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ARTICLE 9 COURT CASES OF INTEREST SINCE THE 2010 UCC ARTICLE 9 AMENDMENTS

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UNINTENDED SPACE RENDERS WISCONSIN FINANCING STATEMENT SERIOUSLY MISLEADING

United States SEC v. ISC, Inc., 15-cv-45-jdp; 2017 U.S. Dist. LEXIS 139258 (W.D. Wis. August 30, 2017). The court found that a creditor's inclusion of an extra space before the period in the debtor's legal name of ISC, Inc. rendered its UCC financing statement seriously misleading. The error prevented the financing statement from showing up on a search of the debtor's actual legal name using Wisconsin search logic and the creditor was found to be an unsecured creditor as classified in a receiver's proposed distribution plan.

Double Bubble objected to its classification as an unsecured creditor arguing that it perfected its security interest by filing a UCC financing statement with the Wisconsin Department of Financial Institutions (DFI). The receiver classified Double Bubble as an unsecured creditor because the financing statement did not appear in the DFI records when a search for financing statements using "ISC, Inc." was conducted. Double Bubble had filed a financing statement providing "ISC, Inc ." as the debtor with a space between the final "c" and the "." The inadvertent extra space prevented Double Bubble's financing statement from appearing on a search of the accurate legal name of ISC, Inc.

A financing statement is effective even if it has minor errors or omissions, unless the errors or omissions make the financing statement seriously misleading. § 409.506(1) A financing statement that fails sufficiently to provide the name of the debtor in accordance with § 409.503(1) is seriously misleading. § 409.506(2) However, if a search of the records of the filing office under the debtor's correct name using the office's standard search logic would disclose a financing statement that fails sufficiently to provide the name of the debtor in accordance with § 409.503(1), the name provided does not make the financing statement seriously misleading. § 49.506(3). The court noted that § 49.506(3) creates a safe harbor that will save a financing statement containing an incorrect name if a searcher can find it in the ordinary course of the search. However, given the DFI's search logic, listed in Wis. Admin. Code DFI-CCS § 504(1), the extra space prevented Double Bubble's financing statement from appearing in a search using ISC's correct legal name.

The court noted that the receiver could have found Double Bubble's financing statement if the searcher had used a different search, for example, a search for "ISC" with no punctuation or corporate designation. Double Bubble had contended that such a search would have been "reasonably diligent." However, reasonable diligence is not the current standard. A primary purpose of the revision to UCC was to replace the former reasonableness standard with a clearer and more precise approach based on the computerized search logic of the filing office.

According to the court, "seriously misleading" has a statutorily defined meaning: a search under the debtor's correct name must find the financing statement, otherwise it is seriously misleading. The fact that the DFI provides search tips and hints that might produce a broader set of results does not change the statutory standard. The court overruled Double Bubble's objection and concluded that Double Bubble was to participate in the distribution plan as an unsecured creditor.

DEBTOR'S NAME ON UCC FILING DID NOT MATCH DRIVER'S LICENSE; UCC FILING DEEMED SERIOUSLY MISLEADING

In re: Ronald Markt Nay, Bankruptcy Case No. 16-90762-BHL, Adv. No. 16-59032, 2017 Bankr. LEXIS 472 (Bankr. S.D. Ind. January 23, 2017). The court found that creditor's inadvertent indication of the debtor's name as Ronald Mark Nay without including the "t" in his middle name as listed in his driver's license invalidated creditor's UCC Financing Statements. The filing was seriously misleading since it did not provide the name as indicated on the driver's license and a search of debtor's correct name using standard search logic did not reveal the correct name.

The debtors were indebted to creditor MainSource Bank ("MainSource") pursuant to various debt instruments including a Promissory Note in the original principal amount of $1,200,000 (the "Note"). To secure repayment of the Note, the debtors executed Security Agreements whereby the debtors granted to MainSource a security interest in personal property, including but not limited to, all present or future inventory, equipment ,general intangibles, crops, farm products, livestock, farm equipment, chattel paper, accounts, and all instruments and all proceeds, profits, replacements, and substitutions related thereto. (The "Security Agreements"). The security interests granted to MainSource by virtue of the Security Agreements were properly perfected by the filing of a financing statement on February 4, 2014 with the Indiana Secretary of State.

Creditor, Leaf Capital Funding, LLC ("LEAF") made a loan to debtor Ronald Nay ("Nay") to finance the purchase of a Terex TA400 Dump Wagon (the "TA400"), evidenced by a finance agreement of $41,000, with a corresponding financing statement filed with the Indiana Secretary of State on December 21, 2015. LEAF also made a loan to Nay in the principal amount of $36,950 to finance the purchase of a Terex 3066C Dump Wagon (the "3066C"), evidenced by a finance agreement with the corresponding financing statement filed on December 10, 2015. According to the court, the TA400 and the 3066C constitute "equipment" as that term is defined under applicable Indiana law, IC 26 –1-9.1-102 (a)(33). LEAF claimed that it had a first priority security interest in both pieces of equipment. The LEAF UCCs both identified the debtor's name as "Ronald Mark Nay" while the debtor's actual name indicated on his most recently issued unexpired Indiana driver's license is "Ronald Markt Nay".

On May 13, 2016, Nay and his wife commenced a Chapter 11 bankruptcy case. On September 21, 2016, MainSource filed a complaint requesting a declaration that MainSource had a first priority interest in the TA400 and 3066C and also requested that the court sustain MainSource's objection to LEAF's proof of claim. The court ruled in favor of MainSource.
In considering the validity of the LEAF UCCs, the court first turned to the language in Indiana Code Section 26-1-9.1-506 regarding the effect of errors or omissions on financing statements' validity.

Section 26-1-9.1-506 (a) provides that a financing statement substantially satisfying requirements of IC 26-1-9.1-501 through IC 26-1-9.1-527 is effective, even if it has minor errors or omissions, unless the errors or omissions make the financing statement seriously misleading. Section 26-1-9.1-506 (b) provides that except as otherwise provided in subsection (c), a financing statement that fails sufficiently to provide the name of the debtor in accordance with IC 26-1-9.1-503 (a) is seriously misleading. Section 26-1-9.1-506(c) provides that if a search of the records of the filing office under the debtor's correct name using the filing office's standard search logic, if any, would disclose a financing statement that fails to sufficiently provide the name of the debtor in accordance with IC 26-1-9.1 503 (a), the name provided does not make the financing statement seriously misleading.

The court noted that LEAF's financing statement(s) contained a minor error in the misspelling of the debtor's name. Whether, the defect made the filing seriously misleading was dependent upon section 503(a). According to the court, in 2010, the language of IC 26-1-9.1-503 was extensively modified. The statute, as amended, effective July 1, 2013, now provides that if the debtor is an individual to whom a driver's license has been issued, a financing statement sufficiently provides the name of the debtor only if it provides the name of the individual which is indicated on the driver's license. The court then noted that based upon the plain language of the amended statutory language, the debtor's misspelled name was seriously misleading since it did not provide the name of the debtor as indicated on his Indiana driver's license. The court then noted that the financing statement was fatally defective unless LEAF could establish under the safe harbor provision of 26-1-9.1-506(c), that its financing statement was otherwise discoverable by searching under the debtor's correct name using the standard search logic promulgated by the Indiana Secretary of State.

The court noted that standard search logic is that logic used by a filing office to determine which filings will appear on an official UCC search. The Indiana Secretary of State's standard search logic is located in an Administrative Rule 503. The standard search logic in Rule 503 sets forth how words or things such as spaces, initials, punctuation, case of letters, and similar details are interpreted in generating a report. Administrative Rule 501.1 specifies in part that: a search request must set forth the full correct name of the debtor or the name variant desired to be searched and must specify whether the debtor is an individual or an organization. A search request will be processed using the name in the exact form it is submitted.

The court agreed with MainSource's response that the full correct name is not necessarily the correct name but more importantly, whether the full correct name or some alternate name is permissible in conducting a search. The court accepted MainSource's contention that it is not required because the statute itself provides that the correct name of the debtor is the name stated on his Indiana driver's license. According to the court, in this case, considering the statute's plain language, given its ordinary meaning, and reading section 503 together with section 506, it seemed clear that the only correct name of the debtor under section 503 is the name on his Indiana driver's license, Ronald Markt Nay. Section 506 provides relief to LEAF only inasmuch as a search of the debtor's correct name (as established by section 503), using standardized search logic, would reveal its financing statement. It did not.

The court pointed out that official comments to 26-1-9.1-503 supported its conclusions. Subsection (a) explains what the debtor's name is for financing statement purposes. Uniform Commercial Code Comment 2 to Section 506 provides that for purposes of subsection (c), any name that satisfies Section 9-503(a) at the time of the search is a correct name. This section and Section 9-503 balance the interests of filers and searchers. The Comment further points out that a financing statement is ineffective even if the debtor is known in some contexts by the name provided on the financing statement and even if searchers know or have reason to know that the name provided on the financing statement refers to the debtor.

The court concluded that it was constrained to interpret the statute in a manner consistent with legislative intent, which is to simplify formal requisites and filing requirements. The court found that MainSource was entitled to judgment as a matter of law and granted the Motion for Judgment on the Pleadings. And, finding that LEAF's security interests were unperfected, the court sustained the objection to LEAF's proof of claim.

CHECKING BOTH "TERMINATION" AND "COLLATERAL CHANGE" ON UCC3 AMENDMENT DOES NOT MAKE FILING SERIOUSLY MISLEADING AND DOES NOT TERMINATE FILING

Monroe Bank & Trust v. Chie Contractors, Inc., Docket No. 310226, 2013 Mich. App. LEXIS 674 (Mich. Ct. App. (unpublished) April 16, 2013). The court found that the filing of a UCC3 amendment with two inconsistent boxes selected, the "Termination" box and the "Collateral Change" box did not render the Financing statement "seriously misleading", nor should it be treated as a Termination of the Financing statement. The UCC3 amendment served its central purpose of providing simple notice to third parties of the possible interest of a secured creditor, the plaintiff.

Plaintiff, Monroe Bank & Trust ("Monroe") is a secured creditor of Chie Contractors, Inc. ("CCI"). Blackstone Equipment Financing, L.P. ("Blackstone") is an intervening plaintiff claiming to be a first priority lien holder of certain CCI equipment disputing Monroe's claim to be a first priority lienholder.

On June 14, 1996, Monroe filed a UCC1 financing statement perfecting its security interest in CCI's property, and described the collateral as "All Assets, All Accounts, Equipment Vehicles, Inventory Furniture, Documents, Chattel Paper, Instruments, and General Intangibles, including any right to any refund of taxes, whether now or hereafter owned, existing or acquired, including but not limited to accounts receivable." On March 7, 2001, the plaintiff filed a UCC3 continuation indicating that the financing statement was still in effect.

On April 29, 2005, plaintiff filed a UCC3 amendment to the financing statement. The court noted that pursuant to MCL 440.9512, a financing statement can be amended so as to delete the collateral covered by the initial financing statement or to terminate the effectiveness of the financing statement. In this case, plaintiff's financing statement amendment purported to do both; section two of the UCC3 relating to Termination and section eight relating to Collateral Change, Deletion were each separately selected on the same filing. The specific collateral deleted was noted to be a "1987 Dyna Pack CA25PD Roller." The court rejected Blackstone's argument that the UCC3 amendment constituted a termination since it was evident there may have been an error made given that two separate boxes were selected.

According to the court, a filed financing statement "serves as notice to the world that a secured party of record may have a secured interest in the collateral described, and invites further inquiry to disclose the complete state of affairs." The financing statement's purpose is to alert third parties to the need for further investigation, not to provide the details of security arrangements. MCL 440.9506(1) provides "A financing statement substantially satisfying the requirements of this part is effective, even if it has minor errors or omissions, unless the errors or omissions make the Financing statement seriously misleading." A financing statement is considered seriously misleading then, if it fails to serve its central purpose of providing notice to third parties of the possible interest of the secured creditor, which would lead interested parties to inquire further to get the full picture, the court noted.

The court found that the amended financing statement was not seriously misleading even though both boxes corresponding to Termination and Collateral Change Deletion were selected, plus, a specific piece of equipment was identified for the collateral deletion. Thus, any interested party should have realized that further investigation was required to ascertain plaintiff's actual effective security interest. The error was plainly apparent on the face of the financing statement. And because of the apparent contradictory nature of the amendment types selected, the financing statement provided notice to an interested party that

further inquiry was required. In addition, the court also rejected Blackstone's arguments that MCL 440.9513(4) applied under the facts of the case. MCL 440.9513 (4) provides that "upon the filing of a Termination Statement with the filing office, the Financing statement to which the termination statement relates ceases to be effective." According to the court, because the filing erroneously indicated that it was both a Collateral Change Amendment and a Termination, it was not merely a Termination within the contemplation of MCL 440.9513(4).

USE OF PLAIN PAPER ATTACHMENT TO LIST ADDITIONAL DEBTORS RENDERS FINANCING STATEMENTS SERIOUSLY MISLEADING

In re: Camtech Precision Manufacturing, Inc., Case No. : 10-22760-BKC-PGH (Jointly Administered) , Ch. 11, Adv. No.: 10-3479-BKC-PGH-A (Bankr. S.D. Fla., January 31. 2011), the court awarded plaintiff's motion for summary judgment against creditor finding that creditor failed to properly perfect its security interests in additional debtors' assets when it filed only a plain paper attachment to UCC filings listing the additional debtors and did not use the approved UCC1Ad (Addendum) or UCC1AP (Additional Party) form.

Creditor Regions Bank ("Regions") filed a series of UCC-1 financing statements with the Florida Secured Transactions Registry (the " Florida UCCs"), and with the state of New York (the "New York UCCs"). The second page of each of the Florida and NY UCCs was a plain paper attachment which stated that debtors Camtech Precision Manufacturing, Inc. ("Camtech") and Avstar Fuel Systems, Inc. ("Avstar Fuel") were additional debtors. Regions did not use the approved UCC1Ad (Addendum) form or the UCC1AP (Additional Party) form approved by each state to list Camtech and Avstar Fuel as additional debtors. There was no direction in the additional debtor box on the first page of each UCC to look at the attachment listing additional debtors.

Camtech and Avstar Fuel subsequently filed for bankruptcy. The Official Committee of Unsecured Creditors ("Plaintiff" or "Committee") filed a motion for summary judgment against Regions seeking to render Regions as an unsecured creditor and seeking disgorgement of adequate protection payments made to Regions in respect of the liens asserted against the assets of Camtech and Avstar Fuel.

The plaintiff argued that the subject UCCs were seriously misleading and ineffective to perfect Regions' asserted security interest based upon the undisputed fact that the prescribed searches of New York and Florida records failed to disclose a financing statement naming Regions as a secured creditor of Camtech or Avstar Fuel. The court agreed. It found that although Regions' UCCs contained the statutorily required information and the correct names of the debtors, the manner in which the information was provided for Camtech and Avstar Fuel made the UCCs seriously misleading as to these additional debtors.

According to the court, both New York and Florida have approved standard national and/or state forms for listing additional debtors.

The court pointed out that the New York UCCs, having neither used the approved additional party form, nor having contained any direction to look beyond the first page of the UCC-1 for additional debtor information, were seriously misleading with respect to additional debtors, Avstar Fuel and Camtech. Florida also expects filers to use the approved forms which were designed to reduce errors, the court said. It pointed out that the Florida Secured Transaction Registry's website states that it *"will accept and process other forms as Unapproved Forms only if the forms contain the same fields as the most recent corresponding... Additional Party Forms approved by the Florida Secretary of State."* The court found that Regions' unapproved attachment did not contain any "fields" corresponding to the most recent additional party form, nor did it contain any additional debtor

"boxes" in which to list the names of the additional debtors. Listing the additional debtors' names elsewhere on an unapproved attachment is irrelevant, the court said. The court also rejected Regions' argument that its UCCs were properly filed, but that both the New York and Florida filing offices mis-indexed them. *"This is not a case in which the error of the filing officer accounts for the financing statement not having been indexed as to the additional debtors. This is a case in which the filer's error in using an unreferenced and unapproved form caused the financing statements to be seriously misleading and ineffective,"* the court concluded.

UPDATE: MARCH 30, 2012

In re: Camtech Precision Manufacturing, Inc., Case No. 11-80419-CIV-MARRA, 2012 U.S. Dist. LEXIS 44579 (S.D. Fla. March 30, 2012). The United States District Court for the Southern District Court of Florida reversed the Bankruptcy Court's decision awarding the Committee summary judgment against Regions. Reviewing the order de novo, the District Court agreed with Regions' assertions that the Bankruptcy Court erred by (1) holding the liens in question were not perfected and by (2) disregarding genuine issues of material fact as to whether the Florida and New York filing offices made indexing errors. The District Court first examined New York and Florida codified versions of Section 9-521 of the UCC. It noted that although both states, by statute, empower their Secretary of State to create approved forms and New York articulates express protections to those that use such a form, neither state requires filers to use any particular form. The District Court then examined what each state did require of a party seeking to file a financing statement, reviewing New York and Florida statutes. It found that the Committee failed to set forth any evidence that would establish that the financing statements in question did not contain sufficient information to match Florida and New York statutory requirements. The District Court then proceeded on the assumption that Regions filed legally sufficient financing statements as defined by New York and Florida law.

The District Court then found the issue to be whether a financing statement is seriously misleading as a matter of law under circumstances where the results of a search of the filing office's records does not disclose a filing statement which is related to the debtor. The District Court noted that under a reading of UCC section 9-506(c) by the Bankruptcy Court, a correct and properly completed, but misfiled statement would be legally ineffective if a search of the records did not disclose the financing statement, even if the misfiling was not attributable to the filer. The District Court stated that this reading of section 9-517, nullifies section 679.517, Florida Statutes, and New York U.C.C. section 9-517, both of which provide that the failure of the filing office to index a record correctly does not affect the effectiveness of the filed record. The District Court also found that its interpretation of those statutes was also supported by Official Comment 2 to both of the statutes concerning effectiveness of mis-indexed records. The Comment provides that the filing office's error in mis-indexing a record does not render ineffective an otherwise effective record. As did former section 9-401, this section imposes the risk of filing-office error on the searcher of the files rather than on the filer. (Both the Florida and New York codification of UCC section 9-517 are identical, both in the text and in the comments, according to the District Court.)

The District Court pointed out that the Committee has not presented any evidence to overcome or defeat Regions affirmative defense of a filing or indexing error by the respective filing offices of New York and Florida. Also, there was no record evidence that the financing statements were considered by the filing offices to be defective, erroneous, or seriously misleading.

The District Court pointed out that the Bankruptcy Court concluded, as a matter of law that failure to use approved forms and the failure to list the debtor in a debtor box on the form used rendered the filing seriously misleading. The District Court concluded that such a finding was a question of fact which could not be determined as a matter of law on the record. The Bankruptcy Court had also resolved other factual questions in favor of the moving party despite the lack of any record

evidence to support the findings. For example, the Bankruptcy Court concluded that had the additional debtor information been submitted using an approved standard form.....or had there been a direction in the additional debtor box on the first page of the UCC form to look at the attachment for additional information, the result would be different. This was a factual finding which refuted Regions indexing error affirmative defense. The Committee, which was the moving party, never presented evidence to overcome the defense, and there is no record evidence to support the Bankruptcy Court's finding. Because the Bankruptcy Court erroneously granted summary judgment despite the existence of genuine questions of material fact, the District Court reversed and remanded the Bankruptcy Court's order.

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