

## Jurisdictional Update

### Upcoming Changes to UCC Filing Location for Some Arkansas Debtors

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Earlier this year, Arkansas enacted House Bill 1984 to change the designated UCC filing office for certain financing statements. Arkansas originally adopted Revised Article 9 with a non-uniform version of UCC Section 9-501, which designates the office for filing financing statements. Under current law, if the debtor named in a financing statement is engaged in farming operations and the collateral includes equipment used in farming operations, farm products, or accounts arising from the sale of farm products, the filing location designated by Ark. Code § 4-9-501(a)(2) is the office of the circuit clerk where the debtor is located.

The effect of HB 1984 is to eliminate the non-uniform filing office designation in the current Arkansas version of Article 9.<sup>1</sup> Starting on January 1, 2010, the office designated for the filing of these farming-related financing statements will be the office of the secretary of state.

The good news for secured parties is that financing statements filed with the circuit clerk prior to January 1, 2010 will remain effective until the lapse date. If necessary, the effectiveness of the county filings can also be continued with the secretary of state.

While the changes offer a long-term benefit for secured parties, HB 1984 failed to adequately address some thorny transition issues. Consequently, many secured parties in Arkansas face increased risk and

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<sup>1</sup> HB 1984 does not apply to UCC financing statements filed in the circuit clerk real estate records.

uncertainty. It also presents a significant administrative challenge for the secretary of state. Even debtors may suffer inconvenience as a result of the new law. Any secured party that has filed financing statements with a circuit clerk in Arkansas must prepare to deal with the changes.

Two provisions of HB 1984 are of the greatest concern for secured parties.<sup>2</sup> The first deals with continuation of records on file with the circuit clerk. New § 4-9-510(d)(3) provides that the effectiveness of financing statements filed with the circuit clerk can be continued by filing a continuation statement with the secretary of state before the lapse date. The only problem is that amendments, including continuations, are indexed under the initial financing statement file number. There is no initial financing statement for the circuit clerk records on file with the secretary of state. Yet, HB 1984 requires the secretary of state to accept continuation records that it cannot index and would otherwise have to reject under Ark. Code § 4-9-516(b)(3) because there is no original record to which it relates. Moreover, the name of the debtor is not required on continuation statements by statute or rule. If the secretary of state were to accept continuation statements filed under § 4-9-510(d)(3) without additional information requirements, all those records would become hidden liens.

The other HB 1984 provision of special concern is found in new § 4-9-510(d)(1). Under this section, any financing statement, termination or continuation filed with the circuit clerk after December 31, 2009 will be ineffective. As the Article 9 definition of “financing statement” includes subsequent amendments, it is safest to assume that § 4-9-510(d)(1) applies to all amendments. Secured parties will be unable to effectively amend any financing statement on file with the circuit clerk after January 1, 2010.

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<sup>2</sup> This article does not address another provision of HB 1984 that created a temporary non-uniform filing office location when the debtor is engaged in farming operations and the collateral is a farm-stored commodity financed by the Commodity Credit Corporation. Those financing statements continue to be filed at the circuit clerk through December 31, 2012. This provision has a very narrow application and the legislature may address the transition issues before it takes effect.

Secured parties and debtors alike could be at risk if circuit clerk records cannot be effectively amended. In some circumstances, such as a debtor name change, the secured party could become unperfected in after-acquired collateral if it cannot file an effective amendment. A debtor may be troubled to learn that the secured party cannot effectively terminate a circuit clerk record upon satisfaction of the obligation.

The secretary of state was left to devise rules for implementing HB 1984 despite the lack of transition guidance. After consultation with a variety of stakeholders, the secretary of state developed administrative rules with two objectives, avoiding hidden liens in the continuation process and to provide a mechanism for amendment of the records that can not be effectively amended by filing with the circuit clerk. To accomplish these objectives, the secretary of state had to adopt rules that push the limits of statutory authority. Those rules are titled “Rules for Central Filing with the Secretary of State for Agricultural Liens and Farm-Related Security Interests – Transition.”

### **Secretary of State Solutions**

The proposed administrative rules impose additional, but necessary requirements on filers to ensure that a continuation statement filed under § 4-9-510(d)(3) can be indexed as a searchable record. Rule 5.03 requires the secured party to provide a certified copy of the circuit clerk financing statement as an attachment to the § 4-9-510(d)(3) continuation statement. The filing office will index the information from the certified copy as if it were an initial financing statement. However, under proposed Rule 5.05, the record will receive the file date and time the circuit clerk originally assigned the financing statement. That will preserve evidence of the secured party's priority in the record. The secretary of state will index the record with the same lapse date that would have been assigned to it by the circuit clerk had the record been continued in that office.

Once the continuation statement has been filed and the certified copy indexed, there will be a new record with the secretary of state that the secured party can later amend. However, the secretary of state cannot accept a continuation statement until six-months before the lapse date of the related circuit clerk financing statement. HB 1984 did not provide a mechanism for the secured party to amend or terminate the financing statement before the six-month continuation window. That could take until 2014 for some financing statements.

Rule 6.00 provides for a method for amending financing statements on file with the circuit clerk. Rule 6.03 permits the secured party to file an “amendment statement” with an attached certified copy of the initial financing statement. The filing office will index the record as an initial financing statement, except that the date and time assigned to the record shall be that indicated by the circuit clerk on the certified copy. After indexing the certified copy, the filing office will index the information on the amendment statement.

One other important provision in the proposed rules is that all amendment statements and continuation statements filed pursuant to new § 4-9-510(d)(3) must be submitted as written records. The records require manual indexing by a filing officer. The electronic UCC filing system would not be able to accept such a record because there is not an initial financing statement to which it relates.

The rules proposed by the secretary of state are unorthodox, but absolutely necessary to ensure the records can be entered in the searchable index. By providing a transparent method for filing the amendment records as well as continuation statements, the secretary of state has made it easier for courts to protect secured parties that make good faith efforts to comply with HB 1984 in spite of its ambiguities.

### Recommended Best Practices

#### **Continuation of Circuit Clerk Records with the Secretary of State.**

The first step in the continuation process for financing statements filed with the circuit clerk is to order a certified copy of the record. The secured party should ensure the certified copy legibly displays the file date and file number of the initial financing statement. It should also include all attachments and amendments. The secretary of state will use the certified copy information to correctly index the record.

Secured parties must be cautious to only submit continuation statements to the secretary of state within the six-month window provided for in § 4-9-515(d). Otherwise, the secretary of state is obligated to reject the record under § 4-9-516(b)(7).

In some cases the secured party may have the choice of filing a continuation statement with the circuit clerk under current law or with the secretary of state after HB 1984 takes effect. It is important for secured parties to understand the options, advantages and drawbacks of filing in each office.

#### Circuit Clerk Records that Lapse Before January 1, 2010.

If the secured party has filed a financing statement with the circuit clerk and it lapses before December 31, 2009, the record can only be continued by filing a continuation statement with the circuit clerk. Filing a continuation statement with the secretary of state prior to January 1, 2010 will be ineffective.

Filing the continuation statement with the circuit clerk extends the effectiveness of the record for another 5

years. If the record must be continued again in 2014, the secured party must file that continuation statement with the secretary of state.

Circuit Clerk Records that Lapse Between January 1 and June 30, 2010.

If a financing statement filed at the office of the circuit clerk has a lapse date sometime during the first half of 2010, part of the six-month continuation window will fall under the old law and part under the new law. The secured party will have a choice between filing a continuation statement with the circuit clerk during the pre-2010 portion of the continuation window or waiting until after the new law takes effect and filing with the secretary of state.

Filing a continuation with the circuit clerk saves the secured party the expense of ordering certified copies. The record will remain effective until the next lapse date in 2014. However, filing the continuation statement with the circuit clerk will complicate the process should it become necessary to amend the financing statement.

If the secured party chooses to file the continuation statement with the secretary of state after January 1, 2010, it must attach a certified copy of the initial financing statement. The advantage of waiting to file the record with the secretary of state is that it will be easier for the secured party to later file amendments.

Circuit Clerk Records that Lapse after June 30, 2010.

The secured party has only one continuation option for a financing statement originally filed with a circuit clerk if it

lapses after June 30, 2010. The effectiveness of the record can only be continued by filing a continuation statement with the secretary of state.

### **Amendments to Circuit Clerk Financing Statements**

The rules proposed by the secretary of state attempt to provide a method for the amendment of financing statements that cannot be amended at the office of the circuit clerk under HB 1984. However, the statute is silent regarding whether records filed in compliance with the proposed rules would have any effect whatsoever. Nevertheless, secured parties that need to amend financing statements filed with the circuit clerk should follow the procedures established by the secretary of state. There is no harm in doing so. After all, the circuit clerk records remain effective until the lapse date. There is no risk that the circuit clerk records would become unperfected if an amendment is also filed with the secretary of state.

In addition to compliance with the secretary of state rules, the secured party should consider also submitting an amendment for filing with the circuit clerk. While such a record may not be effective, it will still help provide notice to searchers.

### **Search Best Practices**

Searchers can expect a minimal impact from HB1984. The best practice for searching in Arkansas has always been to search the secretary of state and, if the debtor is engaged in farming operations, the circuit clerk where the debtor is located. The new law does not change the best practice for now. Effective financing statements could be filed in the office of the circuit clerk, the secretary of state, or both through December 31, 2014. Therefore, searchers will have to look in both locations. However, after January 1, 2015, searchers will no longer need

to search the circuit clerk, except when looking for financing statements filed in the real estate records.

### **Conclusion**

House Bill 1984 will eventually bring the UCC search and filing process in Arkansas into uniformity with other states. The new law, however, was incomplete and failed to offer clear transition procedures. Secured parties can substantially reduce the risks created by HB 1984 by carefully following the new rules promulgated by the secretary of state if it becomes necessary to continue or amend circuit clerk records.

Questions or Concerns? Please feel free to contact Paul Hodnefield, Associate General Counsel for Corporation Service Company, at [phodnefi@cscinfo.com](mailto:phodnefi@cscinfo.com), or 800-927-9801, ext. 2375.

### **About Corporation Service Company**

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