

UCC Secured Transactions: Documenting and Perfecting Security Interests, Navigating Competing and Hidden Liens

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Why does it matter?

- Beat lien creditors
- Beat bankruptcy trustee
- Beat debtor in possession
- Beat other secured creditors
- Only as good as the weakest link



Does Article 9 apply to the transaction?

- Applies to all personal property
- Meaning of ‘security interest’ (§ 1-201(b)(35))
- Hidden secured transactions
 - o ‘Dirty’ leases (§ 1-203)
 - o ‘Sales’ transactions
- Consider taking protective measures, e.g., filing of financing statement (§ 9-505)



Sales of payment rights (§ 9-109(a)(3))

- Accounts
- Chattel paper
- Payment intangibles
- Promissory notes

Consignments (§ 9-109(a)(4))

- Consignment creates a ‘security interest’ (§ 1-201(b)(35))
- Consignor is ‘secured party’ (§ 9-102(a)(74))
- Consignee is ‘debtor’ (§ 9-102(a)(28))
- See purchase-money security interest discussion below



Exclusions

- Government debtors in some states (§ 9-109(c)(2))
- Consumer deposit accounts (§ 9-109(d)(13))




Basic building blocks

- Attachment
- Perfection
- Priority
- Security interest only as good as weakest link

Attachment (§ 9-203)

- Security agreement (§ 9-203(b)(3))
- Rights in the collateral (§ 9-203(B)(2))
- Give value (§ 9-203(b)(1))



Security agreement (§ 9-203(b)(3))

- Agreement that creates or provides for a security interest (§ 9-102(a)(73))
- In transactions covered by Article 9, includes:
 - o Consignment agreement
 - o Sales agreement



Oral security agreement?

- ‘Pursuant to debtor’s security agreement’
 - o Possession of tangible collateral (§ 9-203(b)(3)(B))
 - o Delivery (possession) of certificated security (§ 9-203(b)(3)(C))
 - o Control (§ 9-203(b)(3)(D))
 - Deposit accounts
 - Electronic chattel paper
 - Investment property
 - Letter-of-credit rights




Security agreement

- ‘Grant’ of security interest (§ 9-203(b)(3)(A))
- Consignment or sales language ‘creates or provides’ for ‘security interest’ in consignment and sales transactions




Description of collateral (§ 9-108)

- Must ‘reasonably identify’ the collateral
- May not use ‘all assets’ description in security agreement
- OK to describe collateral by ‘type’ or ‘category’
- Description by ‘type’ not sufficient in some circumstances:
 - o Commercial tort claims
 - o Consumer transaction involving consumer goods, securities entitlement, or securities account



Authentication (§§ 9-102(a)(7) and 9-203(b)(3)(A))

- Allows electronic ‘authentication’



Rights in the collateral or power to transfer (§ 9-203(b)(2))

- ‘Power’ to transfer
 - o Buyer with voidable title
 - o Consignee (if consignor not perfected)
 - o Seller of accounts, chattel paper, or instruments where buyer is not perfected (§ 9-318(b))
- Non-transferable property




Limitations on transferability of collateral

- Generally overridden in full for rights to payment (§ 9-406(d) and (f))
- For other kinds of rights, can create security interest, but cannot force counterparty to acknowledge rights of secured party (§ 9-408)


Give value (§ 9-203(b)(1))

- Meaning of ‘value’ (§ 1-204)
 - o ‘Any consideration sufficient to support a simple contract’
 - o Commitment to make a loan
- To whom?
 - o OK if value goes to third party, e.g., when security interest granted by guarantor and loan made to borrower



Supporting obligations + underlying collateral

- Security interest automatically created when security interest is created in:
 - Supported obligation (§ 9-203(f)) or
 - Secured obligation (§ 9-203(g))



Proceeds (§ 9-102(a)(64))

- Security interest in proceeds automatically attaches if security interest has attached to original collateral (§ 9-203(f))
- Security interest may ‘detach’ after 20 days if certain requirements are not met (§ 9-315)



After-acquired collateral

- Generally allowed (§ 9-204(a))
- Not permitted (§ 9-204(b)):
 - Commercial tort claims
 - Consumer goods, unless acquired within ten days of secured party giving value
- In security agreement should refer to ‘after-acquired’ collateral or the like (§ 9-108, Comment 3)



Future advances

- Security interest may secure future advances (§ 9-204(c))



Perfection (§§ 9-308 *et seq.*)

- Establishes rights against third parties:
 - o Lien creditors
 - o Trustee in bankruptcy
 - o Relevant to priority
- Does not exist unless attachment has occurred (§ 9-308(a))

Automatic perfection (§ 9-309)

- *Sales* (§ 9-309(3) + (4)):
 - o Promissory notes
 - Do not need possession
 - o Payment intangibles (§ 9-102(a)(61))
 - o Not automatic for *sales* of accounts or chattel paper
- May still be subject to non-temporal priority rules
- For non-filing, perfection and priority usually dates from date of perfection



Financing statement – when to use

- Available for all types of collateral (§ 9-310(a)), *except*:
 - o Money
 - o Deposit accounts
 - o Letter-of-credit rights
 - o Required federal or other state filings
- Sometimes subject to non-temporal priority rules



Financing statement – where to file

- File at location of debtor (§ 9-301(1))
- Fixture filing recorded in real property records where fixtures are located (§ 9-301(3)(A))


What is the 'location' of the debtor?

- 'Location' of debtor:
 - o Registered organization (corporation, LLC, LP): state of organization (§ 9-307(e))
 - New rules for certain business trusts
 - o Partnership: state of chief executive office (§ 9-307(b)(3))
 - o Individual: state of principal residence (§ 9-307(b)(1))
 - o Non-US entity: country of chief executive office, if country has filing system for the collateral (§ 9-307(c))



Financing statement – content (§ 9-502(a))

- Debtor name
- Secured party name
- ‘Indication’ of collateral



Financing statement – debtor name (§ 9-503)

- Must be exactly correct
- For registered organization: copy exactly from organizational documents
- Individuals
 - o What is the ‘name’?
 - o New rules discussed below

Financing statement – examples of mistakes

Debtor name	Mistaken financing statement
C. W. Mining Company	CW Mining Company
EDM Corporation	EDM Corporation d/b/a EDM Equipment
Michael Erwin	Mike Erwin
Terrance Joseph Kinderknecht	Terry J. Kinderknecht
Rodger House	Roger House
Michael Barry	Mike Barry
Andrew Fuell	Andrew Fuel
Silver Dollar, LLC	Silver Dollar Stores, LLC
Jim Ross Tires, Inc.	Jim Ross Tire Inc.



Financing statement: registered organization name

- Registered organization
 - o Confirm that must use name in actual organizational document ('public organic document')



Financing statement: individual's name

- Alternative A (waterfall) or Alternative B (safe harbor):
 - o Driver's license (or other state ID from same office) from state of filing
 - o 'Name'
 - o First personal name and surname
- No guidance on what is 'first personal name' and 'surname'
- California: likely to be either of:
 - o 'Name', or
 - o First personal name and surname



Financing statement – secured party's name

- OK to name 'representative' of secured party (§ 9-502(a)(2))
- Do not have to indicate representative status (§ 9-503(d))
- Less stringent rules as to getting secured party's name exactly right (§ 9-506, Comment 2)



Financing statement – 'indication' of collateral

- OK if would satisfy security agreement (§ 9-504(1))
- May use 'all assets' as 'indication' (§ 9-504(a)(2))



Financing statement – amendments

- Change name
- Change collateral
- Change other information
- Assign
- Terminate




Financing statement – post-closing events

- Change in debtor's name (§ 9-507(c))
- Debtor becomes located in different jurisdiction (§ 9-316(a)(2))
- Collateral transferred to a different debtor
 - o Same jurisdiction (§§ 9-315(a)(1) + 9-507(a))
 - o Different jurisdiction (§ 9-316(a)(3))



Possession (§ 9-313)

- Applies only to tangible collateral
- Through agent is OK (§ 9-313, Comment 3)
- Bailee (§ 9-313(c))
 - o Not effective unless bailee authenticates record (§ 9-102(a)(69)) that it has possession for ‘benefit of’ secured party
 - o Bailee may not be too ‘closely connected’ to debtor (§ 9-313, Comment 4)



Control (§ 9-312(b))

- Deposit accounts (§ 9-104)
- Investment property (§§ 9-106 + 8-106)
 - o Security entitlements
 - o Securities
 - o Securities accounts
- Letter-of-credit rights (§ 9-107)
- Electronic chattel paper (§ 9-105)



Methods of control

- Deposits accounts (§ 9-104) and securities accounts (§§ 8-106 + 9-106):
 - o Control agreement
 - Need for affirmantive agreement to listen to secured party
 - Effect of interpleader
 - o Secured party is customer of deposit account or entitlement holder of securities account
 - o Bank or securities intermediary is secured party



Compliance with other laws (§ 9-311)

- Certificate of title (§ 9-311(a)(2))
 - Cars
 - File financing statement for dealers with respect to inventory (seller or lessor of cars) (§ 9-311(d))
 - File financing statement if car dealer not in the business of selling cars (as well as leasing, if leasing is what it does) (§ 9-311(d))
- Airplanes (§ 9-311(a)(1))
 - FAA filing
 - UCC still applies to non-perfection issues
 - Capetown Convention
- Ships
- Railroad rolling stock



Federal law filing (§ 9-311(a)(1))?

- Copyright
 - File in Copyright Office for registered copyright and under UCC for unregistered copyrights
- Patents
 - File under UCC
 - Precautionary PTO filing (to beat buyers)?
- Trademarks
 - File under UCC



Supporting obligations and underlying collateral

- Security interest automatically perfected when security interest is perfected in supported obligation or secured obligation (§ 9-308(d) + (e))

➤ Proceeds – perfection

- Perfected if security interest in original collateral was perfected (§ 9-315(c))
- May lose perfection after 20 days if certain requirements are not met (§ 9-315(d))



Priority: other secured creditors

- First to file or perfect (§ 9-322(a)(1))
- OK to file before elements of attachment have occurred
- See non-temporal exceptions discussed below



Priority: Perfection by control

- Generally first to ‘obtain’ control (§§ 9-327(2) (deposit accounts) and 9-328(2) (securities account))
- See non-temporal exceptions discussed below




Perfection by possession

- First to 'perfect' if both secured parties perfected by possession (§ 9-322(a)(1))
- This means that possession without attachment is not sufficient to set priority because 'perfection' has not occurred yet



Non-temporal priorities

- Instruments (§ 9-330(d)):
 - o Possession plus other conditions
- Investment property
 - o Control (§ 9-328(1))
 - o Method of control
 - o Possession of certificated security (§ 9-328(5))
- Chattel paper (§ 9-330(b) + (c))
 - o Possession plus other conditions
- Deposit accounts (§ 9-327(1))
 - o Control
 - o Method of control



Purchase-money security interests (§ 9-324)

- Goods only (§ 9-103(a)(1))
- Inventory
 - Notice to earlier secured party before deliver (§ 9-324(b))
 - File before deliver (§ 9-324(b)(1))
 - Applies to consignments
- Equipment and no notice to earlier secured party (§ 9-324(a))
 - File within 20 days of delivery



Effect of other articles of UCC

- Article 3 (§ 9-331(a))
 - Holder in due course of negotiable instruments takes free of security interest (§ 3-306)
- Article 8 (§ 9-331(a) + (b))
 - Protected purchaser takes free of security interest and similar rules for security entitlements (§ 8-303(b))




Proceeds – priority (§ 9-322(b) – (e))

- Generally follow priority of original collateral
 - Financing statement for original collateral may give priority even if it does not refer to proceeds
- Special rules for non-temporal priority (§ 9-322(c))




Effect of other laws – ‘hidden’ liens – state law

- Landlord liens
- Warehouse and carrier liens (UCC Article 7)
- Non-UCC possessory liens (UCC § 9-333)
- Other liens arising by statute or common law that are not agricultural liens
 - *E.g.*, California Code of Civil Procedure § 690.020 (possible perfection of employee claims by lapsed financing statement)



Effect of other laws – ‘hidden’ liens – Federal law

- Perishable Agricultural Commodities Act (7 U.S.C. § 499a *et seq.*)
- Perishable Agricultural liens
- Fair Labor Standards Act (29 U.S.C. § 201 *et seq.*)
 - *Citicorp Indus. Credit v. Brock*, 483 U.S. 27 (1987) (secured party cannot move ‘hot goods’ across state lines)
- Tax liens
 - *In re Spearing Tool and Manufacturing Co., Inc.*, 412 F.3d 653 (6th Cir. 2005) (IRS lien filings do not have to follow Article 9 name rules)



‘Hidden’ liens – effect of other Article 9 provisions

- Proceeds rules (see above)
- Sale of payment intangibles (see above)
- M & A and related rules (see above)



Lien creditors against perfected secured party

- Generally perfected security interest has priority over later lien creditor (§ 9-201)
- Priority between lien creditor and unperfected security interest discussed below
- Future advances have priority over subsequent lien creditor if any of the following apply (§ 9-323(b)):
 - o Advance made within 45 days after person becomes a lien creditor
 - o Advance made without knowledge of lien of lien creditor, or
 - o Advance made ‘pursuant to commitment’



Certain transferees against perfected secured party

- Buyer in ordinary course of business takes free of earlier perfected security interest (§§ 9-320 + 1-201(b)(9))
- Lessee in ordinary course of business takes free of earlier perfected security interest (§ 9-321(c))
- Non-exclusive licensee in ordinary course of business takes free of earlier perfected security interest (§ 9-321(b))



Effect of unperfected security interest

- Security interest is ‘subordinate’ to lien creditor that becomes a ‘lien creditor’ before earlier of (§ 9-317(a)(2)):
 - o Perfection of security interest
 - o Financing statement filed and security agreement in place (even though value has not yet been given)
- Trustee in bankruptcy and debtor in possession have same rights (Bankruptcy Code § 544)



Effect of unperfected security interest

- Buyer of tangible collateral takes free if gives value and receives delivery without knowledge of security interest and before it is perfected (§ 9-317(b))
- Lessee of goods takes free if gives value and receives delivery without knowledge of security interest and before it is perfected (§ 9-317(c))
- Licensee of general intangible and buyers (not secured party) of intangibles take free if give value without knowledge of security interest and before it is perfected (§ 9-317(d))



Third-party rights

- Account debtor (§ 9-102(a)(3)) on payment obligation:
 - o Can recoup claims arising out of same contract or transaction (§ 9-404(a)(1))
 - o Can use set off rights that arise before account debtor notified of assignment (§ 9-404(a)(2))



Thank You

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