PEB COMMENTARY NO. 28
COLLATERAL DESCRIPTION FOR INVESTMENT PROPERTY
(January 16, 2024)

By the Permanent Editorial Board for the Uniform Commercial Code*

PREFACE

The Permanent Editorial Board for the Uniform Commercial Code (PEB) acts under the authority of the American Law Institute and the Uniform Law Commission (also known as the National Conference of Commissioners on Uniform State Laws). The PEB has resolved to issue supplemental commentary on the Uniform Commercial Code (UCC) from time to time. The supplemental commentary of the PEB generally will be known as a *PEB Commentary*, to distinguish it from the Official Comments to the UCC. A *PEB Commentary* may be denominated a commentary, a report, or otherwise as determined by the PEB.

The Resolution states that:

> The underlying purposes and policies of the *PEB Commentary* are those specified in Section 1-103(a). A *PEB Commentary* should come within one or more of the following specific purposes, which should be made apparent at the beginning of the Commentary: (1) to resolve an ambiguity in the UCC by restating more clearly what the PEB considers to be the legal rule; (2) to state a preferred resolution of an issue on which judicial opinion or scholarly writing diverges; (3) to elaborate on the application of the UCC where the statute and/or the Official Comment leaves doubt as to the inclusion or exclusion of, or application to, particular circumstances or transactions; (4) consistent with Section 1-103(a)(2), to apply the principles of the UCC to new or changed circumstances; (5) to clarify or elaborate upon the operation of the UCC as it relates to other statutes (such as the Bankruptcy Code and federal and state consumer protection statutes) and general principles of law and equity pursuant to Section 1-103(b); or (6) to otherwise improve the operation of the UCC.

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ISSUE

UCC Section 9-108 provides the rules that determine whether a description of property in a security agreement is sufficient, as required by Section 9-203(b)(3)(A).[1] Section 9-108(a) provides that a description is sufficient if it "reasonably identifies" the collateral. That general rule applies "[*e*]*xcept* as otherwise provided in subsections (c), (d), and (e)."[2] For purposes of Section 9-108, must a security agreement seeking to create a security interest in a security entitlement or a securities account satisfy subsection (d), or will the description also be sufficient without satisfying subsection (d) provided that the description does "reasonably identif[y]" the collateral under subsection (a)?

ANALYSIS

As a general matter, Section 9-108(a)'s "reasonably identifies" standard is satisfied when the description "make[s] possible the identification of the collateral described."[3] Subsection (a) applies "[e]xcept as otherwise provided in subsections (c), (d), and (e)," which read as follows:

> (c) [Supergeneric description not sufficient.] A description of collateral as "all the debtor's assets" or "all the debtor's personal property" or using words of similar import does not reasonably identify the collateral.
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> (d) [Investment property.] Except as otherwise provided in subsection (e), a description of a security entitlement, securities account, or commodity account is sufficient if it describes:
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> (1) the collateral by those terms or as investment property; or
> (2) the underlying financial asset or commodity contract.
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> (e) [When description by type insufficient.] A description only by type of collateral defined in [the Uniform Commercial Code] is an insufficient description of:
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> (1) a commercial tort claim; or
> (2) in a consumer transaction, consumer goods, a security entitlement, a securities account, or a commodity account.

Each of subsections (c), (d), and (e) is framed as an "exception" to subsection (a)'s general rule, but these exceptions do not each function in exactly the same way. An exception to a rule can expand, limit, or explain the application of the rule. Subsections (c) and (e) *limit* the general rule of subsection (a) and have the effect of making insufficient descriptions that would otherwise

[1] A "description" of collateral that satisfies Section 9-108 will also be sufficient to "indicate" the collateral in a financing statement. U.C.C. § 9-504(1). As a result, the conclusion stated in this Commentary will apply also to Section 9-504(1).

[2] All emphasis in quotations from the Uniform Commercial Code is added.

[3] U.C.C. § 9-108 cmt. 2. Section 9-108 also generally "rejects any requirement that a description is insufficient unless it is exact and detailed (the so-called 'serial number' test)." *Id.*

satisfy subsection (a). The exception in subsection (d) functions differently, in that it elaborates on the availability of the general rule of subsection (a) rather than limiting it.[4]

This effect of subsection (d) is best seen by considering its two paragraphs separately. Subsection (d)(1), taken on its own, neither limits nor expands subsection (a), but rather clarifies subsection (b)(3)'s validation of a description by "type of collateral defined in [the Uniform Commercial Code]".[5] Subsection (d)(2) provides in effect that a description that might *not* satisfy subsection (a) is nonetheless sufficient if it satisfies subsection (d)(2). Thus, taken as a whole, subsection (d) affords an additional method of describing investment property. It eliminates the need to determine whether the kinds of description provided for in subsection (d) satisfy subsection (a).

This reading of the effect of subsection (d) is supported by the text of Section 9-108, the purposes of Section 9-108, and the policies of Article 9.

Textually, when Section 9-108 limits the availability of subsection (a)'s "reasonably identifies" test, it expressly says so. Subsection (c) provides that a supergeneric description "does *not* reasonably identify" the collateral. Similarly, subsection (e) provides that certain descriptions by type are "*insufficient*."[6] By their own terms, those two subsections narrow the application of subsection (a). By contrast, the text of subsection (d) positively states that a description meeting the provisions of that subsection "*is* sufficient."[7]

The purposes, too, of subsection (d) differ from those of subsections (c) and (e). Subsection (d) originated as a conforming amendment to Article 9 as part of the 1994 revision of Article 8, which first stated the Code's concepts for the indirect holding of securities.[8] The 1994 revision represented a new conceptual framework for property rights with respect to indirectly held securities, with an accompanying new nomenclature. The drafters of Article 8 recognized that common and well-established patterns of practice and terminology would doubtless persist despite the amendments.[9] The persistence of these practices was particularly foreseeable in Article 9 transactions, in which Article 8 assets are frequent and important forms of collateral. Accordingly in 1994 and then continuing with subsection (d) in Revised Article 9, the drafters took steps to address directly the potential terminological problem.[10] Viewing the statute against this

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[4] Alternatively stated, subsection (d)(2) is an *exception* to a limitation implicit in subsection (a), namely that a description of property is not sufficient if it does not reasonably identify the collateral.

[5] Specifically, subsection (d)(1) clarifies that the more general type "investment property" and the more specific types "security entitlement," "securities account," and "commodity account" are equally valid descriptions.

[6] Other Article 9 provisions are similarly express in their restrictiveness when intended, notably Section 9-503(a) (financing statement sufficiently provides debtor's name "only if" certain conditions are met).

[7] The Official Comment to Section 9-108 is similarly enabling and positive, explaining that "the use of the wrong Article 8 terminology *does not* render a description *invalid*," without stating that the use of the correct Article 8 terminology is a requirement. U.C.C. § 9-108 cmt. 4. In the same vein the Comment goes on to provide as an example that "a security agreement intended to cover a debtor's 'security entitlements' is sufficient if it refers to the debtor's 'securities,'" using "if" rather than "only if." *Id.*

[8] *See* U.C.C. § 9-115(3) (1994).

[9] For example, parties carrying out transactions might refer to "my shares of Acme, Inc." rather than "my security entitlements to shares of Acme, Inc. stock represented by credits to my securities account maintained by Broker."

[10] Notably the chapeau of subsection (d) singles out the new Article 8 concepts of "security entitlement" and "securities account" and expressly gives comfort regarding descriptions of "the underlying financial asset" (for example "shares of Acme, Inc. stock"). A leading treatise explains subsection (d)'s predecessor as follows:

background confirms that subsection (d)(1)'s purpose is to permit but not require use of the new nomenclature, and that subsection (d)(2)'s purpose is to uphold secured transactions against questions arising from perhaps technically incorrect but otherwise perfectly serviceable collateral descriptions.

Finally, Section 1-103(a) instructs that the Code must be "liberally construed and applied to promote its underlying purposes and policies," which include "to simplify, clarify, and modernize the law governing commercial transactions."[11] In the case of investment property collateral, a reading of subsection 9-108(d) that enables parties to use the revised Article 8 terminology—yet does not require them to do so—accords with Section 9-108's overall purpose of rejecting technicalities.[12]

In the unreported decision of *Monticello Banking Co. v. Flener (In re Alexander)*,[13] the U.S. Court of Appeals for the Sixth Circuit misunderstood subsection 9-108(d) as imposing a "requirement" limiting the availability of subsection (a). The debtor had maintained a securities account with Monticello and thereby participated in a "CDARS" service designed to allocate, as between the debtor and others, interests in CDs issued by third-party banks. In connection with a loan from Monticello the debtor had signed a security agreement describing the collateral, but without using the particular terms stated in subsection (d)(1) and without describing the underlying

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> Subsection 9-115(3) supplements the general rule in section 9-110 on sufficiency of description. . . . [I]t is not unlikely that parties will describe securities or other investment property by use of ordinary words of colloquial speech, rather than by using the newly defined terms of art used in Articles 8 and 9. The first description rule set out in subsection 9-115(3) is designed to preclude any arguments that a description is inadequate for Article 9 purposes merely because it does not use, or use with exact precision, the newly defined terms. For example, if a debtor owns 1000 shares of Acme, Inc. stock, and holds them through an account with a broker, the precise description of the property in the new UCC jargon would be that the debtor has a "security entitlement to 1000 shares of Acme, Inc. stock." Yet if the debtor seeks to grant a security interest in this holding and does so by means of a security agreement that identifies the collateral as "1000 shares of Acme, Inc. stock," the mere fact that the phrase "security entitlement" was not used would certainly not leave anyone in doubt about the identity of the collateral. Accordingly, subsection 9-115(3) provides that a description may refer to the collateral either by use of the new UCC jargon, or by more familiar terms referring to the underlying asset.

WILLIAM D. HAWKLAND ET AL., UNIFORM COMMERCIAL CODE SERIES § 9-115:11. *See also* James S. Rogers, *Policy Perspectives on Revised UCC Article 8*, 43 UCLA L. REV. 1431, 1451-52 (1996) ("In most discourse about securities transactions, . . . the fact that one's arrangements would be described under Revised Article 8 as 'security entitlements' rather than direct holdings of securities should neither make any difference for purposes of legal analysis nor require any change in documentation.").

[11] In light of this rule, the subsections of Section 9-108 must sometimes be interpreted narrowly and other times broadly, depending on the circumstances. *See* U.C.C. § 1-103 cmt. 1 ("The Uniform Commercial Code should be construed in accordance with its underlying purposes and policies. The text of each section should be read in the light of the purpose and policy of the rule or principle in question, as also of the Uniform Commercial Code as a whole, and the application of the language should be construed narrowly or broadly, as the case may be, in conformity with the purposes and policies involved.").

[12] *See* U.C.C. § 9-108 cmt. 2 ("This section rejects any requirement that a description is insufficient unless it is exact and detailed.").

[13] No. 11-5054, 2011 WL 9961118, 2011 U.S. App. LEXIS 26350 (6th Cir. Dec. 14, 2011). The Court of Appeals decision affirmed the Bankruptcy Court decision, 429 B.R. 876, 2010 Bankr. LEXIS 1705 (Bankr. W.D. Ky. June 4, 2010), on the basis of the reasoning of the District Court decision, No. 10-CV-121, 2010 WL 5158989, 2010 U.S. Dist. LEXIS 132300 (W.D. Ky. Dec. 14, 2010).

financial assets (i.e., the CDs issued by the third-party banks) under subsection (d)(2).[14] The court concluded that this language did not sufficiently describe the collateral and a security interest had therefore not attached. The court reasoned that subsections (a) and (d) were "both unambiguous" and that subsection (a)'s reference to subsection (d) as an exception "*specifically exempts*" the reasonably identify standard when the collateral is investment property. Thus, the court concluded, subsection (d) alone contains "the requirements" for description of a security entitlement.[15] The court conceded that its interpretation of the statute "place[s] technicalities over functionality" and "confuse[s] the customer in a CDARS transaction," but felt that Section 1-103(a) and related policy considerations could be "given no weight" under what the court found to be "unambiguous statutory language."[16] The court thus misconstrued subsection (d) as limiting rather than elaborating on the available methods of describing investment property.

CONCLUSION

The description of collateral in a security agreement seeking to create a security interest in a security entitlement or a securities account is sufficient without satisfying subsection (d), provided that the description "reasonably identifies" the collateral under subsection (a).[17] Properly understood, subsection (d) elaborates on the available methods of describing investment property, while subsections (c) and (e) limit the available methods of describing the collateral to which they apply. Subsection (d)'s language and purpose indicate that the method of describing investment property stated in that subsection satisfies Section 9-108.

AMENDMENT TO OFFICIAL COMMENT

The first sentence of Official Comment 4 to Section 9-108 is hereby amended as follows:

> 4. Investment Property. Under subsection (d)(2), the use of the wrong Article 8 or commodities terminology does not render a description invalid (e.g., a security agreement intended to cover a debtor's "security entitlements" is sufficient if it refers to the debtor's "securities"); nor does subsection (d) require the use of the terms "security entitlement," "securities account," "commodity account," or "investment property" if the collateral description is otherwise sufficient under subsection (a). See PEB Commentary No. 28, dated January 16, 2024. The Commentary is available at https://www.ali.org/peb-ucc.

[14] The collateral description read, in part, that the debtor granted "a security interest in all Debtor's demand, time, savings, passbook or similar accounts maintained at Bank, and at any other bank or financial institution . . . including, but not limited to, those deposit accounts styled and numbered as follows: . . . Assignment of Certificate of Deposit # —2581 at CDARS CD dated September 30, 2005, issued in the amount of $200,907.28, at the rate of 3.85%, maturing on March 30, 2006 . . . ."

[15] The court wrote that "a description of a security entitlement is *only* sufficient if it describes the collateral as a security entitlement or it describes the underlying financial assets." 2010 WL 5158989, at *3, 2010 U.S. Dist. LEXIS 132300, at *9 (emphasis added).

[16] *Id.*, 2010 U.S. Dist. LEXIS 132300, at *8-9 (emphasis in original). Quotations from the decisions in this matter are from the District Court opinion because, as noted above, it furnished the reasoning for the Court of Appeals ruling.

[17] Similar considerations apply to secured transactions involving commodity contracts and commodity accounts.