

IN RE MILLER: RECENT CASE HIGHLIGHTS THE DIFFICULTY OF PERFECTING SECURITY INTERESTS AGAINST INDIVIDUALS UNDER ARTICLE 9 OF THE UCC

Perfecting a security interest against an individual should be easy, but it isn't. To perfect the security interest, the lender needs to know the name of the individual. This may not seem difficult to do, but consider the following example: what is the "name" of a woman who was at birth given the name Elizabeth Montgomery, was known until marriage as Peggy Montgomery, was known after marriage as Peggy Montgomery-Willisby and has a driver's license with the name Peggy Willisby?

A recent Illinois District Court decision reflects the unique difficulty that individual debtors pose for secured creditors under Article 9 of the Uniform Commercial Code (the "*UCC*"). This memorandum discusses the case as well as pending changes to the UCC that (among other things) provide greater guidance as to the name to be provided on a financing statement for perfecting a security interest against an individual.

In *In re Miller*, 2012 WL 3589426 (C.D. Ill. Aug. 17, 2012), the United States District Court for the Central District of Illinois, Urbana Division, reversed an Order entered by the United States Bankruptcy Court for the Central District of Illinois in *In re Miller*, 2012 WL 32664, 76 UCC Rep. Serv. 2d 435 (Bankr. C.D. Ill. Jan. 6, 2012). The District Court held that neither Illinois law nor Article 9 of the UCC as adopted by the Illinois Legislature in 810 ILCS 5/9-521 (the "*Illinois UCC*") requires that a "legal name" be used on a financing statement in order to perfect a security interest, but rather only a "correct name," and that an individual debtor's name on his driver's license - and the name he publicly goes by - is sufficiently "correct" for this purpose even when it conflicts with the name on the debtor's birth certificate.

On February 25, 1995, Bennie Miller ("*Miller*") and his wife Debbie opened a personal banking account with the State Bank of Arthur (the "*Bank*") in the name of "Bennie A. Miller and Debbie A. Miller" (the "*Millers*"). The Millers subsequently executed promissory notes in favor of the Bank and security agreements giving the Bank a security interest in substantially all of their business assets. All loan documents were signed by Miller as "Bennie A. Miller," and the Bank filed a UCC-1 financing statement identifying the debtors as "Bennie A. Miller" and "Debbie A. Miller." "Bennie A. Miller" was also the name on Miller's unexpired Illinois driver's license, his Social Security card, his federal income tax returns, a credit card account and the signature card signed when the Millers opened their account with the Bank in 1995. However, "Ben Miller" was the name on Miller's birth certificate and on a different credit card account. On December 22, 2010, the Millers filed for Chapter 13 bankruptcy, listing the Bank as a secured creditor. On June 17, 2011, the Millers filed an adversary proceeding seeking to avoid the Bank's security interest against Miller, arguing that the financing statement incorrectly identified Miller as "Bennie A. Miller" when it should have used the name on his birth certificate, "Ben Miller."

The Bankruptcy Court ruled in favor of the Millers, allowing them to avoid the Bank's lien on Mr. Miller's half-interest in the business assets. The Bankruptcy Court held that the Illinois UCC requires financing statements to set forth the "legal name" of the debtor, and a debtor's legal name is properly indicated by his birth certificate rather than his driver's license or Social Security card. Reasoning that because the name on Miller's birth certificate is "Ben Miller" and a search for the name "Ben Miller" using the Illinois filing office's standard search logic did not disclose the financing statement, the Bankruptcy Court concluded that the Bank's use of the name "Bennie A. Miller" was seriously misleading and the financing statement was insufficient to perfect the Bank's security interest.

On appeal, the District Court reversed, holding that Illinois law and the Illinois UCC require only a "correct name," not a "legal name," on a financing statement in order to perfect a security interest. The District Court further held that even if a legal name was required, it was incorrect for the Bankruptcy Court to give the name on a debtor's birth certificate priority over the name on his other commonly accepted documents. First, the District Court looked to the text of the Illinois statute, finding that neither its 1999 nor its 2001 text specified how a debtor's name should be determined, and that neither text required a "legal name" or defined what would constitute a "legal name." Rather, 810 ILCS 5/9-503(a)(4)(A) requires only the debtor's name, and 5/9-506(c) makes a financing statement not seriously misleading if a search of the records under the debtor's "correct name" would disclose the relevant financing statement. The District Court found that no case law supported the position that a "legal name" was required.

The District Court concluded that the name "Bennie A. Miller" was not seriously misleading, as it was used on Miller's driver's license, Social Security card and federal income tax returns. Even if Article 9 required a "legal name," this requirement would still be met, as no Illinois case law specifically required that a legal name be defined only by a birth certificate. The District Court found that Miller had assumed the legal name "Bennie A. Miller" by using it on his driver's license and Social Security card and by going by that name in the community.¹ As the name listed on an official document presented to the Secretary of State (Miller's driver's license), "Bennie A. Miller" is also a proper legal name as defined by non-UCC Illinois law. The District Court also found it relevant that when a search was performed for that name, five of the six secured creditors that filed financing statements showed up in the Illinois database.²

The District Court found that its result was supported by public policy, as the name on an individual's birth certificate should not trump the name on his or her driver's license. A driver's license is more likely to reflect a person's current and accurate name, because while Illinois requires that a person changing his name apply for a corrected driver's license within 30 days, there is no such requirement for a birth certificate. A driver's license is also typically more readily accessible than a birth certificate (and thus easier for creditors to verify).

¹ Common law name changes (made without resort to legal proceedings) are valid in Illinois if the new name was assumed before July 1, 2010.

² On the other hand, a search using the name "Ben Miller" would not have disclosed the "Bennie A. Miller" financing statements.

This decision highlights the need for greater clarity in the UCC concerning financing statements filed against individual debtors. Lenders need to be able to search the lien records to determine whether or not there are liens already filed against the assets of the individual debtor and to do so they need a simple rule to determine the proper name to search.

The Article 9 Joint Review Committee members, Advisors and Observers³ considered the issue and, because there was a great deal of disagreement, the pending changes proposed by the Drafting Committee on Amendments to Uniform Commercial Code Article 9 (sponsored by the American Law Institute and the National Conference of Commissioners on Uniform State Law and currently being considered by state legislatures) give jurisdictions two alternatives to choose from in determining the sufficiency of an individual debtor's name in financing statements:

1. Under Alternative A (also known as the “*only if approach*”), if the debtor has an unexpired driver's license in the jurisdiction where his or her principal residence is located, the name on the driver's license is the “correct name.” If the debtor does not have an unexpired driver's license in such jurisdiction, the financing statement must provide “the individual name” of the debtor (i.e., the debtor's name as required under current law) or the “surname and first personal name of the debtor.”
2. Under Alternative B (also known as the “*safe harbor approach*”), a financing statement sufficiently provides a debtor's name if it (i) provides the name indicated on the debtor's unexpired driver's license in the jurisdiction where the debtor's principal residence is located, (ii) provides the individual name of the debtor (i.e., the debtor's name as required under current law) *or* (iii) provides the debtor's surname and first personal name.

Regardless of which alternative is adopted, a legislative note to the amendments⁴ suggests that state identification cards should be an alternative to driver's licenses for individuals that do not have driver's licenses.

Note that under either of these alternatives, the name used by the Bank in the Miller case would be correct. The name “Bennie Miller” would satisfy Alternative A and Alternative B since it was the name from his unexpired driver's license. Under Alternative B, the use of the birth certificate name could also be sufficient (if it were found to be the debtor's “individual name” or “surname and first personal name”).

While the alternatives presented by the pending UCC changes may reduce confusion as to what name should be used on a financing statement filed against an individual by promoting the use of one key document (an unexpired driver's license issued by the state where the debtor's principal residence is located) to determine an individual debtor's “correct name,” the pending changes do not define “individual name” or “first personal name” so the potential for confusion is not

³ Cindy J. Chernuchin was an Article 9 Joint Review Committee Observer.

⁴ See UCC 9-503.

completely alleviated. In addition, a driver's license is not a public record so there is no easy way to track changes to a debtor's name that may appear on a replacement driver's license if the original driver's license expires or is lost. Under Alternative A, if a search for the name on the replacement license does not disclose the filed financing statement, the financing statement would remain effective for collateral owned by the debtor on the date of the name change and be effective for collateral purchased within four (4) months after the name change. To perfect the secured party's security interest in collateral acquired by the debtor after the end of four (4) months from the date of the name change, the secured party needs to amend the financing statement within the four-month period to indicate the debtor's new name.⁵ Creditors will also need to confirm which alternative has been selected by the jurisdiction of filing, as Alternative A would allow only one possible name if the debtor held an unexpired driver's license from the relevant jurisdiction, while Alternative B could still provide multiple options. However, if the debtor has an unexpired driver's license, use of the name on the license is allowable under either alternative and gives the secured party some certainty. The Article 9 Joint Review Committee agreed that this certainty outweighed the increased risk associated with name changes under either alternative. The New York State proposed bill recommends enacting Alternative A, which is the alternative chosen by the vast majority of the states that have already enacted the revisions to Article 9 promulgated in 2010. That option is also preferred by most banks. As of October 23, 2012, (i) twenty-five (25) states⁶ have enacted the 2010 Amendments to Article 9 of the UCC with Alternative A, (ii) five (5) states have enacted the 2010 Amendments to Article 9 of the UCC with Alternative B, and (iii) twenty-two (22) states have added state or other personal identification cards as alternatives to the name on the driver's license required under Alternative A or B. The recommended effective date for these revisions is July 1, 2013.⁷ There is a five-year transition period that runs from July 1, 2013 through June 30, 2018.⁸ Under the transition rules, a secured party will have until the earlier of the lapse date of its filed financing statement and the end of the transition period to file an amendment to its filed financing statement.

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⁵ The expiration of a driver's license in an Alternative A state may cause a name change event. If a debtor relocates his or her primary residence to a different state, a financing statement filed against the debtor in the state of his or her former residence will remain effective for up to a year following the debtor's move to a new state.

⁶ This includes Puerto Rico.

⁷ All states that enacted the legislation to date have adopted the uniform effective date other than Puerto Rico, where the law will take effect on January 17, 2013.

⁸ For consistency, Puerto Rico enacted a 10-year transition period. (A financing statement filed in Puerto Rico lapses at the end of ten (10) years.)

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