

Tennessee Begins Another UCC Article 9 Transition Period

by

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Two bills enacted in Tennessee this year may require secured parties to take action if they recently filed financing statements on individual debtors. The first was Senate Bill 3732, which created a broad safe harbor for individual debtor names if the financing statement provides the name shown on one of five different identification documents. The second, Senate Bill 372, scaled back the list of documents that can serve as a safe harbor source of individual names.

A consequence of SB 372 is that some individual debtor names sufficient under SB 3732 may now make the financing statement seriously misleading. To protect secured parties that have financing statements at risk from the narrower safe harbor, SB 372 provides for a sixty-day transition period. During that time, secured parties may need to amend non-conforming debtor names to remain perfected.

The sufficiency of individual debtor names provided on financing statements has been an ongoing concern for UCC filers since UCC Revised Article 9 took effect in 2001. A debtor name is sufficient under Article 9 if the financing statement provides the name of the debtor in strict compliance with the requirements of UCC § 9-503(a). A financing statement that fails to sufficiently provide the name of the debtor in accordance with § 9-503(a) is seriously misleading under § 9-506(b). The only exception is found in § 9-506(c), where a financing statement that fails to sufficiently provide the name of the debtor is not seriously misleading if a search on the correct name of the debtor, using the jurisdiction's standard search logic would disclose the record.

Unfortunately, even diligent UCC filers can have difficulty determining what individual name to provide on a financing statement. Article 9 offers no standards or guidance for a filer to identify a sufficient individual name with any certainty. The courts are left to decide the sufficiency of an individual debtor name on a case-by-case basis. The UCC filer has no option but to exercise its best judgment and hope the courts later agree.

Some lenders and legal counsel have found the level of uncertainty surrounding individual names unacceptable. Individual debtors include sole proprietors, farmers, guarantors and private banking customers that often enter into sizeable financial transactions. In many states individual names make up approximately half of all the debtor names in the UCC index. The sheer number and nature of transactions involving individual debtors means that secured parties have a lot at stake.

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With no resolution to the individual name concerns on the horizon, state bar and bankers associations began exploring options for bringing more certainty to the process. Texas was the first state to offer a legislative solution to the individual debtor name sufficiency issue through non-uniform amendments to Bus. & Com. Code § 9.503(a). Along with a clarification on the source of registered organization names, the amendments created a safe harbor if the financing statement provides the individual debtor's name shown on the debtor's driver's license or state identification certificate. The Texas law took effect on June 16, 2007.

Following Texas's lead, the Tennessee Bankers Association promoted similar legislation in 2008. Senate Bill 3732 contained non-uniform amendments to Tenn. Code Ann. § 47-9-503(a) that largely adopted the language enacted in Texas. However, the bill had one significant departure. Instead of limiting the safe harbor to the name shown on an individual's driver's license or state-issued identification, the Tennessee legislation added several other documents to the list, including the debtor's passport, Social Security card, birth certificate or military identification.

The legislation quickly moved through the legislative process and received little comment. Both the senate and the house unanimously passed SB 3732 within six weeks of its introduction. It was promptly signed by the governor. The new law took effect on May 1, 2008.

While SB 3732 offered greater protection for secured parties, it had the unintended consequence of creating a substantial burden for parties that conduct due diligence on individuals. After the law took effect, searches became necessary on all names shown on any of the safe harbor documents.

The new Tennessee law immediately came under criticism from a variety of stakeholders. In response to these concerns, the Tennessee Bankers Association submitted legislation to narrow the safe harbor scope. Senate Bill 372 limited the safe harbor to just the name shown on the individual's driver's license or state-issued identification license authorized by Tenn. Code Ann. § 55-50-336 (a driver's license identification equivalent for non-drivers issued by Tennessee and many other states).

However, there remained a problem with how to deal with financing statements filed after May 1, 2008 that provided a formerly sufficient name shown on one of the documents removed from the safe harbor. If that name differed from the name shown on the driver's license or identification license, it might make the financing statement seriously misleading. To address this problem, SB 372 contains a sixty-day transition period. The governor's signature on June 13th triggered the start of the transition. Secured parties that filed a non-conforming name under SB 372 must file a debtor name amendment by August 12th to ensure the name falls within the safe harbor.

The Tennessee legislation does not apply to every financing statement that lists an individual debtor name. The effect of the new laws and the required secured party actions, if any, depend on the file date.

Financing Statements filed before May 1, 2008. The Tennessee legislation has no effect on UCC records filed before SB 3732 took effect on May 1, 2008. Financing statements that sufficiently provided the name of an individual debtor under former law remain effective. However, if the name on the financing statement is different from the name shown on the driver's license or identification license, the secured party should consider amending the financing statement to add the safe harbor name.

Financing Statements filed between May 1, 2008 and June 13, 2008. If the financing statement provides the name shown on the individual's birth certificate, Social Security card, passport or military identification and it differs from the name shown on the individual's driver's license or identification license, it will only remain sufficient through August 12, 2008. The secured party must amend the financing statement to provide the name of the debtor shown on the individual's driver's license or identification license before August 12th to ensure it falls within the safe harbor after that date.

Financing Statements filed after June 13, 2008. The financing statement must provide the name shown on an individual's driver's license or identification license to fall within the safe harbor.

Secured parties should carefully review all financing statements filed in Tennessee since May 1st and take the appropriate actions. Failure to amend non-conforming individual debtor names could result in an unperfected security interest.