

Post 2010 Amendments, Article 9 of the Uniform Commercial Code is Popping Up in Courts

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Abstract

This article focuses on avoidable errors that eliminate a creditor's security, and why it is imperative that you comply with the requirements under Article 9. Compliance is rewarded, and creditors have prevailed when their security interests have been perfected.

Article 9 of the Uniform Commercial Code (UCC) governs secured transactions in personal property. In the last twenty years, there have been two major revisions to Article 9, with the most recent being the 2010 Amendments.

July 1, 2013. *A day that will live in infamy!* That is if you are familiar with Article 9 of the UCC, as this is the date the 2010 Amendments went into effect. One of the key changes in the 2010 Amendments provided clarity for properly identifying the debtor on the UCC Financing Statement.

In compliance with § 9-503(a), when the debtor is a registered organization, creditors should rely on the information found on the public organic record.

If the debtor is an individual, creditors must first look to the state's legislation. With the 2010 Amendments, each state had to decide whether they would implement "Alternative A" or "Alternative B."

Alternative A: if the debtor holds an unexpired driver’s license, the Financing Statement must list the debtor’s name as it appears on the unexpired driver’s license. (*If* the debtor does not have a driver’s license, the Financing Statement should list the “individual name” of the debtor or the debtor’s surname and first personal name.)

Alternative B: the debtor’s driver’s license name, the debtor’s actual name or the debtor’s surname and first personal name may be used on the Financing Statement.

It comes as no surprise that as we near the 5-year anniversary of the implementation of the 2010 Amendments, we are beginning to see cases where courts were called on to determine whether a security interest had been properly perfected. In this article, we will review a few recent cases that addressed issues such as seriously misleading Financing Statements, compliance with Article § 9-503, a case relative to the right of repossession and, finally, a case on a properly perfected security interest with a liquor license.

Creditor Left Without a “valid, enforceable, properly-perfected, unavoidable prepetition lien”

Filing a UCC to Perfect Your Security Interest? No Security Exists if the Debtor’s Name is Wrong

In a fight for priority, a creditor claimed “...[T]hey have ‘valid, enforceable, properly-perfected, unavoidable prepetition liens...’” which is senior to the bank’s UCC for debtor-in-possession (DIP) financing.

Unfortunately, the creditor did not have a ‘valid, enforceable, properly-perfected, unavoidable prepetition lien’ because the creditor failed to list the debtor’s name on the Financing Statement as the name appeared on the public organic record.

The Case: Fishback Nursery, Inc. v. PNC Bank, NA, Dist. Court, ND Texas 2017

The debtor, BFN Operations LLC (BFN) also known as Zelenka Farms, filed for bankruptcy protection. PNC Bank NA (PNC) had a security interest in substantially all of BFN’s assets and PNC perfected its security interest by filing a UCC. Fishback Nursery Inc. and Surface Nursery Inc. (collectively “Nurseries”) furnished various agricultural products to BFN, and Nurseries also filed UCCs.

Nurseries filed three UCCs, one in each state where they sold products to BFN: Oregon, Michigan & Tennessee. On all three UCCs, Nurseries identified BFN as “BFN Operations, LLC abn Zelenka Farms.” Unfortunately for Nurseries, the addition of “abn Zelenka Farms” rendered their security interests unperfected. BFN’s name, in the public organic record, is “BFN Operations, LLC” and does not include “abn Zelenka Farms.

Not Saved by the Savings Clause

According to the court opinion, Michigan & Tennessee both offer a “savings clause.” The Michigan “savings clause” can be found under MCL 440.9506(3):

“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 sufficiently to provide the name of the debtor in accordance with section 9503(1), the name provided does not make the financing statement seriously misleading.”

Here’s an example of a search in Michigan. PNC would have processed a UCC search by the entity’s correct name, “BFN Operations, LLC” - that search would provide the following results:

Debtor Name Quick Search Instructions

Debtor Quick Search Search Results

Debtor Quick Search Result

File Number	Lien Type	Debtor Name	Filing Date	Lapse Date	Status
2012040340-5	UCC Lien	BFN Operations, LLC	03/15/2012	03/15/2022	Active
2012111890-6	UCC Lien	BFN Operations, LLC	08/02/2012	08/02/2017	Lapsed
2015074345-1	UCC Lien	BFN Operations, LLC	05/27/2015	05/27/2020	Active
2016028170-6	UCC Lien	BFN Operations, LLC	03/02/2016	03/02/2021	Active

A search for the name Nurseries used on their UCCs, “BFN Operations, LLC abn Zelenka Farms” provides these results:

Debtor Name Quick Search Instructions

Debtor Quick Search Search Results

Debtor Quick Search Result

File Number	Lien Type	Debtor Name	Filing Date	Lapse Date	Status
2016087017-3	UCC Lien	BFN Operations, LLC abn Zelenka Farms	06/21/2016	06/21/2021	Active
2016094307-7	UCC Lien	BFN Operations, LLC abn Zelenka Farms	07/05/2016	07/05/2021	Active

If you look closely, you will see the File Numbers in both images are different; 6 different UCCs. The search run by PNC, on the debtor’s correct name, does not reveal the filings by Nurseries; Nurseries’ UCCs would only appear in a search of “BFN Operations, LLC abn Zelenka Farms.”

Some may argue that Nurseries’ UCCs should have appeared, because the debtor’s name begins with “BFN Operations, LLC” but as you can see, a UCC search does not operate as a keyword search. If it were a keyword search, it would pick up any/all variations of the entity’s name.

Seriously Misleading, Security Interest Unperfected

Because the UCCs did not comply with Article 9, Nurseries' security interest was unperfected. Obviously, with an unperfected security interest comes the "parting prize" of unsecured creditor status. PNC properly perfected its security interest; thus, PNC is a secured creditor and its UCC takes priority.

Uncharted Territory under UCC Article 9

Georgia Bankruptcy Court Asks: "Is the Difference between the Names "Kenneth Pierce" and "Kenneth Ray Pierce" a Minor Error, or is it Seriously Misleading?"

As mentioned above, if you are filing a UCC on an individual, to comply with Article § 9-503(a) the Financing Statement ***must*** list the debtor's name as it appears on the debtor's unexpired driver's license.

But what happens if the printed name on the driver's license is different than the individual's signature on the driver's license? *Technically*, both names (the printed & signed) appear on the license - which is correct?

This is uncharted territory under UCC Article 9. Until now, no one has questioned whether the name shown in the signature or the printed name on the driver's license should appear on the Financing Statement.

Of course, we've encountered cases where the name on the Financing Statement and driver's license don't match, but these differences are typically due to spelling errors. Errors such as a misspelled last name: the name on the driver's license is "Susan Walker" vs. the name on the Financing Statement is "Susan Wakler".

But an argument that compliance with Article § 9-503 is achieved when using the driver's license signature vs. the printed name certainly adds a new layer of complexity.

In a recent bankruptcy case, one Georgia court determined the printed name on the unexpired driver's license is the name that should appear on the UCC Financing Statement, leaving one creditor's security interest unperfected.

The Case - Bank Lends Money, Debtor Files for Bankruptcy Protection

In 2015, Kenneth R. Pierce (Pierce) obtained an \$18,000 loan from Farm Bureau Bank (Bank) and the proceeds of the loan were used to purchase farming equipment, a fertilizer spreader. Bank and Pierce executed a security agreement and Bank filed a UCC to perfect its security interest.

In 2017, Pierce filed for Chapter 12 bankruptcy protection. Subsequently, Bank timely filed a proof of claim for the balance owed of \$14,459.81 and attached a copy of their UCC-1 to the proof of claim.

On the UCC filing, Bank identified Pierce as “Kenneth Pierce,” however, Pierce’s name on his unexpired driver’s license was “Kenneth Ray Pierce.” Pierce filed an objection with the Bankruptcy Court, claiming Bank’s security interest was unperfected, because Bank incorrectly identified Pierce on the UCC filing.

Technically Two Names Appear on the Individual’s Driver’s License

Technically two names appear on Pierce’s driver’s license, at least that is Bank’s primary argument. The printed name on his driver’s license is “Kenneth Ray Pierce” though Pierce’s signature reads “Kenneth Pierce.” Bank argued that Article § 9-503(a) doesn’t specify whether the identifying name must be the name that is typed on the driver’s license.

“But as Farm Bureau Bank points out, there are *two names* "indicated on the driver's license": "Kenneth Ray Pierce" (typed) and "Kenneth Pierce" (signed). Farm Bureau Bank argues that O.C.G.A. § 11-9-503(a)(4) is not limited to the name typed on the driver's license, but rather that it *includes* the name signed by the Debtor, and thus its Financing Statement *does* provide the (signed) name of the Debtor.”

Georgia is an Alternative A state, and in the plain text of the law, Bank isn’t necessarily wrong; it does not specify whether the printed name or signed name is the name to be listed on the Financing Statement:

§ 9-503. NAME OF DEBTOR AND SECURED PARTY.

(a) [Sufficiency of debtor's name.]

[Alternative A]

(4) subject to subsection (g), if the debtor is an individual to whom this State has issued a [driver’s license] that has not expired, only if the financing statement provides the name of the individual which is indicated on the [driver’s license];

(5) if the debtor is an individual to whom paragraph (4) does not apply, only if the financing statement provides the individual name of the debtor or the surname and first personal name of the debtor;

Thus, it becomes the Court’s duty to determine whether the error on the Financing Statement is seriously misleading, or if Bank’s security interest is perfected because it substantially complied with the law.

Webster's Dictionary, Case Law & Basic Compliance with the Law

Courts weigh a variety of factors when deciding a case, often relying on previous legal decisions for guidance, the “plain language of the law,” and even Webster’s dictionary.

The Court thought perhaps the answer would lie within the definition of “indicate” as it appears in “indicated on the driver’s license.”

“Turning to Webster's Third New International Dictionary 1150 (1981) the following are among the definitions provided for the word "indicate": "to point out or point to or toward with more or less exactness," to "show or make known with a fair degree of certainty," and to "reveal in a fairly clear way." These definitions do not help the Court determine which of two names is "indicated" on the Debtor's driver's license. Indeed, the presence of two different names on the driver's license is precisely the opposite of “exactness, certainty, and clarity.”

I now understand the saying “clear as mud.”

The Court also reviewed various Georgia cases. Unfortunately, most of the cases did not address the exact issue in this case. The Court then turned to other jurisdictions’ case law, and one Nebraska bankruptcy case shed *some* light, though the case was decided prior to the 2010 Amendments and does not wholly apply to the case at hand.

“In *Genoa Nat'l Bank v. Southwest Implement, Inc. (In re Borden)*, the debtor was identified by his legal name "Michael Ray Borden" or by "Michael R. Borden" on his driver's license and on other legal documents. 353 B.R. 886, 887-88 (Bankr. D. Neb. 2006). However, the debtor often signed legal documents by his nickname, "Mike Borden." *Id.* The court held that financing statements identifying the debtor as "Mike Borden" were seriously misleading. *Id.* at 892. *In re Borden* suggests that the name typed on legal documents trumps the name signed by the debtor.”

What about Standard Search Logic?

The second argument Bank lodged was that the UCC would appear in a search based on Georgia’s standard search logic. But, under that argument, the search would have been done using Pierce’s name on his driver’s license - “Kenneth Ray Pierce.” And, a search for “Kenneth Ray Pierce” would not have uncovered the filing for “Kenneth Pierce.”

As an aside, a search of Georgia’s UCC Index can be done with a partial name. Yes, Bank should have searched by the individual’s name as it appears on the driver’s license, however, a partial search of “Pierce, KE” revealed the UCC:

SEARCH UCC Index > Basic Name Search Fullscreen View Back

BASIC NAME SEARCH
 Name searched: **PIERCE KE**
 County searched: entire state
 Search Type: **individual**
 Query made: 2/12/2018 10:27:03 AM

Table Display Type: 1 Line ?
 12 Records Found Page 1 of 2
[Next >](#)
[Last >>](#)

Display: 10 results per page.

Select	File Number	Document Type*	Secured Party	Date Filed	Original File Number
<input type="checkbox"/>	Debtor: PIERCE, KENNETH				
<input type="checkbox"/>	007-2015-019950	Original	FARM BUREAU BANK FSB	6/23/2015 8:42:00 AM	N/A
<input type="checkbox"/>	044-2016-004790	Termination	DLL FINANCE LLC	10/20/2016 4:01:00 PM	044-2013-004468
<input type="checkbox"/>	048-2013-000109	Original	REPUBLIC FINANCE, LLC	1/22/2013 3:00:00 PM	N/A
<input type="checkbox"/>	059-1997-001081	Original	1ST FRANKLIN FINANCIAL	8/20/1997 9:00:00 AM	N/A
<input type="checkbox"/>	059-2000-001210	Termination	1ST FRANKLIN FINANCIAL	12/15/2000 9:00:00 AM	059-1997-001081
<input type="checkbox"/>	114-2007-000537	Original	UNITED BANK	11/16/2007 8:58:00 AM	N/A
<input type="checkbox"/>	124-2003-000586	Original	BANK OF NEWINGTON	9/12/2003 9:00:00 AM	N/A
<input type="checkbox"/>	124-2011-000299	Original	AGRICREDIT ACCEPTANCE LLC	7/15/2011 10:30:00 AM	N/A
<input type="checkbox"/>	124-2011-000368	Original	IRRIGATION FINANCE SOLUTIONS, LLC	8/22/2011 2:30:00 PM	N/A
<input type="checkbox"/>	124-2013-000484	Continuation	BANK OF NEWINGTON	7/12/2013 4:30:00 PM	124-2008-000614

* Instruments with multiple secured parties are repeated for each secured party. Assignees are designated with an asterisk(*)

Seriously Misleading, Unsecured Status

On its Financing Statement, Bank failed to identify its debtor in compliance with § 9-503. Failing to correctly identify its debtor meant the UCC filing would not be uncovered in a search. The Court declared Bank’s UCC as seriously misleading, bumping Bank to unsecured creditor status.

Alternative A in Action

The Debtor’s Name as it Appears on the Unexpired Driver’s License -- Even if it’s Incorrect

In a recent court decision, one creditor’s security interest was eliminated because they spelled the individual debtor’s name *correctly*. Yes, I said “correctly.” Because, in this case, “correctly” and “as the name appears on the driver’s license in compliance with § 9-503(a)” resulted in two different spellings of the debtor’s name.

Case Background

In 2014 and 2015, MainSource Bank (MainSource) entered into two different loan agreements with the debtor (specific to this case is debtor Ronald Nay). With each loan agreement, there was a signed security agreement and MainSource filed the appropriate UCC Financing Statements to perfect their security interest.

At the end of 2015, LEAF Capital Funding, LLC (LEAF), executed an agreement with one of the debtors, Ronald Nay, for the purchase of two pieces of equipment. With the finance agreement, LEAF also obtained a signed security agreement and subsequently filed a UCC Financing Statement to perfect their security interest.

In May 2016, the Nays filed for bankruptcy protection. As a *presumed* secured creditor, LEAF filed their proof of claim in September 2016, and soon after, MainSource filed a complaint arguing that LEAF did not have a perfected security interest.

The court agreed with MainSource, leaving LEAF with an unperfected security interest.

The Difference Between Two Financing Statements

MainSource's UCC identifies the debtor as "**Ronald Markt Nay**" (emphasis added) which is not how Ronald spells his middle name; it is, however, the way Ronald's name appears on his driver's license.

DEBTOR'S EXACT FULL LEGAL NAME			
INDIVIDUAL'S SURNAME	FIRST PERSONAL NAME	ADDITIONAL NAME(S)/INITIAL(S)	SUFFIX
NAY	RONALD	MARKT	

LEAF's UCC identifies the debtor as "**Ronald Mark Nay**" (emphasis added) which is the correct spelling of Ronald's middle name, but not the spelling as it appears on his driver's license.

DEBTOR'S EXACT FULL LEGAL NAME			
INDIVIDUAL'S SURNAME	FIRST PERSONAL NAME	ADDITIONAL NAME(S)/INITIAL(S)	SUFFIX
NAY	RONALD	MARK	

Why is LEAF's UCC unperfected? After all, LEAF *correctly* spelled Ronald Nay's middle name!

Because, to be compliant with Alternative A under § 9-503(a), the debtor's name must appear on the UCC Financing Statement exactly as it appears on the unexpired driver's license.

Seriously Misleading or Minor Error

In its decision, the court admitted the spelling error on LEAF's UCC was minor, and per Indiana Code § 26-1-9.1-506(a) "A financing statement substantially satisfying the requirements...is

effective, even if it has minor errors or omissions, unless the errors or omissions make the financing statement seriously misleading.”

But, per code § 26-1-9.1-506(b), “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.” So, we must circle back to IC 26-1-9.1-503(a), which is Alternative A, and is, in fact, the technicality that invalidated LEAF’s security interest.

“§ 26-1-9.1-503(a)(4) ... if the debtor is an individual to whom this state has issued a driver's license or an identification card for nondrivers under IC 9-24-16 that has not expired, only if the financing statement provides the name of the individual which is indicated on the driver's license or identification card.”

The Court

A UCC is considered seriously misleading, thus invalid, if a search of the debtor’s name does not reveal the UCC. The court held that LEAF’s UCC would not have been uncovered via a search using standard search logic.

“In this case, considering the plain language of the statute, given its ordinary meaning, and reading section 503 together with section 506, it seems 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 in as much as a search of the debtor’s “correct” name (as established by section 503), using standardized search logic, would reveal its financing statement. It does not.”

Can a Properly Perfected UCC Really Give Me the Right to Repossess?

Yes, a properly perfected security interest and proof of debtor default may afford you the right to repossess the collateral.

In CNH Industrial Capital, America, LLC v. T & P Farms, LLC, Dist. Court, ND Mississippi 2017, the court granted the Secured Party the right to repossess its equipment because it had 1) proven the debtor defaulted on the contract, and 2) properly perfected a security interest through UCC Financing Statements.

Background: The Contract, The UCC-1s & The Replevin

In 2015, the debtor, T & P Farms, LLC (T & P) purchased over \$1M in farming equipment from Medlin Equipment Company of Mississippi County (Medlin).

According to the court opinion, there were 4 pieces of equipment sold, and each sale was “...evidenced by a Retail Installment Sale Contract and Security Agreement.” (3 of the 4 sales

were addressed in the replevin action.) A replevin action seeks the return of the actual product as opposed to money damages.

Included in the contract, aside from the security language and terms of the sale, was a clause regarding debtor default: “the seller has the right to ‘take possession of all Collateral, without notice or hearing...’” and Medlin assigned its interest in the equipment to CNH Industrial Capital America, LLC (CNH). Subsequently, a PMSI filing was properly perfected, by CNH, for each sale/contract.

By the end of 2016, the debtor had stopped making the agreed upon monthly payments, and in May 2017, CNH filed a replevin action.

The Secured Party Prevailed

When a replevin action is filed, the party filing the action needs to prove their right to repossess the collateral. In this case, the Secured Party filed the action, then the Secured Party proved its properly perfected security interest, as well as the default of its debtor.

“A plaintiff in a replevin action establishes the right to immediate possession by demonstrating a default on a purchase contract and a perfected security interest in the collateral.”

The debtor is afforded an opportunity to defend against the repossession. The debtor asked the court to consider equitable defense (*a defense based on fairness, not law*), based on the debtor’s need for the equipment to maintain his business and support his family. The debtor further added he should not have to pay for the equipment because the equipment was faulty. Unfortunately, the debtor’s defense wasn’t persuasive enough.

“While a rule of equity may play some role in this determination, such as where a party claims an equitable lien in the subject of the action, T & P has not cited, and this Court has not found, any authority which supports the proposition that a possessory interest in collateral may be equitably created by either the condition of collateral unrelated to the existence of a default or the need for continued possession.”

CNH properly perfected its security interest and successfully established the debtor’s default, therefore, the court granted CNH the right to repossess the equipment.

Security Interests in Liquor Licenses OK in Pennsylvania

Yes, Creditors Can Take a Secured Interest in a Debtor's Liquor License in Pennsylvania, According to One Recent Bankruptcy Court Decision.

The Case

In 2014, M&T Bank (M&T) loaned B&M Hospitality (B&M) \$85,000. In consideration of the loan, M&T executed a Security Agreement and filed a UCC-1, identifying the collateral as B&M's liquor license.

In 2017, B&M filed for bankruptcy protection under Chapter 7 and, subsequently, a Bankruptcy Trustee (Trustee) was assigned to the case.

In bankruptcy proceedings, the essential role of the Trustee is to take charge of the debtor's estate. Some responsibilities include managing the liquidation of the debtor's assets and ensuring proper distribution of the proceeds to the various creditors.

In this case, the Trustee filed a motion to liquidate B&M's assets and the Trustee stated there were no liens on the liquor license. As you can imagine, M&T piped up and provided proof of its security interest in B&M's liquor license.

Eventually, the Trustee and M&T agreed the liquor license would be sold for \$175,000. However, until the court confirmed whether M&T's security interest was valid, the Trustee would escrow the amount owed to M&T (\$55,166.54) from the proceeds of the sale.

Arguments Before the Court: Can a Security Interest in a Liquor License Exist?

The two primary questions brought before the court were whether Pennsylvania law permitted the granting of a security interest in a liquor license and whether M&T properly perfected its security interest.

First, can a liquor license be collateral for a security interest?

The Trustee believed no security interest exists, because prior to the 1987 amendments, the Pennsylvania Liquor Code provided "...that liquor licenses constitute a privilege and not property."

Unfortunately for the Trustee's argument, in 1987 there was an amendment to the Pennsylvania Liquor Code, which defined a liquor license as "property between third parties and the licensee." This amendment has not changed, and the Liquor Code still identifies a liquor license as property.

"The plain language of the 1987 amendment characterizes a liquor license as property between a licensee and a third party and as a privilege between a licensee and the Board. 47 P.S. § 4-468(d)... based solely upon the text of the 1987 amendment, the Court concludes that, as between a licensee

and a third party, a liquor license constitutes property under Pennsylvania law.”

And, as we know, UCCs are all about perfecting a security interest in personal property!

Second, is a security interest valid if the collateral description on the Financing Statement is different than the collateral description on the Security Agreement?

Next the Trustee argued that M&T failed to properly perfect its security interest because M&T didn’t specifically call out the liquor license in the collateral description on the UCC Financing Statement. Although, M&T did call out the liquor license in its Security Agreement.

Let’s look at the collateral descriptions on the UCC and the Security Agreement:

UCC Financing Statement

“all assets of the debtor, whether now existing or hereafter acquired or arising, wherever located”

Executed Security Agreement

"general intangibles limited to that certain restaurant liquor license number R-1140 issued by the Pennsylvania Liquor Control Board" and "all proceeds of collateral of every kind and nature in whatever form, including, without limitation, both cash and noncash proceeds resulting or arising from the sale or other disposition by the Borrower of the collateral."

Does the collateral description, in either document, meet the three keys? The judge reviewed the case against these three requirements:

- (1) value has been given,
- (2) the debtor has rights in the collateral or the power to transfer rights in the collateral to a secured party, and
- (3) the debtor has authenticated a security agreement which provides a description of the collateral

Has value been given? Yes! Does the debtor have rights to the collateral? According to PA law, yes! Does the Security Agreement identify the collateral? Indeed, it does!

The Court Says: Drink Up!

M&T took the proper steps and perfected its security interest, and the court determined M&T should be paid with the proceeds of the sale of the debtor’s assets.

“Ultimately, Pennsylvania law clearly allows third parties to create security interests in Liquor Licenses. M&T followed all the requirements to create and perfect a lien on the Liquor License and is entitled to proceeds from its sale in the amount of its secured claim.”

Parting Thoughts

Use caution when identifying your customer on the UCC filing, whether it is an organization or an individual. If your debtor is an organization, use the name as it appears on the public organic record. If it's an individual, carefully list their name exactly as it appears on their unexpired driver's license.

We see issues like this time & time again - **avoidable** errors that eliminate a creditor's security. It is imperative to comply with the requirements under Article 9. Compliance is rewarded! It's refreshing to see creditors prevail when they have properly perfected a security interest.

Kristin Alford, NCS Education and Marketing Specialist, assists credit professionals throughout the U.S. and Canada to secure their receivables through the mechanic's lien and bond claim process. NCS is an industry leader in collections, mechanic's lien laws and UCC filings. NCS offers proactive solutions to minimize credit risk and improve profitability.