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Article 9 Filings: Russian Roulette - UCC Style

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**QUARTERLY REPORT**

**Article 9 Filings: Russian Roulette—UCC Style**

*by William E. Carroll and Alvin C. Harrell*

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**I. Introduction**

Each day, alle across America, lenders or their counsel receive a letter from a lender or from a courthouse, indicating the potential for a filing under Article 9 of the Uniform Commercial Code (UCC) or under the Revised Article 9 of the Uniform Commercial Code (R-UCC). These filings are often referred to as "Russian Roulette—UCC Style." The filings are intended to provide a "name" for a debtor to a lender, thereby allowing the lender to have control over the debtor's assets in the event of default.

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1. "A problem at this level is not a problem in a vacuum." The UCC was intended to provide a uniform code for the protection of creditors in the event of default. However, the UCC was also intended to provide a "name" for the debtor, which would allow the creditor to have control over the debtor's assets. This "name" is referred to as the "Discrimination Name." The UCC was intended to provide a uniform code for the protection of creditors in the event of default.

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B. The Union Decision

Another concern is illustrated by the case of Union National Bank of Chan- 
dler v. BancFirst (Seminole). In Union National Bank of Chandler v. BancFirst, 
the court found no violation of the antitrust laws by BancFirst, Inc. in its 
practice of owning and operating an outdoor billboard in violation of an 
agreement with a competitor. The court held that BancFirst's action did not 
constitute a violation of the antitrust laws because it did not result in a 
restraining or per se illegal restraint of trade. The court concluded that the 
practice was reasonable and not an attempt to monopolize the market.

C. The Mines Tires Decision

In another interesting case, the court ruled that the practice of requiring 
the use of a particular brand of tires for the sale of certain vehicles was 
not a restraint of trade. The court held that the practice did not violate 
the antitrust laws because it was not unreasonable or illegal.

In conclusion, the court found that the practices in question did not 
constitute violations of the antitrust laws. The court emphasized that 
the practices were reasonable and not an attempt to monopolize the 
market.
III. Bulletin No. 2 - The Uhlenhake Problem

A prospective lender who searches the UCC records may face an additional problem that is presented in the form of a question in a recent analysis in Peoples National Bank v. Uhlenhake.20 In this case, a first filed financing statement filed under the correct name of Bad's Equipment Co. was held to be effective and sufficient to perfect a security interest, but not necessarily valid or enforceable. The court indicated that one of the original lenders found himself making a similar argument to the court in Union, as noted supra, after having prod all of the facts and circumstances of the transaction to the court in order to seek a determination of whether the first filed financing statement was sufficient to perfect a security interest.

The UCC court also stated that constructive notice by the bank of Uhlenhake's use of the assumed name would have been sufficient to deny prior perfected interest claims. The UCC court stated that in the absence of a financing statement under the correct name of L. W. Uhlenhake, Uhlenhake was an individual, doing business under the assumed name of L. W. Uhlenhake Equipment Co. A bank, in good faith, would not be held to have notice of a conflicting financing statement under the debtor's correct name. Section 9-402(7) requires that a financing statement file under the name "individual, partnership or corporate name of the Debtor." This section permits trade names to be included in a financing statement. In addition, the court noted, Uhlenhake's use of the assumed name was not a "deceptive or misleading" practice.

What is the effect of this decision on banks that have filed financing statements under the wrong names? The effect of the decision in Uhlenhake on your security interest is that you may not have a perfected security interest if the debtor is using a different name.

B. Bulletin No. 3 - Form and Format Problems

This problem is straightforward. If you are unsure about the name that you have filed with the UCC, you may have a perfected security interest. However, if you have filed under the debtor's correct name, you may have a security interest that is not perfected.

C. Bulletin No. 4 - The Question of Priorities

This problem is more complex. If you have filed under the debtor's correct name, you may have a perfected security interest. However, if you have filed under the debtor's assumed name, you may not have a perfected security interest. In order to determine which of your interests is better, you must file a financing statement under the correct name of the debtor.

What is the difference between a perfected and an unperfected security interest? A perfected security interest is a security interest that is perfect by the filing of a financing statement. An unperfected security interest is a security interest that is not perfect by the filing of a financing statement.

D. Bulletin No. 5 - The Question of Priorities

This problem is more complex. If you have filed under the debtor's correct name, you may have a perfected security interest. However, if you have filed under the debtor's assumed name, you may not have a perfected security interest. In order to determine which of your interests is better, you must file a financing statement under the correct name of the debtor.

E. Bulletin No. 6 - The Question of Priorities

This problem is more complex. If you have filed under the debtor's correct name, you may have a perfected security interest. However, if you have filed under the debtor's assumed name, you may not have a perfected security interest. In order to determine which of your interests is better, you must file a financing statement under the correct name of the debtor.

What is the effect of the decision in Union on your security interest? The effect of the decision in Union on your security interest is that you may not have a perfected security interest if the debtor is using a different name.
companies have their chief executive of-
• fice in Minnesota. The lender (Alitaste) entered a factoring arrangement with Dittrich and Zappia secured by personal property including accounts.

To perfect a security interest in accounts, UCC section 9-103(5)(b) calls for a filing at the county to the county in which the underlying debtor is located (UCC section 9-401). The state where the debtor is located. Section 9-103(5)(d) specifies that a debtor is located at its place of business or chief executive of-
• fice. In Alitaste, this would require that a financing statement covering accounts be filed in Minnesota for each of these two debtors.

Alitaste properly filed against Dittrich in Minnesota, but filed against Zappia in New York and Pennsylvania. Without a filing against Zappia in Minnesota, it should have been clear that the security interest in Zappia’s accounts was unperfected.

The Eighth Circuit nonetheless held that the filing in Minnesota under the name “Dittrich & McKee” was also sufficient to perfect a security interest at Zappia Transportation. The court apparently treated the manner as akin to a trade name filing, citing a trade name filing case. The court also emphasized the “unique relationship” between these separate corporations (they share the same president and chief executive officer under a “parent umbrella”), citing Avco Delta Corp. v. Canada, Ltd., v. United States. The court concluded that the filing against Dittrich was not seriously misleading as a filing against Zappia.

This case is troubling enough if considered as trade name filing case. As in Uhlholt and McDerme, the lender’s legal and trade name are entirely dissimi-
• lar, it is not clear whether the lender would have even signed the UCC-4 Request for Information and permitted the filing office to conduct the search for you. That is the best way to avoid the ThriftyWay problem, when the search report generated by the filing office will generally be a written res-
• pose to the exact name that the office was requested to search, and it would be an exception, rather than the rule, for the report to disclose something similar to that of the name that was searched. The folks in the filing office are probably nice people; however, the lender’s perspective is not likely to be better served by obtaining a search report through an independent search company.

Using an independent searching service is known to be aware of all of the risks, potential pitfalls of searching. Search firms generally file a search request with the creditor’s name printed in three different fonts in the search request form, such as how to deal with the five font formats. Make sure that it is one that is aware of the “similar name” prob-
• lem created by cases like ThriftyWay and Mines Tax, and the “assumed name” problem created by cases like Uhlholt and even cases like Alitaste, and will make a concerted effort to avoid all of the pitfalls created by these cases and similar cases.

There is no such thing as a perfect search service that guaran-
• tees to examine the originals of any filing to make that they were made ahead of time. A search in the modern filing office usu-
• ally begins at the computer terminal. However, the searchers keep in mind the fact that the information that is seen on the computer monitor may not be the same information that appears on the original document that was filed. The information that appears on the computer screen may be only the interpretation and rendition by a member of the filing of-
• fice staff of the information that was con-
• tained in the original document that was filed. Any information that is error caused by such staff has been noted to necessi-
• tate the examination of the original of any document that has been filed prior to any filing that has been made by the secured party for whom the search is being made. Recently, for example, while conducting a lien search in the Oklahoma City Clerk’s Office, one of your authors pulled up a continuation statement that had been filed by one of his clients. To his author’s dismay, the continuation statement that was displayed on the computer screen contained a collateral description.

Confident that his client had not filed such a document, he obtained the origi-
• nal continuation statement for examina-
• tion and discovered that the original document did not contain a collateral description. Further, in comparing the collateral description on the computer-
• ized version of the continuation state-
• ment, with the collateral description on the related financing statement, a vari-
• ant was noted. Some of the collateral that appeared on the financing statement was not included in the collateral descrip-
• tion that the Clerk’s Office had grar-
• iniously added to the continuation state-
• ment that appeared on the monitor. As a result of the loan, an unforeseen problem for the lender could easily have been created in believing that the secured party had continued only as to the collateral that appeared on the computerized version of the continuation statement and intended to abandon or release the emi-
• nted collateral. This incident is reported to illustrate that human error occurs in almost any filing office from time to time. Your author called the attention of the Clerk’s Office to the fact that it was not required or authorized to add a collateral description to the continuation statement that were being filed, and that by doing so it was creating unnecessary work for the staff, and further, that it was doubtful that anything but trouble would be the result of the practice. The Clerk has since ceased the practice of adding collateral description to the continuation statements that are filed. In using an independent search, some cause of action may lie against thesearcher for negligence. On the other hand, the filing office typically purports to have sovereign immunity under state law.

VI. Helpful Hints to Lien Searchers

One lesson of all of this is that a UCC search should be wary of relying on a UCC lien search conducted by the staff of the filing office. That is, do not send the filing office a UCC-4 Request for Information and permit the filing office to conduct the search for you. That is the best way to avoid the ThriftyWay problem, when the search report generated by the filing office will generally be a written response to the exact name that the office was requested to search, and it would be an exception, rather than the rule, for the report to disclose something similar to that of the name that was searched. The folks in the filing office are probably nice people; however, the lender’s perspective is not likely to be better served by obtaining a search report through an independent search company.

VII. The Proposed Article 9

Revisions

A. Background and Unresolved Issues

Numerous distinguished Article 9 commentators have seriously advanced having hung, high and dry, swinging in the wind, unperturbed, any secured party who fails to include on the financing state-
• ment, with jolt and title preci-
• sion, the exact legal name of the debtor, with all studies of the “so similar as to not be seriously misleading” concept be-
• ing abandoned, in order to resolve the “thriftyway problem.” However, this approach is not in the best interests of anyone. It could possibly have the effect of turning down the house to get rid of the termites. What is needed, of course, is to give effect to the doctrine that as between two “innocent” parties, any loss should be borne by the party who could have prevented the loss.

Clearly, the revised version of sec-
• tion 9-402(5) should ensure that one or two files under a business entity debtor’s legal name, after having cleared a search report on that name in due course from the filing office, should be given priority. However, it would be wise for Article 9 to stop short of rendering the first file unperturbed for having missed the mark to some minor degree. The best of both words could be utilized by giving effect to a filing under a similar, but inexact, debtor name for the purpose of perfection, but with priority being given to the file who filed first under the debtor’s legal name, after having cleared a search report made under that name. If the first file is rendered unperturbed by reason of having missed the mark, many first filers will find them-
• selves in a secondary and inferior position in that to some lien creditor who was in no way prejudiced or injured by the earlier, deficient filing. Unfortunately, except as noted infra, the Article 9 revision does not address this.

Attemping to solve the myriad of problems associated with the names of individual debtors requires a somewhat different approach from that dealing with business legal entities. Use of the term “legal name” with reference to an individual’s name may leave many questions unanswered. What is an individual’s legal name? Can it be anything less than the full name that appears on the person’s birth certificate? Bell’s Law Dictionary defines “legal name” as: “Under common law consists of one Christian name and one surname, and the insertion, omission, or alteration of any part of an individual’s name is immaterial.” Under that definition, the term “legal name” would be limited to the debtor’s first and last names, with errors as to middle name or initial being rendered incomensurable. As revised Article 9 requires use of the debtor’s individ-
• ual name, there may be some remaining uncertainty as to precisely what that name is.

The Article 9 Drafting Committee Committee is in quest for reasonable certainty in matters of searching and filing, not the least of which may be the soon to be enacted Fed-
• eral Right of Access to Privacy Act. This Act would make it an “unfair credit prac-
• tice” for any insured lender to obtain the birth certificate of an applicant. This noble undertaking is designed to prohibit a lender from discovering either that the applicant was conceived out of wedlock or the identity of the applicant’s parents. Presumably the purpose of the latter safeguard is to impede the possible prejudicial-
• al discovery that a parent may have been deviant or a distant relation of lenders, with the resulting possibility that the ap-
• plicant carries the dreaded TBTF (cause to break fear of gene). Obviously, however,
the Drafting Committee cannot undertake to deal with every example of legislative folly.

Other hurdles include the common use by debtors of initials, abbreviated first names, and nicknames. "Robo in Hill," neither of FBM's two searches, under that name Jeff Sharp, was successful in discovering an earlier filing that Crystal Hill had made under the debtor name of Jeffrey Keith Sharp.74 The Uthahalhe council would not probably hold a filing under the name of "Polo," Davi, as being sufficient to perfect, due to that name's being better known to the general public than the debtor's legal name of Almargen Horatio Davi (the fictitious automobile dealer operating his business in a sole proprietorship). Under the circumstances, it would probably be an unconstitutional invasion of privacy to force such an applicant to disclose his or her legal name to a prospective lender, in such a disclosure might lead to the borrower's loss of membership in the draft's association.

The ultimate goal, of course, is for priority to be given to a secured party who files first under a name that satisfies the requirements of the revised version of current section 9-402.77 and who has relied on a clear search report under that name obtained from the filing officer. How to get there? That is the question.

II. The Proposed Article 9 Revisions

Revised Article 9 (August 5, 1998 draft) deals with these issues primarily at revised sections 9-503 and 9-506. The text of section 9-503 is as follows:

**SECTION 9-503. NAME OF DEBTOR AND SECURED PARTY.**

(a) A financing statement suf-

ficiently identifies the name of the debtor:

(1) if the debtor is a regis-

ted organization, only if the financing statement provides the name of the debtor indicated on the public record of the debtor's jurisdiction of organization which shows the debtor to have been organized;

(2) if the debtor is a decedent's estate and if the financing statement provides the name of the decedent and indicates that the debtor is an estate;

(3) if the debtor is a trust or a trustee acting with respect to property held in trust, only if the financing statement:

(b) provides the name, if any, specified for the trust in its organic documents, or if no name is specified, provides the name of the settlor and additional information sufficient to distinguish the debtor from other trusts having one or more of the same settlor; and

(c) if the debtor is a trust or a trustee acting with respect to property held in trust, only if the financing statement:

(1) a trade or other name of the debtor; or

(2) unless required under subsection (a)(4)(A), names of partners, members, associates, or other persons comprising the debtor.

(c) A financing statement that provides the name of the debtor in accordance with subsection (a) is not rendered ineffective by the absence of:

(1) a trade or other name of the debtor; or

(2) unless required under subsection (a)(4)(B), names of partners, members, associates, or other persons comprising the debtor.

(d) A financing statement that provides only the debtor's trade name does not sufficiently identify the name of the debtor.

(e) Failure to indicate the representative capacity of a secured party or representative of a secured party does not affect the sufficiency of a financing statement.

(f) As excepted otherwise provided in subsection (a), a financing statement that fails sufficiently to provide the name of the debtor (in accordance with Section 9-503(a)) is seriously misleading.

The basic thrust of section 9-503 is to reaffirm the necessity of filing under the debtor's correct legal name, thereby rectifying cases like Thriftywae. While this confirms current law, more specific guidance is provided by referencing the public records of the incorporation state, secured parties will thus need to require a copy of the certificate of incorporation but can then safely rely on use of the name provided in that certificate. Specific guidance is also provided with regard to trusts and decedent's estates, unlike current law which is silent on these issues.

Subsection 9-503(b) similarly provides specific guidance regarding such debtors as unincorporated associations and unregistered joint ventures.

Subsection 9-503(c) deals with the trade-name problem and related issues. It provides clearly that a filing need not include the debtor's trade name to be effective. Revised Article 9 also states at section 9-503(c)(1) that a trade-name filing alone is not sufficient. Surely, this is as clear as it can be, and in conjunction with subsection 9-503(a) constitutes an unmistakable rejection of the Thriftywae rationale.

Revised section 9-506 reads as follows:

**SECTION 9-506. EFFECT OF ERRORS OR OMISSIONS.**

(a) A financing statement substantially complying with the requirements of this part is effective, even if it contains minor errors or omissions. It is less the errors or omissions make the financing statement seriously misleading.

(b) As excepted otherwise provided in subsection (a), a financing statement that fails sufficiently to provide the name of the debtor (in accordance with Section 9-503(c)) is seriously misleading.

The basic thrust of section 9-506 is to reaffirm the necessity of filing under the debtor's correct legal name, thereby rectifying cases like Thriftywae. While this confirms current law, more specific guidance is provided by referencing the public records of the incorporation state, secured parties will thus need to require a copy of the certificate of incorporation but can then safely rely on use of the name provided in that certificate. Specific guidance is also provided with regard to trusts and decedent's estates, unlike current law which is silent on these issues.

Subsection 9-506(c) follows the philosophy of the Texas solution to the Meche case by focusing on whether a party searching under the correct name would have discovered the competing financing statement. If so, then any error is not seriously misleading. If the filing is made effective by section 9-506(a), even if it does not conform to the requirements of section 9-503. Otherwise, unless under subsection 9-506(b), a failure to meet the standards at section 9-503(a) is fatal to perfection. Again clearly rejects the Thriftywae rationale, while providing a safeguard against excessive zeal in pursuit of perfection, under subsection 9-506(c). It is a good package which addresses the major problems discussed supra at Parts II.A., II.C., and III.

The impact on Mines Tire is less clear. In such circumstances, unless the revision, both the arguments of Mines Tire and the Trustee would be inadequate. It will not be sufficient to argue, as the Trustee did, that perfection is required; nor will it be sufficient to say that Mines Tire argued and the court concluded) that computer search logic is irrelevant and a filing good under a manual system will remain valid even when the files are computerized. Instead, under the revision, it will be necessary to test an imperfection filing under the standard set at section 9-506(c). It is quite possible that, as a result, the decision in Mines Tire might be different under revised Article 9.

The Union problem (see supra Pt. II.B.) is addressed in part at revised section 9-506, which reads as follows:

**SECTION 9-508. EFFECTIVENESS OF FINANCING STATEMENT IF NEW DEBTOR BECOMES BOUND UNDER SECURITY AGREEMENT.**

(a) Except as otherwise provided in this section, a filed financing statement naming an original debtor is effective to perfect a security interest in collateral in which a new debtor has or acquires rights to the extent that the financing statement would have been effective had the original debtor acquired rights in the collateral.

(b) If the difference between the name of the original debtor and the new debtor causes a filed financing statement that is effective under subsection (a) to be seriously misleading under the standard set forth in Section 9-506:

(1) the financing statement is effective to perfect a security interest in collateral acquired by the new debtor before, or within forty months after, the new debtor becomes bound under Section 9-203(c); and

74. Subparagraph added by the Bankruptcy Act of May 28, 1938, which changed the name of the Bankrupt and its affiliated companies to the same.

75. Paragraphs (a) and (b) of this section are substantially the same as paragraphs (4) and (5) of section 9-503(a).

76. Paragraph (a) provides a rule for the same purpose as for a similar rule in section 9-503(a), as one of those permitted for a similar purpose under section 9-503(a).
(2) the financing statement is not effective to perfect a security interest in collateral acquired by the new debtor more than four months after the new debtor becomes bound under Section 9-203(c) unless an initial financing statement providing the name of the new debtor is filed before the expiration of that time.

(c) This section does not apply to collateral as to which a filed financing statement remains effective against the new debtor under Section 9-507(a).

Subsection 9-508(a) provides that where a new debtor (e.g., Webb Expanded, Inc.) acquires rights in the collateral of the original debtor (e.g., Webb Metals, Inc.), the financing statement filed under the name of the original debtor will continue to be effective for perfection to the extent it would have been effective against the original debtor. However, if the names of the original and new debtor are so different that under section 9-506 the financing statement is seriously misleading as to the new debtor, the financing statement is effective only as to collateral required before or within four months after the date the new debtor becomes bound by the security agreement under section 9-203(c). In this circumstance (where the difference in names is seriously misleading under section 9-506), the financing statement filed under the name of the new debtor is not effective as to collateral acquired after the four month period unless a new financing statement is filed prior to that time. This does not apply to debtor name changes, which are governed by section 9-507(c). It also does not apply to the sale or other disposition of collateral under section 9-507(a), as specified at section 9-508(c).

The fancy footwork used by co-author Carroll in the Union case is codified to some extent (contrary to current law) by revised section 9-203(d), which reads as follows:

(d) A person becomes bound as debtor by a security agreement entered into by another person if, by operation of law other than this article or by contract:

(1) the security agreement becomes effective to create a security interest in the person’s property; or

(2) the person becomes generally obligated for the obligations of the other person, including the obligation secured under the security agreement, and acquires or succeeds to all or substantially all of the assets of the other person.

Subsection 9-203(d) contemplates that a new debtor may become subject to a security agreement executed by the old debtor, without signing the security agreement, in the enumerated circumstances, as in Union. In such a case, the analysis will then shift to sections 9-506 and 9-508, to determine if any difference in the names of the two debtors is seriously misleading so as to require a new financing statement with regard to collateral acquired by the new debtor more than four months later.

VIII. Conclusions

Revised Article 9 does a commendable job of ending the current game of Russian Roulette—UCC Style. It addresses the major problems and uncertainties discussed in this article, while eliminating some of the rough edges in the current statute (which have probably contributed to some of the aberrant case law).

Revised Article 9 is as clear as it could be on these issues, and indeed could be of use to courts confronting these issues under current law. If revised Article 9 is enacted, the courts will have very little excuse to play the name game with secured parties in the future.
IX. Conclusion

The U.S. Supreme Court in the Rash case determined that a higher standard of value should apply when the debtor proposes to "cram down" the collateral in a Chapter 13 case. However, because of the practical effect of interpreting the meaning of "replacement value," little has changed in the valuation process. And, because the Chapter 13 system is stuck against the auto lender, and especially the sub-prime auto lender, valuation may be the least of the creditor's worries. However, despite the devastating effect of the automatic stay and the Chapter 13 cram-down, there are a few ways the pro-active creditor can and should protect its interests.

Because it is generally perceived by society that a Chapter 13 rehabilitation plan is preferable to a Chapter 7 liquidation from the standpoint of both debtors and creditors, Congress has taken steps to encourage Chapter 13 filings over Chapter 7. However, the societal preference for Chapter 13 is the worst thing that can happen to motor vehicle lien holders.

Commentary: A Case Study in Bankruptcy Abuse?

By Alvin C. Harrell

The articles in this Symposium on Bankruptcy Reform address issues and potential solutions relating to alleged credit and bankruptcy abuses. As a case study to conclude this Symposium, consider the following real-life bankruptcy case scenario.

The debtors obtained a first mortgage home loan on March 1, 1995, in the amount of $3,500 (yes, that is only $3,500), at a rate of 12% interest for three years. The home was old and in poor condition, with an estimated value of around $5,600. The loan payments were $115.10 per month. The loan was fully amortizing and would have been paid in full by now had the scheduled payments been made.

Just over a year after the loan was closed, the borrowers divorced. The husband was awarded the house. The husband had a good income and credit record, but soon filed bankruptcy, discharging his personal liability for this mortgage debt. Nonetheless, the wife (who continued to occupy the property) had a steady job and should have been able to pay the $115.10 per month house payments. She soon remarried and should have once again had a household with two incomes to make this minimum house payment. At the time of the divorce, the first mortgage loan balance had been reduced to just over $2,000.2

Apparently the lawyer who handled the divorce continued afterward to advise the wife (now the sole debtor on the loan) regarding financial matters, as she made several prominent references to her lawyer in early conversations with the lender's staff. For whatever reason, immediately after the divorce the debtor ceased making payments on this $2,000 loan. At the time this article was written she had not made any further payment, except that on July 2, 1997 she made one payment (for September, 1996), apparently in an effort to delay commencement of foreclosure. In the roughly two-year period between late August 1996 and early July 1998, this was the only payment the lender received.

Despite the small size of the loan, and ample collateral, the lender worked hard to develop a forbearance arrangement with the borrower. Several workout arrangements were made and broken by the borrower, with the exception of the September, 1996 payment (paid in July, 1997), the borrower never made any of the promised payments. It finally became apparent that the debtor was merely stalling, and the lender reluctantly concluded that the debtor had no intention of paying the loan.

Finally, on August 22, 1997, a year after the debtor defaulted, the lender began foreclosure. By January 1998, a sheriff's sale had been conducted and the property had been sold (ironically at a price well above the lender's estimate of value) to an unrelated third-party bidder, who borrowed the funds elsewhere and paid the cash into the court. Then, only hours before the scheduled confirmation of the sale, the borrower filed bankruptcy under Chapter 13.

One of the losers in all of this was the buyer at the sheriff's sale, who paid interest on borrowed funds for several months during a frustrating effort to get his money back after the sale was canceled due to the Chapter 13 filing. While sheriff's sale bidders are not exactly a favored group, this sort of experience can only operate to impair the viability of foreclosure sales and further depress the prices received by borrowers and lenders. Ironically, the bidding at this sale was noteworthy for its generosity. But if bankruptcy is used to regularly foil sheriff's sales, frustrating the judicial process and imposing hardships on the bidders, we will soon be hearing more complaints by debtors' counsel that foreclosure bid prices are depressed because independent third parties seldom bid at sheriff's sales.

In the meantime the debtor had lived in the home for 16 payment-free months (through January, 1998). But now, it was thought, after the bankruptcy filing the debtor would at least have to make some payments under the Chapter 13 plan. The lender accepted the debtor's proposed plan, and waited to begin receiving payments. And waited. And waited.

When this article was written (early July, 1998) the lender still had not received a single payment under the Chapter 13 plan. (As this issue went to press, the lender received its first payment from the Chapter 13 trustee.) But the debtor has regular income, as she has had during the entire two-year period in question. And, once the plan was confirmed, she began making payments. Where did the money go between January and July, 1998?

What a surprise: Apparently it mostly went to pay the debtor's attorney, $1,400, along with some other smaller administrative expenses and priority claims.

Surely at this point the lender can be forgiven for feeling that this debtor, possibly in conjunction with her lawyer, intentionally abused the lender's good faith efforts to work with her, the state court legal system, and the bankruptcy process. From the lender's perspective, it appears that the goal of all this was to allow the debtor to retain the collateral for as long as possible without paying this lender, imposing the costs of collateral depreciation on the lender, and in the process divert any payments to the lawyer's burner. When this article was written the lender had received only one payment in nearly two years, and after nearly six months had received nothing in the Chapter 13 case, while $1,400 was paid to the debtor's lawyer under the Chapter 13

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1. As noted infra, when this debtor later filed Chapter 13 bankruptcy she proposed to reduce the payments only slightly, to $480.97, suggesting that the $115.10 payment was not a significant hardship.
2. There were also two judgments against the debtor, but under Oklahoma law at that time it is possible that these would not attach to the homesteaded property. In this case, the debtor could have stopped enforcement of those items merely by occupying the property as a bona fide use. The judgments became dormant after five years.
3. The lender's claim was classified as fully secured, and the interest rate was 17%. The monthly payments were reduced from $115.10 to $108.07.
Yield Spread Premium Litigation:
The Eleventh Circuit Clarifies and Limits Its Holding in Culpepper v. Inland Mortgage

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that yield spread premium payments can be valid payment for goods and services and that class certification is inappropriate. Exactly how the Eleventh Circuit's clarification of its holding in Culpepper will affect existing yield spread premium litigation will depend on how other courts react to this new opinion, and on the particulars of the individual cases. Lenders or other persons interested in the Culpepper decision, its subsequent clarification by the Eleventh Circuit, and other related issues should feel free to contact their counsel, or the authors, for more information.

The Science Behind Credit Card Offers

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past performance was the best indicator of future performance, but that paradigm is changing to a degree, as many products provide cash access utility. The availability of cash allows a greater degree of camouflaging cash flow issues. In addition, a dramatic change in job security, health, or marital status can all negatively impact credit performance.

Rising consumer bankruptcy is the most critical issue we are facing, and controlling the flow of credit to consumers to limit exposure is of utmost importance. Significant effort has been expended to train our employees to be excellent listeners and work with consumers at all times. Households actively supports Consumer Credit Counseling which assists consumers through difficult financial times. On a personal level, I am a tremendous advocate of enhancing consumer credit education. Through my membership with the International Credit Association, I have been involved in teaching a high school curriculum and personally addressing over 1,000 teachers from Alaska to Florida and Delaware to California. Much work is required in this area, as I am convinced that heightened consumer awareness regarding the managing of financial affairs is critical.

I hope that my discussion has provided some insight into the sophistication and complexity involved as we attempt to manage consumer credit. My intent was to demystify a very complex process by discussing the many dimensions of making a credit offer and managing consumer credit. It is not our intent to overburden a consumer with debt, but provide a product that will offer value to the consumer and provide an adequate return to our shareholders.

Commentary: A Case Study in Bankruptcy Abuse?

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plan. Once the lawyer's fee is paid, it is quite possible the debtor will default again, the Chapter 13 case will be dismissed for nonpayment, and the state foreclosure process (with another long delay) will start all over again. It is even possible that the next foreclosure sale could be frustrated by yet another bankruptcy filing. How long can this go on, with the lender receiving nothing while the debtor's counsel earns nice fees? Apparently, a long time. (See note 5.)

There is some additional irony in this case study. All of this legal maneuvering concerned a roughly $2,000 first mortgage loan at a relatively low 12% simple interest rate, fully amortized over a three year term, with payments of only $115.10 per month. This was not some high rate, abusive transaction that the debtor needed to escape from. The debtor had a good deal and was close to having her home paid for. There was no prepayment penalty, and the loan could have been paid in full for little more than the fees she has paid to her lawyer. Had the borrower paid only $115.10 per month the loan would have been paid in full long ago. She had a good equity in the house and should have owned it free of this mortgage by now.

Instead, after two years, the debtor's loan balance (including foreclosure costs and the lender's attorney fees) has doubled to roughly $4,000. The debtor's equity in her home is probably gone (along with her lawyer's bill) if the court is willing to pay a very generous price for the house). While anything is yet possible, it remains possible that this borrower will eventually lose her home to foreclosure. Even if this bankruptcy was used to relieve the debtor of other, more burdensome debts, it is not clear how the debtor benefited by her two-year default on this home mortgage loan.

It is not clear why the debtor decided to default, stall, and file bankruptcy as an alternative to making the payments on her $2,000 first mortgage loan. We cannot know whether this debtor genuinely needed to default and file bankruptcy, or whether she was encouraged to take the easy road of default by the promise of bankruptcy relief.

If the prospect of bankruptcy encouraged the debtor to default on this $2,000 first mortgage loan, is any loan safe? Is it appropriate for bankruptcy to be used primarily as a means to delay a mortgage foreclosure (or enforcement of a security interest)?

Your author does not purport to know the answers to these questions, and is hesitant to sit in an ivory tower criticizing practitioners who are out there in the trenches trying to make the bankruptcy system work. But it is noteworthy that none of the

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4. Again, it is noteworthy that the only modification in the Chapter 13 plan was a $7.03 reduction in the monthly payment.

5. In a best case scenario, if this debtor now decides to make her payments and complete the Chapter 13 plan, ultimately paying the loan in full, paying her counsel fees she will pay roughly three times the $2,000 she owed when she initially defaulted.

6. The divorce decree indicates that the debtor had no other debt at the time of the default, except income taxes and a car loan (both of which the former husband agreed to pay). This is consistent with the original credit application and credit report, which show no other debts except the above and a $600 credit card bill. However, your author has received other information indicating that these may have been significant other debts that justified the bankruptcy filing. But even so, what was the point of defaulting on this minimal home mortgage loan?

7. This case is purely anecdotal and is presented as such. However, other published reports suggest this may not be an isolated incident. See, e.g., Foreclosure Science: When Can Be Done to Stop Home? 32 Real Estate News & Comment No. 13 (July 3, 1990), at 1.