

## Remaining Perfected Through the Revised Article 9 Transition Period

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On July 1, 2001, Revised Article 9 ("RA9") took effect in most states. The new law contained significant changes to long-standing search and filing rules for UCC financing statements. These changes included new rules for the proper filing location and sufficiency of debtor names.

The Revised Article 9 rules apply to all transactions that occurred after the effective date. This created a problem where some existing financing statements were filed in a location correct under old law, but would be incorrect under RA9. The same applied to debtor names and other rule changes that affected the potential effectiveness of financing statements.

To ensure that financing statements initially filed under old law remained effective under RA9, the drafters created special transition rules. The transition rules provide secured parties with a mechanism to bring existing financing statements into compliance with RA9. However, the rules placed a five-year transition period time limit to do so.

The five-year transition period comes to an end in most states on June 30, 2006. The transition rules were not perfect, so it is important for secured parties and legal counsel to prepare how they will handle continuations during this time.

The RA9 code itself contains an ambiguous transition provision, § 9-705(c), which could cause unprepared secured parties to lose their perfected status. Several states adopted RA9 with a non-uniform effective date. This will affect how financing statements need to be continued in those jurisdictions. A few states adopted non-uniform transition rules that require special attention. The following sections describe how to deal with these issues.

### TRANSITION RULE § 9-705(c)

In 2001, many secured parties decided to file continuations for financing statements set to lapse in the months after RA9 took effect during the pre-effective date portion of the continuation window. By continuing under old law they avoided the necessity of complying with the then unfamiliar RA9 requirements. This postponed the problem until the end of the transition period.

Now that the lapse date is again approaching, secured parties have to deal with the effect of the RA9 transition rules. Specifically, §9-705 applies to these financing statements. The applicable portion of §9-705 reads in relevant part:

(c) This act does not render ineffective an effective financing statement that, before July 1, 2001, is filed and satisfies the applicable requirements for perfection under the law of the jurisdiction governing perfection as provided in former Section 9-103. However, except as otherwise provided in subsections (d) and (e) and Section 9-706, the financing statement ceases to be effective at the **earlier** of:

- (1) The time the financing statement would have ceased to be effective under the law of the jurisdiction in which it is filed; or
- (2) June 30, 2006.

What exactly does this mean? Section 9-705(c), does not provide clear direction for secured parties. Even worse, it does not provide guidance to filing officers about how to deal with the transition lapse date.

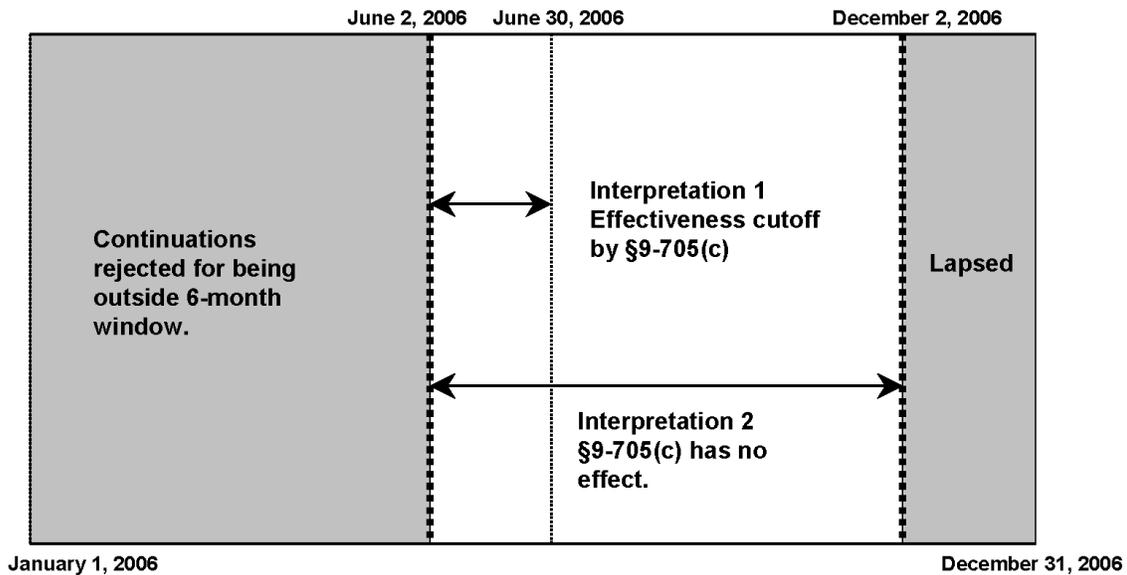
There are two possible interpretations of how § 9-705(c) affects pre-effective date financing statement.

1. It means exactly what it says, that all pre-effective date financing statements will cease to be effective on June 30, 2006, unless brought into compliance with RA9 through continuation or filing In Lieu, or

2. That only financing statements filed in the location correct for Old Article 9, but wrong for RA9 are affected.

The following Chart 1 demonstrates how these scenarios affect the continuation window for a financing statement originally filed on December 2, 1996 and continued on June 3, 2001. It now has a lapse date of December 2, 2006. The normal continuation window opens on June 2, 2006.

**Pre-RA9 Financing Statement due to lapse on December 2, 2006  
Initially filed December 2, 1996, continued June 15, 2001**



**Chart 1.**

If the first interpretation applies, the continuation window runs from June 2 through June 30. The second interpretation provides for the regular 6-month continuation window.

The number of financing statements affected by the §9-705(c) issue is very small. Still, these often represent large transactions or deals in workout. Either way, the secured parties don't want an unexpected lapse.

Fortunately, there is a safe harbor. Under both interpretations, the period from the beginning of the 6-month window through June 30, 2006 is undisputedly a valid time to file the continuation. In some cases this could be almost the full six months. In others, it could be just a few days.

Even the safe harbor may not apply in some jurisdictions. Non-uniform effective dates, transition dates and quirks of prior law can combine to create a situation where there is no safe continuation window. For example, Ohio's version of Old Article 9 allowed the secured party to use the maturity date of the obligation as the lapse date in some situations. The filing offices in Ohio may show a lapse date of 2012 when the financing statement will likely cease to be effective on June 30, 2006. Ohio is not alone. A number of states have unusual circumstances that require the secured party to be vigilant.

**SPECIAL STATE ISSUES**

The §9-705(c) issue applies to nearly all states. However, several states have special circumstances due to non-uniform old Article 9 provisions, non-uniform RA9 transition dates or legislation designed to address §9-705(c). Secured parties that have financing statements filed in the following states need to develop an action plan to remain perfected. There are also a number of states that have introduced legislation to address the issue, so expect changes in this information.

### ALABAMA & MISSISSIPPI

Both Alabama and Mississippi adopted RA9 with an effective date of January 1, 2002. That means financing statements filed in these states during the second half of 2001 were done under the old law. The version of RA9 adopted in both states also has a non-uniform transition period end date of December 31, 2006.

If the filing location in these states was correct for both Old Article 9 and RA9, secured parties have until the earlier of the natural lapse date, or December 31, 2006 to file the continuation. If an in lieu filing is required, the cautious secured party will not wait. All filings in lieu should be completed no later than June 30, 2006, regardless of the jurisdictions involved. The reason is that courts of the new filing state may not recognize the “reach-back” priority of an in lieu financing statement if filed after that state’s transition cutoff date.

Financing statements filed in Alabama and Mississippi under old law that were due to lapse after January 1, 2002, but were continued during the pre-effective date portion of the 6-month window require special attention. Those financing statements should be continued during the “safe harbor” portion of the 6-month window. The safe harbor runs from the opening of the continuation window through December 31, 2006.

### ARIZONA

Under prior law, financing statements in Arizona were effective for six years. To ensure that secured parties had the full benefit of prior law, the Arizona legislature adopted a non-uniform end to the transition period. The transition ends in Arizona on June 30, 2007. This creates the unusual situation where financing statements filed in June 2001 are effective a year longer than those filed the following month.

Secured parties have until the earlier of the natural lapse date, or June 30, 2007 to continue all pre-effective date financing statements filed in Arizona if they were filed in the correct location for both Old Article 9 and RA9. As noted earlier, despite Arizona’s extended transition period, any in lieu filings should be completed by June 30, 2006.

The §9-705(c) issue applies in Arizona, as in most other states. The secured party should file its continuation within the safe harbor portion of the 6-month continuation window for any financing statement that originally would have lapsed after the RA9 effective date, but was continued under old law. The difference in Arizona is that the problem occurs in 2007, a year later than in most other states.

The safe harbor in Arizona runs from the beginning of the 6-month continuation window (based on the 6 year effective period) and June 30, 2007.

### CONNECTICUT

Connecticut adopted RA9 effective October 1, 2001. All financing statements filed in CT between July 1 and September 30, 2001 were filed under old Article 9. However, CT retained the uniform June 30, 2006 transition period end date. The result is that financing statements filed during the three months prior to the effective date could lapse in less than five years.

Any financing statements filed in CT prior to July 1, 2001 should be continued or filed in lieu by the normal scheduled lapse date. Financing statements initially filed between July 1 and September 30, 2001 may cease to be effective on June 30, 2006. The best practice for those financing statements is to

continue or file in lieu during the earliest part of the six-month continuation period, but no later than June 30, 2006. This shortens the continuation window. However, it is necessary to avoid the possibility that these financing statements will be subject to the §9-705(c) cutoff.

There is a larger problem for financing statements filed in Connecticut that had a lapse date between October 1, 2001 and March 31, 2002, but were continued on or before September 30, 2001. Financing statements in this type of situation should be continued between the beginning of the six-month window and June 30, 2006.

The problem is that there is no safe harbor within the 6-month window for financing statements affected by §9-705(c) that lapse after January 1, 2007. Financing statements that were originally due to lapse between January 1 and March 31, 2002, but continued prior to October 1, 2001, may all cease to be effective on June 30, 2006. That is before the 6-month continuation window opens.

To deal with this situation, best practice is to file a continuation statement prior to June 30, 2006. It will be rejected as being outside the 6-month window. The secured party should save the rejection in its files. Then, it will also be necessary to file a continuation within the normal continuation window. The secured party should also consider filing a Correction Statement to document the rejected continuation and its good faith attempt to comply with the law.

## FLORIDA

The Florida legislature adopted RA9 effective January 1, 2002, but retained the uniform transition end date of June 30, 2006. Financing statements filed in Florida between July 1 and December 1, 2001 were filed under old Article 9.

The same continuation and in lieu filing rules apply in FL as for CT. Any financing statements filed in FL prior to July 1, 2001 need to be continued or filed in lieu by the normal scheduled lapse date. Financing statements filed between July 1 and December 31, 2001 must be continued during the earliest part of the six-month continuation period, but no later than June 30, 2006. Again, this could leave a very short window. In lieu filings can be done at any time, but should be completed no later than June 30<sup>th</sup>.

Florida also has a special problem for financing statements that were due to lapse after January 1, 2002, but that had the continuation filed during the pre-effective portion of the 6-month window in 2001. The legislature adopted the uniform transition end date of June 30, 2006. This scheme caused the transition end date to occur before the first possible opening of the six-month continuation window for the affected financing statements. Consequently, there may be no continuation window in these cases.

As in Connecticut, the secured party should file a continuation prior to June 30, 2006 and save the inevitable rejection in its files. Then, a second continuation should be filed within the normal 6-month continuation window. At this time, Florida does not allow secured parties to file a Correction Statement.

## IDAHO

County-level fixture filings require extra attention. Under Idaho's old Article 9, fixture filings had no lapse date. They remained effective until a satisfaction was filed.

The RA9 transition rules will cause all pre-effective date Idaho fixture filings to lapse on June 30, 2006. The legislature recognized the problem and opened a special six-month window to file continuations on the affected fixture filings. The window opened on January 1, 2006. The best practice in Idaho is to file continuations on fixture filings during the special window.

A special warning for secured parties who have active pre-effective date fixture filings. Some secured parties have already attempted to file continuations on these fixture filings under the assumption that RA9 retroactively imposed a five-year effective period on these financing statements. Any such continuations likely had no effect, even if the county accepted them. Secured parties are advised to refile the continuations during the special 6-month window.

Idaho has the same §9-705(c) issue for state-level filings as most other states. The legislature did not address §9-705(c) as it applies at the state-level, so the general best practices apply. Affected filings should be continued during the safe harbor portion of the 6-month window.

### MARYLAND

The Maryland legislature recognized that there would be a problem caused by §9-705(c). Under old law, financing statements in Maryland were effective for 12 years. The legislature adopted the interpretation that applies §9-705(c) to all pre-effective date financing statements through a non-uniform amendment. The filing office, in turn, reset the lapse dates to June 30, 2006 for all pre-effective date filings. The best practice in Maryland is to continue all pre-effective date financing statements by June 30, 2006.

Emergency legislation is pending in Maryland that will clarify the new lapse dates for pre-effective date financing statements continued by June 30<sup>th</sup>. As of April 21, 2006, the legislation has passed and is on its way to the governor for signature.

### MONTANA

Montana fixed the §9-705(c) issue through legislation. The legislature did this by codifying the interpretation that the §9-705(c) cutoff date applies only to pre-effective date financing statements filed in the correct location under old law, but the incorrect location for RA9. These must all be filed In Lieu by the earlier of the lapse date or the transition cutoff date.

### NEW YORK

New York faces the same §9-705(c) issue as most other states. The safe harbor solution applies to most financing statements affected by §9-705(c). However, special attention is required for filings on cooperative interests.

Under old law, New York Coop UCC financing statements that included language indicating they were effective until terminated did not require continuations. Under New York law, the effectiveness of all these pre-effective date co-op financing statements will cease on June 30, 2006, unless they are brought into compliance with RA9.

Secured parties have a couple options for protecting their co-op filing perfection. These financing statements can be continued in compliance with RA9. Secured parties should also consider the option of filing a Co-op Addendum, which makes the financing statement effective for 50 years from the date of initial filing. The Co-op Addendum also avoids some of the strict RA9 compliance requirements. Secured parties considering this option should consult their legal counsel before taking action.

### OHIO

Under old Article 9 Ohio allowed the secured party to designate the obligation's maturity date as the lapse date in certain circumstances. This means that the Ohio Secretary of State filing office may have active pre-effective date financing statements that show lapse dates well after the end of the RA9 transition period. This creates a problem for secured parties.

The active financing statements that use the maturity date as the lapse date are all likely to fall victim to the operation of §9-705(c). They could cease to be effective on June 30, 2006, unless continued. However, the filing office has no statutory authority to accept continuations prior to the 6-month window calculated from the original lapse date. In most cases, that window won't open until well after the financing statements cease to be effective under §9-705(c). This is not an insignificant problem. A query of the Ohio UCC database identified more than 9,500 active pre-effective date financing statements that list the maturity date as lapse date.

In Ohio, secured parties that designated the maturity date as lapse date under old law should file a continuation prior to June 30, 2006. It will likely be rejected and should be saved in the secured party's files to document a good faith attempt to comply with the law. It may also be a good idea for the secured party to document its efforts through a continuation statement. The secured party should then assume the affected financing statements lapse every five years on June 30<sup>th</sup> and file continuations accordingly.

All other Ohio financing statements affected by §9-705(c) should be continued during the safe harbor portion of the 6-month window.

### OKLAHOMA

Oklahoma recognized the §9-705(c) issue and corrected it by statute. Secured parties can file continuations during a special 6-month window that runs through June 30, 2006

### TENNESSEE

Like Ohio, Tennessee's version of Old Article 9 allowed secured parties to designate the maturity date of the obligation as the financing statement's lapse date. Unlike Ohio, the Tennessee legislature did something about the problem created by §9-705(c). The legislature enacted a special 6-month window for these financing statements that runs through June 30, 2006.

The special continuation window doesn't solve all of the problems for secured parties. Often, the secured parties' tickler systems have not been updated to reflect the statutory lapse date. Consequently, secured parties with active filings in Tennessee need to review the lapse dates and reset their tickler systems as necessary.

Unfortunately, Tennessee's legislature failed to address the §9-705(c) issue for non-maturity date filings. The issue is the same as in most other states. Affected filings should be continued during the safe harbor portion of the 6-month window.

### VIRGIN ISLANDS

The U.S. Virgin Islands adopted Revised Article 9 with an effective date of April 1, 2001. However, the territory retained the uniform transition period end date of June 30, 2006. This results in a situation where there may be no continuation window for any financing statements initially filed between January 1, 2002 and March 31, 2002. Secured parties should attempt to continue these financing statements prior to June 30, 2006 and save the rejection notice. Then they should file another continuation during the normal 6-month window.

Financing statements that were due to lapse between April 1 and September 30, 2002, but were continued prior to April 1, 2002 will also have no continuation window. Again, the secured party should file a continuation prior to June 30, 2006 and retain the rejection. The secured party should also consider filing a Correction Statement to document its attempt to comply with all interpretations of the transition rules. Finally, the secured party should also file a continuation during the normal 6-month window.

### NEW LAPSE DATES

Questions still remain about the effect of §9-705(c) on future lapse dates. At this time it seems most states will simply use the normal lapse date in 2011 for financing statements continued this year. However, the lapse date in some states could be different. For example, the new lapse date for pre-effective date financing statements in Maryland will likely be June 30, 2011. Tennessee will use June 30, 2011 as the new lapse date for stated maturity date financing statements continued this year, but keep the normal date in 2011 for other affected financing statements. Secured parties must make an effort to stay informed on new developments to avoid unpleasant surprises down the road.

## **SOLUTIONS**

In those jurisdictions where a continuation window may not exist, it is recommended that the secured party file a continuation prior to the end of the transition period. Secured parties should expect the filing office to reject the record in most cases. The rejected document should be filed as evidence that the continuation was attempted during that time period. In addition, the secured party should also attempt to file a continuation during the six months prior to the lapse date.

A very few states have enacted statutory fixes to the problems created by the RA9 transition end date. Secured parties must comply with the statutory requirements to remain perfected. In other jurisdictions, secured parties are advised to file continuations for financing statements affected by §9-705(c) during the safe harbor portion of the 6-month continuation window. In addition, secured parties should complete all in lieu filing by June 30, 2006

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