.”
294 This example was inspired by the several examples provided by Official Comment 4 to § 9-322 UCC and by Plank 2013, p. 456 and LoPucki & Warren 2012, pp. 520-521. It was also used in subsection 4.3.1 of Chapter 5.
security interests in the same collateral that have been created and have come into existence after the first filing but before the creation of the first lender’s security, even if it knows of the intervening lenders. This ‘Filing Priority Principle’ takes away much of any incentive to manipulate the date of the security agreement, since it is not the date of such agreement and hence attachment that determines the order of priority, but the date of filing. Also, under Art. 9 UCC there is nothing wrong with attachment only at a later point in time.

For a Dutch lawyer this is a curious concept, since in Dutch law ‘perfection’ is not a separate step in the process of creating security and ‘attachment’ has no legal significance. Instead, the order of priority is determined by the order of creation of the security concerned and where by statute registration with the tax authorities is required, such registration is an integral part of the process of creating the security and not merely a matter of perfection; without registration, the security does not only fail to ‘attach’: it does not exist at all.

As a result, ‘antedating’ is no relevant concept when seen only in the (narrow) context of achieving priority between successive secured lenders, which is determined solely by the order of filing. However, under Art. 9 UCC, antedating may still be relevant, especially in circumstances where a lender may hold an earlier filing and may have put the debtor in funds in anticipation of execution of the security agreement, but is confronted with an intervening levy on the collateral concerned, or even a bankruptcy of the debtor, prior to having achieved attachment of the security. I will discuss this separately in subsection 3.2.

Only if the filer agrees to expand the secured collateral package over and beyond what was filed in the financing statement, will it be unable to claim these assets vis-à-vis third parties until an amendment containing this broader description is filed. In that case, if an intervening lender has filed a financing statement covering that collateral in the meantime, the first-in-time lender will therefore be subordinate to the intervening lender.

It should be noted that there is one exception to the rule that a lender cannot claim more vis-à-vis intervening secured lenders than it has filed in the financing statement. First-in-time lenders may have the benefit of more collateral than they have described in their filings. For example, when a lender takes a security interest and perfects it by filing, that security interest will also be perfected with regard to future advances that the debtor draws on the underlying line of credit. Future advances will be covered by the initial financing statement filed by the initial secured creditor, without the need for any new filing. Equally – as was discussed in detail in Chapter 5, section 4 – the initial secured creditor will have priority over (loans by) intervening secured creditors with regard to these future advances as of the filing of the financing statement. The same applies in

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293 See supra Chapter 2, subsection 2.4.1.
294 See Picker 2009, pp. 323-335 and LoPucki & Warren 2012, pp. 522-523. Should you wonder how this can be justified from the viewpoint of ‘publicity’ or ‘the purpose of the filing system of giving notice’, LoPucki & Warren offer the following arguments: ‘An important function of an Article 9 financing statement is to put
This first-to-file mechanism even applies to financing statements that have not (yet) been authorized by the debtor at the time of filing. In principle, financing statements are effective only when the debtor has authorized their filing. Consequently, if the debtor authorizes the filing of a financing statement covering inventory and the lender files a financing statement covering other, or more, collateral, the financing statement is effective (and thus perfected) only with regard to inventory. However, if the debtor authorizes the filing at a later time – for example by signing the security agreement only after the filing – the filing becomes effective with retroactive effect and the § 9-322(a)(1) UCC priority rule will apply.

Because Art. 9 UCC does not provide for all priority conflicts to be settled on the basis of the filing date, the risk of fraudulent ‘antedating’ may still be relevant in bankruptcy or in the case of priority conflicts other than between secured lenders. This will be discussed in the next subsection.


299 See Official Comment 2 to § 9-510 UCC and Sigman 1999a, p. 71, footnote 75.
300 By signing the security agreement the debtor authorizes ipso facto the filing of a financing statement (or an amendment thereof) covering the collateral described in the security agreement and proceeds thereof, whether or not the security agreement expressly covers proceeds. See §§ 9-509(b)(1) and (2) UCC and § 9-315(a)(2) UCC.
301 Official Comment 4 to § 9-322 UCC, adopted in the 2010 amendments, provides this explicitly: “Under a notice-filing system, a filed financing statement indicates to third parties that a person may have a security interest in the collateral described. With further inquiry, they may discover the complete state of affairs. When a financing statement that is ineffective when filed becomes effective thereafter, the policy underlying the notice-filing system determines the ‘time of filing’ for purposes of subsection (a)(1). For example, the unauthorized filing of an otherwise sufficient initial financing statement becomes authorized, and the financing statement becomes effective, upon the debtor’s post-filing authorization or ratification of the filing. See Section 9-509, Comment 3. Because the notice value of the financing statement is independent of the timing of authorization or ratification, the time of the unauthorized filing is the ‘time of filing’ for purposes of subsection (a)(1). The same policy applies to the other priority rules in this part.”


3.2. Shortcomings of the Art. 9 UCC solution

3.2.1. The risk of antedating with regard to intervening judicial lien creditors and buyers, and around bankruptcy

Under Art. 9 UCC, not all priority conflicts are settled on the basis of the filing date. In the context of this research, it is interesting to discuss the priority conflict between secured lenders and judicial lien creditors and buyers. On the basis of § 9-317(a)(2) UCC, a secured lender that has filed a financing statement, or otherwise perfected the security interest, will trump an unsecured creditor but only so if the lender has also authenticated the security agreement and did so before the unsecured creditor ‘has become a lien creditor’ with regard to the assets concerned. Hence, if the debtor authenticates the security agreement only after the unsecured creditor has become a lien creditor, the secured lender will be subordinate to the lien creditor, despite its earlier filing. The same applies to priority conflicts between secured lenders and subsequent buyers outside the ordinary course of business. If the debtor transfers an asset outside the ordinary course of business, the secured lender will only have the benefit of a security interest with respect to that asset if the security had been perfected before the buyer acquired the asset. Accordingly, the lender may be tempted to collude with the debtor to antedate the security agreement and to pretend the security had attached prior to the transfer of the asset, in order to be able to (fraudulently) claim security in priority of the buyer.  

Plank justifies this rule by the fact that the drafters did not have a good policy reason to make an exception to the ‘nemo dat’ rule. In relation to lien creditors specifically, Plank explains that these creditors are not ‘reliance lenders’: ‘(…) a lien creditor (…) did not rely on specific items of the debtor’s property in extending credit and it only gets to be paid out of whatever property the debtor has at the time that it can get an execution lien. It is therefore not relying on the filing system to advance its interests.’ Plank thus seems to argue that because lien creditors do not check the filing system, they deserve to have priority over lenders if they obtained their lien before the lenders stipulated a security interest, and rightly so.

This priority mechanism with respect to security interests also applies in bankruptcy. If a lender claims collateral under a security interest that has been perfected but has not (yet) attached, the trustee in bankruptcy can simply assert the debtor’s claim that the security interest is ineffective and keep the collateral for the bankruptcy estate. Thus, whereas later-in-time attachment can be invoked against a subsequent lender as long as the filing

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302 The moment at which an unsecured creditor qualifies as a ‘(judicial) lien creditor’ varies from state to state. Under the law of most states, the moment a creditor ‘obtains a lien’ is linked to the moment the sheriff takes possession of the goods, i.e. the date of levy. Other states award a lien priority by linking it to the date of delivery of the writ to the sheriff. Then again, more and more states are allowing a judgment creditor to ‘perfect’ the lien by filing a judgment (or a notice of it) in the UCC filing office. See supra Chapter 5; subsection 4.1.3.

303 For several other examples of the operation of this rule, see Plank 2013, pp. 467-468 and Harris & Mooney 2006, p. 29.

304 Plank 2013, p. 469.

305 §§ 9-203 UCC and 541, 558 BC.
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was first in time (see supra subsection 3.1), this does not equally apply vis-à-vis attaching creditors (‘judicial lien creditors’) or when the debtor is bankrupt. The next subsection will therefore discuss if Art. 9 UCC prevents manipulation in respect of the attachment date.

3.2.2. Formal requirements for authentication

In the aforementioned situations, lenders may have an interest in antedating the security agreement, i.e. in manipulating the moment attachment takes place. Such antedating would entail a change from an authentication date after the time when lien creditors or buyers obtained their legal status or the debtor went bankrupt, to an authentication date before such time.306 However, Art. 9 UCC does not provide for a mechanism to ensure date certainty of the security document, so it does not prevent manipulation in respect of the attachment date. Under U.S. law, the requirements for authentication are not substantial, so it is fairly easy to antedate a security agreement.307 To ‘authenticate’ a security agreement means to ‘sign; or with present intent to adopt or accept a record, to attach to or logically associate with the record an electronic sound, symbol, or process.’308 ‘Record’, in turn, is defined as: ‘(…) information that is inscribed on a tangible medium or that is stored in an electronic or other medium and is retrievable in perceivable form.’309 In a nutshell, this means that authentication is no more than an inscription on a record.310 Consequently, an inscription on a Word document that is electronically stored on a USB stick would amount to ‘authentication’, and email, magnetic media, optical disks, digital voice messaging systems, audiotapes, photographic media and paper are also regarded as ‘records’.311 The fact that so much flexibility is given to the requirement of authentication means that the risk of antedating the security agreement is not prevented. This risk may manifest itself particularly in relation to attaching unsecured creditors or in bankruptcy.

306 Such manipulation is conceivable only if the debtor and the lender conspire with regard to adding secured collateral in a new (or the same) security agreement.
307 Authentication of the security agreement is the last of the three requirements for creation of an enforceable security interest. § 9-203(b)(3) UCC.
308 § 9-102(a)(7)(2010) UCC.
309 § 9-102(a)(70)(2010) UCC. In addition, Official Comment 9(a) to § 9-102(a)(70) UCC provides: “A “record” need not be permanent or indestructible, but the term does not include any oral or other communication that is not stored or preserved by any means. The information must be stored on paper or in some other medium. Information that has not been retained other than through human memory does not qualify as a record.”
310 In the Art. 9 (2001) UCC revision, the term ‘signed’ was replaced everywhere in the UCC by the medium-neutral term ‘authenticated’ and the term ‘writing’ was replaced by the medium-neutral term ‘record’. This can be seen as a reflection of Art. 9 UCC’s embracing of modern technology: besides the usual signing – which is in fact still by far the most common form of authenticating a security agreement – the debtor can arrange some other ‘authenticating’ event, such as an electronic communication. The 2010 amendments modified the definition of ‘authenticate’ to conform to definitions of other Articles in the UCC.
311 See Official Comment 9 to § 9-102 UCC.
According to LoPucki & Warren, parties can, and frequently do, fraudulently manufacture a security agreement after the fact.\footnote{LoPucki & Warren 2012 (Teacher’s Manual), p. 92.} This is not surprising in view of the fact that a simple Word document is sufficient and, moreover, Art. 9 UCC allows secured parties to keep the security agreement in their private files. In 2002 White & Summers wrote: “A service is now available to creditors and debtors that will enable the parties to record and later identify the true and only electronic copy of the agreement”. According to Mann, however, its use is not mandatory and the difficulties of verifying a non-signature authentication make its use still very uncommon.

3.2.2. Formal requirements for authentication

One way of looking at the ‘Filing Priority Principle’ is to recognize that although this rule may work fine among secured lenders only, it does represent a fundamental departure from the dogmatic prior tempore rule that is normally applied to determining the order of priority of security interests. After all, the ‘Filing Priority Principle’ does not link the order of priority to notification of security actually having been created, but merely to notification that security may at a future point in time be created, without even putting a time limit to the period within which such creation of security must have been completed. That this compromise comes at a price becomes particularly clear when it comes to considering the position of judicial lien creditors and bankruptcy, where for purposes of determining priority the UCC-rules revert to the traditional prior tempore-rules of the moment in time the filing lender has actually had the security created.

4. Conclusions

Whereas Chapter 5 aimed to unfold how the Art. 9 UCC notice filing system actually works, this chapter evaluated whether Art. 9 UCC offers an effective solution for the problems that exist in a non-public filing system, and if so, if it is likely to do so \textit{at a lower cost} than the parties investigated in this thesis incur in a non-public filing system.\footnote{See supra Chapter 1, subsection D.2.2.} The purpose of this evaluation was to provide insight into the benefits and cost of a U.S.-style filing system for parties that are somehow involved in or exposed to secured transactions. Not only may this assist the EU in making informed decisions about whether or not to adopt a European public notice filing system, it may also help to design the filing system as efficiently as possible. Let me start summarizing the research results with respect to the question to what extent the Art. 9 UCC filing system \textit{solves} the problems and mitigates risks that exist in relation to the investigated parties in the absence of publicity, \textit{i.e.} its alleged ‘effectiveness’.

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\footnote{LoPucki & Warren 2012 (Teacher’s Manual), p. 92.}

\footnote{See supra Chapter 1, subsection D.2.2.}
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4.1. Effectiveness (Yardstick I)

4.1.1. The risk of proprietary conflicts

The Art. 9 UCC approach to proprietary conflicts can be considered ‘effective’ in the sense that it gives first-in-time secured lenders and sellers the opportunity to file security rights or PMSIs in the Art. 9 UCC filing system. As a result of this opportunity, they can warn prospective third parties about the existence of their (conditional) security rights when the latter attempt to lend against, buy or seize the assets, thereby avoiding proprietary conflicts between these parties. But the avoidance of proprietary conflicts has not been given maximum effect under U.S. law. For instance, many U.S. states do not offer judicial lien creditors the possibility to file their judgment lien placed on the assets, leaving these judicial liens undiscoverable vis-à-vis prospective lenders or other parties. Also, most PMSIs will be untraceable until the moment they are filed, which can take up to 20 days after their ‘creation’.314 Furthermore, to the extent that proprietary interests are filed (timely), and hence are discoverable in theory, the Art. 9 UCC filing system has turned out not to be the gateway to ‘further information’ (concerning the status of the debtor's assets) for every type of creditor. Attaching unsecured creditors, for example, will not have the leverage to ask the debtor or secured parties to provide further details of any proprietary rights they purportedly hold. In practice, the only searchers that have such leverage are those that the debtor needs to keep its business running: in practice, lenders.315 As a result, and assuming that ‘third parties’ can only make informed decisions by establishing the exact scope of any proprietary rights they purportedly hold, Art. 9 UCC does not effectively prevent all types of proprietary conflicts.

4.1.2. The risk of fraudulent antedating

Under Art. 9 UCC, the risk of fraudulent antedating is only partly prevented. It is largely contained by the fact that security rights do not have third party effect until a notice of their existence has been filed in the public filing system. As a result, the moment from which a security right can be invoked against prospective third parties is objectively verifiable. In addition to being objectively verifiable, this moment cannot be manipulated in any way, given that entries in the filing system cannot be altered. This makes fraudulent antedating, or better put, manipulation of the order of priority, impossible. In addition to preventing fraudulent antedating, this first-to-file-or-perfect rule – constituting a so-called ‘pure race statute’ – quashes the incentive to commit such fraud in the context of proprietary conflicts between successive lenders. This is explained by the fact that this

314 In many cases, PMSIs might be untraceable for 19 days; see § 9-317(c) UCC. There are exceptions: vis-à-vis first-on-file lenders PMSIs on inventory will have the status of ‘super priority’, but only if the purchase money lender achieves perfection e.g. by filing before the debtor receives possession of the inventory collateral and the purchase money lender has notified the first-on-file lender that it has or expects to acquire a PMSI (§ 9-342(b)). See supra Chapter 5, subsection 4.3.2.

315 See supra footnote 193.
rule affords secured lenders the possibility to create a conditional superior interest in (part of) the debtor’s asset(s) by filing a financing statement with regard to the assets, even though the security interest has not yet attached. Hence, as long as the description of the collateral in the financing statement is formulated ‘broadly enough’, prospective lenders are ‘on notice’ of the fact that first-on-file lenders may attach a security interest (or several) at a later time or date. Consequently, ‘antedating’ is not a relevant concept when considered only in the context of achieving priority between successive secured lenders, which is solely determined by the order of filing (although the cynical view is that advance filing achieves nothing more than legitimizing fraudulent antedating). The order of filing does not take into account whether or not the security has actually been created. This may work well if imposed as a rule between secured lenders amongst themselves. It leads to complications when rights of others come into play. In the context of the priority conflicts between secured lenders and prospective judicial lien creditors and buyers outside the ordinary course, there is some room for antedating. A secured lender, for example, will only trump an unsecured creditor if the lender has filed a financing statement (or otherwise perfected the security interest) and the debtor has authenticated a security agreement, before the unsecured creditor obtains a lien with regard to the property. Hence, if the security agreement is signed after the unsecured creditor has levied upon the property, the secured lender will be subordinate to the enforcing lien creditor, despite the earlier filing. A similar principle applies to priority conflicts between secured lenders and subsequent buyers outside the ordinary course of business and in bankruptcy.316 It is thus not (only) the filing date, but (also) the date the security agreement is authenticated or the security has attached, as the case may be, that is decisive. For this reason, parties may be incentivized to manipulate the date of authentication or attachment to a time that is more convenient to them. Since authenticating and attachment are not a public matter, and the requirements for authentication are not substantial, there is room for this type of antedating.

4.2. Cost-efficiency (Yardstick II)

To the extent that Art. 9 UCC does prevent proprietary conflicts and fraudulent antedating, the Art. 9 UCC filing system is not very user-friendly. Although the filing and search fees are not substantial in relation to the average amount of a secured loan, parties involved in or exposed to secured transactions have to make considerable effort and incur significant cost in order to use or rely on the filing system. Most of the difficulties relate to searching under the debtor’s name and the fact that there is (still) no consistency between the varying search logics between filing offices in different states. This forces searchers and filers to use many possible name variants of the debtor’s name to identify

316 §§ 541, 558 BC.
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pre-existing security interests.317 In addition to the cumbersome process of determining (and searching under) the debtor’s correct name, it takes time and effort to sort out the false hits when names on the financing statements are similar.318 State-specific attempts to eliminate ambiguity in the debtor-name standard have led to even greater differences among states and thus to more ambiguity.319 Besides much filing and search activity, filers and searchers have suffered from much commercial uncertainty over the past decades, and they still do:

“As such, the uncertainty over a sufficient debtor name for purposes of filing a financing statement creates a critical breakdown in the notice-filing system for both UCC filers and UCC searchers.”320

But the process of making ‘further inquiry’ is also not easy. Identifying the right lender and having existing filings terminated proves to be cumbersome, time-consuming and costly in practice. Last but not least, the nature of the filing system entails that filers and searchers have to update and monitor information in financing statements in the filing system after the filing process has been completed to mitigate the risk of becoming unperfected. Both first-in-time and second-in-time creditors must, for example, continue to monitor whether there has been a change of name, whether there has been a relocation of the chief executive office from one state to another, whether the debtor has sold part of its collateral without permission etc. These are all obstacles to the prevention of proprietary conflicts in a manner that is cost-efficient for the parties concerned. Although an attempt to assess the exact amount of these costs falls outside the scope of this thesis, there is ample literature supporting the view that the costs of Article 9 filing are not trivial. In addition to many filing and search costs resulting from the need to make

317 Tu 2010, p. 109: “Differing search logic between filing offices in different jurisdictions compounds the uncertainty because broader search logic may return results that narrower search logic would fail to disclose.” Cf. Kettering 2012, pp. 915-918.
318 LoPucki 2007, p. 289.
319 See Tu 2010, p. 110 et seq. for an overview of these state-specific amendments.
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multiple filings, parties incur many litigation costs and insurance costs in their attempt to mitigate the above-mentioned risks.

Part III of this thesis will evaluate these research results in the light of a possible future European filing system. Mainly, it will consider the question: should we head towards the adoption of a European public notice filing system, and if so, to what extent should it differ from Art. 9 UCC?

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321 Tu 2010, p. 109: “(...) litigation often ensues between filers who believe they have complied with the sufficiency-of-a-debtor-name requirements and subsequent creditors who were unable to discover a previously recorded financing statement after searching the filing-office records.” Livingston 2011, p. 169: “Article 9 (...) has been the most frequently litigated and the most frequently revised of all the U.C.C. articles.” See also on p. 169: “Now, almost ten years later, the case law reveals that despite the many improvements in the 2001 revision, Article 9 still perplexes the courts in many ways.” Tu 2010, p. 109: “Instead of providing greater commercial certainty, revised Article 9 arguably facilitates a disconnect between filers and searchers by failing to provide adequate guidance on a sufficient debtor name. Because of this, the filing and search process breaks down and results in disputes instead of providing a clear and concise procedure for taking and giving notice of security interests.”

322 In this case, then, both searchers and filers are lenders. Cf. Harris, Kilborn & Sigman 2012, p. 488: “When you are dealing with searchers and filers, you do not have one group of secured parties that are searchers and one group of secured parties that are filers. Searchers and filers are essentially the same entities (...).”