

## MEMORANDUM

TO: Joint Review Committee on UCC Article 9  
American Bankers Association Working Group on UCC Article 9

FROM: Steven L. Harris, Reporter

RE: Proposal Concerning Third Tier and Expiration of Debtor's Driver's License under  
"Only If" Rule

DATE: February 26, 2010

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As currently drafted, the "only if" rule for determining the name of an individual debtor has three tiers: (1) the name on the debtor's driver's license; (2) the name on the debtor's state-issued identification card; and (3) the debtor's name in a specified form. The Joint Review Committee's most recent teleconference (February 16, 2010) included an extended discussion about which form of name—surname, first name, and initial of first middle name, or surname, first name, and full first middle name—should be required for the third tier. The teleconference ended without a resolution of the issue.

Since that time several participants on the teleconference have discussed possible resolutions of the issue. This memorandum, which has benefitted greatly from these discussions, proposes that the Joint Review Committee adopt, for the third tier, the existing debtor-name requirement ("the individual name of the debtor") and provide a safe harbor for a financing statement that provides the debtor's name in a specified form. Under this approach, a person who files against someone without a driver's license or ID card issued by the relevant State would be guaranteed to have a form of name that will satisfy § 9-503 without disqualifying other filers who file under the debtor's correct name in a different form.

This memorandum also proposes that the safe-harbor form of name consist of the debtor's first name and surname. Recent Internet searches of records filed with the filing offices in Illinois, Massachusetts, New York, Ohio, and Oregon suggest that the vast proportion of financing statements filed against individual debtors do not include the debtor's full name. Eliminating the need to determine the debtor's second personal name would reduce uncertainty for the filer, particularly with respect to a married woman who uses her husband's surname. Even for the most common names, a search under the first name and surname is unlikely to disclose a significant number of false positives that cannot be readily determined to be such.

The suggested approach would have an additional benefit: It would address the concerns that have led some to advocate for special treatment of situations in which the debtor's driver's license expires before it is renewed or the driver's license is not renewed at all. A substantial part of the Joint Review Committee's most recent teleconference was devoted to the following scenario:

Debtor is an individual who operates a business as a sole proprietorship. Creditor extends credit to Debtor. The debt is secured by Debtor's existing and after-acquired inventory and accounts. The "only if" rule applies. In 2008, Creditor perfects by filing a financing statement that provides the Debtor's name as it appears on Debtor's then-current driver's license, which has an expiration date of April 1, 2010. April 1, 2010 comes and goes. Debtor neglects to renew the license, and Creditor takes no action with respect to the filed financing statement.

Under the "only if" rule in draft § 9-503(a), if the debtor has a current (i.e., unexpired) driver's license, the debtor's name would be the name on the license that was issued most recently. If the debtor does not have a current driver's license, the debtor's name would be determined under one of the other two tiers of the cascade. It follows from this rule that, absent additional statutory amendments, a financing statement providing the name on the debtor's then-current driver's license may become seriously misleading if:

- a. the license is renewed before expiration under a different name; or
- b. the license expires before renewal and the debtor's name under the lower tier is different.

Stated otherwise, if § 9-507 were left unamended, both the renewal of the driver's license before expiration and the expiration of the driver's license before renewal would potentially be a name change that causes the name on the filed financing statement to become seriously misleading.<sup>1</sup> Of course, even if the name change were to cause the financing statement to become seriously misleading, adverse consequences would follow only with respect to collateral that the debtor acquires more than four months after the name change. Despite the name change, the financing statement would remain effective with respect to collateral acquired by the debtor before the name change and within four months thereafter. See § 9-507.

Thus, the draft amendment to § 9-507, under which the expiration of the debtor's driver's license is not a potential name change, is an anomaly. The participants in the recent teleconference appeared comfortable taking the risk that a license renewal before expiration might cause the filed financing statement to become seriously misleading and that the secured party might not discover the name change until after the four-month period had expired. Some, however, expressed concern about the risk of suffering the identical consequences when expiration of the license precedes, rather than follows, renewal, or when the license is never renewed. They argued that treating expiration as a potential name change would create an intolerable risk in the relatively small number of cases where *all* of the following is the case: (1) the name on the expired driver's license does not satisfy the applicable lower-tier requirement (which most likely will be the third tier) for the debtor's name,

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<sup>1</sup> The word "potentially" reflects the possibilities that (1) the debtor's name under the second or third tier does not differ from the debtor's name on the filed financing statement and (2) even if the names are different, the difference may not cause the name on the financing statement to become seriously misleading. See § 9-506(c).

(2) the debtor does not renew the debtor's driver's license in the same name within four months after it expires, *and* (3) the debtor acquires collateral more than four months after the expiration.

The risks associated with treating expiration as a potential name change could be made even smaller if the name on the driver's license more frequently satisfied, or provided the basis for satisfying, the requirements for the third tier. A third tier that requires use of "the individual name of the debtor" but affords a safe harbor for a financing statement that provides the debtor's surname and first personal name is likely to accomplish this result. Under this approach, a secured party who is concerned that the current driver's license will expire before renewal can gain comfort either from (a) adding to the initial financing statement, as an additional debtor name, the safe-harbor name or (b) determining that the filing office's standard search logic for the safe harbor name will disclose the name on the debtor's driver's license (as it would, for example, if a search under "surname, first name" discloses filings under "surname, first name, middle initial" and "surname, first name, middle name" and the driver's license name accurately includes the debtor's first and last names as such.

In addition to addressing the expressed concerns, this approach would eliminate the need to amend § 9-507, either to specify what constitutes a potential name change or to add an extended period for certain types of name changes.

The value of part of this proposal is somewhat dependent on the standard search logic adopted by the filing offices. Recent Internet searches of records in New York, Massachusetts, Illinois, Ohio, and Oregon reveal that these offices have the capability of providing search results for "surname, first name" searches that include "surname, first name, middle initial" and "surname, first name, middle name" filings. If they are typical, then this approach would appear to have considerable value.

S. L. H.