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"MY DEBTOR CHANGED ITS NAME!"

In a previous article, we addressed the importance of knowing just what legal entity your debtor is. It is easy enough to understand the importance of knowing whether you are dealing with an incorporated debtor or an individual, but sometimes a creditor who wishes to be secured by collateral fails to file its financing statement under the proper legal name of its debtor and hence loses the advantage of its security interest.

Now let us consider what happens if you have properly filed a financing statement under the correct legal name of your debtor and thereafter your debtor changes its name.

As is so often the case in matters of law, the legal effect of a name change depends upon the debtor's locality.

The section of the Uniform Commercial Code (UCC) which covers this problem is 9-402. Unfortunately, the "Uniform" Code is not uniform in the language of §9-402 as adopted in various states. In most jurisdictions, if a debtor so changes its name that a filed financing statement under its old name would be "seriously misleading" to subsequent lenders who review the UCC filing records for prior liens, then the secured party who has filed under the misleading name must refile within a set time in order to avoid losing its priority. These jurisdictions place the burden upon the secured creditor to find out whether the name of its debtor has so changed as to render its filing "seriously misleading," and if so, to file under the new name.

In the Commonwealth of Kentucky, however, the old filing under the misleading name only becomes non-effective to perfect a security interest in collateral acquired by the debtor more than four months after the debtor *notifies* the secured party in writing of the debtor's name change—in other words, the burden of notification is upon the debtor.

This obviously poses a great threat to subsequent lenders. When a lender is extending credit to a Kentucky debtor on what it believes to be a secured basis, how is it to know that the debtor has recently changed its name without notifying secured parties who have filed blanket liens under the debtor's old name?

Perhaps a nightmarish example best illustrates this trap for the unwary creditor.

Superior Widgets, Inc. (Superior), an Ohio corporation doing business in Ohio but selling to other states, wishes to be a supplier to Doe Manufacturing , Inc (Doe), a Kentucky manufacturer. Superior's credit manager is sufficiently cautious of his new customer's creditworthiness that he would like to be a secured creditor. The product that Superior is supplying, widgets, will not be held for very long in his customer's inventory, however, since the widgets quickly lose their identity in the manufacturing process of Doe to become part of a different product. Doe does keep a substantial inventory of its own manufactured product in its warehouse at all times, however, and a search of the UCC records in the county of Doe's registered office reveals no filings by secured creditors against the inventory of Doe Manufacturing, Inc. A check with the Secretary of State reveals that Doe Manufacturing, Inc. is a Kentucky corporation in good standing.

Superior's credit manager therefore approves credit sales on the condition that Doe grant a security interest to Superior in all inventory at Doe's warehouse location. Doe agrees, and grants to Superior the security interest, which is duly filed and perfected. Unbeknownst to Superior, however, Doe recently changed its name from John Doe & Sons, Inc., without informing its major secured creditor, Friendly Bank, which has a properly perfected security interest in all of Doe's inventory under its old name. Since Doe did not notify Friendly Bank that it was changing its name, the bank has in blissful ignorance maintained its priority while its debtor has enjoyed a generous extension of credit from Superior, which in short order results in an increase in Friendly Bank's collateral.

If Doe files a bankruptcy petition and lists $100,000 in inventory, Friendly Bank will have first rights to the inventory and proceeds, and unless the value of the inventory and proceeds exceeds Doe's indebtedness to the bank (always an unlikely scenario), Superior will receive nothing—despite the care taken by its credit manager. Superior is simply a general, unsecured trade creditor despite its valiant efforts not to be.

What could Superior's credit manager have done to avoid this problem? Not only would he have had to know that his customer had changed its name, but also that Kentucky has a non-uniform section of the UCC in regard to "seriously misleading" financing statements. It is hard enough for a credit manager to extend credit with known risks—it is nightmarish to ponder unknown pitfalls which arise via such non-uniform statutes.