

D R A F T
FOR DISCUSSION ONLY

**REVISION OF UNIFORM COMMERCIAL CODE
ARTICLE 9 – SECURED TRANSACTIONS;
SALES OF ACCOUNTS AND CHATTEL PAPER**

NATIONAL CONFERENCE OF COMMISSIONERS
ON UNIFORM STATE LAWS

OCTOBER, 1997

WITH PREFATORY NOTE AND COMMENTS

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DRAFTING COMMITTEE TO REVISE
UNIFORM COMMERCIAL CODE ARTICLE 9 –
SECURED TRANSACTIONS; SALES OF ACCOUNTS AND CHATTEL PAPER

WILLIAM M. BURKE, 20th Floor, Standard Chartered Bank Building, 4 Des Voeux Road, Hong Kong, *Chair*
MARION W. BENFIELD, JR., Wake Forest University, School of Law, P.O. Box 7206, Winston-Salem, NC 27109
DALE G. HIGER, Suite 1015, One Capital Center, 999 Main Street, Boise, ID 83702
WILLIAM C. HILLMAN, U.S. Bankruptcy Court, Room 1101, 10 Causeway Street, Boston, MA 02222
MICHAEL HOUGHTON, P.O. Box 1347, 18th Floor, 1201 N. Market Street, Wilmington, DE 19899
RANDAL C. PICKER, University of Chicago Law School, 1111 E. 60th Street, Chicago, IL 60637
DONALD J. RAPSON, Room 3338, 650 CIT Drive, Livingston, NJ 07039, *The American Law Institute Representative*
HARRY C. SIGMAN, P.O. Box 67E08, Los Angeles, CA 90067, *The American Law Institute Representative*
BRADLEY Y. SMITH, 20th Floor, 450 Lexington Avenue, New York, NY 10017, *The American Law Institute Representative*
EDWIN E. SMITH, 21st Floor, 150 Federal Street, Boston, MA 02110
SANDRA S. STERN, 509 Madison Avenue, Suite 2004, New York, NY 10022
STEVEN L. HARRIS, Chicago-Kent College of Law, 565 W. Adams Street, Chicago, IL 60661-3691, *Co-Reporter*
CHARLES W. MOONEY, JR., University of Pennsylvania, School of Law, 3400 Chestnut Street, Philadelphia, PA 19104, *Co-Reporter*

EX OFFICIO

BION M. GREGORY, Office of Legislative Counsel, State Capitol, Suite 3021, Sacramento, CA 95814-4996, *President*
HENRY M. KITTLESON, P.O. Box 32092, 92 Lake Wire Drive, Lakeland, FL 33802, *Chair, Division E, National Conference*

EXECUTIVE DIRECTOR

FRED H. MILLER, University of Oklahoma, College of Law, 300 Timberdell Road, Norman, OK 73019, *Executive Director*
WILLIAM J. PIERCE, 1505 Roxbury Road, Ann Arbor, MI 48104, *Executive Director Emeritus*

Copies of this Act may be obtained from:

NATIONAL CONFERENCE OF COMMISSIONERS
ON UNIFORM STATE LAWS
676 North St. Clair Street, Suite 1700
Chicago, Illinois 60611
312/915-0195

**REVISION OF UNIFORM COMMERCIAL CODE
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SALES OF ACCOUNTS AND CHATTEL PAPER**

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1 **REVISION OF UNIFORM COMMERCIAL CODE**
2 **ARTICLE 9 – SECURED TRANSACTIONS;**
3 **SALES OF ACCOUNTS AND CHATTEL PAPER**

4 REPORTERS' INTRODUCTORY NOTE
5 OCTOBER, 1997, DRAFT

6 This draft reflects the Reporters' responses to a variety of issues that have
7 been raised during the NCCUSL Annual Meeting in Sacramento, by members of
8 the Drafting Committee, and by other interested persons. It is marked to reflect
9 changes from the Interim Draft dated August 7, 1997. Additions are underlined and
10 deletions appear in ~~strikeout~~. As part of an effort at "simplification, described
11 below, this draft divides many provisions of the prior draft into several paragraphs.
12 The resulting punctuation changes and paragraph designations (e.g., (1), (A), (i),
13 (I)) generally *are not marked*.

14 Steve Weise and Lou Del Duca provided us with extensive drafting
15 suggestions in a revised and "simplified" version of the 1997 Annual Meeting
16 Draft. We have taken many, but not all, of their suggestions. Most of the
17 suggestions related to structure and style. For example, they recommended much
18 more extensive use of paragraphs and subparagraphs. In deciding which
19 suggestions to accept, we relied on a host of factors, including our personal tastes,
20 NCCUSL style rules, and our desire to obtain Drafting Committee input before
21 undertaking some of the more extensive suggested revisions. We have addressed
22 the "simplification" suggestions in connection with each part of this draft except
23 Part 6. Time considerations prevented our consideration of that part. We will
24 address the suggestions relating to Part 6 in the next draft. The Drafting Committee
25 should consider whether the draft strikes the right balance, or has been
26 "oversimplified" or "undersimplified."

27 Many changes occasioned by the "simplification" effort caused cross-
28 references to become inaccurate. We have corrected some of the cross-references
29 in the text, but, given the time available, we have made little effort to correct the
30 Reporters' Comments. More generally, we have made only occasional changes to
31 the Comments, preferring instead to devote our time to the text.

32 The Reporters' Comments identify many of the substantive changes, often
33 following a heading designated "Change from Prior Draft." Please note, however,
34 that the numbered Comments reflect some changes that are not identified in the
35 "Change" paragraph. In particular, although we have completely rewritten much of
36 the text and comments addressing letters of credit, we have made no mention of
37 these revisions in the "Change" paragraph. Some substantive changes are not
38 discussed in the Comments at all. Thus, we urge the Drafting Committee members
39 not to ignore the blacklined text.

40 Some Reporters' Comments contain "Discussion Questions." As is the case
41 with "Changes," we have made no effort to include an exhaustive list of discussion
42 questions in the draft. The Tentative Agenda contains additional questions and
43 issues that the Drafting Committee may wish to discuss.

1
2
REPORTERS' PREFATORY COMMENTS
AND STATEMENT OF POLICY ISSUES

3
4
1. Background and History of Article 9 Revisions

5 In 1990, the Permanent Editorial Board for the Uniform Commercial Code
6 ("PEB"), with the support of its sponsors, the American Law Institute ("ALI") and
7 the National Conference of Commissioners on Uniform State Laws ("NCCUSL"),
8 established a committee ("Study Committee") to study Article 9 of the Uniform
9 Commercial Code ("UCC"). The PEB charged the Study Committee to consider
10 whether Article 9 and related provisions of the UCC are in need of revision. The
11 PEB also requested the Study Committee to recommend the nature and the
12 substance of any revisions that it thought desirable. The Study Committee issued
its report as of December 1, 1992 ("Report").

13 The principal recommendation of the Report called for the creation of a
14 drafting committee ("Drafting Committee") for the revision of Article 9. The
15 Report also recommended numerous specific changes to Article 9. The ALI and
16 NCCUSL acted favorably upon the Report's principal recommendation. The
17 Drafting Committee was organized in 1993.

18
19
2. Status and Schedule

20 The Drafting Committee has met eleven times (November, 1993; March,
21 1994; September-October, 1994; December, 1994; March, 1995; June, 1995;
22 December, 1995; March, 1996; June, 1996; November, 1996; March, 1997).
23 Meetings of the ALI Members Consultative Group on Article 9 were held on
24 December 16-17, 1994, November 17, 1995, and October 31, 1996. NCCUSL
25 considered the 1995 Annual Meeting Draft of revised Article 9 at its Annual
26 Meeting in August, 1995, the 1996 Annual Meeting Draft of revised Article 9 at its
27 Annual Meeting in July, 1996, and the 1997 Annual Meeting Draft of revised
28 Article 9 at its Annual Meeting in 1997. The ALI Council reviewed Council Draft
29 No. 1 (November 15, 1995) at its meeting on December 8, 1995, and reviewed
30 Council Draft No. 2 (November 15, 1996) at its meeting on December 13, 1996.
31 The Chair of the Drafting Committee and the Reporters made informational reports
32 to the membership of the ALI during its Annual Meetings in May, 1995, May,
33 1996, and May, 1997. Future meetings of the Drafting Committee are scheduled
34 for November, 1997, February, 1998, and (possibly) March, 1998. We expect the
35 Article 9 revisions to be substantially completed in 1997 and presented to the
sponsors for approval in 1998.

36
37
3. Reorganization and Renumbering

38 The 1996 NCCUSL Annual Meeting Draft was the last draft to follow the
39 organization and numbering of current Article 9. The drafts subsequent to the 1996
40 NCCUSL Annual Meeting, including this one, reflect a material reorganization and
41 renumbering. The restructuring was necessitated in part by the NCCUSL Style
42 Committee's conclusion that the earlier drafts contained sections that were too long
43 and included too many diverse provisions. (For example, Sections 9-312 and 9-402
of the 1996 Annual Meeting Draft each contained 17 subsections and Section 9-504

1 contained 19 subsections.) Accordingly, the number of sections has increased
2 substantially, requiring most sections to be renumbered. Since the reorganization
3 and renumbering first occurred, it became necessary to add a few sections. In order
4 to limit the number of substantial renumberings, the additional sections were
5 designated with an uppercase A (e.g., Section 9-308A). Some sections have been
6 deleted, as well. This usage is temporary and will not appear in the draft presented
7 for the second reading.

8 The reorganization achieves more than a reduction of the length and scope
9 of sections. It also arranges the substantive provisions in a more coherent structure
10 and order. New Subpart 1 of Part 1 contains the required “short title and the
11 definitions. Subpart 2 then addresses issues of scope and applicability. Part 2 is
12 divided into Subpart 1, provisions relating to the validity and attachment of security
13 interests, and Subpart 2, provisions that address various rights and duties of the
14 parties. Part 3 of this draft, like Part 3 of earlier drafts and of current Article 9,
15 deals with perfection and priority. Subpart 2 deals with perfection; Subpart 3,
16 priority. Subpart 4 covers certain rights of depositary institutions with respect to
17 deposit accounts. These subparts are preceded by Subpart 1, which contains the
18 choice-of-law rules applicable to those topics (formerly found in Section 9-103). A
19 new Part 4 covers other third-party issues. Part 5, dealing with filing, consists of
20 two subparts. Subpart 1 covers the filing rules, and Subpart 2 deals with the duties
21 and operation of the filing office. Finally, the former Part 5, dealing with default, is
22 Part 6 of this draft. It also is divided into two subparts. Subpart 1 addresses default
23 and enforcement generally, and Subpart 2 covers noncompliance with the
24 provisions of Article 9.

25 The coherent structure of this draft will make it easier for both practitioners
26 and judges to find and understand the rules. Of course, transition costs will
27 accompany the benefits of the changes. But, judging from the consistently
28 favorable responses we have received to the restructuring of Article 9, the benefits
29 will vastly outweigh the costs.

30 **4. Summary of Revisions**

31 We have deleted the summary of revisions from this draft. We plan to
32 update and revise it for the next draft.

33 **5. Style and Citation Conventions**

34 **a. Bracketed Text.**

35 The Drafting Committee has not reached a consensus on several matters,
36 some of which are reflected in the draft by statutory text that appears in brackets
37 and by bracketed alternative formulations. Contrary to the usual style for drafts of
38 Uniform Acts, the brackets in the draft do not necessarily indicate that the
39 provisions are optional or that the States are to choose one of the alternatives.
40 Brackets that do indicate optional or alternative text are noted in the draft or the
41 Reporters’ Comments. In some cases, the draft uses brackets to indicate
42 disagreement over style issues and notes the disagreement in the Reporters’
43 Comments.

1 **b. Minor Style Changes.**

2 A few sections have been changed to reflect NCCUSL’s currently
3 applicable style requirements, but have not been changed substantively. These
4 sections contain the following notation in their captions: *[MINOR STYLE*
5 *CHANGES ONLY]*.

6 **c. Reference to Current Law.**

7 The Reporters’ Comments refer to current Article 9 as “former Article 9.

8 **6. Statement of Policy Issues**

9 Following is a listing of some of the more important questions of policy
10 raised by the draft with respect to non-consumer secured transactions.

11 a. Should the revised Article 9 include additional provisions designed to
12 protect consumers? Are the new provisions included in the draft appropriate?

13 b. Should the revised Article 9 change the choice-of-law rule for perfection
14 to the location of the debtor? If so, should the location of the debtor be changed to
15 the jurisdiction where an individual debtor resides and where certain other debtors
16 are organized? Is the draft’s distinction between law governing perfection and law
17 governing priority appropriate?

18 c. Should the revised Article 9 include within its scope security interests in
19 deposit accounts as original collateral? Are the perfection and priority rules for
20 security interests in deposit accounts included in the draft appropriate?

21 d. Should the revised Article 9 include within its scope sales of payment
22 intangibles, i.e., general intangibles for money due or to become due? If so, should
23 the sales be automatically perfected?

24 e. Should the revised Article 9 include within its scope security interests in
25 existing, specifically described, commercial tort claims?

26 f. Should the revised Article 9 narrow the exclusion of security interests
27 created by governmental debtors?

28 g. Should the revised Article 9 include provisions governing the relative
29 priority of security interests and statutory liens? If so, are the draft provisions
30 appropriate?

31 h. Should the revised Article 9 include special rules for security interests in
32 instruments secured by real property mortgages?

33 i. Should the revised Article 9 adopt the “open drawer” policy, which limits
34 the discretion of filing offices to reject and delete filed records?

35 j. Should the revised Article 9 afford a nonjudicial means by which a debtor
36 can cause a disputed financing statement to become ineffective?

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7. Source Table

The following table lists the sections of the 1996 NCCUSL Annual Meeting Draft and the corresponding sections and subsections of the 1997 Annual Meeting Draft (which were in most respects the same as those in this draft). Note that the organization of the 1996 Annual Meeting Draft substantially followed that of the Official Text of Article 9.

	1996 Annual Meeting Draft	1997 Annual Meeting Draft
1		
2	§ 9-101. Short Title.	§ 9-101
3	§ 9-102. Scope of Article.	§ 9-112(a), (b)
4	§ 9-103. Multiple State Transactions.	
5	(a)(1)-(3) (non-possessory)	§ 9-301
6	(a)(4)-(5)	§ 9-307
7	(a)(6)	§ 9-314(a)
8	(b)(1)-(2) (possessory)	§ 9-301
9	(b)(3)-(4) (agricultural lien)	§ 9-302
10	(b)(5)	§ 9-314(b)
11	(c)(1)-(4) (cert. of title)	§ 9-303
12	(c)(5)	§ 9-314(c)
13	(c)(6)	§ 9-334
14	(d)(1)-(2) (deposit accounts)	§ 9-304
15	(d)(3)	§ 9-314(d)
16	(e) (minerals)	§ 9-301
17	(f) (investment property)	§ 9-305
18	§ 9-104. Exclusions.	§ 9-112(c)
19	§ 9-105. Definitions.	§ 9-102
20	§ 9-106. Definitions: “Account, etc.	§ 9-103
21	§ 9-107. Definitions: “PMSI, etc.	§ 9-104
22	§ 9-107A. Definitions: “PrMSI, etc.	§ 9-105
23	§ 9-108. Antecedent Debt.	[Deleted]
24	§ 9-109. Classification of Goods.	§ 9-106
25	§ 9-110. Sufficiency of Description.	§ 9-111
26	§ 9-111. Applicability of Article 6.	[Deleted]
27	§ 9-112. Collateral Owned by Nondebtor.	[Deleted]
28	§ 9-113. S/I Under Article 2 or 2A.	§ 9-116
29	§ 9-114. Rights of Consignee and	
30	Receivables Seller.	§ 9-315A

1	§ 9-115. Investment Property.	
2	(a) (definitions)	§ 9-107
3	(b) (attachment)	§ 9-203(e)
4	(perfection)	§ 9-308(e)
5	(c) (description)	§ 9-111(c)
6	(d)(1) (perfection by control)	§ 9-312
7	(d)(2) (perfection by filing)	§ 9-310(a)
8	(d)(3)-(4) (automatic perfection)	§ 9-308A(6)
9	(e) (priority)	§ 9-324
10	(f) (certificate in reg form)	
11	(attachment)	§ 9-203(a)
12	(perfection)	§ 9-311(a)
13	(priority)	§ 9-324
14	§ 9-116. Security Interest in Financial	
15	Asset.	§ 9-206
16	rules re: automatic perfection	§ 9-308A(5)
17	§ 9-117. “Control (Deposit Account).	
18	(a)-(b) (definition)	§ 9-109
19	(c) (no obligation to disclose)	§ 9-339
20	(d) (obligation to release)	§ 9-208
21	(e) (failure to release)	§ 9-624(d)
22	§ 9-118. “Control (Investment Property).	§ 9-108
23	§ 9-119. “Control (Letter of Credit).	§ 9-110
24	§ 9-201. General Validity.	§ 9-201
25	§ 9-202. Title to Collateral.	§ 9-202
26	§ 9-203. Attachment.	§ 9-203
27	(e) (conflict with other statute)	§ 9-115
28	§ 9-204. After-Acq’d Property; Future	

1	Adv.	§ 9-204
2	§ 9-205. Anti-Benedict v. Ratner.	§ 9-205
3	§ 9-206. Waiver of Defenses.	§ 9-403
4	§ 9-207. Collateral in SP's Possession.	§ 9-207
5	§ 9-208. Statement of Account.	§ 9-209
6	(b) (estoppel rule)	§ 9-624(f)
7	§ 9-209. SP/DI's Right of Set-Off.	§ 9-337(b)
8	§ 9-301. Unperfected S/I.	
9	(a)-(b) (basic priority rules)	§ 9-315
10	(d) (future advances)	§ 9-320(b)
11	§ 9-302. Perfection by Filing.	§ 9-309
12	automatic perfection	§ 9-308A
13	(c)-(d) (certificates of title; treaties)	§ 9-309A
14	§ 9-303. When Security Interest Is	
15	Perfected.	§ 9-308
16	§ 9-304. Perfection (Instr., Chattel Paper,	
17	etc.)	§ 9-310
18	§ 9-305. Perfection by Possession.	§ 9-311
19	§ 9-305A. Perfection by Control.	§ 9-312
20	§ 9-306. Proceeds.	§ 9-313
21	§ 9-307. Buyers of Goods.	
22	(a)-(c) (basic rules)	§ 9-316
23	(d) (future advances)	§ 9-320(c)
24	§ 9-308. Purchase of Chattel Paper	
25	and Instr.	§ 9-327
26	§ 9-308A. Transfer of Money and Funds.	§ 9-329
27	§ 9-309. Purchasers of Instrument, etc.	§ 9-328

1	§ 9-310. Liens Arising by Law.	§ 9-330
2	§ 9-311. Alienability of Debtor's Rights.	§ 9-401
3	§ 9-312. Conflicting Security Interest.	
4	(a), (m)-(n) (first-to-file rule)	§ 9-319
5	(b), (f), (l) (PrMSI)	§ 9-321
6	(k) (ag lien)	§ 9-319(c)
7	(c)-(e), (g) (PMSI)	§ 9-322
8	(h) (collateral transferred to 2d debtor)	§ 9-323
9	(i) (after-acquired property of new	
10	debtor)	§ 9-323A
11	(j) (deposit accounts)	§ 9-325
12	(o) (future advances)	§ 9-320(a)
13	(p) (letters of credit)	§ 9-326
14	§ 9-312A. Set-Off Against Deposit	
15	Account.	§ 9-337
16	§ 9-313. Fixtures.	
17	(a)-(g) (priority)	§ 9-331
18	(h) (enforcement)	§ 9-604(c)
19	§ 9-314. Accessions.	§ 9-332
20	§ 9-315. Commingled & Processed Goods.	§ 9-333
21	§ 9-316. Subordination.	§ 9-336
22	§ 9-317. SP Not Obligated on D's	
23	Contract.	§ 9-402
24	§ 9-318. Rights Acquired by Assignee.	§ 9-404
25	§ 9-318A. DI's Disposition of Funds.	§ 9-338
26	§ 9-318B. Restrictions on Assignment.	§ 9-406
27	§ 9-401. Place of Filing.	§ 9-501

1	§ 9-402. Financing Statement.	
2	(a)-(b), (m) (contents)	§ 9-502
3	(c)-(f) (name of debtor & secured	
4	party)	§ 9-503
5	(g) (indication of collateral)	§ 9-504
6	(h) (minor errors)	§ 9-506
7	(i)-(k) (name & other changes)	§ 9-507
8	(l) (amendment)	§ 9-509
9	(n)-(o) (authorization)	§ 9-508
10	(p) (remedy for violation of SP's duty)	§ 9-624(d)
11	§ 9-402A. New Debtor.	§ 9-510
12	§ 9-403. Filing.	
13	(a)-(b), (e), (g) (effectiveness)	§ 9-515
14	(c)-(d), (h)-(i) (refusal)	§ 9-521
15	(f) (incorrect "optional information)	§ 9-335
16	(j)-(k), (l) (2d & 3d sent.),	
17	(m) (duration and lapse)	§ 9-516
18	(l) (1st sent.) (continuation)	§ 9-517
19	(l) (last 3 sent.) (lapsed financing)	§ 9-522
20	(n)-(p) (indexing)	§ 9-520(a)-(c), (e)
21	(q)-(r) (indexing errors)	§ 9-518
22	§ 9-404. Termination Statement.	§ 9-511
23	(c) (remedy for violation)	§ 9-624(d)
24	§ 9-405. Assignment.	
25	(a)-(c) (how to)	§ 9-512
26	(d)-(e) (indexing)	§ 9-520(d), (e)
27	§ 9-406. Multiple Secured Parties.	§ 9-513

1	§ 9-406A. Successor of Secured Party.	§ 9-514
2	§ 9-407. Information From Filing Office.	§ 9-523
3	§ 9-408. Filing for Leases, etc.	§ 9-505
4	§ 9-409. Registered Agent.	§ 9-525
5	§ 9-410. Assignment of Functions.	§ 9-526
6	§ 9-411. Delay by Filing Office.	§ 9-524
7	§ 9-412. Fees.	§ 9-527
8	§ 9-413. Administrative Rules.	§ 9-528
9	§ 9-414. Duty to Report.	§ 9-529
10	§ 9-415. Claim re: Inaccurate Record.	§ 9-519
11	§ 9-501. Secured Party's Rights & Duties;	
12	Waiver, etc.	
13	(a)-(b), (h), (j) (rights & remedies)	§ 9-601
14	(c), (d) (waiver)	§ 9-602
15	(e) (standards re: duties)	§ 9-603
16	(f)-(g) (real estate)	§ 9-604
17	(i) (unknown debtor or secondary	
18	obligor)	§ 9-605
19	(k) (time of default for ag lien)	§ 9-606
20	§ 9-502. Collection and Enforcement.	
21	(a)-(d) (generally)	§ 9-607
22	(e), (g) (application of proceeds)	§ 9-608
23	(f) (jr's right to proceeds)	[Deleted]
24	§ 9-503. Right to Take Possession.	§ 9-609
25	§ 9-504. Disposition of Collateral.	
26	(a), (f) (general; commercial	
27	reasonableness)	§ 9-610

1	(b)-(e) (application of proceeds)	§ 9-614
2	(g)-(h) (whom to notify)	§ 9-611
3	(i) (waiver)	§ 9-623
4	(j) (timeliness of notice)	§ 9-612
5	(k)-(l) (contents of notice)	§ 9-613
6	(m) (pre-collection accounting)	[Deleted]
7	(n)-(o) (rights of transferee)	§ 9-615
8	(p) (rights of guarantor, etc.)	§ 9-616
9	(q) (title clearing)	§ 9-617
10	§ 9-504A. Limitation on Deficiency.	[Deleted]
11	§ 9-505. Acceptance of Collateral.	
12	(a)-(e), (k), (l) (general)	§ 9-618
13	(f)-(g) (notification)	§ 9-619
14	(h)-(i) (effect of acceptance)	§ 9-620
15	(j), (m) (waiver)	§ 9-623
16	§ 9-506. Redemption; Reinstatement.	
17	(a) (redemption)	§ 9-621
18	(b)-(e) (reinstatement)	§ 9-622
19	(f) (waiver)	§ 9-623
20	§ 9-507. Non-compliance with Part 5.	
21	(a)-(b), (g) (damages)	§ 9-624
22	(c) (deficiency actions)	§ 9-625
23	(d)-(f) (commercial reasonableness)	§ 9-626
24	(h) (attorney's fees)	§ 9-628
25	(i)-(k) (no liability)	§ 9-627

1 **REVISION OF UNIFORM COMMERCIAL CODE**
2 **ARTICLE 9 – SECURED TRANSACTIONS;**
3 **SALES OF ACCOUNTS AND CHATTEL PAPER**

4 **PART 1**
5 **GENERAL PROVISIONS**

6 [SUBPART 1. SHORT TITLE, DEFINITIONS, AND GENERAL CONCEPTS]

7 **SECTION 9-101. SHORT TITLE. *[MINOR STYLE CHANGES ONLY]***

8 This article may be cited as Uniform Commercial Code–Secured Transactions.

9 Reporters’ Comments

10 **Discussion Question:** Should the current title of the article should be
11 retained or modified? Three plausible modifications are (i) “Secured
12 Transactions, (ii) Secured Transactions; Sales of Accounts, Chattel Paper, and
13 Payment Intangibles; Consignments, and (ii) “Secured and Related Transactions.
14 Although none of these choices mention “statutory or “agricultural liens, as liens
15 they may be adequately captured by the reference to “secured transactions alone.

16 **SECTION 9-102. DEFINITIONS AND INDEX OF DEFINITIONS.**

17 (a) In this article [unless the context otherwise requires]:

18 (1) “Account debtor means a person obligated on an account, chattel
19 paper, [instrument other than a negotiable instrument,] or general intangible. The
20 term does not include a person obligated to pay a negotiable instrument even if the
21 instrument constitutes part of chattel paper.

22 (2) “Accounting means a record:

23 (A) authenticated by a secured party;

24 (B) ~~which indicates~~ indicating the aggregate unpaid secured
25 obligations as of a date not more than [] days earlier than the date of the record;
26 and

1 (C) ~~reasonably identifies~~ identifying the components of the
2 obligations in reasonable detail.

3 (3) “Agricultural lien” means a statutory lien in favor of a person that in
4 the ordinary course of its business furnishes goods or services to a debtor engaged
5 in a farming operation.

6 (~~4 3A~~) “As-extracted collateral” means:

7 (A) oil, gas, or other minerals;

8 (i) that are subject to a security interest that is created by a debtor
9 having an interest in the minerals before extraction; and

10 (ii) which attaches to the minerals as extracted; and

11 (B) accounts arising out of the sale at the wellhead or minehead of
12 [oil, gas, or other] minerals in which the debtor had an interest before extraction.

13 (~~5 4~~) “Authenticate” means to:

14 (A) sign; or

15 (B) execute or adopt a symbol, or encrypt a record in whole or in
16 part. with present intent to:

17 (i) identify the authenticating party;

18 (ii) adopt or accept a record or term; or

19 (iii) establish the authenticity of a record or term that contains
20 the authentication or to which a record containing the authentication refers.

21 (~~6 5~~) “Certificate of title” means a certificate of title with respect to
22 which a statute provides for the security interest in question to be indicated on the
23 certificate as a condition or result of the security interest’s obtaining priority over
24 the rights of a lien creditor with respect to the collateral.

25 (~~7 6~~) “Chattel paper” means a writing or writings that evidence both a
26 monetary obligation and a [purchase money] security interest in or a lease of

1 specific goods. The term does not include a charter or other contract involving the
2 use or hire of a vessel. If a transaction is evidenced both by a security agreement or
3 lease and by an instrument or series of instruments, the group of writings taken
4 together constitutes chattel paper.

5 (8 7) “Collateral means the property subject to a security interest or
6 statutory lien. The term includes:

7 (A) proceeds to which a security interest attaches under Section
8 9-313;

9 (B) proceeds as to which a statutory lien becomes effective; and

10 (C) accounts, chattel paper, and payment intangibles that have been
11 sold.

12 (9 8) “Commercial tort claim means a claim arising in tort if the claim
13 is generally assignable under applicable law and:

14 (A) the claimant is an organization; or

15 (B) the claimant is an individual and the claim:

16 (i) ~~the claim~~ arose in the course of the claimant’s business or
17 profession; and

18 (ii) does not include damages arising out of [bodily] [personal]
19 injury to or the death of an individual.

20 (10 9) “Communicate means to:

21 (A) send a written or other tangible record;

22 (B) transmit a record by any means agreed upon by the persons
23 sending and receiving the record, or

24 (C) in the case of transmission of a record to or by a filing office,
25 transmit a record by any means prescribed by the rules.

1 (11 9A) “Consignee means a merchant person to which goods are
2 delivered in a consignment.

3 (12 9B) “Consignment means a transaction, regardless of its form, in
4 which a person delivers goods to a merchant for the purpose of sale, and:

5 (A) ~~if~~ the merchant:

6 (i) deals in goods of that kind under a name other than the name
7 of the person making delivery;

8 (ii) is not an auctioneer; and

9 (iii) is not generally known by its creditors to be substantially
10 engaged in selling the goods of others;

11 ~~However, a transaction is not a “consignment if:~~

12 (B) the aggregate value of the goods is \$[1,000] or more ~~less~~ at the
13 time of delivery;

14 (C) the goods are not consumer goods immediately prior to delivery;
15 and

16 ~~the person to which the goods are delivered is an auctioneer or is~~
17 ~~generally known by its creditors to be substantially engaged in selling the goods of~~
18 ~~others; or~~

19 (D) the transaction does not create , ~~regardless of its form,~~ creates a
20 security interest that secures an obligation.

21 (13 9C) “Consignor means a person that delivers goods to a consignee
22 in a consignment.

23 (14 10) “Consumer debtor means a debtor in a consumer secured
24 transaction.

25 (15 11) “Consumer goods secured transaction means a transaction in
26 which:

1 (A) an individual incurs an obligation primarily for personal, family,
2 or household purposes; and

3 (B) a security interest in consumer goods secures the obligation.

4 (16 +2) “Consumer obligor means an obligor who is an individual and
5 who incurred the obligation as part of a transaction entered into primarily for
6 personal, family, or household purposes.

7 (17 +3) “Consumer secured transaction means a transaction in which:

8 (A) an individual incurs an obligation primarily for personal, family,
9 or household purposes;

10 (B) a security interest secures the obligation; and

11 (C) the collateral is held or acquired primarily for personal, family,
12 or household purposes.

13 (18 +4) “Debtor means:

14 (A) a person that has a property interest, other than a security interest
15 or other lien, in the collateral, whether or not the person is an obligor;

16 (B) a seller of accounts, chattel paper, or payment intangibles; [and]
17 [or]

18 (C) a consignee.

19 (19 +5) “Deposit account means a demand, time, savings, passbook, or
20 like account maintained with a depository institution. The term does not include
21 investment property or an account evidenced by an instrument.

22 (20 +6) “Depository institution means an organization that is engaged
23 in the business of banking. The term includes a bank, savings bank, savings and
24 loan association, credit union, and trust company.

25 (21 +7) “Document means a document of title or a receipt of the type
26 described in Section 7-201(2).

1 (22 18) “Encumbrance includes a real property mortgage, other lien on
2 real property, and any other right in real property other than an ownership interest.

3 (23 19) “Filing office means an office designated in Section 9-501 as
4 the place to file a financing statement. [The term includes the filing officer and
5 other personnel of the office.]

6 (24 20) “Financing statement means an initial financing statement and
7 any record on file relating to the initial financing statement.

8 (25 21)(A) “Fixture filing means a filing ~~in the office where a~~
9 ~~mortgage on the real property [is] [would be] filed or recorded~~ of a financing
10 statement:

11 (i) covering goods that are or are to become fixtures; and

12 (ii) ~~which satisfies~~ satisfying the requirements of Section
13 9-502(a).

14 (B) The term includes a filing of financing statement covering
15 goods of a transmitting utility which are or are to become fixtures.

16 (26 22) “Fixtures means goods that have become so related to
17 particular real property that an interest in them arises under real property law.

18 (27 23) “Good faith means honesty in fact and the observance of
19 reasonable commercial standards of fair dealing.

20 (28 24)(A) “Goods means ~~includes~~ all things that are movable when a
21 security interest attaches, including:

22 (i) fixtures;

23 (ii) standing timber that is to be cut and removed under a
24 conveyance or contract for sale;

25 (iii) the unborn young of animals; and

1 (iv) crops grown, growing, or to be grown, including crops
2 produced on trees, vines, and bushes.

3 (B) The term does not include accounts, chattel paper, deposit
4 accounts, documents, general intangibles, instruments, investment property, letters
5 of credit, money, or ~~commercial tort claims~~, and oil, gas, or ~~and~~ other minerals
6 before extraction.

7 (29 25) “Governmental entity means:

8 ~~(A) the United States, a State, a foreign nation, country, or a~~
9 governmental unit.

10 ~~(B) a governmental subdivision, agency, department, commission,~~
11 ~~board, authority, instrumentality, public benefit corporation, or other governmental~~
12 ~~unit of the United States, a State, or a foreign country.~~

13 (30) (A) “Governmental unit means a subdivision, agency,
14 department, county, parish, municipality, or other unit of the government of the
15 United States, a State, or a foreign nation.

16 (B) The term does not include an [governmental] organization with
17 a separate corporate existence, even if its name includes “authority, “board, or the
18 like.

19 (31 26)(A) “Instrument means:

20 (i) a negotiable instrument; or

21 (ii) any other writing that:

22 (I) evidences a right to the payment of money; ~~and~~

23 (II) is not itself a security agreement or lease; and

24 (III) is of a type that in ordinary course of business is
25 transferred by delivery with any necessary indorsement or assignment.

26 (B) The term does not include:

- 1 (i) investment property; or
2 (ii) a writing that evidences a right to payment arising out of the
3 use of a credit or charge card or information contained on or for use with the card.

4 (32) “Letter-of-credit rights means the rights to payment and
5 performance under a letter of credit. The term does not include the right of a
6 beneficiary to demand payment or performance under a letter of credit.

7 (33 27) “Lien creditor means a creditor that has acquired a lien on the
8 property involved by attachment, levy, or the like. The term includes:

9 (A) an assignee for benefit of creditors from the time of assignment;

10 (B) a trustee in bankruptcy from the date of the filing of the petition;

11 and

12 (C) a receiver in equity from the time of appointment.

13 (34 28) “Manufactured home [has the meaning specified in title 42,
14 section 5402(6), of the United States Code means [to come]].

15 (35 29) “Manufactured home transaction means a secured transaction:

16 (A) ~~in which~~ that creates a purchase money security interest in the
17 ~~collateral includes a manufactured home; or~~

18 (B) in which a manufactured home is the primary collateral.

19 (36 30) “Mortgage means a consensual interest in real property,
20 including fixtures, created by a real property mortgage, a trust deed on real
21 property, or the like.

22 (37 31) “New debtor means a person that becomes bound as debtor
23 under Section 9-203(c) by a security agreement previously entered into by another
24 person.

25 (38 32)(A) “New value means:

26 (i) money; or

1 (ii) money's worth in property, services, or new credit; or
2 (iii) release by a transferee of an interest in property previously
3 transferred to the transferee.

4 (B) The term does not include an obligation substituted for another
5 obligation.

6 (39 33)(A) "Obligor means a person that, with respect to an obligation
7 secured by a security interest in or a statutory lien on the collateral,

8 (i) owes payment or other performance of the obligation;

9 (ii) has provided property other than the collateral to secure
10 payment or other performance of the obligation; or

11 (iii) is otherwise accountable in whole or in part for payment or
12 other performance of the an obligation secured by a security interest in or a
13 statutory lien on the collateral.

14 (B) The term does not include an issuer or a nominated person
15 under ~~[with respect to]~~ ~~[of]~~ a letter of credit.

16 (40 34) "Original debtor means a person that, as debtor, entered into a
17 security agreement to which a new debtor has become bound under Section
18 9-203(c).

19 ~~(35) "Public finance transaction means [to come].~~

20 **Alternative A**

21 (41) "Public finance transaction means a secured transaction in which
22 the debtor, the obligor, the secured party, the account debtor or other person
23 obligated on collateral, the assignor or assignee of a secured obligation, or the
24 assignor or assignee of a security interest is a State or a governmental unit of a
25 State.

26 **Alternative B**

1 (41) “Public finance transaction means a secured transaction in which
2 the collateral directly or indirectly supports [the issuer’s] obligations on securities
3 [and] [if] the issuer is a State or a governmental unit of a State.

4 (42 36) “Pursuant to commitment, with respect to an advance made or
5 other value given by a secured party, means pursuant to the secured party’s
6 obligation, whether or not a subsequent event of default or other event not within
7 the secured party's control has relieved or may relieve the secured party from its
8 obligation.

9 (43 37) “Record means information that is inscribed on a tangible
10 medium or that is stored in an electronic or other medium and is retrievable in
11 perceivable form.

12 [(44 38) “Registered agent means a registered agent of a debtor
13 designated under Section 9-525.]

14 (45 39) “Registered entity means an organization organized under the
15 law of a State or the United States and as to which the State or the United States
16 maintains a public record showing the organization to have been organized.

17 (46 40) “Rule means a rule adopted pursuant to Section 9-528.

18 (47 41) “Secondary obligor means an obligor any portion of whose
19 obligation is secondary.

20 (48 42) “Secured party means a person that holds a security interest or
21 a statutory lien. The term includes:

22 (A) a consignor;

23 (B) ~~and~~ a person to which accounts, chattel paper, or payment
24 intangibles have been sold; and

1 (C) ~~If~~ if a security interest [or statutory lien] is created in favor of a
2 trustee, indenture trustee, agent, collateral agent, or other representative, the
3 representative is the secured party.

4 [(49 43) “Secured party of record means a person stated to be the
5 secured party or a representative of the secured party in a financing statement that
6 has been filed with the filing office.]

7 (50 44) “Security agreement means an agreement that creates or
8 provides for a security interest.

9 (51 45) “State means:

10 (A) a State of the United States;

11 (B) the District of Columbia;

12 (C) the Commonwealth of Puerto Rico;

13 (D) the United States Virgin Islands; and or

14 (E) any territory or insular possession subject to the jurisdiction of
15 the United States.

16 (52 46) “State of organization, with respect to a registered entity,
17 means the State jurisdiction under whose law the entity is organized.

18 (53 47)(A) “Statutory lien means an interest in personal property:

19 (i) which secures payment or performance of an obligation;

20 (ii) which is created by statute [in favor of a person that in the
21 ordinary course of its business furnishes goods or services]; and

22 (iii) ~~[whose effectiveness]~~ [the effectiveness of which] does not
23 depend on the person’s possession of the personal property.

24 (B) The term does not include a security interest.

25 (54 48) “Support obligation means a secondary obligation or letter-of-
26 credit rights that support ~~supports~~ the payment or performance of an account,

1 chattel paper, general intangible, document, [insurance policy,] instrument, or
2 investment property.

3 (55 49) “Transmitting utility means a person primarily engaged in the
4 business of:

5 (A) operating a railroad, subway, street railway, or trolley bus;

6 (B) transmitting electric or electronic communications;

7 (C) transmitting goods by pipeline or sewer; or

8 (D) transmitting or producing and transmitting electricity, steam,
9 gas, or water.

10 (b) Other definitions applying to this article and the sections in which they
11 appear are:

12 “Account Section 9-103.

13 “Applicant Section 5-102.

14 “Attach Section 9-203.

15 “Becomes Bound Section 9-203.

16 “Beneficiary Section 5-102.

17 “Cash proceeds Section 9-313.

18 “Commodity account Section 9-107.

19 “Commodity contract Section 9-107.

20 “Commodity customer Section 9-107.

21 “Commodity intermediary Section 9-107.

22 “Construction mortgage Section 9-331.

23 “Consumer goods Section 9-106.

24 “Control (deposit account) Section 9-109.

25 “Control (investment property) Section 9-108.

26 “Control (letter-of-credit rights) Section 9-110.

1	“Crops	Section 9-106.
2	“Equipment	Section 9-106.
3	“Farm products	Section 9-106.
4	“General intangibles	Section 9-103.
5	“Inventory	Section 9-106.
6	“Investment property	Section 9-107.
7	“Issuer	Section 5-102.
8	“Livestock	Section 9-106.
9	“Nominated Person	Section 5-102.
10	“Noncash proceeds	Section 9-313.
11	“Payment intangible	Section 9-103.
12	“Proceeds	Section 9-313.
13	[“Production money crops	Section 9-105.]
14	[“Production money obligation	Section 9-105.]
15	[“Production money security interest	Section 9-105.]
16	[Production of crops	Section 9-105.]
17	“Purchase money security interest	Section 9-104.
18	“Purchase money collateral	Section 9-104.
19	“Purchase money obligation	Section 9-104.
20	“Request for an accounting	Section 9-209.
21	“Request regarding a list of collateral	Section 9-209.
22	“Request regarding a statement of	
23	account	Section 9-209.
24	“Transfer statement	Section 9-617.
25	(c) The following definitions in other articles apply to this article:	
26	“Broker	Section 8-102.

1	“Certificated security	Section 8-102.
2	“Check	Section 3-104.
3	“Clearing corporation	Section 8-102.
4	“Contract for sale	Section 2-106.
5	“Customer	Section 4-104.
6	“Delivery	Section 8-301.
7	“Entitlement holder	Section 8-102.
8	“Financial asset	Section 8-102.
9	“Holder in due course	Section 3-302.
10	“Issuer	Section 5-102.
11	“Lease	Section 2A-103.
12	“Lease agreement	Section 2A-103.
13	“Lease contract	Section 2A-103.
14	“Leasehold interest	Section 2A-103.
15	“Lessee	Section 2A-103.
16	“Lessee in ordinary course of business	Section 2A-103.
17	“Lessor	Section 2A-103.
18	“Lessor’s residual interest	Section 2A-103.
19	“Letter of credit	Section 5-102.
20	“Negotiable instrument	Section 3-104.
21	“Nominated person	Section 5-102.
22	“Note	Section 3-104.
23	“Proceeds of a letter of credit	Section 5-114.
24	“Prove	Section 3-103.
25	“Sale	Section 2-106.
26	“Securities intermediary	Section 8-102.

1	“Security	Section 8-102.
2	“Security certificate	Section 8-102.
3	“Security entitlement	Section 8-102.
4	“Uncertificated security	Section 8-102.

5 (d) Article 1 contains general definitions and principles of construction and
6 interpretation applicable throughout this article.

7 *Legislative Note: States that do not enact Sections 9-105 and 9-321 should delete*
8 *the bracketed definitions in subsection (b).*

9 Reporters’ Comments

10 **Changes from Prior Draft:**

11 A. The filing office has been removed from the definition of “fixture
12 filing. We think it implicit that “perfected by a fixture filing (as in § 9-331)
13 means a filing a proper financing statement (in the form described in the definition)
14 with the right office (as determined by § 9-501).

15 B. New definitions of “governmental entity, “governmental unit,
16 “manufactured home, “manufactured home transaction, and “public finance
17 transaction.

18 C. The definition of “registered entity has been revised. The change is
19 intended to affect primarily the rules determining the debtor’s location for choice-
20 of-law purposes (§ 9-307).

21 D. Changes to the definition of “consignment are attempts to clarify.

22 **Discussion Questions:**

23 A. Should the definition of “chattel paper be limited to obligations
24 secured by a purchase money security interest? If not, should the applicability of
25 the special priority rule in Section 9-327 be limited to those obligations?

26 B. Are the new definitions of “manufactured home, “manufactured
27 housing transaction, and “public finance transaction. satisfactory? See Reporters’
28 Comment 15 for other approaches to the definition of “manufactured home.

29 1. **Source.** Many definitions derive from those in former Section 9-105;
30 others are new.

31 2. **“Account Debtor.”** As a general matter, Article 3, and not Article 9,
32 governs obligations on negotiable instruments. Accordingly, the definition in a
33 prior draft has been revised to exclude from the “account debtor category obligors
34 on negotiable instruments constituting part of chattel paper. The principal effect of
35 this change is that Sections 9-403 and 9-404, dealing with the rights of an assignee,

do not apply to an assignee of chattel paper in which the obligation to pay is evidenced by a negotiable instrument. Rather, the assignee's rights are governed by Article 3. The bracketed language would have the effect of subjecting the rights of an assignee of a non-negotiable instrument to Sections 9-403 and 9-404. It is discussed in the Comments to Section 9-404.

3. **"Agricultural Lien."** This term is new. The definition accommodates the inclusion of agricultural liens within the scope of Article 9. An agricultural lien is a "statutory lien.

3A. **"As-extracted Collateral."** Under this Article, oil, gas, and other minerals that have not been extracted from the ground are treated as real property, to which this Article does not apply. Upon extraction, minerals become personal property and eligible to be collateral under this Article. See the definition of "goods," which excludes "oil, gas, and other minerals before extraction. To take account of financing practices reflecting the shift from real to personal property, this Article contains special rules for perfecting security interests in minerals which attach upon extraction and in accounts resulting from the sale of minerals at the wellhead or minehead. See Sections 9-301(6) (law governing perfection and priority); 9-501 (place of filing); 9-502 (contents of financing statement); 9-520 (indexing of records). The new term, "as-extracted collateral," refers to the minerals and related accounts to which the special rules apply.

The following examples explain how these definitions work:

Example 1: Debtor owns an interest in oil that is to be extracted. To secure Debtor's obligations to Lender, Debtor enters into an authenticated agreement granting Lender an interest in the oil. Although Lender may acquire an interest in the oil under other law, Lender does not acquire a security interest under this Article until the oil becomes personal property, i.e., until it is extracted and becomes "goods" to which this Article applies. Because the debtor had an interest in the oil before extraction and Lender's security interest attached to the oil as extracted, the oil is "as-extracted collateral.

Example 2: Debtor owns an interest in oil that is to be extracted and contracts to sell the oil to Buyer at the wellhead. In an authenticated agreement, Debtor agrees to sell to Lender the right to payment from Buyer. This right to payment is an account that constitutes "as-extracted collateral. If Lender then resells the account to Financer, Financer's acquires a security interest. However, inasmuch as the debtor-seller in that transaction, Lender, had no interest in the oil before extraction, Financer's collateral (the account it owns) is not "as-extracted collateral.

Example 3: Under the facts of Example 2, before extraction, Buyer grants a security interest in the oil to Bank. Although Bank's security interest attaches when the oil is extracted, Bank's security interest is not in "as-extracted collateral, inasmuch as its debtor, Buyer, did not have an interest in the oil before extraction.

4. **"Authenticate."** This definition is new. It replaces and broadens the former definition of "sign" to encompass authentication of all records, not just writings.

1 5. **“Collateral.”** The revised definition of “collateral” includes property
2 subject to a statutory lien. It also makes clear that “collateral” includes proceeds.

3 6. **“Commercial Tort Claim.”** This term is new. Only commercial tort
4 claims may serve as collateral under this Article. See Section 9-112(c)(15).

5 7. **“Communicate.”** The definition of “communicate” includes the act of
6 transmitting both tangible and intangible records.

7 7A. **“Consignment.”** The definition of “consignment” is drawn in part
8 from the October 1, 1995, draft of Article 2. The definition excludes, in paragraphs
9 (A), (B), and (C), transactions for which filing would be inappropriate or of
10 insufficient benefit to justify the costs. The definition also excludes, in paragraph
11 (D), what have been called “consignments intended for security. These
12 “consignments” are not bailments but secured transactions. Accordingly, all of
13 Article 9 should apply to them. The Official Comments could afford guidance in
14 distinguishing between true and security consignments.

15 8. **Consumer-related Definitions.** The definitions of “consumer debtor,
16 “consumer obligor,” “consumer goods secured transaction,” and “consumer secured
17 transaction” have been added in connection with various new (and old) consumer-
18 protection rules. For the most part, the rules appear in Part 6 and apply to
19 “consumer goods secured transactions,” i.e., to consumer transactions in which the
20 some or all of the collateral consists of consumer goods. However, certain rules
21 apply to consumer secured transactions, in which the collateral may be of any type.
22 See, e.g., Sections 9-111(d); 9-112(b)(17).

23 9. **“Debtor”; “Obligor”; “Secondary Obligor.”** Determining whether a
24 person is a “debtor” under the definition in former Section 9-105(1)(d) requires a
25 close examination of the context in which the word is used. To reduce the need for
26 this examination, this Article redefines “debtor” and adds new defined terms,
27 “secondary obligor” and “obligor.” In the context of Part 6, these definitions
28 distinguish among three classes of persons: (1) those persons who may have a
29 stake in the proper enforcement of a security interest by virtue of their non-lien
30 property interest (typically, an ownership interest) in the collateral, (2) those
31 persons who may have a stake in the proper enforcement of the security interest
32 because of their obligation to pay the secured debt, and (3) those persons who have
33 an obligation to pay the secured debt but have no stake in the proper enforcement of
34 the security interest. Persons in the first class are debtors. Persons in the second
35 class are secondary obligors if any portion of the obligation is secondary. One must
36 consult the law of suretyship to determine whether an obligation is secondary. The
37 Restatement (3d), Suretyship and Guaranty § 1 (1996), contains a useful
38 explanation of the concept. Persons in the third class are neither debtors nor
39 secondary obligors.

40 The revised definition of “debtor” renders unnecessary former Section
41 9-112, governing situations in which collateral is not owned by the debtor.

42 As revised, the definition of “debtor” includes a “consignee,” as defined in
43 this section.

1 The definition of “debtor” includes transferees of collateral, whether or not
2 the secured party knows of the transfer or the transferee’s identity. Rather than
3 making adjustments in the definition to allow for the secured party’s lack of
4 knowledge, exculpatory provisions in Part 6 protect the secured party in that
5 circumstance. See Sections 9-605 and 9-627.

6 Consider the following examples:

7 **Example 1:** Mooney borrows money and grants a security interest in his
8 Miata to secure the debt. Mooney is a debtor and an obligor.

9 **Example 2:** Mooney borrows money and grants a security interest in his
10 Miata to secure the debt. Harris co-signs the note. As before, Mooney is the debtor
11 and an obligor. Because Harris’s obligation as a co-maker is secondary, Harris is a
12 secondary obligor.

13 **Example 3:** Mooney borrows money on an unsecured basis. Harris co-
14 signs the note and grants a security interest in his Honda to secure his obligation.
15 Inasmuch as Mooney does not have a property interest in the Honda, Mooney is not
16 a debtor. Having granted the security interest, Harris is the debtor. Because
17 Mooney is a principal obligor, he is not a secondary obligor. Whatever the outcome
18 of enforcement of the security interest against the Honda or Harris’s secondary
19 obligation, Harris will look to Mooney for his losses. The enforcement will not
20 affect Mooney’s aggregate obligations.

21 When the principal obligor (borrower) and the secondary obligor (surety)
22 each has granted a security interest in different collateral, the status of each is
23 determined by the collateral involved.

24 **Example 4:** Mooney borrows money and grants a security interest in his
25 Miata to secure the debt. Harris co-signs the note and grants a security interest in
26 his Honda to secure his obligation. When the secured party enforces the security
27 interest in Mooney’s Miata, Mooney is the debtor, and Harris is a secondary
28 obligor. When the secured party enforces the security interest in the Honda, Harris
29 is the “debtor.” As in Example 3, Mooney is an obligor, but not a secondary
30 obligor.

31 **10. “Deposit Account”; “Depository Institution.”** The revised definition
32 of “deposit account” incorporates the definition of “depository institution,” which is
33 new. The definition derives from the definitions of “bank” in Sections 4-105(1)
34 and 4A-105(a)(2), which focus on whether the organization is “engaged in the
35 business of banking.” The Drafting Committee will consider whether the term
36 “depository institution” should be replaced in the draft by the term “bank.”

37 All accounts evidenced by Article 9 “instruments” are excluded from the
38 scope of “deposit account.” In contrast, the former version excludes from the
39 “deposit account” definition “an account evidenced by a certificate of deposit
40 [CD].” The change clarifies the proper treatment of non-negotiable or
41 uncertificated CD’s issued to reflect a deposit. Under this Article, the latter would
42 be a deposit account (assuming there is no writing evidencing the depository
43 institution’s obligation to pay) whereas the former would be a deposit account only

1 if it is not an “instrument” as defined in this section (a question that turns on
2 whether the non-negotiable CD is “of a type which is in ordinary course of business
3 transferred by delivery with any necessary indorsement or assignment.)

4 A deposit account evidenced by an instrument is subject to the rules
5 applicable to instruments generally. As a consequence, a security interest in such a
6 deposit account cannot be perfected by “control” (see Section 9-109), and the
7 special priority rules applicable to deposit accounts (see Sections 9-325 and 9-337)
8 do not apply.

9 The term “deposit account” does not include “investment property,” such as
10 securities and securities entitlements. Thus, the term does not include, e.g., shares
11 in a money market mutual fund that are redeemable by check.

12 **11. Filing-related Definitions.** Several of the definitions in this section are
13 used exclusively or primarily in the filing-related provisions in Part 5. These
14 include “filing office,” “financing statement,” “original debtor,” “new debtor,” and
15 “rule.” Most of these definitions are self-explanatory, and many are discussed in
16 the Comments to Part 5.

17 **12. “Good Faith.”** This Article expands the definition of “good faith” to
18 include “the observance of reasonable commercial standards of fair dealing.” The
19 definition in this section applies when the term is used in this Article, and the same
20 concept applies for purposes of the obligation of good faith imposed by Section
21 1-203. See subsection (d).

22 **13. “Governmental Entity; Governmental Unit.”** These new terms are
23 used in Section 9-112(c), dealing with excluded transactions, and in Part 3, Subpart
24 1, dealing with choice of law.

25 **14. “Instrument.”** The definition of “instrument” has been modified to
26 make clear that it does not include rights to payment arising out of credit card
27 transactions. The bracketed phrase refers to transactions in which the card itself is
28 not used, e.g., purchases on credit over the telephone. The Drafting Committee has
29 yet to consider whether the language is necessary.

30 **14A. “Letter-of-Credit Rights.”** In this draft the term “letter-of-credit
31 rights” replaces the phraseology used in earlier drafts, “letter of credit and proceeds
32 of the letter of credit.” The reference to the letter of credit itself was thought
33 necessary to make it clear that the statute contemplates an assignment of a present
34 interest and not one that would “spring” only when a letter of credit is honored and
35 proceeds are collected. However, some letter of credit experts expressed concern
36 that references to a security interest in a letter of credit itself might be confused
37 with the transfer of drawing rights (i.e., the beneficiary’s right to demand payment
38 or performance). See Sections 9-110, comment 4, and 9-326, comments 3 and 4.
39 The new term addresses both concerns.

40 **15. “Manufactured Home; Manufactured Home Transaction.”** A
41 financing statement filed in a manufactured home transaction may remain effective
42 for a longer period of time than other financing statements. See Section 9-502(c).
43 The definition of “manufactured home” borrows from the federal Manufactured

1 Housing Act, 42 U.S.C. sections 5401 *et seq.* Another approach would be to set out
2 the definition in full, as follows:

3 “[M]anufactured home means a structure, transportable in one or
4 more sections, which in the traveling mode, is eight body feet or
5 more in width or twenty or more square feet, and which is built on a
6 permanent chassis and designed to be used as a dwelling with or
7 without a permanent foundation when connected to the required
8 utilities, and includes the plumbing, heating, air-conditioning, and
9 electrical systems contained therein; except that such term shall
10 include any structure which meets all the requirements of this
11 paragraph except the size requirements and with respect to which the
12 manufacturer voluntarily files a certification required by the
13 Secretary and complies with the standards established under this
14 title.

15 Alternatively, we could attempt to draft a simpler definition based on the federal
16 definition. We have revised the definition of “manufactured home transaction” as
17 well. The new definition limits qualifying transactions to those in which a security
18 interest in a manufactured home is a central feature.

19 16. **“New Value.”** This Article deletes former Section 9-108. Its broad
20 formulation of new value, which embraces the taking of after-acquired collateral for
21 a pre-existing claim, is unnecessary, counterintuitive, and ineffective for its original
22 purpose of sheltering after-acquired collateral from attack as a voidable preference
23 in bankruptcy. The new definition of “new value” derives from § 547(a) of the
24 Bankruptcy Code. The term is used in with respect to temporary perfection of
25 security interests in instruments, certificated securities, or negotiable documents
26 under Section 9-310(d), with respect to chattel paper priority in Section 9-327, and
27 with respect to production money security interests in Sections 9-105(a) and
28 9-321(a) and (b).

29 17. **“Public Finance Transaction.”** A financing statement filed in a
30 public finance transaction may remain effective for a longer period of time than
31 other financing statements. See Section 9-502(c). The new alternative definitions
32 are intended to capture primarily secured transactions in public debt financings.

33 18. **“Record.”** A “record” includes information that is in intangible form
34 (e.g., electronically stored) as well as tangible form (e.g., written on paper).
35 Whatever is filed in the Article 9 filing system, including financing statements,
36 termination statements, and amendments, whether transmitted in tangible or
37 intangible form, would fall within the definition.

38 The term embraces all means of communicating or storing information
39 except human memory. Given the rapid development and commercial adoption of
40 modern communication and storage technologies, requirements that documents or
41 communications be “written,” “in writing,” or otherwise in tangible form do not
42 necessarily reflect or aid commercial practices. Examples of current technologies
43 commercially used to communicate or store information include, but are not limited
44 to, magnetic media, optical discs, digital voice messaging systems, electronic mail,
45 audio tapes, and photographic media, as well as paper. “Record” is an inclusive

1 term that includes all of these methods of storing or communicating information.
2 Any “writing” is a record.

3 A “record” need not be permanent or indestructible, but the term does not
4 include any oral or other communication that is not stored or preserved by any
5 means. The information must be stored on paper or in some other medium.
6 Information that has not been retained other than through human memory does not
7 qualify as a record. A record may be authenticated. See Section 9-102(a)(3). A
8 record may be created without the knowledge or intent of a particular party.

9 Like the terms “written” or “in writing,” the term “record” does not
10 establish the purposes, permitted uses, or legal effect that a record may have under
11 any particular provision of law. For example, a record may or may not be in
12 appropriate form for filing with a filing office. Other provisions of this Act must be
13 consulted to determine these issues.

14 In some instances, statutes or the rules of filing offices may require that a
15 paper record be filed. In such cases, even if this Article permits the filing of an
16 electronic record, compliance with those statutes or rules is necessary. Similarly, a
17 filer must comply with a statute or rule that requires a particular type of encoding or
18 formatting for an electronic record.

19 This Article occasionally uses the terms “for record,” “real estate records,”
20 “interest of record,” and “record owner.” These are terms traditionally used in real
21 estate law. These contexts “otherwise require[]” that the definition of “record” in
22 this section is not applicable.

23 19. **“Registered Agent.”** This new term is explained in the Comments to
24 Section 9-501.

25 20. **“Registered Entity.”** This new term is explained in the Comments to
26 Section 9-307.

27 21. **“Secured Party.”** The definition of “secured party” clarifies the status
28 of various types of representatives. The secured party is the person in whose favor
29 the security interest has been created, as determined by reference to the security
30 agreement. This definition controls, among other things, which person has the
31 duties and potential liability that Part 6 imposes upon the secured party.

32 Consider, for example, a multi-bank facility, under which Bank A, Bank B,
33 and Bank C are lenders and Bank A serves as the collateral agent. If the security
34 interest is granted to the banks, then they are the secured parties. If the security
35 interest is granted to Bank A as collateral agent, then Bank A is the secured party.

36 As revised, the definition of “secured party” includes a “consignee,” as
37 newly defined.

38 22. **“Secured Party of Record.”** This new term refers to the person named
39 in a financing statement as a secured party or a representative. This person is
40 entitled to take action under Part 5 concerning the financing statement. The person
41 may or may not actually be a “secured party,” as defined in this section. For

1 example, no security interest may have been created, in which case no person is a
2 secured party, or the person named as the secured party in the financing statement
3 may be a representative, not the actual secured party.

4 The definition of “secured party of record” has been placed in square brackets.
5 New § 9-509A reflects an alternative approach to identifying the secured party of
6 record.

7 22A. **“Security Agreement.”** Whether an agreement creates a security
8 interest depends not on whether the parties intend that the law characterize the
9 transaction as a security interest but rather on whether the transaction falls within
10 the definition of “security interest” in Section 1-201. Thus, an agreement that the
11 parties characterize as a “lease” or “consignment” of goods may be a “security
12 agreement,” notwithstanding the parties’ stated intention that the law treat the
13 transaction as a lease or consignment and not as a secured transaction.

14 23. **“State of Organization.”** This new term is explained in the Comments
15 to Section 9-307.

16 24. **“Statutory Lien.”** The somewhat limited inclusion of statutory liens
17 within the scope of this draft, see the Comment to Section 9-112, follows the
18 recommendations made in the Report of the ABA Section of Business Law,
19 Committee on Uniform Commercial Code, Subcommittee on Relation to Other
20 Law (October, 1996). The bracketed language in the definition would limit the
21 term to liens in favor of persons who furnish goods and services in the ordinary
22 course of business. The Drafting Committee should consider whether to retain this
23 limitation. “Agricultural lien” is a subset of “statutory lien.”

24 25. **“Support Obligation.”** This new term covers the most common types
25 of credit enhancements—suretyship obligations (including guarantees) and letter-of-
26 credit rights that support one of the specified types of collateral. As explained in
27 Comment 9 dealing with secondary obligors, suretyship law determines whether an
28 obligation is “secondary” for purposes of this definition. The phrase “insurance
29 policy” is bracketed for further consideration by the Drafting Committee, in light of
30 the limited inclusion of rights under insurance policies as original collateral.

31 This Article contains rules explicitly governing attachment and perfection of
32 security interests in support obligations. See Sections 9-203, 9-308, and 9-309.
33 These provisions reflect the principle that a support obligation is an incident of the
34 collateral it supports.

35 This Article does not contain special priority provisions governing security
36 interests in support obligations. For suretyship obligations, which are included in
37 the definition of “account,” the first-to-file-or-perfect rule normally will apply to
38 both secured parties and buyers, regardless of whether the obligations are taken as
39 independent collateral or as support obligations. Under the special rule governing
40 security interests in letters of credit rights, an accounts financier’s failure to obtain
41 control (Section 9-110) of the supporting letter-of-credit rights may leave its
42 security interest exposed to a priming interest of a party who does take control. See
43 Section 9-326 (security interest in letter-of-credit rights perfected by control has
44 priority over a conflicting security interest).

1 Certain types of credit enhancements are not covered by the definition of
2 “support obligation. Other law determines the competing claims of a person who
3 takes an outright assignment of these obligations and a person who takes a security
4 interest in the related collateral. However, the Drafting Committee is considering
5 whether and, if so, how Article 9 should express the broader common-law principle
6 that “the collateral follows the obligation.

7 26. **“Transmitting Utility.”** The definition of “transmitting utility” has
8 been revised. No change in meaning is intended. The term designates a special
9 class of debtors for whom separate filing rules are provided in Part 5, thereby
10 obviating the many local fixture filings that would be necessary under the rules of
11 Section 9-501 for a far-flung public utility debtor. A transmitting utility may not be
12 regulated or operating as such in a jurisdiction where fixtures are located. For
13 example, a utility might own transmission lines in a jurisdiction, although the utility
14 generates no power and has no customers in the jurisdiction.

15 **SECTION 9-103. DEFINITIONS: “ACCOUNT”; “GENERAL**
16 **INTANGIBLES”; “PAYMENT INTANGIBLE.”**

17 (a)(1) “Account means a right to payment, whether or not earned by
18 performance:

19 (A) for property[,] other than money[,] which ~~that~~ has been or is to
20 be sold, leased, licensed, assigned, or otherwise disposed of;

21 (B) for services rendered or to be rendered;

22 (C) for a policy of insurance issued or to be issued;

23 (D) for a suretyship obligation incurred or to be incurred

24 (E) for energy provided or to be provided;

25 (F) arising out of the use of a credit or charge card or information
26 contained on or for use with the card; or

27 (G) for the use or hire of a vessel under a charter or other contract.

28 (2) The term does not include a right to payment evidenced by an
29 instrument or chattel paper[,] ~~[or] a right to payment under a letter-of-credit rights [,]~~
30 or a deposit account].

1 (b) “General intangible” means any personal property other than goods,
2 accounts, chattel paper, commercial tort claims, documents, instruments,
3 investment property, letters of credit, deposit accounts, and money.

4 (c) “Payment intangible” means a general intangible under which the
5 account debtor's principal obligation is to pay money.

6 Reporters’ Comments

7 1. **Source.** Subsections (a) and (b) derive from former Section 9-106.
8 Subsection (c) is new.

9 2. **“Account.”** The definition of “account” has been expanded and
10 reformulated. Many categories of rights to payment that would have been classified
11 as general intangibles under former Article 9 are accounts under this Article. Thus,
12 if they are sold, a financing statement must be filed to perfect the buyer’s interest in
13 them.

14 3. **“General Intangible.”** The definition in subsection (b) has been revised
15 to establish deposit accounts and commercial tort claims as separate types of
16 collateral. One important consequence is that neither the depositary institution nor
17 the tortfeasor is an “account debtor” having the rights and obligations set forth in
18 Section 9-404. In particular, neither is obligated to pay an assignee (secured party)
19 upon receipt of the notification described in Section 9-404(e). Another important
20 consequence relates to the adequacy of the description in the security agreement.
21 See Section 9-111.

22 Letter-of-credit rights likewise are not general intangibles but rather a
23 separate type of collateral. Accordingly, except as provided with respect to support
24 obligations, filing would not be effective to perfect a security interest, and the issuer
25 would not be an “account debtor.”

26 4. **“Payment Intangible.”** Subsection (c) creates a sub-category of general
27 intangibles the sale of which is subject to this Article. See Section 9-112(a)(3).

28 Virtually any intangible right could give rise to a right to payment of money
29 once one hypothesizes, for example, that the account debtor is in breach of its
30 obligation. The term “payment intangible” embraces only those general intangibles
31 “under which the account debtor’s *principal* obligation is to pay money.
32 (Emphasis added.) Although there may be difficult cases at the margin, attempting
33 a more precise statutory line would not be worthwhile. As with any classification
34 issue, from a planning standpoint it may be necessary for counsel in a sale
35 transaction to make alternative assumptions (i.e., inclusion and exclusion from
36 Article 9).

37 In classifying intangible collateral, a court should begin by identifying the
38 particular rights that have been assigned. The account debtor (promisor) under a
39 particular contract may owe several types of monetary obligations as well as other,
40 nonmonetary obligations. If the promisee’s right to payment of money is assigned

1 separately, the right is an account or payment intangible, depending on how the
2 account debtor's obligation arose. When all the promisee's rights are assigned
3 together, an account, a payment intangible, and a general intangible all may be
4 involved, depending on the nature of the rights.

5 A right to the payment of money is frequently buttressed by ancillary
6 covenants to insure the preservation of collateral, such as covenants in a purchase
7 agreement, note, or mortgage requiring insurance on the collateral or forbidding
8 removal of the collateral; or covenants to preserve credit-worthiness of the
9 promisor, such as covenants restricting dividends, etc. It is not the intention of this
10 Article to treat these ancillary rights separately from the rights to payment to which
11 they relate. Perfection of an assignment of the right to the payment of money,
12 whether it be an account or payment intangible, will also carry these ancillary
13 rights.

14 Every "payment intangible" is also a "general intangible. Accordingly,
15 except as otherwise provided, statutory provisions applicable to general intangibles
16 apply to payment intangibles.

17 **SECTION 9-104. DEFINITIONS: "PURCHASE MONEY SECURITY**
18 **INTEREST"; "PURCHASE MONEY COLLATERAL"; PURCHASE**
19 **MONEY OBLIGATION"; APPLICATION OF PAYMENTS; BURDEN OF**
20 **ESTABLISHING PURCHASE MONEY SECURITY INTEREST.**

21 (a) A security interest in goods[, including fixtures,] is a "purchase money
22 security interest :

23 (1) to the extent that the collateral ("purchase money collateral ") secures
24 an obligation incurred by an obligor as the price of the collateral or for value given
25 to enable the debtor to acquire rights in the collateral ("purchase money
26 obligation ") if the value is in fact so used; and

27 (2) if the security interest is in inventory that is or was purchase money
28 collateral, also to the extent that the security interest secures a purchase money
29 obligation incurred with respect to other inventory in which the secured party holds
30 or held a purchase money security interest.

1 (b) The interest of a consignor in goods that are the subject of a
2 consignment is a purchase money security interest in inventory for purposes of this
3 article.

4 (c) Except in a consumer goods secured transaction, if the extent to which a
5 security interest is a purchase money security interest depends on the application of
6 a payment to a particular obligation, the payment must be applied:

7 (1) in accordance with any reasonable method of application to which
8 the parties agree;

9 (2) in the absence of the parties' agreement to a reasonable method, in
10 accordance with any intention of the obligor manifested at or before the time of
11 payment; or

12 (3) in the absence of an agreement to a reasonable method and a timely
13 manifestation of the obligor's intention, first to obligations that are not secured and
14 then, if more than one obligation is secured, to obligations secured by purchase
15 money security interests in the order in which those obligations were incurred.

1 **Alternative A**

2 (d) In a consumer goods secured transaction, if the extent to which a
3 security interest is a purchase money security interest depends on the application of
4 a payment to a particular obligation:

5 (1) (A) [cite any applicable statute of a State] governs application of the
6 payment to the extent applicable; and

7 (B) to ~~To~~ the extent the statute is not applicable, the payment must
8 be applied to obligations secured by purchase money security interests in the order
9 in which those obligations were incurred, ~~and~~

10 (2) This subsection may not be varied by agreement ~~any agreement to~~
11 ~~the contrary is ineffective~~ [except to the extent that the agreement relates to the
12 application of a payment to interest or other finance charges].

13 **Alternative B**

14 (d)(1) In a consumer goods secured transaction, if the extent to which a
15 security interest is a purchase money security interest depends on the application of
16 a payment to a particular obligation, the payment must be applied to obligations
17 secured by purchase money security interests in the order in which those obligations
18 were incurred.

19 (2) This subsection may not be varied by agreement [except to the
20 extent that the agreement relates to the application of a payment to interest or other
21 finance charges].

22 **[End of Alternatives]**

23 (e) A purchase money security interest does not lose its status as such ~~even~~
24 if:

25 (1) the purchase money collateral also secures an obligation that is not a
26 purchase money obligation;

1 (2) collateral that is not purchase money collateral also secures the
2 purchase money obligation; or

3 (3) the purchase money obligation has been renewed, refinanced,
4 consolidated, or restructured.

5 (f) ~~{If the status of a security interest as a purchase money security interest~~
6 ~~or the extent to which it is a purchase money security interest is placed in issue, the}~~
7 {A} secured party claiming a purchase money security interest has the burden of
8 establishing [whether and] the extent to which the security interest is a purchase
9 money security interest [if either of the following is placed in issue:

10 (1) the status of a security interest as a purchase money security interest;

11 or

12 (2) the extent to which it is a purchase money security interest].

13 *Legislative Note: States that have an applicable statute dealing with allocation of*
14 *payments should enact Alternative A of subsection (d). Other States should enact*
15 *Alternative B.*

16 Reporters' Comments

17 1. **Source.** Former Section 9-107.

18 2. **“Purchase Money Security Interest.”** Subsection (a) limits purchase
19 money security interests to goods, including fixtures. Otherwise, no change in
20 meaning from former Section 9-107 is intended. The second sentence of former
21 Section 9-115(5)(f) made the purchase money priority rule (former Section
22 9-312(4)) inapplicable to investment property. This section's limitation makes that
23 sentence unnecessary.

24 The concept of “purchase money security interest” requires a close nexus
25 between the acquisition of the collateral and the secured obligation. Thus, a
26 security interest does not qualify as a purchase money security interest if a debtor
27 acquires property on unsecured credit and subsequently creates the security interest
28 to secure the purchase price. Similarly, if a debtor buys property for cash and
29 subsequently creates the security interest in the property to secure a borrowing of an
30 amount equivalent to the purchase price, the security interest does not have
31 purchase-money status.

32 As used in subsection (a)(1), the “price” of collateral includes obligations
33 for expenses incurred in connection with acquiring rights in the collateral, sales
34 taxes, finance charges, interest, administrative charges, expenses of collection and
35 enforcement, attorney's fees, and other similar obligations.

1 **3. Cross-Collateralization of Purchase Money Security Interests in**
2 **Inventory.** Subsection (a)(2) deals with the problem of cross-collateralized
3 purchase money security interests in inventory. Consider a simple example:

4 Seller (S) sells an item of inventory (Item-1) to Debtor (D), retaining
5 a security interest in Item-1 to secure Item-1's price and all other
6 obligations, existing and future, of D to S. S then sells another item
7 of inventory to D (Item-2), again retaining a security interest in
8 Item-2 to secure Item-2's price as well as all other obligations of D
9 to S. D then pays to S Item-1's price. D then sells Item-2 to a buyer
10 in ordinary course of business, who takes Item-2 free of S's security
11 interest.

12 Under subsection (a)(2), S's security interest in *Item-1* securing *Item-2's unpaid*
13 *price* would be a purchase money security interest. This is so because S has a
14 purchase money security interest in Item-1, Item-1 secures the price of (a "purchase
15 money obligation incurred with respect to) Item-2 ("other inventory), and Item-2
16 itself was subject to a purchase money security interest. Note that, to the extent
17 Item-1 secures the price of Item-2, S's security interest in Item-1 would not be a
18 purchase money security interest under the definition in subsection (a)(1). The
19 security interest in Item-1 is a purchase money security interest under that
20 subsection only to the extent that "the collateral (i.e., Item-1) secures an obligation
21 incurred as the price of "the collateral (i.e., Item-1) or for value given to enable the
22 debtor to acquire rights in "the collateral (again, Item-1).

23 **4. "Dual-Status" Rule; Allocation of Payments; Burden of Proof.** This
24 Article approves what some cases have called the "dual-status" rule, under which a
25 security interest may be a purchase money security interest to some extent and a
26 non-purchase money security interest to some extent. This rule is implicit in
27 subsections (a)(1) and (a)(2) ("to the extent) and is made explicit in subsection (e).
28 The Article rejects the "transformation" rule adopted by some cases, under which
29 any cross-collateralization, refinancing, or the like destroys the purchase-money
30 status entirely.

31 Consider, for example, what happens when a \$10,000 loan secured by a
32 purchase money security interest is refinanced by the original lender, and, as part of
33 the transaction, the debtor borrows an additional \$2,000 secured by the collateral.
34 Subsection (e) resolves any doubt that the security interest remains a purchase
35 money security interest. Under subsection (a) it enjoys purchase-money status only
36 to the extent of \$10,000.

37 If the debtor makes a \$1,000 payment on the \$12,000 obligation, then one
38 must determine the extent to which the security interest remains a purchase money
39 security interest—\$9,000 or \$10,000. Subsection (c)(1) expresses the overriding
40 principle for determining the extent to which a security interest is a purchase money
41 security interest under these circumstances, in cases other than consumer goods
42 secured transactions: freedom of contract, as limited by principle of
43 reasonableness. An unconscionable method of application is not a reasonable one
44 and so would not be given effect under subsection (c)(1). In the absence of
45 agreement, subsection (c)(2) permits the obligor to determine how payments should
46 be allocated. If the obligor fails to manifest its intention, obligations that are not

1 secured will be paid first. (As used in this Article, the concept of “obligations that
2 are not secured” means obligations for which the debtor has not created a security
3 interest. This concept is different from and should not be confused with the
4 concept of an “unsecured claim” as it appears in Bankruptcy Code § 506(a).) The
5 obligor may prefer this approach, because unsecured debt is likely to carry a higher
6 interest rate than secured debt. A creditor who would prefer to be secured rather
7 than unsecured also would prefer this approach.

8 After the unsecured debt is paid, payments are to be applied first toward the
9 obligations secured by purchase money security interests. In the event that there is
10 more than one such obligation, payments first received are to be applied to
11 obligations first incurred. See subsection (c)(3). Once these obligations are paid,
12 there are no purchase money security interests, and so there is no need for
13 additional allocation rules.

14 The Drafting Committee thinks that freedom of contract with respect to
15 allocation of payments is likely to be illusory in the consumer setting. Accordingly,
16 it would adopt a statutory allocation rule that cannot be varied by agreement.
17 Subsection (d) presents two versions of a mandatory rule. Alternative A enables a
18 State to incorporate another applicable statutory allocation rule by reference. If the
19 statutory rule is inapplicable, then payments are to be applied to purchase money
20 obligations in the order incurred. Under Alternative B, payments are to be applied
21 to purchase money obligations in the order incurred, regardless of whether a
22 statutory allocation rule otherwise would apply. States that have adopted a
23 statutory allocation rule select Alternative A and other States should select
24 Alternative B. The bracketed language at the end of each alternative raises the
25 question whether the otherwise mandatory rule should be relaxed to permit an
26 agreement that payments may be applied first to accrued interest or finance charges.

27 By determining whether a security interest is a “purchase money security
28 interest,” the dual-status rule and allocation formula affect only issues under this
29 Article—primarily perfection and priority. See, e.g., Sections 9-309(a)(7); 9-322.
30 Whether a security interest is a “purchase money security interest” under other law,
31 however, is determined by that law. For example, decisions under Bankruptcy
32 Code § 522(f) have applied both the dual-status and the transformation rules. The
33 Bankruptcy Code does not expressly adopt the state law definition of “purchase
34 money security interest.” Where federal law does not defer to this Article, this
35 Article does not, and could not, determine a question of federal law.

36 The statutory terms “renewed,” “refinanced,” and “restructured” are not
37 defined. Whether the terms encompass a particular transaction depends upon
38 whether, under the particular facts, the purchase-money character of the security
39 interest fairly can be said to survive. Each term contemplates that an identifiable
40 portion of the purchase money obligation could be traced to the new obligation
41 resulting from a renewal, refinancing, or restructuring. As is the case when the
42 extent of a security interest is in issue, the secured party claiming a purchase money
43 security interest has the burden of establishing whether the security interest retains
44 its purchase-money status following a renewal, refinancing, or restructuring. See
45 subsection (f).

1 5. **Consignments.** Under former Section 9-114, the priority of the
2 consignor's interest is similar to that of a purchase money security interest.
3 Subsection (b) achieves this result more directly, by defining the interest of a
4 "consignor, as defined in Section 9-102, to be a purchase money security interest
5 in inventory for purposes of this article. This drafting convention obviates any need
6 to set forth special priority rules applicable to the interest of a consignor. Rather,
7 the priority of the consignor's interest as against the rights of lien creditors of the
8 consignee, competing secured parties, and purchasers of the goods from the
9 consignee can be determined by reference to the priority rules generally applicable
10 to inventory, such as Sections 9-315, 9-316, 9-319, and 9-322. For purposes other
11 than those of this article, including the rights and duties of the consignor and
12 consignee as between themselves, the consignor would remain the owner of goods
13 under a bailment arrangement with the consignee.

14 **[SECTION 9-105. DEFINITIONS: "PRODUCTION MONEY**
15 **SECURITY INTEREST"; "PRODUCTION MONEY CROPS";**
16 **"PRODUCTION MONEY OBLIGATION"; "PRODUCTION OF CROPS";**
17 **BURDEN OF ESTABLISHING PRODUCTION MONEY SECURITY**
18 **INTEREST.**

19 (a) A security interest in crops is a "production money security interest to
20 the extent that the crops ("production money crops) secure an obligation incurred
21 by an obligor for new value given to enable the debtor to produce the production
22 money crops ("production money obligation) if the value is in fact used for the
23 production of the production money crops.

24 (b) The "production of crops includes tilling and otherwise preparing land
25 for growing, planting, cultivating, fertilizing, protecting from damage or disease,
26 irrigating, harvesting, and gathering crops.

27 (c) If the extent to which a security interest is a production money security
28 interest depends on the application of a payment to a particular obligation, the
29 payment must be applied:

30 (1) in accordance with any reasonable method of application to which
31 the parties agree;

1 (2) in the absence of the parties' agreement to a reasonable method, in
2 accordance with any intention of the obligor manifested at or before the time of
3 payment; or

4 (3) in the absence of an agreement to a reasonable method and a timely
5 manifestation of the obligor's intention:

6 (A) first, to obligations that are not secured; and

7 (B) then, if more than one obligation is secured, to obligations
8 secured by production money security interests in the order in which those
9 obligations were incurred.

10 (d) A production money security interest does not lose its status as such if:

11 (1) the production money collateral also secures an obligation that is not
12 a production money obligation;

13 (2) collateral that is not production money collateral also secures the
14 production money obligation; or

15 (3) the production money obligation has been renewed, refinanced, or
16 restructured.

17 (e) ~~[If the status of a security interest as a production money security~~
18 ~~interest or the extent to which it is a production money security interest is placed in~~
19 ~~issue, the]~~ [A] secured party claiming a production money security interest has the
20 burden of establishing [whether and] the extent to which the security interest is a
21 production money security interest] [if either of the following is placed in issue:

22 (1) the status of a security interest as a production money security
23 interest; or

24 (2) the extent to which it is a production money security interest].

25 *Legislative Note: This section is optional. States that do not enact this section also*
26 *should not enact Section 9-321.*

Reporters' Comments

1. **Source.** New.

2. **Production Money Priority; “Production Money Security Interest.”**

There appears to be a general consensus that the former rule affording special priority to those who provide secured credit that enables a debtor to produce crops, found in former Section 9-312(2), is not workable. However, after years of discussion, no consensus concerning the rule has arisen among those who engage in agricultural financing. The issue remains controversial, and opinions differ strongly over whether to replace the rule with one that affords greater protection to providers of production inputs or whether to eliminate the rule without replacing it.

Section 9-321 contains a revised production money priority rule. The brackets surrounding it reflect the likely division of views among state legislatures as to the desirability of the rule. In conjunction with the new priority rule, this section—also bracketed—provides a definition of “production money security interest.” It is patterned closely on Section 9-104, which defines “purchase money security interest.” Subsection (b) makes clear that a security interest can obtain production-money status only to the extent that it secures value that actually can be traced to the direct production of crops. To the extent that a security interest secures indirect costs of production, such as general living expenses, the security interest is not entitled to production-money treatment.

SECTION 9-106. CLASSIFICATION OF GOODS: “CONSUMER GOODS”; “EQUIPMENT”; “FARM PRODUCTS”; “INVENTORY.”

(a) “Consumer goods” means goods that are used or bought for use primarily for personal, family, or household purposes.

(b) “Equipment” means goods [that are used or bought for use primarily in business, including farming or a profession, or by a debtor that is a nonprofit organization or a governmental subdivision or agency. The term includes goods] other than inventory, farm products, or consumer goods.

(c)(1) Goods are “farm Farm products; if:

(A) the ~~with respect to~~ debtor is engaged in raising, cultivating, propagating, fattening, grazing, or other farming, livestock, or aquacultural operations; and means:

(B) the goods are:

- 1 (i) crops grown, growing, or to be grown, including crops produced
2 on trees, vines, and bushes;
- 3 (ii) livestock, born or unborn;
- 4 (iii) supplies used or produced in farming, livestock, or aquacultural
5 operations; or
- 6 (iv) products of crops or livestock in their unmanufactured states.
- 7 (2) The term does not include equipment or inventory.
- 8 (3) For purposes of paragraph (1), the terms “crops” and “livestock
9 include aquatic goods produced in aquacultural operations.
- 10 (d)(1) “Inventory” means goods that are:
- 11 (A) leased by a person [as lessor];
- 12 (B) held by a person for sale or lease or to be furnished under
13 contracts of service;
- 14 (C) furnished by a person under contracts of service; or
- 15 (D) raw materials, work in process, or materials used or consumed in
16 a business.
- 17 (2) [The term does not include equipment.]

Reporters' Comments

1. **Source.** Former Section 9-109.

2. **"Equipment."** Brackets inserted in the definition of equipment reflect the Drafting Committee's division over whether the first sentence is necessary or useful. If the bracketed language in that definition is deleted, the brackets around the final sentence of the definition of inventory indicate that it also should be deleted.

3. **"Farm Products."** The primary revision to the definition of "farm products" is to clarify the status of aquaculture.

4. **"Inventory."** The definition of "inventory" has been revised to make clear that the term includes goods leased by the debtor to others as well as goods held for lease. The same result would obtain under the former definition.

**SECTION 9-107. DEFINITIONS: "COMMODITY ACCOUNT";
"COMMODITY CONTRACT"; "COMMODITY CUSTOMER";
"COMMODITY INTERMEDIARY"; "INVESTMENT PROPERTY."**

(a) "Commodity account" means an account maintained by a commodity intermediary in which a commodity contract is carried for a commodity customer.

(b) "Commodity contract" means a commodity futures contract, an option on a commodity futures contract, a commodity option, or another contract that, in each case, is:

(1) traded on or subject to the rules of a board of trade that has been designated as a contract market for such a contract pursuant to federal commodities laws; or

(2) traded on a foreign commodity board of trade, exchange, or market, and is carried on the books of a commodity intermediary for a commodity customer.

(c) "Commodity customer" means a person for which a commodity intermediary carries a commodity contract on its books.

(d) "Commodity intermediary" means:

1 (1) a person that is registered as a futures commission merchant under
2 the federal commodities laws; or

3 (2) a person that in the ordinary course of its business provides clearance
4 or settlement services for a board of trade that has been designated as a contract
5 market pursuant to the federal commodities laws.

6 (e) “Investment property means a security, whether certificated or
7 uncertificated, security entitlement, securities account, commodity contract, or
8 commodity account.

9 Reporters’ Comments

10 1. **Source.** Former Section 9-115(a).

11 2. **Rules Governing Investment Property.** Section 9-115 was added in
12 conjunction with Revised Article 8 and contains a variety of rules applicable to
13 security interests in investment property. These rules have been relocated to the
14 appropriate sections of Article 9. See, e.g., Sections 9-203(a), (d) (attachment);
15 9-324 (priority).

16 3. **Distinguishing Investment Property from Deposit Accounts.** Some
17 types of investment property (e.g., money market funds) appear to function so much
18 like deposit accounts that distinguishing between the two may prove difficult in
19 certain cases. The Drafting Committee is sensitive to the costs that may result from
20 uncertainty over the proper classification of particular collateral. The Drafting
21 Committee attempted to formulate a single set of rules to cover both types of
22 collateral, so that very little will turn on the distinction. However, the provisions
23 applicable to deposit accounts differ from those applicable to investment property
24 in several important respects. For example, a security interest in investment
25 property may be perfected by filing, whereas filing normally is ineffective to perfect
26 a security interest in a deposit account.

27 **SECTION 9-108. CONTROL OVER INVESTMENT PROPERTY.**

28 (a) A person has control of a certificated security, uncertificated security, or
29 security entitlement as provided in Section 8-106.

30 (b) A secured party has control over a commodity contract if:

31 (1) the secured party is the commodity intermediary with which the
32 commodity contract is carried; or

1 (2) the commodity customer, secured party, and commodity
2 intermediary have agreed that the commodity intermediary will apply any value
3 distributed on account of the commodity contract as directed by the secured party
4 without further consent by the commodity customer.

5 (c) A secured party that has control over all security entitlements or
6 commodity contracts carried in a securities account or commodity account has
7 control over the securities account or commodity account.

8 Reporters' Comment

9 1. **Source.** Former Section 9-115(e).

10 2. **"Control" under Article 8.** As lawyers have attempted to craft
11 agreements that give secured parties "control" under Section 8-106(d)(2), some
12 uncertainty has arisen concerning the effect of a securities intermediary's agreement
13 that it will comply with a secured party's entitlement orders only if certain
14 conditions are met. For a discussion of this issue, see Section 9-109, Comment 3.

15 **SECTION 9-109. CONTROL OVER DEPOSIT ACCOUNT.**

16 (a) A secured party has control over a deposit account if:

17 (1) the secured party is the depository institution with which the deposit
18 account is maintained;

19 (2) the debtor, secured party, and depository institution have agreed in
20 an authenticated record that the depository institution will comply with instructions
21 originated by the secured party directing disposition of the funds in the account
22 without further consent by the debtor; or

23 (3) the secured party becomes the depository institution's customer with
24 respect to the deposit account.

25 (b) A secured party that has satisfied the requirements of ~~subsection (a)(2)~~
26 ~~or (3))~~ subsection (a) has control even if the debtor retains the right to direct the
27 disposition of funds from the deposit account.

28 Reporters' Comments

1 **Change from Prior Draft.** The change to subsection (b) makes clear that
2 the debtor’s right to withdraw or otherwise direct the disposition of funds from the
3 account does not prevent a secured party from having control under any of the
4 control mechanisms described in subsection (a).

5 1. **Source.** New; derived from Section 8-106.

6 2. **Why “Control” Matters.** This section explains the concept of “control
7 over a deposit account. “Control under this section may serve two functions.
8 First, “control by agreement may substitute for a security agreement as an element
9 of attachment. See Section 9-203(a)(1). Second, when a deposit account is taken
10 as original collateral, the only method of perfection is taking control under this
11 section. See Section 9-310(a)(2).

12 3. **Requirements for “Control.”** This section derives from Section 8-106
13 of Revised Article 8, which defines “control over securities and certain other
14 investment property. Under subsection (a)(1), the depositary institution with which
15 the deposit account is maintained has control. The effect of this provision is to
16 afford the depositary institution automatic perfection. No other form of public
17 notice is necessary, because all actual and potential creditors of the debtor are
18 always on notice that the depositary institution with which the debtor’s deposit
19 account is maintained may assert a claim against the deposit account.

20 Under subsection (a)(2), a secured party may take control by obtaining the
21 depositary institution’s authenticated agreement that it will comply with the secured
22 party’s instructions without further consent by the debtor. The analogous provision
23 in Section 8-106 does not require that the agreement be authenticated. As the
24 Comments to Section 9-108 indicate, some uncertainty has arisen concerning the
25 requirements of Section 8-106(d)(2), particularly when a securities intermediary has
26 agreed that it will comply with a secured party’s entitlement orders only if certain
27 conditions are met. An agreement to comply with the secured party’s instructions
28 suffices for “control of a deposit account under this section even if the depositary
29 institution’s agreement is subject to specified conditions, e.g., that the secured
30 party’s instructions are accompanied by a certification that the debtor is in default.
31 (Of course, if the condition is the debtor’s further consent, the statute explicitly
32 provides that the agreement would not confer control.) The Drafting Committee
33 may reconsider whether this resolution is appropriate and, if necessary, will adjust
34 the text of this section and the analogous provision in Section 8-106. For now, a
35 suggested revision to Official Comment 7 to Section 8-106 appears in the
36 Appendix.

37 Under subsection (a)(3), a secured party may take control by becoming the
38 depositary institution’s customer. As the customer, the secured party would enjoy
39 the right to withdraw funds from the deposit account. The Drafting Committee has
40 yet to resolve all the issues that may arise from the situation in which the secured
41 party has only a security interest in a deposit account that it appears to own
42 (because it is maintained in the secured party’s name).

43 Perfection by control is not available for accounts evidenced by an
44 instrument (e.g., certain certificates of deposit), which by definition are not “deposit
45 accounts.

1 Subsection (b) also derives from Revised Article 8. It makes clear that
2 “control” need not deprive the debtor of the ability to reach the funds on deposit.

3 **SECTION 9-110. CONTROL OVER LETTER-OF-CREDIT RIGHTS**
4 ~~**AND PROCEEDS OF LETTER OF CREDIT.**~~ A secured party has control over
5 a letter-of-credit rights and proceeds of the letter of credit to the extent of any right
6 to payment or performance by or proceeds received from if:

7 (1) (A) the issuer or any nominated person if the issuer or nominated person
8 has consented to an assignment of proceeds of the letter of credit under Section
9 5-114(c) or otherwise applicable law or practice.; and

10 ————— (B) the secured party has a perfected security interest in the collateral
11 that the letter of credit supports; or

12 ————— (2) the secured party is a transferee beneficiary of the letter of credit [and
13 the issuer may not refuse to recognize or carry out the transfer under Section
14 5-112(b)].

15 ————— **Alternative B**

16 ————— (1) (A) the issuer or any nominated person has consented to an assignment
17 of proceeds of the letter of credit under Section 5-114(c); or

18 ————— (B) the secured party is a transferee beneficiary of the letter of credit
19 [and the issuer may not refuse to recognize or carry out the transfer under Section
20 5-112(b)]; and

21 ————— (2) the secured party has a perfected security interest in the collateral that
22 the letter of credit supports.

23 **Reporters’ Comments**

24 **Change from Prior Draft:** Rewritten, as described below.

25 1. **Source.** New.

26 2. **“Control.”** Whether a secured party has control over letter-of-credit
27 rights determines the secured party’s rights as against competing secured parties.

1 See Section 9-326. This draft provides that a secured party can acquire control over
2 letter-of-credit rights by receiving an assignment if the secured party obtains the
3 consent of the issuer or any nominated person, such as a confirmer or negotiating
4 bank. Because both issuers and nominated persons may give or be obligated to give
5 value under a letter of credit, this section contemplates that a secured party obtains
6 control of letter-of-credit rights with respect to the issuer or a particular nominated
7 person only to the extent that the issuer or that nominated person consents to the
8 assignment. For example, if a secured party obtains control to the extent of an
9 issuer's obligations but fails to obtain the consent of a nominated person, the
10 secured party does not have control to the extent that the nominated person gives
11 value. In many cases the person or persons who will give value under a letter of
12 credit will be clear from its terms. In other cases, prudence may suggest obtaining
13 consent from more than one person. The details of the consenting issuer's or
14 nominated person's duties to pay or otherwise render performance to the secured
15 party are left to the agreement of the parties.

16 3. **"Proceeds of a Letter of Credit."** Section 5-114 follows traditional
17 banking terminology by referring to a letter of credit beneficiary's assignment of its
18 right to receive payment thereunder as an assignment of the "proceeds of a letter of
19 credit. However, as the seller of goods can assign its right to receive payment (an
20 "account) before it has been earned by delivering the goods to the buyer, so the
21 beneficiary of a letter of credit can assign its contingent right to payment before the
22 letter of credit has been honored. See Section 5-114(b). If the assignment creates a
23 security interest, the security interest can be perfected at the time it is created. An
24 assignment of, including the creation of a security interest in, letter-of-credit rights
25 is an assignment of a present interest.

26 4. **"Transfer" vs. "Assignment."** Letter-of-credit law and practice
27 distinguish the "transfer" of a letter of credit from an "assignment. Under a
28 transfer, the transferee itself becomes the beneficiary and acquires the right to draw.
29 Whether a new, substitute credit is issued or the issuer advises the transferee of its
30 status as such, the transfer constitutes a novation under which the transferee is the
31 new, substituted beneficiary (but only to the extent of the transfer, in the case of a
32 partial transfer).

33 Section 5-114(e) provides that the rights of a transferee beneficiary or
34 nominated person are independent of the beneficiary's assignment of the proceeds
35 of a letter of credit and are independent and superior to the assignee's right to the
36 proceeds. For this reason, transfer does not appear in this draft as a means of
37 control. Section 9-326 recognizes the independent and superior rights of a
38 transferee beneficiary under Section 5-114(e); the priority of a secured party that
39 has obtained control of letter-of-credit rights are made subject to those independent
40 and superior rights.

41 5. **Support Obligation: Automatic Attachment and Perfection.** Letter-
42 of-credit rights are a type of support obligation, as defined in Section 9-102. Under
43 Sections 9-203 and 9-308, a security interest in letter-of-credit rights
44 automatically attaches and is automatically perfected if the security interest in the
45 supported obligation is perfected. However, unless the secured party has control
46 over the letter-of-credit rights or itself becomes a transferee beneficiary, it cannot
47 obtain any rights against the issuer or a nominated person under Article 5.

1 Consequently, as a practical matter, the secured party's rights would be limited to
2 its ability to locate and identify proceeds distributed by the issuer or nominated
3 person under the letter of credit.

4 **SECTION 9-111. SUFFICIENCY OF DESCRIPTION.**

5 (a) Except as otherwise provided in subsections (c), (d), and (e), a
6 description of personal or real property is sufficient, whether or not it is specific, if
7 it reasonably identifies what is described.

8 (b) (1) Except as otherwise provided in paragraph (2) and subsections (c),
9 (d), and (e), a description of collateral reasonably identifies the collateral if it
10 identifies the collateral by:

11 (A) specific listing;

12 (B) category;

13 (C) a term defined in [the Uniform Commercial Code];

14 (D) quantity;

15 (E) computational or allocational formula or procedure; or

16 (F) any other method, if the identity of the collateral is objectively
17 determinable.

18 (2) A description of collateral as all the debtor's assets, all the debtor's
19 personal property, or the like does not reasonably identify the collateral.

20 (c) Except as otherwise provided in ~~Subject to~~ subsection (d), a description
21 of a security entitlement, securities account, or commodity account is sufficient if it
22 describes the collateral by those terms or as investment property, or if it describes
23 the underlying financial asset or commodity contract.

24 (d) In a consumer secured transaction, a description of a security
25 entitlement, securities account, or commodity account is sufficient only if it is
26 specific. A description by type alone is not sufficient.

(e) A description of a commercial tort claim is sufficient only if it is specific. A description by type alone is not sufficient.

Reporters' Comment

Change from Prior Draft: New subsection (b)(2) makes explicit that “supergeneric” collateral descriptions are insufficient for purposes of a security agreement.

Discussion Questions: Should the draft provide greater guidance on the requirement for specificity in subsection (e)? If so, how should it treat a description like “all tort claims arising out of the explosion of my factory” ?

1. **Source.** Former Sections 9-110; 9-115(3).

2. **General Rules; After-acquired Collateral.** Subsection (a) retains substantially the same formulation as former Section 9-110. Subsection (b)(1), which was applicable only to investment property under former Section 9-115(3), has been made applicable to all kinds of collateral. It expands upon subsection (a) by indicating a variety of ways in which a description might reasonably identify collateral. Subsection (b)(1) is subject to subsection (b)(2), which follows prevailing case law and adopts the view that an “all assets” or “all personal property” description for purposes of a *security agreement* is *not* sufficient. Note, however, that under Section 9-504, a *financing statement* sufficiently indicates the collateral if it “covers all assets or all personal property.”

Much litigation has arisen over whether a description in a security agreement is sufficient to include after-acquired collateral if the agreement does not explicitly so provide. This question is one of contract interpretation and is not susceptible to a statutory rule (other than a rule to the effect that it is a question of contract interpretation). Accordingly, this section contains no reference to descriptions of after-acquired collateral.

3. **Investment Property.** Under subsection (c), the use of the wrong Article 8 terminology does not render a description invalid (e.g., a security agreement intended to cover a debtor’s “security entitlements” is sufficient if it refers to the debtor’s “securities”).

4. **Consumer Investment Property; Tort Claims.** Subsections (d) and (e) require greater specificity of description in order to prevent debtors from inadvertently encumbering property. Subsection (d) requires that a description of a security entitlement, a securities account, or a commodity account be specific. A description by “type” (e.g., “all existing and after-acquired investment property” or “all existing and after-acquired security entitlements”) is insufficient. If the collateral consists of a securities account or a commodity account, a specific description of the account is sufficient to cover all existing and future security entitlements or commodity entitlements carried in the account. See Section 9-203(e)(3), (4).

Subsection (d) likewise requires a more exacting description of commercial tort claims than one by “type.” However, under Section 9-204, an after-acquired

1 collateral provision in a security agreement will not reach future commercial tort
2 claims. It follows that when an effective security agreement covering a commercial
3 tort claim is entered into the claim already will exist.

4 [SUBPART 2. APPLICABILITY OF ARTICLE]

5 **SECTION 9-112. SCOPE.**

6 (a) Except as otherwise provided in subsection (c), this article applies to:

7 (1) any transaction, regardless of its form, that creates a security interest
8 in personal property or fixtures by contract;

9 (2) a statutory lien;

10 (3) a sale of an account, chattel paper, or payment intangible; and

11 (4) a consignment.

12 (b) The application of this article to a security interest in a secured
13 obligation is not affected by the fact that the obligation is itself secured by a
14 transaction or interest to which this article does not apply.

15 (c) This article does not apply to the extent that:

16 (1) a ~~security interest subject to any~~ statute, regulation, or treaty of the
17 United States, ~~to the extent that the statute, regulation, or treaty~~ preempts this
18 article;

19 (2) ~~a transfer by this State or by a governmental entity of this State to the~~
20 ~~extent that~~ another statute of this State [expressly] governs the creation, perfection,
21 priority, or enforcement of ~~a~~ the security interest created by this State or a
22 governmental unit of this State ~~the transfer~~;

23 (3) a statute of transfer by another State, a foreign nation country, or a
24 governmental entity unit of another State or a foreign nation country, ~~to the extent~~
25 ~~that a statute of the State or country~~, other than a statute generally applicable to

1 security interests, [expressly] governs creation, perfection, priority, or enforcement
2 of ~~a the security interest interests~~ created by the State, nation, or governmental unit.
3 ~~transfer;~~

4 (d) This article does not apply to:

5 (1 4) a landlord's lien[, other than a statutory lien];

6 (2 5) a lien, other than a statutory lien, given by rule of law for services
7 or materials, except as provided in Section 9-330 with respect to priority of the lien;

8 (3 6) a transfer of a claim for wages, salary, or other compensation of an
9 employee;

10 (4 7) a sale of accounts, chattel paper, or payment intangibles as part of
11 a sale of the business out of which they arose;

12 (5 8) an assignment of accounts, chattel paper, or payment intangibles
13 which is for the purpose of collection only;

14 (6 9) an assignment of a right to payment under a contract to an assignee
15 that is also obliged to perform under the contract;

16 (7 10) an assignment of a single account or payment intangible to an
17 assignee in whole or partial satisfaction of a preexisting indebtedness;

18 (8 11) a transfer of an interest in or claim under any policy of insurance,
19 except[:

20 (A) a transfer by a healthcare provider of a right to payment arising
21 out the furnishing of healthcare goods or services; and

22 (B)] as provided in Sections 9-313 and 9-319 with respect to
23 proceeds and priorities in proceeds;

24 (9 12) a right represented by a judgment, other than a judgment taken on
25 a right to payment that was collateral;

(10 43) a right of recoupment or set-off, except as provided in Section 9-337 with respect to the effectiveness of rights of recoupment or set-off against deposit accounts and in Section 9-404(a) with respect to defenses or claims of an account debtor;

(11 ~~14~~) the creation or transfer of an interest in or lien on real property, including a lease or rents thereunder, except to the extent that provision is made for fixtures in Section 9-331;

(12 ~~15~~) a transfer of any claim arising in tort, except:

(A) a transfer of a commercial tort claim; [and]

(B) as provided in Sections 9-313(a)(5) and 9-319 with respect to proceeds and priorities in proceeds[; or] [and

(C) a transfer of a liquidated and undisputed claim that is generally
assignable under applicable law; or]

~~(16) a transfer of an interest in a deposit account maintained with a Federal Reserve Bank or maintained by a depository institution with another depository institution; or~~

(13 17) a transfer of an interest in a deposit account in a consumer secured transaction, except as provided in Sections 9-313 and 9-319 with respect to proceeds and priorities in proceeds.

Reporters' Comments

Change from Prior Draft: The deletion of former paragraph (16) in subsection (d) was made at the suggestion of a representative from the Federal Reserve Bank of New York.

Discussion Question: Should Article 9 apply to all liquidated and undisputed tort claims, including non-business claims for bodily injury? If not, does the draft sufficiently make clear that security interests in structured settlements can serve as original collateral under Article 9?

1. **Source.** Former Sections 9-102 and 9-104.

1 **2. Basic Scope Provision.** Subsection (a)(1) derives from former Section
2 9-102(1) and (2). These subsections have been combined and shortened. No
3 change in meaning is intended.

4 **3. Statutory Liens.** Subsection (a)(2) is new and expands the scope of this
5 Article to cover statutory liens, as defined in Section 9-102. Certain provisions,
6 such as Section 9-315, relate only to agricultural liens and not to statutory liens
7 generally. In general, the draft deals with more aspects of agricultural liens than is
8 the case with other statutory liens. For example, it covers priority contests between
9 and among *all* statutory liens and security interests, but only those contests between
10 and among *agricultural* liens and other persons, such as lien creditors and buyers.
11 Also, part 6 excludes statutory liens (other than agricultural liens) from its scope.
12 See Section 9-601(e).

13 **4. Sales of Payment Intangibles and Other Receivables.** Subsection
14 (a)(3) expands the scope of Article 9 by including the sale of a “payment
15 intangible,” defined in Section 9-103(c) as “a general intangible under which the
16 account debtor’s principal obligation is to pay money. To a considerable extent,
17 this Article affords these transactions treatment identical to that given sales of
18 accounts and chattel paper. In some respects, however, sales of payment
19 intangibles are treated differently from sales of other receivables. See, e.g., Section
20 9-406. Although this Article occasionally distinguishes between outright sales of
21 receivables and sales that secure an obligation, neither this Article nor the definition
22 of “security interest” (Section 1-201(37)) delineates how a particular transaction is
23 to be classified. That issue is left to the courts.

24 **5. Consignments.** Subsection (a)(4) is new. This Article applies to every
25 “consignment. The term, as defined in Section 9-102, includes many “true
26 consignments (i.e., bailments for the purpose of sale). The term “consignment
27 also includes a “sale or return,” as defined in Section [2-406].

28 Under common law, creditors of a bailee are unable to reach the interest of
29 the bailor (in the consignment case, the consignor-owner). Like the former Article,
30 this Article changes the common-law result; however, it does so in a different
31 manner. For purposes of determining the rights and interests of third-party
32 creditors of, and purchasers of the goods from, the consignee, but not for other
33 purposes, such as remedies of the consignor, the consignee acquires under this
34 Article whatever rights and title the consignor had or had power to transfer. See
35 Section 9-315A. The interest of a consignor is defined to be a security interest, see
36 Section 1-201(37) (reproduced in the Appendix), more specifically, a purchase
37 money security interest in the consignee’s inventory. See Section 9-104(b). Thus,
38 the rules pertaining to lien creditors, buyers, and attachment, perfection, and
39 priority of competing security interests apply to consigned goods. The relationship
40 between the consignor and consignee is left to other law. In particular, consignors
41 have no duties under Part 6. See Section 9-601(d).

42 Sometimes parties characterize transactions that secure an obligation (other
43 than the bailee’s obligation to returned bailed goods) as “consignments. These
44 transactions are not “consignments” within the meaning of Section 9-112(a)(4).
45 See Section 9-102 (last clause of the definition of “consignment”). This Article

1 applies also to these transactions, by virtue of Section 9-112(a)(1). They create a
2 security interest within the meaning of the first sentence of Section 1-201(37).

3 This Article does not apply to consignments that fall outside the definition
4 in Section 9-102 and do not create a security interest that secures an obligation.

5 **6. Federal Preemption.** Former Section 9-104(a) excludes from Article 9
6 “a security interest subject to any statute of the United States, to the extent that such
7 statute governs the rights of parties to and third parties affected by transactions in
8 particular types of property. Some may read the former section (erroneously) to
9 suggest that Article 9 defers to federal law even when federal law does not preempt
10 Article 9. Subsection (c)(1) recognizes explicitly that the Article defers to federal
11 law only when and to the extent that it must—i.e., when federal law preempts it.

12 **7. Governmental Debtors.** At the suggestion of the International Secured
13 Transactions Task Force, the exclusion of former Section 9-104(e), concerning
14 security interests created by governmental debtors, has been revised and replaced by
15 the exclusions in new paragraphs (2) and (3) of subsection (c). These paragraphs
16 reflect the view that Article 9 should apply to security interests created by a
17 “governmental entity (as defined in Section 9-102) except to the extent that
18 another statute governs the issue in question. Under paragraph (2), this Article
19 defers to all statutes of the forum State. (A forum cannot determine whether it
20 should consult the choice-of-law rules in the forum’s UCC unless it first determines
21 that its UCC applies to the transaction before it.) Paragraph (3) defers to statutes of
22 another State or a foreign nation only to the extent that those statutes contain rules
23 applicable specifically to security interests created by the governmental entity in
24 question.

25 ***Example:*** A New Jersey state commission creates a security interest in
26 favor of a New York bank. The validity of the security interest is litigated
27 in New York. To the extent that a New Jersey statute contains rules
28 peculiar to creation of security interests by governmental entities generally,
29 to creation of security interests by state commissions, or to creation of
30 security interests by this particular state commission, then that law will
31 govern. On the other hand, to the extent that New Jersey law provides that
32 security interests created by governmental entities, state commissions, or
33 this state commission are governed by the law generally applicable to
34 secured transactions (i.e., New Jersey’s Article 9), then the New York’s
35 Article 9 will govern.

36 ***Example:*** A airline that is an instrumentality of the foreign nation creates a
37 security interest in favor of a New York bank. The analysis used in the
38 previous example would apply here. That is, if the matter is litigated in
39 New York, New York law would govern except to the extent that the
40 foreign nation enacted a statute applicable to security interests created by
41 governmental entities generally or by the airline specifically.

42 The fact that New York law applies does not necessarily mean that
43 perfection is accomplished by filing in New York. Rather, it means that the court
44 should apply New York’s Article 9, including its choice-of-law provision. Under
45 that provision (assuming New York adopts draft Section 9-301), perfection is

1 governed by the law of the jurisdiction in which the debtor is located. Section
2 9-307 determines the debtor's location for choice-of-law purposes.

3 If a transaction does not bear an appropriate relation to the forum State, then
4 that State's Article 9 will not apply, regardless of whether the transaction would be
5 excluded by paragraph (3).

6 **Example:** A Belgian governmental entity grants a security interest in its
7 equipment to a Swiss secured party. The equipment is located in Belgium.
8 A dispute arises and, for some reason, an action is brought in a New Mexico
9 state court. Inasmuch as the transaction bears no "appropriate relation" to
10 New Mexico, New Mexico's UCC, including its Article 9, is inapplicable.
11 See Section 1-105(1). New Mexico's Section 9-112(c) on excluded
12 transactions should not come into play. Even if the parties agreed that New
13 Mexico law would govern, the parties' agreement would not be effective
14 because the transaction does not bear a "reasonable relation" to New
15 Mexico. See Section 1-105(1).

16 Conversely, Article 9 will come into play only if the litigation arises in a
17 UCC jurisdiction or if a foreign choice-of-law rule leads a foreign court to apply the
18 law of a UCC jurisdiction. For example, if issues concerning a security interest
19 granted by a foreign airline to a New York bank are litigated overseas, the court
20 may be bound to apply the law of the debtor's jurisdiction and not New York's
21 Article 9.

22 An alternative or supplemental approach, which the Drafting Committee did
23 not pursue, is to make certain specified parts or provisions of Article 9 (e.g., part 6,
24 dealing with enforcement; or Section 9-609, dealing with self-help repossession)
25 inapplicable to governmental entities, regardless of the existence of conflicting law.

26 **8. Sales of Payment Intangibles.** Former Section 9-104(f) excludes
27 certain sales and assignments of accounts and chattel paper. Subsection (c)(7) adds
28 to the exclusion similar sales of payment intangibles.

29 **9. Insurance.** Subsection (c)(8) narrows somewhat the broad exclusion of
30 interests in insurance policies under former Section 9-104(g). This Article now
31 covers transfers by a healthcare provider of rights to payment arising out of the
32 furnishing of healthcare goods or services. These rights to payment are the
33 equivalent of accounts receivable for other types of businesses. The Drafting
34 Committee recognizes that insurance policies can be important items of collateral in
35 many other business contexts and that the "cash" or "loan" value of life insurance
36 policies also can be a useful source of collateral for borrowing by individuals.
37 Nevertheless, it decided that other law should continue to govern security interests
38 in insurance policies.

39 **10. Setoffs.** Subsection (c)(10) adds two exceptions to the general
40 exclusion of setoff rights from Article 9 under former subsection (i). The first takes
41 account of new Section 9-337, which regulates the effectiveness of a setoff against
42 a deposit account that stands as collateral. The second recognizes Section 9-404,
43 which affords the obligor on an account, chattel paper, or general intangible the
44 right to raise claims and defenses against an assignee/secured party.

1 **11. Tort Claims.** Subsection (c)(12) narrows somewhat former broad
2 exclusion of transfers of tort claims under former Section 9-104(k). This Article
3 now applies to transfers of “commercial tort claims, as defined in Section 9-102,
4 as well as to security interests in tort claims that constitute proceeds of other
5 collateral (e.g., a right to payment for negligent destruction of the debtor’s
6 inventory). The Official Comments should make clear that once a claim arising in
7 tort has been settled and reduced to a contractual obligation to pay, the right to
8 payment becomes a payment intangible and no longer is a claim arising in tort.

9 The Article contains two special rules governing creation of a security
10 interest in tort-claim collateral. First, a tort claim must be described with
11 specificity in a security agreement as a condition of attachment. See Section
12 9-111(e). Second, no security attaches under an after-acquired property clause to a
13 tort claim. See Section 9-204(b)(2). In addition, this Article does not determine
14 whom the tortfeasor must pay to discharge its obligation. Inasmuch as a tortfeasor
15 is not an “account debtor, the rules governing waiver of defenses and discharge of
16 an obligation by an obligor (Sections 9-403; 9-404) are inapplicable to tort-claim
17 collateral.

18 **12. Deposit Accounts.** With certain exceptions set forth in paragraphs (16)
19 and (17) of subsection (c), deposit accounts may be taken as original collateral
20 under this Article. Under the former Article, which excludes deposit accounts as
21 original collateral, security interests in deposit accounts generally are governed by
22 the common law. The common law is nonuniform, often difficult to discover and
23 comprehend, and frequently costly to implement. As a consequence, debtors who
24 wish to use deposit accounts as collateral sometimes are precluded from doing so as
25 a practical matter.

26 This Article contains several safeguards to protect debtors against
27 inadvertently encumbering deposit accounts and to reduce the likelihood that a
28 secured party will realize a windfall from the debtor’s deposit accounts. For
29 example, because “deposit accounts” is a separate type of collateral, a security
30 agreement covering general intangibles will not adequately describe deposit
31 accounts. Rather, a security agreement must reasonably identify the deposit
32 accounts that are the subject of a security interest, e.g., by using the term “deposit
33 accounts. See Section 9-111. To perfect a security interest in a deposit account as
34 original collateral, a secured party (other than the depository institution with which
35 the deposit account is maintained) must take “control” of the account either by
36 obtaining the depository institution’s written agreement or by putting the funds into
37 its own account. See Sections 9-310(a)(2); 9-109. Either of these steps requires the
38 debtor’s consent.

39 This Article also contains new rules that determine which State’s law
40 governs perfection and priority of a security interest in a deposit account, see
41 Section 9-304, priority of conflicting security interests in a deposit account, see
42 Sections 9-325; 9-337, the rights of transferees of funds from an encumbered
43 deposit account, see Section 9-329, the obligations of the depository institution, see
44 Section 9-338, and enforcement of security interests in a deposit account. See
45 Section 9-607(c).

SECTION 9-113.

[deleted]

SECTION 9-114.

[deleted]

Reporters' Comments

Reason for Deletion. This section, which tracked former Section 9-111, provided that the creation of a security interest is not a bulk sale under Article 6. It would have served no function in the majority of States, which have repealed Article 6. In the few States that adopted Revised Article 6, this section would be superfluous. See Section 6-103(3)(a) (containing similar provision). The same is true even in those States in which old Article 6 is in effect. See old Section 6-103(1) (containing similar provision). Accordingly, this section has been deleted.

SECTION 9-115. APPLICABILITY OF OTHER STATUTES.

(a) A transaction subject to this article may also be subject to [insert reference to any local statute regulating small loans, retail installment sales and the like].

(b) In case of conflict between this article and that statute, the statute controls. Failure to comply with an applicable statute has only the effect the statute specifies.

Reporters' Comments

1. Source. Former Section 9-203(4)

2. **Purpose.** This section makes clear that certain transactions, although subject to this Article, also must comply with other applicable legislation. The Drafting Committee may wish to consolidate these provision with those of Section 9-201.

**SECTION 9-116. SECURITY INTERESTS ARISING UNDER
ARTICLES 2 OR 2A. *[MINOR STYLE CHANGES ONLY]***

(a) A security interest arising solely under Article 2 or 2A is subject to this article.

1 (b) ~~To However,~~ to the extent that, and as long as, the debtor does not have
2 or does not lawfully obtain possession of the goods:

3 (1) a security agreement is not necessary to make the security interest
4 enforceable;

5 (2) filing is not required to perfect the security interest; and

6 (3) the rights of the secured party on default by the debtor are governed
7 by Article 2 or 2A in the case of a security interest arising solely under one of those
8 Articles thereunder.

9 Reporters' Comments

10 1. **Source.** Former Section 9-113.

11 2. **Status.** The Article 2 Drafting Committee has yet to determine whether
12 any rights arising under Article 2 will be characterized as security interests and, if
13 so, which ones. Once that determination is made, the Article 9 Drafting Committee
14 will consider how to address those security interests, and any security interests
15 arising under revised Article 2A, in this Article.

PART 2
**VALIDITY OF SECURITY AGREEMENT;
ATTACHMENT OF SECURITY INTEREST;
RIGHTS OF PARTIES TO SECURITY AGREEMENT**

[SUBPART 1. VALIDITY AND ATTACHMENT]

**SECTION 9-201. GENERAL ~~VALIDITY~~ EFFECTIVENESS OF
SECURITY AGREEMENT. ~~MINOR STYLE CHANGES ONLY~~**

(a) Except as otherwise provided in [the Uniform Commercial Code], a security agreement is effective according to its terms between the parties, against purchasers of the collateral, and against creditors.

(b) Nothing in this article:

(1) validates any charge or practice illegal under any statute or regulation governing usury, small loans, retail installment sales, or the like; or

(2) extends the application of the statute or regulation to a transaction not otherwise subject to it.

[(c) A transaction subject to this article is also subject to any applicable law which establishes a different rule for consumers.]

[(d) With respect to [the Uniform Commercial Code], failure to comply with the laws referred to in subsection (c) has only the effect specified therein.]

Reporters' Comments

1. **Source.** Former Section 9-201.

2. **Laws applicable to consumer transactions.** Subsections (c) and (d), which appear in brackets, derive from Section 2-104 of the 1997 Annual Meeting Draft of Article 2. They reflect a more complete statement of what is implicit in subsection (b)(1). The Drafting Committee may wish to consolidate these provisions with those of Section 9-115.

SECTION 9-202. TITLE TO COLLATERAL IMMATERIAL. Except as otherwise provided with respect to consignments or sales of accounts, chattel paper,

1 or payment intangibles, the provisions of this article with regard to rights,
2 obligations, and remedies apply whether title to collateral is in the secured party or
3 in the debtor.

4 Reporters' Comments

5 1. **Source.** Former Section 9-202.

6 2. **When Title Matters.** This section explicitly acknowledges two
7 circumstances in which the effect of certain Article 9 provisions turns on ownership
8 (title). First, the remedies of a consignor under a true consignment and, for the
9 most part, the remedies of a buyer of accounts, chattel paper, or payment
10 intangibles are determined by other law and not by part 6. See Section 9-601(d).
11 Second, in some respects sales of accounts, chattel paper, and payment intangibles
12 receive special treatment. See, e.g., Sections 9-207(a); 9-209(b); 9-607(b). Buyers
13 of receivables under the former Article are treated specially, as well. See, e.g.,
14 former Section 9-502(2).

15 **SECTION 9-203. ATTACHMENT AND ENFORCEABILITY OF**
16 **SECURITY INTEREST; PROCEEDS; SUPPORT OBLIGATIONS;**
17 **FORMAL REQUISITES.**

18 (a) Except as otherwise provided in subsections (c), (d), and (e), and
19 ~~Subject to~~ Section 4-210 on the security interest of a collecting bank, Section 5-118
20 [on the security interest of a letter of credit issuer or nominated person], Section
21 9-206 [on security interests in investment property], Section 9-116 [on a security
22 interest arising under Article 2 or 2A], ~~and subsection (b)~~, a security interest is ~~not~~
23 enforceable against the debtor and ~~or~~ third parties with respect to the collateral only
24 if and does not attach unless:

25 (1) (A) the debtor has authenticated a security agreement that ~~contains~~
26 provides a description of the collateral and, if the security interest covers timber to
27 be cut, a description of the land concerned;

28 (B) the collateral is in the possession of the secured party under
29 Section 9-311 pursuant to the debtor's agreement; or

1 (C) the collateral is investment property, a deposit account, or a
2 letter-of-credit rights ~~and proceeds of the letter of credit~~ and the secured party has
3 control pursuant to the debtor's agreement;

4 (2) value has been given; and

5 (3) the debtor has rights in the collateral or the power to transfer rights
6 in the collateral to a secured party.

7 (b) A security interest is created in, and attaches to, collateral when it
8 becomes enforceable against the debtor with respect to the collateral, unless an
9 explicit agreement postpones the time of creation or attachment.

10 (c) A person becomes bound as debtor by a security agreement entered into
11 by another person if, by operation of other law or by contract:

12 (1) the security agreement becomes effective to create a security interest
13 in the person's property; or

14 (2) the person:

15 (A) becomes generally obligated for the obligations of the other
16 person, including the obligation secured under the security agreement; and

17 (B) acquires or succeeds to all or substantially all of the assets of the
18 other person.

19 ~~(d)~~ (b) If a new debtor becomes bound as debtor by a security agreement
20 entered into by another person:

21 (1) the agreement satisfies the requirements of subsection (a)(1) ~~as~~ with
22 respect to existing or after-acquired property of the new debtor to the extent the
23 property is described in the agreement; and

24 (2) another agreement is not necessary to make a security interest in the
25 property enforceable.

~~(d) A security interest attaches when it becomes enforceable against the debtor with respect to the collateral. Attachment occurs as soon as all of the events specified in subsection (a) have occurred unless the time of attaching is postponed by express agreement.~~

(e) [Unless otherwise agreed, the] [The] attachment of a security interest in:

(1) collateral ~~a security agreement~~ gives the secured party the rights to proceeds provided by Section 9-313;

(2) attachment of a security interest in collateral is also attachment of a security interest in support obligation with respect to the collateral;

(3) ~~attachment of a security interest in a securities account is also~~
attachment of a security interest in security entitlements carried in the securities
account;

(4) ~~attachment of a security interest in a commodity account is also~~
attachment of a security interest in all commodity contracts carried in the
commodity account; and

(5) ~~attachment of a security interest in a right to payment or performance secured by a [mortgage on real property] [lien on property] gives the secured party~~ is also attachment of a security interest in the [mortgage] [lien].

~~(f) a security interest does not attach to a letter of credit or proceeds of a letter of credit unless it has attached to the collateral that the letter of credit supports.~~

Reporters' Comments

Change from Prior Draft: For clarity, as marked. Note also that the paragraphs of subsection (a) have been reordered.

1. **Source.** Former Sections 9-203 and 9-115(2), (6).

2. Requirement for Agreement. Subsection (a)(1) clarifies two points. First, for purposes of this subsection, the secured party’s possession must be obtained with the debtor’s agreement. “Pursuant to agreement” in this subsection

1 refers to the debtor's agreement to the secured party's possession for the purpose of
2 creating a security interest. In the unlikely event that possession is obtained without
3 the debtor's agreement, it would not suffice as a substitute for an authenticated
4 security agreement. However, once the security interest has become enforceable
5 and has attached, it is not impaired by the fact that the secured party's possession is
6 maintained without the agreement of a subsequent debtor (e.g., a transferee).
7 Second, possession as contemplated by Section 9-311 is possession for purposes of
8 subsection (a), even though it may not constitute possession "pursuant to the
9 debtor's agreement" and consequently might not serve as a substitute for an
10 authenticated security agreement under subsection (a).

11 Subsection (a)(1) also provides that control of investment property, a
12 deposit account, or letter-of-credit rights pursuant to the debtor's agreement is
13 sufficient as a substitute for an authenticated security agreement.

14 **3. Collateral Covered by Other Statute or Treaty.** One purpose of the
15 formal requisites stated in subsection (a)(1) is evidentiary—to minimize the
16 possibility of future disputes as to the terms of a security agreement and as to what
17 property stands as collateral for the obligation secured. One should distinguish the
18 evidentiary functions of the formal requisites of attachment and enforceability (such
19 as the requirement that a security agreement contain a description of the collateral)
20 from the more limited goals of "notice filing" for financing statements under Part 5,
21 explained in former Section 9-402, Official Comment 3. When perfection is
22 achieved by compliance with the requirements of a statute or treaty described in
23 Section 9-309(c), such as a federal recording act or a certificate-of-title act, the
24 manner of describing the collateral in a registry imposed by the statute or treaty may
25 or may not be adequate for purposes of this section and Section 9-111. However,
26 the description contained in the security agreement, not the description in a public
27 registry or on a certificate of title, controls for purposes of this section.

28 **4. Exception to General Rule.** Section 5-118, mentioned in subsection
29 (a), is found in the Appendix.

30 **5. Attachment to Limited Rights.** Subsection (a)(3) conditions
31 attachment on the debtor's having "rights in the collateral or the power to transfer
32 rights in the collateral to a secured party." A debtor's limited rights in collateral,
33 short of full ownership, are sufficient for a security interest to attach. However, in
34 accordance with basic personal property conveyancing principles, the baseline rule
35 is that a security interest attaches only to whatever rights a debtor may have, broad
36 or limited as those rights may be.

37 **6. Attachment to Greater Rights than Debtor Has.** Certain exceptions
38 to this baseline rule enable a debtor to transfer, and a security interest to attach to,
39 greater rights than the debtor has. The bracketed phrase, "or the power to transfer
40 rights in the collateral to a secured party," accommodates those exceptions. In
41 some cases, a debtor may have power to transfer another person's rights to a class
42 of transferees that excludes secured parties. See, e.g., Section 2-403(2) (giving
43 certain merchants power to transfer an entruster's rights to a buyer in ordinary
44 course of business). Under those circumstances, the debtor would not have the
45 power to create a security interest in the other person's rights.

1 **7. New Debtors.** New subsection (b) makes clear that the enforceability
2 requirements of subsection (a)(1) are met when a new debtor becomes bound under
3 an original debtor's security agreement. If a new debtor "becomes bound as
4 debtor by a security agreement entered into by another person, the security
5 agreement satisfies the requirement of Section 9-203(a)(1) as to the existing and
6 after-acquired property of the new debtor to the extent the property is described in
7 the agreement.

8 Subsection (c) explains when a new debtor "becomes bound. Persons who
9 "become[] bound under paragraph (2) are limited to those who both become
10 primarily liable for the original debtor's obligations and succeed to (or acquire) its
11 assets. Thus, the paragraph excludes sureties and other secondary obligors as well
12 as persons who become obligated through veil piercing and other non-successorship
13 doctrines. In many cases, paragraph (2) will exclude successors to the assets and
14 liabilities of a division of a debtor.

15 This subject is discussed in more detail in the Comments to Section 9-510.

16 **8. Support Obligations.** Under new subsection (e)(2), a security interest
17 in a "support obligation (defined in Section 9-102) automatically follows from a
18 security interest in the underlying, supported collateral. We believe this to be
19 implicit in current law.

20 Implicit in subsection (e)(2) is the principle that the secured party's interest
21 in a support obligation extends to the support obligation only to the extent that it
22 supports the collateral in which the secured party has a security interest. Complex
23 issues may arise, however, if a support obligation supports many separate
24 obligations of a particular account debtor and if the obligations are separately
25 assigned as security to several secured parties. The problems may be exacerbated if
26 a support obligation is limited to an aggregate amount that is less than the aggregate
27 amount of the obligations it supports. This Article does not contain provisions
28 dealing with competing claims to a limited support obligation. As under former
29 law, the law of suretyship and the agreements of the parties will control.

30 **9. Real Estate Mortgages.** Subsection (e)(5) codifies the common-law
31 rule that a transfer of an obligation secured by a mortgage also transfers the
32 mortgage. See Restatement (3d) of the Law of Property (Mortgages) § 5.4(a)
33 (1997). The Drafting Committee has not yet considered whether this approach
34 should be extended beyond real estate mortgages to any other "lien on property.

35 **SECTION 9-204. AFTER-ACQUIRED PROPERTY; FUTURE** 36 **ADVANCES.**

37 (a) Except as otherwise provided in subsection (b), a security agreement
38 may create or provide for a security interest in after-acquired collateral.

1 (b) A security interest does not attach under an after-acquired property
2 clause to:

3 (1) consumer goods, other than an accession when given as additional
4 security, unless the debtor acquires rights in them within 10 days after the secured
5 party gives value; or

6 (2) a commercial tort claim.

7 (c) A security agreement may provide that collateral secures₂ or that
8 accounts, chattel paper, or payment intangibles are sold in connection with₂ future
9 advances or other value, whether or not the advances or value are given pursuant to
10 commitment.

11 Reporters' Comments

12 1. **Source.** Former Section 9-204.

13 2. **Sales of Receivables.** This Article validates “after-acquired property
14 and “future advance” clauses in security agreements not only when the transaction
15 is for security purposes but also when the transaction is the sale of accounts, chattel
16 paper, or payment intangibles. We understand this to be the case under existing
17 law.

18 3. **Commercial Tort Claims.** New subsection (b)(2) provides that an
19 after-acquired collateral provision in a security agreement does not reach future
20 commercial tort claims. In order for a security interest in a tort claim to attach, the
21 claim must be in existence when the security agreement is authenticated. In
22 addition, the security agreement must describe the tort claim with specificity. See
23 Section 9-111(e).

1 (a) (1) A security interest in favor of a securities intermediary attaches to a
2 person's security entitlement if:

3 (A) ~~the~~ If a person buys a financial asset through a securities
4 intermediary in a transaction in which the person ~~buyer~~ is obligated to pay the
5 purchase price to the securities intermediary at the time of the purchase; and

6 (B) the securities intermediary credits the financial asset to the
7 buyer's securities account before the buyer pays the securities intermediary; ~~the~~
8 ~~securities intermediary has a security interest in the buyer's security entitlement~~
9 ~~securing the buyer's obligation to pay.~~

10 (2) The security interest secures the person's obligation to pay for the
11 financial asset.

12 (b) (1) A security interest in favor of a person that delivers ~~If~~ a certificated
13 security; or other financial asset represented by a writing attaches to the security or
14 other financial asset if:

15 (A) the security or other financial asset is:

16 (i) ~~which~~ in the ordinary course of business ~~is~~ transferred by
17 delivery with any necessary indorsement or assignment; and

18 (ii) ~~is~~ delivered under an agreement between persons in the
19 business of dealing with such securities or financial assets; and

20 (B) the agreement calls for delivery versus payment; ~~the person~~
21 ~~delivering the certificate or other financial asset has a security interest in the~~
22 ~~certificated security or other financial asset securing the seller's right to receive~~
23 ~~payment.~~

24 (2) The security interest secures the person's obligation to make
25 payment to the seller.

~~(c) A security agreement is not required for attachment or enforceability of a security interest arising under this section.~~

Reporters' Comments

Change from Prior Draft: Subsections (a) and (b) now refer to attachment of a security interest. Attachment under this section has the same consequences (right to proceeds, etc.) as attachment under § 9-203. Subsection (c) has been deleted as unnecessary. This section overrides the general attachment rules in § 9-203. See § 9-203(a).

1. **Source.** Former 9-116.

2. Automatic Perfection. Security interests arising under this section are automatically perfected. See Section 9-309(a).

[SUBPART 2. RIGHTS AND DUTIES]

SECTION 9-207. RIGHTS AND DUTIES IF COLLATERAL IS IN SECURED PARTY'S POSSESSION.

(a) (1) A secured party shall use reasonable care in the custody and
preservation of collateral in the secured party's possession if:

(A) a security interest secures an obligation; or

(B) a buyer of accounts, chattel paper, or payment intangibles is

entitled by agreement:

(i) to charge back uncollected collateral; or

(ii) otherwise to full or limited recourse against the debtor or a

~~secondary obligor, the secured party shall use reasonable care in the custody and preservation of collateral in the secured party's possession~~ based on the nonpayment or other default of an account debtor or other obligor on the collateral.

(2) In the case of an instrument or chattel paper, reasonable care includes taking necessary steps to preserve rights against prior parties unless otherwise agreed.

1 (b) [Unless otherwise agreed, if] [If] a security interest secures an
2 obligation and collateral is in the secured party's possession:

3 (1) reasonable expenses, including the cost of any insurance and
4 payment of taxes or other charges, incurred in the custody, preservation, use, or
5 operation of the collateral are chargeable to the debtor and are secured by the
6 collateral;

7 (2) the risk of accidental loss or damage is on the debtor to the extent of
8 a deficiency in any effective insurance coverage;

9 (3) the secured party:

10 (A) may hold as additional security any increase or profits, except
11 money, received from the collateral;

12 (B) shall apply but money so received under paragraph (3)(A) to
13 reduce the secured obligation, unless remitted to the debtor, ~~must be applied to~~
14 ~~reduce the secured obligation~~;

15 (C) ~~the secured party~~ shall keep the collateral identifiable, but
16 fungible collateral may be commingled; and

17 (D) ~~the secured party~~ may create a security interest in the collateral.

18 (c) If a security interest secures an obligation, the secured party may use or
19 operate collateral:

20 (1) for the purpose of preserving the collateral or its value;

21 (2) ~~or~~ as permitted by an order of a court of appropriate jurisdiction

22 or

23 (3) except in the case of consumer goods, in the manner and to the
24 extent agreed by the debtor ~~provided in the security agreement~~.

25 Reporters' Comments

26 1. **Source.** Former Section 9-207.

1 2. **Statutory Liens.** The revised definitions of “collateral,” “debtor,” and
2 “secured party” in Section 9-102 would make this section applicable to collateral
3 subject to a statutory lien if the collateral is in the statutory lienholder’s possession.
4 The Drafting Committee has not yet considered whether that result is appropriate.

5 3. **Buyers of Chattel Paper and Other Receivables.** This section has
6 been revised to reflect the fact that a seller of accounts, chattel paper, or payment
7 intangibles normally retains no interest in the collateral and so is not disadvantaged
8 by the secured party’s noncompliance with the requirements of this section.
9 Subsection (a) applies only to security interests that secure an obligation and to
10 sales of receivables in which the buyer has recourse against the debtor. (Of course,
11 a buyer of accounts or payment intangibles could not have “possession” of original
12 collateral, but might have possession of proceeds, such as promissory notes or
13 checks.) The meaning of “recourse” in this respect is limited to recourse arising out
14 of the account debtor’s failure to pay or other default. The other subsections are
15 inapplicable to all sales of receivables.

16 4. **“Repledges.”** The change to subsection (b)(5) eliminates the
17 qualification that the terms of a “repledge” may not “impair” a debtor’s “right to
18 redeem” collateral. The change is for clarification only.

19 There is no basis on which to draw from subsection (b)(5) any inference
20 concerning the debtor’s right to redeem the collateral. The debtor enjoys that right
21 under Section 9-621, and this section need not address it. For example, if the
22 collateral is a negotiable note that the secured party (SP-1) repledges to SP-2,
23 nothing in this section suggests that the debtor (D) does not retain the right to
24 redeem the note upon payment to SP-1 of all obligations secured by the note. But,
25 as explained below, the debtor’s unimpaired right to redeem as against the debtor’s
26 original secured party nevertheless may not be enforceable as against the new
27 secured party.

28 In resolving questions that arise from the creation of a security interest by
29 SP-1, one must take care to distinguish D’s rights against SP-1 from D’s rights
30 against SP-2. Once D discharges the secured obligation, under Section 9-621 or
31 otherwise, D becomes entitled to the note; SP-1 has no legal basis upon which to
32 withhold it. If, as a practical matter, SP-1 is unable to return the note because SP-2
33 holds it as collateral for SP-1’s unpaid debt, then SP-1 is liable to D under the law
34 of conversion.

35 Whether SP-2 would be liable to D depends on the priority of SP-2’s
36 security interest. Normally, the *nemo dat* principle will apply, and SP-2’s security
37 interest, which is a security interest in SP-1’s security interest, will be defeated if
38 the debtor discharges its secured obligations under Section 9-621 or otherwise. If
39 so, and if SP-2 fails to deliver the note to D, then D will have a right to replevy the
40 note from SP-2 or recover damages from SP-2 in conversion. In some
41 circumstances, however, SP-2’s security interest will survive discharge of SP-1’s
42 security interest. This will be the case, for example, if SP-2 is a holder in due
43 course. See Sections 9-328, 3-306. Under these circumstances, D has no right to
44 recover the note or recover damages from SP-2. Nevertheless, D will have a
45 damage claim against SP-1.

1 This section does not change existing law in this regard, but rather
2 eliminates a possible ambiguity. Former Section 9-207(2)(e) permits the secured
3 party to “repledge the collateral upon terms that do not impair the debtor’s right to
4 redeem it. This language could be read to override the rule of Section 9-328,
5 under which a qualifying SP-2 takes its security interest free of D’s interest in the
6 collateral. This language also could be read to prohibit SP-1 from creating a
7 security interest to secure a debt owed to SP-2 that is larger than the debt owed by
8 D to SP-1. Both readings are erroneous. Subsection (b)(5) makes clear that
9 nothing in this Article, including subsection (a), prohibits or restricts a secured
10 party from creating, as a debtor, a security interest in collateral in which it holds a
11 security interest. Subsection (b)(5) does not, by negative implication, prohibit or
12 render ineffective a security interest created by a secured party in collateral that is
13 not in the secured party’s possession.

14 **SECTION 9-208. DUTIES OF SECURED PARTY HAVING CONTROL**
15 **OVER COLLATERAL.**

16 (a) This section applies if:

17 (1) ~~if~~ there is no outstanding secured obligation; and

18 (2) the secured party has no commitment to make advances, incur
19 obligations, or otherwise give value

20 (b) ~~as~~ soon as reasonably practicable₂ but not more than [three business]
21 [six] days₂ after receiving an authenticated demand by the debtor a secured party
22 that has control over:

23 (1) ~~a~~ investment property under Section 8-106(d)(2) or 9-108(b) shall
24 send the securities intermediary or commodity intermediary with which the security
25 entitlement or commodity contract is maintained an authenticated record that
26 releases the securities intermediary or commodity intermediary from any further
27 obligation to comply with entitlement orders or directions originated by the secured
28 party;

29 (2) ~~a secured party that has control over~~ a deposit account under Section
30 9-109(a)(2) shall send the depository institution with which the deposit account is

maintained an authenticated statement that releases the depositary institution from any further obligation to comply with instructions originated by the secured party;

~~[(3) a secured party that has control over a deposit account under Section 9-109(a)(3) shall:~~

~~(A) pay the debtor the balance ~~all funds~~ on deposit in the deposit account; or~~

~~(B) transfer the balance on deposit into a deposit account in the debtor's name; and~~

~~(4) a secured party that has control over a letter-of-credit rights and proceeds of the letter of credit under Section 9-110(1) shall send to each any person that has an unfulfilled obligation to pay or deliver proceeds of the letter of credit to the secured party an authenticated release from any further obligation to pay or deliver proceeds of the letter of credit to the secured party.~~

~~(b) Within [a reasonable time] [10 days] after receiving an authenticated demand by the debtor pursuant to subsection (a), a secured party that has control over a letter of credit and proceeds of the letter of credit under Section 9-110(2) shall take such actions as the debtor may reasonably request with respect to the letter of credit.~~

Reporters' Comments

1. **Source.** New.

2. **Scope.** This section imposes duties on a secured party that has control over investment property, a deposit account, or letter-of-credit rights. The duty to terminate the secured party's control is analogous to the duty to file a termination statement, imposed by Section 9-511.

The requirements of this section can be varied by agreement under Section 1-102(3). For example, a debtor could by contract agree that the secured party may release its control over investment property under subsection (a)(1) more than three days following demand. Also, these requirements should not be read to conflict with the terms of the collateral itself. In this connection, subsection (a)(3), which appears in brackets, may be problematic. If the collateral is a time deposit account, for example, subsection (a)(3) should not require a secured party with control to

1 make an early withdrawal of the funds (assuming that is even possible) in order to
2 pay them over to the debtor or put them in an account in the debtor's name.

3 **3. Remedy for Failure to Relinquish Control.** If the secured party fails to
4 comply with the requirements of subsection (a), the debtor has the remedy set forth
5 in Section 9-624(d). This remedy is identical to that applicable to failure to provide
6 or file a termination statement under Section 9-511.

7 **4. Duty to Relinquish Possession.** Although Section 9-207 and former
8 Section 9-207 address directly the duties of a secured party in possession of
9 collateral, neither requires the secured party to relinquish possession when the
10 secured party ceases to hold a security interest. Under common law, absent
11 agreement to the contrary, the failure to relinquish possession of collateral upon
12 satisfaction of the secured obligation would constitute a conversion. This Article
13 could impose an explicit duty to relinquish possession. But inasmuch as problems
14 apparently have not surfaced in the absence of such duties under current law, the
15 common-law duty appears to be sufficient.

16 **5. Duty to "Send."** This section and Sections 9-208A and 9-209 impose a
17 duty to "send" certain items or information to the debtor. The Drafting Committee
18 may wish to consider whether that term should be replaced in these sections by the
19 new term "communicate," as defined in Section 9-102.

20 **SECTION 9-208A. DUTIES OF SECURED PARTY ~~{WHEN}~~{IF}**
21 **ACCOUNT DEBTOR HAS BEEN NOTIFIED OF ASSIGNMENT.**

22 (a) Except as otherwise provided in subsection (c), this section applies if:

23 (1) ~~if~~ there is no outstanding secured obligation; and

24 (2) the secured party has no commitment to make advances, incur
25 obligations, or otherwise give value.

26 (b) As ~~as~~ soon as reasonably practicable, but not more than 3 [three
27 business] [six] days, after the secured party receives an authenticated demand by
28 the debtor, the secured party shall send to an account debtor that has received
29 notification of an assignment to the secured party as assignee under Section
30 9-404(e) an authenticated record that releases the account debtor from any further
31 obligation to the secured party.

32 (c) ~~b~~) This section does not apply to an assignment constituting the sale of
33 an account, chattel paper, or payment intangible.

1. **Source.** New.

2. **Scope.** Like Sections 9-208 and 9-511(c), which require a secured party to relinquish control of collateral and to file or provide a termination statement for a financing statement, this section requires a secured party to free up collateral when there no longer is any outstanding secured obligation or any commitment to give value in the future. This section addresses the case in which account debtors have been notified to pay a secured party to whom the receivables have been assigned. It requires the secured party (assignee) to inform the account debtors that they no longer are obligated to make payment to the secured party.

**SECTION 9-209. REQUEST FOR ACCOUNTING; REQUEST
REGARDING LIST OF COLLATERAL OR STATEMENT OF ACCOUNT.**

(a) In this section:

(1) "Request for an accounting" means a record authenticated by a debtor requesting that the recipient provide an accounting of the unpaid obligations secured by collateral and reasonably identifying the transaction or relationship that is the subject of the request.

(2) "Request regarding a list of collateral" means a record authenticated by a debtor requesting that the recipient approve or correct a list of what the debtor believes to be the collateral securing an obligation and reasonably identifying the transaction or relationship that is the subject of the request.

(3) "Request regarding a statement of account" means a record authenticated by a debtor requesting that the recipient approve or correct a statement indicating what the debtor believes to be the aggregate amount of unpaid obligations secured by collateral as of a specified date and reasonably identifying the transaction or relationship that is the subject of the request.

(4) "Request" means a record of a type described in paragraphs (1), (2), or (3).

1 (b) (1) Subject to subsections (c), (d), and (e), a secured party ~~other than a~~
2 ~~buyer of accounts, chattel paper, or payment intangibles~~ shall comply with a request
3 ~~for an accounting, a request regarding a list of collateral, or a request regarding a~~
4 ~~statement of account~~ within two weeks after receipt by authenticating and sending
5 to the debtor ~~an authenticated~~ a correction or approval or an accounting, as
6 applicable.

7 (2) This subsection does not apply to a secured party that is a buyer of
8 accounts, chattel paper, or payment intangibles.

9 (c) A secured party that claims a security interest in all of a particular type
10 of collateral owned by the debtor may comply with a request regarding a list of
11 collateral by sending to the debtor an authenticated statement to that effect within
12 two weeks after receipt.

13 (d) (1) This subsection applies to a ~~A~~ person that:

14 (A) receives a request regarding a list of collateral; ~~and~~

15 (B) claims no interest in the collateral when it receives the request;

16 and

17 (C) claimed an interest in the collateral at an earlier time.

18 (2) The person shall comply with the request within two weeks after
19 receipt by sending to the debtor an authenticated [record] [statement]:

20 (A) disclaiming any interest in the collateral; and

21 (B) if known to the recipient, containing the name and mailing
22 address of any assignee of or successor to the recipient's security interest in the
23 collateral.

24 (e) (1) This subsection applies to a ~~A~~ person that:

25 (A) receives a request for an accounting or a request regarding a
26 statement of account;

1 (B) claims no interest in the obligations when it receives the a
2 request; and for an accounting or a request regarding a statement of account

3 (C) claimed an interest in the obligations at an earlier time.

4 (2) The person shall comply with the request within two weeks after
5 receipt by sending to the debtor an authenticated [record] [statement]:

6 (A) disclaiming any interest in the obligations; and

7 (B) if known to the recipient, containing the name and mailing
8 address of any assignee of or successor to the recipient's interest in the obligations.

9 (f) A debtor is entitled without charge to one response to a request an
10 approval or correction or an accounting under this section once during any six-
11 month period. The secured party may require payment of a charge not exceeding
12 \$[] for each additional response to a request.

13 Reporters' Comments

14 **Change to Prior Draft:** Subsection (f) has been revised to make clear that,
15 during a six-month period, a debtor is entitled to one free response from the secured
16 party. The debtor is not entitled to a free response to each type of request (i.e.,
17 maximum of three responses).

18 1. **Source.** Former Section 9-208.

19 2. **Scope.** This section resolves some of the issues that have arisen under
20 former Section 9-208 and makes information concerning the secured indebtedness
21 readily available to debtors, both before and after default. It applies to statutory-
22 lien transactions (see the definitions of “debtor, secured party, and “collateral in
23 Section 9-102) but generally not to sales of receivables. See subsection (b).

24 Subsection (a) contemplates that the debtor can request three types of
25 information from the secured party. First, under subsection (a)(1), the debtor can
26 request the secured party to prepare and send an “accounting as defined in Section
27 9-102. Second, under subsection (a)(2), the debtor can submit to the secured party
28 a list of collateral for the secured party's approval or correction. Third, under
29 subsection (a)(3), the debtor can submit to the secured party for its approval or
30 correction a statement of the aggregate amount of unpaid secured obligations.
31 Inasmuch as a secured party may have numerous transactions and relationships with
32 a debtor, each request must identify the relevant transactions or relationships.
33 Problems may arise for secured parties that have many places of business and who
34 may receive a request at a place of business having no relation to the secured
35 transaction. We believe that problem could be addressed best by modifications to
36 Section 1-201(26) and (27). Those provisions should be expanded to address not

1 only notifications but also demands and other records that may be received by an
2 organization.

3 **3. Recipients Claiming No Interest in the Transaction.** A debtor may be
4 unaware that the creditor with whom it has dealt has assigned its security interest or
5 the secured obligation. Subsections (d) and (e) impose upon recipients of requests
6 under this section the duty to inform the debtor that they claim no interest in the
7 collateral or secured obligation, respectively, and to inform the debtor of the name
8 and mailing address of any known assignee or successor.

9 **4. Remedy for Failure to Comply.** Section 9-624(e) sets forth the remedy
10 for noncompliance with the requirements of this section.

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PART 3
PERFECTION AND PRIORITY OF SECURITY INTERESTS
[SUBPART 1. LAW GOVERNING PERFECTION AND PRIORITY]

Reporters’ Prefatory Comment

1. **Scope of Choice-of-Law Rules.** Part 3, Subpart 1 contains choice-of-law rules similar to those of former Section 9-103. Former Section 9-103 generally addresses which State’s law governs “perfection and the effect of perfection or non-perfection of security interests. See, e.g., former Section 9-103(1)(b). This Article follows the broader and more precise formulation in former Section 9-103(6)(b), which was revised in connection with the recent promulgation of Revised Article 8: “perfection, the effect of perfection or non-perfection, and the priority of security interests. Priority, in this context, subsumes all of the rules in Part 3, including “cut off” or “take free” rules such as Sections 9-315(a), (b), and (c), 9-316, and 9-328. This subpart does not address choice of law for other purposes. For example, the law applicable to issues such as attachment, validity, characterization (e.g., true lease or security interest), and enforcement would be governed by the rules in Section 1-105; that governing law typically is specified in the same agreement that contains the security agreement. And, another jurisdiction’s law may govern other third-party matters addressed in Article 9. See Part 4, Reporters’ Prefatory Comment.

2. **Scope of Referral.** In designating the jurisdiction whose law governs, this Article directs the court to apply only the substantive (“local”) law of a particular jurisdiction and not its choice-of-law rules.

Example: Litigation over the priority of a security interest in accounts arises in State X. State X has adopted the Official Text of this Article, which sends one to the local law of the jurisdiction in which the debtor is located. See Section 9-301(3). The debtor is located in State Y. Even if State Y has enacted a nonuniform choice-of-law rule (e.g., one that provides that perfection is governed by the law of State Z), a State X court should look only to the substantive law of State Y. State Y’s substantive law indicates that financing statements should be filed in State Y. Note, however, that 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 a filing in State Y is ineffective. Revision of the Official Text cannot eliminate this problem. A complete solution would require complete uniformity in the enacted text.

Eliminating the reference to the choice-of-law rules is likely to minimize the impact of the nonuniformity. Under former Section 9-103(3), which refers to “the law (including the conflict of laws rules) of a jurisdiction, every time a uniform provision refers one to State Y, one winds up having to file in State Z. Inasmuch as there have been relatively few nonuniform amendments to Section 9-103, lawyers are likely to file in State Y without first checking State Y’s choice-of-laws rules. If this Article, which eliminates the reference to choice-of-laws rules, is widely adopted, then these lawyers will have filed properly if the issue is litigated in any

1 jurisdiction that has adopted a uniform Section 9-301 (i.e., in most jurisdictions
2 other than State Y). The burden now falls on the litigators to file the lawsuit in the
3 “correct place.

4 The approach of this Article is likely to reduce the frequency with which the
5 *renvoi* arises.

6 **Example:** In the preceding Example, assume that State Y’s nonuniform
7 Section 9-301(1) refers to the substantive and choice-of-law rules of State
8 X. If so, State X’s referral to State Y’s choice-of-law rules would present
9 the classic *renvoi*: State X’s Section 9-301 directs one to State Y’s choice
10 of law, and State Y’s Section 9-301 says to look to State X’s choice of law.
11 (The 1972 amendments to Section 9-103(3) created precisely this scenario
12 with respect to security interests in accounts created by debtors whose chief
13 executive offices were in a State that had the 1962 Official Text but whose
14 records concerning the accounts were located in a State that had adopted the
15 1972 Official Text.) Eliminating either State’s reference to choice-of-laws
16 rules, as Section 9-301(1) does, would eliminate the *renvoi*.

17 **SECTION 9-301. LAW GOVERNING PERFECTION AND PRIORITY**
18 **OF SECURITY INTERESTS.** Except as otherwise provided in Sections 9-303
19 through 9-305, the following rules determine the law governing perfection, the
20 effect of perfection or nonperfection, and the priority of a security interest in
21 collateral:

22 (1) Except as otherwise provided in this section, while a debtor is located in
23 a jurisdiction, the local law of that jurisdiction governs perfection, the effect of
24 perfection or nonperfection, and the priority of a security interest.

25 (2) While collateral is located in a jurisdiction, the local law of that
26 jurisdiction governs perfection, the effect of perfection or nonperfection, and the
27 priority of a possessory security interest.

28 (3) While goods, chattel paper, instruments, money, or negotiable
29 documents are located in a jurisdiction, the local law of that jurisdiction governs the
30 effect of perfection or nonperfection and the priority of a nonpossessory security
31 interest.

(4) While goods are located in a jurisdiction, the local law of that jurisdiction governs perfection of a security interest in the goods by filing a fixture filing.

(5) The local law of the jurisdiction in which timber to be cut is located governs perfection of a security interest in the timber.

(6) The local law of the jurisdiction in which the wellhead or minehead is located governs perfection, the effect of perfection or nonperfection, and the priority of a security interest in as-extracted collateral.

Reporters' Comments

1. **Source.** Former Sections 9-103(1)(a), (b); 9-103(3)(a), (b); 9-103(5), substantially modified.

2. Law Governing Perfection: General Rule. Paragraph (1) contains the general rule: the law governing perfection of security interests in both tangible and intangible collateral, whether perfected by filing or automatically, is the law of the jurisdiction of the debtor's location, as determined under Section 9-307. This paragraph substantially simplifies the choice-of-law rules. It eliminates former Section 9-103(1)(c) and (d), which concern nonpossessory security interests in tangible collateral that is removed from one jurisdiction to the other. It is likely to 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.) The approach taken in paragraph (1) also eliminates some difficult priority issues and the need to distinguish between "mobile" and "ordinary" goods, and it reduces the number of filing offices in which secured parties must file or search.

There are potential drawbacks, as well. Arguably, determining the location of the debtor is a less certain enterprise than is generally assumed. Purchase-money equipment financiers and others may be ill-equipped to determine the debtor's location and the peculiar filing requirements of that jurisdiction without incurring significant additional costs. 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. The expansion of the scope of this Article, although modest, is likely to exacerbate the difficulties in applying choice-of-law rules during the transition.

3. Law Governing Perfection: Exceptions. The general rule is subject to several exceptions. It does not apply to goods covered by a certificate of title (see Sections 9-102; 9-303), deposit accounts (see Section 9-304), or investment property (see Section 9-304). Nor does it apply to possessory security interests, i.e., security interests in which the secured party is in possession, or to security interests perfected by a fixture filing.

1 a. **Possessory Security Interests.** Paragraph (2) applies to possessory
2 security interests and provides that perfection is governed by the local law of the
3 jurisdiction in which the collateral is located. This is the rule of former Section
4 9-103(1)(b), except paragraph (2) eliminates the troublesome “last event” test of
5 former law.

6 The distinction between nonpossessory and possessory security interests
7 creates the potential for the same jurisdiction to apply two different choice-of-law
8 rules to determine perfection in the same collateral. For example, were a secured
9 party in possession of an instrument or document to relinquish possession in
10 reliance on temporary perfection, the applicable law immediately would change
11 from that of the location of the collateral to that of the location of the debtor.

12 b. **Fixtures.** Application of the general rule in paragraph (1) to perfection
13 of a security interest in fixtures would yield strange results. For example,
14 perfection of a security interest in fixtures located in Arizona and owned by a
15 Delaware corporation would be governed by the law of Delaware. Although
16 Delaware law would send one to a filing office in Arizona for the place to file a
17 financing statement as a fixture filing, see Section 9-501, Delaware law would not
18 take account of local, nonuniform real property filing and recording requirements
19 that Arizona law might impose. For this reason, paragraph (4) contains a special
20 rule for security interests perfected by a fixture filing; the law of the jurisdiction
21 where the fixtures are located governs perfection, including the formal requisites of
22 a fixture filing.

23 c. **Timber to Be Cut.** Application of the general rule in paragraph (1) to
24 perfection of a security interest in timber to be cut would yield undesirable results
25 analogous to those described with respect to fixtures. Paragraph (5) adopts a
26 similar solution: perfection is governed by the law of the jurisdiction where the
27 timber is located. Note that paragraph (5) applies only to “timber to be cut,” not to
28 timber that has been cut. Consequently, once the timber is cut the choice-of-law
29 rule in paragraph (1), which applies to ordinary goods, becomes applicable. To
30 ensure continued perfection, a secured party should file in both the state where the
31 timber to be cut is located and in the state where the debtor is located. The former
32 filing would be with the office at which a real property mortgage would be filed,
33 and the latter would be a central filing. See Section 9-501. The treatment of timber
34 to be cut differs from that provided in paragraph (6) for as-extracted collateral.
35 Under paragraph (5), the law of the jurisdiction where the timber to be cut is
36 located governs perfection, leaving priority to be governed by the law of the
37 debtor’s location under paragraph (1). Under paragraph (6), the law of the
38 jurisdiction where the wellhead or minehead is located governs both perfection and
39 priority.

40 d. **As-extracted Collateral.** Paragraph (6) adopts the rule of former
41 Section 9-103(5) with respect to certain security interests in minerals and related
42 accounts.

43 4. **Law Governing the Effect of Perfection and Priority.** Under former
44 Section 9-103, the law of a single jurisdiction governs both questions of perfection
45 and those of priority. This Article generally adopts that approach. See paragraph
46 (1). But the approach may create problems if the debtor and collateral are located

1 in different jurisdictions. For example, assume a security interest in equipment is
2 perfected by filing in Illinois (where the debtor is located). The equipment is
3 located in Pennsylvania. If the law of the jurisdiction in which the debtor is located
4 were to govern priority, then the priority of an execution lien on the goods located
5 in Pennsylvania would be governed by rules enacted by the Illinois legislature.

6 To address this problem, paragraph (3) divorces questions of perfection
7 from questions of “the effect of perfection or nonperfection and the priority of a
8 security interest. Under paragraph (3), the rights of competing claimants to
9 tangible collateral are resolved by reference to the law of the jurisdiction in which
10 the collateral is located. Although this bifurcated approach may introduce
11 complexities, its appearance in prior drafts with respect to agricultural liens met
12 with generally favorable reviews. A similar bifurcation applies to security interests
13 in investment property under former Section 9-103(6). See Section 9-305. The
14 principal efficiencies of moving from the location-of-collateral rule to a location-of-
15 debtor rule concern where to file and search and what to file. The bifurcated
16 approach generally preserves these benefits.

17 Paragraph (3) applies the law of the situs to determine priority only with
18 respect to goods (including fixtures), chattel paper, instruments, and negotiable
19 documents. Compare former Section 9-103(1), which applies the law of the
20 location of the collateral to documents, instruments, and “ordinary (as opposed to
21 “mobile) goods. This Article does not distinguish among types of goods. The
22 ordinary/mobile goods distinction appears to address concerns about where to file
23 and search, rather than concerns about priority. There appears to be no reason to
24 preserve this distinction under the bifurcated approach.

25 Particularly serious confusion may arise when the choice-of-law rules of a
26 given jurisdiction result in each of two competing security interests in the same
27 collateral being governed by a different priority rule. The potential for this
28 confusion exists under former Section 9-103(4) with respect to chattel paper:
29 Perfection by possession is governed by the law of the location of the paper,
30 whereas perfection by filing is governed by the law of the location of the debtor.
31 Consider the mess that would be created if the language or interpretation of former
32 Section 9-308 were to differ in the two relevant States, or if one of the relevant
33 jurisdictions (e.g., a foreign state) had not adopted Article 9. The potential for
34 confusion could be exacerbated when a secured party perfects both by taking
35 possession in the State where the collateral is located (State A) and by filing in the
36 State where the debtor is located (State B)—a common practice for some chattel
37 paper financiers. By providing that the law of the jurisdiction in which the collateral
38 is located governs priority, paragraph (3) substantially diminishes this problem.

39 **5. Non-U.S. Debtors.** This Article deletes former Section 9-103(3)(c),
40 which contained the choice-of-law rule governing security interests created by
41 debtors located in a non-U.S. jurisdiction. The rule has proven unsatisfactory for
42 several reasons. First, it determines the applicable law for non-U.S. debtors by
43 reference to the location of the debtor’s “major executive office in the United
44 States. Some, perhaps many, non-U.S. debtors lack any “executive office at all in
45 the U.S.; with respect to others, determining which of the executive offices in the
46 United States is the “major one has proven quite difficult.

1 Second, the rule permits perfection of security interests in accounts and
2 payment intangibles by notification to account debtors. This means of perfection
3 often is not feasible and, even when accomplished, is not likely to afford effective
4 public notice.

5 This Article applies the same choice-of-law rules to all debtors, foreign and
6 domestic. For example, it adopts the bifurcated approach for determining the law
7 applicable to goods and other tangible collateral. See Comment 4, above. The
8 Article contains a new rule governing the location of non-U.S. debtors. The rule
9 appears in Section 9-307 and is explained in the Reporters' Comments following
10 that section.

11 **SECTION 9-302. LAW GOVERNING FILING, PERFECTION, AND**
12 **PRIORITY OF STATUTORY LIENS.**

13 **Alternative A**

14 (a) While a debtor is located in a jurisdiction, the local law of that
15 jurisdiction governs perfection of a statutory lien on collateral.

16 (b) While collateral is located in a jurisdiction, the local law of that
17 jurisdiction governs the effect of perfection or nonperfection and the priority of a
18 statutory lien on the collateral.

19 **Alternative B**

20 While collateral is located in a jurisdiction, the local law of that jurisdiction
21 governs perfection, the effect of perfection or nonperfection, and the priority of a
22 statutory lien on the collateral.

23 Reporters' Comments

24 1. **Source.** New.

25 2. **Statutory Liens.** This section provides choice-of-law rules for statutory
26 liens. Like Section 9-301, Alternative A divorces perfection from priority. Under
27 subsection (a), the law of the jurisdiction of the debtor's location governs
28 perfection—i.e., filing, which is the sole means of perfecting a statutory lien (other
29 than the special rules for proceeds in Section 9-313). Under subsection (b), priority
30 is governed by the law of the jurisdiction where the collateral is located.
31 Alternative B provides that perfection, as well as priority, is governed by the law of
32 the jurisdiction where the collateral is located. Other choice-of-law rules, including
33 Section 1-105, will determine the law governing other matters, such as remedies on
34 default. Nonuniformity in the law governing statutory liens and in non-UCC
35 choice-of-law rules may engender some confusion in this area. Nevertheless, this

section's approach seems generally consistent with current law applicable to statutory liens.

**SECTION 9-303. LAW GOVERNING PERFECTION AND PRIORITY
OF SECURITY INTERESTS IN GOODS COVERED BY A CERTIFICATE
OF TITLE.**

(a) Goods become covered by a certificate of title when a valid application for the certificate of title and the applicable fee are delivered to the appropriate authority.

(b) (1) The local law of the jurisdiction under whose certificate of title the goods are covered governs perfection, the effect of perfection or nonperfection, and the priority of a security interest in goods covered by a certificate of title from the time the goods become covered by the certificate until the earlier of the time the certificate becomes ineffective under the law of that jurisdiction or the time the goods become covered subsequently by a certificate of title from another jurisdiction.

(2) After that time, the goods are not covered by the certificate of title.

(c) This section applies to goods covered by a certificate of title even if there is no other relationship between the jurisdiction under whose certificate of title the goods are covered and the goods or the debtor.

Reporters' Comments

1. **Source.** Former Section 9-103(2)(a), (b), substantially revised.

2. External Constraints on This Section. This section, like former Section 9-103(2), proceeds from the premise that, for goods covered by a certificate of title on which a security interest may be indicated, compliance with the certificate-of-title statute is a more appropriate method of perfection than filing. The concept of perfection by notation on a certificate is simple; however, certificate-of-title statutes are not. Unlike the Article 9 filing system, which is designed to afford publicity to security interests, certificate-of-title statutes were created primarily to deter theft. The need to coordinate Article 9 with a variety of nonuniform certificate-of-title statutes, the need to provide rules to take account of goods that are covered by more than one certificate, and the need to govern the

1 transition from perfection by filing to perfection by notation all create pressure for a
2 detailed and complex set of rules. In particular, much of the complexity arises from
3 the possibility that more than one certificate of title issued by more than one
4 jurisdiction can cover the same goods. That possibility results from defects in
5 certificate-of-title laws and the interstate coordination of those laws, not from
6 deficiencies in Article 9. As long as that possibility remains, the potential for
7 innocent parties to suffer losses will continue. At best, Article 9 can identify
8 clearly which innocent parties will bear the losses in familiar fact patterns.

9 **3. Scope of This Section.** This section applies to “goods covered by a
10 certificate of title. The new definition of “certificate of title” in Section 9-102
11 makes clear that this section applies not only to certificate-of-title acts under which
12 perfection occurs upon notation of the security interest on the certificate but also to
13 those that contemplate notation but provide that perfection is achieved by other
14 means, e.g., delivery of designated documents to an official. Subsection (a)
15 explains that goods become “covered” by a certificate of title when a valid
16 application for a certificate and the applicable fee are delivered to the appropriate
17 issuing authority. The time when goods become “covered” determines when this
18 section begins to apply to perfection of security interests in the goods, and thus
19 when the law of the jurisdiction under whose certificate the goods are covered will
20 begin to apply. Subsection (c), which is also new, makes clear that this section
21 applies to certificates of a jurisdiction having no other contacts with the goods or
22 the debtor. This result comports with most of the reported cases on the subject and
23 with contemporary business practices in the trucking industry.

24 **4. Law Governing Perfection.** Subsection (b) is the basic choice-of-law
25 rule for goods covered by a certificate of title. Perfection is governed by the law of
26 the jurisdiction under whose certificate the goods are covered from the time the
27 goods become covered until the earlier of (i) the time the certificate becomes
28 ineffective under the law of that jurisdiction or (ii) the time the goods become
29 covered subsequently by a certificate of title from another jurisdiction.

30 Normally, under the law of the relevant jurisdiction, the perfection step
31 would consist of compliance with that jurisdiction’s certificate-of-title act and a
32 resulting notation of the security interest on the certificate of title. See Section
33 9-309A(c). In the typical case of an automobile or over-the-road truck, a person
34 who wishes to take a security interest in the vehicle can ascertain whether it is
35 subject to any security interests by looking at the certificate of title. But certificates
36 of title cover certain types of goods in some States but not in others. A secured
37 party who does not realize this may extend credit and attempt to perfect by filing in
38 the jurisdiction where the debtor is located. If the goods had been titled in another
39 jurisdiction, the lender would be unperfected.

40 Subsection (b) explains when the law of the jurisdiction under whose
41 certificate the goods are covered ceases to apply. Former Section 9-103(2)(b)
42 provides that the law of the jurisdiction issuing the certificate ceases to apply upon
43 “surrender” of the certificate. In the case of automobiles, certificate-of-title statutes
44 generally require tender of any outstanding certificate as a condition for issuance of
45 a new certificate. See, e.g., Uniform Motor Vehicle Certificate of Title and Anti-
46 Theft Act § 6(c)(1). This tender is the “surrender” to which former subsection
47 (2)(b) refers. The former rule reflects the idea that notation of a security interest on

1 a certificate of title affords notice to third parties only so long as the certificate is
2 outstanding.

3 This Article eliminates the concept of “surrender. Instead, the law of the
4 original jurisdiction ceases to apply when the certificate “becomes ineffective
5 under the law of that jurisdiction. Given the diversity in certificate-of-title statutes,
6 the term “ineffective” is not defined. Depending on the certificate-of-title law, this
7 revision may ameliorate somewhat the problem of certificates that are wrongfully
8 surrendered. Note, however, that if the certificate is surrendered in conjunction
9 with an appropriate application for a certificate to be issued by another jurisdiction,
10 the law of the original jurisdiction ceases to apply for another reason: the goods
11 became covered subsequently by a certificate of title from another jurisdiction.

12 The last sentence of subsection (b) indicates that, when the certificate
13 becomes ineffective or the goods subsequently become covered by a certificate of
14 title from another jurisdiction, the goods are “not covered by the certificate of title
15 within the meaning of this section.

16 **Example:** The goods are covered by a certificate of title from State X, and
17 a security interest is perfected in accordance with State X’s law. Thereafter,
18 the goods are covered by a certificate of title from State Y. Under
19 subsection (b), the law of State X no longer governs perfection of the
20 security interest. The goods no longer are covered by “the certificate of
21 title (i.e., the *State X* certificate of title). They are, however, covered by a
22 certificate of title (i.e., the *State Y* certificate) as defined in Section 9-102, so
23 that the law of the jurisdiction under whose certificate of title the goods are
24 covered (State Y) governs perfection.

25 **5. Continued Perfection.** The fact that the law of one State ceases to
26 apply under subsection (a) does not necessarily mean that a security interest
27 perfected under that law automatically becomes unperfected. See Section 9-314(c).

28 **6. Inventory.** Compliance with a certificate-of-title act generally is *not* the
29 method of perfecting security interests in inventory. Section 9-309A(b) provides
30 that a security interest created in inventory held by a person in the business of
31 selling goods of that kind is subject to the normal filing rules; compliance with a
32 certificate-of-title act is not necessary or effective to perfect the security interest.
33 Most certificate-of-title acts are in accord.

34 The following example explains the subtle relationship between this rule
35 and the choice-of-law rules in Section 9-303(b) and former Section 9-103(2):

36 **Example:** Goods are located in State A and covered by a certificate of title
37 issued under the law of State A. The State A certificate of title is “clean :
38 it does not reflect a security interest. Owner takes the goods to State B and
39 sells (trades in) the goods to Dealer, who is located (within the meaning of
40 Section 9-307) in State B. As is customary, Dealer retains the duly assigned
41 State A certificate of title pending resale of the goods. Dealer’s inventory
42 financier, SP-B, obtains a security interest in the goods under its after-
43 acquired property clause.

1 Under Section 9-309A(b) of both State A and State B, Dealer's
2 inventory financier, SP-B, must perfect by filing instead of complying with a
3 certificate-of-title law. If under Section 9-303(b) the law applicable to
4 perfection of SP-B's security interest is that of State A, because the goods
5 are covered by a State A certificate, SP-B would be required to file in State
6 A under State A's Section 9-501. That result would be anomalous, to say
7 the least, since the principle underlying Section 9-309A(b) is that the
8 inventory should be treated as ordinary goods.

9 Section 9-303(b) (and former Section 9-103(2)) should be read as
10 providing that the law of State B, not State A, applies. A court looking to
11 the forum's Section 9-303(b) would find that the subsection applies only if
12 two conditions are met: (i) the goods were "covered by the certificate as
13 defined in Section 9-102, i.e., application had been made for a State (here,
14 State A) to issue a certificate of title covering the goods and (ii) the
15 certificate is a "certificate of title as defined in Section 9-102, i.e., a statute
16 of that State "provides for the security interest in question to be indicated on
17 the certificate as a condition or result of perfection. Stated otherwise,
18 Section 9-303(b) applies only when compliance with a certificate-of-title
19 statute, and not filing, is the appropriate method of perfection. Under the
20 law of State A, *for purposes of perfecting SP-B's security interest in the*
21 *dealer's inventory*, the proper method of perfection is filing—not compliance
22 with State A's certificate-of-title act. For that reason, the goods are not
23 covered by a "certificate of title, and the second condition is not met.
24 Thus, Section 9-303(b) does not apply to the goods. Instead, Section 9-301
25 applies, and the applicable law is that of State B, where the debtor (dealer)
26 is located.

27 7. **Relation Back.** We suggest that a Legislative Note recommend the
28 elimination of relation-back provisions in certificate-of-title laws affecting
29 perfection of security interests. See Section 9-309A, Comment 6.

30 SECTION 9-304. LAW GOVERNING PERFECTION AND PRIORITY 31 OF SECURITY INTERESTS IN DEPOSIT ACCOUNTS.

32 (a) The local law of a depository institution's jurisdiction governs perfection
33 ~~Perfection~~, the effect of perfection or nonperfection, and the priority of a security
34 interest in a deposit account ~~are governed by the local law of the depository~~
35 ~~institution's jurisdiction.~~

36 (b) The following rules determine a depository institution's jurisdiction for
37 purposes of this section:

1 (1) If an agreement between the depository institution and the debtor
2 expressly specifies a particular jurisdiction as the depository institution's
3 jurisdiction for purposes of this part, this article, or [the Uniform Commercial
4 Code], that jurisdiction is the depository institution's jurisdiction.

5 (2) If paragraph (1) does not apply and an agreement between the
6 depository institution and its customer ~~does not specify the depository institution's~~
7 ~~jurisdiction pursuant to paragraph (1) but~~ expressly specifies that the deposit
8 account is maintained at an office in a particular jurisdiction, that jurisdiction is the
9 depository institution's jurisdiction.

10 (3) If neither paragraph (1) nor paragraph (2) applies ~~an agreement between~~
11 ~~the depository institution and its customer does not specify a jurisdiction pursuant~~
12 ~~to paragraph (1) or (2),~~ the depository institution's jurisdiction is the jurisdiction in
13 which is located the office identified in an account statement as the office serving
14 the customer's account.

15 (4) If none of the other paragraphs applies ~~an agreement between the~~
16 ~~depository institution and its customer does not specify a jurisdiction pursuant to~~
17 ~~paragraph (1) or (2) and an account statement does not identify an office serving the~~
18 ~~customer's account pursuant to paragraph (3),~~ the depository institution's
19 jurisdiction is the jurisdiction in which is located the chief executive office of the
20 depository institution.

21 Reporters' Comments

22 1. **Source.** New. Derived from Section 8-110(e) and former Section
23 9-103(6).

24 2. **Deposit Accounts.** Under this section, the law of the “depository
25 institution’s jurisdiction” governs perfection and priority of a security interest in
26 deposit accounts. Paragraphs (1) through (4) contain rules for determining the
27 “depository institution’s jurisdiction.” The substance of these rules is substantially
28 similar to that of the rules determining the “security intermediary’s jurisdiction
29 under Section 8-110(e), except that paragraph (1) provides more flexibility than the
30 analogous provision in Section 8-110(e)(1). Paragraph (1) permits the parties to

1 choose the law of one jurisdiction to govern perfection and priority of security
2 interests and a different governing law for other purposes. Section 8-110(e)(1)
3 (included in the Appendix to this draft) has been conformed to paragraph (1) of this
4 section, and Section 9-305(a)(4)(A), concerning a commodity intermediary's
5 jurisdiction, makes a similar departure from former Section 9-103(6)(e)(i).

6 3. **Style.** This section departs stylistically from Section 8-110(e) in several
7 ways. If these departures are retained, Section 8-110(e) probably should be
8 conformed.

9 **SECTION 9-304A. LAW GOVERNING PERFECTION AND PRIORITY**
10 **OF SECURITY INTERESTS IN ~~LETTERS~~ LETTER-OF-CREDIT RIGHTS**
11 **AND PROCEEDS OF LETTERS OF CREDIT.**

12 (a) Subject to subsection (c), the local law of the issuer's jurisdiction or a
13 nominated person's jurisdiction governs perfection ~~Perfection~~, the effect of
14 perfection or nonperfection, and the priority of a security interest in a letter-of-
15 credit rights ~~or proceeds of the letter of credit are governed by the local law of the~~
16 ~~issuer's jurisdiction~~ if the issuer's or nominated person's jurisdiction is a State.
17 ~~The following rules determine an issuer's jurisdiction for purposes of this section:~~
18 ~~———— (1) If the letter of credit specifies a particular jurisdiction as the issuer's~~
19 ~~jurisdiction for purposes of this part, this article, or [the Uniform Commercial~~
20 ~~Code], that jurisdiction is the issuer's jurisdiction.~~
21 ~~———— (2) If the letter of credit does not specify the issuer's jurisdiction~~
22 ~~pursuant to paragraph (1) but the letter of credit indicates an address of the issuer~~
23 ~~the jurisdiction in which that address is located is the issuer's jurisdiction.~~
24 ~~———— (3) If the letter of credit does not specify the issuer's jurisdiction or~~
25 ~~indicate an address of the issuer pursuant to paragraph (1) or (2) or indicates more~~
26 ~~than one address, but the letter of credit indicates that it was issued at an office in a~~
27 ~~particular jurisdiction, that jurisdiction is the issuer's jurisdiction.~~

1 ~~————— (4) If the letter of credit does not specify the issuer’s jurisdiction,~~
2 ~~indicate the address of the issuer or indicate that it was issued at an office in a~~
3 ~~particular jurisdiction pursuant to paragraph (1), (2), or (3), the issuer’s jurisdiction~~
4 ~~is the jurisdiction in which is located the chief executive office of the issuer.~~

5 (b) The local law of an issuer’s or nominated person’s jurisdiction is the
6 local law of the jurisdiction governing its liability with respect to the letter-of-credit
7 rights as [specified] [provided] in Section 5-116.

8 (c) This section does not apply to a security interest that is perfected only
9 under Section 9-308(d).

10 ————— Reporters’ Comments

11 1. **Source.** New. Derived in part from Sections 8-110(e) and 9-305 and
12 former Section 9-103(6).

13 2. ***Sui Generis Treatment.*** This section governs the applicable law for
14 perfection and priority of security interests in letter-of-credit rights, other than a
15 security interest perfected only under Section 9-308(d) (i.e., as a support
16 obligation). The treatment differs substantially from that provided in Section 9-304
17 for deposit accounts. The basic rule is that law of the issuer’s or nominated
18 person’s jurisdiction, derived from the terms of the letter of credit itself, controls
19 perfection and priority, but only if the issuer’s or nominated person’s jurisdiction is
20 a State, as defined in Section 9-102. If the issuer’s or nominated person’s
21 jurisdiction is not a State, the baseline rule of Section 9-301 applies--perfection and
22 priority are governed by the law of the debtor’s location, determined under Section
23 9-307. Export transactions typically involve a foreign issuer and a domestic
24 nominated person, such as a confirmer, located in a State. The principal goal of this
25 section is to reduce the likelihood that perfection and priority would be governed by
26 the law of a foreign jurisdiction in a transaction that is essentially domestic from the
27 standpoint of the debtor-beneficiary, its creditors, and a domestic nominated
28 person.

29 3. **Issuer’s or Nominated Person’s Jurisdiction.** Subsection (b) defers to
30 the rules established under Section 5-116 for determination of an issuer’s or
31 nominated person’s jurisdiction. It should be emphasized that this section
32 addresses only the applicable law for purposes of perfection the effect of perfection
33 or nonperfection, and priority. Section 5-116 itself deals with the law applicable to
34 liability and Article 5 (or other applicable law) deals with the rights and duties of an
35 issuer or nominated person. Stated otherwise, perfection, nonperfection, and
36 priority have no effects on the rights and duties of an issuer or nominated person.

1 **SECTION 9-305. LAW GOVERNING PERFECTION AND PRIORITY**
2 **OF SECURITY INTERESTS IN INVESTMENT PROPERTY.**

3 (a) Except as otherwise provided in subsection (b) ~~the following rules apply~~
4 ~~to a security interest in investment property:~~

5 (1) While a security certificate is located in a jurisdiction, the local law
6 of that jurisdiction governs perfection, the effect of perfection or nonperfection, and
7 the priority of a security interest in the certificated security represented thereby.

8 (2) The local law of the issuer's jurisdiction as specified in Section
9 8-110(d) governs perfection, the effect of perfection or nonperfection, and the
10 priority of a security interest in an uncertificated security.

11 (3) The local law of the securities intermediary's jurisdiction as
12 specified in Section 8-110(e) governs perfection, the effect of perfection or
13 nonperfection, and the priority of a security interest in a security entitlement or
14 securities account.

15 (4) (A) The local law of the commodity intermediary's jurisdiction
16 governs perfection, the effect of perfection or nonperfection, and the priority of a
17 security interest in a commodity contract or commodity account.

18 (B) The following rules determine a commodity intermediary's
19 jurisdiction for purposes of this paragraph and Section 9-314:

20 (i) If an agreement between the commodity intermediary and
21 commodity customer expressly specifies the commodity intermediary's jurisdiction
22 for purposes of this part, this article, or [the Uniform Commercial Code], that
23 jurisdiction is the commodity intermediary's jurisdiction.

24 (ii) If paragraph (1) does not apply and an agreement between
25 the commodity intermediary and commodity customer ~~does not specify the~~
26 ~~commodity intermediary's jurisdiction pursuant to subparagraph (A) but expressly~~

1 specifies that the commodity account is maintained at an office in a particular
2 jurisdiction, that jurisdiction is the commodity intermediary's jurisdiction.

3 (iii) If neither paragraph (1) nor paragraph (2) applies an
4 ~~agreement between the commodity intermediary and commodity customer does not~~
5 ~~specify a jurisdiction pursuant to subparagraph (A) or (B)~~, the commodity
6 intermediary's jurisdiction is the jurisdiction in which is located the office identified
7 in an account statement as the office serving the commodity customer's account.

8 (iv) If none of the other paragraphs applies an agreement
9 ~~between the commodity intermediary and commodity customer does not specify a~~
10 ~~jurisdiction pursuant to subparagraph (A) or (B) and an account statement does not~~
11 ~~identify an office serving the commodity customer's account pursuant to~~
12 ~~subparagraph (C)~~, the commodity intermediary's jurisdiction is the jurisdiction in
13 which is located the chief executive office of the commodity intermediary.

14 (b) The local law of the jurisdiction in which the debtor is located governs:

15 (1) perfection of a security interest in investment property by filing;

16 (2) automatic perfection of a security interest in investment property
17 granted by a broker or securities intermediary; and

18 (3) automatic perfection of a security interest in a commodity contract or
19 commodity account granted by a commodity intermediary.

20 Reporters' Comments

21 1. **Source.** Former Section 9-103(6).

22 2. **Change from Former Law.** Subsection (a)(4)(A) has been revised to
23 provide more flexibility for the parties to select the security intermediary's
24 jurisdiction. See also Section 9-304(1) (depository institution's jurisdiction);
25 Section 8-110(e)(1) (securities intermediary's jurisdiction) (included in the
26 Appendix to this draft).

27 3. **Style.** This section departs stylistically from Section 8-110(e) in several
28 ways. If these departures are retained, Section 8-110(e) probably should be
29 conformed.

1 **SECTION 9-306.**

2 [deleted]

3 **SECTION 9-307. LOCATION OF DEBTOR.**

4 (a) (1) Except as otherwise provided in this section, the following rules
5 determine a debtor's location for purposes of this part:

6 (A) An individual debtor is located at the individual's residence.

7 (B) Any other debtor having only one place of business is located at
8 its place of business.

9 (C) ~~and any~~ Any other debtor having more than one place of
10 business is located at its chief executive office.

11 (2) (A) Paragraph (1) applies ~~but~~ only if a debtor's ~~the~~ residence, place
12 of business, or chief executive office, as applicable, is located either in a State or in
13 a jurisdiction, other than a State, whose law requires information concerning the
14 [possible] existence of a security interest to be made publicly available as a
15 condition or result of the security interest's obtaining priority over the rights of a
16 lien creditor with respect to the collateral.

17 (B) If paragraph (1) does not apply ~~In other cases,~~ the debtor is
18 located in [the District of Columbia].

19 (3) A place where a debtor conducts its affairs is a "place of business
20 for purposes of this subsection.

21 (b) ~~For purposes of this part, a~~ A registered entity that is organized under
22 the law of a State is located in its State of organization.

23 (c) Except as otherwise provided in subsection (f), a registered entity that
24 is organized under the law of the United States and a branch or agency of a bank
25 that is not organized under the law of the United States or a State are located:

_____ (1) in the State that the law of the United States designates, if the law designates a State of location;

(2) in the State that the registered entity designates, if the law of the
United States authorizes the registered entity to designate its State of location; [or]
[and]

(3) in the District of Columbia, if neither paragraph (1) nor paragraph
(2) applies.

(d) A registered entity continues to be located in the jurisdiction specified by subsection (b) [or (c)] notwithstanding the suspension, revocation, forfeiture, or lapse of the registered entity's registration or the [involuntary] dissolution of the registered entity.

(e) For purposes of this part, the The United States and its governmental entities are is located in the District of Columbia.

(f) A branch or agency of a bank that is not organized under the law of the United States or a State is located in the State in which the branch or agency is licensed, if the branches or agencies of the bank are licensed in only one State.

(g d) ~~A~~ For purposes of this part, a foreign air carrier under the Federal Aviation Act of 1958, as amended, is located at the designated office of the agent upon which service of process may be made on behalf of the carrier.

(h) This section applies only for purposes of this part.

Reporters' Comments

Changes from Prior Draft:

A. New paragraph (a)(3) is designed to provide a location for non-profit organizations other than registered entities.

B. New paragraphs (c) and (f) are intended more accurately to reflect federal law.

C. New paragraph (d) addresses loss of registration by registered entities.

1 1. **Source.** Former Section 9-103(3)(d), as substantially revised.

2 2. **General Rule.** As a general matter, the location of the debtor
3 determines the jurisdiction whose law governs perfection of a security interest or a
4 statutory lien. See Sections 9-301(1), 9-302(b), and 9-305(b). This section
5 determines the location of the debtor. Subsection (a) states the baseline rules: An
6 individual debtor is deemed to be located at the individual's residence with respect
7 to both personal and business assets. Any other debtor is deemed to be located at
8 its place of business if it has only one, or at its chief executive office if it has more
9 than one place of business. As used in this subsection, "business" is meant to
10 include the activities of eleemosynary institutions and other organizations that do
11 not conduct "for profit" business activities. See subsection (a)(3). The baseline
12 rule is subject to four exceptions, each of which is discussed below.

13 3. **Registered Entities.** Under subsection (b), "a registered entity is located
14 in its State of organization. Section 9-102 defines a "registered entity" as "an
15 organization organized under the law of a State and as to which the State maintains
16 a public record showing the organization to have been organized" and the "State of
17 organization" as the "State under whose law the [registered] entity is organized.
18 For example, a Delaware corporation is a registered entity, and Delaware is its
19 jurisdiction of organization. Other examples of registered entities are limited
20 partnerships and limited liability companies.

21 Determining the registered entity-debtor's location by reference to the
22 jurisdiction of organization could provide some important side benefits for the
23 filing systems. A jurisdiction could structure its filing system so that it would be
24 impossible to make a mistake in a registered entity-debtor's name on a financing
25 statement. A filing designating an incorrect corporate name for the debtor would be
26 rejected, for example. Linking filing to the jurisdiction of organization also could
27 reduce pressure on the system imposed by transactions in which registered entities
28 cease to exist. The jurisdiction of organization might prohibit such transactions
29 unless steps were taken to ensure that existing filings were refiled against a
30 successor entity or terminated by the secured party.

31 During discussions of the proposal to change the location of a registered
32 entity to its jurisdiction of organization, concerns were expressed that the change
33 might cause a significant shift in filing revenues from some States to others, and to
34 Delaware in particular. That prospect, it was argued, could render the proposal
35 politically impractical. According to a recent study, however, the impact would not
36 be material. See Lynn M. LoPucki, *Why the Debtor's State of Incorporation*
37 *Should Be the Proper Place for Article 9 Filing*, 79 Minn. L. Rev. 577 (1995).
38 Professor LoPucki's study also suggests that for the vast majority of filings, the
39 change would have no impact at all. Most collateral, it appears, is located in the
40 same jurisdiction where the debtor is located (and where corporate debtors are
41 incorporated).

42 4. **United States as Debtor.** To the extent that Article 9 governs (see
43 Sections 1-105; 9-112(c)), the United States and its subdivisions, instrumentalities,
44 and other governmental entities are located in the District of Columbia. See
45 subsection (c).

1 **Example:** Debtor is an instrumentality of the United States, having its chief
2 executive office in New York City. Debtor creates a security interest in its
3 equipment, which is located in Boulder, Colorado. Assuming Article 9
4 applies, subsection (c) provides that Debtor is located in the District of
5 Columbia. Under Section 9-301(1), perfection is governed by the law of the
6 debtor’s location, i.e., the District of Columbia, whereas under 9-301(3), the
7 law of the jurisdiction in which the collateral is located—here,
8 Colorado—governs priority.

9 We are informed that the filing office of the District of Columbia is not as
10 efficient as one might like. The Drafting Committee continues to consider whether
11 another office would be preferable.

12 **5. Non-U.S. Debtors.** The Reporters’ Comments to Section 9-301 explain
13 the shortcomings of former Section 9-103(3)(c), which contains special choice-of-
14 law rules for debtors who are located in a non-U.S. jurisdiction. Under the baseline
15 rule of this section, a non-U.S. debtor normally would be located in a foreign
16 jurisdiction and, as a consequence, foreign law would govern perfection. When
17 foreign law affords no public notice of security interests, the baseline rule yields
18 unacceptable results.

19 Accordingly, subsection (a) provides that the normal rules for determining
20 the location of a debtor apply only if they yield a location that is either a State (as
21 broadly defined in Section 9-102) or “a jurisdiction, other than a State, whose law
22 requires information concerning the [possible] existence of a security interest to be
23 made publicly available as a condition or result of the security interest’s obtaining
24 priority over the right of a lien creditor with respect to the collateral. In other
25 cases, the debtor is located in the District of Columbia. Note that the law of the
26 jurisdiction in which the debtor is located governs not only perfection but also, with
27 respect to accounts and other intangible collateral, “the effect of perfection or
28 nonperfection and the priority of a security interest. Section 9-301(1). With respect
29 to goods and other tangible collateral, these issues are governed by the law of the
30 jurisdiction in which the collateral is located. See Section 9-301(3).

31 A “registered entity” is located in its State of organization. See subsection
32 (b). Inasmuch as “registered entity” is defined to exclude entities that are not
33 organized under the law of a “State,” both foreign individuals and foreign
34 corporations may be deemed located in the District of Columbia.

35 **Example:** Debtor is an English corporation with its chief executive office
36 in London. Debtor creates a security interest in its accounts. Subsection (a)
37 provides that Debtor is located in London if English law conditions
38 perfection on giving public notice. Otherwise, Debtor is located in the
39 District of Columbia. Under Section 9-301(1), perfection, the effect of
40 perfection, and priority are governed by the law of the jurisdiction of the
41 debtor’s location—here, England or the District of Columbia (depending on
42 the content of English law).

43 **Example:** Debtor is an English corporation with its chief executive office
44 in London. Debtor creates a security interest in its equipment. Subsection
45 (a) provides that Debtor is located in London if English law conditions

1 perfection on giving public notice. Otherwise, Debtor is located in the
2 District of Columbia. Under Section 9-301(1), perfection is governed by
3 the law of the jurisdiction of the debtor's location, whereas the law of the
4 jurisdiction in which the collateral is located—here, England—governs
5 priority. See Section 9-301(3).

6 The foregoing discussion assumes that each transaction bears an appropriate
7 relation to the forum State. In the absence of an appropriate relation, the forum
8 State's entire UCC, including the choice-of-law provisions in Article 9 (Sections
9 9-301 through 9-307), will not apply. See Section 9-112, Comment 6..

10 6. **Foreign Air Carriers.** Subsection (d) follows former Section
11 9-103(3)(d).

12 [SUBPART 2. PERFECTION]

1 **SECTION 9-308. WHEN SECURITY INTEREST OR STATUTORY**
2 **LIEN IS PERFECTED; CONTINUITY OF PERFECTION.**

3 (a) (1) Except as otherwise provided in this section and ~~in~~ Section 9-308A,
4 a security interest is perfected if it has attached and all of the applicable
5 requirements for perfection in Sections 9-309 through 9-313 have been satisfied.

6 (2) A security interest is perfected when it attaches if ~~if the~~
7 requirements are satisfied before the security interest attaches, ~~it is perfected when~~
8 ~~it attaches.~~

9 (b) (1) A statutory lien is perfected if it has become effective and all of the
10 applicable requirements for perfection in Sections 9-309 and 9-313 have been
11 satisfied.

12 (2) A statutory lien is perfected when it becomes effective if ~~if the~~
13 requirements are satisfied before the statutory lien becomes effective ~~it is perfected~~
14 ~~when it attaches.~~

15 (c) (1) A security interest or statutory lien is perfected continuously if it ~~if a~~
16 ~~security interest or statutory lien~~ is originally perfected in one manner under this
17 article and is later perfected in another manner under this article, without an
18 intermediate period when it was unperfected, ~~the security interest or statutory lien is~~
19 ~~perfected continuously.~~

20 (d) Perfection of a security interest in:

21 (1) an account, chattel paper, document, instrument, [insurance policy,]
22 general intangible, or security also perfects a security interest in a support
23 obligation for the collateral.

24 (2) ~~(c) Perfection of a security interest in~~ a securities account also
25 perfects a security interest in all security entitlements carried in the securities
26 account;

(3) ~~Perfection of a security interest in a commodity account also~~
perfects a security interest in all commodity contracts carried in the commodity
account; and

(4) (f) ~~Notwithstanding other law to the contrary, perfection of a security interest in a right to payment or performance also perfects a security interest in a [mortgage on real property] [lien on property] securing the right,~~ notwithstanding other law to the contrary.

Legislative Note: To avoid confusion, any statute conflicting with subsection (f) should be made expressly subject to that subsection.

Reporters' Comments

1. Source. Former Sections 9-303, 9-115(2).

2. **General Rule.** Subsection (a) explains that a security interest is perfected only when it has attached and when a required “perfection” or “public notice” step has been taken. The “except” clause refers to the automatic perfection rules appearing in Section 9-308A. It also reflects that other subsections of this section, e.g., subsection (d), contain perfection steps.

3. **Statutory Liens.** Subsection (b) is new. It describes the elements of perfection of a statutory lien.

4. **Support Obligation.** Subsection (d) is new. It provides for automatic perfection of a security interest in a support obligation for collateral if the security interest in the collateral is perfected. This is unlikely to effect any change in current law.

Example: Buyer is obligated to pay Debtor for goods sold. Buyer's president guarantees the obligation. Perfection of a security interest in Debtor's right to payment (an account) constitutes perfection of a security interest in Debtor's rights under the guarantee.

5. Investment Property. Subsection (e) follows former Section 9-115(2).

6. Right to Payment Secured by Mortgage. Subsection (f) is new and overrides other law to the contrary. It deals with the situation in which a mortgagee of real property creates a security interest in an obligation (e.g., a note) secured by a real property mortgage. Section 9-203(e)(5) adopts the traditional view that the transferee of the note acquires the mortgage, as well. This subsection adopts a similar principle: perfection of a security interest in the right to payment constitutes perfection of a security interest in the mortgage securing it.

An important consequence of the rules in Section 9-203(e)(5) and subsection (f) is that, by acquiring a perfected security interest in a mortgage note,

1 the secured party acquires a security interest in the mortgage that is senior to the
2 rights of a person who becomes a lien creditor of the mortgagee (Article 9 debtor).
3 See Section 9-315(a)(2). This result helps prevent the separation of the mortgage
4 from the note.

5 Real estate law determines who has the power to release a mortgage of
6 record.

7 **Example:** Mortgagor makes a note and secures the note creates a mortgage to
8 secure the note. Mortgagee The fact that a mortgage is subject to a perfected
9 security interest does not give the secured party the power to release the mortgage.

10 **SECTION 9-308A. SECURITY INTEREST PERFECTED UPON**
11 **ATTACHMENT.** The following security interests are perfected when they attach:

12 (1) a purchase money security interest in consumer goods except as
13 otherwise provided in Section 9-309A(c) with respect to consumer goods that are
14 subject to a statute or treaty described in Section 9-309A(a);

15 (2) an assignment of accounts or payment intangibles which does not by
16 itself or in conjunction with other assignments to the same assignee transfer a
17 significant part of the assignor's outstanding accounts or payment intangibles;

18 (3) a sale of a payment intangible;

19 (4) a security interest of a collecting bank arising under Section 4-210;

20 (5) a security interest arising in the purchase or delivery of a financial asset
21 under Section 9-206;

22 (6) a security interest in investment property created by a broker or
23 securities intermediary;

24 (7) a security interest in a commodity contract or a commodity account
25 created by a commodity intermediary;

26 (8) an assignment for the benefit of all the creditors of the transferor, and
27 subsequent transfers by the assignee thereunder;

1 (9) a security interest created by an assignment of a beneficial interest in a
2 trust unless the beneficial interest constitutes investment property;

3 (10) a security interest created by an assignment of a beneficial interest in a
4 decedent's estate; and

5 (11) a security interest arising under Article 2 or 2A.

6 Reporters' Comments

7 1. **Source.** Derived from former Sections 9-302(1); 9-115(4)(c), (d); 9-116.

8 2. **Automatic Perfection.** This section contains the automatic perfection
9 rules previously located former Sections 9-302(1), 9-115(4)(c), (d), and 9-116.
10 Rather than continue to state the rule by indirection, this section explicitly provides
11 for perfection upon attachment.

12 3. **Purchase Money Security Interest in Consumer Goods.** Former
13 Section 9-302(1)(d) has been revised and appears here as paragraph (1). No filing
14 or other step is required to perfect a purchase money security interest in consumer
15 goods, other than goods that are subject to a statute or treaty described in Section
16 9-309A(a). However, filing is necessary to prevent a buyer of the goods from
17 taking free of the security interest under Section 9-316(b), and a fixture filing is
18 required for priority over conflicting interests in fixtures to the extent provided in
19 Section 9-331.

20 4. **Payment Intangibles.** Paragraph (2) expands upon former subsection
21 (1)(e) by affording automatic perfection to certain assignments of payment
22 intangibles. Paragraph (3), which is new, affords automatic perfection to sales of
23 payment intangibles. It reflects the practice under former Article 9. Under that
24 Article, filing a financing statement does not affect the rights of a buyer of payment
25 intangibles, inasmuch as the Article does cover those sales. To the extent that the
26 exception in paragraph (2) covers outright sales of payment intangibles, which
27 automatically are perfected under paragraph (3), the exception is redundant.

28 5. **Investment Property.** Paragraphs (5) replaces the last clause of each
29 subsection of former Section 9-116. Paragraphs (6) and (7) replace former Section
30 9-115(4)(c) and (d). The last two indicated that, with respect to certain security
31 interests created by a securities intermediary or commodity intermediary, "[t]he
32 filing of a financing statement . . . has no effect for purposes of perfection or
33 priority with respect to that security interest. No change in meaning is intended by
34 the deletion of the quoted phrase.

35 6. **Beneficial Interests in Trusts.** The formulation of paragraph (9) is
36 new. It explicitly limits automatic perfection in a beneficial interest in a trust to
37 those beneficial interests that do not constitute investment property. Thus, a
38 collateral assignment of the beneficial interest in a business trust would not be
39 automatically perfected, whereas a collateral assignment of the beneficial interest in
40 a family trust would be.

1 **SECTION 9-309. WHEN FILING REQUIRED TO PERFECT**
2 **SECURITY INTEREST OR STATUTORY LIEN; SECURITY INTERESTS**
3 **AND STATUTORY LIENS TO WHICH FILING PROVISIONS DO NOT**
4 **APPLY.**

5 (a) Except as otherwise provided in subsection (b), a ~~A~~ financing statement
6 must be filed to perfect all security interests and statutory liens ~~other than a security~~
7 ~~interest.~~

8 **(b) The filing of a financing statement is not necessary to perfect a security**
9 **interest:**

- 10 (1) in a support obligation under Section 9-308(d);
- 11 (2) that is perfected when it attaches (Section 9-308A);
- 12 (3) in property subject to a statute, regulation, or treaty described in
- 13 Section 9-309A(a);
- 14 (4) in instruments, certificated securities, ~~chattel paper~~, or documents
- 15 perfected without filing or possession under Section 9-310(d) or (e);
- 16 (5) in collateral in the secured party's possession under Section 9-311;
- 17 (6) in investment property, a deposit account, or a letter-of-credit rights
- 18 ~~and proceeds of the letter of credit~~ which is perfected without filing under Section
- 19 9-312;
- 20 (7) in or statutory lien on proceeds under Section 9-313(e); or
- 21 (8) perfected under Section 9-314(a), (c), or (d).

22 **(c)** ~~b~~ If a secured party assigns a perfected security interest, a filing under
23 this article is not required to continue the perfected status of the security interest
24 against creditors of and transferees from the original debtor.

25 Reporters' Comments

26 1. **Source.** Former Section 9-302(1), (2).

1 2. **General Rule.** Subsection (a) establishes a central Article 9 principle:
2 Filing a financing statement is necessary for perfection of all security interests
3 unless the subsection specifies otherwise.

4 3. **Support Obligations.** New subsection (a)(1) reflects the rule in new
5 Section 9-308(d), which provides for automatic perfection of a security interest in a
6 support obligation for collateral if the security interest in the collateral is perfected.

7 4. **Automatic Perfection.** The automatic perfection rules of former
8 Section 9-302(1) have been relocated to new Section 9-308A, to which subsection
9 (a) now makes reference.

10 5. **Preemptive Federal Law; Certificate of Title Acts.** New subsection
11 (a)(3) excepts from the filing requirement property covered by a statute, regulation,
12 or treaty described in Section 9-309A(a). Perfection as to this property is governed
13 by Section 9-309A(c).

14 6. **Statutory Liens.** Statutory liens may be perfected only by filing, except
15 to the extent that Section 9-313(e) provides otherwise with respect to proceeds.
16 Thus agricultural liens are not mentioned in subsection (a)(5) or Section 9-311,
17 which deal with possessory security interests. The priority rule in Section 9-330
18 remains applicable to possessory statutory liens.

19 7. **Investment Property; Letters of Credit; Deposit Accounts.**
20 Subsection (a)(6) is new. It reflects that a security interest in investment property,
21 letter-of-credit rights, and a deposit account may be perfected by control under
22 Section 9-312.

23 8. **Assignments of Perfected Security Interests.** Subsection (b) concerns
24 assignment of a perfected security interest. It provides that no filing is necessary in
25 connection with an assignment of a perfected security interest by a secured party to
26 an assignee in order to maintain perfection as against creditors and transferees of
27 the debtor. Although subsection (b) addresses explicitly only the absence of an
28 additional filing requirement, the same result normally will follow in the case of an
29 assignment of a security interest perfected in a manner other than by filing, such as
30 by control, by possession, or by compliance with a statute, regulation, or treaty
31 under Section 9-309A(c). For example, as long as possession of collateral is
32 maintained by an assignee or by the assignor or another person on behalf of the
33 assignee, no further perfection steps need be taken on account of the assignment.
34 Of course, additional action may be required for perfection of the assignee's interest
35 as against creditors and transferees of the *assignor*.

36 **SECTION 9-309A. PERFECTION OF SECURITY INTERESTS IN**
37 **PROPERTY SUBJECT TO CERTAIN STATUTES, REGULATIONS, AND**
38 **TREATIES.**

1 (a) Except as otherwise provided in subsection (b), the filing of a financing
2 statement is not necessary or effective to perfect a security interest in property
3 subject to:

4 (1) a statute, regulation, or treaty of the United States whose
5 requirements for a security interest's obtaining priority over the rights of a lien
6 creditor with respect to the property preempt Section 9-309(a); [or]

7 (2) [list any certificate-of-title statute covering automobiles, trailers,
8 mobile homes, boats, farm tractors, or the like, which provides for a security
9 interest to be indicated on the certificate as a condition or result of perfection, and
10 any non-UCC central filing statute] [.] [; or]

11 (3) a certificate-of-title statute of another jurisdiction which provides for
12 a security interest to be indicated on the certificate as a condition or result of the
13 security interest's obtaining priority over the rights of a lien creditor with respect to
14 the property.]

15 (b) During any period in which collateral is inventory held for sale or lease
16 by a person or leased by that a person as lessor and that person is in the business of
17 selling or leasing goods of that kind; subsection[s] (a)(2) [does] [and (a)(3) do] not
18 apply to a security interest in that collateral created by that person as debtor.

19 (c) (1) Compliance with the requirements prescribed by a statute,
20 regulation, or treaty described in subsection (a) for obtaining priority over the rights
21 of a lien creditor is equivalent to the filing of a financing statement under this
22 article.

23 (2) Except as otherwise provided in Sections 9-311 and 9-314(c) for
24 goods covered by a certificate of title, a security interest in property subject to a
25 statute, regulation, or treaty described in subsection (a) may be perfected only by
26 compliance with those requirements, and a security interest so perfected remains

1 perfected notwithstanding a change in the use or transfer of possession of the
2 collateral.

3 (3) Except as otherwise provided in Section 9-314(c), duration and
4 renewal of perfection of a security interest perfected by compliance with the
5 requirements prescribed by the statute, regulation, or treaty are governed by the
6 statute, regulation, or treaty. In other respects the security interest is subject to this
7 article.

8 Reporters' Comments

9 1. **Source.** Former Section 9-302(3), (4).

10 2. **Federal Statutes, Regulations, and Treaties.** Subsection (a)(1)
11 provides explicitly that the filing requirement of this Article defers only to federal
12 statutes, regulations, or treaties whose requirements for a security interest's
13 obtaining priority over the rights of a lien creditor preempt Section 9-309(a). The
14 provision eschews reference to the term "perfection, inasmuch as Section 9-308
15 specifies the meaning of that term and a preemptive rule may use other
16 terminology.

17 3. **Forum's Certificate-of-title Statute.** The description of certificate-of-
18 title statutes in subsection (a)(2) has been revised to track the language of Section
19 9-303.

20 4. **Foreign Jurisdiction's Certificate-of-title Statute.** Subsection (a)
21 retains paragraph (3) (former Section 9-302(3)(c)), with appropriate revisions to
22 conform that paragraph to Section 9-303. However, paragraph (3) appears in
23 brackets because Section 9-303 apparently makes the paragraph unnecessary.
24 Assume that a court is applying Section 9-309A as enacted in State B. If goods are
25 covered by a State A certificate of title and State B has not issued a certificate, then
26 State A's law, including its Section 9-309A(a)(2), will apply. Once application is
27 made for a State B certificate, State B's law will apply, including State B's Sections
28 9-303(b) and 9-309A(a)(2). There seems to be no room for a security interest to be
29 perfected *under the law of State B* through compliance with *State A's certificate-of-*
30 *title act*. Note, however, that State B's 9-314(c) does terminate perfection if
31 perfection would have lapsed under the law of State A.

32 5. **Inventory Covered by a Certificate of Title.** Under subsection (d),
33 perfection of a security interest in the inventory of a dealer is governed by the
34 normal perfection rules, even if the inventory is covered by a certificate of title.
35 Under former Section 9-302(3), a secured party who finances a dealer may need to
36 perfect by filing for goods held for sale and by compliance with a certificate-of-title
37 statute for goods held for lease. In some cases, this may require notation on
38 thousands of certificates. The problem is compounded by the fact that dealers,
39 particularly of automobiles, often do not know whether a particular item of

1 inventory will be sold or leased. Under subsection (d), notation is both unnecessary
2 and ineffective.

3 The filing and other perfection provisions of this Article apply to goods
4 covered by a certificate of title only “during any period in which collateral is
5 inventory held for sale or lease or leased. If the debtor takes goods of this kind out
6 of inventory and uses them, say, as equipment, a filed financing statement would
7 not remain effective to perfect a security interest.

8 The phrase “held for sale or lease or leased by a person who is in the
9 business of selling or leasing goods” is intended to include inventory in the
10 possession of a lessee from a dealer. The definition of “inventory” (former Section
11 9-101(4)) contains a similar phrase, but omits any reference to goods that are
12 “leased. Section 9-106(d) conforms the definition of inventory to Section
13 9-309A(a)(2) by including a reference to “leased” goods. (See also former Section
14 9-103(3)(a), which seems to distinguish goods “leased” and goods “held for lease.”)

15 **6. Compliance with Perfection Requirements of Other Statute.**

16 Subsection (c) clarifies former Section 9-302(4) by providing that compliance with
17 the perfection requirements (i.e., the requirements for obtaining priority over a lien
18 creditor), but not other requirements, of a statute, regulation, or treaty described in
19 subsection (a) is equivalent to filing and is sufficient for perfection under this
20 Article.

21 The Study Committee recommended that Article 9 preempt non-UCC law
22 in this regard and provide that perfection occurs “upon receipt by appropriate state
23 officials of a properly tendered application for a certificate of title on which the
24 security interest is to be indicated. Recommendation 22.A. The draft does not
25 include such a preemptive rule in Article 9 itself. We recognize that, in
26 jurisdictions where perfection occurs upon issuance of a certificate, the absence of a
27 preemptive rule may create a gap between the time that the goods are “covered” by
28 the certificate under Section 9-303 and the time of perfection and also may result in
29 turning some unobjectionable transactions into avoidable preferences under
30 Bankruptcy Code § 547. (The preference risk arises if more than ten days passes
31 between the time a security interest attaches and the time it is perfected.) A Note
32 that instructs the legislature to amend the applicable certificate-of-title act to reflect
33 the result urged by the Study Committee seems appropriate. Unless adjustments are
34 made to a certificate-of-title act itself, conflicting rules in the Act and Article 9
35 could create confusion and uncertainty.

36 Under some certificate-of-title statutes, including the Uniform Motor
37 Vehicle Certificate of Title and Anti-Theft Act, perfection generally occurs upon
38 delivery of specified documents to a state official but may, under certain
39 circumstances, relate back to the time of attachment. This relation-back feature can
40 create great difficulties for the application of the rules in Sections 9-303 and
41 9-309A(c). Accordingly, we suggest that this Article include a Note recommending
42 to legislatures that they remove any relation-back provisions from certificate-of-title
43 laws affecting security interests.

44 **7. Compliance with Other Statute as Equivalent of Filing.** Like former
45 Section 9-302(4), subsection (c) provides that compliance with a statute or treaty

described in subsection (a) (former Section 9-302(3)) “is equivalent to the filing of a financing statement. The meaning of this phrase currently is unclear, and many questions have arisen concerning the extent to which and manner in which Article 9 rules referring to “filing” are applicable to perfection by compliance with a certificate-of-title statute. There are at least three separate approaches for applying Article 9 filing rules to compliance with other statutes and treaties. First, as discussed in Comment 6 above, there are rules such as the rule establishing time of perfection (Section 9-515(a)) that we believe should be determined by the other statutes themselves. Second, some Article 9 filing rules can be applied to perfection under other statutes or treaties by revisions to the Article 9 text. Examples are Section 9-309(b) and Section 9-505. Third, other Article 9 rules may be made applicable to security interests perfected by compliance with another statute through the “equivalent to . . . filing” provision in the first sentence of Section 9-309A(c). We suggest that the third approach be reflected for the most part in the Official Comments. Official Comments could be added to various sections to explain how particular rules apply when perfection is accomplished under Section 9-309A(c). In the alternative, the Official Comments to Section 9-309A could be expanded to explain the “equivalent to . . . filing” concept as making applicable to the other statutes and treaties all references in Article 9 to “filing,” “financing statement,” and the like.

8. Perfection by Possession of Goods Covered by a Certificate-of-title Statute. A secured party that has perfected a security interest under the law of State A in goods that subsequently are covered by a State B certificate of title may face a predicament. Ordinarily, the secured party will have four months under State B’s Section 9-314(c) in which to (re)perfect by having its security interest noted on a State B certificate. This procedure is likely to require the cooperation of the debtor and any competing secured party whose security interest has been noted on the certificate. Official Comment 4(e) to former Section 9-103 observes that “that cooperation is not likely to be forthcoming from an owner who wrongfully procured the issuance of a new certificate not showing the out-of-state security interest, or from a local secured party finding himself in a priority contest with the out-of-state secured party. According to the Comment, “[t]he only solution for the out-of-state secured party under present certificate of title laws seems to be to reperfect by possession, i.e., by repossessing the goods. But, as the Report observes, the “solution” may not work. Report, 176. Former Section 9-302(4) provides that a security interest in property subject to a certificate-of-title statute “can be perfected only by compliance therewith.

This Article resolves the conflict in Sections 9-314(c), 9-309A(c), and 9-311(b) to provide that a security interest that remains perfected solely by virtue of Section 9-314(c) can be (re)perfected by the secured party’s taking possession of the collateral. These sections contemplate only that taking possession of goods covered by a certificate of title will work as a method of perfection. None of these sections creates a right to take possession. Section 9-609 and the agreement of the parties define the secured party’s right to take possession.

SECTION 9-310. PERFECTION OF SECURITY INTERESTS IN INSTRUMENTS, CHATTEL PAPER, INVESTMENT PROPERTY,

1 **DOCUMENTS, MONEY, DEPOSIT ACCOUNTS, ~~LETTERS~~ LETTER-OF-**
2 **CREDIT RIGHTS, AND GOODS COVERED BY DOCUMENTS;**
3 **PERFECTION BY PERMISSIVE FILING; TEMPORARY PERFECTION**
4 **WITHOUT FILING OR TRANSFER OF POSSESSION.**

5 (a) (1) A security interest in instruments, chattel paper, investment
6 property, or negotiable documents may be perfected by filing.

7 (2) Except as otherwise provided in Section 9-313(e) for cash proceeds,
8 a security interest in:

9 (A) money may be perfected only by the secured party's taking
10 possession under Section 9-311;

11 (B) ~~a security interest in~~ a deposit account may be perfected only by
12 control under Section 9-312; and

13 (C) ~~except as otherwise provided in Section 9-308(d) for support~~
14 ~~obligations, a security interest in a letter-of-credit rights and proceeds of the letter~~
15 ~~of credit~~ may be perfected only by control under Section 9-312, except as otherwise
16 provided in Section 9-308(d).

17 (b) While goods are in the possession of a bailee that has issued a
18 negotiable document under Section 7-104(1) [or federal law] covering the goods, a
19 security interest in the goods:

20 (1) is perfected by perfecting a security interest in the document, and

21 (2) any security interest in the goods otherwise perfected during the
22 period is subordinate to the security interest perfected in the document.

23 (c) A security interest in goods in the possession of a bailee that has issued
24 a non-negotiable document under Section 7-104(2) [or federal law] covering the
25 goods is perfected by:

26 (1) issuance of a document in the name of the secured party;

1 (2) ~~by~~ the bailee's receipt of notification of the secured party's interest;

2 or

3 (3) ~~by~~ filing as to the goods.

4 (d) A security interest in instruments, certificated securities, or negotiable
5 documents is perfected without filing or the taking of possession for a period of 20
6 days from the time it attaches to the extent that it arises for new value given under
7 an authenticated security agreement.

8 (e) A security interest remains perfected for 20 days without filing if a
9 secured party having a perfected security interest in an instrument, a certificated
10 security, a negotiable document, or goods in possession of a bailee other than one
11 that has issued a negotiable document for the goods:

12 (1) makes available to the debtor the goods or documents representing
13 the goods for the purpose of:

14 (A) ultimate sale or exchange; or

15 (B) ~~for the purpose of~~ loading, unloading, storing, shipping,
16 transshipping, manufacturing, processing, or otherwise dealing with them in a
17 manner preliminary to their sale or exchange, but priority among conflicting
18 security interests in the goods is subject to Section 9-322; or

19 (2) delivers the instrument or certificated security to the debtor for the
20 purpose of:

21 (A) ultimate sale or exchange; or

22 (B) ~~of~~ presentation, collection, enforcement, renewal, or registration
23 of transfer.

24 (f) After the 20-day period specified in subsection (d) [~~or~~] [and] (e) expires,
25 perfection depends upon compliance with this article.

26 Reporters' Comments

1 1. **Source.** Former Section 9-304, with additions and some minor changes.

2 2. **Instruments.** Under subsection (a), a security interest in instruments
3 may be perfected by filing. This security interest is subject to defeat by subsequent
4 purchasers (including secured parties). Section 9-328 provides that filing a
5 financing statement does not constitute notice that would preclude a subsequent
6 purchaser from becoming a holder in due course and taking free of all claims under
7 Section 3-306. Moreover, if Section 9-327 is made applicable to instruments,
8 purchasers that take possession of an instrument and give new value generally
9 would achieve priority over a security interest in the instrument perfected by filing.

10 3. **Deposit Accounts.** Under new subsection (a)(2), the only means of
11 perfecting a security interest in a deposit account as original collateral is by control.
12 Filing is ineffective, except as provided in Section 9-313 with respect to proceeds.
13 As defined in Section 9-109, “control” can arise as a result of an agreement among
14 the secured party, debtor, and depository institution, whereby the last agrees to
15 comply with instructions of the first with respect to disposition of the funds on
16 deposit, even though the debtor retains the right to direct disposition of the funds.
17 Thus, subsection (a)(2) takes an intermediate position between certain non-UCC
18 law, which conditions the effectiveness of a security interest on the secured party’s
19 enjoyment of such dominion and control over the deposit account that the debtor is
20 unable to dispose of the funds, and the approach this Article takes to securities
21 accounts (approved by the Conference as part of the Article 8 revisions in 1994),
22 under which a secured party who is unable to reach the collateral without resort to
23 judicial process may perfect by filing. By conditioning perfection on “control,”
24 subsection (a)(2) accommodates the views of those who think that a secured party
25 who wishes to rely upon a deposit account should take steps to be able to reach the
26 funds upon the debtor’s default without having to resort to the judicial process. It
27 also accommodates those who think that a more stringent perfection requirement--
28 e.g., requiring the secured party to achieve absolute dominion and control, to the
29 exclusion of the debtor--would prevent perfection in transactions in which the
30 secured party actually relies on the deposit account and maintains some meaningful
31 control over it.

32 4. **Letter-of-Credit Rights.** Letter-of-credit rights commonly are “support
33 obligations,” as defined in Section 9-102. Perfection as to the related account,
34 chattel paper, document, instrument, [insurance policy,] general intangible, or
35 investment property will perfect as to the letter-of-credit rights. See Section
36 9-308(d). Subsection (a)(3) provides, except for perfection under Section 9-308(d)
37 as support obligations, a security interest in a letter of credit or the proceeds of the
38 letter of credit may be perfected only by control.

39 5. **Goods in Possession of Bailee.** The rule in subsection (c) has been
40 limited to goods in the possession of a bailee that has issued a non-negotiable
41 document of title under Article 7 [or federal law]. Subsection (b) applies to goods
42 in the possession of a bailee that has issued a negotiable document. Section 9-311
43 governs perfection of a security interest in goods in the possession of a bailee that
44 has not issued a document of title.

45 The perfection step under subsection (c) occurs when the bailee receives
46 notification of the secured party’s interest in the goods, regardless of who sends the

1 notification. Receipt of notification is effective to perfect regardless of whether the
2 bailee attorns to the secured party. Compare Section 9-311(c) (perfection by
3 possession as to goods not covered by a document requires bailee's
4 acknowledgment).

5 **6. Maintaining Perfection After Surrendering Possession.**

6 "Enforcement has been added in subsection (e) as one of the special and limited
7 purposes for which a secured party can release an instrument or certificated security
8 to the debtor and still remain perfected.

9 **7. Length of Temporary Perfection.** The time periods in subsections (d),
10 (e), and (f) have been reduced from 21 to 20 days, which is the time period
11 generally applicable in this Article.

12 **SECTION 9-311. WHEN POSSESSION BY SECURED PARTY**
13 **PERFECTS SECURITY INTEREST WITHOUT FILING.**

14 (a) Except as otherwise provided in subsection (b), a security interest in
15 goods, instruments, money, negotiable documents, or chattel paper may be
16 perfected by the secured party's taking possession of the collateral. a security
17 interest in certificated securities may be perfected by the secured party's taking
18 possession of the security certificates.

19 (b) A security interest in goods covered by a certificate of title issued by
20 this State may be perfected by the secured party's taking possession of the collateral
21 only in the circumstances described in Section 9-314(c).

22 (c) (1) This subsection applies to collateral other than goods covered by a
23 document.

24 (2) A secured party acquires possession of collateral ~~If the collateral is~~
25 in the possession of a person other than the debtor, the secured party, or a lessee of
26 the collateral from the debtor in the ordinary course of the debtor's business, ~~the~~
27 ~~secured party takes possession~~ when:

28 (A) the person in possession signs a record acknowledging that it
29 holds possession for the secured party's benefit; or

1 (B) ~~the If a person, other than the debtor, the secured party, or a~~
2 ~~lessee of the collateral from the debtor in the ordinary course of the debtor's~~
3 ~~business, takes possession of the collateral after having authenticated a record~~
4 ~~acknowledging that it will hold possession of collateral for the secured party's~~
5 ~~benefit, the secured party takes possession when the person takes possession.~~

6 (3) {A security interest is perfected by possession when the secured
7 party takes possession, without a relation back, and continues only while the
8 secured party retains possession, unless otherwise provided in this article.}

9 (d) A person in possession of collateral is not required to acknowledge that
10 it holds possession for a secured party's benefit.

11 (e) If a person acknowledges that it holds possession for the secured party's
12 benefit:

13 (1) the acknowledgment is effective under subsection (c) even if the
14 acknowledgment violates the rights of a debtor; and

15 (2) unless the person otherwise agrees or other law otherwise provides,
16 the person owes no duties to the secured party and is not required to confirm the
17 acknowledgment to another person.

18 [(f) A security interest may be perfected as otherwise provided in this
19 article before or after a period of possession by a secured party.]

20 Reporters' Comments

21 **Change from Prior Draft:** Brackets removed from subsection (c)(3) and
22 added to subsection (f). Is the latter subsection necessary?

23 1. **Source.** Former Sections 9-305; 9-115(6).

24 2. **Certificated Securities.** The second sentence of subsection (a) reflects
25 the traditional rule for perfection of a security interest in certificated securities.
26 Compare Sections 9-115(4)(a), 8-106(a), 9-115(6) (1994 Official Text); Sections
27 8-321, 8-313(1)(a) (1978 Official Text); Section 9-305 (1972 Official Text).

28 3. **Goods Covered by a Certificate of Title.** Subsection (b) is necessary to
29 effect changes to the choice-of-law rules governing goods covered by a certificate

of title. These changes are described in the Reporters' Comments to Section 9-309. Subsection (b), like subsection (a), does not create a right to take possession. Rather, it indicates the circumstances under which the secured party's taking possession of goods covered by a certificate of title is effective to perfect a security interest in the goods.

4. Goods in Possession of a Third Party: Perfection. Former Section 9-305 permits perfection of a security interest by notification to a bailee in possession of collateral. This Article distinguishes between goods in the possession of a bailee that has issued an Article 7 [or federal] document of title covering the goods and goods in the possession of a third party that has not issued a document. Section 9-310(b) or (c) applies to the former, depending on whether the document is negotiable; Section 9-311(c) applies to the latter.

Notification of a third person does not suffice to perfect under Section 9-311(c). Rather, perfection does not occur unless the third person authenticates an acknowledgment that it holds possession of the collateral for the secured party's benefit. Compare Section 9-310(c), under which receipt of notification of the security party's interest by a bailee holding goods subject to a non-negotiable document is sufficient to perfect, even if the bailee does not acknowledge receipt of the notification. a third person may acknowledge that it will hold for the secured party's benefit goods to be received in the future. Under these circumstances, perfection by possession occurs when the third person obtains possession of the goods.

Under subsection (c), acknowledgment of notification by a lessee in ordinary course of business (as defined in Section 2A-103) does not suffice for possession. The section thus rejects the reasoning of *In re Atlantic Systems, Inc.*, 135 B.R. 463 (Bankr. S.D.N.Y. 1992) (holding that notification to debtor-lessor's lessee sufficed to perfect security interest in leased goods). See Steven O. Weise, *Perfection by Possession: The Need for an Objective Test*, 29 Idaho Law Rev. 705 (1992-93) (arguing that lessee's possession in ordinary course of debtor-lessor's business does not provide adequate public notice of possible security interest in leased goods). Inclusion of a per se rule concerning lessees is not meant to preclude a court, under appropriate circumstances, from determining that a third person is so closely connected to or controlled by the debtor that the debtor has retained effective possession. If so, the third person's acknowledgment would not be sufficient for perfection.

The brackets around the last sentence of subsection (c) reflect uncertainty about whether the sentence is necessary and, if so, where it should appear.

5. Goods in Possession of a Third Party: Consequences of Acknowledgment. Subsections (e) and (f) are new and address matters as to which former Article 9 is silent. They derive in part from Section 8-106(g). Subsection (e) provides that a person in possession of collateral is not required to acknowledge that it holds for a secured party. Subsection (f) provides that an acknowledgment is effective even if wrongful as to the debtor and that, in the absence of the person's agreement, the person has no responsibilities to a secured party by virtue of its making an acknowledgment. For example, by acknowledging, a third party does not become obliged to act on the secured party's direction or to remain in

1 possession of the collateral. Arrangements involving the possession of goods are
2 hardly standardized. They include bailments for services to be performed on the
3 goods (such as repair or processing), for use (leases), as security (pledges), for
4 carriage, and for storage. This Article leaves to the agreement of the parties and to
5 any other applicable law the imposition of duties and responsibilities upon a person
6 who acknowledges under subsection (d). The purpose of subsections (e) and (f) is
7 to make clear that an acknowledgment does not give rise to any such duties or
8 responsibilities under this Article.

9 6. **“Possession.”** This section does not define “possession. In
10 determining whether a particular person has possession, the principles of agency
11 apply. For example, if the collateral clearly is in possession of an agent of the
12 secured party for the purposes of possessing on behalf of the secured party, and if
13 the agent is not also an agent of the debtor, the secured party has taken actual
14 possession without the need to rely on a third-party acknowledgment. However, if
15 the agent is an agent of both the secured party and the debtor, prudence might
16 suggest that the secured party obtain the agent’s acknowledgment in order to ensure
17 perfection by possession.

18 SECTION 9-312. PERFECTION BY CONTROL.

19 (a) A security interest in investment property, a deposit account, or a letter-
20 of-credit rights ~~and proceeds of the letter of credit~~ may be perfected by control of
21 the collateral under Section 9-108, 9-109, or 9-110.

22 (b) A security interest is perfected by control from the time the secured
23 party obtains control [without a relation back] and continues only while control is
24 retained[, unless otherwise provided in this article].

25 (c) A security interest may be otherwise perfected as provided in this article
26 before or after the period of control by the secured party.

27 Reporters’ Comments

28 1. **Source.** New.

29 2. **Control.** This section provides for perfection by control with respect to
30 letters of credit and proceeds of letters of credit, deposit accounts, and investment
31 property.

32 SECTION 9-313. “PROCEEDS”; SECURED PARTY’S RIGHTS ON 33 DISPOSITION OF COLLATERAL AND IN PROCEEDS.

34 (a) “Proceeds means ~~includes~~ the following property:

1 (1) whatever is acquired upon the sale, lease, license, exchange, or other
2 disposition of collateral;

3 (2) whatever is collected on, or distributed on account of, collateral;

4 (3) rights arising out of collateral;

5 (4) to the extent of the value of collateral, claims arising out of the loss
6 or nonconformity of, defects in, or damage to the collateral; and

7 (5) to the extent of the value of collateral and to the extent payable to the
8 debtor or the secured party, insurance payable by reason of the loss or
9 nonconformity of, defects in, or damage to the collateral.

10 (b) "Cash proceeds means money ~~Money~~, checks, deposit accounts, and
11 the like ~~are "cash proceeds."~~ "Noncash proceeds means all ~~All~~ other proceeds ~~are~~
12 ~~"noncash proceeds."~~

13 (c) (1) Except as otherwise provided in this article, a security interest;

14 (A) continues in collateral notwithstanding sale, lease, license,
15 exchange, or other disposition thereof unless the secured party authorized the
16 disposition free of the security interest [in the security agreement or otherwise]; and

17 (B) ~~also~~ attaches to any identifiable proceeds.

18 (2) Other law determines whether a statutory lien continues on
19 collateral notwithstanding disposition or becomes effective as to proceeds.

20 (d) Proceeds that are commingled with other property are identifiable
21 proceeds:

22 (1) if the proceeds are goods, to the extent provided by Section 9-333;

23 and

24 (2) if the proceeds are not goods, to the extent that the secured party
25 identifies the proceeds by a method of tracing, including application of equitable

1 principles, that is permitted under other law with respect to commingled property of
2 the type involved.

3 (e) (1) A security interest in or a statutory lien on proceeds is a perfected
4 security interest or statutory lien if the interest in or lien on the original collateral
5 was perfected.

6 (2) The security interest in or statutory lien on proceeds ceases to be a
7 perfected security interest or statutory lien and becomes unperfected on the 21st day
8 after the security interest attaches to the proceeds or the statutory lien becomes
9 effective as to the proceeds unless:

10 (A) (i) a filed financing statement covers the original collateral;

11 (ii) ~~and~~ the proceeds are collateral in which a security interest
12 may be perfected by filing in the office in which the financing statement has been
13 filed; and

14 (iii) if the proceeds are acquired with cash proceeds or funds
15 from a deposit account, the description of collateral in the financing statement
16 indicates the type of property constituting the proceeds;

17 (B) the proceeds are identifiable cash proceeds; or

18 (C) the security interest in or statutory lien on the proceeds is
19 perfected within 20 days after the security interest attaches to the proceeds or the
20 statutory lien becomes effective as to the proceeds.

21 (f) Except as otherwise provided in subsection (e), a security interest in or
22 statutory lien on proceeds may be perfected only by the methods or under the
23 circumstances permitted in this article for original collateral of the same type.

24 (g) If a filed financing statement covers the original collateral, a security
25 interest in or statutory lien on proceeds which remains perfected under subsection
26 (e)(2)(a) ~~(e)(1)~~ becomes unperfected at the later of:

1 (1) when the effectiveness of the filed financing statement lapses under
2 Section 9-516 or is terminated under Section 9-511; and
3 (2) ~~but in no event before~~ the 21st day after the security interest attaches
4 to the proceeds or the statutory lien becomes effective as to the proceeds.

Reporters' Comments

1. **Source.** Former Section 9-306.

2. **What Constitutes Proceeds.** Subsection (a) expands the definition of proceeds beyond that contained in former Section 9-306 and resolves ambiguities in the former section.

a. **Distributions on Account of Collateral.** The phrase “whatever is . . . distributed on account of, collateral,” in subsection (a)(2), is broad enough to cover cash or stock dividends distributed on account of securities or other investment property that is original collateral. Compare former Section 9-306 (1994 Official Text) (“Any payments or distributions made with respect to investment property collateral are proceeds. ”). This section rejects the holding of *Hastie v. FDIC*, 2 F.3d 1042 (10th Cir. 1993) (holding that post-petition cash dividends on stock subject to pre-petition pledge are not “proceeds” under Bankruptcy Code § 552(b)) to the extent the holding relies on the Article 9 definition of “proceeds.”

b. **Distributions on Account of Support Obligations.** Subsection (a)(2) makes explicit what is implicit under current law: Collections and distributions under collateral consisting of various credit support arrangements (“support obligations,” as defined in Section 9-102) are afforded treatment identical to proceeds collected from or distributed by the obligor on the underlying (supported) right to payment or other intangible collateral. Proceeds of support obligations also are proceeds of the underlying rights to payment or intangible.

c. **Proceeds of Proceeds.** The definition of “proceeds” no longer provides that proceeds of proceeds are themselves proceeds. This idea is expressed in the revised definition of “collateral” in Section 9-102. No change in meaning is intended.

d. **Proceeds Received by Person Who Did Not Create Security Interest.** When collateral is sold subject to a security interest and the buyer then resells the collateral, a question has arisen under former Article 9 concerning whether the “debtor” has “received” what the buyer received on resale and, therefore, whether those receipts are “proceeds.” See former Section 9-306(2). This Article contains no requirement that property be “received” by the debtor for the property to qualify as proceeds. It is necessary only that the property be traceable, directly or indirectly, to the original collateral.

3. **Authorized Dispositions.** Subsection (c), which derives from existing subsection (2), makes explicit that the authorized disposition to which it refers is an authorized disposition “free of” security interests. See PEB Commentary No. 3. The change in language is not intended to address the frequently-litigated situation in which the effectiveness of the secured party’s consent to a disposition is conditioned upon the secured party’s receipt of the proceeds. In that situation, subsection (c) would leave the determination of authorization to the courts, as under current law.

4. **Identifiability; Tracing.** Subsection (d) is new. It indicates when proceeds commingled with other property are identifiable proceeds. The “equitable

1 principles to which subsection (d) refers may include the “lowest intermediate
2 balance rule. See Restatement of Trusts, Second, § 202.

3 **5. Automatic Perfection in Proceeds.** This Article extends the period of
4 automatic perfection in proceeds from 10 days to 20 days, commencing with the
5 day the security interest attaches to the proceeds. See subsection (e). The loss of
6 perfected status under subsection (e) is prospective only. Compare, e.g., Section
7 9-516(a) (deeming security interest unperfected retroactively).

8 **a. Proceeds Acquired with Cash Proceeds or Funds from Deposit**
9 **Account.** Under former Section 9-306(3)(a), a security interest in proceeds remains
10 perfected beyond the period of automatic perfection if a filed financing statement
11 covers the original collateral and the proceeds are collateral in which a security
12 interest may be perfected by filing in the office where the financing statement has
13 been filed. a different rule applies if the proceeds are acquired with cash proceeds,
14 as is the case if the original collateral (inventory) is sold for cash (cash proceeds)
15 that is used to purchase equipment (proceeds). Under these circumstances, the
16 security interest in the equipment proceeds remains perfected only if the description
17 in the filed financing indicates the type of property constituting the proceeds
18 (equipment). Subsection (e)(1) of this Article applies the rule of former Section
19 9-306(3)(a) to proceeds that have been acquired with funds from a deposit account
20 serving as original collateral.

21 Security interests in the proceeds of bank accounts evidenced by an
22 instrument (e.g., certain certificates of deposit), which by definition are not “deposit
23 accounts, would be governed by the rules applicable to proceeds of instruments
24 generally.

25 **b. Continuation of Perfection in Cash Proceeds.** Former subsection
26 (3)(b) provides that if a filed financing statement covers original collateral, a
27 security interest in cash proceeds of the collateral remains perfected beyond the ten-
28 day period of automatic perfection. Subsection (e)(2) extends the benefits of
29 former paragraph (3)(b) to proceeds of original collateral in which a security
30 interest is perfected by a method other than filing. This subsection provides that if
31 the security interest in the original collateral was perfected, a security interest in
32 identifiable cash proceeds will remain perfected indefinitely, regardless of whether
33 the security interest in the original collateral remains perfected.

34 **6. Transferees of Cash Proceeds.** The former text of and Official
35 Comments to Section 9-306 do not deal adequately with the rights of a person to
36 whom the debtor has transferred cash proceeds, such as a person who receives
37 payment of a check drawn on a deposit account constituting proceeds. Section
38 9-329 addresses this issue.

39 **7. Insolvency Proceedings; Returned and Repossessed Goods.** This
40 Article deletes former subsection (4), which deals with proceeds in insolvency
41 proceedings, and former subsection (5), which deals with returned and repossessed
42 goods. In the absence of Section 9-306(5), Official Comments to Section 9-327
43 will explain and clarify the application of priority rules to returned and repossessed
44 goods as proceeds of chattel paper.

1 **8. Proceeds of Collateral Subject to Statutory Lien.** Subsection (c),
2 which gives a secured party an interest in proceeds automatically, applies only to
3 collateral encumbered by a security interest. If collateral is encumbered by a
4 statutory lien, other law (e.g. the statute giving rise to the statutory lien), and not
5 subsection (c), determines the extent to which the lien continues in proceeds. Only
6 if other law provides that the statutory lien covers proceeds do the rules relating to
7 continued perfection of security interests in proceeds (i.e., subsections (e), (f), and
8 (g)) apply to the proceeds.

9 **9. Lapse or Termination of Financing Statement During 20-day Period.**
10 Subsection (g) provides that a security interest in or statutory lien on proceeds
11 perfected under subsection (e)(1) ceases to be perfected when the financing
12 statement covering the original collateral lapses or is terminated. If the lapse or
13 termination occurs before the 21st day after the security interest or statutory lien
14 attaches, however, the security interest in or statutory lien on the proceeds remains
15 perfected until the 21st day. Section 9-309A(c) provides that compliance with the
16 perfection requirements of a statute or treaty described in Section 9-309A(a) “is
17 equivalent to the filing of a financing statement. It follows that collateral subject
18 to a security interest perfected by such compliance under Section 9-309A(c) is
19 covered by a “filed financing statement” within the meaning of Section 9-313(e)(1)
20 and (g).

1 **SECTION 9-314. [CONTINUED] PERFECTION OF SECURITY**
2 **INTEREST OR STATUTORY LIEN FOLLOWING CHANGE IN**
3 **APPLICABLE LAW.**

4 (a) (1) A security interest perfected pursuant to the law designated in
5 Section 9-301(1) or a statutory lien perfected pursuant to the law designated in
6 Section 9-302(1) remains perfected until the earliest of:

7 (A) the expiration of four months after a change of the debtor's
8 location to another jurisdiction;

9 (B) the expiration of four months after a transfer of collateral to a
10 debtor located in another jurisdiction;

11 (C) the expiration of four months after a new debtor located in
12 another jurisdiction becomes bound under Section 9-203(c); [or] [and]

13 (D) the time perfection would have ceased under the law of the first
14 jurisdiction.

15 (2) If the security interest or statutory lien becomes perfected under the
16 law of the other jurisdiction before the end of that period, it continues perfected
17 thereafter.

18 (3) If the security interest does not become perfected under the law of
19 the other jurisdiction before the end of that period ~~Otherwise~~, it becomes
20 unperfected and is deemed never to have been perfected as against a previous or
21 subsequent purchaser of the collateral for value.

22 (b) A possessory security interest in collateral, other than goods covered by
23 a certificate of title and as-extracted collateral consisting of goods, remains
24 continuously perfected if:

25 (1) the collateral is located in one jurisdiction and subject to a security
26 interest perfected under the law of that jurisdiction;

(2) thereafter the collateral is brought into another jurisdiction; and

(3) upon entry into the other jurisdiction the security interest is perfected under the law of the other jurisdiction.

4 Alternative A

(c) (1) A security interest in goods covered by a certificate of title which is perfected by any method under the law of another jurisdiction when the goods become covered by a certificate of title from this jurisdiction remains perfected until the earlier of:

9 (A) the time the security interest would have become unperfected
10 under the law of the other jurisdiction had the goods not become so covered; [or]
11 [and]

12 (B) the expiration of four months after the goods had become so
13 covered.

(2) If the security interest becomes perfected under Section 9-309A(c) or 9-311 before the earlier of that time [or] [and] the expiration of that period, it continues perfected thereafter.

17 (3) If the security interest does not become perfected under one of those
18 sections before the earlier of that time or the end of that period Otherwise, it
19 becomes unperfected and is deemed never to have been perfected as against a
20 previous or subsequent purchaser of the collateral for value.

21 **Alternative B**

(c) (1) A security interest in goods covered by a certificate of title which is perfected by any method under the law of another jurisdiction when the goods become covered by a certificate of title from this jurisdiction remains perfected until the security interest would have become unperfected under the law of the other jurisdiction had the goods not become so covered.

1 (2) A security interest becomes unperfected as against a purchaser of
2 the goods for value and is deemed never to have been perfected as against a
3 previous or subsequent purchaser of the collateral for value However, if the
4 applicable requirements for perfection under Section 9-309A(c) or 9-311 are not
5 satisfied before the earlier of the time:

6 (A) the security interest would have become unperfected under the
7 law of the other jurisdiction had the goods not become so covered; [or] [and]

8 (B) the expiration of four months after the goods had become so
9 covered, ~~the security interest becomes unperfected as against a purchaser of the~~
10 ~~goods for value and is deemed never to have been perfected as against a previous or~~
11 ~~subsequent purchaser of the collateral for value.~~

12 **End of Alternatives**

13 (d) (1) A security interest in deposit accounts[, a letter-of-credit rights ~~or~~
14 ~~proceeds of the letter of credit,~~] [or investment property] perfected under the law of
15 the depository institution's jurisdiction[, the issuer's jurisdiction, a nominated
16 person's jurisdiction,] [, the securities intermediary's jurisdiction, or the commodity
17 intermediary's jurisdiction, as applicable] remains perfected until the earlier of:

18 (A) the expiration of four months after a change of the [depository
19 institution's] [applicable] jurisdiction;[or] [and]

20 (B) the time perfection would have ceased under the law of the first
21 jurisdiction.

22 (2) If the security interest becomes perfected under the law of the other
23 jurisdiction before the end of that period, it continues perfected thereafter.

24 (3) If the security interest does not become perfected under the law of
25 the other jurisdiction before the end of that period Otherwise, it becomes

1 unperfected and is deemed never to have been perfected as against a previous or
2 subsequent purchaser of the collateral for value.

3 [(e) (1) A security interest in a letter-of-credit ~~rights or proceeds of the~~
4 ~~letter of credit~~ perfected by control under the law of the issuer's or nominated
5 person's jurisdiction remains perfected until the earlier of:

6 (A) the expiration of four months after a change of the issuer's or
7 nominated person's jurisdiction; [or] [and]

8 (B) the time perfection would have ceased under the law of the first
9 jurisdiction.

10 (2) If the security interest becomes perfected under the law of the other
11 jurisdiction before the end of that period, it continues perfected thereafter.

12 (3) If the security interest does not become perfected under the law of
13 the other jurisdiction before the end of that period ~~Otherwise~~, it becomes
14 unperfected and is deemed never to have been perfected as against a previous or
15 subsequent purchaser of the collateral for value.]

16 [(f)(1) A security interest in investment property perfected under the law of
17 the securities intermediary's jurisdiction or the commodity intermediary's
18 jurisdiction, as applicable, remains perfected until the earlier of:

19 (A) the expiration of four months after a change of the intermediary's
20 jurisdiction; [or] [and]

21 (B) the time perfection would have ceased under the law of the first
22 jurisdiction.

23 (2) If the security interest becomes perfected under the law of the other
24 jurisdiction before the end of that period, it continues perfected thereafter. If the
25 security interest does not become perfected under the law or the other jurisdiction
26 before the end of that period ~~Otherwise~~, it becomes unperfected and is deemed

- 1 never to have been perfected as against a previous or subsequent purchaser of the
- 2 collateral for value.]

1. **Source.** Former Section 9-103(1)(d), (2)(b), (3)(e).

2. **Retroactive Unperfection.** This section deals with continued perfection of security interests and statutory liens that have been perfected under the law of another jurisdiction. The fact that the law of a particular jurisdiction ceases to govern perfection under Sections 9-301 through 9-307 does not necessarily mean that a security interest or statutory lien perfected under that law automatically becomes unperfected. This section generally provides that a security interest or statutory lien perfected under the law of one jurisdiction remains perfected for four months even though the jurisdiction whose law governs perfection changes.

This section generally follows the approach of former Section 9-103(1)(d) and (3)(e) with respect to the consequences of a secured party's failure to reperfect a security interest within four months after the other jurisdiction's law ceases to apply: the security interest becomes unperfected prospectively and, as against purchasers for value but not as against donees or lien creditors, retroactively. The rule applies to statutory liens, as well. See also Section 9-516 (taking the same approach with respect to lapse). Although this approach creates the potential for circular priorities, the alternative—retroactive unperfection against lien creditors—would create substantial and unjustifiable preference risks.

3. **Goods Covered by a Certificate of Title.** The Drafting Committee has yet to reach consensus on which alternative subsection (c) it prefers. Under both alternatives, the failure to reperfect within four months results in the security interest becoming unperfected both prospectively and retroactively as against purchasers of the goods for value. With respect to prospective unperfection against lien creditors, Alternative A takes the same approach as subsections (a), (d), and (e); i.e., the failure to reperfect results in the security interest becoming unperfected prospectively against lien creditors. However, under Alternative B, a prior perfection under the law of another jurisdiction can remain effective against lien creditors until perfection lapses under the law of the other jurisdiction, which may occur well beyond the four-month period.

4. **Depository Institutions, Letter of Credit Issuers and Nominated Persons, and Securities Intermediaries.** The bracketed language in subsection (d) and the brackets around subsections (e) and (f) raise the issue whether one subsection is adequate to address changes in the jurisdiction of a depository institution, issuer of or nominated person with respect to a letter of credit, securities intermediary, and commodity intermediary, or whether one or more separate subsections are needed.

[SUBPART 3. PRIORITY]

**SECTION 9-315. INTERESTS THAT TAKE PRIORITY OVER AND
TAKE FREE OF UNPERFECTED SECURITY INTEREST OR
AGRICULTURAL LIEN.**

1 (a) An unperfected security interest or agricultural lien is subordinate to the
2 rights of:

3 (1) a person entitled to priority under Section 9-319; and

4 (2) a person that becomes a lien creditor before the security interest or
5 agricultural lien is perfected and before a financing statement covering the
6 collateral is filed.

7 (b) An unperfected statutory lien other than an agricultural lien is
8 subordinate to the rights of a person entitled to priority under Section 9-319A.

9 (c) Except as otherwise provided in subsection (f), a buyer of goods,
10 instruments, documents, a security certificate, or chattel paper which is not a
11 secured party takes free of a security interest if the buyer gives value and receives
12 delivery of the collateral without knowledge of the security interest and before it is
13 perfected.

14 (d) Except as otherwise provided in subsection (f), a lessee of goods takes
15 free of a security interest if the lessee receives delivery of the collateral without
16 knowledge of the security interest and before it is perfected.

17 (e) A buyer of accounts, general intangibles, or investment property other
18 than a security certificate which is not a secured party takes free of a security
19 interest if the buyer gives value without knowledge of the security interest and
20 before it is perfected.

21 (f) Except as otherwise provided in ~~Section~~ Sections 9-316 and 9-317, if a
22 ~~secured party~~ person files a financing statement with respect to a purchase money
23 security interest before or within 20 days after the debtor receives delivery of the
24 collateral, the security interest takes priority over the rights of a buyer, lessee, or
25 lien creditor which arise between the time the security interest attaches and the time
26 of filing.

1. **Source.** Former Section 9-301.

2. **Filed but Unattached Security Interests.** Under former Section 9-301(1)(b), a lien creditor's rights have priority over an unperfected security interest. Perfection requires attachment (former Section 9-303) and attachment requires the giving of value (former Section 9-203). It follows that, if a secured party has filed a financing statement but has not yet given value, an intervening lien creditor whose lien arises after filing but before attachment of the security interest acquires rights that are senior to those of the secured party that later gives value. This result comports with the *nemo dat* concept: When the security interest attaches, the collateral is already subject to the judicial lien.

On the other hand, this result treats the first secured advance differently from all other advances. The special rule for future advances in Section 9-320(b) (former Section 9-301(d)) affords priority to a discretionary advance made by a secured party within 45 days after the lien creditor's rights arise as long as the secured party is "perfected" when the lien creditor's lien arises—i.e., so long as the advance is not the first one and an earlier advance has been made.

Subsection (a)(2) revises former Section 9-301(1)(b) and treats the first advance the same as subsequent advances. That is, a judicial lien that arises after the a financing statement is filed and before the security interest attaches and becomes perfected is subordinate to all advances secured by the security interest.

3. **Security Interests of Consignors and Receivables Buyers.** "Security interest" is defined in Section 1-201(37) to include the interest of a true consignor and the interest of a buyer of certain receivables (accounts, chattel paper, and payment intangibles). A consignee or a seller of receivables each has rights in the collateral that a lien creditor may reach, as long as the competing security interest of the consignor or buyer is unperfected. This is so even though the debtor-consignee or debtor-seller may not have any rights in the collateral as between it and the consignor or buyer. See Section 9-315A.

4. **Receivables Buyers That Are Not Secured Parties.** A buyer of accounts, chattel paper, or payment intangibles can be a person "which is not a secured party" under subsection (c) or (d) only in a transaction that is excluded from Article 9 by Section 9-112(c)(7), (8), (9), or (10).

5. **Statutory Liens.** Subsection (a) subordinates unperfected agricultural liens in the same fashion that it subordinates unperfected security interests. Subsection (b), which is new, incorporates by reference a priority rule governing competing statutory liens and security interests. See Section 9-319A. This Article does not govern the relative priority of a judicial lien creditor and a holder of a non-agricultural statutory lien.

6. **Bulk Sales; Bulk Transfers.** This section deletes the references, contained in prior official texts, to the transferee in bulk and the buyer in a bulk sale. Each of these persons is a "buyer not in ordinary course of business."

7. **“Receives Delivery.”** The Official Comments should clarify when a debtor “receives delivery” of collateral for purposes of subsections (c), (d), and (f).

SECTION 9-315A. RIGHTS AND TITLE OF CONSIGNEE AND SELLER OF ACCOUNT OR CHATTEL PAPER WITH RESPECT TO CREDITORS AND PURCHASERS.

(a) For purposes of determining the rights of creditors of, and purchasers for value of an account or chattel paper from, a debtor that has sold an account or chattel paper, while the buyer's security interest is unperfected, the debtor has rights and title to the account or chattel paper identical to those the debtor sold.

(b) Except as otherwise provided in subsection (c), for For purposes of determining the rights of creditors of, and purchasers for value of goods from, a consignee, ~~while goods are in the possession of the consignee and the consignor's security interest is unperfected,~~ the consignee has rights and title to the goods identical to those the consignor had or had power to transfer while the goods are in the possession of the consignee.

(c) For purposes of determining the rights of a creditor of a consignee, other law determines the rights and title of a consignee while goods are in the consignee's possession if, under this part, a perfected security interest held by the consignor would be senior to the rights of the creditor.

Reporters' Comments

Changes from Prior Draft: Order of subsections (a) and (b) reversed. Rules limited to purchasers “for value. Re: new subsection (c), see comment 3.

1. **Source.** New.

2. **Consignments.** Revised Section 1-201(37), reproduced in the Appendix, defines “security interest” to include the interest of a consignor of goods under many true consignments. Subsection (a) of this section provides that, for purposes of determining the rights of third parties, the consignee acquires all rights and title that the consignor had, if the consignor’s security interest is unperfected. The consignee acquires these rights even though, as between the parties, it purchases a limited interest in the goods (as would be the case, e.g., in a true

consignment, under which the consignee acquires only the interest of a bailee). As a consequence of this section, creditors of the consignee can acquire judicial liens and security interests in the goods. Former Section 9-114 contained priority rules applicable to security interests in consigned goods. Under this Article, the priority rules for purchase money security interests in inventory apply to consignments. See Section 9-104(b). Accordingly, a special section containing priority rules for consignments no longer is needed. Section 9-315 determines whether the rights of a judicial lien creditor are senior to the interest of the consignor, Sections 9-319 and 9-322 govern competing security interests in consigned goods, and Sections 9-315, 9-313, and 9-316 determine whether a buyer takes free of the consignor's interest.

Example 1: SP-1 delivers goods to D in a transaction that constitutes a "consignment" as defined in Section 9-102. SP-1 does not file a financing statement. D then grants a security interest in the goods to SP-2. SP-2 files a proper financing statement. Assuming D is a mere bailee, as in a "true consignment, D would not appear to have any rights in the collateral (beyond those of a bailee) so as to permit SP-2's security interest to attach to the greater rights. Nevertheless, under this section, for purposes of determining the rights of D's creditors, D acquires SP-1's rights. Accordingly, SP-2's security interest attaches, is perfected by the filing, and is senior to SP-1's interest.

Insofar as creditors of the consignee are concerned, this Article to a considerable extent reformulates the former law, which appears in Sections 2-326 and former 9-114, without changing the results. Neither Article 2 nor former Article 9 specifically addresses the rights of non-ordinary course buyers from the consignee.

3. Perfected Consignments. Subsection (c) contains a special rule with to consignments that are perfected. If application of this article would result in the consignor having priority over a competing creditor, then other law determines the rights and title of the consignee.

Example 2: SP-1 delivers goods to D in a transaction that constitutes a "consignment" as defined in Section 9-102. SP-1 files a proper financing statement. D then grants a security interest in the goods to SP-2. Under the priority rules of this part, SP-1's security interest would be senior to SP-2's. Subsection (c) indicates that, for purposes of determining SP-2's rights, other law determines the rights and title of the consignee. If, for example, a consignee obtains only the special property of a bailee, then SP-2's security interest would attach only to that special property.

Example 3: SP-1 obtains a security interest in all D's existing and after-acquired inventory. SP-1 perfects its security interest with a proper filing. Then SP-2 delivers goods to D in a transaction that constitutes a "consignment" as defined in Section 9-102. SP-2 files a proper financing statement but does not send notification to SP-1 pursuant to Section 9-322(a). Accordingly, SP-2's security interest is junior to SP-1's under Sections 9-319(a). Under Section 9-315A(b), D has the consignor's rights and title, so that SP-1's security interest attaches to SP-2 ownership interest in the goods. Thereafter, D grants a security interest in the goods to SP-3, and SP-3 perfects. Because SP-2's perfected security interest is senior to

1 SP-3's under Section 9-319(a), subsection (c) applies. Other law determines
2 D's rights and title to the goods insofar as SP-3 is concerned, and SP-3's
3 security interest attaches to those rights.

4 We intend to consider further whether certain other sections should be made
5 "subject to this section (e.g., Sections 9-315, 9-319, and 9-319A).

6 4. **Buyers of Accounts and Chattel Paper.** Subsection (b) takes a similar
7 approach to the interest of a debtor that has sold an account or chattel paper. If the
8 buyer-secured party's security interest is unperfected, then the seller can transfer
9 and the creditors of the seller can reach the account or chattel paper as if it had not
10 been sold.

11 *Example:* D sells accounts or chattel paper to B-1 and retains no interest in
12 them as against B-1. B-1 does not file a financing statement. D then sells the
13 same receivables to B-2. B-2 files a proper financing statement. Having sold
14 the receivables to B-1, D would not appear to have any rights in the collateral so
15 as to permit B-2's security (ownership) interest to attach. Nevertheless, under
16 this section, for purposes of determining the rights of D's creditors, D has the
17 rights that D sold. Accordingly, B-2's security interest attaches, is perfected by
18 the filing, and is senior to B-1's interest.

19 4. **Effect of Perfection.** This section leaves to other law (including Article
20 2 and applicable Article 9 cut-off and priority rules) the question whether a
21 consignee has a property interest in the goods (beyond that of a bailee) that could be
22 reached by creditors or acquired by purchasers if the consignor's security interest is
23 perfected. However, if the security interest of a buyer of an account or chattel paper
24 is perfected, the seller normally would not retain property rights in the account or
25 chattel paper.

26 SECTION 9-316. BUYER OF GOODS.

27 (a) [Subject to] [Except as otherwise provided in] subsection (d), a buyer
28 in ordinary course of business [, other than a person buying farm products from a
29 person engaged in farming operations,] takes free of a security interest created by
30 the buyer's seller, even if the security interest is perfected and even if the buyer
31 knows of its existence.

32 (b) (1) [Subject to] [Except as otherwise provided in] subsection (d), a
33 buyer of consumer goods takes free of a security interest, even if perfected, if the
34 buyer buys:

35 (A) without knowledge of the security interest;

1 (B) for value; ~~and~~
2 (C) for the buyer's own personal, family, or household purposes; and
3 (D) ~~unless before the buyer's purchase the secured party a person~~
4 files ~~filed~~ a financing statement covering the goods.

5 (2) To the extent that it affects the priority of a security interest over a
6 buyer of consumer goods under this section, the period of effectiveness of a filing
7 made in the jurisdiction in which the debtor is located is governed by Section
8 9-314(a).

9 (c) ~~[[Subject to]~~ [Except as otherwise provided in] subsection (d), a] [A]
10 buyer in ordinary course of business buying oil, gas, or other minerals at the
11 wellhead or minehead or after extraction takes free of an interest arising out of an
12 encumbrance.

13 (d) This section does not affect a security interest in goods in the possession
14 of the secured party under Section 9-311.

15 Reporters' Comments

16 1. **Source.** Former Section 9-307.

17 2. **Possessory Security Interests.** Subsection (c) is new. It rejects the
18 holding of *Tanbro Fabrics Corp. v. Deering Milliken, Inc.*, 350 N.E.2d 590 (N.Y.
19 1976) and, together with Section 9-315(c), prevents a buyer of collateral from
20 taking free of a security interest if the collateral is in the possession of the secured
21 party. "The secured party referred in subsection (c) is the holder of the security
22 interest referred to in one of the preceding subsections. A secured party is in
23 possession of collateral for purposes of this subsection if the collateral is in the
24 possession of a third party and the secured party takes possession under Section
25 9-311(c).

26 3. **Farm Products.** Brackets have been added to the farm products
27 exception in subsection (a). The Drafting Committee will consider this question
28 further.

29 4. **Oil, Gas, and Other Minerals.** Under subsection (a), a buyer in
30 ordinary course of business of minerals at the wellhead or minehead or after
31 extraction takes free of a security interest created by the seller. New subsection (c)
32 generally follows the recommendation of the ABA Oil and Gas Task Force by
33 expanding the protection afforded these buyers. See Alvin C. Harrell & Owen L.
34 Anderson, *Report of the ABA UCC Committee Task Force on Oil and Gas Finance*,

26 Texas Tech. L. Rev. 805, 813-14 (1994). Specifically, it provides that the buyers take free not only of Article 9 security interests but also of interests “arising out of an encumbrance.” The term “encumbrance” is defined in Section 9-102 to include real property mortgages, other liens on real property, and “any other right in real property other than an ownership interest.” Thus, to the extent that a real property mortgage encumbers minerals not only before but also after extraction, this section enables a buyer in ordinary course of the minerals to take free of the mortgage. The draft does not, however, follow the Task Force’s recommendation that these buyers should also take free of interests arising out of ownership interests in the real property. This issue is significant only in a minority of states. Several of them have adopted special statutes and nonuniform amendments to Article 9 to provide special protections to mineral owners, whose interests often are highly fractionalized in the case of oil and gas. See Terry I. Cross, *Oil and Gas Product Liens--Statutory Security Interests for Producers and Royalty Owners Under the Statutes of Kansas, New Mexico, Oklahoma, Texas and Wyoming*, 50 Consumer Fin. L. Q. Rep. 418 (1996). Inasmuch as a complete resolution of the issue is likely to require the addition of complex provisions to the draft, and there are good reasons to believe that a uniform solution would not be feasible, the draft leaves its resolution to other legislation.

SECTION 9-317. LESSEE OF GOODS IN ORDINARY COURSE OF

BUSINESS. A lessee of goods in ordinary course of business takes the leasehold interest free of a security interest in the goods created by the lessor even if the security interest is perfected and the lessee knows of its existence.

Reporters' Comments

1. **Source.** Section 2A-307(3).

2. **Status.** The Drafting Committee for Articles 2A and 9 will coordinate their work on the issues addressed by this section.

SECTION 9-318. LICENSEE IN ORDINARY COURSE OF BUSINESS.

[To be moved from Article 2B]

Reporters' Comments

Status. The Article 2B Drafting Committee has been developing the rules governing licenses and other transfers of intellectual property rights, including the creation of security interests in intellectual property. We have been communicating with the Reporter for Article 2B, Raymond Nimmer, in an effort to ensure that the provisions of Articles 2B and 9 are consistent.

We anticipate that rules having their principal effect on security interests in intellectual property will appear in Article 9. Although rules of general applicability to transferees or creditors are likely to appear in Article 2B, we expect

1 that the Article 9 Drafting Committee will have an opportunity to review and
2 comment upon them before they are finalized.

3 **SECTION 9-319. PRIORITIES AMONG CONFLICTING SECURITY**
4 **INTERESTS AND AGRICULTURAL LIENS IN SAME COLLATERAL.**

5 (a) Except as otherwise provided in this part, Section 4-210 [with respect to
6 a security interest of a collecting bank], and Section 5-118 [with respect to a
7 security interest of an issuer or nominated person], priority among conflicting
8 security interests and agricultural liens in the same collateral is determined
9 according to the following rules:

10 (1) (A) Conflicting security interests and agricultural liens rank
11 according to priority in time of filing or perfection.

12 (B) Priority dates from the earlier of the time:

13 (i) a filing covering the collateral is first made; or

14 (ii) the time the security interest or agricultural lien is first
15 perfected, if unless there is no a period thereafter when there is neither filing nor
16 perfection.

17 (2) The first security interest or agricultural lien to attach or become
18 effective has priority if As long as conflicting security interests and agricultural
19 liens are unperfected, ~~the first to attach or to become effective has priority.~~

20 **Alternative A**

21 (b) For the purposes of subsection (a), a date of filing or perfection as to
22 collateral is also a date of filing or perfection as to proceeds.

23 **Alternative B**

24 (b) Except as otherwise provided in [this Article] [the Uniform Commercial
25 Code] [Sections 9-322 and 9-325], a security interest in or agricultural lien on
26 collateral which has priority over a conflicting security interest or agricultural lien

1 also has priority in [identifiable] proceeds of the collateral while the security
2 interest or agricultural lien in proceeds is perfected.

3 **[End of Alternatives]**

4 (c) If a statute under which an agricultural lien in collateral is created
5 provides that the agricultural lien has priority over a conflicting security interest or
6 agricultural lien in the same collateral, the statute governs priority if the agricultural
7 lien is perfected.

8 **Reporters' Comments**

9 1. **Source.** Former Section 9-312(5), (6).

10 2. **General Rule.** Subsection (a)(1) contains the basic, first-in-time rule,
11 under which the first security interest that is filed or perfected takes priority. This
12 rule is subject to the other rules contained in Part 3 of this Article, including cases
13 of production money security interests, purchase money security interests, security
14 interests in deposit accounts, and security interests in letters of credit that qualify
15 for the special priorities in Sections 9-321, 9-322, 9-325, and 9-326. This
16 subsection also is subject to Sections 4-210 and 5-118. The latter is new. It affords
17 a security interest in letter of credit documents to an issuer or nominated person and
18 appears in the Appendix to the draft. Inasmuch as Section 9-104(b) treats the
19 interest of a consignor to be a purchase money security interest in inventory, the
20 reference to former Section 9-114 has been deleted.

21 3. **Priority in Proceeds.** Subsection (b), Alternative A, derives from
22 former Section 9-312(6). It recognizes that the temporal (first-in-time) priority rule
23 of subsection (a) should apply to proceeds as well as to the antecedent collateral.
24 Under that approach, it is necessary to make special provision for situations where
25 the applicable priority rule is not based on the first-in-time principle. For example,
26 former Section 9-312(3) and (4) provided that purchase money priority in inventory
27 extended only to certain cash proceeds and purchase money priority in other
28 collateral extended to all proceeds. Section 9-322 continues this approach.
29 However, the purchase money priority rules are not the only priority rules that do
30 not observe the first-in-time principle. See[, e.g.], Sections 9-321, 9-322, 9-323, 9-
31 323A, 9-324, 9-325, 9-326, 9-327, 9-331, 9-332, 9-333, and 9-334. Consequently,
32 if Alternative A is retained, it will be necessary to specify in connection with each
33 of these sections whether or not the same priority obtains in the case of proceeds.

34 Alternative B takes a simpler approach. It provides that the priority for
35 proceeds generally follows the priority for the antecedent collateral, as long as the
36 security interest in proceeds is perfected. The Drafting Committee has decided that,
37 in some cases, priority in proceeds should not follow priority in the original
38 collateral. The rule of Alternative B should be subject to those special rules. For
39 example, it should not override the limitation on the priority of the proceeds of
40 collateral subject to a purchase money security interest in inventory and livestock.
41 See Section 9-322. Nor should the rule override the limitation on the priority of the

proceeds of a deposit account. See Section 9-325. If the Drafting Committee approves Alternative B, it will be necessary to determine whether other exceptions are in order.

4. **Agricultural Liens.** Subsections (a) and (b) apply the same the same priority rule to agricultural liens as to security interests, regardless of whether they conflict with other agricultural liens or with security interests. New subsection (c) sets forth narrow circumstances under which a non-UCC priority rule may displace the Article 9 priority rule applicable to agricultural liens: a perfected agricultural lien may achieve priority notwithstanding the Article 9 priority rules only if the statute creating the lien so provides.

**SECTION 9-319A. PRIORITIES BETWEEN CONFLICTING
SECURITY INTERESTS AND STATUTORY LIENS OTHER THAN
AGRICULTURAL LIEN IN SAME COLLATERAL.**

(a) Except as otherwise provided in this part, priority between a conflicting security interest and a statutory lien other than an agricultural lien in the same collateral is determined according to the following rules:

(1) (A) A conflicting security interest and a statutory lien other than an agricultural lien rank according to priority in time of filing or perfection.

(B) Priority dates from the earlier of the time:

(i) a filing covering the collateral is first made; or

(ii) the time the security interest or statutory lien is first perfected, if unless there is no a period thereafter when there is neither filing nor perfection.

(2) The first security interest or agricultural lien to attach or become effective has priority if ~~As long as~~ a conflicting security interest and statutory lien other than an agricultural lien are unperfected, ~~the first to attach or to become effective has priority.~~

(b) For the purposes of subsection (a), a date of filing or perfection as to collateral is also a date of filing or perfection as to proceeds.

1 (c) If a statute under which a statutory lien other than an agricultural lien in
2 collateral is created provides that the statutory lien has priority over a conflicting
3 security interest in the same collateral, the statute governs priority [if the statutory
4 lien is perfected].

5 Reporters' Comments

6 1. **Source.** New; derived from Section 9-319.

7 2. **Non-Agricultural Statutory Liens.** Although this section derives from
8 Section 9-319, its scope is more narrow. Consistent with the apparent
9 recommendation in the Report of the Subcommittee on Relation to Other Law, this
10 section governs priority between a statutory lien (other than an agricultural lien) and
11 a security interest, but does not address priority contests between or among
12 statutory liens. Inasmuch as the approach taken in this section could give rise to
13 circular priorities and statutory liens are being brought into the Article 9 filing
14 regime, the Drafting Committee may wish to consider whether this approach should
15 be abandoned in favor of the approach taken in Section 9-319 for agricultural liens.
16 Also, the bracketed language in subsection (c) invites the Drafting Committee to
17 consider whether an overriding non-Article 9 statutory priority rule should control
18 when a statutory lien is unperfected.

19 **SECTION 9-320. FUTURE ADVANCES.**

20 (a) (1) This subsection applies only to a security interest that secures an
21 obligation.

22 (2) For purposes of determining the priority of a security interest under
23 Section 9-319(a) ~~of a security interest that secures an obligation~~, perfection of the
24 security interest dates from the time an advance is made to the extent that the
25 security interest secures an advance made:

26 (A) [other than] [not] pursuant to commitment; and

27 (B) ~~made~~ while the security interest is temporarily perfected under
28 Section 9-310(d) or (e) [or is perfected when it attaches under Section 9-308A] and
29 by no other method, ~~perfection of the security interest dates from the time an~~
30 ~~advance is made.~~

1 (b 3) A security interest ~~that secures an obligation~~ is subordinate to the
2 rights of a person that becomes a lien creditor while the security interest is
3 perfected only to the extent that it secures advances made more than 45 days after
4 the person becomes a lien creditor unless the advance is made:

5 (A) without knowledge of the lien; or

6 (B) pursuant to a commitment entered into without knowledge of the
7 lien.

8 (b e) (1) A buyer of goods other than a buyer in ordinary course of
9 business takes free of a security interest to the extent that it secures advances made
10 after the earlier of:

11 (A) the time the secured party acquires knowledge ~~learns~~ of the
12 buyer's purchase; or

13 (B) ~~more than 45 days after the purchase, whichever occurs first,~~
14 ~~unless.~~

15 (2) This subsection does not apply if the advance is made pursuant to a
16 commitment entered into without knowledge of the buyer's purchase and before the
17 expiration of the 45-day period.

18 (3) This subsection does not affect a security interest in goods in the
19 possession of the secured party under Section 9-311.

20 (c d) (1) A lessee of goods other than a lessee of goods in ordinary course
21 of business takes the leasehold interest free of a security interest to the extent that it
22 secures advances made after the earlier of:

23 (A) the time the secured party acquires knowledge ~~learns~~ of the
24 lease; or

25 (B) ~~more than 45 days after the lease contract becomes enforceable~~
26 ~~whichever occurs first, unless.~~

(2) This subsection does not apply if the advance is ~~the future advances~~ are made pursuant to a commitment entered into without knowledge of the lease and before the expiration of the 45-day period.

Reporters' Comments

1. **Source.** Former Sections 9-312(7), 9-301(4), 9-307(3), 2A-307(4).

2. Competing Security Interests. This section collects all of the special rules dealing with “future advances. Subsection (a) replaces and clarifies former Section 9-312(7). No substantive change is intended. Former subsection (7) was added by the 1972 Revisions to Article 9 in order to override some decisions that subordinated future advances to intervening interests. Under a proper reading of the first-to-file-or-perfect rule of Section 9-319(a) (and former Section 9-312(5)), it is abundantly clear the time that an advance is made plays no role in determining priorities among conflicting security interests except when the advance is the giving of value as the last step for attachment and perfection. Subsection (a), accordingly, states affirmatively the only other instance when the time of an advance figures in the priority scheme. See UCC, 1972 Official Text, Section 9-312, Reasons for 1972 Change:

The proposed unified priority rule of subsection 9-312(5) would indicate that subsequent advances by the first-filed party have priority, and subsequent advances under a security interest perfected by possession likewise have priority over an intervening filed security interest. These priority rules are expressly stated in subsection (7). That proposal also deals with the rare case of the priority position of a subsequent advance made by a secured party whose security interest is temporarily perfected without either filing or possession, against an intervening secured party. Since there is no notice by the usual method of filing or possession of the existence of the security interest, the subsequent advances rank only from the actual date of making unless made pursuant to commitment.

Although the drafting history of the 1972 amendments suggests that the drafters may have assumed that the special rule under which the priority of future advances differs from that of the first advance would apply only to cases of temporary perfection, former Section 9-312(7) appears to apply to cases of automatic perfection, as well. The addition of the bracketed language in subsection (a), which refers to the automatic perfection provisions of new Section 9-308A, would conform subsection (a) to the former law. The Drafting Committee has yet to consider whether the reference to automatic perfection should be added to subsection (a).

The new formulation in subsection (a) also omits the ambiguous treatment in former subsection (7) of the situation where the initial advance is paid and a new (“future”) advance is made subsequently: Was the new advance “made while a security interest is perfected by filing or the taking of possession”? We think so, but clarification seems worthwhile.

1 3. **Competing Lien Creditors.** Subsection (b) replaces former Section
2 9-301(4). It addresses the problem considered by P.E.B. Commentary No. 2 and
3 removes the ambiguity that necessitated the commentary. Former subsection (4)
4 appears to state a general rule that a lien creditor has priority over a perfected
5 security interest and is “subject to the security interest “only in specified
6 circumstances. Because subsection (4) speaks to the making of an “advance, it
7 arguably implies that to the extent a security interest secures non-advances
8 (expenses, interest, etc.), it is junior to the lien creditor’s interest. Subsection (b)
9 solves the problem by providing that a security interest is subordinate only to the
10 extent that the specified circumstances occur, thereby eliminating the erroneous
11 implication. As under former Section 9-301(4), a secured party’s knowledge does
12 not cut short the 45-day period during which future advances can achieve priority
13 over an intervening lien creditor’s interest.

14 4. **Competing Buyers and Lessees.** Subsection (c) replaces former
15 Section 9-307(3) and subsection (d) replaces former Section 2A-307(4). These
16 subsections contain minor style changes only.

17 5. **Buyers of Receivables.** As drafted, subsections (a) and (b) do not apply
18 to outright sales of accounts, chattel paper, or payment intangibles. They may need
19 refinements to take account of particular financing practices.

20 **[SECTION 9-321. PRIORITY OF PRODUCTION MONEY SECURITY**
21 **INTERESTS AND AGRICULTURAL LIENS.**

22 (a) (1) Except as otherwise provided in subsection (d e), if the requirements
23 of subsection (b) are met, a perfected production money security interest in
24 production money crops has priority over a conflicting security interest in the same
25 crops and, except as otherwise provided in Section 9-325, also has priority in their
26 identifiable proceeds.

27 (2) A production money security interest has priority under this
28 subsection only to the extent that the conflicting security interest secures
29 obligations incurred more than [] months before the production money secured
30 party first gives new value to enable the debtor to produce the crops.

31 (b) A production money security interest has priority under subsection (a)
32 if:

(1) the production money security interest is perfected by filing when the production money secured party first gives new value to enable the debtor to produce the crops;

(2) the production money secured party gives an authenticated notification to the holder of the conflicting security interest not less than 10 or more than 30 days before the production money secured party first gives new value to enable the debtor to produce the crops if the holder had filed a financing statement covering the crops before the date of the filing made by the production money secured party; and

(3) the notification states that the production money secured party has or expects to acquire a production money security interest in the debtor's crops and contains a description of the crops.

(c) Except as otherwise provided in subsection (d), if more than one security interest qualifies for priority in the same collateral under subsection (a), the security interests rank according to priority in time of filing under Section 9-319(a).

(d) To the extent that a person holds both an agricultural lien and a production money security interest in the same collateral securing the same obligations, the rules of priority applicable to agricultural liens govern priority.]

Legislative Note: This section is optional. States that do not enact this section also should not enact Section 9-105.

Reporters' Comments

1. **Source.** New.

2. Legislative Option. This new section replaces the limited priority in crops afforded by former Section 9-312(2). As explained in Section 9-105, Comment 2, that priority generally has been thought to be of little value for its intended beneficiaries. Neither the Drafting Committee nor the agricultural financing community has been able to reach a consensus on the desirability of including a special production money priority rule in Article 9. For this reason, the rule appears as an optional provision for each State to consider during the legislative enactment process.

1 **3. Production Money Security Interests.** This section attempts to balance
2 the interests of the production money secured party with those of a secured party
3 who has previously filed a financing statement covering the crops that are to be
4 produced. For example, to qualify for priority under this section, the production
5 money secured party must notify the earlier-filed secured party prior to extending
6 the production money credit. The notification affords the earlier secured party the
7 opportunity to prevent subordination by extending the credit itself. Moreover, the
8 production money security interest does not take priority over all secured
9 obligations owed to the earlier filer. Rather, the production money security interest
10 has priority only over obligations incurred relatively recently, i.e., those incurred
11 during the [] months before the production money secured party first gives new
12 value.

13 **4. Multiple Production Money Security Interests.** In the case of multiple
14 production money security interests that qualify for priority under subsection (a),
15 the first to file has priority. See subsection (c). Note that only a security interest
16 perfected by filing is entitled to production money priority. See subsection (b)(1).
17 Consequently, subsection (c) does not adopt the first-to-file-*or-perfect* formulation.

18 **5. Holder of Agricultural Lien and Production Money Security**
19 **Interest.** Subsection (d) deals with a creditor who holds both an agricultural lien
20 and an Article 9 production money security interest in the same collateral. In these
21 cases, the priority rules applicable to agricultural liens govern. The creditor can
22 avoid this result by waiving its agricultural lien. These rules remain under
23 consideration by the Drafting Committee.

24 **SECTION 9-322. PRIORITY OF PURCHASE MONEY SECURITY**
25 **INTERESTS.**

26 (a) Except as otherwise provided in subsection (e), a perfected purchase
27 money security interest in inventory has priority over a conflicting security interest
28 in the same inventory and, except as otherwise provided in Section 9-325, also has
29 priority in its identifiable cash proceeds to the extent the identifiable cash proceeds
30 are received on or before the delivery of the inventory to a buyer₂ if:

31 (1) the purchase money security interest is perfected when the debtor
32 receives possession of the inventory;

33 (2) the purchase money secured party gives an authenticated notification
34 to the holder of the conflicting security interest, if the holder had filed a financing
35 statement covering the same types of inventory:

1 (A) before the date of a filing made by the purchase money secured
2 party; or

3 (B) if the purchase money security interest is temporarily perfected
4 without filing or possession under Section 9-310(e), before the beginning of the
5 20-day period thereunder;

6 (3) the holder of the conflicting security interest receives the notification
7 no earlier than five years before the debtor receives possession of the inventory; and

8 (4) the notification states that the person giving the notification has or
9 expects to acquire a purchase money security interest in inventory of the debtor and
10 describes the inventory by item or type.

11 (b) If a purchase money security interest in inventory has priority over a
12 conflicting security interest under subsection (a), a security interest held by the
13 purchase money secured party in chattel paper [or an instrument] constituting
14 proceeds of the inventory has priority over a conflicting security interest in the
15 chattel paper [or instrument] if:

16 (1) the conflicting security interest in the chattel paper [or instrument] is
17 claimed merely as proceeds of inventory subject to a security interest; and

18 (A) the purchase money secured party takes possession of the chattel
19 paper [or instrument] in the ordinary course of its business; and

20 (B) the chattel paper [or instrument] does not indicate that it has
21 been assigned to [an identified assignee] [the person holding the conflicting security
22 interest]; or

23 (2) the purchase money secured party takes possession of the chattel
24 paper [or instrument] in good faith, in the ordinary course of its business, and
25 without knowledge that its security interest violates the rights of the person holding
26 the conflicting security interest.

1 (c) Except as otherwise provided in subsection (e), a perfected purchase
2 money security interest in livestock that are farm products has priority over a
3 conflicting security interest in the same livestock and, except as otherwise provided
4 in Section 9-325, also has priority in its identifiable proceeds [and identifiable
5 products in their unmanufactured states] if:

6 (1) the purchase money security interest is perfected when the debtor
7 receives possession of the livestock;

8 (2) the purchase money secured party gives an authenticated notification
9 to the holder of the conflicting security interest, if the holder had filed a financing
10 statement covering the same types of livestock:

11 (A) before the date of a filing made by the purchase money secured
12 party; or

13 (B) if the purchase money security interest is temporarily perfected
14 without filing or possession under Section 9-310(e), before the beginning of the
15 20-day period thereunder;

16 (3) the holder of the conflicting security interest receives the notification
17 no earlier than six months before the debtor receives possession of the livestock;
18 and

19 (4) the notification states that the person giving the notification has or
20 expects to acquire a purchase money security interest in livestock of the debtor and
21 describes the livestock by item or type.

22 (d) Except as otherwise provided in subsection (e), a purchase money
23 security interest in goods other than inventory or livestock has priority over a
24 conflicting security interest in the same collateral and, except as otherwise provided
25 in Section 9-325, also has priority in its identifiable proceeds if the purchase money

1 security interest is perfected when the debtor receives possession of the collateral or
2 within 20 days thereafter.

3 (e) If more than one security interest qualifies for priority in the same
4 collateral under subsection (a), (c), or (d):

5 (1) a security interest securing an obligation incurred [by an obligor] as
6 the price of the collateral has priority over a security interest securing an obligation
7 incurred [by an obligor] for value given to enable the debtor to acquire rights in
8 collateral; and

9 (2) in all other cases, Section 9-319(a) applies to the qualifying security
10 interests.

11 Reporters' Comments

12 1. **Source.** Former Section 9-312(3), (4).

13 2. **Purchase Money Security Interests in Inventory.** Subsection (a),
14 which affords a special priority to certain purchase money security interests in
15 inventory, derives from former Section 9-312(3). No change in meaning is
16 intended.

17 3. **Consignments.** Subsection (a) also determines the priority of a
18 consignor's interest in consigned goods as against a security interest in the goods
19 created by the consignee. Inasmuch as a consignment subject to this Article is
20 defined to be a purchase money security interest, see Section 9-104(b), no inference
21 concerning the nature of the transaction should be drawn from the fact that a
22 consignor uses the term "security interest" in its notice under subsection (a)(4).
23 Similarly, a notice stating that the consignor has delivered or expects to deliver
24 goods, properly described, "on consignment" meets the requirements of subsection
25 (a)(4), even if it does not contain the term "security interest" and even if the
26 transaction subsequently is determined to be a security interest. Cf. Section 9-505
27 (use of "consignor" and "consignee" in financing statement).

28 4. **Priority in Chattel Paper Proceeds.** Subsection (b) is new. It enables
29 the holder of a purchase money security interest in inventory to obtain priority in
30 chattel paper that constitutes the proceeds of inventory. Unlike Section 9-327,
31 subsection (b) awards priority in chattel paper proceeds to the holder of a purchase
32 money security interest in inventory even if the holder does not give new value.

33 5. **Purchase Money Security Interests in Livestock.** New subsection (c)
34 provides a purchase money priority rule for farm-products livestock. It is patterned
35 on the purchase money priority rule for inventory found in subsection (a) and
36 includes a requirement that the purchase money secured party notify earlier-filed
37 parties. Two differences between subsections (a) and (c) are noteworthy. First,

1 unlike the purchase money inventory lender, the purchase money livestock lender
2 enjoys priority in *all* proceeds of the collateral. Thus, under subsection (c), the
3 purchase money secured party takes priority in accounts over an earlier-filed
4 accounts financier. Second, the bracketed language in subsection (c) affords priority
5 in products of the collateral as well as proceeds. Former Article 9 does not deal
6 with products in any meaningful way. The Drafting Committee has deferred
7 considering whether the subsection (d) priority should carry over into products until
8 such time as it considers the larger issues.

9 **6. Purchase Money Security Interests in Aquatic Farm Products.**

10 Aquatic goods produced in aquacultural operations (e.g., catfish raised on a catfish
11 farm) are farm products. See Section 9-106(c) (definition of “farm products”). The
12 definition does not indicate whether aquatic goods are “crops, as to which the
13 (optional) production money security interest priority in Section 9-321 applies, or
14 “livestock, as to which the purchase money priority in subsection (c) of this
15 section applies. One possibility is to treat aquatic vegetables as “crops and aquatic
16 animals as “livestock. An alternative is to place all aquatic goods in the category
17 that seems to fit better most often. a third option is to leave the courts free to
18 determine the classification of particular goods on a case-by-case basis, applying
19 whichever priority rule makes more sense in the overall context of the debtor’s
20 business. The Drafting Committee has yet to resolve this issue.

21 **7. Purchase Money Priority in Goods Other than Inventory and**
22 **Livestock.** Subsection (d) extends from 10 days to 20 days the “grace period” for
23 achieving purchase money priority in non-inventory collateral found in former
24 Section 9-312(4). It reflects that a secured party may hold a “purchase money
25 security interest” only in goods. See also Section 9-104(a).

26 Several reported cases arising under former Section 9-312(4) address the
27 question of when the “debtor” receives “possession” of collateral for purposes of
28 that section. Among other issues, these cases concern collateral that is delivered in
29 stages and goods that were held in a person’s possession for a period of time (e.g.,
30 under a lease) before the person created a security interest in them. The Drafting
31 Committee is inclined to address this question and the analogous question under
32 Section 9-315(f) in the Official Comments.

33 **8. Multiple Purchase Money Security Interests.** New subsection (e)
34 governs priority among multiple purchase money security interests in the same
35 collateral. It grants priority to purchase money security interests securing the price
36 of collateral (i.e., created in favor of the seller) over purchase money security
37 interests that secure enabling loans. Section 7.2(c) of the Restatement of the Law
38 of Property (Mortgages), Tentative Draft No. 4 (February 28, 1995), approves this
39 rule with respect to real property mortgages, on the ground that:

40 the equities favor the vendor. Not only does the vendor part with
41 specific real estate rather than money, but the vendor would never
42 relinquish it at all except on the understanding that the vendor will
43 be able to use it to satisfy the obligation to pay the price. This is the
44 case even though the vendor may know that the mortgagor is going
45 to finance the transaction in part by borrowing from a third party and
46 giving a mortgage to secure that obligation. In the final analysis, the

1 law is more sympathetic to the vendor's hazard of losing real estate
2 previously owned than to the third party lender's risk of being
3 unable to collect from an interest in real estate that never previously
4 belonged to it.

5 The first-to-file-or-perfect rule of Section 9-319 applies to multiple purchase money
6 security interests securing enabling loans.

7 Subsection (e) makes no reference to proceeds. The Official Comments can
8 explain how the proceeds rules would be applied in these unusual cases.

9 **SECTION 9-323. PRIORITY OF SECURITY INTERESTS IN**
10 **TRANSFERRED COLLATERAL.**

11 [(a)] [Subject to subsection (b), a] [A] security interest created by a debtor
12 is subordinate to a security interest in the same collateral created by another person,
13 notwithstanding anything to the contrary in this part, if:

14 (1) the ~~If a debtor acquired the collateral~~ acquires property subject to a
15 security interest created by the other ~~another~~ person;

16 (2) the security interest created by the other person was ~~is~~ perfected
17 when the debtor acquired the collateral ~~acquires the property~~; and

18 (3) there is no period thereafter when ~~it~~ the security interest is
19 unperfected, ~~any security interest created by the debtor is subordinate to the security~~
20 ~~interest created by the other person, notwithstanding anything to the contrary in this~~
21 ~~part.~~

22 [(b)] ~~If However,~~ if the security interest created by the other person is
23 unperfected when the debtor acquires the property or at any time thereafter, the
24 other provisions of this part, as applicable, determine its priority.]

Reporters' Comments

1. **Source.** New.

2. **"Double Debtor" Problem.** This section addresses the "double debtor problem that arises when a debtor acquires property that is subject to a security interest created by another debtor.

3. **Taking Subject to Perfected Security Interest.** Consider the following scenario:

Example: A owns an item of equipment subject to a perfected security interest in favor of SP-A. A sells the equipment to B, not in the ordinary course of business. B acquires its interest subject to SP-A's security interest. See Sections 9-201; 9-313(c).

Under the first sentence of this section, if B creates a security interest in the equipment in favor of SP-B, SP-B's interest is subordinate to SP-A's interest, even if SP-B filed against B before SP-A filed against A, and even if SP-B took a purchase money security interest. Normally, SP-B could have investigated the source of the equipment and discovered SP-A's filing before making an advance against the equipment, whereas SP-A had no reason to search the filings against someone other than its debtor, A.

4. **Taking Subject to Unperfected Security Interest.** If, in the foregoing Example, SP-A's security interest is unperfected, B will take free of it as long as B gives value and takes delivery of the equipment without knowledge of the security interest. See Section 9-315(c). If B takes free of SP-A's security interest and then creates a security interest in favor of SP-B, no priority issue arises; SP-B has the only security interest in the equipment. Suppose, however, that B knows of SP-A's security interest and therefore takes the equipment subject to it. If B creates a security interest in the equipment in favor of SP-B, and SP-B perfects its security interest, then the second sentence of this section provides that the normal priority rules govern. Under Section 9-319(a)(1), the "first-to-file-or-perfect" rule, SP-A's unperfected security interest will be junior to SP-B's perfected security interest. The award of priority to SP-B is premised on the belief that SP-A's failure to file could have misled SP-B.

5. **Taking Subject to Perfected Security Interest that Becomes Unperfected.** If SP-A's interest is perfected when B acquires the equipment but for some reason SP-A's security interest later becomes unperfected, the second sentence of this section provides that the normal priority rules govern. For example, if SP-A's financing statement lapses while SP-B's security interest is perfected, SP-B's security interest would become senior to SP-A's security interest. See Sections 9-319(a)(1); 9-516(c).

6. **Bracketed Sentence.** The first sentence of this section covers some, but not all, "double debtor" cases. As explained above, if a case falls outside the first sentence, in the absence of a special "double debtor" rule, the normal priority rules would apply. The second sentence makes this point explicitly. Inasmuch as one could reach the right result without the second sentence, the sentence appears in

brackets. However, retaining the explicit statement in the second sentence is likely to make the statute easier to use.

SECTION 9-323A. PRIORITY OF SECURITY INTERESTS CREATED BY NEW DEBTOR.

(a) Subject to subsection (b), a a security interest that is perfected by a filed financing statement that is effective solely under Section 9-510 in collateral in which a new debtor has or acquires rights is subordinate to a security interest in the same collateral that is perfected in another manner.

(b) If ~~However~~, if more than one security interest in the same collateral is subordinate under this section, the other provisions of this part, as applicable, determine the priority among of the subordinated security interests ~~as among themselves~~.

Reporters' Comments

1. **Source.** New.

2. **Collateral of New Debtors.** This section addresses the priority contests that may arise when a new debtor becomes bound by the security agreement of an original debtor and each has a secured creditor.

The first sentence subordinates the original debtor's secured party's security interest perfected under Section 9-510 to security interests in the same collateral perfected in another manner, e.g., by filing against the new debtor.

Example 1: SP-X holds a perfected-by-filing security interest in X Corp’s existing and after-acquired inventory, and SP-Z holds a perfected-by-filing security interest in Z Corp’s existing and after-acquired inventory. Z Corp “becomes bound” as debtor by X Corp’s security agreement (e.g., Z Corp buys X Corp’s assets and assumes its security agreement). Under Section 9-510, SP-X’s financing statement is effective to perfect a security interest in inventory acquired by Z Corp after it becomes bound.

The first sentence of this section provides that SP-X's security interest is subordinate to SP-Z's, regardless of which financing statement was filed first.

The second sentence of this section addresses the priority among security interests created by the original debtor (X Corp). By invoking the other priority rules of this subpart, as applicable, the second sentence preserves the relative priority of security interests created by the original debtor.

1 **Example 2:** Under the facts of Example 1, SP-Y also holds a perfected-by-
2 filing security interest in X Corp's existing and after-acquired inventory.
3 SP-Y filed after SP-X.

4 SP-X has priority over SP-Y. See Section 9-319(a)(1).

5 **SECTION 9-324. PRIORITY OF SECURITY INTERESTS IN**
6 **INVESTMENT PROPERTY.** The following rules govern priority ~~Priority~~ among
7 conflicting security interests in the same investment property is governed by ~~the~~
8 ~~following rules:~~

9 (1) A security interest of a secured party that has control over investment
10 property has priority over a security interest of a secured party that does not have
11 control over the investment property.

12 (2) A possessory security interest in a certificated security in registered
13 form has priority over a conflicting security interest perfected by a method other
14 than control.

15 (3) Except as otherwise provided in paragraphs (4) and (5), conflicting
16 security interests of secured parties each of which has control rank equally.

17 (4) A security interest held by a securities intermediary in a security
18 entitlement or a securities account maintained with the securities intermediary has
19 priority over a conflicting security interest held by another secured party.

20 (5) A security interest held by a commodity intermediary in a commodity
21 contract or a commodity account maintained with the commodity intermediary has
22 priority over a conflicting security interest held by another secured party.

23 (6) Conflicting security interests granted by a broker, securities
24 intermediary, or commodity intermediary which are perfected without control rank
25 equally.

(7) In all other cases, priority among conflicting security interests in investment property is governed by Sections 9-319(a) and 9-320(a).

Reporters' Comments

1. **Source.** Former Section 9-115(5).

2. **Security Interests of Equal Rank.** Former Section 9-115, added recently in conjunction with Revised Article 8, introduced into Article 9 the concept of security interests that rank equally. Some observers have questioned the wisdom of ranking equally the security interests of parties holding adverse interests in the same collateral. The Drafting Committee may reconsider this issue.

SECTION 9-325. PRIORITY OF SECURITY INTERESTS IN DEPOSIT

ACCOUNTS. The following rules govern priority ~~Priority~~ among conflicting security interests in the same deposit account is governed by ~~the following rules~~:

(1) A security interest held by a secured party that has control over the deposit account has priority over a conflicting security interest held by a secured party that does not have control.

(2) Except as otherwise provided in paragraphs (3) and (4), security interests perfected by control rank equally.

(3) Except as otherwise provided in paragraph (4), a security interest held by the depository institution with which the deposit account is maintained has priority over a conflicting security interest held by another secured party.

(4) A security interest perfected by control pursuant to Section 9-109(a)(3) has priority over a security interest held by the depository institution with which the deposit account is maintained.

Reporters' Comments

1. **Source.** New; derived from former Section 9-115(5).

2. **Deposit Accounts.** This section does not apply to accounts evidenced by an instrument (e.g., certain certificates of deposit), which by definition are not "deposit accounts."

1 3. **Control.** Under subsection (1), security interests perfected by control
2 (Section 9-109) take priority over those perfected otherwise, e.g., as identifiable
3 cash proceeds under Section 9-313(e)(2). Secured parties for whom the deposit
4 account is an integral part of the credit decision will, at a minimum, insist upon the
5 right to immediate access to the deposit account upon the debtor's default (i.e.,
6 control). Those secured parties for whom the deposit account is less essential will
7 not take control, thereby running the risk that the debtor will dispose of funds on
8 deposit (either outright or for collateral purposes) after default but before the
9 account can be frozen by court order or the secured party can obtain control.

10 Subsection (2) governs the case (expected to be very rare) in which a
11 depositary institution enters into a Section 9-109(a)(2) control agreement with more
12 than one secured party. Subsection (a)(2) provides that the security interests rank
13 equally. If the depositary institution is solvent, there often will be no need for a
14 priority rule inasmuch as the depositary institution is likely to be liable to each
15 secured party.

16 4. **Priority of Depositary Institution.** Under subsection (3), the security
17 interest of the depositary institution with which the deposit account is maintained
18 normally takes priority over all other conflicting security interests in the deposit
19 account, regardless of whether the deposit account constitutes the competing
20 secured party's original collateral or its proceeds. a rule of this kind enables
21 depositary institutions to extend credit to their depositors without the need to
22 examine either the public record or their own records to determine whether another
23 party might have a security interest in the deposit account.

24 A secured party who takes a security interest in the deposit account as
25 original collateral can protect itself against the results of this rule in one of two
26 ways. It can take control of the deposit account by becoming the depositary
27 institution's customer (i.e., by having the account in its name). Under subsection
28 (4), this arrangement operates to subordinate the depositary institution's security
29 interest. Alternatively, the secured party can obtain an express subordination
30 agreement from the depositary institution. See Section 9-336. Additional
31 clarification of subsection (4) or the Official Comments is likely to be needed to
32 cover cases in which both the debtor and the secured party are indebted to the
33 depositary institution.

34 A secured party who claims the deposit account as proceeds of other
35 collateral can reduce the risk of becoming junior by obtaining the debtor's
36 agreement to deposit proceeds into a specific cash collateral account and obtaining
37 the agreement of that depositary institution to subordinate all its claims to those of
38 the secured party. But if the debtor violates its agreement and deposits funds into a
39 deposit account other than the cash collateral account, the secured party risks being
40 subordinated.

41 5. **Priority in Proceeds.** The priority afforded by this section is not
42 intended to extend to proceeds of a deposit account. Accordingly, Section
43 9-319(a)(1), the first-to-file-or perfect rule, normally will govern priorities in
44 proceeds. a secured party who obtains control but who nevertheless leaves the
45 debtor with the power (but perhaps not the right) to withdraw from the deposit
46 account is not entitled to special priority in the proceeds. Section 9-313(e)

addresses continuation of perfection in proceeds of deposit accounts. As to funds transferred from a deposit account that serves as collateral, see Section 9-329.

SECTION 9-326. PRIORITY OF SECURITY INTERESTS IN LETTERS

LETTER-OF-CREDIT RIGHTS. The following rules govern priority Priority among conflicting security interests in the same letter-of-credit rights and proceeds of the letter of credit is governed by the following rules:

(1) Except as otherwise provided in paragraph (2):

(A) a security interest held by a secured party that has control over the letter-of-credit rights and proceeds of the letter of credit has priority to the extent of its control over a conflicting security interest held by a secured party that does not have control; and

(B) ~~(2) security~~ Except as otherwise provided in paragraph (3), security interests perfected by control rank equally.

(2) The rights of a transferee beneficiary or nominated person are independent and superior to the extent provided by Section 5-114.

~~(3) A security interest held by a transferee beneficiary has priority over a conflicting security interest held by another secured party.~~

Reporters' Comments

1. **Source.** New; loosely modeled after former Section 9-115(5).

2. **General Rule.** Paragraph (1) awards priority to a secured party that perfects its security interest directly in letter-of-credit rights (i.e., one that takes an assignment of proceeds and obtains consent of the issuer or any nominated person under Section 5-114(c)) over another conflicting security interest, such as a perfected security interest in an account supported by the letter-of-credit rights (the perfected security interest in the account gives rise to a perfected security interest in collections under the letter of credit under Section 9-308(d)). The Drafting Committee has asked the Reporters to reconsider whether the control priority may intrude unnecessarily on the priority of a financier of an underlying receivable supported by a letter-of-credit rights. The revisions reflect the Reporters' discussions with letter-of-credit experts and others.

3. **Transferee Beneficiaries.** Paragraph (2) confirms that a transferee beneficiary's rights are paramount under Section 5-114(e), which provides that the

1 “[r]ights of a transferee beneficiary or nominated person are independent of the
2 beneficiary’s assignment of the proceeds of a letter of credit and are superior to the
3 assignee’s right to the proceeds. Arguably, paragraph (2) is unnecessary and the
4 same result would obtain under Article 5, inasmuch as there is in effect a novation
5 upon the transfer with the issuer becoming bound on a new, independent obligation
6 to the transferee. In the interest of clarity, however, subsection (2) makes the
7 priority explicit in Article 9.

8 **4. Secured Party-Transferee Beneficiaries.** Drawing rights under letters
9 of credit are transferred in many commercial contexts in which the transferee is not
10 a secured party claiming a security interest in an underlying receivable supported by
11 the letter of credit. Consequently, a transfer of a letter credit is not a means of
12 “perfection” of a security interest. The transferee’s independent right to draw under
13 the letter of credit and to receive and retain the value thereunder (in effect, priority)
14 is not based on Article 9 but on letter-of-credit law and the terms of the letter of
15 credit. Assume, however, that a secured party does hold a security interest in a
16 receivable that is owned by a beneficiary-debtor and supported by a transferable
17 letter of credit. Assume further that the beneficiary-debtor causes the letter of credit
18 to be transferred to the secured party, the secured party draws under the letter of
19 credit, and, upon the issuer’s payment to the secured party-transferee, the
20 underlying account debtor’s obligation to the original beneficiary-debtor is
21 satisfied. If the payment to the secured party-transferee were considered to be
22 proceeds of the receivable collected by the secured party-transferee, the secured
23 party-transferee would have certain duties to the debtor and third parties under
24 Article 9. For example, it would be obliged to collect under the letter of credit in a
25 commercially reasonable manner and to remit any surplus pursuant to Section 9-
26 608. If, on the other hand, the secured party-transferee’s rights as transferee under a
27 new, independent obligation of the issuer are controlling, no such duties would
28 exist.

29 We see two possible resolutions of the problem presented in the preceding
30 paragraph. First, the comments (and, if necessary the statute) could explain that
31 under letter-of-credit law and practice a transferee beneficiary collects in its own
32 right arising from its own performance. Accordingly, under Section 5-114, the
33 independent and superior rights of a transferee control over any inconsistent duties
34 under Article 9. a transferee beneficiary takes a transfer of drawing rights to avoid
35 reliance on the original beneficiary’s credit and collateral; it considers any Article 9
36 rights superseded by its Article 5 rights. Moreover, it will not always be clear
37 whether a transferee beneficiary has a security interest in the underlying collateral
38 or whether any security interest senior to the rights of others. If Article 9 were to
39 control, a transferee beneficiary would find it necessary to examine the underlying
40 transaction in order to determine whether any basis exists to conclude that it may
41 have a security interest in a supported receivable or other collateral. Treating funds
42 received by a transferee beneficiary under a letter of credit as if they were funds
43 received under the supported receivable could seriously undermine the
44 independence principle as well as the commercial expectations of most transferees.
45 Moreover, the transaction described in the preceding paragraph, while not unheard
46 of, is not typical of the transactional patterns in which letters of credit are
47 transferred. a beneficiary-debtor could protect itself by arranging for a partial
48 transfer, which would entitle the transferee beneficiary to receive only the value that
49 it is entitled to retain. Finally, absolving the transferee beneficiary of duties is not

1 likely to place unreasonable risks on holders of subordinate interests in the
2 supported receivable.

3 The second approach is based on Article 9 principles. Under this view, letter-
4 of-credit law notwithstanding, a secured party should not be allowed to escape
5 otherwise nonwaivable duties by receiving a transfer of a letter of credit. Under
6 this view, a commercial party should not be unduly inconvenienced by the need to
7 determine that it has a security interest under applicable law. If it has a security
8 interest in the supported receivable, it then would be required to treat its collection
9 under the letter of credit as its collection also of the receivable. Letter-of-credit law
10 would supply the controlling priority rule by providing the transferee with
11 independent and superior rights with respect to the letter of credit and its proceeds.
12 But Article 9 would supply the necessary rules governing the secured party-
13 transferee beneficiary's duties to the debtor and third parties.

14 Letter-of-credit experts have raised concerns that the second approach could
15 result in uncertainty as to the extent to which Article 9 duties would impose on
16 applicable letter-of-credit law and practice. For example, if the secured party-
17 transferee beneficiary submits documents that an issuer deems discrepant, would
18 the beneficiary be held to a commercially reasonable standard in reaching a
19 settlement with the issuer? The Drafting Committee may wish to consider whether,
20 in the interest of certainty, Article 9 should give way to letter-of-credit law and
21 practice entirely as it concerns the rights and duties of a transferee beneficiary.

22 **SECTION 9-327. PURCHASE OF CHATTEL PAPER AND** 23 **INSTRUMENTS.**

24 (a) A purchaser of chattel paper [or an instrument] has priority over a
25 security interest in the chattel paper [or instrument] which is claimed merely as
26 proceeds of inventory subject to a security interest and, except as otherwise
27 provided in Section 9-325, in proceeds of the chattel paper if:

28 (1) in good faith and in the ordinary course of the purchaser's business,
29 the purchaser gives new value and takes possession of the chattel paper [or
30 instrument]; and

31 (2) the chattel paper [or instrument] does not indicate that it has been
32 assigned to [an identified assignee] [the person holding the conflicting security
33 interest].

1 (b) A purchaser of chattel paper {for an instrument} has priority over a
2 security interest in the chattel paper {for instrument} which is claimed other than
3 merely as proceeds of inventory subject to a security interest and, except as
4 otherwise provided in Section 9-325, in proceeds of the chattel paper {for
5 instrument} if the purchaser, ~~in good faith, in the ordinary course of the purchaser's~~
6 ~~business, and without knowledge that the purchase violates the rights of the secured~~
7 ~~party,~~ gives new value and takes possession of:

8 (1) the chattel paper in good faith, in the ordinary course of the
9 purchaser's business, and without knowledge that the purchase violates the rights of
10 the secured party; or

11 (2) the instrument in good faith and without knowledge that the
12 purchase violates the rights of the secured party.

13 (c) For purposes of subsection (b), if chattel paper {for an instrument}
14 indicates that it has been assigned to an identified secured party, a purchaser of the
15 chattel paper {for instrument} has knowledge that the purchase violates the rights of
16 the secured party.

17 [(d) Except as otherwise provided in Section 9-328(c), a [possessory
18 security interest in] [purchaser for value that takes possession of] an instrument has
19 priority over a [nonpossessory security interest in the instrument perfected by
20 means other than filing] [security interest in the instrument perfected by filing].]

21 Reporters' Comments

22 **Changes from Prior Draft:**

23 A. The draft proposes to add a good-faith requirement to subsection (a).

24 B. After discussions with the Joint Editorial Board for Uniform Real
25 Property Acts, we have revised subsection (b) to create a special priority rule for
26 purchasers of instruments who take delivery. The priority afforded by this rule
27 extends to good-faith purchasers for new value, even if they do not purchase in the
28 ordinary course of business.

1 **Discussion Question:** Is there a need to provide protection for a broader
2 class of purchasers than subsection (b) protects (e.g., secured parties who perfect by
3 possession but whose security interest secures an antecedent debt)?

4 1. **Source.** Former Section 9-308.

5 2. **Chattel Paper.** This section enables purchasers of chattel paper,
6 including secured parties, to obtain priority over earlier-perfected security interests
7 in the chattel paper. It follows former Section 9-308 in distinguishing between
8 earlier-perfected security interests in chattel paper that is claimed merely as
9 proceeds of inventory subject to a security interest and chattel paper that is claimed
10 other than merely as proceeds. Like former Section 9-308, this section does not
11 elaborate upon the phrase “merely as proceeds. For an elaboration, see P.E.B.
12 Commentary No. 8.

13 This section retains the requirements of “the ordinary course of the
14 purchaser’s business and the giving of “new value as a conditions for priority.
15 Concerning the latter, the Article deletes former Section 9-108 and adds to Section
16 9-102 a completely different definition of the term “new value.

17 A possessory security interest in chattel paper that does not qualify for
18 priority under this section may be subordinate to a perfected-by-filing security
19 interest under Section 9-319(a). In this respect, the priority rules applicable to
20 negotiable instruments constituting part of chattel paper differ from those
21 applicable to security certificates. Compare Section 9-324(2) (security interest
22 perfected by possession takes priority over security interest perfected other than by
23 control).

24 3. **Possession.** The priority afforded by this section turns in part on
25 whether a purchaser “takes possession of chattel paper. Similarly, the governing
26 law provisions in Section 9-301 address both “possessory and “nonpossessory
27 security interests. Two common practices have raised particular concerns. First, in
28 some cases the parties create more than one copy or counterpart of chattel paper
29 evidencing a single secured obligation or lease. This practice raises questions as to
30 which counterpart is the “original and whether it is necessary for a purchaser to
31 take possession of all counterparts in order to “take possession of the chattel paper.
32 Second, parties sometimes enter into a single “master agreement. The master
33 agreement contemplates that the parties will enter into separate “schedules from
34 time to time, each evidencing chattel paper. Must a purchaser of an obligation or
35 lease evidenced by a single schedule also take possession of the master agreement
36 as well as the schedule in order to “take possession of the chattel paper?

37 The problem raised by the first practice is easily solved. The parties may in
38 the terms of their agreement and by designation on the chattel paper identify only
39 one counterpart as the original chattel paper for purposes of taking possession of
40 the chattel paper. Concerns about the second practice also are easily solved by
41 careful drafting. Each schedule should provide that it incorporates the terms of the
42 master agreement, not the other way around. This will make it clear that each
43 schedule is a “stand alone document.

1 **4. Chattel Paper Claimed Merely as Proceeds.** Subsection (a) revises the
2 rule in former Section 9-308(b) to eliminate reference to what the purchaser knows.
3 Instead, a purchaser who meets the possession, ordinary course, and new value
4 requirements takes priority over a competing security interest unless the chattel
5 paper itself indicates that it has been assigned to an identified assignee or a person
6 holding the conflicting security interest. Thus subsection (a) recognizes the
7 common practice of placing a “legend” on chattel paper to indicate that it has been
8 assigned. The Drafting Committee is informed that this approach, under which the
9 chattel paper purchaser who gives new value in ordinary course can rely on
10 possession of unlegended paper without any concern for other facts that it may
11 know, comports with the expectations of both inventory and chattel paper financiers.

12 **5. Chattel Paper Claimed Other Than Merely as Proceeds.** Subsection
13 (b) revises the rule in former Section 9-308(a) by adding the requirement that the
14 purchaser take in good faith. It also eliminates the requirement that the purchaser
15 take without knowledge that the “specific paper” is subject to the security interest
16 and substitutes for it the requirement that the purchaser take “without knowledge
17 that the purchase violates the rights of the secured party. This standard derives
18 from the definition of “buyer in ordinary course of business” in Section 1-201(9).
19 The source of the purchaser’s knowledge is irrelevant. Note, however, that
20 “knowledge” means “actual knowledge.” Section 1-201(25). Thus, without more,
21 a purchaser of chattel paper who has seen a financing statement covering the chattel
22 paper or who knows that the chattel paper is encumbered with a security interest,
23 does not have knowledge that its purchase violates the secured party’s rights.
24 However, under new subsection (c), a legend to the effect that the chattel paper had
25 been assigned to an identified assignee or the person holding the conflicting
26 security interest would cause a purchaser to have wrongful knowledge for purposes
27 of subsection (b), thereby preventing the purchaser from qualifying for priority
28 under that subsection, even if the purchaser did not have actual knowledge.

29 **6. “Electronic Chattel Paper.”** The Drafting Committee (with the
30 assistance of the Working Group on Secured Transactions, Committee on the Law
31 of Commerce in Cyberspace, ABA Section of Business Law) is pursuing the
32 possibility of extending subsections (a) and (b) to cover obligations that otherwise
33 would meet the definition of “chattel paper” but are not evidenced by a writing. If
34 this proves feasible (e.g., if a suitable analogue for “possession” can be developed)
35 and desirable, the subsections might be expanded even further to cover accounts.

36 **7. Instruments.** The bracketed language in subsections (a), (b), and (d)
37 reflects the unresolved status of the priority of security interests in instruments
38 (both negotiable and nonnegotiable) which are perfected by filing. This issue is not
39 significant under current law, inasmuch as security interests in instruments
40 generally can be perfected only by possession.

41 Bracketed language in the draft presents three possible approaches. One
42 would be to adopt the bracketed language in subsections (a) and (b), thereby
43 affording purchasers of instruments, both buyers and secured parties, the same
44 rights as purchasers of chattel paper. This is the approach of former Section 9-308.
45 Adoption of this approach would eliminate any need for bracketed subsection (d).

1 Subsection (d) presents two other options for a priority rule. One is to adopt
2 for instruments the priority rule applicable to certificated securities. The 1994
3 revisions to Articles 8 and 9 marked the first time that Article 9 permitted
4 perfection of security interests in securities by filing. This Article carries forward
5 that approach. See Section 9-310(a). The 1994 revisions recognize that, in order to
6 avoid disruption of existing practices in the securities markets, it is necessary to
7 give perfection by filing a different and more limited effect for securities than for
8 other forms of collateral. In particular, the necessity of conducting a search in order
9 to ensure priority of a security interest would be enormously disruptive and
10 detrimental. Consequently, the revisions provide that a possessory security interest
11 in a security evidenced by a security certificate in registered form has priority over a
12 security interest perfected by filing. Section 9-324(2) of this Article carries this rule
13 forward.

14 The priority rule stated in Section 9-324(2) may seem anomalous, in that it
15 can afford less favorable treatment to purchasers who buy collateral outright than to
16 those who take a security interest in it. For example, a buyer of a security
17 certificate would cut off a security interest perfected by filing only if the buyer
18 achieves the status of a protected purchaser under Section 8-303. The buyer would
19 not be a protected purchaser, for example, if it does not obtain “control” under
20 Section 8-106 (e.g., if it fails to obtain a proper indorsement of the certificate) or if
21 it had notice of an adverse claim under Section 8-105. As Official Comment 5 to
22 Section 9-115 suggests, however, the priority rule is best understood not as one
23 intended to protect careless or guilty parties, but one that eliminates the need to
24 conduct a search of the public records only insofar as necessary to serve the needs
25 of the securities markets.

26 The third option, also presented in subsection (d), is to afford priority to all
27 buyers of instruments as well as to secured parties. This approach would protect
28 every purchaser for value who takes possession of an instrument. The purchaser
29 would take priority even if, for example, the purchaser knew of a conflicting claim
30 to the instrument that would disqualify it from becoming a holder in due course
31 under Section 3-302, or the instrument was not negotiable.

32 It is possible that no single rule will be optimal for all the circumstances in
33 which it might be applied. For example, broad protection of the kind suggested in
34 the third option may be useful with respect to notes secured by real property
35 mortgages, for which there is a secondary market, but considerably less so for bank
36 certificates of deposit that are transferred in non-market transactions.

37 **8. Priority in Proceeds.** Subsections (a) and (b) provide that the priority
38 afforded to purchasers of chattel paper [or instruments] extends also to proceeds of
39 the chattel paper or instrument. The purchaser acquires priority in proceeds
40 regardless of whether the purchaser perfects as to the proceeds. Former Article 9 is
41 silent as to the priority of a security interest in proceeds when a purchaser qualifies
42 for priority under Section 9-308.

43 **9. Priority in Returned and Repossessed Goods.** Returned and
44 repossessed goods may constitute proceeds of chattel paper. The following
45 Comments explain the treatment of returned and repossessed goods as proceeds of

chattel paper. The analysis is consistent with that of PEB Commentary No. 5, which these Comments replace, and is based upon the following example:

Example: Secured Party 1 (SP-1) has a security interest in all the inventory of a dealer in goods (Dealer); SP-1's security interest is perfected by filing. Dealer sells some of its inventory to a buyer in the ordinary course of business (BIOCOB) pursuant to a conditional sales contract (chattel paper). Secured Party 2 (SP-2) purchases the chattel paper from Dealer and takes possession of the paper in the ordinary course of business and without knowledge that the purchase violates the rights of SP-1. Subsequently, BIOCOB returns the goods to Dealer because they are defective. Alternatively, Dealer acquires possession of the goods following BIOCOB's default.

10. Assignment of Non-Lease Chattel Paper.

a. Loan by SP-2 to Dealer Secured by Chattel Paper (or Functional Equivalent Pursuant to Recourse Arrangement).

(1) **Returned Goods.** If BIOCOB returns the goods to Dealer for repairs, Dealer is merely a bailee and acquires thereby no meaningful rights in the goods to which SP-1's security interest could attach. (Although SP-1's security interest could attach to Dealer's interest as a bailee, that interest is not likely to be of any particular value to SP-1.) Dealer is the owner of the *chattel paper* (i.e., the owner of a right to payment secured by a security interest in the goods); SP-2 has a security interest in the chattel paper, as does SP-1 (as proceeds of the goods under Section 9-313(c)). Pursuant to Section 9-327, SP-2's security interest in the chattel paper is senior to that of SP-1. SP-2 enjoys this priority regardless of whether, or when, SP-2 filed a financing statement covering the chattel paper. Because chattel paper and goods represent different types of collateral, Dealer does not have any meaningful interest in *goods* to which either SP-1's or SP-2's security interest could attach in order to secure Dealer's obligations to either creditor. See Section 9-102 (defining "chattel paper" and "goods").

Now assume that BIOCOB returns the goods to Dealer under circumstances whereby Dealer once again becomes the owner of the goods. This would be the case, for example, if the goods were defective and BIOCOB were entitled to reject or revoke acceptance of the goods. See Sections 2-602 (rejection); 2-608 (revocation of acceptance). Unless BIOCOB has waived its defenses as against assignees of the chattel paper, SP-1's and SP-2's rights against BIOCOB would be subject to BIOCOB's claims and defenses. See Sections 9-403; 9-404. SP-1's security interest would attach again because the returned goods would be proceeds of the chattel paper. Dealer's acquisition of the goods easily can be characterized as proceeds consisting of an "in kind" collection on or distribution on account of the chattel paper. See Section 9-313(a). Assuming that SP-1's security interest is perfected by filing against the goods and that the filing is made in the same office where a filing would be made against the chattel paper, SP-1's security interest in the goods would be perfected. See Section 9-313(e).

Because Dealer's newly reacquired interest in the goods is proceeds of the chattel paper, SP-2's security interest also would attach in the goods as proceeds. If

1 SP-2 had perfected its security interest in the chattel paper by filing (again,
2 assuming that filing against the chattel paper was made in the same office where a
3 filing would be made against the goods), SP-2's security interest in the reacquired
4 goods would be perfected beyond 20 days. See Section 9-313(e). However, if the
5 SP-2 had relied only on its possession of the chattel paper for perfection and had
6 not filed against the chattel paper or the goods, SP-2's security interest would be
7 unperfected after the 20-day period. See Section 9-313(e). Nevertheless, SP-2's
8 unperfected security interest in the goods would be senior to SP-1's security interest
9 under Section 9-327. The result in this priority contest is not affected by SP-2's
10 acquiescence or non-acquiescence in the return of the goods to Dealer.

11 (2) **Repossessed Goods.** As explained above, Dealer owns the chattel
12 paper covering the goods, subject to security interests in favor of SP-1 and SP-2. In
13 Article 9 parlance, Dealer has an interest in chattel paper, not goods. If Dealer,
14 SP-1, or SP-2 repossesses the goods upon BIOCOP's default, whether the
15 repossession is rightful or wrongful as among Dealer, SP-1, or SP-2, Dealer's
16 interest will not change. The location of goods and the party who possesses them
17 does not affect the fact that Dealer's interest is in chattel paper, not goods. The
18 goods continue to be owned by BIOCOP. SP-1's security interest in the goods
19 does not attach until such time as Dealer reacquires an interest (other than a bare
20 possessory interest) in the goods. For example, Dealer might buy the goods at a
21 foreclosure sale from SP-2 (whose security interest in the chattel paper is senior to
22 that of SP-1); that disposition would cut off BIOCOP's rights in the goods. Section
23 9-615.

24 In many cases the matter would end upon sale of the goods to Dealer at a
25 foreclosure sale and there would be no priority contest between SP-1 and SP-2;
26 Dealer would be unlikely to buy the goods under circumstances whereby SP-2
27 would retain its security interest. There can be exceptions, however. For example,
28 Dealer may be obliged to purchase the goods from SP-2, SP-2 may convey the
29 goods to Dealer, and Dealer may fail to pay SP-2. Or, one could imagine that SP-2,
30 like SP-1, has a general security interest in the inventory of Dealer. In the latter
31 case, SP-2 should not receive the benefit of any special priority rule, since its
32 interest in no way derives from priority under Section 9-327. In the former case,
33 SP-2's security interest in the goods reacquired by Dealer is senior to SP-1's
34 security interest under Section 9-327.

35 b. **Dealer's Outright Sale of Chattel Paper to SP-2.** Article 9 also
36 applies to a transaction whereby SP-2 buys the chattel paper in an outright sale
37 transaction without recourse against Dealer. Sections 1-201(37); 9-102. Although
38 Dealer does not, in such a transaction, retain any residual ownership interest in the
39 chattel paper, the chattel paper constitutes proceeds of the goods to which SP-1's
40 security interest will attach and continue following the sale of the goods. Section
41 9-313(c). Even though Dealer has not retained any interest in the chattel paper, as
42 discussed above BIOCOP subsequently may return the goods to Dealer under
43 circumstances whereby Dealer reacquires an interest in the goods. The priority
44 contest between SP-1 and SP-2 will be resolved as discussed above; Section 9-327
45 makes no distinction among purchasers of chattel paper on the basis of whether the
46 purchaser is an outright buyer of chattel paper or one whose security interest
47 secures an obligation of Dealer.

1 **11. Assignment of Lease Chattel Paper.** As defined in Section 9-102,
2 chattel paper includes not only writings that evidence security interests in specific
3 goods but also those that evidence true leases of goods.

4 The analysis with respect to lease chattel paper is similar to that set forth
5 above with respect to non-lease chattel paper. It is complicated, however, by the
6 fact that, unlike the case of chattel paper arising out of a sale, Dealer retains a
7 residual interest in the *goods*. See Section 2A-103(1)(q) (defining “lessor’s residual
8 interest”); *In re Leasing Consultants, Inc.*, 486 F.2d 367 (2d Cir. 1973) (lessor’s
9 residual interest under true lease is an interest in goods and is a separate type of
10 collateral from lessor’s interest in the lease). If Dealer leases goods to a “lessee in
11 ordinary course of business” (LIOCOB), then LIOCOB takes its interest under the
12 lease (i.e., its “leasehold interest”) free of the security interest of SP-1. See
13 Sections 2A-307(3); 2A-103(1)(m) (defining “leasehold interest”), (1)(o) (defining
14 “lessee in ordinary course of business”). SP-1 would, however, retain its security
15 interest in the residual interest. In addition, SP-1 would acquire an interest in the
16 lease chattel paper as proceeds. If Dealer then assigns the lease chattel paper to
17 SP-2, Section 9-327 gives SP-2 priority over SP-1 with respect to the chattel paper,
18 *but not* with respect to the residual interest in the *goods*. Consequently, assignees
19 of lease chattel paper typically take a security interest in and file against the lessor’s
20 residual interest in goods, expecting their priority in the goods to be governed by
21 the first-to-file-or-perfect rule of Section 9-319.

22 If the goods are returned to Dealer, other than upon expiration of the lease
23 term, then the security interests of both SP-1 and SP-2 normally would attach to the
24 goods as proceeds of the chattel paper. (If the goods are returned to Dealer at the
25 expiration of the lease term and the lessee has made all payments due under the
26 lease, however, then Dealer no longer has any rights under the chattel paper.
27 Dealer’s interest in the goods consists solely of its residual interest, as to which
28 SP-2 has no claim.) This would be the case, for example, when the lessee rescinds
29 the lease or when the lessor recovers possession in the exercise of its remedies
30 under Article 2A. See, e.g., Section 2A-525. If SP-2 enjoyed priority in the chattel
31 paper under Section 9-327, then SP-2 likewise would enjoy priority in the returned
32 goods as proceeds. This does not mean that SP-2 necessarily is entitled to the entire
33 value of the returned goods. The value of the goods represents the sum of the
34 present value of (i) the value of their use for the term of the lease and (ii) the value
35 of the residual interest. SP-2 has priority in the former, but SP-1 ordinarily would
36 have priority in the latter. Thus, an allocation of a portion of the value of the goods
37 to each component may be necessary.

38 **SECTION 9-328. PRIORITY OF RIGHTS OF PURCHASERS OF**
39 **INSTRUMENTS, DOCUMENTS, AND SECURITIES UNDER OTHER**
40 **ARTICLES; PRIORITY OF INTERESTS IN FINANCIAL ASSETS AND**
41 **SECURITY ENTITLEMENTS UNDER ARTICLE 8.**

1 (a) (1) Except as otherwise provided in subsection (d), nothing in this
2 article limits the rights of a holder in due course of a negotiable instrument, a holder
3 to whom a negotiable document of title has been duly negotiated, or a protected
4 purchaser of a security.

5 (2) These holders or purchasers take priority over an earlier security
6 interest, even if perfected, to the extent provided in Articles 3, 7, and 8.

7 (b) A person that deals with or has an interest in a financial asset or security
8 entitlement has priority over a security interest, even if perfected, to the extent
9 provided in Article 8.

10 (c) Filing under this article does not constitute notice of a ~~security interest~~
11 claim or defense to the holders, or purchasers, or persons mentioned in subsections
12 (a) and (b).

13 (d) The holder of a subordinate security interest in an account takes an
14 instrument constituting proceeds of the account subject to the claim of a holder of a
15 security interest having higher priority in the account unless:

16 (1) the holder of the subordinate security interest is a holder in due
17 course;

18 (2) the holder of the subordinate security interest gives an authenticated
19 notification to the holders of all security interests having higher priority in the
20 account;

21 (3) each holder of a security interest having higher priority receives the
22 notification at least 21 days prior to the receipt of the instrument by the holder of
23 the subordinate security interest;

24 (4) the notification provides the name, address, and telephone number of
25 the holder of the subordinate security interest and the name of the debtor; and

(5) the notification states that the holder of the subordinate security interest holds a security interest in the account.

Reporters' Comments

Discussion Question: See Comment 6.

1. **Source.** Former Section 9-309.

2. **“Priority.”** In some provisions, this Article distinguishes between claimants that take collateral free of a security interest (in the sense that the security interest no longer encumbers the collateral) and those that take an interest in the collateral that is senior to a surviving security interest. See, e.g., Section 9-315. Whether a holder or purchaser referred to in this section takes free or is senior to a security interest depends on whether the purchaser is a buyer of the collateral or takes a security interest in it. The term “priority” is meant to encompass both scenarios, as it does in Section 9-327. It also is intended to embrace protections against liability under Article 8. See, e.g., §§ 8-115; 8-502.

3. **Rights Acquired by Purchasers.** The holders and purchasers referred to in this section do not always take priority over a security interest. See, e.g., Section 7-503 (affording paramount rights to certain owners and secured parties as against holder to whom a negotiable document of title has been duly negotiated). Accordingly, this section adds the clause, “to the extent provided in Articles 3, 7, and 8” to former Section 9-309.

4. **Financial Assets and Security Entitlements.** New subsection (b) responds to some suggestions that this section should provide explicit protection for those who deal with financial assets and security entitlements which are parallel to those under subsection (a) for protected purchasers of securities. The new subsection makes explicit in Article 9 what is already implicit in Article 9 and explicit in several provisions of Article 8. See, e.g., Sections 8-502; 8-503(e); 8-510; 8-511. This does not change current law. As with its predecessor, former Section 9-309, the purpose of this section is to make an explicit statement in Article 9 of what would otherwise be implicit. However, further consideration must be given to whether this subsection is necessary, whether it is too broad, and whether it might spawn unintended consequences.

5. **Instrument Constituting Proceeds of Account.** Subsection (d) contains an exception to the general deference this Article pays to Article 3. It provides that the priority of a security interest in an account extends to an instrument that is proceeds of the right to payment. The general rule in subsection (a) leaves open the possibility that the holder of a junior security interest in accounts might be able to collect the accounts and, as a holder in due course, rightfully refuse to turn over the collections to the holder of the senior security interest. Accounts financiers are professionals and should know whether their security interests are senior or junior. The holder-in-due-course rules of Article 3 should not enable a junior secured party to improve its position unless it first takes steps to permit the senior secured party to protect its position. Under subsection (d), a junior secured party’s holder-in-due-course status affords it priority over a

senior secured party's interest only if the junior party complies with the notification requirements in paragraphs (2) - (5).

6. Liability for Collections by Junior Secured Parties. It is imaginable that a senior secured party would not undertake direct collections and that a junior secured party would collect receivables directly from account debtors over a substantial period of time. If, under subsection (d), the junior secured party takes subject to the senior's claim, the issue of the junior's liability to the senior and the amount of any liability arises. We assume that in some circumstances the junior will be liable to the senior for the entire amount of the junior's collections. However, we also assume that the senior would not be entitled to a windfall; the junior should not be liable to the senior for any amount beyond the senior's actual loss. For example, if the debtor would have been entitled to collect and use the receivables had the junior not collected them (perhaps because the senior's loan-to-value requirements (borrowing base) had at all times been satisfied), in our view the junior should bear no liability. The Drafting Committee may wish to consider whether it is necessary to address this issue directly in the statute.

SECTION 9-329. TRANSFER OF MONEY; TRANSFER OF FUNDS FROM DEPOSIT ACCOUNT.

(a) A transferee of money takes the money free of a security interest unless the transferee acts in collusion with the debtor in violating the rights of the secured party.

(b) A transferee of funds from a deposit account takes the funds free of a security interest in the deposit account unless the transferee acts in collusion with the debtor in violating the rights of the secured party.

Reporters' Comments

1. **Source.** New.

2. **Scope.** This section affords broad protection to transferees who take funds from a deposit account and to those who take money. The term “transferee” is not defined; however, the debtor itself is not a transferee. Thus this section does not cover the case in which a debtor withdraws money (currency) from its deposit account or the case in which a depository institution debits an encumbered account and credits another account it maintains for the debtor.

A transfer of funds from a deposit account, to which subsection (b) applies, normally will be made by check, by funds transfer, or by debiting the debtor's deposit account and crediting another depositor's account.

Example 1: Debtor maintains a deposit account with Bank A. The deposit account is subject to a security interest in favor of Lender. At Bank B's

1 suggestion, Debtor moves the funds from the account at Bank A to Debtor's
2 deposit account with Bank B. Unless Bank B acted in collusion with
3 Debtor in violating Lender's rights (an unlikely scenario, where, as here,
4 Lender allowed Debtor access to an account sufficient to transfer funds),
5 Bank B takes the funds (the credits running in favor of Bank B) free from
6 Lender's security interest. See subsection (b). However, inasmuch as the
7 deposit account maintained with Bank B constitutes the proceeds of the
8 deposit account at Bank A, Lender's security interest would attach to that
9 account as proceeds. See Section 9-313.

10 Subsection (b) also would apply if, in the example, Bank A debited Debtor's
11 deposit account in exchange for the issuance of Bank A's cashier's check. Lender's
12 security interest would attach to the cashier's check as proceeds of the deposit
13 account, and the rules applicable to instruments would govern any competing
14 claims to the cashier's check. See Sections 3-306; 9-328.

15 If Debtor withdraws money (currency) from an encumbered deposit account
16 and transfers the money to a third party, then subsection (a), to the extent not
17 displaced by federal law relating to money, applies. It contains the same rule as
18 subsection (b).

19 Subsection (b) applies to *transfers of funds from* a deposit account; it does
20 not apply to *transfers of the deposit account* itself or of an interest therein. For
21 example, this section does not apply to the creation of a security interest in a
22 deposit account. Competing claims to the deposit account itself are dealt with by
23 other Article 9 priority rules. See Sections 9-315(a); 9-325; 9-337; 9-338.
24 Similarly, a corporate merger normally would not result in a transfer of funds from
25 a deposit account. Rather, it might result in a transfer of the deposit account itself.
26 The normal rules applicable to transferred collateral would apply; this section
27 would not.

28 **3. Policy.** Broad protection for transferees helps to ensure that security
29 interests in deposit accounts do not impair the free flow of funds. It also minimizes
30 the likelihood that a secured party will enjoy a claim to whatever the transferee
31 purchases with the funds. Rules concerning recovery of payments traditionally
32 have placed a high value on finality. The opportunity to upset a completed
33 transaction, or even to place a completed transaction in jeopardy by bringing suit
34 against the transferee of funds, should be severely limited. Although the giving of
35 value usually is a prerequisite for receiving the ability to take free from third-party
36 claims, where payments are concerned the law is even more protective. Thus,
37 Section 3-418(c) provides that, even where the law of restitution otherwise would
38 permit recovery of funds paid by mistake, no recovery may be had from a person
39 "who in good faith changed position in reliance on the payment. Rather than
40 adopt this standard, this section eliminates all reliance requirements whatsoever.
41 Payments made by mistake are relatively rare, but payments of funds from
42 encumbered deposit accounts (e.g., deposit accounts containing collections from
43 accounts receivable) occur with great regularity. In the mine run of cases, unlike
44 payment by mistake, no one would object to these payments. In the vast proportion
45 of cases, the transferee probably would be able to show a change of position in
46 reliance on the payment. This section does not put the transferee to the burden of
47 having to make this proof.

1 4. **“Bad Actors.”** To deal with the question of the “bad actor, this section
2 borrows “collusion” language from Article 8. See, e.g., Sections 8-115, 8-503(e).
3 This is the most protective (i.e., least stringent) of the various standards now found
4 in the UCC. Compare, e.g., Section 1-201(9) (“without knowledge that the sale . . .
5 is in violation of the . . . security interest”); Section 1-201(19) (“honesty in fact in
6 the conduct or transaction concerned”); Section 3-302(a)(2)(v) (“without notice of
7 any claim”).

8 5. **Other Remedies for Aggrieved Secured Party.** The Drafting
9 Committee may consider whether (and, if so, how) to address remedies that might
10 be available to an aggrieved secured party, other than enforcement of its security
11 interest. One approach might be to treat this issue in the statute itself. For
12 example, the protection that Section 8-503 affords to certain purchasers extends to
13 immunize them from any action based on the property interest, “whether framed in
14 conversion, replevin, constructive trust, equitable lien, or other theory. Another
15 approach would address the issue in the Official Comments, as is done in Official
16 Comment 9 to Section 9-115 (addressing the relation of Article 9’s priority rules to
17 other law that affords a remedy for wrongful conduct). A third possibility is to
18 leave development of the law to the courts without additional guidance.

19 6. **Transferee Who Does Not Take Free.** This section sets forth the
20 circumstances under which certain transferees of money or funds take free of
21 security interests. It does not determine the rights of a transferee who does not take
22 free of a security interest.

23 **Example 2:** The facts are as in Example 1, but, in wrongfully moving the
24 funds from the deposit account at Bank A to Debtor’s deposit account with
25 Bank B, Debtor acts in collusion with Bank B. Bank B does not take the
26 funds free of Lender’s security interest under this section. If Debtor grants a
27 security interest to Bank B, Section 9-325 governs the relative priorities of
28 Lender and Bank B. Under Section 9-325(3), Bank B’s security interest in
29 the Bank B deposit account is senior to Lender’s security interest in the
30 deposit account as proceeds. However, Bank B’s senior security interest
31 does not protect Bank B against any liability to Lender that might arise from
32 Bank B’s wrongful conduct. As noted in Example 1, the potential for
33 collusion in violating a secured party’s rights under these circumstances
34 seems more theoretical than real.

35 **SECTION 9-330. PRIORITY OF CERTAIN LIENS ARISING BY**
36 **OPERATION OF LAW. [MINOR STYLE CHANGES ONLY]** If a person in
37 the ordinary course of the person's business furnishes services or materials with
38 respect to goods subject to a security interest, a lien upon goods in the possession of
39 the person given by statute or rule of law for the materials or services takes priority

1 over a perfected security interest unless the lien is statutory and the statute
2 expressly provides otherwise.

3 Reporters' Comments

4 1. **Source.** Former Section 9-310.

5 2. **Status.** The Drafting Committee has not considered this section. The
6 liens that it covers are possessory liens under common law or statute. It may be
7 necessary to clarify this section to make clear that it does not deal with statutory
8 liens, as defined in Section 9-102. Statutory liens do not depend on possession for
9 their effectiveness.

10 **SECTION 9-331. PRIORITY OF SECURITY INTERESTS IN**
11 **FIXTURES.**

12 (a) A mortgage is a construction mortgage to the extent that it secures an
13 obligation incurred for the construction of an improvement on land including the
14 acquisition cost of the land if the recorded record so indicates.

15 (b) (1) Subject to paragraph (2), a a security interest under this article may
16 be created in goods that are fixtures or may continue in goods that become fixtures.

17 (2) No ~~However, no~~ security interest exists under this article in ordinary
18 building materials incorporated into an improvement on land.

19 (c) This article does not prevent creation of an encumbrance upon fixtures
20 under real property law.

21 (d) A perfected security interest in fixtures has priority over a conflicting
22 interest of an encumbrancer or owner of the real property if:

23 (1) (A) except as otherwise provided in subsection (g), the security
24 interest is:

25 (i) a purchase money security interest; [and]

26 (ii) [the interest of the encumbrancer or owner arises before the
27 goods become fixtures; and

1 (iii)] the security interest is perfected by a fixture filing before
2 the goods become fixtures or within ~~10~~ 20 days thereafter; and

3 (B) the debtor has an interest of record in the real property or is in
4 possession of the real property;

5 (2) (A) the security interest:

6 (i) is perfected by a fixture filing before the interest of the
7 encumbrancer or owner is of record;

8 (ii) the security interest has priority over any conflicting interest
9 of a predecessor in title of the encumbrancer or owner; and

10 (B) the debtor has an interest of record in the real property or is in
11 possession of the real property;

12 (3) (A) the fixtures are readily removable:

13 (i) factory or office machines;

14 (ii) ~~readily removable~~ equipment that is not primarily used or
15 leased for use in the operation of the real property; or

16 (iii) ~~readily removable~~ replacements of domestic appliances that
17 are consumer goods; and

18 (B) before the goods become fixtures the security interest is
19 perfected by any method permitted by this article; ~~or~~

20 (4) the conflicting interest is a lien on the real property obtained by legal
21 or equitable proceedings after the security interest was perfected by any method
22 permitted by this article; or

23 (5) the security interest is:

24 (A) created in a manufactured home in a manufactured home
25 transaction; and

1 (B) perfected pursuant to a statute described in Section 9-309A(a)(2)
2 or (3) [before the manufactured home becomes a fixture or within 20 days
3 thereafter].

4 (e) A security interest in fixtures, whether or not perfected, has priority over
5 a conflicting interest of an encumbrancer or owner of the real property if:

6 (1) the encumbrancer or owner has, in an authenticated record,
7 consented to the security interest or disclaimed an interest in the goods as fixtures;
8 or

9 (2) the debtor has a right to remove the goods as against the
10 encumbrancer or owner.

11 (f) The priority of the security interest under subsection (e) continues for a
12 reasonable time if ~~if~~ the debtor's right to remove the goods as against the
13 encumbrancer or owner terminates, ~~the priority of the security interest under~~
14 ~~subsection (e) continues for a reasonable time.~~

15 (g) (1) Notwithstanding subsection Subject to (d)(1) but otherwise subject
16 to subsections (d)(2) through (4), (e), and (f), a security interest in fixtures is
17 subordinate to a construction mortgage recorded before the goods become fixtures
18 if the goods become fixtures before the completion of the construction.

19 (2) A mortgage has this priority to the same extent as a construction
20 mortgage to ~~To~~ the extent that it is given to refinance a construction mortgage, ~~a~~
21 ~~mortgage has this priority to the same extent as the construction mortgage.~~

22 (h) In cases not governed by subsections (b) through (g), a security interest
23 in fixtures is subordinate to a conflicting interest of an encumbrancer or owner of
24 the related real property which is not the debtor.

25 Reporters' Comments

26 **Changes from Prior Draft:**

1 A. Like all other 10-day periods, the one in this section has been
2 changed to 20 days

3 B. Regarding subsection (d)(5), see Comment 2.

4 1. **Source.** Former Section 9-313, conformed to Section 2A-309 and to
5 prevailing style conventions.

6 2. **Manufactured Home Priority.** Subsection (d)(5) is new. It responds to
7 a proposal made on behalf of the Manufactured Housing Institute. Under the new
8 priority rule, a security interest in a manufactured home which is perfected under a
9 certificate of title law (see Section 9-309A(a)) has priority over a conflicting
10 interest of an encumbrancer or owner of the real property. (Priority contests with
11 other Article 9 security interests would be governed by the usual priority rules.)
12 Bracketed language in subparagraph (B) raises the question whether the priority
13 rule should apply only when perfection is achieved before or within 20 days after
14 the manufactured home becomes a fixture (as under subsection (d)(1), for purchase
15 money security interests).

16 **SECTION 9-332. ACCESSIONS.**

17 **Alternative A**

18 (a) [In this section,] “accession means goods that are [installed in,]
19 [affixed to,] [attached to,] [assembled with,] [manufactured into,] [processed with,]
20 [or] [processed into] other goods in a manner such that the identity of the original
21 goods is not lost.

22 **Alternative B**

23 (a) [In this section,] “accession means goods that are physically united
24 with other goods in a manner such that the identity of the original goods is not lost.

25 **[End of Alternatives]**

26 (b) A security interest may be created in an accession and continues in
27 collateral that becomes an accession.

28 (c) If a security interest is perfected when the collateral becomes an
29 accession, the security interest remains perfected in the [collateral] [accession].

30 (d) Except as otherwise provided in subsection (e), the other provisions of
31 this part determine the priority of a security interest in an accession.

1 (e) A security interest in an accession is subordinate to a security interest in
2 the whole which is perfected by compliance with the requirements of a certificate-
3 of-title statute under Section 9-309A(b).

4 (f) On default, subject to part 6, a secured party may remove an accession
5 from other goods if[:

6 (1)] the security interest in the accession has priority over the claims of
7 every person having an interest in the whole[; and

8 (2) removal will not cause [material] [serious] [irreparable] physical
9 injury to the whole].

10 (g) (1) ~~[Unless otherwise agreed, a]~~ [A] secured party that removes an
11 accession under subsection (f) shall promptly reimburse any encumbrancer or
12 owner of the whole, other than the debtor, for the cost of repair of any physical
13 injury to the whole.

14 (2) The secured party need not reimburse the encumbrancer or owner
15 for any diminution in value of the whole caused by the absence of the accession
16 removed or by any necessity for replacing it.

17 (3) A person entitled to reimbursement may refuse permission to
18 remove until the secured party gives adequate assurance for the performance of the
19 obligation to reimburse.

20 Reporters' Comments

21 1. **Source.** New. This section replaces former Section 9-314.

22 2. **Status.** The Drafting Committee discussed former Section 9-314 in
23 November, 1997. This section reflects those deliberations. The Drafting
24 Committee has yet to review this section. The Comments below explain the text
25 and indicate specific issues that the Drafting Committee may wish to address.

26 3. **Background.** Grant Gilmore set forth the pre-UCC rule governing
27 accessions as follows: when accessories were installed in or attached to goods in
28 which a security interest existed (e.g., a radio was installed in an automobile),
29 courts subordinated the security interest in the automobile to the (usually, purchase
30 money) security interest in the accessory; however, when the accessories could be

described as “integral parts of the car (e.g., an engine), the security interest in the accessory was not infrequently subordinated to the competing interest in the automobile. Former Section 9-314 was, in Gilmore’s words, “an exact replica of the 1962 version of Section 9-313 on fixtures. As such, it went somewhat beyond the protection that the pre-UCC automobile cases afforded security interests in accessories.

4. **“Accession.”** This section applies to an “accession, as defined, regardless of the cost or difficulty of removing the accession from the other goods, and regardless of whether the original goods have come to form an integral part of the other goods. This section does not apply to goods whose identity has been lost. Goods of that kind are “commingled goods governed by Section 9-333. Neither this section nor the following one addresses case of collateral that changes form without the addition of other goods.

The Drafting Committee has yet to choose between the alternative definitions of “accession. The alternatives are intended to convey the same meaning and differ only in the level of specificity.

5. **“Accession” versus “Other Goods.”** This section distinguishes among the “accession, the “other goods, and the “whole. The last term refers to the combination of the “accession and the “other goods. If one person’s collateral becomes physically united with another person’s collateral, each is an “accession.

Example 1: SP-1 holds a security interest in the debtor’s tractors (which are not subject to a certificate-of-title law), and SP-2 holds a security interest in a particular tractor engine. The engine is installed in a tractor. From the perspective of SP-1, the tractor becomes an “accession and the engine is the “other goods. From the perspective of SP-2, the engine is the “accession and the tractor is the “other goods. The completed tractor–tractor cum engine–constitutes the “whole.

6. **Scope.** This section governs only a few issues concerning accessions. Subsection (b) contains rules governing continuation of a security interest in an accession. Subsection (c) contains a rule governing continued perfection of a security interest in goods that become an accession. Subsection (e) contains a special priority rule governing accessions that become part of a whole covered by a certificate of title. Subsections (f) and (g) govern enforcement of a security interest in an accession. The Drafting Committee may wish to consider whether these disparate provisions should remain together in a single section or should be divided according to topic (e.g., subsections (f) and (g) might fit better in part 6).

7. **Matters Left to Other Provisions of This Article: Attachment and Perfection.** In this connection, consider that other provisions of this Article often will govern accession-related issues. For example, this section does not address whether a secured party acquires a security interest in the whole if its collateral becomes an accession. Normally this will turn on the description of the collateral in the security agreement. The Drafting Committee may wish to consider whether to add a *per se* rule under which a security interest would extend automatically to all accessions, as it does to proceeds.

1 **Example 2:** Debtor owns a computer subject to a perfected security interest
2 in favor of SP-1. Debtor acquires memory and installs it in the computer.
3 Whether SP-1's security interest attaches to the memory depends on
4 whether the security agreement covers it.

5 Similarly, this section does not determine whether perfection against
6 collateral that becomes an accession is effective to perfect a security interest in the
7 whole. Other provisions of this article, including the requirements for indicating
8 the collateral covered by a financing statement, resolve that question.

9 **8. Matters Left to Other Provisions of This Article: Priority.** With one
10 exception, concerning goods covered by a certificate of title (see subsection (e)), the
11 other provisions of this part, including the rules governing purchase money security
12 interests, determine the priority of most security interests in an accession, including
13 the relative priority of a security interest in an accession and a security interest in
14 the whole. See subsection (d).

15 **Example 3:** Debtor owns an office computer subject to a security interest in
16 favor of SP-1. Debtor acquires memory and grants a perfected security
17 interest in the memory to SP-2. Debtor installs the memory in the
18 computer, at which time (we assume) SP-1's security interest attaches to the
19 memory. The first-to-file-or-perfect rule of Section 9-319 governs priority
20 in the memory. If, however, SP-2's security interest is a purchase money
21 security interest, Section 9-322(d) would afford priority in the memory to
22 SP-2, regardless of which security interest was perfected first.

23 **9. Goods Covered by a Certificate of Title.** This section does govern the
24 priority of a security interest in an accession that is or becomes part of a whole that
25 is subject to a security interest perfected by compliance with a certificate-of-title
26 statute. Subsection (e) provides that a security interest in the whole, perfected by
27 compliance with a certificate-of-title statute, takes priority over a security interest in
28 the accession. It enables a secured party to rely upon a certificate of title without
29 having to check the UCC files to determine whether any components of the
30 collateral may be encumbered. The subsection imposes a corresponding risk upon
31 those who finance goods that may become part of goods covered by a certificate of
32 title. In doing so, it reverses the priority that appeared reasonable to most pre-UCC
33 courts.

34 **Example 4:** Debtor owns an automobile subject to a security interest in
35 favor of SP-1. The security interest is perfected by notation on the
36 certificate of title. Debtor buys tires subject to a perfected-by-filing
37 purchase money security interest in favor of SP-2 and mounts the tires on
38 the automobile's wheels. If the security interest in the automobile attaches
39 to the tires, then SP-1 acquires priority over SP-2. The same result would
40 obtain if SP-1's security interest attached to the automobile and was
41 perfected after the tires had been mounted on the wheels.

42 **SECTION 9-333. COMMINGLED GOODS.**

43 **Alternative A**

(a) In this section, “commingled goods” means goods that are manufactured, processed, assembled, or commingled with other goods in such a manner that their identity is lost in a product or mass.

Alternative B

(a) In this section, “commingled goods” means goods that are physically [united with] [related to] other goods in such a manner that their identity is lost in a product or mass.

[End of Alternatives]

Alternative A

(b) Except as otherwise provided in subsection (c), a security interest may not be created in commingled goods.

(c) [(1)] If collateral becomes commingled goods, the security interest in the collateral is discharged, and a security interest attaches to the product or mass.

[(2) The secured party may not enforce the security interest in the product or mass to the extent the value of product or mass at the time of enforcement exceeds the value of the collateral at the time it became commingled goods.]

Alternative B

(b) Except as otherwise provided in subsection (c), no security interest exists [under this Article] in commingled goods.

(c) [(1)] If collateral becomes commingled goods, a security interest attaches to the product or mass.

[(2) The secured party may not enforce the security interest in the product or mass to the extent the value of product or mass at the time of enforcement exceeds the value of the collateral at the time it became commingled goods.]

[End of Alternatives]

1 (d) If a security interest in collateral is perfected before the collateral
2 becomes commingled goods, the security interest that attaches to the product or
3 mass under subsection (c) is perfected.

4 (e) Except as otherwise provided in subsection (f), the other provisions of
5 this part, as applicable, determine the priority of a security interest that attaches to
6 the product or mass under subsection (c).

7 (f) If more than one security interest attaches to the product or mass under
8 subsection (c), the following rules determine priority:

9 (1) A security interest that is perfected under subsection (d) has priority
10 over a security interest that is unperfected at the time the collateral becomes
11 commingled goods.

12 (2) If more than one security interest is perfected under subsection (d),
13 the security interests rank equally in proportion to value of the collateral at the time
14 it became commingled goods.

15 Reporters' Comments

16 1. **Source.** New. This section replaces former Section 9-315.

17 2. **Status.** The Drafting Committee discussed former Section 9-315 in
18 November, 1997. This section reflects those deliberations. The Drafting
19 Committee has yet to review this section. The Comments below explain the text
20 and indicate specific issues that the Drafting Committee may wish to address.

21 3. **“Commingled Goods.”** Subsection (a) defines “commingled goods. It
22 is meant to include not only goods whose identity is lost through manufacturing or
23 production (e.g., flour that has become part of baked goods) but also goods whose
24 identity is lost by commingling with other goods from which they cannot be
25 distinguished (e.g., ball bearings).

26 The Drafting Committee has yet to choose between the alternative
27 definitions of “commingled goods. The alternatives are intended to convey the
28 same meaning and differ only in the level of specificity. The introductory clause,
29 “in this section, appears in brackets pending a determination whether the defined
30 term will appear elsewhere in the Article.

31 4. **Consequences of Becoming “Commingled Goods.”** By definition, the
32 identity of the original collateral cannot be determined once the original collateral
33 becomes commingled goods. Consequently, the security interest in the specific

original collateral alone is lost once the collateral becomes commingled goods, and no security interest in the original collateral can be created thereafter except as a part of the resulting product or mass. See subsections (b) and (c).

Once collateral becomes commingled goods, the secured party's security interest is transferred from the original collateral to the product or mass. See subsection (c). If the security interest in the original collateral was perfected, the security interest in the product or mass is a perfected security interest. See subsection (d). This perfection continues until lapse.

A security interest in a product or mass that arises under subsection (c) can be enforced only to the extent of the value of the original collateral (or, if it is less, the amount of the secured obligation). This section leaves the courts free to define "value" in this context.

5. Priority of Perfected Security Interests That Attach under this Section. This section governs the priority of competing security interests in a product or mass only when both security interests arise under this section. In that case, if both security interests are perfected by operation of this section (see subsections (c) and (d)), then the security interests rank equally, in proportion to the value of the collateral at the time it became commingled goods. See subsection (f)(2).

Example 1: SP-1 has a perfected security interest in Debtor's eggs, which have a value of \$ 300 and secure a debt of \$ 400, and SP-2 has a perfected security interest in Debtor's flour, which has a value of \$ 500 and secures a debt of \$ 600. Debtor uses the flour and eggs to make cakes, which have a value of \$ 1000. The two security interests rank equally and share in the ratio of 3:5. Applying this ratio to the entire value of the product, SP-1 would be entitled to \$ 375 (i.e., $3/8 \times \$ 1000$), and SP-2 would be entitled to \$ 625 (i.e., $5/8 \times \$ 1000$). However, under subsection (c), SP-1 may enforce its security interest only to the extent of \$ 300, and SP-2 may enforce its security interest only to the extent of \$ 500. This leaves \$ 200 for Debtor.

Example 2: Assume the facts of Example 1, except that SP-1's collateral, worth \$ 300, secures a debt of \$ 200. Recall that, if the cake is worth \$ 1000, then applying the ratio of 3:5 would entitle SP-1 to \$ 375 and SP-2 to \$ 625. However, SP-1 is not entitled to collect from the product more than it is owed. Accordingly, SP-1's share would be only \$ 200, SP-2 would receive \$ 500 (the value of its original collateral), and Debtor would keep the remaining \$ 300.

Example 3: Assume that the cakes in the previous examples have a value of only \$ 600. Again, the parties share in the ratio of 3:5. If, as in Example 1, SP-1 is owed \$ 400, then SP-1 is entitled to \$ 225 (i.e., $3/8 \times \$ 600$), and SP-2 is entitled to \$ 375 (i.e., $5/8 \times \$ 600$). Debtor receives nothing. If, however, as in Example 2, SP-1 is owed only \$ 200, then Debtor receives \$ 25.

The results in the foregoing examples remain the same, regardless of whether SP-1 or SP-2 (or each) has a purchase money security interest.

1 **6. Perfection: Unperfected Security Interests.** The rule explained in the
2 preceding Comment applies only when both security interests in original collateral
3 are perfected when the goods become commingled goods. If a security interest in
4 original collateral is unperfected at the time the collateral becomes commingled
5 goods, subsection (f)(1) applies.

6 ***Example 4:*** SP-1 has a perfected security interest in the debtor's eggs, and
7 SP-2 has an unperfected security interest in the debtor's flour. Debtor uses
8 the flour and eggs to make cakes. Under subsection (c), both security
9 interests attach to the cakes. But since SP-1's security interest was
10 perfected at the time of commingling and SP-2's was not, only SP-1's
11 security interest in the cakes is perfected. See subsection (d). Under
12 subsection (f)(1) and Section 9-319, SP-1's perfected security interest has
13 priority over SP-2's unperfected security interest.

14 If both security interests are unperfected, the residual first-to-attach rule of Section
15 9-319 would apply.

16 **7. Multiple Security Interests.** On occasion, a single input may be
17 encumbered by more than one security interest. In those cases, we suggest that the
18 multiple secured parties be treated like a single secured party for purposes of
19 determining their collective share under subsection (f)(2). The normal priority rules
20 would determine how that share would be allocated between them. Consider the
21 following example, which is a variation on Example 1 above:

22 ***Example 5:*** SP-1A has a perfected, first-priority security interest in
23 Debtor's eggs. SP-1B has a perfected, second-priority security interest in
24 the same collateral. The eggs have a value of \$ 300. Debtor owes \$ 200 to
25 SP-1A and \$ 200 to SP-1B. SP-2 has a perfected security interest in
26 Debtor's flour, which has a value of \$ 500 and secures a debt of \$ 600.
27 Debtor uses the flour and eggs to make cakes, which have a value of \$ 1000.

28 For purposes of subsection (f)(2), we suggest that SP-1A and SP-1B be
29 treated like a single secured party. The collective security interest would
30 rank equally with that of SP-2. Thus, the secured parties would share in the
31 ratio of 3 (for SP-1A and SP-1B combined) to 5 (for SP-2). Applying this
32 ratio to the entire value of the product, SP-1A and SP-1B in the aggregate
33 would be entitled to \$ 375 (i.e., $3/8 \times \$ 1000$), and SP-2 would be entitled to
34 \$ 625 (i.e., $5/8 \times \$ 1000$). However, under subsection (c), SP-1A and
35 SP-1B may enforce their security interest only to the extent of \$ 300.
36 (Likewise, SP-2 would be limited to a \$ 500 recovery.)

37 SP-1A and SP-1B would share the \$ 300 in accordance with their priority,
38 as established under other rules. Inasmuch as SP-1A has first priority, it
39 would receive \$ 200, and SP-1B would receive \$ 100.

40 If the Drafting Committee agrees with this approach, we will attempt to draft an
41 appropriate provision. It is possible that an explanation in the Official Comments
42 would suffice.

8. Priority of Security Interests That Attach Other than by Operation of this Section. Under subsection (e), the normal priority rules determine the priority of a security interest that attaches to the product or mass other than by operation of this section. For example, assume that SP-1 has a perfected security interest in Debtor's existing and after-acquired baked goods, and SP-2 has a perfected security interest in Debtor's flour. When the flour is processed into cakes, subsections (c) and (d) provide that SP-2 acquires a perfected security interest in the cakes. If SP-1 filed against the baked goods before SP-2 filed against the flour, then SP-1 will enjoy priority in the cakes. See Section 9-319 (first-to-file-or-perfect). But if SP-2 filed against the flour before SP-1 filed against the baked goods, then SP-2 will enjoy priority in the cakes to the extent of its security interest.

9. **Organization.** As is the case with Section 9-332, this section contains attachment, perfection, and priority rules. The Drafting Committee may wish to consider whether these disparate provisions should remain together in a single section or should be divided according to topic.

SECTION 9-334. PRIORITY OF SECURITY INTERESTS IN GOODS COVERED BY CERTIFICATE OF TITLE. If, while a security interest in

goods is perfected by any method under the law of another jurisdiction, this State issues a certificate of title that neither shows that the goods are subject to the security interest nor contains a statement that they may be subject to security interests not shown on the certificate:

(1) a buyer of the goods, other than a person that is in the business of selling goods of that kind, takes free of the security interest to the extent that the buyer gives value and receives delivery of the goods after issuance of the certificate and without knowledge of the security interest; and

(2) the security interest is subordinate to a conflicting security interest in the goods that attaches, and is perfected under Section 9-309A(c), after issuance of the certificate and without the conflicting secured party's knowledge of the security interest.

Reporters' Comments

1. **Source.** Derived from former Section 9-103(2)(d).

2. Protection for Buyers and Secured Parties. This section affords protection to certain good faith purchasers for value who are likely to have relied on

a “clean” certificate of title, i.e., one that neither shows that the goods are subject to a particular security interest nor contains a statement that they may be subject to security interests not shown on the certificate. Under this section, a protected buyer can take free of, and a protected secured party can acquire priority over, a security interest that is perfected by any method under the law of another jurisdiction. The fact that the security interest has been reperfected by possession does not of itself disqualify a secured party from protection under subsection (b).

**SECTION 9-335. PRIORITY OF SECURITY INTEREST OR
STATUTORY LIEN PERFECTED BY EFFECTIVE FINANCING
STATEMENT CONTAINING INCORRECT INFORMATION.**

(a) A security interest or agricultural lien perfected by a filed financing statement complying with Section 9-502(a) but containing information described in Section 9-515(b)(5) that is incorrect is subordinate to the rights of a holder of a perfected security interest in or [another purchaser] [a buyer] of the collateral to the extent that the secured party or [other purchaser] [buyer] gives value in reasonable reliance upon the incorrect information.

(b) A statutory lien, other than an agricultural lien, perfected by a filed financing statement complying with Section 9-502(a) but containing information described in Section 9-515(b)(5) that is incorrect is subordinate to the rights of a holder of a perfected security interest in the collateral to the extent that the secured party gives value in reasonable reliance upon the incorrect information.

Reporters' Comments

1. **Source.** New.

2. Effect of Incorrect Information in Financing Statement. Section 9-521(a) requires the filing office to reject financing statements that do not contain information concerning the debtor as specified in Section 9-515(b)(5). A error in this information does not render the financing statement ineffective. On rare occasions, a subsequent purchaser of the collateral (i.e., a buyer or secured party) may rely on the misinformation to its detriment. Subsection (a) of this section subordinates a security interest or agricultural lien perfected by an effective, but flawed, financing statement to the rights of a purchaser to the extent the purchaser gives value in reasonable reliance on the incorrect information. Subsection (b) contains a similar rule subordinating non-agricultural statutory liens, but, in keeping with the limited treatment of statutory liens under this Article, the subordination

1 rule is limited to competing security interests and does not apply to buyers. A
2 purchaser who has not made itself aware of the information in the filing office with
3 respect to the debtor cannot act in “reasonable reliance upon incorrect information.

4 **SECTION 9-336. PRIORITY SUBJECT TO SUBORDINATION.**

5 *[MINOR STYLE CHANGES ONLY]* Nothing in this article prevents
6 subordination by agreement by a person entitled to priority.

7 Reporters’ Comments

8 1. **Source.** Former Section 9-316.

9 2. **Status.** The Drafting Committee has not considered this section.

10 [SUBPART 4. RIGHTS OF DEPOSITARY INSTITUTION]

11 **SECTION 9-337. EFFECTIVENESS OF RIGHT OF RECOUPMENT**
12 **OR SET-OFF AGAINST DEPOSIT ACCOUNT.**

13 (a) Except as otherwise provided in subsection (c), a depositary institution
14 with which a deposit account is maintained may exercise against a secured party
15 that holds a security interest in the deposit account any right of recoupment or set-
16 off.

17 (b) Except as otherwise provided in subsection (c), the application of this
18 article to a security interest in a deposit account does not affect a right of
19 recoupment or set-off of the secured party as to a deposit account maintained with
20 the secured party.

21 (c) The exercise by a depositary institution of a set-off against a deposit
22 account is ineffective against a secured party that holds a security interest in the
23 deposit account which is perfected by control under Section 9-109(a)(3), if the set-
24 off is based on a claim against the debtor.

25 Reporters’ Comments

1 **Change from Prior Draft:** The addition to subsection (c) addresses cases
2 in which both the debtor and the secured party are indebted to the depository
3 institution. It makes clear that the rule in subsection (c) does not apply if the set-off
4 is based on a claim against the secured party.

5 1. **Source.** New. Subsection (b) is based on a nonuniform Illinois
6 amendment.

7 2. **Set-off versus Security Interest.** This section resolves the conflict
8 between a security interest in a deposit account and the depository institution's
9 rights of recoupment and set-off. It is an exception to the general exclusion of the
10 right of set-off from Article 9. See Section 9-112(c)(13). The issue has been the
11 subject of much dispute under former Article 9.

12 Subsection (a) states the general rule and provides that the depository bank
13 may effectively exercise rights of recoupment and set-off against the secured party.
14 Subsection (c) contains an exception: if the secured party has control under Section
15 9-109(a)(3) (i.e., if it has become the depository institution's customer), then any
16 setoff exercised by the depository institution against a debt owed by the debtor is
17 ineffective. The depository institution may, however, exercise its recoupment rights
18 effectively. This result is consistent with the priority rule in Section 9-325(4),
19 under which the security interest of a depository institution in a deposit account is
20 subordinate to that of a secured party that has control under Section 9-109(a)(3).

21 This section deals with rights of set-off and recoupment that a depository
22 institution may have under other law. It does not create a right of set-off or
23 recoupment, nor is it intended to override any limitations or restrictions that other
24 law imposes on the exercise of those rights.

25 3. **Deposit Evidenced by Instrument.** Under Section 9-102, a deposit
26 evidenced by an instrument (e.g., certain certificates of deposit) is not a "deposit
27 account. Accordingly, this section does not apply to the depository institution's
28 right to set off against such an account. If the instrument is an Article 3
29 "instrument and the secured party is a holder in due course (HDC), Section 9-328
30 makes clear that Article 3 governs, and the secured party would prevail. But if the
31 secured party is not a holder in due course, the result under former Article 9 is
32 uncertain: either the security interest prevails over the right of set-off under Section
33 9-201, or the secured party has the rights of any other non-HDC under Article 3 (in
34 which case it might or might not prevail, depending on whether the right of set-off
35 is a defense or claim in recoupment of the kind described in Section 3-305(a)(2) or
36 (3)). A similar uncertainty arises under current law if the Article 9 instrument is not
37 negotiable: either the secured party prevails over the right of set-off under Section
38 9-201, or the secured party has the rights of any other assignee under the common
39 law or any applicable statute. The Drafting Committee has yet to determine
40 whether to resolve these issues and, if so, how to do so.

41 4. **Preservation of Set-off Right.** Subsection (b) makes clear that a
42 depository institution may hold both a right of set-off against, and an Article 9
43 security interest in, the same deposit account. The subsection does not pertain to
44 accounts evidenced by an instrument (e.g., certain certificates of deposit), which are
45 excluded from the definition of "deposit accounts."

is liable to the holder of a security interest. Although the fact that a secured party has control over the deposit account and the manner by which control was achieved may be relevant to the imposition of liability, whatever rule applies generally when a bank pays out funds in which a third party has an interest should determine liability to a secured party. Often, this rule is found in a non-UCC adverse claim statute. If a rule were to be introduced into the UCC, Article 4, and not Article 9, would seem to be the proper location for it. Cf. Section 8-115 (securities intermediary not liable to adverse claimant).

5. Certificates of Deposit. This section does not address the obligations of depository institutions that issue instruments evidencing deposits (e.g., certain certificates of deposit).

**SECTION 9-339. DEPOSITORY INSTITUTION'S RIGHT TO REFUSE
TO ENTER INTO OR DISCLOSE EXISTENCE OF CONTROL**

AGREEMENT. This article does not require a depository institution to enter into an agreement of the type described in Section 9-109(a)(2) even if its customer so requests or directs. A depository institution that has entered into such an agreement is not required to confirm the existence of the agreement to another person unless requested to do so by its customer.

Reporters' Comments

1. **Source.** New. Derived from Section 8-106(g).

2. Protection for Depository Institution. This section protects depository institutions from the need to enter into agreements against their will and from the need to respond to inquiries from persons other than their customers.

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PART 4
RIGHTS OF THIRD PARTIES

Reporters' Prefatory Comment

Part 3, Subpart 3, deals with priorities. This part deals with several other issues affecting third parties (i.e., parties other than the debtor and the secured party). Under current law, there is some uncertainty as to which jurisdiction's law (usually, which jurisdiction's version of Article 9) applies to the matters that this part addresses. These matters are not governed by the laws specified in Part 3, Subpart 1, since the matters do not relate to perfection, the effect of perfection or nonperfection, or priority.

It would be odd if a designation of applicable law by a debtor and secured party were to control some of these matters. Consider an example that may arise under current law. Former Section 9-318(4) makes ineffective terms in certain contracts that restrict assignment of the right to payment under the contracts. Under California's nonuniform version of Article 9, security interests in most insurance policies are within the scope of the Article. Under New York's (and most States') version, security interests in insurance policies are excluded. If an insurance policy provides that it is governed by the law of New York, it would seem appropriate for New York's law to determine whether a term restricting assignment of the policy is effective. Since New York's Article 9 does not cover an assignment of the policy, New York's Section 9-318(4) would not appear to render ineffective the restriction on assignment. Now assume that the owner of the policy, a California resident, assigns it as security to a California bank, and the security agreement provides that it is governed by the law of California. Does California's Section 9-318(4) then render the restriction in the policy ineffective? We are inclined to think it should not, but the answer is uncertain.

To the extent that jurisdictions adopt identical versions of this part and the courts interpret it consistently, the inability to identify the applicable law may be inconsequential. To the extent that nonuniform amendments and inconsistent interpretations occur, however, determining the applicable law may be significant. We think it plausible to assume that some nonuniformity in the rules and applicability of Part 4 will persist as the new version of Article 9 is submitted to and adopted by the States.

Nevertheless, after considering the issue, the Drafting Committee decided not to attempt to fashion choice-of-law rules for the matters covered by this Part. It opted instead to leave courts completely free to determine the applicable law on a case-by-case basis in accordance with Section 1-105 and non-UCC principles.

SECTION 9-401. ALIENABILITY OF DEBTOR'S RIGHTS. A debtor's rights in collateral may be voluntarily or involuntarily transferred notwithstanding

1 any agreement [provision in the security agreement] prohibiting a transfer or
2 making a transfer a default.

3 Reporters' Comments

4 1. **Source.** Former Section 9-311.

5 2. **Negative Pledge Covenant.** The debtor may grant a security interest to
6 secure a debt in excess of the collateral's value and agree not to create subsequent
7 security interests in the collateral. In violation of [its agreement with the secured
8 party] [the security agreement], the debtor may purport to grant a subsequent
9 security interest. This section validates the subsequent (prohibited) security
10 interest, which might even achieve priority over the earlier security interest.

11 3. **Sale of Receivables.** If a debtor sells an account, chattel paper, or
12 payment intangible outright, as against the buyer the debtor may have no remaining
13 rights to transfer. If, however, the buyer fails to perfect its interest, then insofar as
14 the rights of third parties are concerned, the debtor retains its rights and title. See
15 Section 9-315A(b). The debtor has the power to convey these rights to a
16 subsequent purchaser. If the subsequent purchaser (buyer or secured lender)
17 perfects, it will achieve priority over the earlier, unperfected purchaser.

18 **SECTION 9-402. SECURED PARTY NOT OBLIGATED ON**
19 **CONTRACT OF DEBTOR.** The existence of a security interest, statutory lien, or
20 authority given to a debtor to dispose of or use collateral, without more, does not
21 impose contract or tort liability upon a secured party for the debtor's acts or
22 omissions.

23 Reporters' Comments

24 **Source.** Former Section 9-317, expanded to cover statutory liens.

25 **SECTION 9-403. AGREEMENT NOT TO ASSERT DEFENSES**
26 **AGAINST ASSIGNEE.**

27 (a) In this section, "value" has the meaning provided in Section 3-303(a).

28 (b) Except as otherwise provided in this section, an agreement between an
29 account debtor and an assignor not to assert against an assignee any claim or
30 defense that the account debtor may have against the assignor is enforceable by an
31 assignee that takes an assignment:

- 1 (1) for value;
- 2 (2) in good faith;
- 3 (3) without notice of a claim of a property or possessory right to the
- 4 property assigned; and
- 5 (4) without notice of a defense or claim in recoupment of the type that
- 6 may be asserted against a person entitled to enforce a negotiable instrument under
- 7 Section 3-305(a).
- 8 (c) An agreement described in subsection (b) is not enforceable with
- 9 respect to defenses of a type that may be asserted against a holder in due course of a
- 10 negotiable instrument under Section 3-305(b).
- 11 (d) This section is subject to other law that establishes a different rule for
- 12 an account debtor who is an individual and who incurred the obligation primarily
- 13 for personal, family, or household purposes.
- 14 (e) This section does not displace other law that gives effect to an
- 15 agreement by an account debtor not to assert a claim or defense against an assignee.

16 Reporters' Comments

17 1. **Source.** Former Section 9-206.

18 2. **Scope.** This section has been expanded to apply to all account debtors,

19 not just those who buy or lease goods.

20 3. **Relationship to Article 3.** Former Section 9-206(1) was designed to

21 treat certain assignees of receivables like holders in due course of negotiable

22 instruments. It left open certain issues, e.g., whether the section incorporates the

23 special Article 3 definition of "value" in Section 3-303 or the generally applicable

24 definition in Section 1-201(44). In 1990, the definition of "holder in due course

25 (Section 3-302) and the articulation of the rights of a holder in due course (Sections

26 3-305 and 3-306) were revised substantially. This section has been reformulated to

27 track more closely the rules of Sections 3-302, 3-305, and 3-306.

28 This section applies only to the obligations of an "account debtor," as

29 defined in Section 9-102. Thus, it does not determine the circumstances under

30 which and the extent to which a person who is obligated on a negotiable instrument

31 is disabled from asserting claims and defenses. Rather, Article 3 must be

32 consulted. See, e.g., Sections 3-305; 3-306. Article 3 governs even when the

33 negotiable instrument constitutes part of chattel paper. See Section 9-102 (an

obligor on a negotiable instrument constituting part of chattel paper is not an “account debtor”).

4. Relationship to Terms of Assigned Property. Former Section 9-206(2), concerning warranties accompanying the sale of goods, has been deleted as unnecessary. This Article does not regulate the terms of the account, chattel paper, or general intangible that is assigned, except insofar as the account, chattel paper, or general intangible itself creates a security interest (as often is the case with chattel paper). Thus, Article 2, and not this Article, determines whether a seller of goods makes or effectively disclaims warranties, even if the sale is secured. Similarly, other law, and not this Article, determines the effectiveness of an account debtor’s undertaking to pay notwithstanding, and not to asset, any defenses or claims against an assignor—e.g., a “hell or high water” provision in the underlying agreement that is assigned. If other law gives effect to this undertaking, then, under principles of *nemo dat*, it would be enforceable by the assignee (secured party). If other law prevents the assignor from enforcing the undertaking, this section nevertheless might permit the assignee to do so. The right of the assignee to enforce would depend upon whether, under the particular facts, the account debtor’s undertaking fairly could be construed as an agreement that falls within the scope of this section and whether the assignee meets the requirements of this section.

5. Relationship to Other Law. The reference to “other law,” in subsection (d) encompasses administrative rules and regulations; the reference it replaces (“statute or decision”) arguably would not. However, because Federal Trade Commission Rule 433 (the so-called “anti-holder-in-due-course” rule) requires creditors to preserve defenses by including a notice in the agreement between the assignor and the account debtor, and does not directly render waiver-of-defense agreements ineffective, Section 9-403 may not be “subject to” the FTC rule within the meaning of subsection (d). Regardless, a creditor taking an assignment with knowledge that the documentation does not comply with the FTC rule would not be in good faith and would not qualify for protection under subsection (b).

This section does not displace other law that gives effect to a non-consumer account debtor’s agreement not to assert defenses against an assignee, even if the agreement would not qualify under subsection (b). See subsection (e).

This section also does not displace other law to the extent that the other law permits an assignee who takes an assignment with notice of a claim of a property or possessory right, a defense, or a claim in recoupment to enforce an agreement not to assert claims and defenses against the assignor. This section also does not displace an assignee’s right to assert that an account debtor is estopped from asserting a claim or defense. Nor does this section displace other law with respect to waivers of potential future claims and defenses that are the subject of an agreement between the account debtor and the assignee. Finally, this section does not displace Section 1-107, concerning waiver of a breach that allegedly already has occurred.

1 **SECTION 9-404. RIGHTS ACQUIRED BY ASSIGNEE; DEFENSES**
2 **AGAINST ASSIGNEE; MODIFICATION OF CONTRACT; DISCHARGE**
3 **OF ACCOUNT DEBTOR; NOTIFICATION OF ASSIGNMENT;**
4 **IDENTIFICATION AND PROOF OF ASSIGNMENT; TERM**
5 **PROHIBITING ASSIGNMENT INEFFECTIVE.**

6 (a) Unless an account debtor has made an enforceable agreement not to
7 assert defenses or claims, and subject to subsections (b) and (i), the rights of an
8 assignee are subject to:

9 (1) all the terms of the agreement between the account debtor and
10 assignor and any defense or claim in recoupment arising from the transaction that
11 gave rise to the contract; and

12 (2) any other defense or claim of the account debtor against the assignor
13 which accrues before the account debtor receives a notification of the assignment
14 authenticated by the assignor or the assignee.

15 (b) Subject to subsection (i), the claim of an account debtor may be asserted
16 against an assignee under subsection (a) only to reduce the amount owing or for the
17 assignee's fraud.

18 (c) (1) Subject to subsection (i), this subsection applies to the extent that:

19 (A) the right to payment or a part thereof under an assigned contract
20 has not been fully earned by performance; or

21 (B) to the extent that the right to payment or a part thereof has been
22 fully earned by performance and the account debtor has not received notification of
23 the assignment under subsection (d).

24 (2) A any modification of or substitution for the contract is effective
25 against an assignee if made in good faith and in accordance with reasonable

1 commercial standards is ~~effective against an assignee unless the account debtor has~~
2 ~~otherwise agreed.~~

3 (3) ~~The~~ the assignee acquires corresponding rights under the modified
4 or substituted contract.

5 (4) The assignment may provide that the modification or substitution is
6 a breach of contract by the assignor.

7 (d) (1) Subject to subsections (e), (f), (g), and (i), an account debtor on an
8 account, chattel paper, [instrument other than a negotiable instrument,] or payment
9 intangible may discharge its obligation by paying the assignor until, but not after,
10 the account debtor receives a notification, authenticated by the assignor or the
11 assignee, that the amount due or to become due has been assigned and that payment
12 is to be made to the assignee.

13 (2) After receipt of the notification, the account debtor may discharge
14 its obligation by paying the assignee and may not discharge the obligation by
15 paying the assignor.

16 (e) Subject to subsection (i), a notification is ineffective under subsection
17 (d):

18 (1) if it does not reasonably identify the rights assigned;

19 (2) to the extent that an agreement between an account debtor and a
20 seller of a payment intangible limits the account debtor's duty to pay a person other
21 than the seller and the limitation is effective under other law; or

22 (3) at the option of an account debtor, if the notification notifies the
23 account debtor to make less than the full amount of any installment or other
24 periodic payment to the assignee, regardless of whether:

25 (A) only a portion of the account, chattel paper, or general intangible
26 has been assigned to that assignee;

1 (B) a portion has been assigned to another assignee; or
2 (C) the account debtor knows that the assignment to that assignee is
3 limited.

4 (f) Subject to subsection (i), if requested by the account debtor, the assignee
5 must seasonably furnish reasonable proof that the assignment has been made.
6 Unless the assignee complies, the account debtor may discharge its obligation by
7 paying the assignor even if the account debtor has received [an effective] [a]
8 notification under subsection (d).

9 (g) (1) Except as otherwise provided in Sections 2A-303 and 9-405, and
10 subject to subsection (i), a term in an agreement between an account debtor and an
11 assignor is ineffective if it prohibits, restricts, or requires the account debtor's
12 consent to the assignment or transfer of or the creation, attachment, or perfection of
13 a security interest in an account, chattel paper, or payment intangible.

14 (2) This subsection does not apply to the sale of a payment intangible.

15 (h) [Subject to subsection (i), an] [An] account debtor may not waive or
16 vary its option under subsection (e)(3).

17 (i) This section is subject to other law that establishes a different rule for an
18 account debtor who is an individual and who incurred the obligation primarily for
19 personal, family, or household purposes.

20 Reporters' Comments

21 **Discussion Question:** Should the draft or comments clarify the
22 consequences of an account debtor's paying an assignee (i) who notified the
23 account debtor in violation of an agreement with the assignor, or (ii) who bought an
24 account in which the debtor had no interest? The latter situation would arise if the
25 debtor sells an account to X, who perfects a security interest in the account before
26 the debtor sells the account to Y. See Comment 9 below.

27 1. **Source.** Former Section 9-318.

28 2. **Rights of Assignee.** Subsection (a) has been revised to reflect that
29 waiver-of-defense clauses under Section 9-206 are not limited to sales and leases
30 and to track Section 3-305(a)(3) more closely.

1 New subsection (b) limits the claim that the account debtor may assert
2 against an assignee. Borrowing from Section 3-305(a)(3) and cases construing
3 former Section 9-318, subsection (b) generally does not afford the account debtor
4 the right to an affirmative recovery from an assignee. Although most claims may
5 be asserted against an assignee only to reduce the amount owing, the account debtor
6 may assert an affirmative claim based on the assignee's fraud.

7 New subsection (i) makes clear that the rules of this section are subject to
8 other law establishing special rules for consumer account debtors.

9 **3. Application to "Account Debtor."** This section deals only with the
10 rights and duties of "account debtors –and for the most part only with account
11 debtors on accounts, chattel paper, and payment intangibles. Neither this section
12 nor any other provision of this Article, including Sections 9-406 and 9-406A,
13 provides analogous regulation of the rights and duties of other obligors on
14 collateral, such as the maker of a negotiable instrument (governed by Article 3), the
15 issuer of or nominated person under a letter of credit (governed by Article 5), or the
16 issuer of a security (governed by Article 8). Article 9 leaves those rights and duties
17 untouched; however, Section 9-406A deals with the special case of letters of credit.
18 When chattel paper is composed in part of a negotiable instrument, the obligor on
19 the instrument is not an "account debtor," and Article 3 governs the rights of the
20 assignee of the chattel paper with respect to the issues this section addresses. See,
21 e.g., Section 3-601 (dealing with discharge of an obligation to pay a negotiable
22 instrument). However, bracketed language in the definition of "account debtor" in
23 Section 9-102 would make it clear that an obligor on a non-negotiable instrument is
24 an account debtor; accordingly, this section would be applicable to such an obligor.
25 The Drafting Committee has not yet discussed that issue.

26 References in this section to an "account debtor" include account debtors on
27 collateral that is proceeds.

28 **4. Modification of Assigned Contract.** Subsection (c) changes former
29 Section 9-318(2) by providing that good faith modifications are binding against an
30 assignee except to the extent that the right to payment has been earned and
31 notification has not been given to the account debtor.

32 **5. Account Debtor's Right to Pay.** Subsection (d) provides the general
33 rule concerning an account debtor's right to pay the assignor until the account
34 debtor receives appropriate notification. The revision makes clear that once the
35 account debtor receives the notification, the account debtor cannot discharge its
36 obligation by paying the assignor. It also makes explicit that payment to the
37 assignor before notification, or payment to the assignee after notification,
38 discharges the obligation. No change in meaning from former Section 9-318 is
39 intended.

40 Subsection (d) also has been revised to apply only to account debtors on
41 accounts, chattel paper, and payment intangibles. (The term "account debtor" is
42 defined in Section 9-102 to include those obligated on all general intangibles.)
43 Although this revision renders subsection (d) more precise, it probably does not
44 change the law. Former Section 9-318(3) refers to the account debtor's obligation

1 to “pay, thereby suggesting that the subsection is limited to account debtors on
2 accounts, chattel paper, and other payment obligations.

3 The bracketed phrase in subsection (d) raises the issue whether this
4 subsection should govern the rights and obligations of an obligor on a non-
5 negotiable instrument. Today, these rights and obligations are governed by
6 common law. Some observers believe that the “notification” rule of subsection (d)
7 is preferable to the traditional common-law “merger” rule, under which the
8 obligation to pay runs to the person in possession of an indispensable instrument.
9 The “merger” rule may have particularly undesirable effects in the case of a real
10 property mortgagor who pays the full amount of the mortgage note to the
11 mortgagee, only to discover that the obligation was not discharged because the note
12 and mortgage had been assigned and delivered to the assignee prior to payment. On
13 the other hand, creating a rule for assignees under Article 9 that may differ from the
14 rule applicable to non-Article 9 assignees (e.g., buyers of non-negotiable notes),
15 carries with it the potential for mischief.

16 Nothing in this section conditions the effectiveness of a notification on the
17 identity of the person who gives it. An account debtor that doubts whether the right
18 to payment has been assigned may avail itself of the procedures in subsection (f).

19 **6. Limitations on Effectiveness of Notification.** This section contains
20 three special rules concerning the effectiveness of a notification under subsection
21 (d).

22 Subsection (e)(1) tracks former Section 9-318(3) and makes ineffective a
23 notification that does not reasonably identify the rights assigned. A reasonable
24 identification need not identify the account with specificity.

25 Subsection (e)(2), which is new, applies only to sales of payment
26 intangibles. It makes a notification ineffective to the extent that other law gives
27 effect to an agreement between an account debtor and a seller of a payment
28 intangible that limits the account debtor’s duty to pay a person other than the seller.
29 Payment intangibles are substantially less fungible than accounts and chattel paper.
30 In some (e.g., commercial bank loans), account debtors customarily and
31 legitimately expect that they will not be required to pay any person other than the
32 financial institution that has advanced funds.

33 It has become common in financing transactions to assign interests in a
34 single obligation to more than one assignee. Requiring an account debtor that owes
35 a single obligation to make multiple payments to multiple assignees would be
36 unnecessarily burdensome. Thus, under subsection (e)(3), an account debtor that is
37 notified to pay an assignee less than the full amount of any installment or other
38 periodic payment has the option to treat the notification as ineffective, ignore the
39 notice, and discharge the assigned obligation by paying the assignor. Some account
40 debtors may not realize that the law affords them the right to ignore certain notices
41 of assignment with impunity. By making the notification ineffective at the account
42 debtor’s option, subsection (e)(3) permits an account debtor to pay the assignee in
43 accordance with the notice and thereby to satisfy its obligation *pro tanto*. Under
44 subsection (h), the rights and duties created by subsection (e)(3) cannot be waived
45 or varied.

1 **7. Proof of Assignment.** Subsection (f) links payment with discharge, as
2 in subsection (d). It follows former Section 9-318(3) in referring to the right of the
3 account debtor to pay the assignor if the requested proof of assignment is not
4 seasonably forthcoming. Arguably, the notification of assignment would remain
5 effective, so that, in the absence of reasonable proof of the assignment, the account
6 debtor could discharge the obligation by paying either the assignee or the assignor.
7 Of course, if no assignment was in fact made, the putative assignee has no right to
8 payment under any circumstances, and the account debtor cannot discharge the
9 obligation by paying the putative assignee. If no assignment was made, the quality
10 of the notice or the “proof” of assignment are irrelevant.

11 An account debtor may face another problem if its obligation becomes due
12 while the account debtor is awaiting reasonable proof of the assignment that it has
13 requested from the assignee. This section does not excuse the account debtor from
14 timely compliance with its obligations. Consequently, an account debtor may
15 discharge its obligation by paying the assignor when payment is due, even if the
16 account debtor has not yet received a response to its request for proof of the
17 assignment. On the other hand, after requesting reasonable proof of the assignment,
18 an account debtor may not discharge its obligation by paying the assignor before
19 payment is due unless the assignee has failed to provide the proof seasonably.

20 **8. Restrictions on Assignment.** Former subsection (4) renders ineffective
21 an agreement between an account debtor and an assignor that prohibits assignment
22 of an account (whether outright or for collateral purposes) or prohibits a security
23 assignment of a general intangible for the payment of money due or to become due.
24 Subsection (g) essentially follows former Section 9-318(4), but expands the rule of
25 free assignability to chattel paper (subject to Sections 2A-303 and 9-405), and
26 explicitly overrides restrictions on assignability as well as prohibitions.

27 Former Section 9-318(4) does not apply to sales of payment intangibles but
28 does apply to assignments for security. Subsection (g) continues this approach.
29 Section 9-406 addresses anti-assignment clauses with respect to sales of payment
30 intangibles.

31 Like former subsection (4), subsection (g) provides that anti-assignment
32 clauses are “ineffective. The quoted term means that the clause is of no effect
33 whatsoever; it does not prevent the assignment from taking effect between the
34 parties, nor does the prohibited assignment constitute a default under the agreement
35 between the account debtor and assignor.

36 **9. Multiple Assignments.** The section remains silent concerning multiple
37 assignments. The Official Comments might refer to applicable non-UCC rules.

38 **SECTION 9-405. RESTRICTIONS ON CREATION OR**
39 **ENFORCEMENT OF SECURITY INTEREST IN LEASEHOLD INTEREST**
40 **OR IN LESSOR’S RESIDUAL INTEREST.**

1 (a) In this section, "creation of a security interest" includes the sale of a
2 lease contract that is subject to this article.

3 (b) (1) Except as otherwise provided in subsection (c), a provision in a
4 lease agreement is not enforceable if it:

5 (A) ~~which~~ prohibits the creation or enforcement of a security interest
6 in an interest of a party under the lease contract or in the lessor's residual interest in
7 the goods; or

8 (B) ~~which~~ makes such a transfer an event of default, ~~is not~~
9 ~~enforceable unless, and then only.~~

10 (c) A lease provision described in subsection (b) is enforceable to the extent
11 that there is:

12 (1) a transfer by the lessee of the lessee's right of possession or use of
13 the goods in violation of the provision; or

14 (2) a delegation of a material performance of either party to the lease
15 contract in violation of the provision.

16 (d) (1) Except as otherwise provided in paragraph (2), neither ~~Neither~~ the
17 granting nor the enforcement of a security interest in the lessor's interest under the
18 lease contract or the lessor's residual interest in the goods is a transfer that
19 materially impairs the prospect of obtaining return performance by, materially
20 changes the duty of, or materially increases the burden or risk imposed on, the
21 lessee within Section 2A-303(5).

22 (2) This subsection does not apply ~~unless, and then only~~ to the extent
23 that, there is a delegation of a material performance of the lessor.

24 Reporters' Comments

25 1. **Source.** Section 2A-303.

26 2. **Status.** Inasmuch as these provisions deal explicitly with the creation of
27 a security interest, some people think they belong in Article 9. Others disagree and

1 would keep the provisions in Article 2A. We expect that both Drafting Committees
2 will consider the issue. In any event, it is likely that some revision of these
3 provisions will be appropriate.

4 **SECTION 9-406. RESTRICTIONS ON ASSIGNMENT OF CERTAIN**
5 **GENERAL INTANGIBLES INEFFECTIVE.**

6 (a) (1) A term in a general intangible, including a contract, permit, license,
7 or franchise, between an account debtor and a debtor which prohibits, restricts, or
8 requires the account debtor's consent to the assignment or transfer of or creation,
9 attachment, or perfection of a security interest in the general intangible, is
10 ineffective to the extent that:

11 (A) the term would impair the creation, attachment, or perfection of
12 a security interest; or

13 (B) the creation, attachment, or perfection of the security interest
14 would cause a default, breach, right of recoupment, claim, defense, termination,
15 right of termination, or remedy under the general intangible.

16 (2 ~~b~~) This subsection ~~Subsection (a)~~ applies to a security interest in a
17 payment intangible only if the security interest arises out of a sale of the payment
18 intangible.

19 (~~b~~ e) A provision in a statute or governmental rule or regulation that
20 prohibits, restricts, or requires the consent of a government or governmental body
21 or official to the assignment or transfer of or creation of a security interest in a
22 general intangible, including a contract, permit, license, or franchise, between an
23 account debtor and a debtor is ineffective to the extent that:

24 (1) the term would impair the creation, attachment, or perfection of a
25 security interest; or

(2) the creation, attachment, or perfection of the security interest would cause a default, breach, claim, defense, termination, right of termination, or remedy under the general intangible.

(d) To the extent that a term in a general intangible, or provision in a statute, rule, or regulation, is ineffective under subsection (a) or (c) but is effective under other law, the creation, attachment, or perfection of a security interest in the general intangible:

(1) is not enforceable against the account debtor;

(2) imposes no duties or obligations on the account debtor; and

(3) does not require the account debtor to recognize the security interest, pay or render performance to the secured party, or accept payment or performance from the secured party.

(e) This section prevails over any inconsistent provisions of the following statutes, rules, and regulations:

[List here any statutes, rules, and regulations containing provisions inconsistent with this section.]

Reporters' Comments

1. **Source.** New.

2. **Free Assignability.** This section makes ineffective any attempt to restrict assignment of a general intangible, whether the restriction appears in the terms of the general intangible (subsection (a)) or in a statute, rule, or regulation (subsection (c)). The principal goal is to protect the creation, attachment, and perfection of a security interest (including a sale of a payment intangible) while preventing these events from giving rise to a default or breach by the assignor or from triggering a remedy of the account debtor, all in the interest of enhancing the ability of certain debtors to obtain credit. On the other hand, subsection (d) protects the other party obligated to perform (the “account debtor”) from any adverse effects of the security interest. It leaves the account debtor’s rights and obligations unaffected if a restriction rendered ineffective by subsection (a) or (c) would be effective under other law.

3. **Terminology: “Account Debtor.”** This section uses the term “account debtor” to refer to the party other than the debtor to a general intangible such as a permit, franchise, or the like. In many cases the principal payment obligation under a general intangible may be a obligation to pay *by* the debtor *to* the account debtor.

1 But the definition of “account debtor” in Section 9-102 does not limit the term to
2 persons who are obligated to *pay* under a general intangible. Because the other
3 party to a general intangible may not have affirmative executory duties or
4 obligations, it has been suggested that another term be used. Alternatively, the
5 Drafting Committee may wish to consider whether the definition of “account
6 debtor” should be expanded to include “a person, other than the debtor, that is a
7 party to a general intangible.

8 **4. Scope: Sales of Payment Intangibles and Other General Intangibles.**

9 This section applies to a security interest in payment intangibles only if the security
10 interest arises out of sale of the payment intangibles. Security interests in payment
11 intangibles that secure an obligation are subject to the even broader anti-assignment
12 rule in Section 9-404(g).

13 This section does not render ineffective any term that restricts outright sales
14 of general intangibles other than payment intangibles. It deals only with restrictions
15 on security interests. The only sales of general intangibles that create security
16 interests are sales of payment intangibles.

17 **5. Effect in Assignor’s Bankruptcy.** This section is likely to have a
18 substantial effect if the assignor enters bankruptcy. Roughly speaking, Bankruptcy
19 Code § 552 invalidates security interests in property acquired after a bankruptcy
20 petition is filed, except to the extent that the post-petition property constitutes
21 proceeds of pre-petition collateral. Consider the owner of a cable television
22 franchise that, under applicable law, cannot be assigned without the consent of the
23 municipal franchisor. a lender wishes to extend credit to the franchisee, secured by
24 the debtor’s “going business” value. To secure the loan, the debtor grants a security
25 interest in all its existing and after-acquired property. The franchise represents the
26 principal value of the business. The municipality refuses to consent to any
27 assignment for collateral purposes. As a consequence, by virtue of other law, the
28 security interest in the franchise does not attach. If the debtor enters bankruptcy
29 and sells the business, the secured party will receive but a fraction of the business’s
30 value. Under this section, however, the security interest would attach to the
31 franchise. As a result, the security interest would attach to the proceeds of any sale
32 of the franchise during bankruptcy. This section would protect the interests of the
33 municipality, by preventing the secured party from enforcing its security interest to
34 the detriment of the municipality.

35 **6. Contrary Federal Law.** This section does not override federal law to
36 the contrary.

37 **SECTION 9-406A. RESTRICTIONS ON ASSIGNMENT OF LETTERS**
38 **OF CREDIT INEFFECTIVE.**

39 (a) A term in a letter of credit or a rule of law, custom, or practice
40 applicable to the letter of credit that prohibits, restricts, or requires the consent of an
41 applicant, issuer, or nominated person to a beneficiary's assignment of or creation

1 of a security interest in ~~the letter-of-credit~~ rights ~~or proceeds of the letter of credit~~ is
2 ineffective to the extent that:

3 (1) the term or rule of law, custom, or practice would impair the
4 creation, attachment, or perfection of a security interest in the letter-of-credit rights
5 ~~or proceeds of the letter of credit~~; or

6 (2) the creation, attachment, or perfection of the security interest would
7 cause a default, breach, claim, defense, termination, right of termination, or remedy
8 under the letter-of-credit rights ~~or proceeds of the letter of credit~~.

9 (b) To the extent that a provision in a letter of credit is ineffective under
10 subsection (a) but is effective under Article 5, other law, or a rule of custom or
11 practice applicable to the letter of credit, to the transfer of a right to draw or
12 otherwise demand performance under the letter of credit, or to the assignment of a
13 right to proceeds of the letter of credit, the creation, attachment, or perfection of a
14 security interest in the letter-of-credit rights ~~or the proceeds of the letter of credit~~:

15 (1) is not enforceable against the applicant, issuer, nominated person, or
16 transferee beneficiary;

17 (2) imposes no duties or obligations on the applicant, issuer, nominated
18 person, or transferee beneficiary; and

19 (3) does not require the applicant, issuer, nominated person, or
20 transferee beneficiary to recognize the security interest, pay or render performance
21 to the secured party, or accept payment or other performance from the secured
22 party.

23 Reporters' Comments

24 1. **Source.** Former Section 9-318.

25 2. **Purpose and Relevance.** This section, patterned on Section 9-406, limits
26 the effectiveness of any attempt to restrict the creation, attachment, or perfection of
27 a security interest in letter-of-credit rights, whether the restriction appears in the

1 letter of credit or a rule of law, custom, or practice applicable to the letter of credit.
2 It is intended to be consistent with Article 5.

3 The principal goal of subsection (a) is to protect the creation, attachment, and
4 perfection of a security interest while preventing these events from giving rise to a
5 default or breach by the assignor or from triggering a remedy or defense of the
6 issuer or other person obligated on a letter of credit. On the other hand, subsection
7 (b) protects the issuer and other parties from any adverse effects of the security
8 interest. It explicitly preserves the “independence principle” of letter-of-credit law
9 by leaving unaffected the rights and obligations of issuers, nominated persons, and
10 transferee beneficiaries if a restriction rendered ineffective by subsection (a) would
11 be effective under other law.

12 Letter-of-credit rights are a type of support obligation. See Section 9-102.
13 Under Sections 9-203 and 9-308, a security interest in a support obligation attaches
14 and is perfected automatically if the security interest in the supported obligation
15 attaches and is perfected. See Section 9-110, Comment 5. It may be anomalous, or
16 at least misleading, to provide for automatic attachment and perfection in Article 9
17 if, under other law (e.g., Article 5), a restriction on transfer or assignment is
18 effective to block attachment. This section makes it clear that restrictions on an
19 assignment of a letter of credit are ineffective to prevent attachment and perfection,
20 but preserves letter-of-credit law and practice limiting the right of a beneficiary to
21 transfer its right to draw or otherwise demand performance (Section 5-112) and
22 limiting the obligation of an issuer or nominated person to recognize a beneficiary’s
23 assignment of letter-of-credit proceeds (Section 5-114). Thus, this section’s
24 treatment of letter-of-credit rights differs from that of instruments and investment
25 property.

1 **PART 5**

2 **FILING**

3 [SUBPART 1. FILING OFFICE; CONTENTS AND
4 EFFECTIVENESS OF FINANCING STATEMENT]

5 **SECTION 9-501. FILING OFFICE.**

6 (a) Except as otherwise provided in subsection (b), if ~~If~~ the law of this State
7 governs perfection of a security interest or statutory lien, the office with which to
8 file a financing statement to perfect the security interest or statutory lien is:

9 (1) the office designated for the filing or recording of a mortgage on the
10 real property, if:

11 (A) the collateral is timber to be cut or as-extracted collateral; or

12 (B) the financing statement is filed as a fixture filing and the
13 collateral is goods that are or are to become fixtures; [and]

14 [(2) the office of the debtor's registered agent, if the debtor has
15 designated a registered agent under Section 9-525; and]

16 (3) the office of [] [or any office duly authorized by []] in all other
17 cases, including if the goods are or are to become fixtures and the financing
18 statement is not filed as a fixture filing.

19 (b) The office with which to file a financing statement to perfect a security
20 interest or statutory lien in collateral, including fixtures, of a transmitting utility is
21 the office of []. The ~~This~~ financing statement [also] constitutes a fixture filing as
22 to the collateral indicated in the financing statement which is or is to become
23 fixtures.

24 *Legislative Note: The State should designate the filing office where the brackets*
25 *appear. The filing office may be that of a governmental official (e.g., the Secretary*
26 *of State) or a private party that maintains the State's filing system (see Section*
27 *9-526).*

Reporters' Comments

1. **Source.** Former Section 9-401, revised as indicated below.

2. **Where to File.** Subsection (a) indicates where in a given State a financing statement is to be filed. Former Article 9 affords each State three alternative approaches, depending on the extent to which the State desires central filing (usually with the Secretary of State), local filing (usually with a county office), or both. Local filing increases the net costs of secured transactions by increasing uncertainty and the number of required filings. Any benefit that local filing may have had in the 1950's (e.g., ease of access to local creditors) is now insubstantial. Accordingly, this Article dictates central filing for most situations, while retaining local filing for real-estate-related collateral and special filing provisions for transmitting utilities. (The Drafting Committee has yet to consider whether the current definition of "transmitting utility" is adequate.)

3. **Minerals and Timber.** Under subsection (a)(1), a filing with the office where a mortgage on the relevant real property would be filed will perfect a security interest in as-extracted collateral. Inasmuch as the security interest does not attach until extraction, the filing continues to be effective after extraction. A different result occurs with respect to timber to be cut, however. Unlike as-extracted collateral, standing timber may be goods before it is cut. See Section 9-102 (defining "goods"). Once cut, however, it is no longer timber *to be* cut, and the filing in the real property mortgage office ceases to be effective. The timber then becomes ordinary goods, and filing in the office specified in subsection (a)(3) is necessary for perfection. Note also that after the timber is cut the law of the debtor's location, not the location of the timber, governs perfection under Section 9-301.

4. **Registered Agent.** The Reporters distributed to the Drafting Committee a proposal under which a State would permit each debtor to select a "registered agent" to maintain financing statements and other Article 9 records pertaining to the debtor. Subsection (a)(2) provides for filing with such a registered agent, should the Drafting Committee elect to pursue this proposal.

**SECTION 9-502. CONTENTS OF FINANCING STATEMENT;
MORTGAGE AS FINANCING STATEMENT; TIME OF FILING
FINANCING STATEMENT.**

(a) Subject to subsection (b), a ~~A~~ financing statement is sufficient only if it:

(1) provides the name of the debtor and the name and mailing address of the secured party or a representative of the secured party; and

(2) indicates the collateral covered by the financing statement.

(b) (1) This subsection applies to a financing statement that:

1 (A) ~~If the financing statement~~ covers timber to be cut or as-extracted
2 collateral; or

3 (B) ~~the financing statement~~ is filed as a fixture filing and the
4 collateral is goods that are or are to become fixtures.

5 (2) Except as otherwise provided in Section 9-501(b), to be sufficient,
6 the financing statement also must:

7 (A) indicate that it covers this type of collateral;

8 (B) indicate that it is to be filed [for record] in the real property
9 records;

10 (C) provide a description of the real property [sufficient if it were
11 contained in a mortgage of the real property to give constructive notice of the
12 mortgage under the law of this State]; and

13 (D) if the debtor does not have an interest of record in the real
14 property, provide the name of a record owner.

15 *Legislative Note: Language in brackets is optional. Where the State has any*
16 *special recording system for real property other than the usual grantor-grantee*
17 *index (as, for instance, a tract system or a title registration or Torrens system)*
18 *local adaptations of subsection (b) and Section 9-520(b) may be necessary. See,*
19 *e.g., Mass. Gen. Laws Chapter 106, Section 9-410.*

20 (c ~~b~~) If a financing statement ~~states~~ indicates that it is filed in connection
21 with a [public finance transaction] [or] [manufactured home transaction], it also
22 may indicate that its period of effectiveness is [10, 20, or 30] years after the date of
23 filing.

24 (d ~~e~~) A real property mortgage is effective from the date of recording as a
25 financing statement filed as a fixture filing or as a financing statement covering
26 [timber to be cut or] as-extracted collateral only if:

27 (1) the mortgage indicates the goods or accounts that it covers;

28 **~~Paragraph 2—Alternative A~~**

1 ~~(2) (A) the goods are or are to become fixtures related to the real~~
2 ~~property described in the mortgage;~~

3 ~~(B) the goods are minerals [related to] [located in/on] the real~~
4 ~~property described in the mortgage; or~~

5 ~~(C) the accounts arise from the sale of minerals [related to] [located~~
6 ~~in/on] the real property described in the mortgage;~~

7 **Paragraph 2—Alternative B**

8 (2) (A) the goods are or are to become fixtures related to the real
9 property described in the mortgage; or

10 (B) the collateral is as-extracted collateral related to the real property
11 described in the mortgage;

12 (3) the mortgage complies with the requirements for a financing
13 statement in this section other than an indication that it is to be filed in the real
14 property records; and

15 (4) the mortgage is [duly] recorded.

16 (e ~~d~~) A financing statement may be filed before a security agreement is
17 made or a security interest otherwise attaches.

18 Reporters' Comments

19 1. **Source.** Former Section 9-402(1), (5), (6).

20 2. **Debtor's Signature; Required Authorization.** Subsection (a) omits
21 the requirement that the debtor sign a financing statement. As PEB Commentary
22 No. 15 indicates, a paperless financing statement may be filed electronically under
23 existing law. Nevertheless, the elimination of the signature requirement facilitates
24 paperless filing. Elimination of the debtor's signature requirement makes the
25 exceptions provided by former Section 9-402(2) unnecessary.

26 The fact that this Article does not require that an authenticating symbol be
27 contained in the public record does not mean that all filings are authorized. To the
28 contrary, this Article contains several provisions designed to insure that only
29 authorized records are filed. Section 9-508(a) entitles a person to file an initial
30 financing statement or an amendment that adds collateral only if the debtor
31 authorizes the filing, and Section 9-624(d) provides a remedy for unauthorized

1 filings. Of course, a filing has legal effect only to the extent it is authorized. See
2 Section 9-508A.

3 Making an unauthorized filing may give rise to civil or criminal liability under
4 other law. In addition, this Article contains provisions that assist in the discovery
5 of unauthorized filings and the amelioration of their practical effect. For example,
6 Section 9-520(a)(5) requires the filing office to communicate the information in
7 each filed record to every debtor and secured party that might be affected. In
8 addition, Section 9-519 provides a procedure whereby a person may add to the
9 public record a statement to the effect that a financing statement indexed under the
10 person's name was wrongfully filed, and Section 9-508(c) entitles any person to file
11 a termination statement if the secured party of record fails to comply with its
12 obligation to file or send one to the debtor.

13 **3. Certain Other Requirements.** This section deletes other formerly
14 required information because it seems unwise (real property description for
15 financing statements covering crops), unnecessary (adequacy of copies of financing
16 statements, address of debtor), or both (copy of security agreement as financing
17 statement). Inasmuch as a secured party owes no obligation to disclose information
18 concerning the security interest to third parties, the address requirement now refers
19 to "a mailing address" for the secured party. Although a mailing address for the
20 debtor no longer is required as a condition of effectiveness, the filing office must
21 reject a financing statement that does not provide that information. See Sections
22 9-521(a); 9-515(b)(5)(A).

23 **4. Public Finance Transactions; Manufactured Home Transactions.**
24 The normal 5-year period of effectiveness is inapplicable to public finance
25 transactions and manufactured home transactions. See Section 9-516 and the
26 Comments thereto. Subsection (b) permits a financing statement filed in
27 connection with a transaction of either kind to indicate its period of effectiveness.
28 The Drafting Committee has yet to consider the specifics of this subsection.

29 **5. Real-Property-Related Filings.** Subsection (b) contains the
30 requirements for fixture filings and financing statements covering timber, minerals,
31 and certain accounts. Subsection (d) explains when a real property mortgage is
32 effective as a fixture filing or to cover [timber to be cut or] minerals and minerals-
33 related accounts constituting as-extracted collateral. The changes relating to
34 minerals and accounts in subsections (a) and (d) primarily respond to
35 recommendations of the ABA Oil and Gas Task Force.

36 In some cases it may be difficult to determine whether goods are or will
37 become fixtures. Nothing in this part prohibits the filing of a "precautionary
38 fixture filing, which would provide protection in the event goods are determined to
39 be fixtures. The fact of filing should not be a factor in the determining whether
40 goods are fixtures. Cf. Section 9-505(a)(2).

41 Subsection (b) contains the following terms: "for record, "real property
42 records, "interest of record, and "record owner. These are terms traditionally
43 used in real estate law. This context "otherwise requires" that the definition of
44 "record" in Section 9-102(a) is not applicable.

1 6. **“Pre-filed Financing Statement.** Subsection (e), which is taken from
2 former Section 9-402(1), may be unnecessary. Nevertheless, a majority of the
3 Drafting Committee believe that the provision has proven useful. See also Section
4 9-308(a) (contemplating situations in which a financing statement is filed before a
5 security interest attaches).

6 **SECTION 9-503. NAME OF DEBTOR AND SECURED PARTY.**

7 (a) A financing statement sufficiently provides the name of the debtor:

8 (1) if the debtor is a registered entity, only if the financing statement
9 provides the name of the debtor as shown on the public records of the debtor's State
10 of organization;

11 (2) if the debtor is a decedent's estate, only if the financing statement
12 provides the name of the decedent and indicates that the debtor is an estate;

13 (3) if the debtor is a trust or a trustee acting with respect to property of a
14 trust, only if the financing statement:

15 (A) provides the name, if any, specified for the trust in its organic
16 documents or, if no name is specified, provides the name of the settlor and
17 additional information sufficient to distinguish the debtor from other trusts having
18 one or more of the same settlors; and

19 (B) indicates, in the debtor's name or otherwise, that the debtor is a
20 trust; and

21 (4) in other cases:

22 (A) if the debtor has a name, only if it provides the individual or
23 organization ~~organizational~~ name of the debtor; and

24 (B) if the debtor does not have a name, only if it provides the names
25 of the partners, members, associates, or other persons comprising the debtor.

1 (b) A financing statement that sufficiently provides the name of the debtor
2 in accordance with subsection (a) is not rendered ineffective by the [presence or]
3 absence of:

4 (1) a trade or other name [of the debtor]; or

5 (2) except when required under subsection (a)(4)(B), names of partners,
6 members, ~~or associates, or other persons comprising~~ of the debtor.

7 (c) A financing statement that provides only the debtor's trade name ~~or only~~
8 ~~the names of the debtor's partners, members, or associates~~ does not sufficiently
9 provide the name of a debtor ~~that has a name~~.

10 (d) A financing statement may provide the name of more than one debtor
11 and the name of more than one secured party.

12 (e) The failure to indicate the representative capacity of a secured party or
13 representative of a secured party does not affect the sufficiency of a financing
14 statement.

15 Reporters' Comments

16 **Discussion Questions:** Should the name for a trust be that of the trustee,
17 perhaps accompanied by a trust number and date of trust agreement, rather than the
18 settlor? Should the draft provide more guidance for cases in which there is more
19 than one trustee/settlor or in which the trustee's name changes after filing?

20 1. **Source.** Subsection (a)(4) derives from former Section 9-402(7);
21 otherwise, new.

22 2. **Debtor's Name.** The requirement that a financing statement give the
23 debtor's name is particularly important. Financing statements are indexed under
24 the name of the debtor, and those who wish to find financing statements search for
25 them under the debtor's name. Subsection (a) explains what the debtor's name is
26 for purposes of a financing statement. If the debtor is a "registered entity" (defined
27 in Section 9-102 so as to ordinarily include corporations, limited partnerships, and
28 limited liability companies), then the debtor's name is the name shown on the
29 public records of the debtor's "State of organization" (also as defined in Section
30 9-102). Subsections (a)(2) and (a)(3) contain special rules for decedent's estates
31 and trusts, as to which current law is now silent.

32 Subsection (a)(4)(A) essentially follows the first sentence of former Section
33 9-402(7). Section 1-201(28) defines the term "organization," which appears in
34 subsection (a)(4), very broadly, to include all legal and commercial entities as well

1 as associations that lack the status of a legal entity. If the organization has a name,
2 that name is the correct name to put on a financing statement. If the organization
3 does not have a name, then the financing statement should name the individuals or
4 other entities who comprise the organization.

5 Together with subsections (b) and (c), subsection (a) reflects the prevailing
6 view that the actual individual or organizational name of the debtor on a financing
7 statement is both necessary and sufficient, whether or not the financing statement
8 provides trade or other names of the debtor and, if the debtor has a name, whether
9 or not the financing statement provides the names of the partners, members, or
10 associates who comprise the debtor.

11 3. **Secured Party's Name.** New subsection (e) makes clear that when the
12 secured party is a representative, the financing statement is sufficient if it names the
13 secured party, whether or not it indicates any representative capacity. Similarly, a
14 financing statement that names a representative of the secured party need not
15 indicate the representative capacity.

16 *Example:* Debtor grants a security interest to a group of secured parties, but
17 not to their representative, the collateral agent. The collateral agent is not
18 itself a secured party. See Section 9-102. Under Sections 9-502(a) and
19 9-503(e), however, a financing statement is effective if it names as secured
20 party the collateral agent and not the actual secured parties, even if it omits
21 the collateral agent's representative capacity.

22 Difficulties may arise if (i) a person (A) is the representative for one group
23 of lenders (Group A), (ii) the financing statement names A as the secured party
24 without indicating that A serves as a representative for Group A, and (iii) A agrees
25 to serve as representative for another group of lenders (Group B) and further agrees
26 that it is a representative for Group B under the financing statement originally filed
27 on behalf of Group A. What are the relative priorities as between Group A and
28 Group B, to the extent that each group claims the same collateral? Arguably, the
29 priority of each group would date from the initial filing. In a case of undersecurity,
30 the later-in-time Group B's interest could deprive Group A of the full benefit of
31 otherwise available collateral.

32 To prevent this result, Group A might have insisted that the financing
33 statement recite that it operates only for the benefit of lenders under a particular
34 agreement, as it may be amended from time to time, and recite further that it is
35 ineffective for other purposes. If Group A did not do so, presumably it could be
36 hold A liable for money damages for breach of its agreement with Group A. In any
37 event, the financing statement serves the functions of informing interested third
38 parties that a security interest may have been created in the property indicated in the
39 financing statement and providing a source for more information concerning
40 possible security interests.

41 4. **Multiple Names.** Subsection (d) makes explicit what is implicit in
42 current law, that a financing statement may provide the name of more than one
43 debtor or secured party. See Section 1-102(5)(a) (words in the singular include the
44 plural).

SECTION 9-504. INDICATION OF COLLATERAL. A financing statement sufficiently indicates the collateral that it covers if the financing statement provides:

- (1) a description of the collateral pursuant to Section 9-111;
- (2) an indication of the type of collateral; or
- (3) a statement to the effect an indication that the financing statement covers all assets or all personal property is sufficient to indicate the collateral that is covered by a financing statement.

Reporters' Comments

1. Source. Former Section 9-402(1).

2. Indication of Collateral. This section expands the class of sufficient collateral references to embrace “a statement to the effect that the financing statement covers all assets or all personal property. If the property in question belongs to the debtor and is personal property, any searcher will know that the property is covered by the financing statement. A broad statement of this kind would not be a sufficient description for purposes of a security agreement. See Section 9-111. It follows that a somewhat narrower description than “all assets, e.g., “all assets other than automobiles, is sufficient for purposes of this section even if it does not suffice for purposes of a security agreement.

**SECTION 9-505. FILING AND COMPLIANCE WITH OTHER
STATUTES AND TREATIES FOR CONSIGNMENTS, LEASES,
BAILMENTS, AND OTHER TRANSACTIONS.**

(a) A consignor, lessor, or bailor of goods or a buyer of a payment intangible may file a financing statement, or may comply with a statute or treaty described in Section 9-309A(a), using the terms “consignor, “consignee, “lessor, “lessee, “bailor, “bailee, “owner, “registered owner , “buyer, “seller, or the like, instead of the terms “secured party and “debtor.

(b) (1) This part applies to the filing of such a financing statement and, as appropriate, to compliance that is equivalent to filing a financing statement under

1 Section 9-309A(c), but the filing or compliance is not of itself a factor in
2 determining whether the collateral secures an obligation.

3 (2) ~~If However,~~ if it is determined for another reason that the collateral
4 secures an obligation, a security interest held by the consignor, lessor, bailor,
5 owner, or buyer which attaches to the collateral is perfected by the filing or
6 compliance.

7 Reporters' Comments

8 1. **Source.** Former Section 9-408, expanded.

9 2. **Goods Covered by a Certificate of Title.** This section provides the
10 same benefits for compliance with a statute or treaty described in Section
11 9-309A(a) that former Section 9-408 provides for filing, in connection with the use
12 of terms such as "lessor, consignor, etc. It also expands the rule to embrace more
13 generally other bailments and transactions. The references to "owner and
14 "registered owner are intended to address, for example, the situation where a
15 putative lessor is the registered owner of an automobile covered by a certificate of
16 title and the transaction is determined to create a security interest. Although this
17 section provides that the security interest is perfected, it may be advisable or
18 necessary to amend the relevant certificate-of-title act in order to ensure that this
19 result will be achieved. The references to "buyer and "seller encompass sales
20 transactions, primarily sales of receivables.

21 3. **"Intended as Security."** Former Article 9 and Section 1-201 refer to
22 transactions, including leases and consignments, "intended as security. This
23 misleading phrase creates the erroneous impression that the parties to a transaction
24 can dictate how the law will classify it (e.g., as a bailment or as a security interest)
25 and thus affect the rights of third parties. The phrase has been deleted wherever it
26 appears. The last two sentences of this section substitute the concept of whether
27 collateral secures an obligation for the existing "intention standard.

28 4. **Consignments.** Although a "true consignment is a bailment, the filing
29 and priority provisions of former Article 9 apply to it; a consignment "intended as
30 security creates a security interest that is in all respects subject to former Article 9.
31 This Article subsumes many true consignments under the rubric of "security
32 interest. Nevertheless, it maintains the distinction between a (true)
33 "consignment, as to which only certain aspects of Article 9 apply, and a would-be
34 consignment that actually "secures an obligation, to which Article 9 applies in full.
35 The revisions to this section reflect the change in terminology.

36 **SECTION 9-506. EFFECT OF INSUFFICIENCY ~~MINOR ERRORS.~~**

1 (a) A financing statement substantially complying with the requirements of
2 this part is effective; even if it contains an insufficiency, ~~minor errors that are not~~
3 unless the insufficiency makes the financing statement seriously misleading.

4 (b) Except as otherwise provided in subsection (c), a A financing statement
5 that fails to sufficiently provide the ~~correct~~ name of the debtor in accordance with
6 Section 9-503(a) ~~contains an error that~~ is seriously misleading.

7 (c) If ~~unless~~ a search of the records of the filing office under the debtor's
8 correct name, utilizing the filing office's standard search technique, would disclose
9 a the financing statement that fails to sufficiently provide the correct name of the
10 debtor in accordance with Section 9-503(a), in which case the incorrect name
11 provided does is not make an error that renders the financing statement seriously
12 misleading.

13 (d) For purposes of Section 9-510(b), the "debtor's correct name in
14 subsection (c) means the correct name of the new debtor.

15 Reporters' Comments

16 **Changes from Prior Draft:**

17 A. The formulation of the "minor error" rule has been conformed to
18 usage elsewhere (see, e.g., § 9-502, which explains when a financing statement is
19 "sufficient").

20 B. Subsection (d) is new. It provides that, in determining the extent to
21 which a financing statement naming an original debtor is effective against a new
22 debtor, the sufficiency of financing statement should be tested against the name of
23 the new debtor.

24 **Discussion Question:**

26 Many filing offices divide search results into two categories. Those
27 financing statements that appear "above the line" are thought to match the name
28 submitted, whereas those that appear the "below the line" contain names that the
29 filing office thinks are sufficiently similar to that searched that they may be of
30 interest to the searcher.

31 Filing offices are working to develop an agreed search logic that will be
32 applied to determine the "above the line" results. However, they wish to remain

1 free to supplement results obtained through the agreed search logic with results
2 obtained with a broader search logic.

3 Under what circumstances should a financing statement containing an
4 incorrect name for the debtor be effective? Here are three possibilities:

5 A. All financing statements that the filing office would disclose to the
6 searcher after conducting a search under the correct name in accordance with *that*
7 *filing office's* standard procedure. This approach would make "below the line
8 financing statements (which may be quite numerous) effective. It also would
9 require a change in practice on the part of those searchers who ignore whatever is
10 "below the line. The approach would yield nonuniform results among
11 jurisdictions, depending on the search logic employed by the filing office. In
12 addition, the effectiveness of a financing statement within a jurisdiction might be
13 affected by a change in the search logic that is employed.

14 B. Financing statements that the filing office would disclose to the
15 searcher as "above the line, after conducting a search under the correct name in
16 accordance with *that filing office's* standard procedure. Under this approach, the
17 effectiveness of a financing statement would turn on the manner in which the filing
18 office categorizes its requests. Like the first approach, this one would yield
19 nonuniform results among jurisdictions, and the effectiveness of a financing
20 statement within a jurisdiction might be affected by a change in the search logic
21 that is employed.

22 C. Financing statements that would be discovered if the filing office
23 searched using a specified search logic. (Article 9 might spell out the search logic
24 or might incorporate by reference a search logic established by a third party.) This
25 approach would result in uniformity among the jurisdictions that adopted this
26 Article 9 provision and would reduce the likelihood of changes in effectiveness
27 over time. However, it could result in validating financing statements that could
28 not be found using the relevant filing office's search logic.

29 1. **Source.** Former Section 9-402(8), as expanded.

30 2. **Errors.** This section adds to former Section 9-402(8) two per se rules
31 concerning the effectiveness of financing statements in which the debtor's name is
32 incorrect. If the financing statement nevertheless would be discovered in a search
33 under the debtor's correct name using the filing office's standard search technique,
34 as a matter of law the incorrect name does not make the financing statement
35 seriously misleading. If the financing statement would not be discovered in a
36 search under the debtor's correct name using the filing office's standard search
37 technique, as a matter of law the financing statement is seriously misleading. A
38 financing statement that is seriously misleading under this section is ineffective
39 even if it is disclosed by (i) using a filing office's nonstandard search technique
40 (e.g., disclosed by the filing office as a "similar name but not as matching the
41 debtor's correct name), (ii) using a search technique other than that of the filing
42 office to search the official records, or (iii) searching a data base other than that of
43 the filing office.

SECTION 9-507. EFFECT OF CERTAIN CHANGES ON EFFECTIVENESS OF FINANCING STATEMENT.

(a) If a debtor so changes its name that a filed financing statement becomes seriously misleading under Section 9-506(c):

(1) the financing statement is effective to perfect a security interest in collateral acquired by the debtor before, or within four months after, the change; and

(2) the financing statement is not effective to perfect a security interest in collateral acquired by the debtor more than four months after the change, unless an amendment to the financing statement that renders the financing statement not seriously misleading is filed within four months after the change.

(b) A filed financing statement remains effective with respect to collateral that is sold, exchanged, leased, licensed, or otherwise disposed of and in which a security interest continues under Section 9-313(c), even if the secured party knows of or consents to the disposition.

(c) Except as otherwise provided in subsection (a) and Section 9-510, a financing statement is not rendered ineffective if, after the financing statement is filed, the information contained in the financing statement becomes ~~erroneous and~~ seriously misleading under Section 9-506.

Reporters' Comments

1. Source. Former Section 9-402(7).

2. Post-filing Change in Debtor’s Name. This section deals with situations in which the information in a proper financing statement becomes inaccurate. Subsection (a) addresses a “pure change of name that does not implicate a new debtor. It clarifies the effectiveness of a seriously misleading financing statement for the four months following a name change and provides that the record can be corrected by an amendment to the financing statement that specifies the debtor’s new correct name or otherwise renders the financing statement not seriously misleading.

1 **3. Post-filing Transfer of Collateral.** Subsection (b) clarifies the third
2 sentence of former Section 9-402(7) by providing that a financing statement
3 remains effective following the transfer of collateral only when the security interest
4 continues in that collateral. This result is consistent with the conclusion of PEB
5 Commentary No. 3.

6 **4. Other Post-filing Changes.** Subsection (c) provides that, except for the
7 four-month rules in subsection (a) (“pure name change) and Section 9-510 (new
8 debtor that becomes bound by original debtor’s security agreement), post-filing
9 changes that render a financing statement inaccurate and seriously misleading have
10 no effect on a financing statement. The financing statement remains effective.

11 **SECTION 9-508. WHEN RECORD MAY BE FILED; EFFECTIVENESS**
12 **~~OF FILED RECORD.~~**

13 (a) A person ~~may~~ is entitled to file an initial financing statement, ~~or an~~
14 amendment that adds collateral covered by a financing statement, or an amendment
15 that adds a debtor to a financing statement only if:

16 (1) the debtor authorizes the filing in an authenticated record; or

17 (2) (A) the person holds a statutory lien that has become effective at the
18 time of filing; and

19 (B) the financing statement covers only collateral in which the
20 person holds a statutory lien.

21 (b) By ~~signing~~ authenticating a security agreement, a debtor authorizes the
22 filing of an initial financing statement, and an amendment, covering[:

23 (1)] the collateral described in the security agreement; [and

24 (2) proceeds of the collateral, whether or not the security agreement
25 expressly covers proceeds].

26 (c) A person ~~may~~ is entitled to file an amendment other than an amendment
27 that adds collateral covered by a financing statement or an amendment that adds a
28 debtor to a financing statement only if:

1 (1) the secured party of record authorizes the filing [in an authenticated
2 record]; or

3 (2) the amendment is a termination statement for a financing statement
4 as to which the secured party of record has failed to file or send a termination
5 statement as required by Section 9-511(b) or (c).

6 (d) If there is more than one secured party of record for a financing
7 statement, each secured party of record may ~~file~~ authorize the filing of an
8 amendment under subsection (c) ~~Section 9-509(a)~~.

9 ~~(d) A filed record is effective only to the extent that this section permits a~~
10 ~~person to file it.~~

11 ~~(e) If a person is permitted to file a termination statement only under~~
12 ~~subsection (c)(2), the filed termination statement is effective only if the debtor~~
13 ~~authorizes the filing and the termination statement indicates that the filing is made~~
14 ~~by or on behalf of the debtor.~~

Changes from Prior Draft: Subsection (a) now addresses amendments that add debtors. New subsection (d) previously appeared in Section 9-513. Former subsections (d) and (e) have been moved to Section 9-508A.

1. **Source.** New.

2. **Scope and Approach of This Section.** This section collects in one place most of the rules determining whether a record may be filed. Section 9-508A explains the extent to which a filed record is effective. These sections reflect the draft's indifference as to the person who effects a filing. The filing scheme contemplated by this part does not contemplate that the identity of a "filer" will be a part of the searchable records. This is consistent with, and a necessary aspect of, eliminating signatures or other evidence of authorization from the system (except to the extent that filing offices may choose to employ authentication procedures in connection with electronic communications). As long as the appropriate person authorizes the filing, or, in the case of a termination statement, the debtor is entitled to the termination, it is largely insignificant whether the secured party or another person files any given record.

3. **Unauthorized Filings.** Subsection (a)(1) substitutes for the debtor's signature a requirement that the debtor authorize the filing of an initial financing statement or an amendment that adds collateral. A person who files an unauthorized record in violation of subsection (a)(1) is liable under Section 9-624(d) for a statutory penalty and damages. Of course, a financing statement that is filed without authorization is ineffective to perfect a security interest. See Section 9-508A(a).

4. **Authorization in Security Agreement.** Under subsection (b), the authentication of a security agreement *ipso facto* constitutes the debtor's consent to the filing of a financing statement covering the collateral described in the security agreement. The secured party need not obtain a separate authorization. Thus, if an authenticated security agreement covers inventory, and the filed financing statement covers inventory and accounts, the financing statement is authorized insofar as it covers inventory and unauthorized insofar as it covers accounts. (Note, however, that the financing statement will be effective to perfect a security interest in accounts constituting proceeds of the inventory to the same extent as a financing statement covering only inventory.)

5. **Statutory Liens.** Under subsection (a)(2), an statutory lienholder may file a financing statement covering collateral subject to the lien without obtaining the debtor's authorization. Because the lien arises as matter of law, the debtor's consent should not be required. However, the filing office normally will inform the debtor about the filing pursuant to Section 9-520(a)(6).

6. **Amendments; Termination Statements Authorized by the Debtor.** Most amendments may not be filed unless the secured party of record authorizes the filing. [Section 9-509A] explains how to determine the identity of the secured party of record. Under subsection (c)(2), the debtor itself may authorize and file an effective termination statement in the circumstances under which the secured party of record is obliged to file or send a termination statement. However, under Section

1 9-508A(c), the termination statement must indicate that it is filed by or on behalf of
2 the debtor; otherwise, it will not be effective.

3 **7. Multiple Secured Parties of Record.** Subsection (d) deals with
4 multiple secured parties. It permits a secured party of record to authorize the filing
5 of amendments concerning its own rights under a financing statement. Section 9-
6 508A(b) protects those rights from the effects of filings made by another secured
7 party of record.

8 ***Example 1:*** A financing statement names A and B as the secured parties. If
9 B an amendment deleting some collateral covered by the financing
10 statement is filed pursuant to B's authorization, A's would remain perfected
11 in all the collateral.

12 ***Example 2:*** A financing statement names A and B as the secured parties. If
13 a termination statement is filed pursuant to B's authorization, A's rights as a
14 secured party of record would be unaffected. That is, the financing
15 statement would continue to be effective to perfect A's security interest..

16 **8. Successor to Secured Party of Record.** A person may succeed to the
17 powers of the secured party of record by operation of other law, e.g., the law of
18 corporate mergers. If so, the successor has the power to authorize filings within the
19 meaning of this section.

20 **SECTION 9-508A. EFFECTIVENESS OF FILED RECORD.**

21 (a) Subject to subsection (c), a ~~A~~ filed record is effective only to the extent
22 that ~~this section permits a person to file it~~ a person is entitled to file it under Section
23 9-508.

24 _____ (b) A record ~~filed~~ authorized by one secured party of record ~~affects only the~~
25 ~~rights of the filer and~~ does not affect the rights under the financing statement of
26 another secured party of record.

27 (c) If a person is ~~permitted~~ entitled to file a termination statement only
28 under ~~subsection~~ Section 9-508(c)(2), the filed termination statement is effective
29 only if the debtor authorizes the filing and the termination statement indicates that
30 the filing is made by or on behalf of the debtor.

31 **Reporters' Comments**

32 **Changes from Prior Draft:** Subsections (a) and (c) appeared in Section 9-
33 508 of the prior draft. Subsection (b) appeared in Section 9-513.

1
2 1. **Source.** New.

3 2. **Ineffectiveness of Unauthorized or Overbroad Filings.** Subsection (a)
4 provides that a filed financing statement is not effective to the extent that a person
5 was not entitled to file it.

6 ***Example:*** Debtor authorizes the filing of a financing statement covering
7 inventory. The filed financing statement covers inventory and equipment.
8 The secured party is entitled to file the financing statement; however, the
9 financing statement is effective only to the extent authorized. That is, the
10 financing statement is effective to perfect a security interest in inventory but
11 ineffective to perfect a security interest in equipment.

12 3. **Multiple Secured Parties of Record.** Section 9-508(d) permits any
13 secured party of record to authorize the filing of most amendments. Subsection (b)
14 of this section prevents a filing authorized by one secured party of record from
15 affecting the rights of another secured party of record without the latter's consent.

16 **SECTION 9-509. AMENDMENT OF FINANCING STATEMENT.**

17 (a) Subject to ~~Section[s 9-509 and] 9-513~~, Section 9-508, a person may add
18 or delete collateral covered by a financing statement or, subject to subsection (d),
19 otherwise amend the information contained in a financing statement by filing an
20 amendment that identifies the initial financing statement by ~~the~~ its file number
21 ~~assigned pursuant to Section 9-520(a) or if the initial financing statement was filed~~
22 ~~before the effective date of this article~~ file number does not itself indicate the date
23 of filing, by the date of filing and file number.

24 (b) Except as otherwise provided in Section 9-516, the filing of an
25 amendment does not extend the period of effectiveness of a financing statement.

26 (c) A financing statement that is amended by an ~~if an~~ amendment that adds
27 collateral, ~~it is effective as to the added collateral only from the date of~~ the filing of
28 the amendment.

29 (d) A financing statement that is amended by an amendment that adds a
30 debtor is effective as to the added debtor only from the date of the filing of the
31 amendment.

~~(d) A filed record that adds a debtor is not effective as an amendment.~~

(e) An amendment is ineffective to the extent it:

(1) purports to delete all secured parties of record and fails to provide
the name of a new secured party of record; or

(2) purports to delete the names of all debtors and fails to provide the name of a debtor not previously covered by the financing statement.

Reporters' Comments

Changes from Prior Draft:

A. New subsection (d) contemplates the filing of an amendment adding a debtor. See Comment 4. If these changes are approved, Section 9-510 may need to be conformed.

B. New subsection (e) assures that there will be a debtor and secured party of record for every financing statement.

Discussion Questions:

A. The national forms include a “change statement,” to be used for amendments, assignments, terminations, and continuations. Should the statute adopt this terminology? This would result in an “amendment” becoming a “change statement.”

B. Should the amendments described in subsection (e) operate to terminate the effectiveness of the financing statement?

1. **Source.** Former 9-402(4).

2. Changes to Financing Statements. This section addresses changes to financing statements, including addition and deletion of collateral. Although termination statements, assignments, and continuation statements are types of amendment, this Article follows former Article 9 and treats these types of amendments separately. See Section 9-511 (termination statements); 9-512 (assignments); 9-517 (continuation statements). One should not infer from this separate treatment that this Article requires a separate amendment to accomplish each change. Rather, a single amendment would be legally sufficient to, e.g., add collateral and continue the effectiveness of the financing statement.

3. **Amendments.** An amendment under this Article may identify only the information contained in a financing statement that is to be changed or, alternatively, it may take the form of an amended and restated financing statement. The latter would state, for example, that the financing statement “is amended and restated to read as follows: . . . References in this Part to an “amended financing statement” are to a financing statement as amended by an amendment.

1 This section revises former Section 9-402(4) to permit secured parties of
2 record to make changes in the public record without the need to obtain the debtor's
3 signature. However, the filing of an amendment that adds collateral must be
4 authorized by the debtor or it will not be effective. See Section 9-508(a), (d).

5 4. **Addition of a Debtor.** An amendment that adds a debtor is effective,
6 provided that the added debtor authorizes the filing See Section 9-508(a)(1).
7 However, filing an amendment adding a debtor to a previously filed financing
8 statement affords no advantage over filing an initial financing statement against that
9 debtor. With respect to the added debtor, for purposes of determining the priority
10 of the security interest, the time of filing is the time of the filing of the amendment.
11 See subsection (d). Moreover, the effectiveness of the financing statement lapses
12 with respect to added debtor at the time it lapses with respect to the original debtor.
13 See subsection (b).

14 [SECTION 9-509A. SECURED PARTY OF RECORD.]

15 (a) A secured party of record with respect to a financing statement is a
16 person whose name is provided as the name of the secured party or a representative
17 of the secured party in an initial financing statement that has been filed.

18 (b) A person [whose name is provided] remains a secured party of record
19 until the filing of an effective amendment of the financing statement which
20 indicates that the person is not a secured party or a representative of a secured party.

21 (~~c~~ **b**) If an effective amendment of a financing statement which provides the
22 name of a person as a secured party or a representative of a secured party is filed,
23 the person named in the amendment is a secured party of record.]

24 Reporters' Comments

25 1. **Source.** New.

26 2. **"Secured Party of Record."** This new section reflects an alternative to
27 the definition of "secured party of record" in § 9-102. The goal is to explain how
28 the secured party of record is to be determined. If SP-1 is named as the secured
29 party in an initial financing statement, it is the secured party of record. If,
30 subsequently, an amendment is filed assigning SP-1's status to SP-2, then SP-2
31 becomes the secured party of record in place of SP-1. The same result obtains if a
32 subsequent amendment deletes the reference to SP-1 and substitutes therefor a
33 reference to SP-2. If, however, a subsequent amendment adds SP-2 as a secured
34 party but does not purport to remove SP-1 as a secured party, then SP-2 and SP-1
35 each is a secured party of record. An amendment purporting to remove the only
36 secured party of record without providing a successor is ineffective. See Section 9-
37 509(e). Although this new section describes the means of determining the secured

1 party of record in somewhat more detail, the same results should be obtained by
2 applying the definition in Section 9-102. At any point in time, all effective records
3 that comprise a financing statement must be examined to determine the person or
4 persons that have secured party of record status.

5 Application of other law may result in a person succeeding to the powers of a
6 secured party of record. For example, if the secured party of record (A) merges into
7 another corporation (B) and the other corporation (B) survives, other law may
8 provide that B has all of A's powers. If so, then B is authorized to take all actions
9 under this part that A would have been authorized to take. Similarly, acts taken by
10 a person who is authorized under generally applicable principles of agency to act on
11 behalf of the secured party of record are effective under this part.

12 **SECTION 9-510. EFFECTIVENESS OF FINANCING STATEMENT IF**
13 **NEW DEBTOR BECOMES BOUND BY SECURITY AGREEMENT.**

14 (a) Except as otherwise provided in subsections (b) and (c), a filed
15 financing statement naming an original debtor is effective to perfect a security
16 interest in collateral in which a new debtor has or acquires rights to the extent that
17 the financing statement would have been effective had the original debtor acquired
18 rights in the collateral.

19 (b) If the difference between the name of the original debtor and that of the
20 new debtor causes a filed financing statement that is effective under subsection (a)
21 to be seriously misleading under Sections 9-506(c) and (d):

22 (1) the financing statement is effective to perfect a security interest in
23 collateral acquired by the new debtor before, and within four months after, the new
24 debtor becomes bound under Section 9-203(c); and

25 (2) the financing statement is not effective to perfect a security interest
26 in collateral acquired by the new debtor more than four months after the new debtor
27 becomes bound under Section 9-203(c) unless an initial financing statement
28 providing the name of the new debtor is filed before the expiration of that time.

29 (c) This section does not apply to collateral as to which a filed financing
30 statement remains effective against the new debtor under Section 9-507(b).

Change from Prior Draft: See Change B. to § 9-506.

1. **Source.** New.

2. **The Problem.** Sections 9-203(b) and 9-510 deal with situations where one party (the “new debtor”) becomes bound as debtor by a security agreement entered into by another person (the “original debtor”). These situations often arise as a consequence of changes in business structure. For example, the original debtor may be an individual debtor who operates a business as a sole proprietorship and then incorporates it. Or, the original debtor may be a corporation that is merged into another corporation. Under both former Article 9 and this Article, collateral that is transferred in the course of the incorporation or merger normally would remain subject to a perfected security interest. See Sections 9-313(c); 9-507(b). Former Article 9 is less clear with respect to whether an after-acquired property clause in a security agreement authenticated by the original debtor would be effective to create a security interest in property acquired by the new corporation or the merger survivor and, if so, whether a financing statement filed against the original debtor would be effective to perfect the security interest. This section and Section 9-203(b) are an attempt at clarification.

3. **How a New Debtor Becomes Bound.** Normally, a security interest is unenforceable unless the debtor has authenticated a security agreement describing the collateral. See Section 9-203(a). New Section 9-203(b) creates an exception, under which a security agreement entered into by one person is effective with respect to the property of another. This exception comes into play if a “new debtor” “becomes bound” as debtor by a security agreement entered into by another person (the “original debtor”). (The first and last quoted terms are defined in new subsections of Section 9-102; “becomes bound” is defined in Section 9-203(c).) If a new debtor does become bound, then the security agreement entered into by the original debtor satisfies the security-agreement requirement of Section 9-203(a)(1) as to existing or after-acquired property of the new debtor to the extent the property is described in the agreement. In that case, no other agreement is necessary to make a security interest enforceable in that property. See Section 9-203(b).

Section 9-203(c) provides the way in which a new debtor “becomes bound” by an original debtor’s security agreement. Under Section 9-203(c)(1), a new debtor becomes bound as debtor if it becomes bound by contract or by operation of non-UCC law. The latter would occur if, for example, the applicable corporate law of mergers provides that, if A Corp merges into B Corp, B Corp becomes a debtor under A Corp’s security agreement. The former might occur when B contractually assumes A’s obligations under the security agreement.

Under certain circumstances, a new debtor “becomes bound” for purposes of Article 9 even though it would not be bound under other law. Under Section 9-203(c)(2), a new debtor becomes bound when (i) it becomes obligated not only for the secured obligation but also generally under applicable non-UCC law for the obligations of the original debtor and (ii) acquires or succeeds to substantially all the assets of the original debtor. For example, some corporate laws provide that, when two corporations merge, the surviving corporation succeeds to the assets of its merger partner and “has all liabilities” of both corporations. In the case where,

1 for example, A Corp merges into B Corp (and A Corp ceases to exist), some people
2 have questioned whether A Corp's grant of a security interest in its existing and
3 after-acquired property becomes a "liability" of B Corp, such that B Corp's existing
4 and after-acquired property becomes subject to a security interest in favor of A
5 Corp's lender. Even if corporate law were to give a negative answer, under Section
6 9-203(c)(2), B Corp would "become bound" for purposes of Section 9-203(b) and
7 this section. Section 9-203(c)(2) excludes sureties and other secondary obligors as
8 well as persons who become obligated through veil piercing and other non-
9 successorship doctrines. In many cases, it will exclude successors to the assets and
10 liabilities of a division of a debtor.

11 **4. When a Financing Statement Is Effective Against a New Debtor.**

12 Subsection (a) provides that a filing against the original debtor is effective to
13 perfect a security interest in collateral that a new debtor acquires before the
14 expiration of four months after the new debtor becomes bound by the security
15 agreement. Under subsection (b), however, if the filing against the original debtor
16 is seriously misleading as to the new debtor's name, the filing is effective as to
17 collateral acquired by the new debtor after the four-month period only if a person
18 files during the four-month period an initial financing statement providing the name
19 of the new debtor. A similar rule appears in Section 9-507(a) with respect to
20 changes in a debtor's name.

21 Note, however, that this section does not apply to collateral transferred by
22 the original debtor to a new debtor. Under those circumstances, the filing against
23 the original debtor continues to be effective until it lapses. See subsection (c);
24 Section 9-507(b).

25 **5. Priority.** Section 9-323A governs the priority contest between a secured
26 creditor of the original debtor and a secured creditor of the new debtor. This
27 priority rule no doubt will be both under- and over-inclusive.

28 **SECTION 9-511. TERMINATION STATEMENT.**

29 (a) A termination statement for a financing statement is an amendment of
30 the a financing statement that:

31 (1) complies ~~in addition to complying~~ with the requirements of Section
32 9-509(a); and

33 (2) indicates either that it is a termination statement or that an identified
34 financing statement is no longer effective.

35 (b) (1) ~~If a financing statement covers consumer goods, within one month,~~
36 ~~or [within 10 days] [as soon as reasonably practicable, but not more than three~~
37 ~~days,] after the secured party receives a [signed] [authenticated] demand by the~~

1 ~~debtor, The secured party shall cause the secured party of record for a financing~~
2 ~~statement to file with the filing office a termination statement for the financing~~
3 ~~statement if:~~

4 (A) the financing statement covers consumer goods; and

5 (B)(i) ~~and if there is no outstanding secured obligation and no~~
6 ~~commitment to make an advance, incur an obligation, or otherwise give value; or~~

7 (ii) ~~if the debtor did not authorize the filing of the initial~~
8 ~~financing statement, the secured party of record shall file with the filing office a~~
9 ~~termination statement for the financing statement.~~

10 (2) The secured party shall cause the secured party of record to file the
11 termination statement:

12 (A) within one month after there is no outstanding secured
13 obligation and no commitment to make an advance, incur an obligation, or
14 otherwise give value; or, if earlier,

15 (B) [within 10 days] [as soon as reasonably practicable, but not more
16 than three days,] after the secured party receives a [signed] [authenticated] demand
17 by the debtor.

18 (c) In other cases, within 10 days after the secured party receives a [signed]
19 [authenticated] demand by the debtor, the secured party shall cause the secured
20 party of record for a financing statement to send to the debtor a termination
21 statement for the financing statement or file the termination statement with filing
22 office if:

23 (1) there is no outstanding secured obligation and no commitment to
24 make an advance, incur an obligation, or otherwise give value;

25 (2) the debtor did not authorize the filing of the initial financing
26 statement; or

(3) if a the financing statement covers accounts, chattel paper, or payment intangibles that have been sold but as to which the account debtor or other person obligated has discharged its obligation, ~~the secured party of record for a financing statement, [within 10 days] [as soon as reasonably practicable but not more than three days] after the secured party receives [a] [an authenticated] demand by the debtor, shall send to the debtor a termination statement for the financing statement or file the termination statement with filing office.~~

(e d) Except as otherwise provided in Section ~~9-513~~, 9-508A, upon the filing of [a] ~~[an effective]~~ termination statement with the filing office ~~under subsection (b)~~, the financing statement to which the termination statement relates becomes ineffective.

Reporters' Comments

Change from Prior Draft: Subsection (d) now refers to the filing of “a termination statement” rather than “an effective termination statement. If a termination statement is not effective, it does not affect the financing statement. The same is true for any other amendment. If we expressly require an “effective termination statement here, we should do so every other place in the Article where effectiveness is implicit. This would include not only provisions of Part 5 but other provisions as well (e.g., proceeds rules that turn on whether “a filed financing statement” covers the collateral).

Discussion Questions:

A. When the secured party is not the secured party of record, who owes a duty to provide a termination statement? As written, the draft imposes this duty on the secured party. Should the debtor have a remedy against the secured party of record, as well?

B. Should the time frame be changed from “three days” to “three business days”?

1. Source. Former Section 9-404.

2. Requirements for Termination Statement. Subsection (a) establishes the requirements for a termination statement, thereby eliminating some redundancies in former Section 9-404. Most of the other changes in the section are for clarification or to embrace medium-neutral drafting. Note that, like a financing statement, a termination statement need not be signed or otherwise authenticated.

1 3. **Duty to File or Send.** Subsections (b) and (c) specify when a secured
2 party of record must file or send to the debtor a termination statement for a
3 financing statement. Subsection (b) applies to a financing statement covering
4 consumer goods. Subsection (c) applies to other financing statements. Each
5 subsection makes explicit what may have been implicit in earlier drafts and under
6 the former article: If the debtor did not authorize the filing of a financing statement
7 in the first place, the secured party of record should file or send a termination
8 statement. The liability imposed upon a secured party that fails to comply with
9 subsection (b) or (c) is identical to that imposed for the filing of an unauthorized
10 financing statement or amendment. See Section 9-624(d). If there is more than one
11 secured party of record, a termination statement filed by one does not affect the
12 rights of the others. See Section 9-508A.

13 4. **Buyers of Receivables.** Applied literally, former Section 9-404(1)
14 would require many buyers of receivables to file a termination statement
15 immediately upon filing a financing statement because “there is no outstanding
16 secured obligation and no commitment to make advances, incur obligations, or
17 otherwise give value. Subsection (c) has been revised to remedy this problem.

18 5. **Effect of Filing.** Subsection (d) is new. It states the effect of filing a
19 termination statement. If one of several secured parties of record files a termination
20 statement, subsection (d) applies only with respect to the rights of the person filing
21 the termination statement. See Section 9-508A. The financing statement remains
22 effective with respect to the rights of the others.

23 6. **“Bogus” Filings and Disappearing Secured Parties.** Filing offices in
24 some states have been beset by “bogus” filings containing forged debtor signatures.
25 Apparently, some of these filings have been made as a form of protest or civil
26 disobedience. Section 9-508(c)(2) addresses this problem, along with the problem
27 faced by a debtor whose secured party has disappeared or gone out of business after
28 having received full payment of the secured obligation.

29 **SECTION 9-512. ASSIGNMENT OF RIGHTS UNDER FINANCING**
30 **STATEMENT POWERS OF SECURED PARTY OF RECORD.**

31 (a) (1) Except as otherwise provided in subsection (c), an initial financing
32 statement may reflect an assignment of all of the secured party’s rights power to
33 authorize an amendment to the financing statement with respect to some or all of
34 the collateral indicated in the financing statement by providing the name and
35 mailing address of the assignee as the name and address of the secured party.

1 (2) {Upon filing, the assignee named in an initial financing statement
2 filed under this subsection is the secured party of record for the financing statement
3 ~~with respect to the collateral indicated in the assignment.~~}

4 (3) ~~{Unless an initial financing statement filed under this subsection
5 indicates otherwise, the rights under the financing statement are assigned of record
6 with respect to all of the collateral covered by the financing statement.}~~

7 (b) (1) Except as otherwise provided in subsection (c), a person secured
8 party of record may assign of record all or part of ~~the rights of a secured party of~~
9 ~~record under~~ its power to authorize an amendment to a financing statement by filing
10 in the filing office an amendment of the financing statement that:

11 (A) complies with the requirements of Section 9-509(a);

12 (B) provides the name and mailing address of the secured party of
13 record; and

14 (C) provides the name and mailing address of the assignee.

15 (2) {Upon filing, the assignee named in an amendment filed under this
16 subsection is becomes a secured party of record for the financing statement.}

17 (c) An assignment of record of a security interest in a fixture covered by a
18 real property mortgage that is effective as a fixture filing under Section 9-502(c)
19 may be made only by an assignment of record of the mortgage in the manner
20 provided by other law of this State.

21 Reporters' Comments

22 **Change from Prior Draft:** This draft eliminates the possibility of using an
23 initial financing statement to effectuate a partial assignment. Neither current law
24 nor the financing statement forms currently in use contemplates this practice.

25 1. **Source.** Former Section 9-405.

26 2. **Comparison to Prior Law.** Most of the changes to this section are for
27 clarification or to embrace medium-neutral drafting. As a general matter, this
28 Article preserves the opportunity given by former Section 9-405 to assign a security
29 interest of record in one of two different ways. Under subsection (a), a secured

party may assign all of its power to affect a financing statement by naming an assignee in the initial financing statement. The secured party of record may accomplish the same result under subsection (b) by making a subsequent filing. Subsection (b) also may be used for an assignment of only some of the secured party of record's power to affect a financing statement, e.g., the power to affect the financing statement as it relates to particular items of collateral. An initial financing statement may not be used to change the secured party of record with respect to some, but not all, of the collateral.

3. **Bracketed Paragraphs.** The bracketed paragraphs, which explain the effect of an assignment on the identity of the secured party of record, may be unnecessary if Section 9-509A is adopted.

~~SECTION 9-513. MULTIPLE SECURED PARTIES OF RECORD.~~

[deleted]

~~(a) If there is more than one secured party of record for a financing statement, each secured party of record may file an amendment under Section 9-509(a).~~

~~(b) A record filed by one secured party of record affects only the rights of the filer and does not affect the rights under the financing statement of another secured party of record.~~

Reporters' Comments

Reason for Deletion. The substance of this section now appears in Sections 9-508(d) and 9-508A(b)).

~~[SECTION 9-514. SUCCESSOR OF SECURED PARTY. A person that succeeds to substantially all of the rights of a secured party by operation of law and itself becomes a secured party may act under this part without disclosing its status as a successor or may act in its own name as the disclosed successor of a secured party.]~~

[deleted]

Reporters' Comments

Reason for Deletion. This section was intended to resolve a practical problem faced by successors to a secured party—how to identify itself with respect

1 to records filed by its predecessor. Under this draft, the effectiveness of a filed
2 record depends not upon the identity of the filer but rather on whether the filing was
3 authorized. See Sections 9-508 and 9-508A.

4 **SECTION 9-515. WHAT CONSTITUTES FILING RECORD;**
5 **EFFECTIVENESS OF FILING.**

6 (a) Except as otherwise provided in subsection (b), communication of a
7 record to a filing office and tender of the filing fee or acceptance of the record by
8 the filing office constitutes filing.

9 (b) Filing does not occur with respect to a record that a filing office refuses
10 to accept because:

11 (1) [except as otherwise provided in Section 9-521(c) and (d),] the
12 record is not communicated by a method or medium of communication authorized
13 by the filing office;

14 (2) an amount equal to or greater than the applicable filing fee is not
15 tendered;

16 (3) the filing office is unable to index the record because:

17 (A) in the case of an initial financing statement, the record does not
18 provide a name for the debtor;

19 (B) in the case of an amendment or correction statement ~~other cases,~~
20 the record:

21 (i) does not identify the initial financing statement as required by
22 Section 9-509 or 9-519, as applicable ~~this part or the filing office is unable to read~~
23 ~~or decipher the identification; or~~

24 (ii) the record identifies an initial financing statement whose
25 effectiveness has lapsed under Section 9-516; or

1 (B) ~~in the case of an amendment that amends the name of the debtor,~~
2 ~~the record does not provide an amended name for the debtor; or~~

3 (4) in the case of an initial financing statement and an amendment that
4 adds a secured party of record, the record does not provide a name and mailing
5 address for the secured party of record;

6 (5) in the case of an initial financing statement, the statement does not:

7 (A) provide a mailing address for the debtor;

8 (B) indicate whether the debtor is an individual or an organization;

9 or

10 (C) if the financing statement indicates that the debtor is an
11 organization, provide:

12 (i) the type of organization;

13 (ii) ~~provide~~ a State of organization for the debtor; or

14 (iii) ~~provide~~ an organizational identification number for the
15 debtor or indicate that the debtor has none; ~~or~~

16 (6) in the case of an assignment reflected in an initial financing
17 statement under Section 9-512(a) or an amendment filed under Section 9-512(b),
18 the record does not provide a name and mailing address for the assignee; or

19 (7) in the case of an amendment that provides a name of a debtor which
20 was not previously provided in the financing statement to which the record relates,
21 the record does not provide a mailing address for the debtor.

22 (c) For purposes of subsection (b):

23 (1) a record does not provide information if the filing office is unable to
24 read or decipher the information; and

(2) a record that neither indicates it is an amendment nor identifies the initial financing statement as required by Section 9-509 or 9-519, is an initial financing statement.

(d) Except as otherwise provided in Section 9-335, a filed financing statement complying with Section 9-502(a) is effective even if some or all of the information described in subsection (b)(5) is not stated or is incorrect.

(e) A record that is presented to the filing office with tender of the filing fee₂ but which the filing office refuses to accept for a reason other than one set forth in subsection (b)₂ is effective as a filed record except as against a purchaser of the collateral which gives value in reasonable reliance upon the absence of the record in the files.

Reporters' Comments

Changes from Prior Draft:

A. A provision has been added requiring the filing office to reject an amendment that relates to a lapsed initial financing statement.

B. Subsection (b)(4) no longer applies to every record, only those that affect the identity of the secured party of record.

C. Subsection (b)(7) requires a mailing address for debtors who are added to the record after the initial financing statement has been filed.

Discussion Question: The brackets around the “except” clause in subsection (b)(1) raise the question whether a filing office that otherwise does not accept paper-based financing statements should be obliged nevertheless to accept the national financing statement forms in Section 9-521.

1. **Source.** Subsection (a): former Section 9-403(1); the remainder is new.

2. What Constitutes Filing. Subsection (a) deals generically with what constitutes filing of a record, including an initial financing statement and amendments of all kind (e.g., assignments, termination statements, and continuation statements). It follows former Section 9-403(1), under which either acceptance of a record by the filing office or presentation of the record and tender of the filing fee constitutes filing.

3. Acceptance or Rejection of Entire Record. Subsection (b) contemplates rejection of an entire record for one of the specified reasons, although the statute does not determine when information is contained in only in one record

1 or in more than one record in connection with any particular medium of
2 communication. For example, if an initial financing statement omitted some of the
3 information described in subsection (b)(5) with respect to one of two named
4 debtors, a rejection of the financing statement under subsection (b)(5) would be a
5 rejection with respect to the filing against both debtors. Inasmuch as the singular
6 includes the plural under Section 1-102(5)(a), we do not believe that the statute
7 requires greater specificity in this respect.

8 **4. Method or Medium of Communication.** Rejection pursuant to
9 subsection (b)(1) for failure to communicate a record properly should be understood
10 to mean noncompliance with procedures relating to security, authentication, or
11 other communication-related requirements that the filing office may impose. The
12 official comments will explain this point.

13 **5. Inability of Filing Office to Read or Decipher Information.** Under
14 subsection (c), if the filing office cannot read or decipher information, the
15 information is not provided by a record for purposes of subsection (b).

16 **6. Effectiveness of Rejected Records.** A financing statement or other
17 record that is presented to the filing office but which the filing office refuses to
18 accept provides no public notice, regardless of the reason for the rejection.
19 However, this section distinguishes between records that the filing office rightfully
20 rejects and those that it wrongfully rejects. A filer is able to prevent a rightful
21 rejection by complying with the requirements of subsection (b). (Failure to comply
22 with subsection (b) affords the only grounds for rejection. See Section 9-521(a).)
23 No purpose is served by giving effect to records that justifiably never find their way
24 into the system, and subsection (b) so provides.

25 Subsection (e) deals with the filing office's unjustified refusal to accept a
26 record. Here, the filer is in no position to prevent the rejection and, many believe,
27 as a general matter should not be prejudiced by it. Although wrongfully rejected
28 records generally are effective, subsection (e) contains a special rule to protect a
29 third party purchaser of the collateral (e.g., a buyer or competing secured party)
30 who gives value in reliance upon the apparent absence of the record from the files.
31 As against an innocent reliance party, subsection (e) imposes upon the filer the risk
32 that a record failed to make its way into the filing system. This risk is likely to be
33 small, particularly when a record is presented electronically, and the filer can guard
34 against this risk by conducting a post-filing search of the records. Moreover,
35 Section 9-521(b) requires the filing office to give prompt notice of its refusal to
36 accept a record for filing.

37 **7. Effectiveness of Rejectable But Unrejected Records.** Section 9-521(a)
38 requires the filing office to refuse to accept an initial financing statement lacking
39 the information described in subsection (b)(5). However, if the filing office accepts
40 such a financing statement nevertheless, the absence of the information normally
41 does not affect the effectiveness of the financing statement. See subsection (d).
42 Similarly, an otherwise effective financing statement remains so even though the
43 information described in subsection (b)(5) is incorrect, except as against certain
44 persons who relied upon the incorrect information. See Section 9-335.

1 **SECTION 9-516. DURATION AND EFFECTIVENESS OF FINANCING**
2 **STATEMENT; EFFECT OF LAPSED FINANCING STATEMENT.**

3 (a) Except as otherwise provided in subsections (b), (e), (f), and (g), and
4 Section 9-519(i), a filed financing statement is effective for a period of five years
5 after the date of filing.

6 (b) Except as otherwise provided in subsections (e), (f), and (g), and
7 Section 9-519(i), if an initial financing statement is filed in connection with a
8 [public finance transaction] [or] [manufactured home transaction] and indicates that
9 it is effective for an extended period under Section 9-502(b), the filed financing
10 statement is effective for the extended period indicated.

11 (c)(1) The effectiveness of a filed financing statement lapses on the
12 expiration of the period of its effectiveness unless before the lapse a continuation
13 statement is filed pursuant to subsection (d) [, notwithstanding the commencement
14 of insolvency proceedings by or against the debtor].

15 (2) Upon lapse, a financing statement becomes ineffective and any
16 security interest or statutory lien that was perfected by the financing statement
17 becomes unperfected, unless the security interest [or statutory lien] is perfected
18 without filing.

19 (3) If the security interest or a statutory lien becomes unperfected upon
20 lapse, it is deemed never to have been perfected as against a prior or subsequent
21 purchaser of the collateral for value.

22 (d) A continuation statement may be filed only within six months before
23 the expiration of the five-year period specified in subsection (a) or the extended
24 period under subsection (b).

25 (e) (1) ~~Subject to Section 9-508~~ Except as otherwise provided in 9-508A,
26 upon timely filing of a continuation statement, the effectiveness of the initial

1 financing statement continues for a period of five years commencing on the day on
2 which the financing statement would have become ineffective in the absence of the
3 filing.

4 (2) Upon the expiration of the five-year period, the financing statement
5 lapses in the same manner as provided in subsection (c), unless, before the lapse,
6 another continuation statement is filed pursuant to subsection (d).

7 (3) Succeeding continuation statements may be filed in the same
8 manner to continue the effectiveness of the initial financing statement.

9 (f) If a debtor is a transmitting utility and a filed financing statement so
10 indicates, the financing statement is effective until a termination statement is filed.

11 (g) A real property mortgage that is effective as a fixture filing under
12 Section 9-502(c) remains effective as a fixture filing until the mortgage is released
13 or satisfied of record or its effectiveness otherwise terminates as to the real
14 property.

15 Reporters' Comments

16 1. **Source.** Former Section 9-403(2), (3), (6).

17 2. **Period of Financing Statement's Effectiveness.** Subsection (a) states
18 the general rule: a financing statement is effective for a five-year period unless its
19 effectiveness is continued under this section or terminated under Section 9-519.
20 Subsection (b) provides for a longer period in the case of a public finance
21 transaction or a manufactured home transaction, inasmuch as these financings
22 typically extend beyond the standard, five-year period. Under subsection (f), a
23 financing statement filed against a transmitting utility remains effective indefinitely,
24 until a termination statement is filed. Likewise, under subsection (g), a real
25 property mortgage effective as a fixture filing remains effective until its
26 effectiveness terminates under real property law.

27 3. **Lapse.** When the period of effectiveness under subsection (a) or (b)
28 expires, the effectiveness of the financing statement lapses. Under former Section
29 9-403(2), lapse was tolled if the debtor entered bankruptcy or another insolvency
30 proceeding. A few years ago, Bankruptcy Code § 362(b)(3) was amended to permit
31 a secured party to continue or maintain the perfected status of its security interest
32 without first obtaining relief from the automatic stay. Accordingly, subsection (c)
33 deletes the former tolling provision. It also contains bracketed language for the
34 Drafting Committee's consideration, to the effect that lapse occurs notwithstanding
35 the debtor's entry into insolvency proceedings. With or without the bracketed

1 language, this subsection imposes a new burden on the secured party: to be sure
2 that a financing statement does not lapse during the debtor's bankruptcy. The last
3 paragraph of the subsection addresses the effect of lapse. Of course, to the extent
4 that federal bankruptcy law dictates the consequences of lapse, the provisions of
5 this Article would be of no effect.

6 **4. Continuation Statements.** Subsection (d) explains when a continuation
7 statement may be filed. A continuation statement filed at a time other than that
8 prescribed by subsection (d) is ineffective. However, the filing office nevertheless
9 must accept it, unless the initial financing statement to which it relates has lapsed.
10 See Sections 9-521(a); 9-515(b). Subsection (e) specifies the effect of a
11 continuation statement and provides for successive continuation statements.

12 **SECTION 9-517. CONTENTS OF CONTINUATION STATEMENT.** A
13 continuation statement for a financing statement is an amendment of the a financing
14 statement that:

15 (1) complies in addition to complying with the requirements of Section
16 9-509(a); and

17 (2) indicates that it is a continuation statement for, or that it is filed to
18 continue the effectiveness of, the financing statement.

19 Reporters' Comments

20 **1. Source.** Former Section 9-403(3).

21 **2. Contents of Continuation Statement.** A continuation statement must
22 comply with the requirements for an amendment, see Section 9-509(a) and, in
23 addition, indicate that it is a continuation statement or that it has been filed to
24 continue the effectiveness of the financing statement to which it relates. Consistent
25 with the medium-neutral approach of Part 5, no signature is required for a
26 continuation statement.

27 **SECTION 9-518. EFFECT OF INDEXING ERRORS.**

28 (a) Except as otherwise provided in subsection (b), the failure of the filing
29 office to index a record correctly does not affect the effectiveness of the record.

30 (b) A filed but improperly indexed record is ineffective against a purchaser
31 of the collateral which gives value in reasonable reliance upon the apparent absence
32 of the record in from the files.

1 Reporters' Comments

2 **Discussion Question:** The Reporters' Comments to this section previously
3 observed:

4 This section and Section 9-515(d) raise questions that the Drafting
5 Committee has not yet fully addressed, including how to distinguish
6 reporting or processing errors, for which the filer should not be responsible,
7 from indexing errors, and how to deal with mis-indexed records that are re-
8 indexed correctly and vice versa.

9 Does the Drafting Committee prefer to resolve these questions itself or leave the
10 resolution to the courts?

11 1. **Source.** New.

12 2. **Protection for Reliance Parties.** Like a record that the filing office
13 refuses to accept, a record that the filing office accepts but mis-indexes affords no
14 public notice. This section treats a mis-indexed record much like Section 9-515(d)
15 treats a record that the filing office wrongfully refuses to accept. Generally, under
16 subsection (a), the filing office's error does not affect the effectiveness of the filing.
17 Cf. Section 9-515(a). However, under subsection (b), the filer (who knows how the
18 record should have been indexed and can verify whether in fact it was indexed
19 properly) runs the risk that a purchaser of the collateral will give value in reliance
20 upon the apparent absence of the record in the files. Cf. Section 9-515(d).

21 **SECTION 9-519. CLAIM CONCERNING INACCURATE OR**
22 **WRONGFULLY FILED RECORD.**

23 (a) A person may file with the filing office a correction statement with
24 respect to a record indexed there under the person's name if the If a person believes
25 that a the record indexed under the person's name with the filing office is inaccurate
26 or was wrongfully filed, ~~the person may file with the filing office a correction~~
27 ~~statement with respect to the record.~~

28 (b) A correction statement must:

29 (1) identify the record to which it relates by the file number assigned to
30 the initial financing statement to which the record relates ~~under Section 9-520(a)~~ or,
31 if the ~~initial financing statement was filed before the effective date of this article~~
32 file number does not itself indicate the date of filing, by the date of filing and file
33 number;

1 (2) indicate that it is a correction statement; and
2 (3) (A) provide the basis for the person's belief that ~~a~~ the record ~~is~~
3 ~~inaccurate or~~ was wrongfully filed; ~~and or~~
4 (B) provide the basis for the person's belief that the record is
5 inaccurate and indicate the manner in which the person believes the record should
6 be amended to cure any inaccuracy.
7 (c) The filing of a correction statement does not affect the effectiveness of
8 the initial financing statement or other record [relating to it] [to which it relates].

9 Reporters' Comments

10 **Discussion Questions:**

11 A. Should the "correction statement" approach be retained, or should
12 the approach adopted with respect to debtor-initiated termination statements (see §
13 9-508(c), (g)) be expanded to cover mistakes and overbreadth? I.e., should the
14 debtor be able to file an effective amendment that deletes collateral not covered by
15 a security agreement and not otherwise properly included in a financing statement?

16 B. What if the error relates not to the debtor but to an assignment?
17 Should the approach adopted with respect to debtor-initiated termination statements
18 be expanded to cover errors in assignments. Suppose, for example, that the secured
19 party assigned its security interest in two items of collateral but the recorded
20 amendment reflects only one item. Should the assignee have the power to file an
21 effective amendment assigning of record the other item of collateral?

22 1. **Source.** New.

23 2. **Correction Statements.** Existing law affords no nonjudicial means for a
24 debtor to correct a financing statement or other record that is inaccurate or
25 wrongfully filed. Subsection (a) affords the debtor the right to file a correction
26 statement. The statement must give the basis for the debtor's belief that the public
27 record should be corrected. See subsection (b). The statement becomes part of the
28 "financing statement," as defined in Section 9-102; however, subsection (c)
29 provides that the filing does not affect the effectiveness of the initial financing
30 statement or other record to which it relates. These provisions resemble the
31 analogous remedy in the Fair Credit Reporting Act.

32 This section does not displace other provisions of this Article that impose
33 liability for making unauthorized filings or failing to file or send a termination
34 statement. See Section 9-624(d). Nor does it displace any available judicial
35 remedies.

36 3. **Resort to Other Law.** After having considered a variety of approaches
37 to this problem, the Drafting Committee concluded that Article 9 is unlikely to

1 provide a satisfactory or complete solution to problems caused by misuse of the
2 public records. The problem of “bogus filings is not limited to the UCC filing
3 system but extends to the real property records, as well. A summary judicial
4 procedure for correcting the public record and criminal penalties for those who
5 misuse the filing and recording systems are likely to be more effective and put less
6 strain on the filing system than provisions requiring action by the filing office.

7 [SUBPART 2. DUTIES AND OPERATION OF FILING OFFICE]

8 **SECTION 9-520. NUMBERING, MAINTAINING, AND INDEXING**
9 **RECORDS; COMMUNICATING INFORMATION CONTAINED IN**
10 **RECORDS.**

11 (a) For each record filed with a filing office, the filing office shall:

12 (1) assign a ~~file~~ unique number to the record ~~pursuant to Section 9-~~
13 ~~520A;~~

14 (2) create a record that bears the ~~file~~ number assigned to the record and
15 the date and time of filing;

16 (3) maintain the filed record for public inspection;

17 (4) index the record in accordance with subsections (b), (c), and (d);

18 and

19 (5) communicate the [information contained in the record] [the fact that
20 the record has been filed with the filing office] to each person whose name was
21 provided as the name of the debtor or secured party or representative of the secured
22 party in the financing statement to which the record relates and to the person that
23 filed the record with the filing office.]

24 (b) Except as otherwise provided in subsections (c) and (d):

25 (1) the filing office shall index {an initial financing statement} {and an
26 amendment that changes the name of the debtor} [a financing statement] according
27 to the name of the debtor and shall index all filed records relating to the initial

1 financing statement in a manner that associates with one another an initial financing
2 statement and all filed records relating to the initial financing statement; and

3 (2) the filing office shall index a record that provides a name of a debtor
4 which was not previously provided in the financing statement to which the record
5 relates also according to the name that was not previously provided.

6 (c) If a financing statement is filed as a fixture filing or covers timber to be
7 cut or as-extracted collateral, [it must be filed for record and] the filing office shall
8 index it:

9 (1) under the names of the debtor and of each owner of record shown on
10 the financing statement as if they were the mortgagors under a mortgage of the real
11 property described; and

12 (2) to the extent that the law of this State provides for indexing of
13 mortgages under the name of the mortgagee, under the name of the secured party as
14 if the secured party were the mortgagee thereunder, or, if indexing is by description,
15 as if the financing statement were a mortgage of the real property described.

16 (d) If a financing statement is filed as a fixture filing or covers timber to be
17 cut or as-extracted collateral, the filing office shall index an assignment filed under
18 Section 9-512(a) or an amendment filed under Section 9-512(b):

19 (1) under the name of the assignor as grantor; and

20 (2) to the extent that the law of this State provides for indexing the
21 assignment of a real property mortgage under the name of the assignee, ~~the filing~~
22 ~~office shall index the assignment or the amendment~~ under the name of the assignee.

23 (e) The filing office shall maintain a storage and retrieval capability that:

24 (1) provides for retrieval of a record by the name of the debtor and by
25 the file number assigned to initial financing statement to which the record relates;
26 and

1 (2) associates with one another an initial financing statement and each
2 filed record relating to the initial financing statement.

3 (f) The filing office shall not remove a debtor's name from the index [until
4 the effectiveness of a financing statement naming the debtor lapses under Section 9-
5 516(a) with respect all secured parties of record].

6 (f g) The filing office shall perform the acts required by subsections (a)
7 through (d) at the time and in the manner prescribed by rule, but not later than two
8 business days after the filing office receives the record in question.

9 *Legislative Note: In States in which writings will not appear in the real property*
10 *records and indices unless actually recorded the bracketed language in subsection*
11 *(c) should be used.*

12 Reporters' Comments

13 **Changes from Prior Draft:**

14 A. The changes to subsection (a), together with the change to Section 9-
15 520A, make clear that although the filing office assigns a number to every filed
16 record, it assigns a "file number" only to an initial financing statement.

17 B. New subsection (b)(2) requires the filing office to index amendments
18 changing the debtor's name or adding a new debtor under the changed or new name
19 as well as the old name.

20 C. New subsection (f) makes clear that a debtor's name is not to be
21 removed from the index until it has lapsed with respect to all secured parties of
22 record. This will prevent removal when the debtor's name is amended. Deletion of
23 the bracketed language would prohibit removal of a debtor's name, even upon
24 lapse, thereby giving searchers access to lapsed financing statements. See also
25 Changes to § 9-522 and § 9-523.

26 **Discussion Question:**

27 We have received correspondence from filing officers and users arguing
28 that the potential benefits do not justify the significant burdens and costs that
29 paragraph (a)(5) imposes on filing offices. Should paragraph (a)(5) be deleted?

30 1. **Source.** Former Sections 9-403(4), (7); 9-405(2).

31 2. **Filing Office's Duties.** Subsections (a) through (d) set forth the duties
32 of the filing office with respect to filed records. Subsection (e) requires the filing
33 office to maintain appropriate storage and retrieval facilities.

1 3. **Time of Filing.** Subsection (a) and § 9-523 refer to the “date and time
2 of filing. The statutory text does not contain any instructions to a filing office as to
3 how the time of filing is to be determined. The method of determining or assigning
4 a time of filing is an appropriate matter for the administrative rules to address.

5 4. **Information from Filing Office.** In an effort to reveal the fact of
6 unauthorized filings as soon as practicable, subsection (a)(5) adds a requirement
7 that the filing office inform affected persons of each record filed. Rather than
8 specify the persons that would be “affected by a particular record, subsection (a) in
9 effect deems all debtors and secured parties of record to be affected by every record
10 relating to a financing statement. This approach is easier to understand and
11 administer.

12 The draft contains two alternatives for the information that the filing office
13 is to communicate. The first requires the filing office to communicate all of the
14 information contained in the record. For example, a photocopy of a written record
15 would satisfy that requirement. The second alternative is less burdensome, but
16 nevertheless might be adequate to accomplish the purpose of policing unauthorized
17 filings. It would require the filing office to communicate only the fact that the
18 record had been filed. For example, the second alternative would be satisfied by
19 the following statement, communicated in writing or otherwise:

20 Please take note that a record was filed with this office as indicated below:

21 Date and time of filing: January 2, 1999

22 File No. of initial
23 financing statement 123456

24 Type of record: Amendment

25 Debtor’s name: ABC Corp.

26 Debtor’s address XXX XXXX
27 YYY, YYYY

28 Secured party’s name: XYZ Finance Co.

29 Secured party’s address XXX XXXX
30 YYY, YYYY

31 The details of the information to be specified might be left to the Rules.

32 4. **Prohibition on Deleting Names from Index.** This article contemplates
33 that[, except upon lapse with respect to all secured parties of record,] the filing
34 office never deletes the name of a debtor from the index. See subsection (f). This
35 rule applies even to an amendment purporting to delete or modify the name of a
36 debtor or terminate the effectiveness of the financing statement. Note that if an
37 amendment provides a modified name for a debtor, the amended name should be
38 added to the index, see subsection (b)(2), but the pre-amendment name should
39 remain. The same principles apply with respect to names of secured parties.

1 **5. Standard of Performance.** Subsection (g) is new. It imposes a
2 minimum standard of performance. Prompt indexing is crucial to the effectiveness
3 of any filing system. An accepted but un-indexed record affords no public notice.

4 **SECTION 9-520A. ~~ASSIGNMENT OF FILE NUMBER.~~**

5 [(a)] “File number” means the number assigned to an initial financing
6 statement ~~A file number assigned to a record~~ [pursuant to Section 9-520(a)(1)].

7 [(b) A file number must be unique and contain at least three separate
8 segments in the following order:

9 (1) The first segment must indicate, in numbers, the date of filing;

10 (2) The second segment must consist of a number that is assigned
11 sequentially based on the order in which records are filed on each business day.

12 (3) The third segment must consist of [an algorithmically derived] [a]
13 verification number based on the numbers assigned pursuant to paragraphs (1) and
14 (2).]

15 Reporters’ Comments

16 **Changes from Prior Draft:**

17 A. Subsection (a) defines the term “file number.” As the draft uses the
18 term, although the filing office assigns a unique number to every record, that
19 number is the “file number” only if the record is an initial financing statement. The
20 definition might need to be relocated.

21 B. Subsection (b) has been bracketed to raise the question whether it should
22 take effect with the rest of the article or should be revised to allow more time for
23 filing offices to conform their numbering systems.

24 1. **Source.** New.

25 2. **File Numbers.** This section prescribes a uniform method of assigning
26 file numbers to records. The Drafting Committee has yet to review it.

27 **SECTION 9-521. ACCEPTANCE AND REFUSAL TO ACCEPT**
28 **RECORD.**

1 (a) ~~Subject to subsections (c) and (d),~~ [Except as otherwise provided in
2 subsections (c) and (d),] a filing office shall refuse to accept a record for filing for a
3 reason set forth in Section 9-515(b) and may refuse to accept a record for filing only
4 for a reason set forth in Section 9-515(b).

5 (b) (1) If a filing office refuses to accept a record for filing, it shall
6 communicate the fact of and reason for its refusal to the person that presented the
7 record.

8 (2) The communication must be made at the time and in the manner
9 prescribed by rule, but in no event more than two business days after the filing
10 office receives the record.

11 (c) ~~[The filing office]~~ [A filing office that accepts written records] may not
12 refuse to accept a written initial financing statement in the following form except
13 for a reason set forth in Section 9-515(b):

1 (d) [The filing office] [A financing statement that accepts written records]
2 may not refuse to accept a written record in the following form except for a reason
3 set forth in Section 9-515(b):

Change from Prior Draft: The brackets and bracketed language raise the question whether a filing office that does not accept paper-based financing statements should be obliged nevertheless to accept the national financing statement forms in this section.

1. **Source.** New.

2. **Refusal to Accept a Record for Filing.** In some States, filing offices have considered themselves obligated to review the form and content of a financing statement and to refuse to accept those that they determine are legally insufficient. Some filing offices impose requirements for or conditions to filing that do not appear in the statute. Under this section, the filing office would not be expected to make legal judgments and would not be permitted to impose additional conditions or requirements.

Subsection (a) both prescribes and limits the bases upon which the filing office must and may reject records by reference to the reasons set forth in Section 9-515(b). For the most part, the bases for rejection are limited to those that prevent the filing office from dealing with a record that it receives—because some the requisite information (e.g., the debtor's name) is missing or cannot be deciphered, because the record is not communicated by a method or medium that the filing office accepts (e.g., it is mime-, rather than uu-encoded), or because the filer fails to tender an amount equal to or greater than the filing fee.

3. **Consequences of Accepting a Rejectable Record.** Section 9-515(b) includes among the reasons for rejection of an initial financing statement the failure to give certain information that is not required as a condition of effectiveness. In conjunction with Section 9-515(b)(5), this section requires the filing office to refuse to accept an otherwise legally sufficient financing statement that does not contain a mailing address for the debtor, does not disclose whether the debtor is an individual or an organization (e.g., a partnership or corporation) or, if the debtor is an organization, does not give specific information concerning the organization. The information required by Section 9-515(b)(5) assists searchers in weeding out “false positives,” i.e., records that a search reveals but which do not pertain to the debtor in question. It assists filers by helping to insure that the debtor's name is correct and that the financing statement is filed in the proper jurisdiction.

If the filing office accepts a financing statement that does not give this information at all, the filing is fully effective. Section 9-515(c). The financing statement generally is effective if the information is incorrect; however, the security interest is subordinate to the rights of a purchaser who gives value in reasonable reliance upon the incorrect information. Section 9-335.

4. **Filing Office's Duties with Respect to Rejected Record.** Subsection (b) requires the filing office to communicate the fact of rejection and the reason therefor within a fixed period of time. Inasmuch as a rightfully rejected record is ineffective and a wrongfully rejected record is not fully effective, prompt communication concerning any rejection is important.

5. **“Safe Harbor” Written Forms.** Although subsection (a) limits the bases upon which the filing office can refuse to accept records, subsections (c) and (d) provide sample written forms that would be acceptable in every filing office in the country. By using one of the statutory forms, a secured party could be certain that the filing office is obligated to accept every record it presents, even if the filing office’s Rules permit it to reject written communications. The formatting of the forms has been designed to reduce error by both filers and filing offices.

The forms in subsection (c) are based upon national financing statement forms that already are in use. Those forms were developed over an extended period and reflect the comments and suggestions of filing officers, secured parties and their counsel (both directly and through organizations such as the American Bar Association), service companies, and the Drafting Committee. They are widely available from printers and search companies, and filing offices in a majority of States have undertaken to accept them, in most cases without any extra or non-standard filing fee.

The multi-purpose form in subsection (d) covers changes with respect to the debtor, the secured party, the collateral, and the status of the financing statement (termination and continuation).

SECTION 9-522. LAPSED FINANCING STATEMENTS.

(a) Except to the extent that a statute governing disposition of public records provides otherwise ~~for destruction at a later time~~, if a financing statement lapses under Section 9-516(a) with respect to all secured parties of record, the filing office immediately may destroy any written record evidencing the financing statement.

(b) If the filing office destroys a written record evidencing a financing statement, it shall maintain another record of the financing statement which is retrievable by using [the name of the debtor or by using the] file number assigned to the initial financing statement to which ~~of~~ the destroyed record relates.

Reporters' Comments

Discussion Question: Is the bracketed language in subsection (b), which would permit a filing office to locate lapsed financing statements filed against a specified debtor, desirable? See § 9-523(b) and Reporters' Comment 4.

1. Source. Former Section 9-403(3).

2. **Retention of Written Records.** This section has been revised to clarify that the filing office may destroy written records evidencing a financing statement

1 only if it has lapsed under Section 9-516(a). Until a financing statement lapses
2 under Section 9-516(a), the filing office remains responsible to maintain the written
3 records and to provide information under Section 9-523, even though the financing
4 statement has been terminated under Section 9-511.

5 **SECTION 9-523. INFORMATION FROM FILING OFFICE; SALE OR**
6 **LICENSE OF RECORDS.**

7 (a) If a person filing a written record furnishes a copy to the filing office,
8 the filing office upon request shall:

9 (1) (A) note upon the copy:

10 (i) the ~~file~~ number assigned to the record pursuant to Section 9-
11 520(a)(1); and

12 (ii) the date and time of the filing of the original; and

13 (B) deliver or send the copy to the person; or

14 (2) send to the person an image of the record showing the ~~file~~ number
15 assigned to the record pursuant to Section 9-520(a)(1) and the date and time of the
16 filing of the original.

17 **Subsection (b)--Alternative A**

18 (b) The filing office shall communicate the following information to any
19 person that requests it:

20 (1) whether there is on file on a date and time specified by the filing
21 office, but not a date earlier than three business days before the filing office
22 receives the request, any financing statement that:

23 (A) designates a particular debtor [or, if the request so states,
24 designates a particular debtor at the address specified in the request]; and

25 (B) has not lapsed under Section 9-516(a) with respect to all secured
26 parties of record[, and, if the request so states, has lapsed under Section 9-516(a)];

27 (2) the date and time of filing of each financing statement; and

1 (3) the information contained in each financing statement.

2 **Subsection (b)--Alternative B**

3 (b) The filing office shall communicate the following information to any
4 person that requests it:

5 (1) whether there is on file on a date and time specified by the filing
6 office, but not a date earlier than three business days before the filing office
7 receives the request, any financing statement that:

8 (A) designates a particular debtor [or, if the request so states,
9 designates a particular debtor at the address specified in the request]; and

10 (B) has not lapsed under Section 9-516(a) with respect to all secured
11 parties of record[, and, if the request so states, has lapsed under Section 9-516(a)];

12 (2) the date and time of filing of each financing statement; and

13 (3)[(A)] the information contained in each financing statement; [or

14 (B) if the request so states, [with respect to each record ~~included in~~
15 comprising the financing statement:

16 (i) the ~~file~~ number ~~of~~ assigned to the record pursuant to Section
17 9-520(a)(1);

18 (ii) the names and addresses of the debtor and secured party
19 provided in the record; and

20 (iii) whether the record is an initial financing statement or an
21 amendment] [a reasonable summary of the information (other than an indication of
22 collateral) contained in the record].

23 (c) In complying with its duty under subsection (b), the filing office may
24 communicate information in any medium. However, if requested, the filing office
25 shall communicate information by issuing [its written certificate] [a record that can

1 be admitted into evidence in the courts of this State without extrinsic evidence of its
2 authenticity].

3 (d) At least weekly, the [insert appropriate official or governmental agency]
4 [filing office] shall sell or license to the public on a nonexclusive basis, in bulk,
5 copies of all records filed with it under this part, in every medium from time to time
6 available to the filing office.

7 (e) The filing office shall perform the acts required by subsections (a) and
8 (b) at the time and in the manner prescribed by rule, but not later than two business
9 days after the filing office receives the request.

10 *Legislative Note: States whose filing office responds to search requests limited to a*
11 *particular address should adopt the bracketed language in subsection (b)(1).*

12 Reporters' Comments

13 1. **Source.** Former Section 9-407; subsections (d) and (e) are new.

14 2. **Filing Office's Duty to Provide Information.** Former Section 9-407,
15 dealing with obtaining information from the filing office, was bracketed to suggest
16 to legislatures that its enactment was optional. Experience has shown that the
17 method by which interested persons can obtain information concerning the public
18 records should be uniform. Accordingly, the analogous provisions of this Article
19 are not in brackets. This section reflects the policy that only lapsed financing
20 statements will be removed from the records; terminated financing statements will
21 remain part of the filing office's data base. See the Comment to Section 9-522,
22 above.

23 Most of the other changes from former Section 9-407 are for clarification, to
24 embrace medium-neutral drafting, or to impose standards of performance on the
25 filing office.

26 3. **Information that Must Be Provided.** The draft presents alternative
27 approaches to defining the information that the filing office must provide.
28 Subsection (b), Alternative A, requires the filing office to provide "the information
29 contained in each financing statement to a person who requests it. However, this
30 alternative does not in any manner restrict the filing office from offering to provide
31 less than all of the information (presumably for a lower price) to a person who asks
32 for less. The Official Comments could be expanded to make it quite clear that the
33 statute accommodates the current practice of providing only the filing number, date
34 and time of filing, and names and addresses of the debtor and secured party when a
35 requesting person asks for no more (i.e., when the person does not ask for copies of
36 financing statements).

1 Alternative B provides an explicit statutory treatment of requests for less
2 than all information contained in a financing statement. Alternative B itself
3 contains two alternatives. One specifies the more limited information that the filing
4 office must provide when requested; the other requires that it provide only a
5 “reasonable summary. In the interest of brevity and flexibility, we prefer
6 Alternative A with an expanded official comment.

7 **4. Lapsed Financing Statements.** Each alternative of subsection (b)(1)(B)
8 contains a bracketed provision that would require a filing office to conduct a search
9 and report as to lapsed financing statements, when requested.

10 **5. Search by Debtor’s Address.** Both alternatives of subsection (b)(1)(A)
11 contemplate that, by making a single request, a searcher will receive the results of a
12 search of the entire public record maintained by any given filing office. Under
13 current practice, some filing offices routinely limit their searches (and reports of
14 search results) to financing statements showing a particular address for the debtor.
15 The bracketed language in subsection (b)(1)(A) would permit a limited search
16 report of this kind, but only if the search request is so limited. With or without the
17 bracketed language, this subsection does not permit the filing office to compel a
18 searcher to limit a request by address.

19 **6. Medium of Communication; Certificates.** The former statute provides
20 that the filing office respond to a request for information by providing a certificate.
21 The principle of medium-neutrality would suggest that the statute not require a
22 written certificate. However, official written certificates might be introduced into
23 evidence more easily than official communications in another medium. The
24 bracketed language in subsection (c) recognizes that there may be satisfactory
25 alternatives to a filing office’s “written certificate. We are exploring this area with
26 some experts on evidence; this language is illustrative only. In addition, by
27 permitting communication “in any medium, subsection (c) is not inconsistent with
28 a system (e.g., as in New Mexico) in which persons other than filing office staff
29 conduct searches of the filing office’s (computer) records.

30 **7. Performance Standard.** In some States, filing offices take weeks to
31 respond to requests for information. In some States, requests are filled using
32 information that is weeks old. The utility of the filing system depends on the ability
33 of searchers to get current information quickly. Accordingly, subsection (e)
34 requires that the filing office respond to a request for information no later than two
35 business days after it receives the request. The information contained in the
36 response must be current as of a date no earlier than three business days before the
37 filing office receives the request. See subsection (b)(1). The Official Comments
38 will be revised to explain that the failure of the filing office to comply with
39 performance standards, such as subsection (e), has no effect on the private rights of
40 persons affected by the filing of records.

41 **8. Sales of Records in Bulk.** Subsection (d), which is new, mandates that
42 the appropriate official or the filing office sell or license the filing records to the
43 public in bulk, on a nonexclusive basis, in every medium available to the filing
44 office. The details of implementation are left to the administrative rules.

SECTION 9-524. DELAY BY FILING OFFICE. Delay by the filing office beyond the time limits prescribed in this part is excused if:

(1) the delay is caused by interruption of communication or computer facilities, war, emergency conditions, failure of equipment, or other circumstances beyond control of the filing office; and

(2) the filing office exercises reasonable diligence under the circumstances.

Reporters' Comment

Source. New; derived from Section 4-109.

[SECTION 9-525. REGISTERED AGENT.

[Intentionally omitted]

Reporters' Comments

1. **Source.** New.

2. **Registered Agent.** The Reporters distributed to the Drafting Committee a proposal under which a State would permit each debtor to select a “registered agent” to maintain financing statements and other Article 9 records pertaining to the debtor. Pending the Drafting Committee’s determination whether it wishes to pursue that proposal, the Reporters have not prepared the draft statutory text that would be needed to give effect to the proposal.

1 (C) ~~[plus in each case, if the financing statement is subject to the~~
2 ~~second sentence of Section 9-502(a), of the kind described in Section 9-502(b)(1), \$~~
3 _____; and]

4 (2) ~~The fee for~~ each name more than ~~one~~ two required to be indexed [, if
5 the record is communicated in writing,] is \$ _____;

6 (3) ~~The fee for~~ filing a financing statement stating an extended period of
7 effectiveness under Section 9-502(b) is [\$____, if the period of effectiveness is 10
8 years, \$____, if the period of effectiveness is 20 years, and \$____, if the period of
9 effectiveness is 30 years]; and

10 (4) ~~[The fee for~~ filing a written record in a form other than as set forth in
11 Sections 9-521(c) and (d) may not be less than the fee charged for filing a written
12 record of the same kind in the form set forth in those sections.]

13 (b) [No fee is required for the filing of ~~With reference to~~ a mortgage filed
14 as a financing statement, ~~a fee is not required~~ other than the regular recording and
15 satisfaction fees with respect to the mortgage.]

16 (c) The fee for responding to a request for information from the filing
17 office, including for [issuing a certificate showing] [communicating] whether there
18 is on file any financing statement naming a particular debtor, is

19 (1) \$ ____ if the request is communicated in writing; and

20 (2) \$ ____ if the request is communicated by another medium
21 authorized by rule.]

22 *Legislative Note: A State may wish to consolidate the provisions of this section*
23 *with statutes setting fees for other services.*

24 Reporters' Comments

25 **Changes from Prior Draft:** Bracketed language in subsection (a) raises
26 the questions whether (1) the draft should mandate a lower fee for as an incentive to
27 file electronically, (2) whether the draft should mandate a higher fee for longer
28 written records than for shorter ones, (3) whether the additional charge for multiple
29 debtors should apply to more than more than two debtors, rather than more than

1 one, and (4) whether the additional charge for more than multiple debtors should
2 apply only with respect to written records. We are inclined to answer each question
3 in the affirmative.

4 1. **Source.** Various sections of former Part 4.

5 2. **Fees.** This section contains all fee requirements for filing and for
6 responding to requests for information. Subsection (a)(4) is intended to discourage
7 filing offices from favoring a local “standard form” over the national forms set forth
8 in subsections (c) and (d) of Section 9-521. The entire section is bracketed to
9 indicate that a States may wish to consolidate its provisions with statutes setting
10 fees for other services.

11 **SECTION 9-528. ADMINISTRATIVE RULES.**

12 (a) The [insert appropriate official or governmental agency] [filing office]
13 shall adopt rules to carry out the provisions of this article. The rules must be:

14 (1) consistent with this article[; and

15 (2) ~~must be~~ adopted in accordance with the [insert any applicable state
16 administrative procedure act].

17 (b) To keep the rules and practices of the filing office in harmony with the
18 rules and practices of filing offices in other jurisdictions that enact substantially this
19 part, and to keep the technology used by the filing office compatible with the
20 technology used by filing offices in other jurisdictions that enact substantially this
21 part, the filing office, so far as is consistent with the purposes, policies, and
22 provisions of this article, shall in ~~(1) before~~ adopting, amending, and repealing
23 rules:

24 (1) consult with filing offices in other jurisdictions that enact
25 substantially this part; and

26 (2) consult the most recent version of the Model Rules promulgated by
27 the International Association of Corporate Administrators or any successor
28 organization; and

(3) ~~in adopting, amending, and repealing rules,~~ take into consideration the rules and practices of, and the technology used by, filing offices in other jurisdictions that enact substantially this part.

Reporters' Comments

1. **Source.** New. Subsection (b) derives in part from the Uniform Consumer Credit Code (1974).

2. Rules Required. Operating a filing office is a complicated business, requiring many more rules and procedures than this Article usefully can provide. Subsection (a) requires the adoption of administrative rules to carry out the provisions of Article 9. The rules must be consistent with the provisions of the statute and adopted in accordance with local procedures.

3. **Importance of Uniformity.** In today's national economy, uniformity of the policies, practices, and technology of the filing offices will reduce the costs of secured transactions substantially. The International Association of Corporate Administrators (IACA), referred to in subsection (b), is an organization whose membership includes filing officers from every State. These individuals are responsible for the proper functioning of the Article 9 filing system. IACA has been working with liaisons from the Drafting Committee to develop workable statutory provisions as well as model administrative rules, all with a view toward efficiency and uniformity.

SECTION 9-529. DUTY TO REPORT.

(a) The [insert appropriate official or governmental agency] [filing office] shall report [annually on or before _____] to the [Governor and Legislature] on the operation of the filing office.

(b) The report must contain a statement of the extent to which:

(1) the filing office has complied with the time limits prescribed in this part and the reasons for any noncompliance;

(2) ~~a statement of the extent to which~~ the rules are not in harmony with the rules of filing offices in other jurisdictions that enact substantially this part and the reasons for these variations; and

(3) ~~a statement of the extent to which the rules are not in harmony with~~
the most recent version of the Model Rules promulgated by the International

1 Association of Corporate Administrators or any successor organization and the
2 reasons for these variations.

3 Reporters' Comments

4 1. **Source.** New; derived in part from the Uniform Consumer Credit Code
5 (1974).

6 2. **Duty to Report.** This section is designed to promote compliance with
7 the standards of performance imposed upon the filing office and with the
8 requirement that the filing office's policies, practices, and technology be consistent
9 and compatible with the policies, practices, and technology of other filing offices.

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PART 6
DEFAULT

[SUBPART 1. DEFAULT AND ENFORCEMENT OF SECURITY INTEREST]

**SECTION 9-601. RIGHTS AND REMEDIES AFTER DEFAULT;
JUDICIAL ENFORCEMENT; CONSIGNOR OR BUYER OF ACCOUNTS,
CHATTEL PAPER, OR PAYMENT INTANGIBLES; CERTAIN
STATUTORY LIENS.**

(a) After default, a secured party has the rights and remedies provided in this part and, except as otherwise provided in Section 9-602(a), those provided by agreement of the parties. A secured party may reduce the claim to judgment, foreclose, or otherwise enforce the claim, security interest, or agricultural lien by any available judicial procedure. If the collateral is documents, a secured party may proceed either as to the documents or as to the goods they cover. [A secured party in possession has the rights, remedies, and duties provided in Section 9-207.] The rights and remedies referred to in this subsection are cumulative and may be exercised simultaneously.

(b) Except as otherwise provided in subsection (d) and Section 9-605, after default, a debtor and an obligor have the rights and remedies provided in this part [and] [,] by agreement of the parties[, and in Section 9-207].

(c) If a secured party has reduced its claim to judgment, the lien of any levy that may be made upon the collateral by virtue of an execution based upon the judgment relates back to the earliest of the date of perfection of the security interest or agricultural lien in the collateral, the date of filing a financing statement covering the collateral, or any date specified in a statute under which the agricultural lien was

1 created. A sale pursuant to the execution is a foreclosure of the security interest or
2 agricultural lien by judicial procedure within the meaning of this section. A
3 secured party may purchase at the sale and thereafter hold the collateral free of any
4 other requirements of this article.

5 (d) Except as otherwise provided in Sections 9-607(d), 9-608(b), and 9-
6 614(e), the duties of a secured party under this part do not apply to a secured party
7 that is a consignor or is a buyer of accounts, chattel paper, or payment intangibles.

8 (e) This part applies to an agricultural lien but not to any other statutory
9 lien.

10 Reporters' Comments

11 1. **Source.** Former Section 9-501(1), (2), (5); subsections (d) and (e) are
12 new.

13 2. **When Remedies Arise.** Under subsection (a) the secured party's
14 remedies arise "[a]fter default. Like former Section 9-501, this Article leaves the
15 agreement of the parties to define the circumstances giving rise to a default. This
16 Article does not determine whether a secured party's post-default conduct can
17 constitute a waiver of default in the face of an agreement stating that such conduct
18 shall not constitute a waiver. Rather, it continues to leave to the parties' agreement,
19 as supplemented by non-UCC law, the determination whether a default has
20 occurred. See Section 1-103.

21 3. **Cumulative Remedies.** Former Section 9-501(1) provides that the
22 secured party's remedies are cumulative but does not explicitly provide whether the
23 remedies may be exercised simultaneously. The last sentence of subsection (a)
24 permits the simultaneous exercise of remedies if the secured party acts in good
25 faith. The liability scheme of Subpart 2 affords redress to an aggrieved debtor or
26 obligor. Moreover, subsection (a) does not override non-UCC law, including the
27 law of tort and statutes regulating collection of debts, which would render a creditor
28 liable for abusive behavior or harassment.

29 4. **Judicial Enforcement.** Subsection (c) generally follows former Section
30 9-501(5). The principal change provides that a levy relates back to the earlier of the
31 date of filing or the date of perfection. This provides a secured party that enforces
32 its security interest by levy with the benefit of the "first-to-file-or-perfect" priority
33 rule of Section 9-319(a)(1).

34 5. **Sales of Receivables.** New subsection (d) provides that, except as
35 provided in the sections that it mentions, the duties imposed on secured parties do
36 not apply to buyers of accounts, chattel paper, or payment intangibles. Although
37 denominated "secured parties," these buyers normally own the entire interest in the
38 property sold and so may enforce their rights without regard to the seller ("debtor").

1 **6. Consignments.** This Article is inapplicable to the true consignor's
2 enforcement of its ownership interest. See subsection (d). However, this Article
3 does govern cases in which the ownership interest of the true consignor is
4 subordinate to the rights of the consignee's secured party. We have yet to draft a
5 rule governing this situation. An appropriate rule might be that an enforcing senior
6 secured party must pay all of the excess proceeds to the junior consignor-owner.

7 **7. Statutory Liens.** Part 6 does not apply to statutory liens other than
8 agricultural liens. For the most part, this Part provides parallel treatment for the
9 enforcement of agricultural liens and security interests. Several minor changes to
10 former Part 6 were necessary to accomplish this result. For example, inasmuch as
11 there normally would not be a security agreement in connection with an agricultural
12 lien, subsections (a) and (b) change the references to the "security agreement" to the
13 "agreement of the parties" as a source of rights and remedies.

14 Because agricultural liens are statutory rather than consensual, this Article
15 does draw a few distinctions between the liens and security interests. Under
16 subsection (c), the statute creating an agricultural lien would govern whether and
17 the date to which an execution lien relates back. Section 9-606 explains when a
18 "default" occurs in the agricultural lien context.

1 **SECTION 9-602. WAIVER AND VARIANCE OF RIGHTS AND**
2 **DUTIES.**

3 (a) To the extent that they give rights to a debtor or an obligor and impose
4 duties on a secured party, the rules stated in the following sections may not be
5 waived or varied by a debtor or by a consumer obligor in a consumer goods secured
6 transaction, except as expressly provided in Section 9-623:

7 (1) Section 9-607(~~d~~ e)[, which deals with collection and enforcement of
8 collateral];

9 (2) Sections 9-610(b), 9-611, and 9-613[, which deal with disposition of
10 collateral];

11 (3) Section 9-609 insofar as it imposes upon a secured party that takes
12 possession of collateral without judicial process the duty to do so without breach of
13 the peace;

14 (4) Sections ~~9-607(d)~~ 9-608(a) and 9-614(c) insofar as they deal with
15 application or payment of noncash proceeds of collection, enforcement, or
16 disposition;

17 (5) Sections ~~9-607(d)~~, 9-608(a), and 9-614(d) insofar as they require
18 accounting for or payment of surplus proceeds of collateral;

19 (6) Section 9-614(e)[, which deals with calculation of a deficiency or
20 surplus when the proceeds of a disposition are unreasonably low];

21 (7) Section 9-618, 9-619, or 9-620[, which deal with acceptance of
22 collateral in satisfaction of obligation];

23 (8) Section 9-621[, which deals with redemption of collateral];

24 (9) Section 9-622[, which deals with reinstatement of obligations];

25 (10) Section 9-623[, which deals with permissible waivers];

1 (11) Sections 9-624, 9-625, and 9-628[, which deal with the secured
2 party's liability for failure to comply with this article]; and

3 (12) Section 9-209[, which deals with requests for an accounting and
4 requests concerning a list of collateral and statement of account].

5 (b) An obligor other than a consumer obligor in a consumer goods secured
6 transaction may waive or vary the rules referred to in subsection (a) to the extent
7 and in the manner provided by other law.

8 Reporters' Comments

9 **Discussion Question:** At the 1997 NCCUSL Annual Meeting the
10 Committee of the Whole adopted two sense of the house resolutions relating to
11 subsection (b). One was to the effect that the duty to give notifications to a
12 secondary obligor under Part 6 could not be waived. The other was to the effect
13 that subsection (b) should not override any Part 6 duties of "good faith, diligence,
14 reasonableness and care, which are made nonwaivable by current Section 1-103(3)
15 and draft Section 1-303(b). While this would not render subsection (b)
16 meaningless, it would mean that waivers of notice or, for example, commercial
17 reasonableness would be ineffective even if otherwise permitted under other law.
18 Inasmuch as these issues were debated at some length by the Drafting Committee,
19 we have not conformed the draft. Does the Drafting Committee wish us to do so?
20 (If so, then with regard to the second, we will consult with the Reporter for the
21 revision of Article 1 on how best to achieve the intended result.)

22 1. **Source.** Former Section 9-501(3).

23 2. **Waiver by Debtors.** Subsection (a) contains restrictions on waivers by
24 debtors. In an effort at clarification, this Article uses the term "waive or vary
25 instead of "renounc[e] or modify[]" which appears in former Section 9-504(3).
26 Subsection (a) revises former Section 9-501(3) by restricting the ability to waive or
27 modify additional rights and duties: (i) the duty to collect collateral in a
28 commercially reasonable manner (Section 9-607), (ii) the implicit duty to refrain
29 from a breach of the peace in taking possession of collateral under Section 9-609,
30 (iii) the duty to apply noncash proceeds of collection or disposition in a
31 commercially reasonable manner (Sections 9-602 and 9-614), (iv) the right to
32 reinstate a secured obligation in a consumer goods secured transaction (Section
33 9-622), (v) the right to limitations on the effectiveness of certain waivers (Section
34 9-623), and (vi) the right to a response to a request for an accounting, concerning a
35 list of collateral, or concerning a statement of account (Section 9-209). The
36 descriptions of the nonwaivable rights appear in brackets pending resolution of a
37 disagreement over style.

38 Subsection (a) provides generally that the specified rights and duties "may
39 not be waived or varied. However, the subsection does not restrict the ability of
40 parties to agree to settle or compromise claims for past conduct that may have

1 constituted a violation or breach of those rights and duties, even if the settlement
2 involves an express “waiver.”

3 **3. Waiver by Others.** The restrictions on waiver imposed in subsection (a)
4 relate to waivers by a debtor (defined in Section 9-102 as a person with a property
5 interest, other than a security interest or other lien, in the collateral) and an obligor
6 (whether or not a debtor) in a consumer goods secured transaction. Subsection (b)
7 provides explicitly that a waiver by an obligor other than a consumer obligor in a
8 consumer goods transaction is governed by non-UCC law. This is so
9 notwithstanding the first sentence of Section 1-102(3), which generally prohibits
10 disclaimers of the “obligations of good faith, diligence, reasonableness and care
11 prescribed by this Act. In this way, an obligor’s ability to waive is the same,
12 regardless of whether the obligation is incurred in connection with a secured
13 transaction under this Article.

14 Secondary obligors enjoy many of the same rights as debtors. However,
15 under subsection (b) a non-debtor obligor may waive all of its rights and all of the
16 secured party’s duties under Part 6 in accordance with other law. The waiver of
17 rights or duties by a secondary obligor does not prejudice the rights of a debtor. For
18 example, the debtor may assert its claims and defenses arising out of a secured
19 party’s noncompliance with Part 6 in an action brought by the secondary obligor
20 based on either reimbursement or subrogation. See Restatement (3d), Suretyship
21 and Guaranty §§ 24(1)(c); 28(1)(a)(1996).

22 To see the operation of subsection (b), consider the following examples:

23 **Example 1:** Corporation grants a security interest in its equipment to secure
24 a loan. President issues an unsecured guarantee of Corporation’s debt.
25 Corporation is the debtor, and President is the secondary obligor. Under
26 subsection (b), President may effectively waive notification of disposition to
27 the extent and in the manner prescribed by non-UCC law.

28 **Example 2:** Corporation is obligated to creditor. The debt is secured only
29 by equipment owned by Parent. Here, although Parent is a secondary
30 obligor, it also is the debtor. Corporation, the principal obligor, is neither
31 the debtor nor a secondary obligor. Although subsection (b) permits
32 Corporation to waive its rights and the secured party’s duties to the extent
33 and in the manner prescribed by non-UCC law, the secured party has no
34 duty to notify Corporation of a disposition. However, a purported waiver of
35 notification by Parent would be effective only if in writing after default
36 under Section 9-623(a).

37 **Example 3:** Child owes creditor a debt for a purchase money loan secured
38 by Child’s automobile. The automobile is used primarily for transportation
39 between home and the university Child attends. Parent has co-signed the
40 promissory note. Parent is a secondary obligor. Nevertheless, because
41 Parent is an obligor in a consumer goods secured transaction, subsection (b)
42 does not negate the restrictions on waiver imposed by subsection (a).

SECTION 9-603. AGREEMENT ON STANDARDS CONCERNING

RIGHTS AND DUTIES. The parties may determine by agreement the standards measuring the fulfillment of the rights of a debtor or obligor and the duties of a secured party, other than duties concerning taking possession of collateral without breach of the peace under Section 9-609, if the standards are not manifestly unreasonable.

Reporters' Comments

1. **Source.** Former Section 9-501(3).

2. Limitation on Ability to Set Standards. This section does not permit the parties to set standards measuring fulfillment of the secured party's duty to take collateral without breaching the peace.

**SECTION 9-604. PROCEDURE IF SECURITY AGREEMENT COVERS
REAL PROPERTY OR FIXTURES.**

(a) If a security agreement covers both personal and real property, a secured party may proceed:

(1) under this part as to the personal property without prejudicing any rights and remedies with respect to the real property; or

(2) as to both the personal and real property in accordance with the rights and remedies with respect to the real property, in which case the other provisions of this part do not apply.

(b) If a security agreement covers goods that are or become fixtures, a secured party, subject to subsection (c), may proceed under this part or in accordance with the rights and remedies with respect to real property, in which case the other provisions of this part do not apply.

(c) If a secured party with a security interest in fixtures has priority over all owners and encumbrancers of the real property, the secured party may, on default, subject to the other provisions of this part, remove the collateral from the real property. [Unless otherwise agreed, a] [A] secured party that removes collateral shall promptly reimburse any encumbrancer or owner of the real property, other than the debtor, for the cost of repair of any physical injury. The secured party need not reimburse the encumbrancer or owner for any diminution in value of the real property caused by the absence of the goods removed or by any necessity of replacing them. A person entitled to reimbursement may refuse permission to remove until the secured party gives adequate assurance for the performance of the obligation to reimburse.

Reporters' Comments

1. **Source.** Former Section 9-501(4); 9-313(8).

2. **Real-property-related Collateral.** Subsection (a) alters former Section 9-501(4) to make clear that a secured party who exercises rights under Part 6 does not prejudice any rights under real property law.

This Article does not address certain other real-property-related problems. In a number of States, the exercise of remedies by a creditor that is secured by both real property and non-real property collateral is governed by special legal rules. For example, under some anti-deficiency laws, creditors risk loss of rights against personal property collateral if they err in enforcing their rights against the real property. Under a “one-form-of-action” rule (or rule against splitting a cause of action), a creditor that judicially enforces a real property mortgage and does not proceed in the same action to enforce a security interest in personalty may (among other consequences) lose the right to proceed against the personalty. Obviously, statutes of this kind create impediments to Article 9 secured parties. Several approaches are available, including: (i) revise Article 9 to override any limitations contained in other law and (ii) continue to submit to other law. Pending a decision to the contrary by the Drafting Committee, we have opted for the latter approach.

3. **Fixtures.** Subsection (b) is new. It is intended to make clear that a security interest in fixtures may be enforced either under real property law or under any of the applicable provisions of Part 6, including sale or other disposition either before or after removal of the fixtures (see subsection (c)). Subsection (b) also serves to overrule cases holding that a secured party's only remedy after default is the removal of the fixtures from the real property. See, e.g., *Maplewood Bank & Trust v. Sears, Roebuck & Co.*, 625 A.2d 537 (N.J. Super. Ct. App. Div. 1993).

Former Section 9-313(8) affords to the secured party the right to remove fixtures under certain circumstances. This remedy, with minor modifications, now appears in subsection (c).

SECTION 9-605. UNKNOWN DEBTOR OR SECONDARY OBLIGOR.

A secured party owes no duty ~~under this article~~ based on its status as secured party to a person, or to a secured party or lienholder that has filed a financing statement against the person, unless the secured party knows that a person is a debtor or a secondary obligor, knows the identity of the person, and knows how to communicate with the person.

Reporters' Comments

Change from Prior Draft: The new language relieves a secured party not only from duties arising under this article, but also from duties arising under other law by virtue of the secured party's status as such.

1. **Source.** New.

2. Duties to Unknown Persons. This section relieves a secured party from duties to a debtor or secondary obligor and to a secured party or lienholder who has filed a financing statement against the debtor, if the secured party does not know about the debtor or secondary obligor. For example, a secured party may be unaware that the original debtor has sold the collateral subject to the security interest and that the new owner now is the debtor. This subsection should be read in conjunction with the exculpatory provisions in Section 9-627.

SECTION 9-606. TIME OF DEFAULT FOR AGRICULTURAL LIEN.

For purposes of this part, a default occurs in connection with an agricultural lien at the earlier of the time provided by agreement of the parties and the time at which the secured party becomes entitled to enforce the lien in accordance with the statute under which it was created.

Reporters' Comments

1. **Source.** New.

2. **Time of Default.** Remedies under this part become available upon the debtor's "default." See Section 9-601. This section explains when "default" occurs in the agricultural lien context. It requires one to consult the enabling statute to determine when the lienholder is entitled to enforce the lien.

SECTION 9-607. COLLECTION AND ENFORCEMENT BY SECURED PARTY.

(a) If so agreed, and in any event on default, a secured party may:

(1) notify an account debtor or other person obligated on collateral to make payment or otherwise render performance to or for the benefit of the secured party, whether or not a debtor had been making collections on or enforcing the collateral;

(2) take any proceeds to which the secured party is entitled under Section 9-313; and

(3) enforce the obligations of an account debtor or other person obligated on collateral[, including by exercising the rights and remedies of the debtor with respect to the obligation of the account debtor or other person obligated

1 on collateral to make payment or otherwise render performance to the debtor, and
2 with respect to any property that secures the obligations of the account debtor or
3 other person obligated on the collateral].

4 [(b) In order to exercise under subsection (a)(3) the rights of a debtor to
5 enforce nonjudicially any [mortgage/deed of trust] covering real property, a secured
6 party may [file/record] in the office in which the [mortgage/deed of trust] is
7 [filed/recorded] a copy of the security agreement that entitles the secured party to
8 exercise those rights and ~~an affidavit authenticated by the secured party~~ party's
9 sworn affidavit in recordable form stating that a default has occurred and that the
10 secured party is entitled to enforce nonjudicially the [mortgage/deed of trust].]

11 (c) If so agreed, and in any event on default:

12 (1) a secured party that holds a security interest in a deposit account
13 perfected by control under Section 9-109(a)(1) may apply the ~~funds in~~ balance of
14 the deposit account to the obligation secured by the deposit account; and

15 (2) a secured party that holds a security interest in a deposit account
16 perfected by control under Section 9-109(a)(2) or (3) may instruct the depository
17 institution to pay the ~~funds in~~ balance of the deposit account to or for the benefit of
18 the secured party.

19 (d) A secured party that is entitled [by agreement] to charge back
20 uncollected collateral or otherwise to full or limited recourse against the debtor or
21 against a secondary obligor and that undertakes to collect from or enforce an
22 obligation of an account debtor or other person obligated on collateral shall proceed
23 in a commercially reasonable manner. The secured party may deduct from the
24 collections reasonable expenses of collection and enforcement, including
25 reasonable attorney's fees and legal expenses incurred by the secured party.

26 Reporters' Comments

1 1. **Source.** Former Section 9-502; subsections (b) and (c) are new.

2 2. **Scope.** As a general matter Part 6 deals with the rights and duties of
3 debtors and secured parties following default. However, this section applies to the
4 collection and enforcement rights of secured parties whether or not a default has
5 occurred. Although seemingly anomalous, in practice it is not unusual for debtors
6 to agree that secured parties are entitled to collect and enforce rights against
7 account debtors prior to default.

8 This section permits a secured party to collect and enforce obligations
9 included in collateral in its capacity as a secured party. It is not necessary for a
10 secured party first to become the owner of the collateral pursuant to a disposition or
11 acceptance. However, the secured party's rights to collect from and enforce
12 collateral against account debtors and others obligated on collateral under
13 subsection (a) are subject to Sections 9-338, 9-404, 9-405, 9-406, 9-406A and other
14 applicable law. Neither this Article nor former Section 9-502 should be understood
15 to regulate the duties of an account debtor or other person obligated on collateral.
16 For example, the secured party may be unable to exercise the debtor's rights under
17 an instrument if the debtor is in possession of the instrument, or under a non-
18 transferable letter of credit if the debtor is the beneficiary. Unless a secured party
19 has control over letter-of-credit rights and is entitled to receive payment or
20 performance from the issuer or a nominated person under Article 5, its remedies
21 with respect to the letter of credit may be limited to the recovery of any identifiable
22 proceeds from the debtor. This section establishes only the baseline rights of the
23 secured party *vis-a-vis the debtor*—the secured party is entitled to enforce and collect
24 upon default or earlier if so agreed.

25 3. **Primary Changes.** The primary substantive changes to this section are:
26 (i) expansion of its application to collection and enforcement against all persons
27 obligated on collateral, not just account debtors; (ii) explicit provision for the
28 secured party's enforcement of the debtor's rights in respect of the account debtor's
29 (and other third parties') obligations; and (iii) provision for the secured party's
30 enforcement of support obligations with respect to those obligations (support
31 obligations are components of the collateral, see Section 9-203(d)).

32 4. **Rights Against Third Parties.** The rights of a secured party against an
33 account debtor or other third party under subsection (a) include the right to enforce
34 claims that the debtor may enjoy against others. The claims might include a breach
35 of warranty claim arising out of a defect in equipment that is collateral or a secured
36 party's action for an injunction against infringement of a patent that is collateral.
37 Those claims typically would be proceeds of original collateral under Section
38 9-313(a).

39 5. **Rights Against Real Property Mortgagor.** Subsection (b) addresses
40 the situation in which the collateral consists of a mortgage note. After the debtor's
41 (mortgagee's) default, the secured party (assignee) may wish to proceed with a
42 nonjudicial foreclosure of the real property mortgage securing the note but may be
43 unable to do so because it has not become the assignee of record. The
44 assignee/secured party may not have taken a recordable assignment at the
45 commencement of the transaction; perhaps the mortgage note in question was one
46 of hundreds assigned to the secured party as collateral. Having defaulted, the

1 mortgagee may be unwilling to sign a recordable assignment. This section enables
2 the secured party (assignee) to become the assignee of record by recording the
3 security agreement and an affidavit certifying default in the applicable real property
4 records. Of course, the secured party's rights derive from those of its debtor.
5 Subsection (b) would not entitle the secured party to proceed with a foreclosure
6 unless the mortgagor also is in default or the debtor (mortgagee) otherwise enjoyed
7 the right to foreclose. Brackets around the subsection indicate some doubt about
8 the desirability of the provision.

9 **6. Deposit Account Collateral.** New subsection (c) sets forth the self-help
10 remedy for a secured party whose collateral is a deposit account. Subsection (c)(1)
11 addresses the rights of a secured party that is the depository institution with which
12 the deposit account is maintained. That secured party automatically has control
13 under Section 9-109(a)(1). On default, and otherwise if so agreed, the depository
14 institution/secured party may apply the funds on deposit to the secured obligation.

15 If a security interest of a third party is perfected by control (Section
16 9-109(a)(2) or (a)(3)), the secured party may on default, and otherwise if so agreed,
17 instruct the depository institution to pay out the funds in the account. If the third
18 party has control under Section 9-109(a)(3), the depository institution is obliged to
19 obey the instruction because the secured party is its customer. See Section 4-401.
20 If the third party has control under Section 9-109(a)(2), the control agreement
21 determines the depository institution's obligation to obey.

22 If a security interest in a deposit account is unperfected, or is perfected by
23 filing by virtue of the proceeds rules of Section 9-313, the depository institution
24 ordinarily owes no obligation to obey the secured party's instructions. See Section
25 9-338. To reach the funds, the secured party must use an available judicial
26 procedure.

27 **7. Commercial Reasonableness.** Subsection (d) provides that the secured
28 party's collection and enforcement rights under subsection (a) must be exercised in
29 a commercially reasonable manner. These rights include the right to settle and
30 compromise claims against the account debtor, subject to the standard of
31 commercial reasonableness. The secured party's failure to observe the standard of
32 commercial reasonableness could render it liable to an aggrieved person under
33 Section 9-624, and the secured party's recovery of a deficiency would be subject to
34 Section 9-625. Subsection (d) does not apply if, as is characteristic of most sales of
35 accounts, chattel paper, and payment intangibles, the secured party (buyer) has no
36 right of recourse against the debtor (seller) or a secondary obligor.

37 **8. Attorney's Fees and Legal Expenses.** The phrase "reasonable
38 attorney's fees and legal expenses, which appears in subsection (d), includes only
39 those fees and expenses incurred in proceeding against account debtors or other
40 third parties. The secured party's right to recover these expenses arises
41 automatically under this section. The secured party also may incur other attorney's
42 fees and legal expenses in proceeding against the debtor or obligor. Whether the
43 secured party has a right to recover those fees and expenses depends on whether the
44 debtor or obligor has agreed to pay them, as is the case with respect to attorney's
45 fees and legal expenses under Sections 9-608(a)(1)(A) and 9-614(b)(1). The parties

1 also may agree to allocate a portion of the secured party's overhead to collection
2 and enforcement under subsection (d) or Section 9-608(a).

3 **SECTION 9-608. APPLICATION OF PROCEEDS OF COLLECTION**
4 **OR ENFORCEMENT; LIABILITY FOR DEFICIENCY AND RIGHT TO**
5 **SURPLUS.**

6 (a) If a security interest or agricultural lien secures payment or performance
7 of an obligation, the following rules apply:

8 (1) A secured party shall apply or pay over for application the cash
9 proceeds of collection or enforcement under this section in the following order to:

10 (A) the reasonable expenses of collection and enforcement and, to
11 the extent provided for by agreement and not prohibited by law, reasonable
12 attorney's fees and legal expenses incurred by the secured party;

13 (B) the satisfaction of obligations secured by the security interest or
14 agricultural lien under which the collection or enforcement is made; and

15 (C) the satisfaction of obligations secured by any subordinate
16 security interest in or other lien on the collateral subject to the security interest or
17 agricultural lien under which the collection or enforcement is made if the secured
18 party receives an authenticated demand for proceeds before distribution of the
19 proceeds is completed.

20 (2) If requested by a secured party, a holder of a subordinate security
21 interest or other lien shall furnish reasonable proof of the interest or lien within a
22 reasonable time. Unless the holder complies, the secured party need not comply
23 with the holder's demand under paragraph (1)(C).

24 (3) A secured party need not apply or pay over for application the
25 noncash proceeds (Section 9-313) of collection and enforcement under this section.

1 A secured party that applies or pays over for application noncash proceeds shall do
2 so in a commercially reasonable manner.

3 (4) A secured party shall account to and pay a debtor for any surplus
4 notwithstanding any agreement to the contrary, and, unless otherwise agreed, the
5 obligor is liable for any deficiency. Recovery of a deficiency under this subsection
6 is subject to Section 9-625.

7 (b) If the underlying transaction is a sale of accounts, chattel paper, or
8 payment intangibles, the debtor is entitled to any surplus, and the obligor is liable
9 for any deficiency, only if its agreement so provides. Recovery of a deficiency
10 under this subsection is subject to Section 9-625.

11 Reporters' Comments

12 1. **Source.** Subsection (a) is new. Subsection (b) derives from former
13 Section 9-502(2).

14 2. **Modifications of Prior Law.** Subsection (a) modifies former Section
15 9-502(2) by (i) explicitly providing for the application of proceeds recovered by the
16 secured party in substantially the same manner as provided in Section 9-614(a) and
17 (c) for dispositions of collateral; and (ii) referring to the applicability of Section
18 9-625 in the event of the secured party's failure to comply with the commercial
19 reasonableness requirement.

20 3. **Noncash Proceeds.** Subsection (a)(3) addresses the situation in which
21 an enforcing secured party receives noncash proceeds.

22 ***Example:*** An enforcing secured party receives a promissory note from the
23 account debtor. The secured party may wish to credit the debtor with the
24 principal amount of the note upon receipt of the note or may wish to credit
25 the debtor only as and when the note is paid. Under subsection (a)(3), the
26 secured party is under no duty to apply the note or its value to the
27 outstanding obligation. If the secured party elects to apply the note to the
28 outstanding obligation, however, it must do so in a commercially reasonable
29 manner. The parties may provide for the method of application of noncash
30 proceeds in the security agreement, if the method is not manifestly
31 unreasonable. See Section 9-603.

32 Although the secured party is not required to "apply or pay over for application
33 noncash proceeds, the proceeds nonetheless remain collateral subject to this
34 Article. If the secured party were to dispose of them, for example, appropriate
35 notification would be required (see Section 9-611), and the disposition would
36 subject to the standards provided in this part (see Section 9-610). Moreover, a

1 secured party in possession of the noncash proceeds would have the duties specified
2 in Section 9-207.

3 **SECTION 9-609. SECURED PARTY'S RIGHT TO TAKE POSSESSION**

4 **AFTER DEFAULT. [MINOR STYLE CHANGES ONLY]** Unless otherwise
5 agreed, a secured party has the right on default to take possession of the collateral.
6 In taking possession, a secured party may proceed without judicial process, if the
7 taking can be done without breach of the peace, or may proceed by action. If a
8 security agreement so provides, a secured party may require a debtor to assemble
9 the collateral and make it available to the secured party at a place to be designated
10 by the secured party which is reasonably convenient to both parties. Without
11 removal, a secured party may render equipment unusable, and may dispose of
12 collateral on a debtor's premises under Section 9-610.

13 **Reporters' Comments**

14 1. **Source.** Former Section 9-503.

15 2. **Multiple Secured Parties.** More than one secured party may be entitled
16 to take possession under this section. Conflicting rights to possession among
17 parties are resolved by the priority rules of this Article or, as applicable, other law.
18 Thus, a senior secured party is entitled to possession as against a junior claimant.
19 Non-UCC law governs whether a junior secured party in possession of collateral is
20 liable to the senior in conversion. Normally, a junior who refuses to relinquish
21 possession of collateral upon the demand of a secured party having a superior
22 possessory right thereto is liable in conversion. Section 9-614 governs a junior
23 secured party's rights to recover its expenses from the collateral.

24 **SECTION 9-610. DISPOSITION OF COLLATERAL AFTER**

25 **DEFAULT.**

26 (a) A secured party after default may sell, lease, license, or otherwise
27 dispose of any or all of the collateral in its then condition or following any
28 commercially reasonable preparation or processing. Unless effectively disclaimed
29 or modified, a contract for sale, lease, license, or other disposition includes the
30 warranties relating to title, possession, quiet enjoyment, and the like which by

1 operation of law accompany a voluntary disposition of property of the kind subject
2 to the contract. A secured party may disclaim or modify warranties under this
3 section in the contract for disposition by giving a purchaser an authenticated
4 statement that contains specific language disclaiming or modifying the warranties.
5 Language in an authenticated statement is sufficient to disclaim warranties under
6 this section if it states “There is no warranty relating to title, possession, quiet
7 enjoyment, or the like in this disposition, or words of similar import.

8 (b) Every aspect of a disposition of collateral, including the method,
9 manner, time, place, and other terms, must be commercially reasonable. If
10 commercially reasonable, a secured party may dispose of collateral by public or
11 private proceedings, by one or more contracts, as a unit or in parcels, and at any
12 time and place and on any terms. A secured party may buy at a public sale. A
13 secured party may buy at a private sale only if the collateral is of a kind customarily
14 sold on a recognized market or is of a kind that is the subject of widely distributed
15 standard price quotations.

16 Reporters’ Comments

17 1. **Source.** Former Section 9-504(1), (3)

18 2. **Warranties.** Subsection (a) affords the transferee at a disposition under
19 this section the benefit of any title, possession, quiet enjoyment, and similar
20 warranties that would have accompanied the disposition by operation of non-Article
21 9 law had the disposition been conducted under ordinary circumstances. For
22 example, the Article 2 warranty of title would apply to a sale of goods, the
23 analogous warranties of Article 2A would apply to a lease of goods, and any
24 common law warranties of title would apply to dispositions of other types of
25 collateral. See, e.g., Restatement (2d) Contracts § 333 (warranties of assignor).

26 Subsection (a) explicitly contemplates that these warranties can be
27 disclaimed. It provides a sample of wording that will effectively exclude the
28 warranties in a disposition under this section, whether or not the exclusion would
29 be effective under non-Article 9 law.

30 The warranties incorporated by subsection (a) are those relating to “title,
31 possession, quiet enjoyment, and the like. Non-Article 9 law determines whether
32 other statutory or implied warranties, e.g., warranties of quality or fitness for
33 purpose, apply to a disposition under this section. It also determines issues relating

1 to disclaimer of such warranties. For example, a foreclosure sale of a car by a car
2 dealer would give rise to an implied warranty of merchantability (Revised Section
3 2-404) unless effectively disclaimed or modified (Revised Section 2-406).

4 This section's approach to these warranties conflicts with Official Comment
5 5 to Section 2-312: "Subsection (2) [of Section 2-312] recognizes that sales by . . .
6 foreclosing lienors and person similarly situated are so out of the ordinary
7 commercial course that their peculiar character is immediately apparent to the buyer
8 and therefore no personal obligation is imposed upon the seller that is purporting to
9 sell only an unknown or limited right. This Article rejects the baseline assumption
10 that commercially reasonable dispositions under this section are "out of the
11 ordinary commercial course or "peculiar. Any conflict between this Article and
12 Revised Article 2 will be worked out between the Drafting Committees.

13 **3. Pre-disposition Preparation and Processing.** Former Section 9-504(1)
14 appears to give the secured party the choice of disposing of collateral either "in its
15 then condition or following any commercially reasonable preparation or
16 processing. Many courts have held that the "commercially reasonable standard of
17 Section 9-504(3) nevertheless may impose an affirmative duty on the secured party
18 to process or prepare the collateral prior to sale. The Drafting Committee was
19 concerned that if the quoted language were added to the second sentence of
20 subsection (b), courts might be unnecessarily quick to impose a duty of preparation
21 or processing on the secured party. Accordingly, the Drafting Committee chose to
22 retain the language in subsection (a). Subsection (a) does not grant the secured
23 party the right to dispose of the collateral "in its then condition under all
24 circumstances. A secured party may not dispose of collateral "in its then condition
25 when, taking into account the costs and probable benefits of preparation or
26 processing and the fact that the secured party would be advancing the costs at its
27 risk, it would be commercially unreasonable to dispose of the collateral in its then
28 condition.

29 **4. Disposition by Junior Secured Party.** Subsection (a) is not limited to
30 first-priority security interests. Rather, any secured party as to which there has been
31 a default enjoys the right to dispose of collateral under this subsection. The
32 exercise of this right by a secured party whose security interest is subordinate to
33 that of another secured party does not of itself constitute a conversion or otherwise
34 give rise to liability in favor of the holder of the senior security interest. Section
35 9-614 addresses application of the proceeds of a disposition by a junior secured
36 party. Under Section 9-614(b), a junior secured party owes no obligation to apply
37 the proceeds of disposition to the satisfaction of obligations secured by a senior
38 security interest. Section 9-614(g) builds on this general rule by protecting certain
39 juniors from claims of a senior concerning cash proceeds of the disposition. Even
40 if a senior were to have a non-Article 9 claim to proceeds of a junior's disposition,
41 Section 9-614(g) would protect a junior that acts in good faith and without
42 knowledge that its actions violate the rights of a senior party. Because the
43 disposition by a junior would not cut off a senior's security interest or lien (see
44 Section 9-615), in many (probably most) cases the junior's receipt of the cash
45 proceeds would not violate the rights of the senior.

46 The holder of a senior security interest is entitled, by virtue of its priority, to
47 take possession of collateral from the junior secured party and conduct its own

1 disposition, provided that the senior enjoys the right to take possession of the
2 collateral from the debtor. See Section 9-609. The holder of a junior security
3 interest normally must notify the senior secured party of an impending disposition.
4 See Section 9-611. Regardless of whether the senior receives a notification from
5 the junior, the junior's disposition does not of itself discharge the senior's security
6 interest. See Section 9-615. Unless the senior secured party has authorized the
7 disposition free and clear of its security interest, the senior's security interest
8 ordinarily will survive the disposition by the junior and continue under Section
9 9-313(c). If the senior enjoys the right to repossess the collateral from the debtor,
10 the senior likewise may recover the collateral from the transferee.

11 When a secured party's collateral is encumbered by another security interest
12 or by a lien, one of the claimants may seek to invoke the equitable doctrine of
13 marshaling. As explained by the Supreme Court, that doctrine "rests upon the
14 principle that a creditor having two funds to satisfy his debt, may not by his
15 application of them to his demand, defeat another creditor, who may resort to only
16 one of the funds. *Meyer v. United States*, 375 U.S. 233, 236 (1963), quoting
17 *Sowell v. Federal Reserve Bank*, 268 U.S. 449, 456-57 (1925). The purpose of the
18 doctrine is "to prevent the arbitrary action of a senior lienor from destroying the
19 rights of a junior lienor or a creditor having less security. *Id.* at 237. Because it is
20 an equitable doctrine, marshaling "is applied only when it can be equitably
21 fashioned as to all of the parties having an interest in the property. *Id.* This
22 Article leaves courts free to determine whether marshaling is appropriate in any
23 given case. See Section 1-103.

24 **5. Security Interests of Equal Rank.** Sometimes two security interests
25 enjoy the same priority. This situation may arise by contract, e.g., pursuant to
26 "equal and ratable" provisions in indentures, or by operation of law. See Section
27 9-324(3); 9-325(2); 9-326(2). This Article treats a security interest having equal
28 priority like a senior security interest in many respects. Assume, for example, that
29 SP-X and SP-Y enjoy equal priority, SP-W is senior to them, and SP-Z is junior. If
30 SP-X disposes of the collateral under this section, then (1) SP-W's and SP-Y's
31 security interests survive the disposition but SP-Z's does not, see Section 9-615,
32 and (2) neither SP-W nor SP-Y is entitled to receive a distribution of proceeds but
33 SP-Z is. See Section 9-614(b)(3).

34 When one considers the ability to obtain possession of the collateral, a
35 secured party with equal priority is unlike a senior secured party. As the senior
36 secured party, SP-W should enjoy the right to possession as against SP-X. See
37 Section 9-609, Comments. If SP-W takes possession and disposes of the collateral
38 under this section, it is entitled to apply the proceeds to satisfy its secured claim.
39 SP-Y, however, should not have such a right to take possession from SP-X;
40 otherwise, once SP-Y took possession from SP-X, SP-X would have the right to get
41 possession from SP-Y, which would be obligated to redeliver possession to SP-X,
42 and so on. Resolution of this problem is left to the parties and, if necessary, the
43 courts.

44 **6. Public vs. Private Dispositions.** This Article maintain three distinctions
45 between "public" and other dispositions: (i) the secured party may buy at the
46 former, but not at the latter (Section 9-610(b)); (ii) the debtor is entitled to
47 notification of "the time and place of a public sale" and notification of "the time

1 after which a private sale or other intended disposition is to be made (Section
2 9-613(a)(1)(E)); (iii) the section is less protective of transferees in a noncomplying
3 public sale than in other noncomplying dispositions (Section 9-615(a)). As used in
4 this Article, a “public sale” is one at which the price is determined after the public
5 has had a meaningful opportunity for competitive bidding. “Meaningful
6 opportunity” is meant to imply that some form of advertisement or public notice
7 must precede the sale and that the public (or the commercially relevant segment of
8 the public) must have access to the sale.

9 **7. Investment Property.** Dispositions of investment property may be
10 regulated by the federal securities laws. Although the “public sale” of securities
11 under this Article may implicate the registration requirements of the Securities Act
12 of 1933, it need not do so. A disposition that qualifies for deviations from the rules
13 for “private placement” exemptions under the Securities Act of 1933 in connection
14 with public advertising nevertheless may constitute a “public sale” within the
15 meaning of this section. Moreover, the “commercially reasonable” requirements of
16 subsection (b) need not prevent a secured party from conducting a foreclosure sale
17 without first complying with federal registration requirements. To eliminate any
18 doubt, a secured party whose collateral consists of unregistered securities may wish to
19 obtain an undertaking by the debtor to cause the securities to be registered under the
20 1933 Act upon the secured party’s request. The debtor’s failure to comply with
21 such a requirement should free the secured party (insofar as Article 9 is concerned)
22 to dispose of the unregistered securities in an otherwise commercially reasonable
23 manner. An agreement along these lines would be enforceable as a “standard[]
24 that is not “manifestly unreasonable” under Section 9-603.

25 **8. “Recognized Market.”** A “recognized market,” as used in subsection
26 (b) and Section 9-611(b), is one in which the items sold are fungible and prices are
27 not subject to individual negotiation. For example, the New York Stock Exchange
28 is a recognized market, whereas the markets for used automobiles and livestock are
29 not.

30 **9. Wholesale vs. Retail Dispositions.** A disposition at wholesale is not per
31 se commercially unreasonable. Regarding whether disposition at wholesale is
32 commercially reasonable when retail facilities are readily available, this Article
33 leaves the courts free to resolve each case on its own facts.

34 **10. Relevance of Price.** The amount of proceeds received in a disposition
35 (e.g., the cash price if the disposition is by way of sale) is not a term that must be
36 commercially reasonable. See the Comments to Sections 9-614 and 9-626.

37 **SECTION 9-611. PERSONS ENTITLED TO NOTIFICATION BEFORE** 38 **DISPOSITION OF COLLATERAL.**

39 (a) In this section, “notification date” means the earlier of the date on which
40 a secured party sends to the debtor and any secondary obligor an authenticated

1 notification of disposition and the date on which the debtor and any secondary
2 obligor waive the right to notification.

3 (b) A secured party shall send to a debtor and any secondary obligor a
4 reasonable authenticated notification of disposition under Section 9-613 unless
5 collateral is perishable or threatens to decline speedily in value or is of a type
6 customarily sold on a recognized market. In the case of consumer goods, another
7 notification need not be sent. In other cases a secured party shall send an
8 authenticated notification of disposition to:

9 (1) any other person from which the secured party has received, before
10 the notification date, an authenticated notification of a claim of an interest in the
11 collateral;

12 (2) any other secured party that, [] days before the notification date,
13 held a security interest or agricultural lien in the collateral perfected by the filing of
14 a financing statement that identified the collateral, was indexed under the debtor's
15 name as of that date, and was filed in the office in which to file a financing
16 statement against the debtor covering the collateral as of that date; and

17 (3) any other secured party that, [] days before the notification date,
18 held a security interest in the collateral perfected by compliance with a statute or
19 treaty described in Section 9-309A(a).

20 (c) A secured party complies with the notification requirement specified in
21 subsection (b)(2) if:

22 (1) not later than [] days before the notification date, the secured party
23 requests, in a commercially reasonable manner, information concerning financing
24 statements indexed under the debtor's name in the office indicated in subsection
25 (b)(2); and

26 (2) before the notification date the secured party:

1 (A) did not receive a response to the request for information; or
2 (B) received a response to the request for information and sent an
3 authenticated notification of disposition to each secured party named in that
4 response and whose financing statement covered the collateral.

5 Reporters' Comments

6 1. **Source.** Former Section 9-504(3).

7 2. **Notification to Debtors and Secondary Obligors.** This section
8 imposes a duty to send notification of a disposition not only to the debtor but also
9 to a secondary obligor. It resolves an uncertainty under former Article 9 by
10 providing that secondary obligors (sureties) will be entitled to receive notification
11 of an intended disposition of collateral, regardless of who created the security
12 interest in the collateral. If the surety created the security interest, it would be the
13 debtor. If it did not, it would be a secondary obligor. (This Article also resolves
14 the question of the secondary party's ability to waive the right to notification. See
15 Section 9-602.) Section 9-605 relieves a secured party from any duty to send
16 notification to a debtor or secondary obligor unknown to the secured party.

17 Under subsection (b), the principal obligor (borrower) is not always entitled
18 to notification of disposition.

19 ***Example:*** Mooney borrows on an unsecured basis, and Harris grants a
20 security interest in his car to secure the debt. Mooney is a primary obligor,
21 not a secondary obligor. As such, he is not entitled to notification of
22 disposition under this section.

23 3. **Notification to Other Secured Parties.** Prior to the 1972 amendments,
24 Section 9-504(3) required the enforcing secured party to send reasonable
25 notification of the sale:

26 except in the case of consumer goods to any other person who has a security
27 interest in the collateral and who has duly filed a financing statement
28 indexed in the name of the debtor in this State or who is known by the
29 secured party to have a security interest in the collateral.

30 The 1972 amendments eliminated the duty to give notice to secured parties other
31 than those from whom the foreclosing secured party had received written notice of
32 a claim of an interest in the collateral.

33 Many of the problems arising from dispositions of collateral encumbered by
34 multiple security interests can be ameliorated or solved by informing all secured
35 parties of an intended disposition and affording them the opportunity to work with
36 one another. To this end, subsection (b)(2) expands the duties of the foreclosing
37 secured party to include the duty to notify (and the corresponding burden of
38 searching the files to discover) certain competing secured parties. The subsection
39 imposes a search burden that in some cases may be greater than the pre-1972

1 burden on foreclosing secured parties but certainly is more modest than that faced
2 by a new lender.

3 To determine who is entitled to notification, the foreclosing secured party
4 must determine the proper office for filing a financing statement as of a particular
5 date, measured by reference to the “notification date” as defined in subsection (a).
6 This determination requires reference to the choice-of-law provisions of Part 3.
7 The secured party must ascertain whether any financing statements covering the
8 collateral and indexed under the debtor’s name, as the name existed as of that date,
9 in fact were filed in that office. The foreclosing secured party generally need not
10 notify secured parties whose effective financing statements have become more
11 difficult to locate because of changes in the location of the debtor, proceeds rules,
12 or changes in the debtor’s name.

13 Under subsection (b)(3), the secured party also must notify a secured party
14 that has perfected a security interest by complying with a statute or treaty described
15 in Section 9-309A(a), such as a certificate-of-title act.

16 Subsection (c) provides a “safe harbor” that takes into account the inevitable
17 delays attendant to receiving information from the public filing offices. It provides,
18 generally, that the secured party will be deemed to have satisfied its notification
19 duties under subsection (b)(2) if it requests search(es) from the proper office(s) at
20 least [] days before sending notification to the debtor and it also sends a notification
21 to all secured parties reflected on the search report(s). The secured party’s duties
22 under subsection (b)(2) also will be satisfied if the secured party does not receive
23 any search report(s) before the notification is sent to the debtor.

24 In considering the extent, if any, to which expansion of the notification
25 requirement is desirable, one should keep in mind the consequences of failing to
26 send notification to the holder of a competing security interest: the aggrieved
27 secured party has the burden of establishing its loss. See Section 9-624. Also
28 relevant are Section 9-614(g), under which senior secured parties ordinarily are not
29 entitled to share in proceeds of a junior’s disposition, Section 9-615(a), under
30 which a disposition cuts off junior security interests, and Section 9-614(b), under
31 which junior secured parties are not entitled to receive excess proceeds from the
32 disposing secured party unless they demand them.

33 **4. Authentication Requirement.** Subsection (b) explicitly provides that
34 notification of disposition must be “authenticated.” Some cases read former
35 Section 9-504(3) as validating oral notification.

36 **5. Second Try.** This Article leaves to judicial resolution, based upon the
37 facts of each case, the question whether the requirement of “reasonable
38 notification” requires a “second try,” i.e., whether a secured party that sends
39 notification and learns that the debtor did not receive it must attempt to locate the
40 debtor and send another notification.

41 **6. Failure to Conduct Notified Disposition.** Nothing in this Article
42 prevents a secured party from not conducting a disposition after sending notice or
43 sending a revised notification if its plans for disposition change; provided, however,
44 that the secured party acts in good faith, the revised notification is reasonable, and

1 the revised plan for disposition and any attendant delay are commercially
2 reasonable.

3 **SECTION 9-612. TIMELINESS OF NOTIFICATION BEFORE**

4 **DISPOSITION OF COLLATERAL.** Unless otherwise agreed, in a transaction
5 other than a consumer goods secured transaction a notification of disposition is sent
6 within a reasonable time before the disposition if it is sent after default and 10 days
7 or more before the earliest time of disposition set forth in the notification. Whether
8 a notification sent less than 10 days before the earliest time of disposition set forth
9 in the notification nevertheless is sent within a reasonable time is a question of fact.

10 Reporters' Comments

11 1. **Source.** New.

12 2. **Timeliness of Notification.** The 10-day notice period in this section is
13 intended to be a "safe harbor" and not a minimum requirement. To qualify for the
14 "safe harbor" the notification must be sent after default. A notification also must be
15 sent in a commercially reasonable manner. See Section 9-611(b) ("reasonable
16 authenticated notification"). Those requirements prevent a secured party from
17 taking advantage of the "safe harbor" by, for example, giving the debtor a
18 notification at the time of the original extension of credit or sending the notice by
19 surface mail to a debtor overseas. the "safe harbor" is not applicable in a consumer
20 goods secured transaction.

21 **SECTION 9-613. CONTENTS AND FORM OF NOTIFICATION**
22 **BEFORE DISPOSITION OF COLLATERAL.**

23 (a) Except in a consumer goods secured transaction, the following rules
24 apply:

25 (1) Unless otherwise agreed, the contents of a notification of disposition
26 are sufficient if the notification:

27 (A) describes the debtor and the secured party;

28 (B) describes the collateral that is the subject of the intended
29 disposition;

30 (C) states the method of intended disposition;

1 (D) states that the debtor [or secondary obligor] is entitled to an
2 accounting of the unpaid indebtedness and states the charge, if any for an
3 accounting; and

4 (E) states the time and place of a public sale or the time after which
5 any other disposition is to be made, whether or not the notification contains
6 additional information.

7 (2) Whether a notification that lacks any of the information set forth in
8 paragraph (1) is nevertheless sufficient is a question of fact.

9 (3) A particular phrasing of the notification is not required. A
10 notification substantially complying with the requirements of this subsection is
11 sufficient, even if it contains minor errors that are not seriously misleading.

12 (4) The following form of notification, when completed, contains
13 sufficient information:

14 **NOTIFICATION OF DISPOSITION OF COLLATERAL**

15 To: [Name of debtor, obligor, or other person to which the
16 notification is sent]

17 From: [Name, address, and telephone number of secured
18 party]

19 Name of Debtor(s): [Include only if debtor(s) are not an addressee]
20 [For a public disposition:]

21 We will sell [or lease or license, *as applicable*] the [describe collateral]
22 [to the highest qualified bidder] in public as follows:

23 Day and Date: _____

24 Time: _____

25 Place: _____

26 [For a private disposition:]

We will sell [or lease or license, *as applicable*] the [describe collateral]
privately sometime after [day and date].

You are entitled to an accounting of the unpaid indebtedness secured by the property that we intend to sell [or lease or license, *as applicable*] [for a charge of \$ _____]. You may request an accounting by calling us at _____ [*telephone number*].

* * *

[End of Form]

(b) In a consumer goods secured transaction, the following rules apply:

(1) A notification of disposition must contain the following information:

(A) the information specified in Section 9-613(a)(1);

(B) a description of any liability for a deficiency of the person to which the notification is sent;

(C) a telephone number from which the amount that must be paid to the secured party to redeem the collateral under Section 9-621 is available;

(D) a telephone number from which the amount that must be paid to the secured party to reinstate the obligation secured under Section 9-622 is available; and

(E) a telephone number or mailing address from which additional information concerning the disposition and the obligation secured is available.

(2) A particular phrasing of the notification is not required. A notification substantially complying with the requirements of this subsection is sufficient even if it contains minor errors that are not seriously misleading.

(3) The following form of notification, when completed, contains sufficient information:

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NOTIFICATION OF OUR PLAN TO SELL PROPERTY

To: [Name of debtor or obligor to whom the notification is sent]

From: [Name, address, and telephone number of secured party]

Name of Debtor(s): [Include only if debtor(s) are not an addressee]

[You] [name of obligor, if different] owe(s) us money on a debt and [you have] [has] not paid it to us on time. We have [your] [the debtor's] [describe collateral] because we took it from [you] [the debtor] or [you] [the debtor] voluntarily gave it to us. [You] [name of debtor, if different] agreed to let us do that when [you] [name of obligor, if different] created the debt.

[For a public disposition:]

We plan to sell [or lease or license, *as applicable*] the [describe collateral] [to the highest qualified bidder] in public. The sale [or lease or license, *as applicable*] will be held as follows:

Day and Date: _____

Time: _____

Place: _____

You can bring bidders to the sale if you want.

[For a private disposition:]

We will sell [or lease or license, *as applicable*] the [describe collateral] privately sometime after [day and date].

The money that we get from the sale [or lease or license, *as applicable*] (after paying our costs) will be paid on the debt that [you] [name of obligor, if different] owe(s) to us. [Include the following sentence only if the addressee is obligated on the secured debt.] IF WE GET LESS MONEY THAN YOU OWE, YOU WILL STILL OWE US THE DIFFERENCE, and we may sue you and take part of your wages or other property. [Include the following sentence only if the

addressee is a debtor.] If we get more money than [you] [name of obligor, if different] owe(s) to us, [you] [name of obligor, if different] will get the extra money.

You can stop the sale [and get] [and the debtor will get] the property back. To do this, [you] [name of obligor, if different] must:

{Alternative A}

Pay us \$ before the sale. That will pay off the debt plus our costs and [you] [name of obligor, if different] will not owe us any more money;

[add the following paragraph if applicable] OR

~~Pay us our costs of retaking the property, all regular payments that are overdue, and all late charges. That amount is now about \$, but that amount may change. To learn the exact amount, call us at [telephone number]. You would have to make this payment by [date]. If you make the payment, [you] [name of obligor, if different] will have to keep on making the rest of the regular [monthly] payments.~~

{Alternative B}

Pay us the full amount of the debt plus our costs before the sale. Then [you] [name of obligor, if different] will not owe us any more money. To learn the exact amount you must pay, call us at [telephone number]. ;

[add the following paragraph if applicable] OR

Pay us our costs of retaking the property, all regular payments that are overdue, and all late charges. To learn the exact amount you must pay, call us at [telephone number]. You would have to make this payment by [date]. If you make the payment, [you] [name of obligor, if different] will have to keep on making the rest of the regular [monthly] payments.

1 If you want us to explain to you in writing how we have figured the amount that
2 you owe us, you may call us at [telephone number]. [We will charge you

\$ for the explanation.]

[End of Form]

Reporters' Comments

1. **Source.** New.

2. Contents of Notification. To comply with the “reasonable authenticated notification” requirement of Section 9-611(b), the contents of a notification must be reasonable. Except in a consumer goods secured transaction, the contents of a notification that includes the information set forth in subsection (a) are sufficient as a matter of law, unless the parties agree otherwise. (The reference to “time of disposition” means here, as it does in former Section 9-504(3), not only the hour of the day but also the date.) Although a secured party may choose to include additional information concerning the transaction or the debtor’s rights and obligations, no additional information is required unless the parties agree otherwise. A notification that lacks some of the information set forth in subsection (a)(1) nevertheless may be sufficient if found to be so by the trier of fact. See subsection (a)(2). A properly completed sample form of notification in subsection (a)(4) is one example of a notification that would contain the information set forth in subsection (a)(1). No particular phrasing of the notification is required, however.

3. Consumer Goods Secured Transactions. Subsection (b)(1) sets forth the information required for an effective notification in a consumer goods secured transaction. A notification that lacks any of the information set forth in subsection (b)(1) is insufficient as a matter of law. Compare subsection (a)(2), under which the trier of fact may find a notification to be sufficient even if it lacks some information listed in subsection (a)(1). However, under subsection (b)(3), a notification that is substantially complying is sufficient, even if it contains minor errors that are not seriously misleading.

**SECTION 9-614. APPLICATION OF PROCEEDS OF DISPOSITION;
LIABILITY FOR DEFICIENCY AND RIGHT TO SURPLUS.**

(a) In this section: ~~“affiliate means [a person controlling, controlled by, or under common control with another person]~~

(1) “Person related to with respect to an individual means:

(A) the spouse of the individual;

(B) a brother, brother-in-law, sister, or sister-in-law of the

individual;

(C) an ancestor or lineal descendant of the individual or the spouse

of the individual; and

1 (D) any other relative, by blood or marriage, of the individual or the
2 spouse of the individual who shares the same home with the individual

3 (2) "Person related to with respect to an organization means:

4 (A) a person directly or indirectly controlling, controlled by, or
5 under common control with the organization;

6 (B) an officer or director of, or a person performing similar functions
7 with respect to, the organization;

8 (C) an officer or director of, or a person performing similar functions
9 with respect to, a person described in paragraph (A);

10 (D) the spouse of a person described in paragraph (A), (B), or (C);
11 and

12 (E) a person related by blood or marriage to a person described in
13 paragraph (A), (B), or (C) or (D) and who shares the same home with the person.

14 (b) A secured party shall apply or pay over for application the cash
15 proceeds of disposition in the following order to:

16 (1) the reasonable expenses of retaking, holding, preparing for
17 disposition, processing, and disposing, and, to the extent provided for by agreement
18 and not prohibited by law, reasonable attorney's fees and legal expenses incurred by
19 the secured party;

20 (2) the satisfaction of obligations secured by the security interest or
21 agricultural lien under which the disposition is made;

22 (3) the satisfaction of obligations secured by any subordinate security
23 interest in or other lien on the collateral if the secured party receives an
24 authenticated demand for proceeds before distribution of the proceeds is completed.

25 (c) If requested by a secured party, a holder of a subordinate security
26 interest or other lien shall furnish reasonable proof of the interest or lien within a

1 reasonable time. Unless the holder does so, the secured party need not comply with
2 the holder's demand under subsection (b)(3).

3 (d) A secured party need not apply or pay over for application noncash
4 proceeds of disposition under this section. A secured party that applies or pays over
5 for application noncash proceeds shall do so in a commercially reasonable manner.

6 (e) If the security interest under which a disposition is made secures
7 payment or performance of an obligation, after making the payments and
8 applications required by subsection (b) the secured party shall account to and pay a
9 debtor for any surplus, and, unless otherwise agreed, the obligor is liable for any
10 deficiency. If the underlying transaction is a sale of accounts, chattel paper, or
11 payment intangibles, the debtor is entitled to any surplus, and the obligor is liable
12 for any deficiency, only if its agreement so provides. Recovery of any deficiency
13 under this subsection is subject to Section 9-625.

14 (f) This subsection applies to a disposition at which the transferee is the
15 secured party, a person related to ~~an affiliate of~~ the secured party, or a secondary
16 obligor. If the amount of proceeds of the disposition is unreasonably low, the
17 surplus or deficiency under subsection (e) is calculated based on the amount of
18 proceeds that would have been realized in a commercially reasonable disposition to
19 a transferee other than the secured party, a person related to ~~an affiliate of~~ the
20 secured party, or a secondary obligor.

21 (g) A secured party that receives cash proceeds of disposition in good faith
22 and without knowledge that the receipt violates the rights of the holder of a security
23 interest or other lien that is not subordinate to the security interest or agricultural
24 lien under which the collection or enforcement is made:

25 (1) takes the cash proceeds free of the security interest or other lien;

1 (2) is not obligated to apply the proceeds of disposition to the
2 satisfaction of obligations secured by the security interest or other lien; and
3 (3) is not obligated to account to or pay the holder of the security
4 interest or other lien for any surplus.

5 Reporters' Comments

6 1. **Source.** former Section 9-504(1), (2).

7 2. **Application of Proceeds.** This section contains the rules governing
8 application of proceeds and the debtor's liability for a deficiency. Subsection (b)
9 provides a "safe harbor" for a secured party that complies with its terms. However,
10 a secured party that does not comply with subsection (b) is liable only as provided
11 in Section 9-624.

12 3. **Noncash Proceeds.** Subsection (d) addresses the application of noncash
13 proceeds of a disposition, such as a note or lease. The explanation in the
14 Comments to Section 9-608 generally applies to this subsection. Under subsection
15 (d), if a disposition produces noncash proceeds, such as a promissory note, the
16 secured party is under no duty to apply the proceeds or their value to the secured
17 obligation. If a secured party elects to apply the note to the outstanding obligation,
18 however, it must do so in a commercially reasonable manner. One would expect
19 that where noncash proceeds are or may be material, the parties would agree to
20 more specific standards in an agreement entered into before or after default. The
21 parties may provide for the method of application of noncash proceeds in the
22 security agreement, if the method is not manifestly unreasonable. See Section
23 9-603.

24 4. **Surplus and Deficiency.** Subsection (e) deals with surplus and
25 deficiency. It revises former Section 9-504(2) by imposing an explicit requirement
26 that the secured party "pay" the debtor for any surplus, while retaining the secured
27 party's duty to "account." Inasmuch as the debtor may not be an obligor,
28 subsection (e) now provides that the obligor (not the debtor) is liable for the
29 deficiency. The special rule governing surplus and deficiency when receivables
30 have been sold likewise has been revised to take into account the new distinction
31 between debtor and obligor.

32 5. **Collateral Under New Ownership.** When the debtor sells collateral
33 subject to a security interest, the original debtor (creator of the security interest) is
34 no longer a debtor inasmuch as it no longer has a property interest in the collateral;
35 the buyer is the debtor. See Section 9-102. As between the debtor (buyer of the
36 collateral) and the original debtor (seller of the collateral), the debtor (buyer)
37 normally would be entitled to the surplus. Subsection (d) therefore requires the
38 secured party to pay the surplus to the debtor (buyer), not to the original debtor
39 (seller) with which it has dealt. But, because this situation arises as a result of the
40 debtor's wrongful act, this Article does not expose the secured party to the risk of
41 determining ownership of the collateral. If the secured party does not know about
42 the new debtor and accordingly pays the surplus to the original debtor, the
43 exculpatory provisions of this Article exonerate the secured party from liability to

1 the new debtor. See Section 9-627(a), (b). If a debtor sells collateral *free* of a
2 security interest, such as a sale to a buyer in ordinary course of business (see
3 Section 9-316(a)), the property is no longer collateral and the buyer is not a debtor.

4 6. **“Low Price” Dispositions.** Subsection (f) provides a special method for
5 calculating a deficiency or surplus when the secured party, a person related to the
6 secured party (as defined in subsection (a)), or a secondary obligor acquires the
7 collateral at a foreclosure disposition. It recognizes that when the foreclosing
8 secured party or a related party is the transferee of the collateral, the secured party
9 sometimes lacks the incentive to maximize the proceeds of disposition. As a
10 consequence, the disposition may comply with the procedural requirements of this
11 Article (e.g., it is conducted in a commercially reasonable manner following
12 reasonable notice) but nevertheless fetch a price that is unreasonably low.

13 Subsection (f) adjusts for this lack of incentive. If the proceeds of a
14 disposition of collateral to a secured party, a person related to the secured party, or
15 a secondary obligor are “unreasonably low,” then instead of calculating a deficiency
16 (or surplus) based on the actual net proceeds, the calculation is based upon the
17 amount that would have been received in a commercially reasonable disposition to
18 an unrelated person. Subsection (f) thus rejects the view that the secured party’s
19 receipt of an unreasonably low amount constitutes noncompliance with Part 6.

20 The term “unreasonably low” is not susceptible to precise definition. An
21 amount of proceeds is “unreasonably low” if it is less than the “reasonably
22 equivalent value” of the collateral as that term was construed in the context of
23 fraudulent transfer law prior to the opinion in *BFP v. Resolution Trust Corp.*, 511
24 U.S. 531 (1994).

25 7. **“Person related to.”** The definition of “person related to” in subsection
26 (a) is patterned closely on the corresponding definition in Section 1.301(32) of the
27 Uniform Consumer Credit Code. The Drafting Committee has yet to consider this
28 definition. It replaces the tentative definition of “affiliate” in the preceding draft.
29 The Drafting Committee also may wish to consider whether the definition should
30 be based on the definition of “insider” in Section 101 of the Bankruptcy Code.

31 **SECTION 9-614A. NOTIFICATION OF CALCULATION**

32 **EXPLANATION OF SURPLUS OR DEFICIENCY.**

33 (a) This section applies to a consumer goods secured transaction in which
34 the debtor is entitled to a surplus or a consumer obligor is liable for a deficiency
35 under Section 9-614(e).

36 (b) In this section:

37 (1) “Explanation” means a writing that:

1 ~~(b) Before or when the secured party accounts to the debtor and pays any~~
2 ~~surplus or first makes written demand on the obligor for payment of the deficiency,~~
3 ~~the secured party shall send to the debtor or obligor a written notification:~~

4 ~~(A 1) stating states~~ the amount of the surplus or deficiency; and

5 ~~(B 2) providing provides~~ a reasonable explanation of how the
6 secured party calculated the surplus or deficiency, including an indication of:

7 ~~(i A)~~ the amount of the obligation secured, calculated as of a date
8 not more than [] days before disposition of the collateral;

9 ~~(ii B)~~ the components of the obligation secured, including, as
10 applicable, the unpaid balance of principal or purchase price, interest or other
11 finance charges, delinquency, default, deferral, or other additional charges, and
12 reasonable expenses and attorney's fees described in Section 9-614(b)(1); and

13 ~~(iii C)~~ the amount of credit applied to the obligation secured,
14 made after the date of calculation, and its components, including, as applicable,
15 payments, rebates, and proceeds of a disposition of collateral.

16 (2) “Request” means a record:

17 (A) authenticated by a debtor or consumer obligor; and

18 (B) requesting that the recipient provide an explanation.

19 (c) A secured party shall send an explanation to the debtor or consumer
20 obligor, as applicable:

21 (1) before or when the secured party accounts to the debtor and pays any
22 surplus or first makes written demand on the consumer obligor for payment of the
23 deficiency; and

24 (2) within two weeks after receipt of a request.

25 ~~(d e)~~ A particular phrasing of the ~~notification~~ explanation is not required.

26 ~~A notification~~ An explanation complying substantially with the requirements of this

subsection is sufficient even if it contains minor errors that are not seriously misleading.

(e) A debtor or consumer obligor is entitled without charge to one response to a request under this section during any six-month period in which the secured party did not send to the debtor or consumer obligor an explanation pursuant to subsection (c)(1). The secured party may require payment of a charge not exceeding \$[] for each additional response.

Reporters' Comments

Change from Prior Draft: Rewritten to add a duty to respond to a request for an explanation of calculation. In the absence of a request, the duty to provide an explanation arises only when the secured party makes written demand.

1. **Source.** New.

2. **Duty to Send Information Concerning Deficiency.** This section reflects the view that, in every consumer goods secured transaction, the obligor should be entitled to know the amount of the deficiency claimed by the secured party and the basis upon which the deficiency was calculated. Under subsection (c)(1), a secured party is obligated to provide this information no later than the time of its first written attempt to collect the deficiency. The obligor need not make a request for an accounting in order to receive it. A secured party that does not attempt to collect a deficiency in writing has no obligation to send notification under subsection (c)(1) and, consequently, cannot be liable for noncompliance.

A debtor or secondary obligor need not wait until the secured party commences written collection efforts in order to receive an explanation of how a deficiency or surplus was calculated. Subsection (c)(2) obliges the secured party to respond to a request for an explanation.

3. **Information Concerning Surplus.** This section also requires the secured party to explain to the debtor in a consumer goods secured transaction how a surplus was calculated.

4. **Liability for Noncompliance.** A secured party that fails to comply with a request under subsection (c)(2) is liable for any loss caused, plus \$500, plus statutory minimum damages. See Sections 9-624(c) and (e). A secured party that fails to send an explanation under subsection (c)(1) is liable for any loss caused. See Section 9-624(b).

SECTION 9-615. RIGHTS OF TRANSFEREE OF COLLATERAL.

1 (a) A secured party's disposition of collateral after default transfers to a
2 transferee for value all of a debtor's rights in the collateral and discharges the
3 security interest under which the disposition is made and any subordinate security
4 interest or other lien [other than liens created under] [cite acts or statutes providing
5 for liens, if any, that are not to be discharged]. The transferee takes free of those
6 rights and interests, even if the secured party fails to comply with the requirements
7 of this article or any judicial proceedings:

8 (1) in a public sale, if the transferee has no knowledge of any defects in
9 the sale, does not buy in collusion with the secured party, other bidders, or the
10 person conducting the sale, and acts in good faith; or

11 (2) in any other case, if the transferee acts in good faith.

12 (b) If a transferee does not take free of the rights and interests described in
13 subsection (a), the transferee takes the collateral subject to the debtor's rights in the
14 collateral and subject to any security interest or agricultural lien under which the
15 disposition is made and any [subordinate] security interest or other lien.

16 (c) Except as otherwise provided in this subsection or elsewhere in this
17 article, a secured party's disposition of collateral does not discharge any security
18 interest or other lien.

19 Reporters' Comments

20 1. **Source.** Former Section 9-504(4).

21 2. **Title Taken by Transferee.** Subsection (a) sets forth the rights acquired
22 by persons that qualify under paragraphs (1) or (2). Such a person is a "transferee,
23 inasmuch as a buyer at a foreclosure sale does not meet the definition of
24 "purchaser" in Section 1-201. By virtue of the expanded definition of the term
25 "debtor" in Section 9-102, subsection (a) makes clear that the ownership interest of
26 a person that bought the collateral subject to the security interest is terminated.
27 Such a person is a debtor under this Article. Under the former Article, the result
28 arguably is the same, but the statute is not clear. Under subsection (a), a disposition
29 normally discharges the security interest being foreclosed and any subordinate
30 security interests. Subsection (c) makes clear that a disposition does not discharge
31 senior interests or interests of equal rank unless they would be discharged under
32 other provisions of Article 9.

1 Subsection (b) specifies the consequences for a transferee that does not
2 qualify for protection (e.g., a transferee with knowledge of defects in a public sale).

3 **3. Disposition by Third Party.** Secured parties may utilize the services of
4 third persons to dispose of repossessed collateral.

5 *Example:* Secured Party (SP) takes possession of goods collateral after
6 default and entrusts the goods to Merchant. Merchant then wrongfully sells
7 the collateral to a buyer in ordinary course of business (Buyer). That
8 disposition would transfer to Buyer all of SP's rights and the rights that SP
9 had the power to transfer (including those of the debtor). Sections 2-403(1);
10 9-615(a). The sale would constitute a disposition under this Article and, as
11 such, would give rise to the consequences specified in this Part. SP would
12 have a conversion claim against Merchant, and the debtor could assert its
13 rights under Part 6 arising out SP's (probably) noncomplying disposition.

14 **SECTION 9-616. RIGHTS AND DUTIES OF CERTAIN [SECONDARY**
15 **OBLIGORS] [PERSONS LIABLE TO SECURED PARTY].**

16 (a) A [secondary obligor] [person that is liable to a secured party under a
17 guaranty, indorsement, repurchase agreement, or the like] acquires the rights and
18 ~~[assumes]~~ ~~[becomes obligated to perform]~~ the duties of the secured party after ~~if~~ the
19 [person] [secondary obligor]:

20 (1) receives an assignment of a secured obligation from the secured
21 party;

22 (2) receives a transfer of collateral from the secured party ~~[and agrees to~~
23 accept the rights and assume the duties of the secured party]; or

24 (3) is subrogated to the rights of a secured party with respect to
25 collateral.

26 (b) An assignment, transfer, or subrogation described in subsection (a) is
27 not a disposition of collateral under [Section 9-610] [this article] and does not
28 relieve the secured party of its duties under this article.

29 Reporters' Comments

30 **Changes from Prior Draft:** See Comments 3 and 4.

31 **1. Source.** Former Section 9-504(5).

1 **2. Scope of This Section.** Under this section, assignments of secured
2 obligations and other transactions (regardless of form) that function like
3 assignments of secured obligations are not dispositions to which Part 6 applies.
4 Rather, they constitute assignments of rights and (occasionally) delegations of
5 duties. Application of this section may require an investigation into the agreement
6 of the parties, which may not be reflected in the words of the repurchase agreement
7 (e.g., when the agreement requires a recourse party to “purchase the collateral” but
8 contemplates that the purchaser will then conduct an Article 9 foreclosure sale).

9 This section, like former Section 9-504(5), does not constitute a general and
10 comprehensive rule for allocating rights and duties upon assignment of a secured
11 obligation. Rather, it applies only in the recourse situations described in the first
12 clause of subsection (a). In this regard, we suggest that the Drafting Committee
13 consider whether term “secondary obligor,” defined in Section 9-102, should
14 replace the newly bracketed language in subsection (a), which originally was taken
15 from former Section 9-504(5). In other contexts, the agreement of the parties and
16 applicable law determine whether the assignment imposes upon the assignee any
17 duty to the debtor and whether the assignor retains its duties to the debtor after the
18 assignment.

19 Subsection (a)(1) applies when there has been an assignment of an
20 obligation that is secured at the time it is assigned. Thus, if a secondary obligor
21 acquires the collateral at a disposition under Section 9-610 and simultaneously or
22 subsequently discharges the unsecured deficiency claim, subsection (a)(1) is not
23 implicated. Similarly, subsection (a)(3), as revised, applies only when the
24 secondary obligor is subrogated to the secured party’s rights with respect to
25 collateral. Thus, this subsection will not be implicated if a secondary obligor
26 discharges the debtor’s unsecured obligation for a post-disposition deficiency.
27 Similarly, if the secured party disposes of some of the collateral and the secondary
28 obligor thereafter discharges the remaining obligation, subsection (a) applies only
29 with respect to rights and duties with respect to the remaining collateral and, under
30 subsection (b), the subrogation is not a disposition *of the remaining collateral*.

31 As discussed more fully in the following comment, a secondary obligor may
32 receive a transfer of collateral in a disposition made under Section 9-610 in
33 exchange for a payment that is applied against the secured obligation. However, a
34 secondary obligor that pays and receives a transfer of collateral does not necessarily
35 become subrogated to the rights of the secured party as contemplated by subsection
36 (a)(3). Only to the extent the secondary obligor makes a payment in satisfaction of
37 its secondary obligation would it become subrogated. To the extent its payment
38 constitutes the price of the collateral in a Section 9-610 disposition by the secured
39 party, the secondary obligor would not be subrogated. Thus, if the amount paid by
40 the secondary obligor for the collateral in a Section 9-610 disposition is insufficient
41 to discharge the secured obligation and the secondary obligor satisfies the
42 remaining balance, it would be subrogated to the secured party’s deficiency claim.
43 But the duties of the secured party *as such* would have come to an end with respect
44 to that collateral. In some situations the capacity in which the payment is made
45 may be unclear. Accordingly, the parties should in their relationship provide clear
46 evidence of the nature and circumstances of the payment by the secondary obligor.

1 **3. Transfer of Collateral to Secondary Obligor.** We have deleted the
2 brackets in subsection (a)(2), retaining the previously bracketed language. As
3 revised, it is possible for a secured party to transfer collateral to a secondary obligor
4 in a transaction that is a disposition under Section 9-610 and that establishes a
5 surplus or deficiency under Section 9-614. Deleting the bracketed language would
6 have been inconsistent with the Drafting Committee's decision to adopt a special
7 rule, in Section 9-614(f), for establishing a deficiency in the case of dispositions to,
8 *inter alia*, secondary obligors. If a disposition to a secondary obligor would never
9 constitute a disposition under Section 9-610, the Drafting Committee's decision
10 would have been superfluous. Given the difficult and time-consuming efforts to
11 reach the compromise and consensus on the approach taken in Section 9-614, we
12 are reluctant to encourage or facilitate a fundamental change.

13 Some advocates for consumers have objected to retaining the bracketed
14 language in subsection (a)(2). They read former Section 9-504(5) to provide that a
15 transfer of collateral can *never* constitute a disposition of collateral under that
16 section. They argue that their reading provides a "protection for debtors from
17 unfair "churning of collateral by dealers who, under recourse arrangements, buy
18 collateral at low prices (with resulting high deficiencies and corresponding high
19 profits on resale by the dealer). We doubt that theirs is a reasonable construction of
20 the statute or that the results they advocate were intended. It would be odd that a
21 secured party could itself buy collateral at its own public sale while a recourse party
22 would be entirely prohibited from purchasing at the sale.

23 One possible approach toward further compromise would be to permit
24 secondary obligors to purchase collateral under Section 9-614 only a public sale--
25 essentially the same rule that applies for secured parties. That approach might
26 unnecessarily interfere with existing commercial practices, however. On balance,
27 we suspect that the compromise worked out for Section 9-614(f) offers an
28 appropriate middle ground.

29 **4. Timing and Scope of Obligations.** The word "after" now replaces the
30 word "if" at the end of the introductory portion of subsection (a). This change is
31 intended to make clear that when a successor assignee, transferee, or subrogee
32 becomes obligated it does not assume any liability for earlier actions or inactions of
33 the secured party that it has succeeded. Once the successor becomes obligated,
34 however, it is responsible for complying with the secured duties thereafter. For
35 example, if the successor is in possession of collateral it has the duties specified in
36 Section 9-207. Some concern has been expressed about imposing obligations on
37 (for example) a subrogee who does not take any steps to enforce a security interest
38 or who may not even be aware that its subrogation rights and duties have arisen.
39 Because Article 9 generally places no affirmative duties of enforcement on a
40 secured party, we doubt that this situation presents a practical problem. It may
41 require some adjustment to the secured parties duties under Section 9-209,
42 however.

43 **SECTION 9-617. TRANSFER OF RECORD OR LEGAL TITLE.**

1 (a) In this section, "transfer statement" means a record authenticated by a
2 secured party stating:

3 (1) that the debtor has defaulted in connection with an obligation
4 secured by specified collateral;

5 (2) that the secured party has exercised its post-default remedies with
6 respect to the collateral;

7 (3) that, by reason of the exercise, a transferee has acquired the rights of
8 the debtor in the collateral; and

9 (4) the name and mailing address of the secured party, the debtor, and
10 the transferee.

11 (b) A transfer statement entitles the transferee to the transfer of record of all
12 rights of the debtor in the collateral specified in the statement in any official filing,
13 recording, registration, or certificate-of-title system covering the collateral. If a
14 transfer statement is presented with the applicable fee and request form to the
15 official or office responsible for maintaining the system, the official or office must
16 accept the transfer statement, promptly amend its records to reflect the transfer, and,
17 if applicable, issue a new appropriate certificate of title in the name of transferee.

18 (c) A transfer of the record or legal title to collateral to a secured party is
19 not of itself a disposition of collateral under this article and does not of itself relieve
20 the secured party of its duties under this article.

21 Reporters' Comments

22 1. **Source.** New.

23 2. **Transfer of Record or Legal Title.** Potential buyers of collateral that is
24 covered by a certificate of title (e.g., an automobile) or is subject to a registration
25 system (e.g., a copyright) typically require as a condition of their purchase that the
26 certificate or registry reflect their ownership. In many cases, this condition can be
27 met only with the consent of the record owner. If the record owner is the debtor
28 and, as often is the case after the default, the debtor refuses to cooperate, the
29 secured party may have great difficulty disposing of the collateral. Applicable non-
30 UCC law (e.g., a certificate-of-title act, federal registry, or the like) may provide a

1 means by which the secured party obtains record or legal title for the purpose of a
2 subsequent disposition of the property under this Article.

3 Subsection (b) provides a simple mechanism for obtaining record or legal
4 title, for use primarily when other law does not provide one. Of course, use of this
5 mechanism will not be effective to clear title to the extent that subsection (b) is
6 preempted by federal law. The Drafting Committee has not yet considered whether
7 this mechanism should be available if other law provides a separate title-clearing
8 mechanism. Subsection (c) acknowledges that obtaining record or legal title under
9 subsection (b) or under other law merely puts the secured party in a position to pass
10 legal or record title to a transferee at foreclosure. A secured party that has obtained
11 record or legal title retains its duties with respect to enforcement of its security
12 interest, and the debtor retains its rights as well.

13 **SECTION 9-618. ACCEPTANCE OF COLLATERAL IN FULL OR**
14 **PARTIAL SATISFACTION OF OBLIGATION; COMPULSORY**
15 **DISPOSITION OF COLLATERAL.**

16 (a) In this section and in Sections 9-619 and 9-620, “proposal” means a
17 [written] statement authenticated by a secured party containing the terms on which
18 the secured party is willing to accept collateral in full or partial satisfaction of the
19 obligation it secures.

20 (b) A secured party may accept collateral in full or partial satisfaction of the
21 obligation it secures only if:

22 (1) the debtor consents to the acceptance under subsection (d);

23 (2) the secured party does not receive, within the time set forth in
24 subsection (e), a notification of objection to the proposal authenticated by a person
25 to which the secured party was required to send a proposal under Section 9-619 or
26 any other person holding an interest in the collateral subordinate to the security
27 interest that is the subject of the proposal; and

28 (3) if the collateral is consumer goods, the collateral is not in the
29 possession of the debtor when the debtor consents to the acceptance.

1 (c) A purported or apparent acceptance of collateral under this section is
2 ineffective unless the secured party:

3 (1) consents to the acceptance in an authenticated record or sends to the
4 debtor a proposal; and

5 (2) the conditions of subsection (b) are met.

6 (d) For purposes of this section:

7 (1) a debtor consents to an acceptance of collateral in partial satisfaction
8 of the obligation it secures only if the debtor agrees to the terms of the acceptance
9 in a record authenticated after default; and

10 (2) a debtor consents to an acceptance of collateral in full satisfaction of
11 the obligation it secures only if the debtor agrees to the terms of the acceptance in a
12 record authenticated after default or the secured party:

13 (A) sends to the debtor after default a proposal that is unconditional
14 or subject only to a condition that collateral not in the possession of the secured
15 party be preserved or maintained;

16 (B) in the proposal, proposes to accept collateral in full satisfaction
17 of the obligation it secures; and

18 (C) does not receive a notification of objection authenticated by the
19 debtor within 20 days after the proposal is sent.

20 (e) To be effective under subsection (b)(2), a notification of objection must
21 be received by the secured party:

22 (1) in the case of a person to which the proposal was sent pursuant to
23 Section 9-619, within 20 days after notification was sent to that person; and

24 (2) in other cases, within 20 days after the last notification was sent
25 pursuant to Section 9-619 or, if a notification was not sent, before the debtor
26 consents to the acceptance under subsection (d).

(f) If 60 percent of the cash price has been paid in the case of a purchase money security interest in consumer goods or 60 percent of the principal amount of the obligation secured has been paid in the case of another security interest in consumer goods[, and the debtor has not consented to an acceptance,] a secured party that has taken possession of collateral shall dispose of the collateral pursuant to Section 9-610 within 90 days after taking possession or within any extended period to which all secondary obligors have agreed by signing a statement to that effect after default.

Reporters' Comments

Discussion Question: We have placed brackets around a clause in subsection (f). Our notes of the March, 1997 meeting reflect the Drafting Committee's vote to permit partial strict foreclosures in consumer goods transactions was "subject to the 60 percent mandatory disposition rule of subsection (f). Should the bracketed phrase be deleted?

1. **Source.** Former Section 9-505, completely rewritten.

2. **Overview and Organization.** This section and the two sections following deal with strict foreclosure, a procedure by which the secured party acquires the debtor's interest in the collateral without the need for a sale or other disposition under Section 9-610. The provisions have been entirely reorganized and substantially rewritten. The more straightforward approach taken in this Article eliminates the fiction that the secured party always will present a "proposal for the retention of collateral and the debtor will have a fixed period to respond. By eliminating the need (but preserving the possibility) for proceeding in this fashion, this section eliminates much of the awkwardness of former Section 9-505. It reflects the belief that strict foreclosures should be encouraged and often will produce better results than a disposition for all concerned. This Comment explains how the three sections are organized. The following Comments contain a subsection-by-subsection analysis of the text.

Subsection (b) sets forth the conditions necessary to an effective acceptance (formerly, retention) of collateral in full or partial satisfaction of the secured obligation. The first condition is that the debtor must consent to the acceptance. Subsection (d) provides that this consent must be manifested either by the debtor's post-default, authenticated agreement to the acceptance or, in the case of an acceptance in full satisfaction, by the debtor's 20-day silence after receipt of an authenticated "proposal (as defined in subsection (a)). Subsection (c) conditions the effectiveness of an apparent acceptance on the secured party's authenticated acceptance or its sending a proposal; "constructive or "deemed acceptances are not effective.

1 The second condition necessary to an effective acceptance of collateral is
2 the absence of a timely objection from a person that holds an interest subordinate to
3 the security interest in question. Subsection (e) indicates when an objection is
4 timely. If either of these conditions is not met, any purported or apparent
5 acceptance in satisfaction is ineffective.

6 The third condition applies only in a consumer goods secured transaction:
7 the collateral may not be in the possession of the debtor when the debtor consents
8 to the acceptance.

9 In addition to the conditions described above, Section 9-619 requires that a
10 secured party that wishes to proceed under this section notify certain other persons
11 that have or that claim an interest in the collateral. Unlike the failure to meet the
12 conditions in subsection (b), under Section 9-620(b) the failure to comply with the
13 notification requirement of Section 9-619 does not render the acceptance of
14 collateral ineffective. Rather, the acceptance can take effect notwithstanding the
15 secured party's noncompliance. Section 9-620(b) indicates that a person to which
16 the required notice was not sent has the right to recover damages under Section
17 9-624(b). Section 9-620(a) sets forth the effect of an acceptance of collateral.

18 **3. Proposals.** Subsection (a) defines the term "proposal. A "proposal is
19 necessary only if the debtor does not agree to an acceptance in an authenticated
20 record as described in subsection (d)(1) or (d)(2). A proposal under subsection (a)
21 need not take any particular form as long as it sets forth the terms under which the
22 secured party is willing to accept collateral in satisfaction. A proposal to accept
23 collateral should specify the amount (or a means of calculating the amount, such as
24 by including a per diem accrual figure) of the secured obligations to be satisfied,
25 state the conditions (if any) under which the proposal may be revoked, and describe
26 any other applicable conditions. Note, however, that a conditional proposal
27 generally requires the debtors agreement in order to take effect. See subsection (d),
28 discussed in the following Comment.

29 **4. Conditions to Effective Acceptance.** Subsection (b) contains the
30 conditions necessary to the effectiveness of an acceptance of collateral. Subsection
31 (b)(1) requires the debtor's consent. Under subsections (d)(1) and (d)(2), the debtor
32 may consent by agreeing to the acceptance in writing after default. Subsection
33 (d)(2) contains an alternative method by which to satisfy the debtor's-consent
34 condition in subsection (b)(1). It follows the proposal-and-objection model found
35 in former Section 9-505: The debtor consents if the secured party sends a proposal
36 to the debtor and does not receive an objection within 20 days. Subsection (d)(1)
37 provides that silence is not deemed to be consent with respect to acceptances in
38 partial satisfaction. Thus, a secured party that wishes to conduct a "partial strict
39 foreclosure must obtain the debtor's agreement in an record authenticated after
40 default. In all other respects, the conditions necessary to an effective partial strict
41 foreclosure are the same as those governing acceptance of collateral in full
42 satisfaction.

43 The time when a debtor consents to a strict foreclosure is significant in
44 several circumstances under this section and the following one. See Sections
45 9-618(b)(1), (b)(3), (e)(2); 9-619(a)(1), (a)(2), (a)(3). For purposes of determining
46 the time of consent, a debtor's conditional consent constitutes consent.

1 Subsection (b)(2) contains the second condition to the effectiveness of an
2 acceptance under this section—the absence of an objection from a person holding a
3 junior interest in the collateral or from a secondary obligor. Any junior
4 party—secured party or lienholder—is entitled to lodge an objection to a proposal,
5 even if that person was not entitled to notification under Section 9-619. Subsection
6 (e), discussed below, indicates when an objection is timely.

7 In a consumer goods secured transaction, an acceptance is not effective
8 unless the collateral is not in the possession of the debtor when the debtor consents
9 to the acceptance. Subsection (b)(3).

10 **5. Secured Party's Agreement.** The conditions of subsection (b) relate to
11 actual or implied consent by the debtor and any secondary obligor or holder of a
12 junior security interest or lien. To insure that the debtor cannot unilaterally cause
13 an acceptance of collateral, subsection (c) provides that compliance with these
14 conditions is necessary but not sufficient to cause an acceptance of collateral.
15 Rather, under subsection (c), acceptance does not occur unless, in addition, the
16 secured party consents to the acceptance in an authenticated record or sends to the
17 debtor a proposal.

18 **6. When Acceptance Occurs.** This section does not impose any
19 formalities or identify any steps that a secured party must take in order to accept
20 collateral once the conditions of subsections (b) and (c) have been met. Absent
21 facts or circumstances indicating a contrary intention, the fact that the conditions
22 have been met provides a sufficient indication that the secured party has accepted
23 the collateral on the terms to which the debtor has agreed or failed to object.
24 Acceptance of the collateral normally is automatic upon the secured party's
25 becoming bound and the time for objection passing. As a matter of good business
26 practice, an enforcing secured party may wish to memorialize its acceptance, such
27 as by notifying the debtor that the strict foreclosure is effective or by placing a
28 written record to that effect in its files. The secured party's agreement to accept
29 collateral is self-executing and cannot be breached. The secured party is bound by
30 its agreement to accept collateral and by any proposal to which the debtor consents.

31 **7. No Possession Requirement.** This section eliminates the former
32 requirement that the secured party be "in possession of collateral. Intangible
33 collateral, which cannot be possessed, may be subject to a strict foreclosure under
34 this section. However, under subsection (b)(3), if the collateral is consumer goods,
35 acceptance does not occur unless the debtor is not in possession.

36 **8. No Constructive Strict Foreclosure.** Under subsection (c), a delay in
37 collection or disposition of collateral does not constitute a "constructive strict
38 foreclosure. Instead, a delay that is unreasonable may be a factor relating to
39 whether the secured party acted in a commercially reasonable manner for purposes
40 of Section 9-607 or 9-610. A debtor's voluntary surrender of collateral to a secured
41 party and the secured party's acceptance of possession of the collateral raises no
42 implication whatsoever that the secured party intends or is proposing to accept the
43 collateral in satisfaction of the secured obligation under this section.

44 **9. When Objection Timely.** Subsection (e) explains when an objection is
45 timely and thus prevents an acceptance of collateral from taking effect. An

1 objection by a person to which notification was sent under Section 9-619 is
2 effective if it is received by the secured party within 20 days from the date the
3 notification was sent to that person. Other objecting parties (i.e., third parties that
4 are not entitled to notification) may object at any time within 20 days after the last
5 notification is sent under Section 9-619. If no such notification is sent, third parties
6 must object before the debtor agrees to the acceptance in writing or is deemed to
7 have consented by silence. The former may occur any time after default, and the
8 latter requires a 20-day waiting period.

9 **10. Applicability of Other Law.** This section does not purport to regulate
10 all aspects of the transaction by which a secured party may become the owner of
11 collateral previously owned by the debtor. For example, a secured party's
12 acceptance of a motor vehicle in satisfaction of secured obligations may require
13 compliance with the applicable motor vehicle certificate-of-title law. State
14 legislatures should conform those laws so that they mesh well with this section and
15 Section 9-610, and courts should construe those laws and this section
16 harmoniously. A secured party's acceptance of collateral in the possession of the
17 debtor also may implicate statutes dealing with a seller's retention of possession of
18 goods sold. See, e.g., Cal. Civ. Code § 3440.1-9.

19 **11. Accounts, Chattel Paper, and Payment Intangibles.** If the collateral
20 is accounts, chattel paper, or payment intangibles, then a secured party's acceptance
21 of the collateral in satisfaction of secured obligations would constitute a sale to the
22 secured party. That sale would give rise to a new security interest (the ownership
23 interest) under Sections 1-201(37) and 9-112. The new security interest would
24 remain perfected by a filing that was effective to perfect the secured party's original
25 security interest. However, the procedures for acceptance of collateral under this
26 section satisfy all necessary formalities and a new security agreement authenticated
27 by the debtor would not be necessary.

28 **12. Obligation to Dispose of Consumer Goods.** Subsection (f) imposes
29 an obligation on the secured party to dispose of consumer goods under certain
30 circumstances. Regarding the 60% test, see the Comments to Section 9-622.

31 **SECTION 9-619. NOTIFICATION OF PROPOSAL TO ACCEPT**
32 **COLLATERAL.** A secured party that desires to accept collateral in partial
33 satisfaction of the obligation it secures shall send its proposal to any secondary
34 obligor, and a secured party that desires to accept collateral in full or partial
35 satisfaction of the obligation it secures shall send its proposal also to:

36 (1) any person from which the secured party has received, before the debtor
37 consented to the acceptance, an authenticated notification of a claim of an interest
38 in the collateral;

1 (2) any other secured party or lienholder that, [] days before the debtor
2 consented to the acceptance, held a security interest in or other lien on the collateral
3 perfected by the filing of a financing statement that identified the collateral, was
4 indexed under the debtor's name as of that date, and was filed in the office or
5 offices in which to file a financing statement against the debtor covering the
6 collateral as of that date; and

7 (3) any other secured party that, [] days before the debtor consented to the
8 acceptance, held a security interest in the collateral perfected by compliance with a
9 statute or treaty described in Section 9-309A(a).

10 Reporters' Comments

11 1. **Source.** Former Section 9-505, substantially expanded.

12 2. **Notification.** This section specifies three classes of competing claimants
13 to which the secured party must send notification of its proposal: (i) those that
14 notify the secured party that they claim an interest in the collateral, (ii) holders of
15 certain security interests and liens which have filed against the debtor, and (iii)
16 holders of certain security interests and liens which have perfected by compliance
17 with a certificate-of-title statute. With regard to (ii), see the Comment to Section
18 9-611. This section also requires notification to any secondary obligor if the
19 proposal is for acceptance in partial satisfaction.

20 **SECTION 9-620. EFFECT OF ACCEPTANCE OF COLLATERAL.**

21 (a) A secured party's acceptance of collateral in full or partial satisfaction
22 of the obligation it secures:

23 (1) discharges the obligation to the extent consented to by the debtor,
24 but recovery of a deficiency is subject to Section 9-625;

25 (2) transfers to the secured party all of a debtor's rights in the collateral;

26 (3) discharges the security interest or agricultural lien that is the subject
27 of the debtor's consent and any subordinate security interest or other lien; and

28 (4) terminates any other subordinate interest.

1 (b) A subordinate interest is discharged or terminated under subsection (a)
2 whether or not the secured party is required to send or does send its proposal to the
3 holder of the interest. However, any person to which the secured party was
4 required to send, but did not send, its proposal has the remedy provided by Section
5 9-624(b).

6 Reporters' Comments

7 1. **Source.** New.

8 2. **Effect of Acceptance.** Subsection (a) specifies the effect of an
9 acceptance of collateral in full or partial satisfaction of the secured obligation.
10 Paragraph (1) expresses the fundamental consequence of accepting collateral in full
11 or partial satisfaction of the secured obligation—the obligation is discharged to the
12 extent consented to by the debtor. Paragraphs (2) through (4) indicate the effects of
13 an acceptance on various property rights and interests. Paragraph (2) follows
14 Section 9-615(a) in providing that the secured party acquires “all of a debtor’s
15 rights in the collateral. Under paragraph (3), the effect of strict foreclosure on
16 holders of junior security interests and liens is the same regardless of whether the
17 collateral is accepted in full or partial satisfaction of the secured obligation: all
18 junior encumbrances are discharged. Subsection (b) makes clear that this is the
19 effect regardless of whether a proposal was required to be sent or, if required, was
20 sent. Paragraph (4) provides for the termination of other subordinate interests.
21 Given the breadth of the definition of the term debtor, however, paragraph (2) may
22 render paragraph (4) superfluous.

23 **SECTION 9-621. RIGHT TO REDEEM COLLATERAL.** At any time
24 before a secured party has collected collateral under Section 9-607, disposed of
25 collateral or entered into a contract for its disposition under Section 9-610, or
26 accepted collateral in full or partial satisfaction of the obligation it secures under
27 Section 9-618, the debtor, any secondary obligor, or any other secured party or
28 lienholder may redeem the collateral by tendering fulfillment of all obligations
29 secured by the collateral as well as the reasonable expenses and attorney's fees
30 described in Section 9-614(b)(1).

31 Reporters' Comments

32 1. **Source.** Former Section 9-506.

1 2. **Redemption.** Subsection (a) follows former Section 9-506 but extends
2 the right of redemption to holders of nonconsensual liens. Most of the other
3 changes are not substantive.

4 3. **Effect of “Repledging.”** Section 9-207 generally permits a secured
5 party to create a security interest in the collateral. As explained in the Comments to
6 that section, the debtor’s right (as opposed to its practical ability) to redeem
7 collateral is not affected by, and does not affect, the priority of a security interest
8 created by the debtor’s secured party.

9 **SECTION 9-622. REINSTATEMENT OF OBLIGATION SECURED**
10 **WITHOUT ACCELERATION.**

11 (a) If 60 percent of the cash price has been paid in the case of a purchase
12 money security interest in consumer goods or 60 percent of the principal amount of
13 the obligation secured has been paid in the case of another consumer goods secured
14 transaction, a debtor or a secondary obligor who is a consumer obligor may cure a
15 default consisting only of the failure to make a required payment and may reinstate
16 the secured obligation without acceleration by tendering the unpaid amount of the
17 secured obligation due at the time of tender, without acceleration, including charges
18 for delinquency, default, or deferral, and reasonable expenses and attorney’s fees
19 described in Section 9-614(b)(1).

20 (b) A tender of payment under subsection (a) is ineffective to cure a default
21 or reinstate a secured obligation unless made before the later of:

22 (1) 21 days after the secured party sends a notification of disposition
23 under Section 9-611(b) to the debtor and any consumer obligor who is a secondary
24 obligor; and

25 (2) the time the secured party disposes of collateral or enters into a
26 contract for its disposition under Section 9-610 or accepts collateral in full or partial
27 satisfaction of the obligation it secures under Section 9-618.

1 (c) A tender of payment under subsection (a) restores to the debtor and a
2 consumer obligor who is a secondary obligor their respective rights as if the default
3 had not occurred and all payments had been made when scheduled, including the
4 debtor's right, if any, to possess the collateral. Promptly upon the tender, the
5 secured party shall take all steps necessary to cause any judicial process affecting
6 the collateral to be vacated and any pending action based on the default to be
7 dismissed.

8 (d) A secured obligation may be reinstated under subsection (a) only once.

9 Reporters' Comments

10 1. **Source.** New.

11 2. **Reinstatement.** This section provides a one-time right to reinstatement
12 of a debt following a default consisting only of the failure to make one or more
13 payments. It applies only in a consumer goods secured transaction in which 60
14 percent or more of the cash price or secured obligation has been paid. Application
15 of the 60 percent test is straightforward when an item of collateral secures only its
16 purchase price or a single obligation. In the less typical case in which an item of
17 collateral secures several obligations, its application is more difficult. In the
18 interest of avoiding unnecessary statutory complexity, however, the statute leaves it
19 to the [agreement of the parties and the] courts to work out sensible approaches.
20 For example, if an item secures its own purchase money debt as well as other
21 obligations, the 60 percent test should take into account only the purchase money
22 debt. The debtor could elect to cure a default on that debt which, in turn, also
23 would cure defaults on other debt arising out of "cross-defaults" based on the
24 purchase money debt. On the other hand, if an item secures several non-purchase
25 money obligations, the 60 percent test should be applied to the aggregate amount of
26 the obligations at the time of the debtor's or secondary obligor's tender.

27 3. **Waiver or Variance.** The debtor's rights under this section may not be
28 waived or varied by agreement, see Section 9-602(a)(9), except as otherwise
29 provided in Section 9-623(a). Likewise, this section overrides any contrary
30 agreement adversely affecting the debtor's rights, such as a provision for a higher
31 finance charge following a reinstatement. However, this section does not prevent a
32 secured party from making an enforceable agreement granting the debtor additional
33 reinstatement rights, which may be more generous than those that this section
34 provides.

35 **SECTION 9-623. WAIVER.**

36 (a) Subject to subsection (c), a debtor or a consumer obligor in a consumer
37 goods secured transaction may waive the right to notification of disposition of

1 collateral under Section 9-611, the right to redeem the collateral under Section
2 9-621, or the right to reinstate a secured obligation under Section 9-622 only by
3 signing a record containing a statement to that effect after default.

4 (b) Subject to subsection (c), a consumer obligor in a consumer goods
5 secured transaction may waive the obligor's rights and the secured party's duties
6 under Section 9-618 or 9-619 only by signing a record containing a statement to
7 that effect after default.

8 [(c) In a consumer goods secured transaction, a statement authenticated by
9 the debtor or a consumer obligor is ineffective under subsection (a) or (b) unless the
10 secured party establishes by clear and convincing evidence that the debtor or
11 consumer obligor expressly agreed to its terms.]

12 Reporters' Comments

13 1. **Source.** Former Sections 9-504(3); 9-505; 9-506.

14 2. **Waiver.** This section is a limited exception to Section 9-602, which
15 generally prohibits waiver by debtors or by consumer obligors in consumer goods
16 secured transactions. It makes no provision for waiving the rule prohibiting a
17 secured party from buying at its own private sale. Transactions of this kind are
18 equivalent to "strict foreclosures" and are governed by Section 9-619.

19 The brackets around subsection (c) indicate division among the Drafting
20 Committee as to whether the secured party should bear the burden of proving that a
21 debtor expressly agreed to the terms of a purported waiver in consumer goods
22 secured transactions.

23 [SUBPART 2. NONCOMPLIANCE WITH ARTICLE.]

1 **SECTION 9-624. REMEDIES FOR SECURED PARTY'S FAILURE TO**
2 **COMPLY WITH THIS ARTICLE.**

3 (a) If it is established that a secured party is not proceeding in accordance
4 with this article, a court may order or restrain collection, enforcement, or
5 disposition of collateral on appropriate terms and conditions.

6 (b) A secured party is liable for damages in the amount of any loss caused
7 by a failure to comply with this article. Except as otherwise provided in Section
8 9-627, a person that, at the time of the failure, was a debtor, was a secondary
9 obligor, or held a security interest in or other lien on the collateral has a right to
10 recover damages for its loss under this subsection. A debtor whose deficiency is
11 eliminated under Section 9-625 may recover damages for the loss of any surplus,
12 but a debtor or consumer obligor whose deficiency is eliminated or reduced under
13 Section 9-625 may not otherwise recover under this subsection for noncompliance
14 with [Sections 9-607 through 9-614] [the provisions of this part relating to
15 collection, enforcement, disposition, or acceptance].

16 (c) Except as otherwise provided in Section 9-627, in a consumer goods
17 secured transaction, a person that was a debtor at the time a secured party failed to
18 comply with this part has a right to recover from the noncomplying secured party an
19 amount equal to the interest or finance charges plus 10 percent of the principal
20 amount of the obligation less the sum of:

21 (1) any amount by which any consumer obligor's personal liability for a
22 deficiency is eliminated or reduced under Section 9-625; and

23 (2) any amount for which the secured party is liable under subsection
24 (b).

25 ~~This subsection does not apply if the only failure to comply is a failure to send a~~
26 ~~written notification pursuant to Section 9-614A.~~

(d) The secured party has the burden of establishing the amount of any deduction under paragraph (c)(1).

(e) ~~(d)~~ A secured party that fails to comply with Section 9-208, a person that files ~~an initial financing statement or an amendment~~ a record that the person is not entitled to file under ~~in violation of~~ Section 9-508(a), a secured party ~~of record~~ that fails to cause the secured party of record to file or send a termination statement as required by Section 9-511 ~~(b) or (c)~~, or a secured party that fails to comply with Section 9-614A ~~(c)(2)~~ is liable to the debtor or requestor, as applicable, in each case for \$500 and, in addition, for any damages under subsection (b).

(f) ~~(e)~~ A person that, without reasonable excuse, fails to comply with a request under Section 9-209 is liable to the debtor for \$500, for damages in the amount of any loss resulting from the debtor's inability to obtain, or increased costs of, alternative financing, and, in addition, for any damages under subsection (b). A recipient of a request under Section 9-209 which never claimed an interest in the collateral or obligations that are the subject of a request under that section has a reasonable excuse for failure to comply with the request.

(g) ~~(f)~~ As against a person reasonably misled by a secured party's failure to comply with a request regarding a list of collateral or a statement of account under Section 9-209, the secured party may claim a security interest only as shown in the statement contained in the request.

Reporters' Comments

Change from Prior Draft:

627. A. The last sentence of subsection (c) has been relocated to Section 9-

B. The \$500 minimum recovery in subsection (e) applies only to the secured party's failure to comply with the requirement in Section 9-614A(c)(2) to a request for an explanation of how a deficiency or surplus was calculated. It does not apply to the secured party's failure to comply with the requirement in Section 9-614A(c)(1) to send an explanation in the absence of a request.

1 1. **Source.** Former Section 9-507.

2 2. **Scope.** Subsections (a) and (b) no longer are limited to noncompliance
3 with provisions of this part of Article 9; rather they apply to noncompliance with
4 any provision of this Article. The change makes this section applicable to
5 noncompliance with Sections 9-207 (duties of secured party in possession of
6 collateral); 9-208 (duties of secured party having control over deposit account);
7 9-209 (duty to comply with request for accounting, etc.); 9-508(a) (duty to refrain
8 from filing unauthorized financing statement); and 9-511(c) (duty to provide
9 termination statement). Subsections (d), (e), and (f) impose supplemental damages
10 for violation of those sections. Subsection (c), which gives a minimum damage
11 recovery in consumer goods secured transactions, applies only to noncompliance
12 with the provisions of this part.

13 3. **Injunctions.** Subsection (a) modifies the first sentence of former
14 subsection (1) by adding the references to “collection” and “enforcement.”

15 4. **Damages for Noncompliance with this Article.** Subsection (b) sets
16 forth the basic remedy for failure to comply with the requirements of this Article: a
17 damage recovery in the amount of loss caused by the noncompliance. This
18 subsection affords a remedy to any aggrieved person that is a secondary obligor or
19 that holds a competing security interest or lien, regardless of whether the aggrieved
20 person is entitled to notification under Part 6. The remedy is available even to
21 holders of senior security interests and liens. The exercise of this remedy is subject
22 to the normal rules of pleading and proof. A person that has delegated the duties of
23 a secured party but that remains obligated to perform them is liable under this
24 subsection. The last sentence of subsection (b) eliminates the possibility of double
25 recovery or other over-compensation arising out of noncompliance with [Sections
26 9-607 through 9-614] [the provisions of this part relating to collection,
27 enforcement, disposition, or acceptance]. Assuming no double recovery, a debtor
28 whose deficiency is reduced or eliminated under Section 9-625 can pursue a claim
29 for a surplus.

30 5. **Supplemental Damages.** Subsection (d) imposes an additional \$500
31 liability upon a person who makes an unauthorized filing in violation of Section
32 9-508(a). It imposes the same sanction on a person who fails to relinquish control
33 over investment property, a deposit account, or letter-of-credit rights under Section
34 9-208, fails to file or send a termination statement as required by Section 9-511(c),
35 or fails to provide notification of calculation of surplus or deficiency under Section
36 9-614A.

37 Under subsection (e), a person that fails to comply with a request for an
38 accounting or a request regarding a list of collateral or statement of account under
39 Section 9-209 is liable not only for the loss caused (subsection (b)) but also for
40 \$500 and for damages in the amount of any loss resulting from the debtor’s
41 inability to obtain, or increased costs of, alternative financing.

42 6. **Estoppel.** Subsection (f) limits the extent to which a secured party who
43 fails to comply with a request regarding a list of collateral or statement of account
44 may claim a security interest.

7. Minimum Damages in Consumer Goods Secured Transactions.

Subsection (c) provides a minimum damage recovery for debtors in a consumer goods secured transaction. It is designed to insure that every noncompliance with the requirements of Part 6 results in liability, regardless of any injury that may have resulted. If an aggrieved person is entitled to recover damages under subsection (b) or a reduction of personal liability for a deficiency under Section 9-625, those amounts are deducted from the amount available under this subsection. Regarding calculation of the principal amount of the obligation for purposes of this subsection, see the Comments to Section 9-622.

Alternative A

(“Absolute Bar” Rule for Consumer Goods Secured Transactions;

“Rebuttable Presumption” Rule for Other Transactions)

SECTION 9-625. ACTION IN WHICH DEFICIENCY OR SURPLUS IS

IN ISSUE. In an action in which the amount of a deficiency or surplus is in issue, the following rules apply:

(1) A secured party need not establish compliance with [Sections 9-607 through 9-614] [the provisions of this part relating to collection, enforcement, disposition, or acceptance] unless the debtor or a secondary obligor places the secured party's compliance in issue. In that case, the secured party has the burden of establishing that the collection, enforcement, disposition, or acceptance was conducted in accordance with [Sections 9-607 through 9-614, as applicable] [the applicable provisions of this part].

(2) Except as otherwise provided in Section 9-627, if a secured party fails to prove that the collection, enforcement, disposition, or acceptance was conducted in accordance with [Sections 9-607 through 9-614] [the provisions of this part relating to collection, enforcement, disposition, or acceptance]:

(A) In a consumer goods secured transaction for which no other property remains to secure the obligation, neither the debtor nor a secondary obligor is liable for a deficiency.

1 (B) In other cases, the liability of a debtor or a secondary obligor for a
2 deficiency is limited to an amount by which the sum of the secured obligation,
3 expenses, and attorney's fees exceeds the greater of the proceeds of the collection,
4 enforcement, disposition, or acceptance or the amount of proceeds that would have
5 been realized had the noncomplying secured party proceeded in accordance with
6 [Sections 9-607 through 9-614] [the provisions of this part relating to collection,
7 enforcement, disposition, or acceptance]. However, the amount that would have
8 been realized is equal to the sum of the secured obligation, expenses, and attorney's
9 fees unless the secured party proves that the amount is less than that sum.

10 (C) In a consumer goods secured transaction, liability under paragraph
11 (B) is not a personal liability of a consumer obligor but may be satisfied only by
12 enforcing a security interest or other consensual lien against property securing the
13 obligation.

14 **Alternative B**
15 **("Rebuttable Presumption" Rule for All Transactions)]**

16 **SECTION 9-625. ACTION IN WHICH DEFICIENCY OR SURPLUS IS**
17 **IN ISSUE.** In an action in which the amount of a deficiency or surplus is in issue,
18 the following rules apply:

19 (1) A secured party need not establish compliance with [Sections 9-607
20 through 9-614] [the provisions of this part relating to collection, enforcement,
21 disposition, or acceptance] unless the debtor or a secondary obligor places the
22 secured party's compliance in issue. In that case, the secured party has the burden
23 of establishing that the collection, enforcement, disposition, or acceptance was
24 conducted in accordance with [Sections 9-607 through 9-614, as applicable] [the
25 applicable provisions of this part].

(2) Except as otherwise provided in Section 9-627, if a secured party fails to prove that the collection, enforcement, disposition, or acceptance was conducted in accordance with [Sections 9-607 through 9-614,] [the provisions of this part relating to collection, enforcement, disposition, or acceptance,] the liability of a debtor or a secondary obligor for a deficiency is limited to an amount by which the sum of the secured obligation, expenses, and attorney's fees exceeds the greater of the proceeds of the collection, enforcement, disposition, or acceptance or the amount of proceeds that would have been realized had the noncomplying secured party proceeded in accordance with [Sections 9-607 through 9-614] [the provisions of this part relating to collection, enforcement, disposition, or acceptance]. However, the amount that would have been realized is equal to the sum of the secured obligation, expenses, and attorney's fees unless the secured party proves that the amount is less than that sum.

Reporters' Comments

1. **Source.** New.

2. **Scope.** The basic damage remedy under Section 9-624(b) is subject to the special rules contained in this section. This section addresses situations in which the amount of a deficiency or surplus is in issue, i.e., situations in which the secured party has collected, enforced, disposed of, or accepted the collateral. It contains special rules applicable to a determination of the amount of a deficiency or surplus. The rules in this section apply only to noncompliance under [Sections 9-607 through 9-614, as applicable] [the applicable provisions of this part]. For other types of noncompliance with Part 6, the general rule liability rule, recovery of actual damages under Section 9-624(b), applies. Consider, for example, a repossession that does not comply with Section 9-609 for want of a default. The debtor's remedy is under Section 9-624(b). In a proper case the secured party also may be liable for conversion under non-UCC law. If the secured party thereafter disposed of the collateral, however, it would violate Section 9-610 at that time, and this section would apply.

3. **Alternative Versions of Section 9-625.** Courts construing former Section 9-507 have disagreed about the consequences of a secured party's failure to comply with the requirements of former Part 5. Three general approaches have emerged. Some courts have held that a noncomplying secured party may not recover a deficiency (the "absolute bar" rule). Other courts have held that the debtor can offset against a claim to a deficiency all damages recoverable under former Section 9-507 resulting from the secured party's noncompliance (the

1 “offset rule). A plurality of courts considering the issue has held that the
2 noncomplying secured party is barred from recovering a deficiency unless it
3 overcomes a rebuttable presumption that compliance with former Part 5 would have
4 yielded an amount sufficient to satisfy the secured debt (the “rebuttable
5 presumption rule). In addition to the nonuniformity resulting from court
6 decisions, some States have adopted special rules governing the availability of
7 deficiencies.

8 This Article adopts a version of the rebuttable presumption rule for
9 transactions other than consumer goods secured transactions. The Article leaves to
10 each legislature the decision whether to adopt the rebuttable presumption rule for
11 consumer goods secured transactions as well (Section 9-625 Alternative B), or to
12 adopt the absolute bar rule for consumer goods secured transactions (Section 9-625
13 Alternative A).

14 **4. Rebuttable Presumption Rule.** Under paragraph (1), the secured party
15 need not prove compliance with [Sections 9-607 through 9-614, as applicable] [the
16 applicable provisions of this part] as part of its prima facie case. If, however, the
17 debtor raises the issue (in accordance with the forum’s rules of pleading and
18 practice), then the secured party bears the burden of proving that the collection,
19 enforcement, or disposition complied. In the event the secured party is unable to
20 meet this burden, then paragraph (2) explains how to calculate the deficiency. In
21 cases other than consumer goods secured transactions (Alternative A), or in all
22 cases (Alternative B), the rebuttable presumption rule applies. Under this rule, the
23 debtor or obligor is to be credited with the greater of the actual proceeds of the
24 disposition and the proceeds that would have been realized had the secured party
25 complied with [Sections 9-607 through 9-614, as applicable] [the applicable
26 provisions of this part]. If a deficiency remains, then the secured party is entitled to
27 recover it. The references to “the secured obligation, expenses, and attorney’s fees
28 in paragraph (2) (Alternative A) and paragraph (2)(B) (Alternative B) embrace the
29 application rules in Sections 9-608(a) and 9-614(a).

30 Unless the secured party proves that compliance with Part 6 would have
31 yielded a smaller amount, the amount that a complying collection, enforcement, or
32 disposition would have yielded is deemed to be equal to the amount of the secured
33 obligation, together with expenses and attorney’s fees. Thus, the secured party may
34 not recover any deficiency unless it meets this burden of proof. (The UCC does not
35 generally use the terms “prove” or “establish. Rather, it defines “burden of
36 establishing” to mean “the burden of persuading the triers of fact that the existence
37 of the fact is more probable than its non-existence. Section 1-201(8).)

38 **5. Consumer Goods Secured Transactions.** Paragraph (2)(A) of
39 Alternative A provides an “absolute bar” rule for consumer goods secured
40 transactions in which no other property remains to secure the obligation. If other
41 property remains, then the debtor remains liable for a deficiency as calculated under
42 the rebuttable presumption rule (paragraph (2)(B)), but the secured party may
43 collect the deficiency only from other property subject to a security interest or other
44 consensual lien (e.g., real property mortgage). The deficiency may not be collected
45 as a personal liability of the debtor. See paragraph (2)(C).

1 **6. Delay in Applying This Section.** There is an inevitable delay between
2 the time a secured party engages in noncomplying collections or dispositions and
3 the time of a subsequent judicial determination that the secured party did not
4 comply with Part 6. During the interim, the secured party, believing that the
5 secured debt is larger than it ultimately is determined to be, may continue to make
6 collections on and dispositions of collateral. If the secured indebtedness is
7 discharged thereafter by the operation of the rebuttable presumption rule, a
8 reasonable application of this section would impose liability on the secured party
9 for the amount of the excess, unwarranted recoveries.

10 **SECTION 9-626. DETERMINATION OF WHETHER CONDUCT WAS**
11 **COMMERCIALLY REASONABLE.**

12 (a) The fact that a greater amount could have been obtained by a collection,
13 enforcement, disposition, or acceptance at a different time or in a different method
14 from that selected by the secured party is not of itself sufficient to preclude the
15 secured party from establishing that the collection, enforcement, disposition, or
16 acceptance was made in a commercially reasonable manner.

17 (b) A disposition of collateral is made in a commercially reasonable manner
18 if the disposition is made:

19 (1) in the usual manner on any recognized market therefor;

20 (2) at the price current in any recognized market at the time of the
21 disposition; or

22 (3) otherwise in conformity with reasonable commercial practices
23 among dealers in the type of property that was the subject of the disposition.

24 (c) A collection, enforcement, disposition, or acceptance that has been
25 approved in any judicial proceeding or by any [court appointed] bona fide creditors'
26 committee[,] [or] [court appointed] representative of creditors[, or assignee for the
27 benefit of creditors] is commercially reasonable. However, approval need not be
28 obtained, and lack of approval does not mean that the collection, enforcement,
29 disposition, or acceptance is not commercially reasonable.

1. **Source.** Former Section 9-507(2).

2. **Relationship of Price to Commercial Reasonableness.** Some observers have found the notion contained in subsection (a) (former Section 9-507(2)) (the fact that a better price could have been obtained does not establish lack of commercial reasonableness) to be inconsistent with that found in Section 9-610(b) (former Section 9-504(3) (every aspect of the sale, including its terms, must be commercially reasonable). The Drafting Committee perceives no inconsistency, but it favors an explanation of the relationship between price and commercial reasonableness in the Official Comments. In most cases there is a range of commercially reasonable prices that collateral will fetch. Disposing of collateral for a price within that range may be commercially reasonable even though the particular price is not the best price.

The law long has grappled with the problem of dispositions of personal and real property that comply with applicable procedural requirements (e.g., advertising, notice to interested persons, etc.) but which yield an extremely low price. This Article addresses that issue in Section 9-614. That section contains a special rule for determining deficiencies in complying dispositions that yield an unreasonably low price. The section applies only when the transferee is the secured party, its affiliate, or a secondary obligor.

This Article thus rejects the view that the price is one of the “terms” that, under Section 9-610(b), must be commercially reasonable. Rather, except as otherwise provided in Section 9-614(b), a low price is relevant to whether a disposition has been commercially reasonable only to the extent that a low price suggests the need for careful judicial scrutiny of other aspects of the disposition. In fact, where the price is extremely low, other aspects of the disposition (e.g., the time and manner) might well have been commercially unreasonable. But if they were not, then the disposition complies with the requirements of this Article.

3. **“Recognized Market.”** The concept of a “recognized market” in subsections (b)(1) and (2) is quite limited; it applies only to markets where there are standardized price quotations for property that is essentially fungible, such as stock exchanges.

SECTION 9-627. NONLIABILITY AND LIMITATION ON LIABILITY OF SECURED PARTY; LIABILITY OF SECONDARY OBLIGOR.

(a) Unless a secured party knows that a person is a debtor or a secondary obligor, knows the identity of the person, and knows how to communicate with the person:

1 (1) the secured party is not liable to the person or to a secured party or
2 lienholder that has filed a financing statement against the person for failure to
3 comply with this article; and

4 (2) the secured party's failure to comply with this article does not affect
5 the liability of the person for a deficiency.

6 (b) A secured party is not liable to any person and a person's liability for a
7 deficiency is not affected because of any act or omission, other than the failure to
8 send a notification required by Section 9-611(b)(2), that occurs before the secured
9 party knows that the person is a debtor or a secondary obligor or knows that the
10 person has a security interest or other lien in the collateral.

11 (c) A secured party is not liable to any person and a person's liability for a
12 deficiency is not affected because of any act or omission arising out of the secured
13 party's reasonable belief that a transaction is not a consumer goods secured
14 transaction or a consumer secured transaction or that goods are not consumer
15 goods, if the secured party's belief is based on its reasonable reliance on a debtor's
16 representation concerning the purpose for which collateral was to be used, acquired,
17 or held, or an obligor's representation concerning the purpose for which a secured
18 obligation was incurred.

19 (d) A secured party is not liable to any person under Section 9-624(c) if the
20 secured party proves that its failure to comply with this part was not intentional and
21 resulted from a good-faith error notwithstanding the secured party's maintenance of
22 procedures reasonably adapted to avoid the failure. Examples of a good-faith error
23 include clerical, calculation, computer malfunction, programing, and printing
24 errors. An error of legal judgment concerning the secured party's rights and duties
25 under this part is not a good-faith error.

1 (e) The total recovery under Section 9-624(c) in a class action or a series of
2 class actions arising out of the same noncompliance by the same secured party shall
3 not be more than the lesser of \$500,000 or one percent of the net worth of the
4 secured party.

5 (f) A secured party is not liable to any person under Section 9-624(c) for its
6 failure to comply with Section 9-614A(c)(1).

7 Reporters' Comments

8 **Change from Prior Draft:** New subsection (f) has been relocated from
9 Section 9-624(c).

10 1. **Source.** New.

11 2. **Exculpatory Provisions.** Subsections (a), (b), and through (c) contain
12 exculpatory provisions that should be read in conjunction with Section 9-605.
13 Without this group of provisions, a secured party could incur liability to unknown
14 persons and under circumstances that would not allow the secured party to protect
15 itself. The broadened definition of the term "debtor" underscores the need for these
16 provisions.

17 3. **Bona Fide Error.** Subsection (d) immunizes a noncomplying secured
18 party from liability only for the minimum damages imposed under Section
19 9-624(c). The standard for "intentional" under this subsection is whether the
20 secured party actually intended to fail to comply with the Article, as is the case
21 under § 130(c) of the Truth in Lending Act, 15 U.S.C. § 1640(c).

22 **SECTION 9-628. ATTORNEY'S FEES IN CONSUMER GOODS**

23 **SECURED TRANSACTIONS.** If the secured party's compliance with this article
24 is placed in issue in an action with respect to a consumer goods secured transaction,
25 the following rules apply:

26 (1) If the secured party would have been entitled to attorney's fees as the
27 prevailing party, the court shall award to a consumer debtor or consumer obligor
28 prevailing on the issue the costs of the action and reasonable attorney's fees.

29 (2) In other cases, the court may award to a consumer debtor or consumer
30 obligor prevailing on that issue the costs of the action and reasonable attorney's
31 fees.

(3) In determining the attorney's fees, the amount of the recovery on behalf of the prevailing consumer debtor or consumer obligor is not a controlling factor.

Reporters' Comments

1. **Source.** New.

2. Attorney's Fees. In an action involving a secured party's compliance with Article 9, this section requires a court to award attorney's fees to a prevailing consumer debtor or consumer obligor if the secured party would have been entitled to attorney's fees had it prevailed. For purposes of awarding attorney's fees, a consumer debtor or consumer obligor is a prevailing party if it is determined that the secured party failed to comply with Article 9, even though Section 9-627(d) excuses the secured party from liability under Section 9-624(c).

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PART 7
TRANSITION

3 **SECTION 9-701. EFFECTIVE DATE.** This [Act] takes effect

4 **SECTION 9-702. SAVINGS CLAUSE.**

5 [To be added]

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* * *

(37) “Security interest means . . . The term also includes any interest of a consignor and a buyer of accounts, chattel paper, or a payment intangible in a transaction that is subject to Article 9. The special property interest of a buyer of goods on identification of those goods to a contract for sale under Section 2-401 is not a “security interest , but a buyer may also acquire a “security interest by complying with Article 9.

* * *

Reporters' Comments

1. **“Buyer in Ordinary Course of Business.”** Many of the revisions to the definition of “buyer in ordinary course of business” in subsection (9) are for clarification and style. The second sentence of the subsection is new. It provides that the “ordinary course” requirement is met only if the sale is in the ordinary course of the seller’s business. The third sentence, which tracks Section 6-102(1)(m), explains when a sale is in the ordinary course of the seller’s business.

The penultimate sentence of subsection (9) also is new. It prevents a buyer that does not have the right to possession against the seller from taking free of the rights of third parties. The Article 2 sections referred to would be Sections 2-807 (specific performance) and 2-824 (prepaying buyer) of the May 16, 1997, Article 2 draft.

2. **“Security Interest.”** The definition of “security interest” in subsection (37) has been revised to turn the interests of all “consignors” (as defined in Section 9-102) into “security interests.” See generally the Comments to Section 9-112.

SECTION 5-118. SECURITY INTEREST OF ISSUER OR NOMINATED PERSON.

(a) An issuer or nominated person has a security interest in a ~~certificated security, chattel paper, instrument, or negotiable~~ document presented under a letter of credit and any identifiable proceeds of the collateral to the extent that the issuer or nominated person honors or gives value for the presentation.

(b) Subject to subsection (c), as long as and to the extent that an issuer
or nominated person has not been reimbursed or has not otherwise recovered the

value given with respect to a security interest under subsection (a), the security interest continues and is subject to Article 9, but:

(1) ~~a~~ no security agreement is not necessary to make the security interest enforceable under Section 9-203(a)(1); and

(2) ~~if the security interest is perfected and [by possession under Section 9-311]~~ it has priority over conflicting [perfected] security interests in the collateral or its proceeds}.

(c) A security interest that arises under this section is subject to the rights of a subsequent purchaser under Section 9-327 or [Section] 9-328 or a transferee under Section 9-329.

Reporters' Comments

1. **Source.** New.

2. **Article 5 Security Interest.** This section gives the issuer of a letter of credit or a nominated person thereunder an automatic perfected security interest in a document (as that term is defined in Section 5-102(a)(6)). The security interest arises only if the document is presented to the issuer or nominated person under the letter of credit and to the extent of the value that is given. This security interest is analogous to that awarded to a collecting bank under Section 4-210. Under subsection (b)(2), the security interest is perfected and has first priority, subject to exceptions. Because the security interest is conditioned on presentation of the document, perfection by possession under Section 9-311 normally would occur even without the automatic perfection provided by subsection (b)(2). Documents that are written on paper and that are not an otherwise a defined type of collateral (e.g., a certificated security or a document of title) would be goods, for example. The issuer or nominated party also could rely on temporary perfection, under Section 9-310, or filing. However, because the definition of document in Section 5-102(a)(6) includes records (e.g., electronic records) that may not be goods, it is necessary to provide for automatic perfection (i.e., without filing). The priority afforded by subsection (b) is limited by subsection (c), which recognizes that subsequent purchasers of negotiable collateral or chattel paper should obtain protection under Section 9-327 or 9-328, when applicable, as should transferees of funds under Section 9-329.

It is arguable that this section is not necessary for a document that is a certificated security, a negotiable instrument, or a negotiable document that is presented to an issuer or nominated person. Those parties might achieve the same result under a proper interpretation of Sections 2-506 and 4-210 and the good-faith-purchaser rules of Articles 3, 7, and 8. See Section 9-328. However, those rules would not apply to other types of documents. An issuer or nominated person might find these non-negotiable documents to be quite important. For example, a

1 confirmer who pays the beneficiary must be assured that its rights to all documents
2 are not impaired. It will find it necessary to present all of the required documents to
3 the issuer in order to be reimbursed. For this reason, we believe that taking the
4 general approach taken by Section 4-210 is sound. However, because the security
5 interest is not dependent on continued possession, it is necessary to qualify the
6 priority of the security interest pursuant to subsection (c).

7 **SECTION 8-106. CONTROL.**

8 (a) A purchaser has "control" of a certificated security in bearer form if the
9 certificated security is delivered to the purchaser.

10 (b) A purchaser has "control" of a certificated security in registered form if
11 the certificated security is delivered to the purchaser, and:

12 (1) the certificate is indorsed to the purchaser or in blank by an effective
13 indorsement; or

14 (2) the certificate is registered in the name of the purchaser, upon
15 original issue or registration of transfer by the issuer.

16 (c) A purchaser has "control" of an uncertificated security if:

17 (1) the uncertificated security is delivered to the purchaser; or

18 (2) the issuer has agreed that it will comply with instructions originated
19 by the purchaser without further consent by the registered owner.

20 (d) A purchaser has "control" of a security entitlement if:

21 (1) the purchaser becomes the entitlement holder; or

22 (2) the securities intermediary has agreed that it will comply with
23 entitlement orders originated by the without further consent by the entitlement
24 holder.

25 (e) If an interest in a security entitlement is granted by the entitlement
26 holder to the entitlement holder's own securities intermediary, the securities
27 intermediary has control.

1 (f) A purchaser who has satisfied the requirements of subsection (c)(2) or
2 (d)(2) has control even if the registered owner in the case of subsection (c)(2) or the
3 entitlement holder in the case of subsection (d)(2) retains the right to make
4 substitutions for the uncertificated security or security entitlement, to originate
5 instructions or entitlement orders to the issuer or securities intermediary, or
6 otherwise to deal with the uncertificated security or security entitlement.

7 (g) An issuer or a securities intermediary may not enter into an agreement
8 of the kind described in subsection (c)(2) or (d)(2) without the consent of the
9 registered owner or entitlement holder, but an issuer or a securities intermediary is
10 not required to enter into such an agreement even though the registered owner or
11 entitlement holder so directs. An issuer or securities intermediary that has entered
12 into such an agreement is not required to confirm the existence of the agreement to
13 another party unless requested to do so by the registered owner or entitlement
14 holder.

15 **[Revised] Official Comment**
16 **[marked to show changes from Official Comment]**

17 1. The concept of "control" plays a key role in various provisions dealing
18 with the rights of purchasers, including secured parties. See Sections 8-303
19 (protected purchasers); 8-503(e) (purchasers from securities intermediaries); 8-510
20 (purchasers of security entitlements from entitlement holders); ~~9-115(4)~~ 9-312
21 (perfection of security interests); ~~9-115(5)~~ 9-324 (priorities among conflicting
22 security interests).

23 Obtaining "control" means that the purchaser has taken whatever steps are
24 necessary, given the manner in which the securities are held, to place itself in a
25 position where it can have the securities sold, without further action by the owner.

26 * * *

27 Example 8. Able & Co. a securities dealer, holds a wide range of securities
28 through its account at Clearing Corporation. Able enters into an arrangement
29 with Alpha Bank pursuant to which Alpha provides financing to Able secured
30 by securities identified as the collateral on lists provided by Able to Alpha on a
31 daily or other periodic basis. Able, Alpha, and Clearing Corporation enter into
32 an agreement under which Clearing Corporation agrees that if at any time Alpha
33 directs Clearing Corporation to do so, Clearing Corporation will transfer any
34 securities from Able's account at Alpha's instructions. Because Clearing

1 Corporation has agreed to act on Alpha's instructions with respect to any
2 securities carried in Able's account, at the moment that Alpha's security interest
3 attaches to securities listed by Able, Alpha obtains control of those securities
4 under subsection (d)(2). There is no requirement that Clearing Corporation be
5 informed of which securities Able has pledged to Alpha.

6 * * *

7 7. The term "control" is used in a particular defined sense. The
8 requirements for obtaining control are set out in this section. The concept is not to
9 be interpreted by reference to similar concepts in other bodies of law. In particular,
10 the requirements for "possession" derived from the common law of pledge are not
11 to be used as a basis for interpreting subsection (c)(2) or (d)(2). Those provisions
12 are designed to supplant the concepts of "constructive possession" and the like. A
13 principal purpose of the "control" concept is to eliminate the uncertainty and
14 confusion that results from attempting to apply common law possession concepts to
15 modern securities holding practices.

16 The key to the control concept is that the purchaser has the ~~present~~ ability to
17 have the securities sold or transferred without further action by the transferor.
18 There is no requirement that the powers held by the purchaser be exclusive. For
19 example, in a secured lending arrangement, if the secured party wishes, it can allow
20 the debtor to retain the right to make substitutions, or to direct the disposition of the
21 uncertificated security or security entitlement. Subsection (f) is included to make
22 clear the general point stated in subsection (c) that the test of control is whether the
23 purchaser has obtained the requisite power, not whether the debtor has retained
24 other powers. There is no implication that retention by the debtor of powers other
25 than those mentioned in subsection (f) is inconsistent with the purchaser having
26 control. Moreover, the purchaser's right to direct the intermediary may be subject
27 to conditions. For example, a purchaser may have present control of a security
28 entitlement even though the purchaser's right to give entitlement orders to the
29 securities intermediary is conditioned on the entitlement holder's default or the
30 purchaser's informing the securities intermediary that the entitlement holder is in
31 default. Better practice for both the intermediary and the purchaser would be to
32 insist that any conditions be effective only as between the purchaser and the
33 entitlement holder. That would avoid the risk that the intermediary could be caught
34 between conflicting assertions of the entitlement holder and the purchaser as to
35 whether the conditions in fact have been met. Nonetheless, the existence of
36 unfulfilled conditions effective against the intermediary would not preclude the
37 purchaser from having control.

38 **SECTION 8-110. APPLICABILITY; CHOICE OF LAW.**

39 * * *

40 (e) The following rules determine a "securities intermediary's jurisdiction"
41 for purposes of this section:

1 (1) If an agreement between the securities intermediary and its
2 entitlement holder expressly specifies ~~that it is governed by the law of a particular~~
3 ~~jurisdiction~~, the securities intermediary's jurisdiction for purposes of this part, this
4 article, or this act, that jurisdiction is the securities intermediary's jurisdiction.

5 (2) If an agreement between the securities intermediary and its
6 entitlement holder does not specify the ~~governing law~~ securities intermediary's
7 jurisdiction as provided in paragraph (1), but expressly specifies that the securities
8 account is maintained at an office in a particular jurisdiction, that jurisdiction is the
9 securities intermediary's jurisdiction.

10 (3) If an agreement between the securities intermediary and its
11 entitlement holder does not specify a jurisdiction as provided in paragraph (1) or
12 (2), the securities intermediary's jurisdiction is the jurisdiction in which is located
13 the office identified in an account statement as the office serving the entitlement
14 holder's account.

15 (4) If an agreement between the securities intermediary and its
16 entitlement holder does not specify a jurisdiction as provided in paragraph (1) or (2)
17 and an account statement does not identify an office serving the entitlement holder's
18 account as provided in paragraph (3), the securities intermediary's jurisdiction is the
19 jurisdiction in which is located the chief executive office of the securities
20 intermediary.

21 (f) A securities intermediary's jurisdiction is not determined by the physical
22 location of certificates representing financial assets, or by the jurisdiction in which
23 is organized the issuer of the financial asset with respect to which an entitlement
24 holder has a security entitlement, or by the location of facilities for data processing
25 or other record keeping concerning the account.

26 Reporters' Comments

1 This section has been revised to provide more flexibility for the parties to
2 select the security intermediary's jurisdiction. See also Sections 9-304(1)
3 (depository institution's jurisdiction); 9-305(a)(4)(A) (commodity intermediary's
4 jurisdiction).

5 **SECTION 8-302. RIGHTS OF PURCHASER.**

6 (a) Except as otherwise provided in subsections (b) and (c), a purchaser
7 ~~upon delivery~~ of a certificated or uncertificated security ~~to a purchaser, the~~
8 ~~purchaser~~ acquires all rights in the security that the transferor had or had power to
9 transfer.

10 (b) A purchaser of a limited interest acquires rights only to the extent of the
11 interest purchased.

12 (c) A purchaser of a certificated security who as a previous holder had
13 notice of an adverse claim does not improve its position by taking from a protected
14 purchaser.

15 **Reporters' Comment**

16 The proposed change to Section 8-302(a) is for clarification only. The pre-
17 1994 version of Article 8 provided (in pre-1994 Section 8-301(1)) that a purchaser
18 acquired a transferor's rights in a security "upon transfer. The 1994 revisions
19 eliminated the "transfer" concept. In its place, the term "delivery" was included in
20 Section 8-302(a). The change proposed in this draft is intended to preclude any
21 possible negative implication that a "delivery" under Section 8-301 is a condition
22 precedent to a purchase of an interest in a security. For example, a secured party
23 may become a purchaser if it is granted a security interest in investment property.
24 The security interest may be perfected without delivery (e.g., by filing). Similarly,
25 a purchaser may obtain "control" of an uncertificated security under Section 8-
26 106(c)(2), even though no delivery has occurred.