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REAL ESTATE TRANSACTIONS AND THE UNIFORM COMMERCIAL CODE: METHODS OF INDEXING FINANCING STATEMENTS

by Lynda L. Butler

As any experienced real estate attorney knows, the relationship between real estate transactions and commercial law is close — sometimes too close for comfort. Not only must the real estate attorney understand the intricacies of real property law; he or she also must master the complexities of the Uniform Commercial Code (UCC). With its recently proposed Article 2A on leases, its Article 3 and 4 provisions on negotiable instruments, and its Article 9 sections on security interests and financing statements, the UCC always seems to have some provision that is applicable to real estate transactions. When the provision dictates a result that is contrary to the basic practices of real property law, attorneys understandably become frustrated.

Take, for example, the issue of disbursement of settlement proceeds. Because of the final payment provisions of the UCC, a diligent settlement attorney could easily breach his statutory duty to disburse. See generally Butler, "The Wet Settlement Act and the Problem of Delayed Disbursements," 6 Real Property Section Newsletter 13 (May 1986). Or consider the problem of lost note affidavits. Under basic negotiable instruments law, a real estate attorney cannot rely on a lost note affidavit to assure her client that payment to the party making the affidavit will discharge the client's liability on the note. See generally Butler, "Lambert v. Barker and Lost Note Affidavits," 8 Real Property Section Newsletter 16 (November 1987).

Because of the role that commercial law principles play in real estate transactions, an ongoing column focusing on that role seems appropriate. Past Newsletters have already discussed the disbursement and payoff issues mentioned above. See Newsletters cited supra. Today's Newsletter will focus on methods of indexing the continuation of financing statements by clerks of the circuit courts. A recent Virginia Attorney General's opinion discusses that topic in some detail. The opinion is set forth below.

June 9, 1989

The Honorable G. Steven Agee
Member, House of Delegates
1919 Electric Road, S.W.
Roanoke, Virginia 24013

You ask whether § 8.9-401 and 8.9-403 of the Code of Virginia, or any other portions of the Uniform Commercial Code, require a particular method of indexing the continuation of financing statements by the clerk of a circuit court. You state that some clerks index continuation statements chronologically with all other financing statements received on the day of filing, and that other clerks index the continuation statement on the same page as the original financing statement was indexed.
I. Applicable Statutes

Section 8.9-401 details the different places in which financing statements must be filed to perfect a security interest in certain types of collateral. Section 8.9-402 establishes the formal requisites for a financing statement, and, in subsection 4 provides, in part, that "[a]ll amendments to financing statements shall identify the original financing statement by file number."

Section 8.9-403 specifically concerns continuation statements and provides, in part:

(2) Except as provided in subsection (6) a filed financing statement is effective for a period of five years from the date of filing. The effectiveness of a filed financing statement lapses on the expiration of the five-year period unless a continuation statement is filed prior to the lapse. . . .

(3) A continuation statement may be filed by the secured party within six months prior to the expiration of the five-year period specified in subsection (2). Any such continuation statement must be signed by the secured party, identify the original statement by file number and state that the original statement is still effective. . . . Upon timely filing of the continuation statement, the effectiveness of the original statement is continued for five years after the last date to which the filing was effective whereupon it lapses in the same manner as provided in subsection (2) unless another continuation statement is filed prior to such lapse. Succeeding continuation statements may be filed in the same manner to continue the effectiveness of the original statement. Unless a statute on disposition of public records provides otherwise, the filing officer may remove a lapsed statement from the files along with the index thereto and destroy it immediately if he has retained a microfilm or other photographic record, magnetic tape or security record, or in other cases after one year after the lapse. The filing officer shall so arrange matters by physical annexation of financing statements to continuation statements or other related filings, or by other means, that if he physically destroys the financing statements of a period more than five years past, those which have been continued by a continuation statement shall be retained.

(4) A filing officer shall mark each statement with a file number and with the date and hour of filing and shall hold the statement or a microfilm or other photographic copy thereof for public inspection. In addition the filing officer shall index the statements according to the name of the debtor and shall note in the index the file number and the address of the debtor given in the statement.

Section 17-78 is the general statute requiring that certain indices be maintained by circuit court clerks and provides, in part, that "[t]he clerk of every court shall have an index to each book he is required to keep, except those for which general indexes are required and kept, or permitted and kept, making convenient reference to every order, record or entry therein." Section 17-79(1) further provides:
There shall be kept in every clerk's office modern, family name or ledgerized alphabetical key-table general indexes to all deed books, miscellaneous liens, will books, judgment dockets and court order books. The clerk shall enter daily either in such general indices or in the daily index to instruments admitted to record, all instruments admitted to record, indexing each instrument in the names of all parties appearing therein who are thereby shown to be affected by the instrument.

Section 17-79(9) further provides that "[t]he clerk may maintain his indices on computer, word processor, microfilm, microfiche or other micrographic process."

II. Indexing Method Used Depends on Whether Clerk's Office Has Manual or Computerized Operation

The statutes quoted above, when read together, merely require that circuit court clerks maintain a system of indices for records filed. Section 8.9-403(4) requires that a financing statement shall be indexed according to the name of the debtor, with a notation indicating the file number and the debtor's address. Continuation statements are to be attached to the original corresponding financing statements to avoid destruction of older financing statements. See § 8.9-403(3). These statutes are silent, however, concerning the specific indexing method to be used by circuit court clerks for continuation statements.

Circuit court clerks' offices in the Commonwealth serve jurisdictions with varied populations. The larger the jurisdiction served by the circuit court clerk, the more likely it is that the clerk's office will be a computerized, rather than a manual, operation. If a circuit court clerk's office uses a manual index book for financing statements, a clerk often will record the continuation statement on the same page of the index as the original financing statement was filed. In these jurisdictions, a title examiner simply would check the financing statement index for the year of the filing of the original financing statement and a complete history of the lien would be shown on that page.

Other jurisdictions utilize manual recordation systems, but are contemplating computerization and the microfilming process that accompanies computerization of these systems. These circuit court clerks often find it preferable to avoid updating their original indices and to file continuation statements chronologically, or by the date of their receipt.

In circuit court clerks' offices using a computerized recordation system, chronological indexing is preferable, although not required by statute, given the practical inability of the clerk to update the indexing notation on the original financing statement. Assuming the alphabetical index of financing statement debtors, the title examiner would locate the debtor's name in the index and complete a six-year search under the debtor's name to find any applicable financing statements, continuation statements, or other entries.

III. Chronological Filing by Date of Receipt Is Preferable Indexing Method, But Not Required by Statute

The varied methods used by circuit court clerks to index financing and continuation statements place different burdens on title examiners. As noted in the Official Comment to § 8.9-403, the purpose of this statute is to allow for "self-clearing" files.
The clerk automatically may discard each financing statement after a period of five years, plus an additional year of lapse required in § 8.9-403(3), unless a continuation statement is filed or unless the financing statement remains effective under § 8.9-403(6), which deals with real estate mortgages that are treated as fixture filings. The Comment further notes that, if the indices are arranged by years, the title examiner will have a limited and defined search of six years. This implies a legislative preference for chronological indexing. As long as the clerk follows the requirements of the statute by referencing the original financing statement and attaching the copy of the original financing statements to the continuation statements, a manual system organized by alphabetic debtor indices also should allow for a manageable search process.

Because of the diversity of circuit court clerks' offices in the Commonwealth, both in terms of the varied sizes of the jurisdictions served and their degrees of computerization, it is my opinion that, in the absence of a specific statutory requirement for the chronological indexing of financing statements and continuation statements, clerks may use either of the indexing methods described above. Although statewide consistency in the indexing of these statements may be preferable, a single method of recordation has not been required by the General Assembly.

VIRGINIA PROPERTY OWNER'S ASSOCIATION ACT UPDATE

The Office of the Attorney General was recently requested to respond to several questions regarding the interpretation of the Virginia Property Owner's Association Act.

On October 17, 1989 the Attorney General issued an official opinion which concluded that a purchaser has the option to avoid a sales contract subject to the Act if the seller has not inserted language in the contract as required by Section 55-511(A). Further, if a purchaser, whose contract was properly prepared in accordance with the requirements of Section 55-511(A) did not make a written request for the disclosure packet, the purchaser had waived his right to the packet's detailed disclosure.

In an unofficial letter opinion, dated November 13, 1989, the Office of the Attorney General responded to an inquiry whether, where a seller has fully complied with the requirements of the Act in providing to a purchaser under a sales contract the mandatory disclosure information, the purchaser has an implied right to rescind the contract if the disclosure information is unacceptable to the purchaser. The response of the Attorney General's Office to the foregoing is that there is nothing in the Act which gives the purchaser the right to avoid or rescind the contract if, upon review of the information received in the disclosure packet, the purchaser finds that information unacceptable. However, the letter opinion continued that "if the sales contract used, however, is prepared in such a way as to directly provide a purchaser with such an avoidance option, then the terms of the contract insofar as it applied to that provision would govern. The Act does not directly address the question, thereby leaving the parties the right and responsibility to negotiate such a term if they feel it is necessary."

The Board of Governors would like to receive comments on the Act, particularly with respect to problems which the membership is confronting with its application. Please direct communications to Joseph W. Richmond, Jr., P.O. Box 559, Charlottesville, Virginia 22902.