ALTERNATIVE 1

BASIC RULE: LOCATION OF DEBTOR

SPECIAL RULE FOR POSSESSORY SECURITY INTERESTS

9-103. Perfection of Security Interest in Multiple State Transactions.

(a) Non-possessory security interest.

(1) This subsection applies to a non-possessory security interest in collateral other than goods covered by a certificate of title described in subsection (c), deposit accounts, investment property and minerals and related accounts described in subsection (e).

(2) Except as otherwise provided in this subsection, during the time that the debtor is located in a jurisdiction, perfection and the effect of perfection or non-perfection of a security interest in the collateral are governed by the law (but not the conflict-of-law rules) of that jurisdiction.

[(3) During the time that the debtor is located in a jurisdiction which is not a part of the United States, and which does not provide for perfection of the security interest by filing or recording in that jurisdiction, the law of the jurisdiction in the United States in which the debtor has its major executive office in the United States governs the perfection and the effect of perfection or non-perfection of the security interest through filing. In the alternative, if the debtor is located in a jurisdiction which is not a part of the United States or Canada and the collateral is accounts or general intangibles for money due or to become due, the security interest may be perfected by notification to the account debtor. As used in this paragraph, "United States" includes its territories and possessions and the Commonwealth of Puerto Rico.]1 We have proposed no changes to this subsection. We are soliciting input concerning cross- border transactions generally and may propose revisions to this subsection for consideration at a later meeting.

(4) A debtor shall be deemed located at the debtor's place of business if the debtor has only one, at the debtor's chief executive office if the debtor has more than one place of business, otherwise

at the debtor's residence. [If, however, the debtor is a foreign air carrier under the Federal Aviation Act of 1958, as amended, it shall be deemed located at the designated office of the agent upon whom service of process may be made on behalf of the foreign air carrier.]2 We have not addressed the bracketed second sentence.

(5) A security interest perfected under the law of the jurisdiction of the location of the debtor remains perfected until the expiration of four months after a change of the debtor's location to another jurisdiction, or until perfection would have ceased by the law of the first jurisdiction, whichever period first expires. If it becomes perfected under the law of the other jurisdiction before the end of that period, the security interest continues perfected thereafter. If it does not become perfected under the law of the other jurisdiction before the end of that period, the security interest becomes unperfected and is deemed to have been unperfected at all times prior thereto, but if insolvency proceedings are commenced by or against the debtor during the period, the security interest remains perfected until the insolvency proceedings are closed and thereafter for a period of sixty days.

(6) Insofar as it affects the priority of a security interest over a buyer of consumer goods (subsection (2) of Section 9-307), the period of the effectiveness of a filing made in the jurisdiction of the location of the debtor is governed by the rules with respect to perfection in paragraph (5).

(b) Possessory security interest.

(1) This subsection applies to a possessory security interest in collateral other than [goods covered by a certificate of title described in subsection (c) and]3 The Drafting Committee should clarify whether a security interest in goods covered by a certificate of title may be perfected by taking possession of the goods. We recommend that the Drafting Committee take up this issue at a later meeting, in conjunction with other issues concerning certificates of title. minerals described in subsection (e).

(2) Except as otherwise provided in this subsection, during the time that collateral is located in a jurisdiction, perfection and the effect of perfection or non-perfection of a security interest in the collateral are governed by the law (but not the conflict-of-law rules) of that jurisdiction.

(3) A security interest remains continuously perfected if (i) the collateral is located in one jurisdiction and subject to a security interest perfected under the law of that jurisdiction, (ii) thereafter the collateral is brought into another jurisdiction and (iii) upon entry into the other jurisdiction the security interest becomes perfected under the law of the other jurisdiction.

(c) Certificate of title.

[to be addressed in connection with other certificate of title issues]

(d) Deposit accounts.

[to be added, if necessary]

(e) Minerals.

[to be addressed in connection with other issues concerning oil, gas, and minerals]

(f) Investment property.

[see Article 8 Draft]

ALTERNATIVE 2

THE EXISTING SCHEME WITH CLARIFICATIONS AND IMPROVEMENTS

9-103. Perfection of Security Interest in Multiple State Transactions.

(a) Ordinary goods.

(1) This subsection applies to goods other than those covered by a certificate of title described in subsection (b), mobile goods described in subsection (c), and minerals described in subsection (e).

(2) Except as otherwise provided in this subsection, during the time that collateral is located in a jurisdiction, perfection and the effect of perfection or non-perfection of a security interest in the collateral are governed by the law of that jurisdiction.

(3) If the parties to a transaction creating a purchase money security interest in goods in one jurisdiction understand at the time that the security interest attaches that the goods will be kept in another jurisdiction, then the law of the other jurisdiction governs the perfection and the effect of perfection or non-perfection of the security interest from the time

-6-

it attaches until thirty days after the debtor receives possession of the goods and thereafter if the goods are taken to the other jurisdiction before the end of the thirty-day period.
(4) A security interest perfected under the law of the jurisdiction of the location of the collateral remains perfected until the expiration of four months after a change of the collateral's location to another jurisdiction, or until perfection would have ceased by the law of the first jurisdiction, whichever period first expires. If it becomes perfected under the law of the other jurisdiction before the end of that period, the security interest continues perfected thereafter. If it does not become perfected under the law of the other jurisdiction before the end of that period, the security interest becomes unperfected and is deemed to have been unperfected at all times prior thereto, but if insolvency proceedings are commenced by or against the debtor during the period, the security interest remains perfected until the insolvency proceedings are closed and thereafter for a period of sixty days.

(5) Insofar as it affects the priority of a security interest over a buyer of consumer goods (subsection (2) of Section 9-307), the period of the effectiveness of a filing made in the jurisdiction of the location of the collateral is governed by the rules with respect to perfection in paragraph (4).

(b) Certificate of title.

[to be addressed in connection with other certificate of title issues]

(c) Accounts, general intangibles and mobile goods.

(1) This subsection applies to accounts (other than an account described in subsection (5) on minerals) and general intangibles (other than uncertificated securities) and to goods which are mobile and which are of a type normally used in more than one jurisdiction, such as motor vehicles, trailers, rolling stock, airplanes, shipping containers, road building and construction machinery and commercial harvesting machinery and the like, if the goods are equipment or are inventory leased or held for lease by the debtor to others, and are not covered by a certificate of title described in subsection (b).

(2) Except as otherwise provided in this subsection, during the time that the debtor is located in a jurisdiction, perfection and the effect of perfection or non-perfection of a security interest in the collateral are governed by the law of that jurisdiction.

[(3) If, however, the debtor is located in a jurisdiction which is not a part of the United States, and which does not provide for perfection of the security interest by filing or recording in that jurisdiction, the law of the jurisdiction in the United States in which the debtor has its major executive office in the United States governs the perfection and the effect of perfection or non-perfection of the security interest through filing. In the alternative, if the debtor is located in a jurisdiction which is not a part of the United States or Canada and the collateral is accounts or general intangibles for money due or to become due, the security interest may be perfected by notification to the account debtor. As used in this paragraph, "United States" includes its territories and possessions and the Commonwealth of Puerto Rico.]4 We have proposed no changes to this subsection. See supra note 1.

(4) A debtor shall be deemed located at the debtor's place of business if the debtor has one, at the debtor's chief executive office if the debtor has more than one place of business, otherwise at the

debtor's residence. [If, however, the debtor is a foreign air carrier under the Federal Aviation Act of 1958, as amended, it shall be deemed located at the designated office of the agent upon whom service of process may be made on behalf of the foreign air carrier.]5 We have not addressed the bracketed second sentence.

(5) A security interest perfected under the law of the jurisdiction of the location of the debtor remains perfected until the expiration of four months after a change of the debtor's location to another jurisdiction, or until perfection would have ceased by the law of the first jurisdiction, whichever period first expires. If it becomes perfected under the law of the other jurisdiction before the end of that period, the security interest continues perfected thereafter. If it does not become perfected under the law of the other jurisdiction before the end of that period, the security interest becomes unperfected and is deemed to have been unperfected at all times prior thereto, but if insolvency proceedings are commenced by or against the debtor during the period, the security interest remains perfected until the insolvency proceedings are closed and thereafter for a period of sixty days.

(d) Chattel paper, documents and instruments.

The rules stated for ordinary goods in subsection (a) apply to a possessory security interest in chattel paper, documents and instruments. The rules stated for accounts in subsection (c) apply to a non-possessory security interest in chattel paper, documents and instruments, but the security interest may not be perfected by notification to the account debtor.

(e) Minerals.

[to be addressed in connection with other issues concerning oil, gas, and minerals]

(f) Investment property.

[see Article 8 Draft]

(g) Deposit accounts.

[to be added, if necessary]

Reporters' Explanatory Notes

1. The draft presents for the Drafting Committee's consideration alternative versions of certain provisions of 9-103. The provisions presented are those governing perfection and the effect of perfection or non-perfection of security interests in collateral other than goods covered by a certificate of title, deposit accounts, and minerals. Choice-of-law rules with respect to those types of collateral will be prepared in conjunction with the discussions of related issues. Inasmuch as the Article 8 Drafting Committee continues to work on special rules for uncertificated securities and other investment property, this draft does not address that topic.

2. The first alternative follows Recommendation 9.A. Subsection (a), which derives from existing subsection (3) (accounts, general intangibles, and mobile goods), provides that the law applicable to non-possessory security interests, both those perfected by filing and those perfected automatically, would be the law of the jurisdiction of the debtor's location. Under subsection (b), which derives from existing subsection (1) (documents, instruments and ordinary goods), the law applicable to possessory security interests would continue to be the law of the jurisdiction in which the collateral is located.

Proponents of the first alternative believe that its adoption would simplify the choice-of-law rules greatly (note the elimination of existing 9-103(1)(c) and (d), which concern non-possessory security interests in tangible collateral that is removed from one jurisdiction to the other), reduce the frequency of cases in which the governing law changes after a financing statement is properly filed (presumably, debtors change their own location less frequently than they change the location of their collateral), eliminate some difficult priority issues, eliminate the need to distinguish among "mobile" and "ordinary" goods, and reduce the number of filing offices in which secured parties must file or search. Opponents of this approach argue that determining the location of the debtor is a less certain enterprise than is generally assumed; that debtors who are approaching bankruptcy can be expected to relocate surreptitiously, thereby rendering security interests unperfected; that purchase-money equipment financers and others are likely to be ill-equipped to determine the debtor's location and the peculiar filing requirements of that jurisdiction without incurring significant additional costs; and that local interests may perceive the potential changes in the volume of filings to be so great that they may be motivated to oppose revision on this ground. In addition, all acknowledge the difficulties that would attend the transition from one set of choice-of-law rules to another. If the scope of revised Article 9 is expanded, as by including deposit accounts as original collateral, then the application of

choice-of-law rules during the transition will prove even more problematic. (Inasmuch as the Drafting Committee has not approved this alternative, even in principle, we have not attempted to draft a transition rule.)

3. The second alternative makes more modest changes. Among them are the elimination of the "last event" test and clarification and tolling of the "four-month" rule of 9-103(1)(d) (Recommendations 9.B, 9.D, and 9.E), which also are reflected in the first alternative.

4. If the Drafting Committee is inclined to adopt the first alternative, it may wish to move even closer to a unitary choice-of-law rule by eliminating location of the collateral as a factor in all cases, even when perfection is by possession. The bifurcation of non-possessory and possessory security interests creates the potential for the same jurisdiction to apply two different choice-of-law rules to determine perfection in the same collateral. This situation is not optimal. For example, under the draft, were a secured party in possession of an instrument or document to relinquish possession in reliance on temporary perfection, the applicable law immediately would change from that of the location of the collateral to that of the location of the debtor.

Particularly serious confusion may arise when the choice-of-law rules of a given jurisdiction result in each of two competing security interests in the same collateral being governed by a different priority rule. The potential for this confusion exists under existing 9-103 with respect to chattel paper: Perfection by possession is governed by the law of the location of the paper, whereas perfection by filing is governed by the law of the location of the debtor. Consider the mess that would be created if the language or interpretation of 9-308 were to differ in the two relevant states. If filing becomes a perfection option for instruments (see Recommendation 18.A), then the potential for this problem arising can be expected to increase.

Another difficult situation may arise when a secured party perfects both by taking possession in the state where the collateral is located (State A) and by filing in the state where the debtor is located (State B)--a common practice for some chattel paper financers. In that case, is the security interest a non-possessory one, a possessory one, or both non-possessory and possessory? What result if SP-1 takes possession in State A, SP-2 then files in State B, and SP-1 then files second in State B? Assuming both states follow the priority rule in existing 9-312(5), we would award priority to SP-1's security interest, which was perfected by possession before SP-2 filed or perfected. We fear, however, that a court may find itself in a quandary: If SP-1's security interest is possessory, then SP-1 would be entitled to priority under 9-312(5), as the first to perfect; but if SP-1's security interest is non-possessory, then SP-2 would be senior under the same section, as the first to file. One hopes that the court would not conclude that SP-1's subsequent filing operated to deprive SP-1 of its priority as the first to perfect. However, we suspect that any attempted clarification of this point in the statute would introduce undesirable complexity.

5. Recommendation 9.F encourages the Drafting Committee to consider whether the reference to the governing law should include the conflict-of-law rules. To see what is at stake, consider the following example: Litigation over the priority of a security interest in accounts arises in State X.

State X has adopted the official text of existing 9-103(3), which sends one to "the law (including the conflict of laws rules)" of the jurisdiction of the location of the debtor. The debtor is located in State Y. Had State Y also adopted the official text of 9-103, its choice-of-law rules would have been the same as State X's and would have indicated that the substantive law of State Y governs. But in fact State Y adopted a nonuniform provision, under which perfection is governed by the substantive law of the jurisdiction in which the debtor is located and under which the debtor is deemed located in its state of incorporation, State Z. Accordingly, perfection is to be accomplished by filing in State Z.

By eliminating the reference to the conflict-of-laws rules in the uniform version, a State X court would look only to the substantive law of State Y, which indicates that financing statements should be filed at one or more offices in State Y. This strikes many observers the desired result. Unfortunately, removing the reference to conflict-of-laws rules in the uniform version is not a complete solution. The problem arises from the enactment of a nonuniform version. If the identical perfection issue were to be litigated in State Y, the court would look to State Y's nonuniform 9-103 and conclude that the State Y filing is ineffective.

We see no way to eliminate this problem through revision of the uniform text. A complete solution would require complete uniformity. Nevertheless, the draft adopts what we believe to be the better approach: It eliminates the reference to the conflict-of-laws rules. We think this approach has two advantages. First, it is likely to minimize the impact of the nonuniformity. Under existing UCC 9-103(3), every time one of the uniform provisions refers one to State Y, one winds up having to file in State Z. Inasmuch as there have been relatively few nonuniform amendments to UCC 9-103, lawyers are likely to file in State Y without first checking State Y's conflict-of-laws rules. If the uniform text is revised to eliminate the reference to conflict-of-laws rules and the revised text is widely adopted, then these lawyers will have filed properly if the issue is litigated in any jurisdiction that has adopted a uniform UCC 9-103 (i.e., in most jurisdictions other than State Y). The burden now falls on the litigators to file the lawsuit in the "correct" place.

Second, suppose State Y's nonuniform 9-103 refers to the substantive and choice-of-law rules of State X. If so, State X's referral to State Y's choice-of-law rules would present the classic renvoi: State X's 9-103 says to look to State Y's choice of law, and State Y's 9-103 says to look to State X's choice of law. (The 1972 amendments to 9-103(3) created precisely this scenario with respect to security interests in accounts created by debtors whose chief executive offices were in a state that had the 1962 official text but whose records concerning the accounts were located in a state that had adopted the 1972 official text.) Eliminating either state's reference to conflict-of-laws rules would eliminate the renvoi.

6. Both alternatives depart somewhat from Recommendation 9.E. This recommendation deals with the effect of failing to reperfect within four months after the debtor's location changes. Rather than provide that a security interest whose perfection is not continued within the four-month period is deemed to have been unperfected as against all persons who acquired an

interest in the collateral after the change, the draft provides that such a security interest is deemed to have been unperfected as against all persons, whether they acquired an interest in the collateral before or after the change.

The following example illustrates the difference. SP-1 acquires a security interest in Debtor's accounts in 1991; SP-2 acquires a security interest in the same collateral in 1992. Both perfect by filing immediately upon attachment. Thereafter Debtor's location changes. SP-2 reperfects in the new jurisdiction within the four-month period, but SP-1 does not. Since SP-2 was not a purchaser after the change, neither existing 9-103(3)(e) nor recommendation 9.E would afford priority to SP-2. For several reasons, we would. First, to award priority to SP-2 would be consistent with 9-403(2), under which SP-1's failure to continue its financing statement would result in loss of priority. Second, to do so would eliminate the possibility of circular priorities. (Assume that SP-3 takes and perfects a security interest after the change. Under every scheme SP-2 would have priority over SP-3, who would have priority over SP-1. But under existing 9-103(3) and under the Recommendation SP-1 would be senior to SP-2.) Third, we think SP-2 is no less deserving than a judicial lien creditor who took its lien after the change and who would enjoy priority over SP-1. Finally, we note that, to the best of our recollections, the Study Committee did not focus on this point.