Secured Claim Issues:
How Lenders and Their Lawyers Make Work for Litigators and Bankruptcy Lawyers; Developments Involving Commercial and Consumer Creditors

Concurrent Session

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Secured Claim Issues:
How Lenders and Their Lawyers Make Work for Litigators and Bankruptcy Lawyers; Developments Involving Commercial and Consumer Creditors

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A Dozen Questions to Which Transaction Lawyers Should Know the Answers Before They Create More Work for Bankruptcy Trustees[1]

In recent years, commercial transactions, particularly those applying the new rules contained in the 2001 revision of Article 9, have been tested under fire. A pattern of problems may be emerging and, while the following is not a comprehensive list of questions or cases, it is a survey of some of the most significant issues arising in recent cases.

1. Do I still need to check a security agreement and a financing statement to be sure that they both cover all the same things?

A financing statement, more limited in scope than the security agreement that it perfects, limits the collateral in which the creditor has a perfected interest to that described in the financing statement as against third-party creditors and a trustee in bankruptcy. Thus, in *In re The Holladay House*, 2008 WL 714144 (Bankr. E.D. Va. 2008), a bankruptcy court applied Virginia law to rule that a consignor's security interest was perfected only to the extent that it attached to inventory that the consignor delivered to a retail furniture business pursuant to the terms of a consignment and security agreement.

2. How do I need to describe the transaction in the security agreement?

Include language granting a security interest.

In a case involving an assignment of rights by a bank that had issued a letter of credit, the bankruptcy court administering the estate of the applicant for that letter of credit concluded that the issuer bank did not have a security interest in the debtor's assets because there was not document granting a security interest to the issuing bank and therefore nothing to assign to the creditor. *In re Covenant at Southhills, Inc.*, 410 B.R. 426 (Bankr. W.D. Pa. 2009). An intercreditor agreement provided that "the Bank and the Trustee shall both have a first lien on and security interest in the Shared Collateral," and the debtor signed that intercreditor agreement and agreed to be bound by its terms, but the court concluded that the agreement did not actually grant a security interest.

In a similar case, a creditor attempted to track through several documents that accompanied a signed security agreement, including an unsigned loan receipt describing the intended collateral and providing that by endorsing the loan check, the borrower agreed to have the described property secure the loan. *In re Stearns*, 2009 WL 4330832 (Bankr. N.D.N.Y. 2009). However, the court concluded that this was not sufficient to act as a security agreement without clear evidence that the debtor had negotiated the check with knowledge of the language printed on the receipt or that the actions of the parties verified the required "present intent" necessary to authenticate the grant of a security interest.

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[1] Thanks to my friends Kathi Allen and John Murdock for digging out several of the Article 9 cases discussed in these first sections, in preparation for their excellent presentation to the Mid-South Commercial Law Institute in December, 2010.

Describe collateral carefully - Exchanges of cash for licenses did not generate "accounts"

Transactions by which customers of an amusement facility paid cash for licenses to use the facility's miniature golf course did not generate "accounts" for purposes of Article 9, held the court, applying Indiana law, in *In re Wright Group, Inc.*, 2011 WL 570019 (Bankr. N.D. Ind. 2011). Accordingly, the cash was not the proceeds of collateral in which the creditor of the bankrupt facility operator had a perfected security interest. The exchanges of cash for licenses were simultaneous transactions, with no customer being allowed to use the course without paying the fee, and the cash was "money" under Article 9, in which a security interest could only be perfected by possession. The creditor did not have possession of any of the receipts from the miniature golf course when the bankruptcy petition was filed.

Describe collateral carefully - After-acquired assets not included in security interest

In *Yatooma v. Barker*, 2010 WL 5373807 (Mich. Ct. App. 2010), the court, applying Michigan law, held that a security agreement that gave a creditor a security interest in "all of the assets" and "all collateral" of debtors did not give the creditor a security interest in an after-acquired right of first refusal. That description in the security agreement did not sufficiently identify after-acquired assets as assets that would be covered by the agreement, and the assets contemplated by the agreement were not by their nature in constant fluctuation.

Describe collateral carefully - CD was "deposit account," not "instrument"

In *In re Perez*, 2010 WL 4942033 (Bankr. D.N.J. 2010), the court, applying New Jersey law, held that a certificate of deposit (CD) that had been pledged as collateral for a credit union's loan to an employee who later filed a bankruptcy petition was a deposit account not an instrument. A perfected security interest in the account, therefore, would be held by the credit union under Article 9 if it had control over the account for the purpose of determining whether the bankruptcy trustee could obtain relief from the automatic stay and apply the CD proceeds to the balance of the loan. The CD was nonnegotiable and nontransferable. The CD was not of a type that in the ordinary course of business would be transferred by delivery with any necessary endorsement or assignment. Even though the CD was technically certificated, it had no value and neither functioned like an instrument nor possessed the attributes ordinarily associated with an instrument.

Describe the collateral carefully - "sums recovered" is not the same as "judgment."

A bank's interest in interpleaded funds in a New York case was unperfected and therefore junior to a competing claimant's interest, because the bank failed to perfect its interest by taking possession of the proceeds of the funds. *Goldberg & Connolly v. New York Community Bancorp, Inc.*, 565 F.3d 66 (2d Cir. 2009). A general loan and security agreement that created the bank's interest, assigning "all sums recovered" from a judgment was not an assignment of the judgment, itself, reasoned the court. As a result, the bank's interest was a security interest in money.

Some wins for creditors:

In an action by a bank against the federal government for an alleged wrongful tax levy of payments made by the IRS, the court, applying Iowa law, held that the bank had priority over a June 22, 2005, tax lien in respect to the payments under Consulting Agreement B because it was a perfected secured party. *Quad City Bank and Trust Company v. United States*, 2009 WL 2105982 (S.D. Iowa 2009). The financing statement filed by the bank covered "Assignment of Consulting Agreement Payments" and had the debtor's assignment of Consulting Agreement A attached. It covered "any of the foregoing ... acquired later; [and] additions ... to any of the foregoing." The broad "additions to" and "acquired later" language was limited by its reference to "the foregoing." The only terms coming before it were "Assignment of Consulting Agreement Payments," and "See Attached Exhibit 'A.'" A description of collateral reasonably identifies the collateral if it identifies the collateral by category. Since either party's interpretation of the financing statement language was reasonable. The court concluded that the statement's coverage was ambiguous, but it put subsequent creditors on notice that payments due to the debtor from consulting agreements might be subject to a security interest. It also perfected the bank's interest in the payments under Consulting Agreement B on the date on which the debtor gave the bank a security interest in the payments from Consulting Agreement B, which, in turn, was collateral covered by the financing statement. Even though the financing statement was filed before the security agreement was executed, it resulted in perfection of the security interest the moment that it attached.

In *Jahn v. Cornerstone Cmty. Bank (In re U.S. Ins. Group, LLC)*, 429 B.R. 903 (E.D. Tenn. 2010), the district court affirmed the bankruptcy court's ruling that a collateral description, including accounts, commission accounts and books related to the commission accounts, was adequate to cover insurance agent's "book of business" without need to use either that phrase or the Article 9 category, "general intangibles."

In *In re CHA Hawaii LLC*, 2010 WL 797285 (Bankr. D. Hawaii 2010), the collateral description in a security agreement excluded "accounts," as defined in Article 9. The court held that the term "accounts" included Medicare and Medicaid payments (as "healthcare insurance receivables") but not disproportionate share hospital (DSH) payments, which are supplemental to Medicare and Medicaid. Therefore the DSH payments were included in the collateral.

Subordinate lenders each had security interest

Subordinate lenders each had a security interest in a stockholder's ownership interest in a corporation even though the stockholder, who shared the corporation's single stock certificate with her husband, did not sign documents entitled “security agreement” for the subordinate lenders, held the court, applying New York law, in *In re Keisler*, 2010 WL 4627892 (Bankr. E.D. Tenn. 2010). With respect to each lender, the stockholder and her husband executed a packet of documents, including a note agreement, that formed the entire contractual agreements between the parties. Each note agreement contained a covenant that provided for an interest in the shares of stock to secure payment of the promissory note issued to the lender. The covenant supported testimony that it was the intention of the parties that the stockholder and her husband would pledge any interest held in the stock as collateral to secure the promissory notes.

No tribal court judgments?

Liens arising from a tribal court judgment did not fall within the scope of Article 9, held the court in *In re Juhl*, 2009 WL 234346 (Minn. App. 2009). Judgment debtors sought a determination of the effectiveness of purported financing statements in which they were named as debtors. The court concluded that challenged liens were outside Article 9 by process of elimination, finding that they were not the result of a transaction that created a security interest in personal property or fixtures by contract; were not agricultural liens; did not arise from a sale of accounts, chattel paper, payment intangibles, or promissory notes or from a consignment; were not security interests arising under Article 2 or 2A; and were not security interests of a collecting bank in items, accompanying documents and proceeds, or security interest in a document presented under a letter of credit.

3. Can't I use a "supergeneric" description of the collateral in the security agreement?

In *In re Lifestyle Home Furnishings, LLC*, 2009 WL 1270317 (Bankr. D. Idaho 2009), a bankruptcy court applying Idaho law held that collateral descriptions were sufficient even though their loan agreements contained a supergeneric description, "all of grantor's personal property" because a collateral description contained in a disclosure listed categories of collateral, including all accounts, inventory, equipment, documents of title, farm products, titled goods, money and investment property. Although supergeneric descriptions are generally insufficient under § 9-108, an extraordinary degree of specificity is not required. Descriptions by category or by type of collateral defined in the UCC are sufficient. The court, added that there is nothing in the UCC to prohibit parties from integrating several documents to create a security agreement.

4. Where do I file a financing statement?

In a case involving a debtor incorporated in Florida, the secured party filed a financing statement in Pennsylvania. *In re Trafford Distributing Center, Inc.*, 414 B.R. 849 (Bankr. S.D. Fla. 2009). The court noted that a secured party is required to make only one filing in the state of the debtor's location, rather than filing where the collateral is located, with very few exceptions not applicable here. § 9-301(1). As a result, the financing statement was not effective to perfect the security interest.

5. If I get the debtor's name close on the financing statement, subsequent searchers will have to look for it, won't they?

The (latest) bad news for filers - "close" probably doesn't count:

A financing statement filed against "Lohrey Investments LLC" was ineffective to perfect against equipment owned by Lohrey Enterprises, Inc. *In re Lohrey Enterprises, Inc.*, 2010 WL 147916 (Bankr. N.D. Cal. 2010).

Financing statements were seriously misleading where they failed to properly list the debtor's registered organization name: the debtor's registered organization name was "C. W.

Mining Company" (periods after the letters and spaces between) and the financing statements listed it as "CW Mining Company" (no periods or spaces). In addition, using standard search logic, a search of the database using the debtor's registered organization name did not reveal the financing statements. *In re C.W. Mining Company*, 2009 WL 2601246 (Bankr. D. Utah 2009).

In an adversary proceeding in which the issue was whether financing statements filed by a bank under the assumed name of a debtor, "Silver Dollar Stores, LLC," rather than its organizational name, "Silver Dollar, LLC," sufficiently named the debtor, a bankruptcy court in Tennessee held that the filing did not meet the requirements of § 9-503(a)(1), even though the assumed name was arguably "registered." *In re Silver Dollar, LLC*, 388 B.R. 317 (Bankr. E.D. Tenn. 2008).

A financing statement filed by a bank identifying its debtor, whose official name was "EDM Corporation," as "EDM Corporation d/b/a EDM Equipment" was seriously misleading under the Nebraska UCC, § 9-506(c), rendering its security interest unperfected, held the court in *Hastings State Bank v. EDM Corp. (In re EDM Corp.)*, 2010 WL 1929772 (B.A.P. 8th Cir. 2010). The debtor's name must be the name indicated on the public record in its organizational jurisdiction, § 9-503. A search performed against the correct legal name ("EDM Corporation," with no d/b/a) using the Secretary of State's "standard search logic" did not disclose the existence of the financing statement.

The "additional debtor" problem

Financing statements that a bank filed in New York were seriously misleading with respect to the debtor status of a New York corporation that was listed as an additional debtor on plain-paper attachments to the financing statements, held the court in *In re Camtech Precision Mfg., Inc.*, 2011 WL 294034 Bankr. (S.D. Fla. 2011). Accordingly, under New York law, the financing statements were ineffective to perfect the bank's alleged security interests in the corporation's assets. Although the bank filed the financing statements using Florida-approved U.C.C.-1 forms, which the New York filing office accepted, the plain-paper attachments were unapproved and were not even referenced in the box for additional debtors on the first page of each U.C.C.-1 form. The filing office, pursuant to a New York rule governing U.C.C. forms and procedures, was allowed to, and apparently did, treat the 'additional debtor' information contained in the unapproved attachments as not having been provided in the financing statements. As a result, and as indicated by a search using New York's U.C.C. public-inquiry system, the financing statements were not indexed under the name of the corporation.

Tax liens continue to produce unusual results for filers and trustees alike.

In a priority dispute between a federal tax lien and a judgment lien, the notice of federal tax lien was effective even though it used a prior name of the taxpayer-debtor. *Trane Company v. CGI Mechanical, Inc.*, 2010 WL 2998516 (D.S.C. 2010). The judgment creditor had done business with the debtor for years under the old name and continued to use the old name in some correspondence. A search under the new name would not have disclosed the tax lien notice, but the court held that a reasonably diligent search conducted by this particular creditor should have

included the debtor's old name. The court relied in part on the decision in *In re Spearing Tool and Manufacturing Co.*, 412 F.3d 653 (6th Cir. 2005), cert. denied 549 U.S. 810 (2006).

In In re Crystal Cascades Civil, LLC (United States v. Buenting), 415 B.R. 403 (B.A.P. 9th Cir. 2009), the IRS had filed a notice of federal tax lien in the correct place in Nevada to cover real property. The notice identified the taxpayer as "Crystal Cascades, LLC" instead of "Crystal Cascades Civil, LLC." After the IRS filed its notice, a bank filed deeds of trust against the taxpayer's real property. When the taxpayer went bankrupt, the bank proceeded against the real property collateral. The IRS learned of this and asserted that it had the prior lien. The bank argued that the notice filed by the IRS did not satisfy the federal regulation requiring that the notice be filed "in such a manner that a reasonable inspection of the [applicable real property] index will reveal the existence of the lien." At issue was whether the similarity of the taxpayer's actual name to the name filed by the IRS was sufficient that a "reasonable" inspection of the Nevada records would have revealed the notice. The court held that in Nevada a title searcher could reasonably search under the exact correct name of the relevant party without searching variants of the taxpayer's name. Therefore, the IRS notice was not sufficiently filed and the bank had the prior lien on the real property.

Good news for filers (but not so much for searchers) from the Fifth Circuit:

In an action to determine the ownership of cattle and whether two contesting banks held a security interest in them, a bank's financing statement was not seriously misleading even though the bank's financing statement identified "Louie Dickerson" as the debtor instead of his proper legal name, "Brooks L. Dickerson," held the Fifth Circuit, applying Mississippi law. The purpose of the filing system is to give notice to creditors and other interested parties that a security interest exists in property of the debtor. Perfect accuracy, however, is not required as long as the financing statement contains sufficient information to put any searcher on inquiry. The other bank was put on inquiry notice that a security interest in the property of "Brooks L. Dickerson" could be listed under the name "Louie Dickerson." The debtor held himself out to the community as Louie Dickerson, and he used this name in bank accounts, on bills of sale, and with others with whom he did business. Moreover, the other bank had actual notice that the debtor was known as both "Louie Dickerson" and "Brooks L. Dickerson." In its own files, the debtor was identified by both names in numerous places. Here the other bank was not seriously misled by the bank's financing statement. *Peoples Bank v. Bryan Brothers Cattle Company*, 504 F.3d 549 (5th Cir. 2007).

Legislative fix

The National Council of Commissioners on Uniform State Laws (NCCUSL) has addressed the issue of filing on individual debtors (and several other post-2001 issues) by proposing changes in the uniform §§ 9-502 and 9-503 and related comments. See Appendix A for the text of these recommendations and legislative notes.

6. I don't have to file a financing statement, if I think perfection may be automatic or if I think I have perfected some other way, do I?

A company that provided funding to a lender, who was in the business of making short-term subprime loans to consumers to cover the cost of constructing modular homes, had an unperfected security interest in notes secured by mortgages, where, notwithstanding the requirements of the credit and security agreements, the lender retained possession of the notes at issue, and the lender could not possess the notes on the company's behalf. *Prime Financial Services LLC v. Vinton*, 279 Mich. App. 245, 761 N.W.2d 694 (2008).

See Appendix B for a chart of perfection methods under Article 9.

7. Filing a financing statement in the Secretary of State's office bankruptcy-proofs my claim, doesn't it?

No real estate:

A secured party that held a security interest in both the intangible and tangible assets of a bar had no secured interest in the former owner's leasehold interest in the premises because § 9-109(d)(11) expressly leaves interests in real estate, including leaseholds, outside the scope of security agreements provided for in Article 9. *Bischoff v. LCG Blue, Inc.*, 2009 WL 148519 at *5 (Cal. App. 2009).

But: Security interest in hotel revenues was interest in personalty

A hotel's revenues from room occupancy, food and beverage sales, catering, gift shop purchases, and spa and related hotel services were "accounts" or "payments intangible" as those terms were defined in Article 9, held the court, applying New Jersey law, *In re Ocean Place Development, LLC*, 2011 WL 119594374 (Bankr. D.N.J. 2011). Accordingly, a security interest in the hotel revenues was an interest in personalty, not an interest in realty, and was therefore required to be perfected and enforced pursuant to Article 9. Documents executed with a loan agreement between a bank and the hotel included an assignment of rents and leases and broadly defined "rents" as all revenues collected from guest rooms, restaurants, food and beverage retail sales, and various other sources, and Article 9 excluded from its scope the creation or transfer of any interest in real property, including a lease or rents thereunder. The occupants of the hotel, however, were not tenants who possessed an interest in real property. They were merely licensees. Further, the parties' designation of the hotel revenues as "rents" did not establish that the hotel revenues could appropriately be treated like leasehold interests. To do so for that reason alone would directly contravene New Jersey statutes on "hotels," "landlords," and "tenants," Article 9's provisions, and relevant case law.

But are manufactured homes real estate?

In *Textron Financial Corp. v. New Horizon Home Sales, Inc.*, 2011 WL 901844 (N.D.W. Va. 2011), the court, applying West Virginia law, held that a lender's purchase-money security interest in a mobile home that was later affixed to real property owned by the debtor had priority

over a deed of trust filed by the vendor of the real property that encumbered the property and any after-acquired or after-constructed buildings, structures, improvements, and fixtures, even though the deed of trust was filed before the lender's fixture filing. The lender's security interest in the mobile home arose, and was perfected by the fixture filing, before the mobile home became a fixture.

In *In re Starks*, 2011 WL 248521 (Bankr. E.D. Ky. 2011), the court, applying Kentucky law, held that even if a manufactured home located on two mortgagors' real property was a fixture to which the mortgage referred, the mortgagee could not perfect a security interest in the manufactured home through Article 9's provision that a perfected security interest in a manufactured home as a fixture would have priority over a conflicting interest of an encumbrancer or owner of the real property. The manufactured home, which had never been converted to real estate, had an active certificate of title. Accordingly, the perfection of the security interest in the manufactured home was by notation on the certificate of title, as specifically required by a motor-vehicle statute governing the creation and perfection of a security interest in a titled manufactured home.

In *In re Akers*, 427 B.R. 408 (Bankr. W.D. Ky. 2010), the court held that a mortgagee held a valid first, prior, and superior lien on real property that included a manufactured home. The Chapter 7 debtors and another debtor consensually granted the mortgagee a lien on the manufactured home. The documents of record established that their clear intent was to make the manufactured home part of the real estate. Although they had agreed to surrender the certificate of title, they failed to do so, despite the mortgagee's efforts to obtain it. Under Kentucky law, a grant of a mortgage or security interest is binding between the parties, regardless as to whether or not it is perfected. Kentucky recognizes equitable liens that attach upon the advancement of money. Such a lien is effective as against the mortgagor and anyone dealing with the property with actual knowledge of it.

In *In re Ritchie (Palmer v. Washington Mutual Bank)*, 416 B.R. 638 (B.A.P. 6th Cir. 2009), the Court affirmed the bankruptcy court's holding that a bank's security interest in a manufactured home was unperfected under Kentucky law, because its security interest had not been noted on the certificate of title. The bank's security interest could therefore be avoided by the bankruptcy trustee. The home remained personal property because the debtor had not taken the steps required under the Kentucky law to convert it to real property, so the only way to perfect the bank's security interest was by notation of the lien on the certificate of title. The bank made several unsuccessful arguments: (1) The home was not real property, so the bank's lis pendens filed in a previous state court action was not effective under state law. (2) Similarly, any constructive notice that may have been provided by the lis pendens would not have protected the bank from the trustee's strong arm powers as a hypothetical lien creditor as to personal property, even if it may have provided constructive notice to the trustee as a hypothetical bona fide purchaser of real property. (3) The bankruptcy court's ruling was not inconsistent with the state court's previous enforcement of an "equitable lien." An "equitable lien" is essentially an unperfected security interest in the Sixth Circuit and, as such, would still be avoidable by the trustee.

No fixture priority over other real property claimants without a fixture filing:

An energy guard fell within the definition of consumer goods, as well as within the definition of a fixture, held the court in *In re Troutt*, 2009 WL 2905923 (Bankr. S.D. Ill. 2009). The UCC defines fixtures as goods that have become so related to particular real property that an interest in them arises under real property law and the term is usually applied to articles that were once tangible personal property but which have been physically attached to the real estate so that they become a part thereof. In determining whether an item is a fixture or personal property, Illinois courts look at three factors: (1) the nature of the attachment to the real estate, (2) the item's adaptation to and necessity for the purpose for which the premises are devoted and (3) whether it was intended that the item be part of the realty. Intent to permanently improve the real estate, vel non, is the crucial factor. This energy guard was an insulation blanket installed in an attic by conforming it to the size of the attic, cutting it to fit around roof support beams, and stapling it into place. If removed, it would have no utility for any other attic, and also damage to the underlying ceiling would occur. These facts made the energy guard a fixture and the creditor was unsecured because there was no fixture filing.

Financing company did not have perfected security interest in bills of lading

A company that financed a customer's purchase of raw materials from its supplier did not have constructive possession of the bills of lading for two shipments of raw materials as necessary under Article 9 to perfect its security interest in the bills of lading and, through them, in the underlying raw materials, held the court, applying New York law, in *Ancile Inv. Co. Ltd. v. Archer Daniels Midland Co.*, 2011 WL 813724 (S.D.N.Y. 2011). Therefore, the financing company failed to allege a superior interest in possession of the bills of lading so as to support its constructive bailment claim against the supplier. Under Article 9, a secured party could establish constructive possession of collateral by showing that the party in possession of the collateral, which could not be the party that pledged the collateral, authenticated a record either before or after taking possession of the collateral acknowledging that its possession was or would be for the benefit of the secured party. The financing company made no such showing with respect to the supplier's possession of the bills of lading, merely alleging that the supplier "acknowledged" the financing company's security interest.

8. I don't need to file a financing statement if I retain title in a lease or a consignment, do I?

Invoice purchase agreement was financing agreement

An invoice purchase agreement between two corporations, one of which later filed a bankruptcy petition, was a financing agreement not a true sale of the receivables described in the agreement, held the court, applying California law, in *In re Qualia Clinical Service, Inc.*, 441 B.R. 325 (B.A.P. 8th Cir. 2011). The creditor corporation's perfection of its security interest was therefore a transfer of an interest in the debtor corporation's property that the trustee of the bankruptcy estate could avoid as a preference if it occurred within the 90-day period before the filing of the bankruptcy petition. The agreement shifted virtually the entire risk of non-collection of the accounts to the debtor corporation, requiring it to repurchase at full value any uncollectible

accounts.

Leases:

A transaction that gave a "lessee" an option to purchase the leased personalty at the end of the term for 10% of the purchase price, was a secured transaction, rather than a "true lease." *In re Phoenix Equipment Company, Inc.*, 2009 WL 3188684 (Bankr. D. Ariz. 2009). No estimate was presented to establish the estimated fair value of the goods at the end of the term or the cost of not exercising the purchase option, so the bankruptcy judge was unwilling to conclude that the option price was "nominal." The Court noted that the option price was the same for a series of sale-leaseback arrangements by which the "lessee" refinanced its equipment and seemed to bear "no relation to the anticipated fair market value of the equipment" at the end of the term. The court also concluded, based on the fact that the lessee needed to exercise the option in order to remain in business, that its "only reasonable economic choice" was to exercise that option.

The same conclusion resulted from a 10% fixed price in a state court opinion out of Indiana. *Gangloff Industries, Inc. v. Generic Financing & Leasing Corp.*, 907 N.E.2d 1059 (Ind. App. 2009). The price was so low in relation to an originally estimated fair market value of the goods that the "only sensible course of action" for the "lessee" was to exercise the option and purchase the goods at the end of the lease.

In *Uni Imaging Holdings, LLC*, 2010 WL 148422 (Bankr. N.D.N.Y. 2010), the debtor lessee under a 66-month lease of MRI equipment, sought to characterize the lease as a secured sale. The court held that residual price of 13% of the original cost was not nominal and that the debtor had not carried its burden of proof to characterize the lease as a secured sale.

A consignor bears the burden of proof to show that a transaction falls outside the scope of Article 9, held a bankruptcy court in Indiana, where the creditor contended that the creditors of the "consignee" generally knew that the consignee was substantially engaged in selling the goods of others. *In re Downey Creations, LLC*, 414 B.R. 463 (Bankr. S.D. Ind. 2009). The court required evidence that a majority of creditors, determined by number rather than amount, knew that the debtor was substantially engaged in selling the goods of others. But see *Farba v. Dealer Services Corp.* 100 Cal. Rptr. 3d 219 (Cal. App. 2009) (concluding that actual knowledge by single secured creditor satisfied test).

In a bank's replevin action, it was held under Missouri law that a secured creditor who provided floor-plan financing to a used car dealer was entitled to retain possession of 18 seized vehicles because the relationship between the bank and the dealer was a consignment subject to the perfection requirements of the UCC *Excel Bank v. National Bank of Kansas City,* 290 S.W.3d 801 (Mo. App. W.D. 2009). The bank's possession of the certificates of title in the bank's name was insufficient to perfect the bank's interest, the secured creditor had a validly perfected security interest in the dealer's entire inventory, that was superior to the bank's unperfected purchase-money security interest. The bank argued that although it did not file a financing statement covering the vehicles, the secured creditor had a duty to conduct due diligence by examining the public motor vehicle registration records to determine whether any other entity asserted an interest in the vehicles. However, the due diligence required is checking for perfected security interests. The bank could easily have filed a financing statement to protect

its interest but failed to take that step to inform third parties that it retained any interest in the vehicles, instead keeping the certificates of title in its possession. The secured creditor could have checked the vehicle registry in addition to the UCC filings but was not required to do so.

In *Royale Pigments & Chemicals LLC v. Bomanite Corporation*, 2009 WL 800911 (E.D. Cal. 2009), the court held that a bank had a senior perfected security interest in a buyer's inventory, including industrial chemicals in a dispute with a subsequent provider of inventory financing which claimed a purchase-money security interest under an alleged consignment. The buyer and the bank were parties to a loan and security agreement. The buyer granted the bank, and the bank perfected, a continuing first priority security interest in the buyer's assets, including the inventory. The bank showed financing statements filed with the Secretary of State perfecting its security interest in, inter alia, "inventory" in 2005. Title transferred to the disputed inventory upon its delivery to the buyer in 2008. The 2008 invoices did not evidence the seller's intention to retain title in the goods. The seller did not file a financing statement with respect to the inventory or provide notice to the bank of the alleged consignment of the inventory when it delivered it to the buyer. Even if the seller's claim of a sale agreement converted to a consignment agreement was true, the seller's unperfected interest in the inventory was subordinate to the bank's senior security interest in the inventory, the court ruled.

A liquidator's perfected security interest in consigned rugs in Alabama was held to be senior to the consignor's unperfected security interest in *Woven Treasures, Inc. v. Hudson Capital, L.L.C.*, 2009 WL 4980283 (Ala. 2009). An owner of a store had granted the liquidator a security interest in all the merchandise displayed at the store (including the consigned rugs) and the liquidator perfected this interest, while the consignor never filed a financing statement asserting its interest in the rugs. The liquidator's security interest attached, was perfected by the filing and, under § 9-322, was senior to consignor's interest.

In a priority dispute between an auto dealer's consignor and secured party, the consignor's title had priority, where the secured party had actual knowledge that the auto dealer was substantially engaged in selling the goods of others. *Fariba v. Dealer Services Corp.*, 178 Cal. App. 4th 156, 2009 WL 319538 (Cal. App. 4th Dist. 2009). The court described two exceptions to the rule that consigned goods in the possession of the consignee are subject to the claims of its creditors: (i) the consignor files a UCC financing statement, or (ii) the consignee is generally known to its creditors to be in the business of selling the goods of others. The court then viewed the second exception as a kind of constructive notice to the competing secured party, and reasoned that it would be a nonsensical reading of the statute to protect the consignor if a competing creditor had constructive notice but not if it had actual notice.

Possible consignments

In *In re WFG, LLC*, 2010 WL 4607614 (Bankr. E.D. Tenn. 2010), the court, applying Tennessee law, held that genuine issues of material fact existed as to whether a gemstone-acquisition company's transactions, specifically the delivery of gemstones and jewelry, with a jewelry store that later filed for bankruptcy were consignments, and thus secured transactions, so as to preclude summary judgment in an adversary proceeding in which a trustee sought the avoidance of transfers of the items.

Better news for consumers:

In a dispute over whether consigned recreational vehicles (RVs) on the lot of a Chapter 7 debtor were property of the bankruptcy estate, where resolution of the legal issues rested primarily on what law the court should apply regarding consignments, a bankruptcy court certified to the Tennessee Supreme Court the issue of "orphan consignments" following the UCC revisions that removed some, and possibly all, consignments from Article 2. *Waldschmidt v. Adams (In re Music City RV, LLC)*, 2009 WL 77248 (Bankr. M.D. Tenn. 2009). There was no agreement between any consignor and the dealer concerning a designation of the consignment of RV's as "sale on approval" or "sale or return." No UCC-1 financing statements were filed. The trustee asserted that the rights of the consignors (as unperfected consignors) were subordinate to the rights of the trustee, as a hypothetical judgment lien creditor. The consignors contended that the RVs were consumer goods, not part of the dealer's inventory, and therefore not property of the estate. The Supreme Court of Tennessee, answering the certified question in favor of the consignors, held that § 2-326 as adopted in Tennessee, providing that goods on sale or return are subject to the claims of the buyer's creditors while in the buyer's possession, does not apply to such transactions, so that the consignment of an RV by a consumer to an RV dealer, for the purpose of selling that RV to a third person, is not a transaction covered by that section. In re Music City RV, LLC, 304 S.W.3d 806 (Tenn. 2010).

9. When do I have to file a financing statement to perfect a purchase-money security interest?

In *In re T & R Flagg Logging, Inc.*, 2009 WL 192569 (Bankr. D. Maine, 2009), a Maine court held that a bank's blanket security interest in a debtor's assets trumped an equipment financer's lien because, although it claimed to do so, the equipment financer did not hold a prior purchase-money security interest (PMSI) in four pieces of logging equipment purchased by the debtor from a dealer before the debtor filed for bankruptcy relief. The dealer failed to perfect the security interest within 20 days of the debtor's acquiring rights in the equipment, which was required to give it the statutory leg-up over the bank's preexisting blanket lien.

10. How do I document an assignment of loan documents?

Be careful how you describe the subject of the assignment in Article 9 terms.

The transfer in *321 Henderson Receivables Origination LLC v. Sioteco*, 2009 WL 1219366 (Cal. App. 2009), was to a factoring company in exchange for lump-sum payments. The structured settlement payments were considered general intangibles. Under California's UCC, once a claim arising in tort has been settled and reduced to a contractual obligation to pay (as in, but not limited to, a structured settlement) the right to payment becomes intangible and ceases to be a claim arising in tort. Moreover, § 9-408 applied to sales of structured settlement payments because, unlike the model UCC, the California UCC did not contain the uniform provision excluding annuities from its reach. The court concluded that § 9-408, as adopted in California, evidenced a public policy against anti-assignment provisions in general and that the state insurance code evidenced a public policy in favor of court-approved factoring transactions.

Thus public policy favored the legal conclusion that anti-assignment provisions did not bar court-approved transfers of structured settlement payments. Therefore, the court concluded, where no interested parties objected to the transfer of structured settlement payment rights, the anti-assignment provisions in the annuity contract, settlement agreement, or other related contracts did not bar the factoring transaction at issue.

Attach evidence of assignment to bankruptcy claim:

Discussing the "serial assignments" of mortgages that have "complicated what was previously a generally straight-forward standing analysis," the Chapter 7 trustee's objection to stay relief was sustained, when the motion was filed by MERS as "nominee" for the mortgagee, and the motion provided no documentation or evidence that the party for whom MERS was acting had any interest in the note or mortgage. *In re Sheridan,* Case No. 08-20381-TLM (Bankr. D. Idaho, March 12, 2009).

The Tenth Circuit held that a creditor didn't satisfy its burden of proof when it filed a proof of claim without supporting documentation and the creditor failed to present evidence in the face of the trustee's objection. The burden can't be shifted to the trustee to disprove the claim lacking documentation. *Caplan v. B-Line, LLC (In re Kirkland),* 572 F.3d 838 (10th Cir. 2009).

When the assignee attached unendorsed copies of mortgage note to its proof of claim, the assignee failed to show that it was actually the holder of the note, with the right to enforce the note. *In re Wells,* 407 B.R. 873 (Bankr. N.D. Ohio 2009).

Distinguish between security interests and sales.

In *JD Factors LLC v. Freightco LLC,* 2009 WL 2509145 (N.D. Ind. 2009), a suit in which a factor sought collection of outstanding payments from an account debtor on accounts receivable that it had purchased from a creditor pursuant to a factoring and security agreement, the court held that the factor was entitled to enforce collection of the account debtor's outstanding debt. The factoring agreement, at a minimum, provided the factor with a security interest in the disputed account and, after default, under Indiana law, a secured party may enforce the obligations of an account debtor.

A close call for MERS:

In *In re Agard*, 444 B.R. 231 (Bankr. E.D.N.Y. 2011), a mortgage servicer for a bank serving as trustee under a mortgage loan trust moved for relief from the automatic stay to permit it to foreclose on a Chapter 7 debtor's real property. The debtor opposed the motion, challenging servicer's standing. The Bankruptcy Court held that the servicer failed to show that bank was holder of note and the mortgage did not authorize the mortgage electronic registration system (MERS), named as "nominee" to make an assignment of the mortgage and no agency relationship existed between MERS and its members to support such and assignment on behalf of and to members under New York law. However, the trustee's filing of a no-asset report did not act to abandon the real property, which remained estate property subject to automatic stay. The *Rooker-Feldman* doctrine and res judicata were applied to bar the debtor's standing

challenge. "However, in all future cases which involve MERS, the moving party must show that it validly holds both the mortgage and the underlying note in order to prove standing before this Court."

Don't worry about changing the secured party on the underlying documents(?)

The third assignee of a properly perfected security interest in a used motor vehicle was not required to reperfect the security interest, held the court, applying Kansas law, in *In re McMullen*, 441 B.R. 144 (Bankr. D. Kan. 2011). The trustee of the vehicle owner's bankruptcy estate could therefore not avoid the assignee's lien. The original assignee perfected its security interest by complying with a Kansas certificate-of-title statute, which, under Article 9, was the equivalent of filing a financing statement. Although the trustee argued that each subsequent assignee had a duty to reperfect the security interest, Article 9 did not require a filing for the continuation of the perfected status of an assigned perfected security interest as to the creditors and transferees of the debtor, and the certificate-of-title statute did not contain a provision to the contrary.

An assignee of a note and security agreement who claimed a perfected security interest in a recreational vehicle (RV) that was alleged to be property of a Chapter 7 estate had a perfected interest, even though it was not noted on the RV's certificate of title in compliance with the Arkansas certificate of title act, because the perfected security interest in the RV remained perfected when it was assigned. The Code and commentary state that the language used in the certificate of title law should be read as permissive and that the overall scheme of the UCC should be followed if at all possible. The general rule under the UCC is that no further action need be taken to continue perfection when dealing with assignments. Reading the UCC and the state certificate of title act together, the court could not infer that the General Assembly meant that failure to comply with the certificate of title act would result in an assigned lien in a motor vehicle being unperfected. *In re Johnson*, 407 B.R. 364 (Bankr. E.D. Ark. 2009).

Similarly, under Indiana law, the assignee of a security interest perfected by notation on a certificate of title is not required to be named on the certificate of title to continue perfection. *Boston v. Chrysler Fin. Servs. Americas LLC (In re Scott)*, 427 B.R. 123 (Bankr. S.D. Ind. 2010). Under § 9-311(c), the duration and renewal of a security interest perfected by compliance with a state's certificate of title statute are governed by that statute, and the Court found that the Indiana certificate of title statute did not clearly require the assignee to be named on the certificate. The court also looked to § 9-311(b) (compliance with state's certificate of title statute is equivalent of filing financing statement), UCC § 9-310(c) (filing financing statement amendment not required to continue perfection upon assignment of security interest) and Comment 4 to § 9-310 (stating that assignee should not be required to take action to have certificate of title reflect assignment or assignee's name, unless statute expressly provides to contrary).

McMullen, Johnson and *Scott* may be in conflict, however, with *Farmer v. LaSalle Bank (In re Morgan)*, 291 B.R. 795 (Bankr. E.D. Tenn. 2003). In *Morgan*, a Chapter 7 trustee brought an adversary proceeding to recover insurance proceeds that creditor received, based upon its security interest in debtor's car, when car was destroyed in a postpetition accident. The Bankruptcy Court held that the creditor (with which the debtor had refinanced her car loan),

having failed, prior to commencement of the bankruptcy, to acquire a duplicate title noting its interest, could not rely on the doctrine of equitable subrogation to avoid effects of not having its interest noted on title certificate on petition date. The creditor's belated attempt to perfect its security interest in motor vehicle more than two years after it provided financing to debtor and subsequent to commencement of debtor's Chapter 7 case was void as a violation of automatic stay. The trustee, in the exercise of his strong-arm power under 11 U.S.C. § 544(a), had priority over the creditor's unperfected security interest and could recover the insurance proceeds. See also *In re Clark Contracting Services, Inc.*, 39 B.R. 789 (Bankr. W.D. Tex. 2008) (distinguished by *In re Johnson*). *Clark Contracting* has been overruled legislatively. Texas Transportation Code §§ 501.113 & 501.114.

Does the "mortgage follow the note"?

The recent Massachusetts Supreme Court decision in *U.S. Bank National Association v. Ibanez,* 941 N.E. 2d 40 (Mass. 2011), dealt with issues raised by inaccurate recording of a mortgage assignment. Lenders each filed actions in the Massachusetts Land Court for declarations of clear title after each foreclosed on residential mortgages and purchased the property at the foreclosure sale. In both cases, the Massachusetts Supreme Court held that the lenders lacked the authority to exercise the power of sale because they were not the assignees of the mortgages at the time of the notice of sale and subsequent foreclosure sale. However, in *Musselman v. Deutsche Bank Trust Company Americas (In re Balderrama)*, --- B.R. ----, 2011 WL 1750679 (Bankr. M.D. Fla. May 4, 2011), a Chapter 7 trustee brought an adversary proceeding to quiet title and to value at zero dollars a bank's alleged interest in the debtor's non-homestead real property. The trustee moved to compel the bank to produce discovery related to its purchase of promissory note and mortgage on property. The Bankruptcy Court, held that the bank had to respond to the trustee's interrogatory and requests for production of documents related to determining whether bank was holder of properly endorsed promissory note, but the bank would not be compelled to respond to trustee's additional discovery requests. Under Florida law, proof of a creditor's status as the holder of a note secured by a mortgage is proof of creditor's purchase of the debt, supporting application of the general rule that the mortgage, even without written assignment, may travel equitably to holder of underlying debt.

Note that Section 9-203(g) of the UCC provides that "[t]he attachment of a security interest in a right to payment or performance secured by a security interest or other lien on personal or real property is also attachment of a security interest in the security interest, mortgage, or other lien." Section 9-607(b) of the UCC provides that a secured party may record a copy of the security agreement transferring an interest in the note. However, as a matter of state real estate law, without a recorded mortgage assignment, a party may not be able to enforce the mortgage.

11. The default and remedies rules are very forgiving, aren't they?

Be diligent in pursuing your remedies.

A franchisee, a judgment creditor, was held entitled to collect the money in a debtor's bank account and a portion of its future revenue streams even though a bank had a priority

interest in the debtor's assets because the bank failed to exercise its rights to those assets under its security agreement with the debtor. *One CW, LLC v. Cartridge World North America, LLC*, 661 F. Supp. 2d 931 (N.D. Ill. 2009). The security agreement provided that the bank only took on the rights of a secured creditor under the UCC after a default occurred. The bank did declare the debtor to be in default on the day that the bank was served with the citation. Subsequently it did not take consistent actions to pursue its rights and remedies resulting from the default; it froze the debtor's assets for only five days before allowing it to resume unencumbered use of the account, after the debtor's president assured the bank that it was attempting to resolve the dispute with the franchisee. § 9-401(b), adopted by both Minnesota and Illinois, explicitly notes that an "agreement between the debtor and the secured party which prohibits a transfer of the debtor's rights in collateral or makes the transfer a default does not prevent the transfer from taking effect." The mere declaration of a default, absent other affirmative remedial action, such as the acceleration of the loan, does not entitle the secured party to take possession of the collateral, the court said. Thus the bank could not, consistent with the UCC, fail to exercise its rights under the security agreement, while it impaired the status of other creditors by preventing them from exercising valid liens.

Some good news for creditor: Alleged failure to perfect security interest did not give rise to cause of action

In *Melancon v. Countrywide Bank*, 2011 WL 692051 (E.D. La. 2011), the court, applying Louisiana law, held that an alleged failure of a bank to perfect its security interest in mortgaged property did not give rise to a cause of action by borrowers against the bank after it initiated foreclosure proceedings following the borrowers' default on a promissory note accompanying the mortgage. Perfection of a security interest was relevant only as to third parties claiming priority over the interest. An unperfected security interest remained valid between the parties to an agreement as long as the interest attached to the collateral.

But: Security interests not perfected within reasonable time

In *State ex rel. Wagner v. Amwest Sur. Ins. Co.*, 280 Neb. 729, 2010 WL 4263081 (2010), the court held that a surety company did not perfect within a reasonable time a bank's security interests in leases and related assets. Accordingly, the surety company breached agreements under which it had an obligation to perfect the security interests, given that the agreements did not state a time within which perfection had to occur and that Nebraska law would therefore imply a reasonable time for performance. Nearly 18 months after the parties had entered into the last agreement, the surety company still had not perfected the security interests.

12. I'm not a farm lender, so I don't have to worry about caring for and feeding collateral, do I?

Don't forget to file a continuation statement.

In *In re Kanoff*, 2009 WL 1783521 (Bankr. M.D. Pa. 2009), a Chapter 13 proceeding in which a city contended that it held a security interest in the debtor's liquor license, the bankruptcy court, applying Pennsylvania law, held that the city's security interest was

unperfected on the date the debtor filed, rejecting the city's argument that it had constructive possession of the license. The city perfected its interest in the liquor license by filing a UCC-1 with the appropriate agency. However, the city's interest became unperfected when it failed to file a continuation statement. The liquor license could not be perfected by possession, whether actual or constructive, because it was a general intangible and not goods. General intangibles are not one of the types of property in which a security interest may be perfected by possession.

A loan agreement did not abrogate the first-to-file rule under the circumstances in *In re QuVIS, Inc.*, 2010 WL 2228246 (Bankr. D. Kan. 2010), and thus payments to the noteholders who filed new UCC-1 statements should be made in the order in which each noteholder filed a financing statement, held the court, applying Kansas law. The issue in QuVIS arose from a loan agreement, which contemplated that the debtor would file a financing statement to perfect the noteholders' security interests collectively as it, in fact, did on March 14, 2002. When that financing statement lapsed, however, the noteholders were left to fend for themselves to preserve and perfect their security interest in the assets of the debtor. The loan agreement and the UCC both permitted the noteholders to take those steps. Nothing in the loan agreement, however, purported to alter the general first-to-file priority scheme in Article 9. If the 2002 financing statement had not lapsed, all of the noteholders (perfected under the same financing statement) might have enjoyed the same priority. The noteholders' collective enforcement of their security interest would result in a pro-rata recovery, but when the noteholders as a group became unperfected, and only some of them exercised their right to perfect, they were no longer similarly situated or acting collectively to enforce their rights or remedies under the loan agreement. The pro-rata sharing provision of the loan agreement could only be applied when the noteholders were similarly situated and acting collectively, which was not the case under the existing circumstances.

In *United States ex rel. Solera Constr. v. J.A. Jones Constr. Group*, 2010 WL 1269938 (E.D.N.Y. 2010), a bank had a properly perfected security interest in the debtor's assets, which lapsed when the bank's financing statement was not continued. The bank thereafter filed an effective financing statement. A judgment creditor issued a levy during the time between the bank's filings, but the levy was returned with no assets found. The court ruled that the judgment creditor's rights were not perfected by the levy, so the bank's re-filed financing statement gave it priority under Article 9's general, "first-to-file" priority rule.

In Travel Express Aviation Maintenance, Inc. v. Bridgewiew Bank Group, 2011 WL 190415 (Ill. App. Ct. 2d Dist. 2011), the court, applying Illinois law, held that a creditor that perfected its security interest in an aircraft by recording its security agreement with the Federal Aviation Administration (FAA) in accordance with federal law was not required to file a continuation statement to maintain the priority of its lien over liens subsequently acquired by two aircraft maintenance companies that filed their own lien statements with the FAA. Although issues of priority and validity of a security interest remained subject to state law, the U.C.C. provided that the duration and renewal of a security interest perfected under another statute was to be governed by that other statute. Because the federal statute requiring security interests in aircraft to be perfected by filing them with the FAA did not require the filing of a continuation statement to maintain the perfection of the security interest, the creditor's lien retained its priority over the companies' liens, which were later extinguished when the creditor disposed of the

collateral after default by selling the aircraft.

A lender that was granted a security interest in all of a borrower's chattel paper, accounts, notes, instruments, general intangibles, and all related proceeds was entitled to file a second U.C.C.-1 financing statement after its first financing statement inadvertently lapsed, held the court, applying Louisiana law, in *Hancock Bank of Louisiana v. Advocate Financial, LLC*, 2011 WL 94425 (M.D. La. 2011). Article 9 authorized a secured creditor to file as many financing statements as it deemed necessary to perfect its security interest. Further, the loan documents explicitly authorized the lender to file multiple financing statements to perfect its security interest.

"Control" of a deposit or securities account is tricky.

In a civil forfeiture action with a cumbersome style, *U.S. v. Two Bank Accounts Described as Bank Account in Amount of $197,524.99 Bank of America Seattle Washington*, 2009 WL 803615 (D.S.D., 2009), it was held that a creditor's security interest in two corporate bank accounts was unsecured because the creditor did not have control over the accounts. Under Article 9, a security interest in a deposit account can be perfected only by control. Here, the creditor was not the bank with which the deposit account is maintained. Also, there was no evidence of an authenticated agreement indicating that the depository bank was to follow the directions of the creditor in relation to disposition of the corporations' funds. Finally, there was no evidence showing that the creditor became a customer of the bank with respect to the bank accounts. As a result, he did not have a perfected security interest in the bank accounts and the court concluded that he lacked standing to contest the forfeiture of the bank accounts.

The rule that the secured party can be the depositary bank and therefore automatically perfected by control was analyzed in *In re Hawaiian Telecom Communications, Inc.*, 2009 WL 2575663 (Bankr. D. Haw. 2009). In that case, the collateral agent for the benefit of a group of lenders was held to be the "secured party" for purposes of Article 9. § 9-102(a)(72)(E) & cmt. 2(b). However, the collateral agent in that case lacked a control agreement with the depositary bank and, even though the depositary was a member of the lender group, it was not the collateral agent and therefore was not a "secured party."

In *In re Alexander*, 429 B.R. 876 (Bankr. W.D. Ky. 2010), the court, applying Kentucky law, determined that a bank did not have a continuously perfected security interest in certificates of deposits (CDs) issued by its certificate of deposit account registry service (CDARS) and the funds disbursed from them at maturity. The funds used to purchase the CDARS CDs were transferred from the debtor's account with the bank first to another bank and then to the three institutions that issued the CDs. The bank lost control when the funds were transferred to the second bank to complete the CDARS transactions; once the funds left the bank, the bank's security interest no longer applied and its security interest no longer attached.

In *Fifth Third Bank v. Lincoln Financial Securities Corp.*, 2009 WL 2523444 (W.D. Ky. 2009), a securities intermediary breached a control agreement when it reversed trades of securities in the securities account. The control agreement contained waivers of all the securities intermediary's rights to liens, encumbrances, claims and rights of setoff and representations and

warranties by the intermediary regarding the market value of the securities held in the account as of the date of the control agreement. The intermediary reversed the purchases of those securities when the debtor's check for the purchase was returned for insufficient funds.

A judgment creditor levied upon the bank accounts of its judgment debtor in *Full Throttle Films, Inc. v. National Mobile Television, Inc.*, 180 Cal. App. 4th 1438, 103 Cal. Rptr. 3d 560 (2009). A finance company affiliate of the depository bank claimed a prior security interest in the accounts and tendered control agreements to show perfection and at trial the court awarded the finance company priority in the accounts. The court of appeals, however, reversed, finding that the record did not demonstrate that the accounts subject to the finance company's control agreements were the accounts that had been levied, so the control agreements did not establish perfection.

In *In re Montagne*, 418 B.R. 809 (Bankr. D. Vt. 2009), a bankruptcy court applying Vermont law held that the defense under § 9-332(a) (providing transferee of money takes free of security interest, absent collusion with debtor) did not apply in an action in which a secured party alleged that an individual converted a $240,000 check, the proceeds from a sale of cattle by a debtor business who had pledged the livestock to secure a $457,000 loan. Although the individual was a transferee because she was the recipient of the check, she was not a transferee of "money." "Money" is defined as a medium of exchange currency while a check is a negotiable instrument, a draft payable on demand and drawn on a bank. Therefore, concluded the court, the individual's effort to gain the protection of § 9-332, failed.

In *In re Delco Oil, Inc.*, 2010 WL 918058 (11th Cir. 2010), a secured party had a perfected security interest in all the debtor's assets, and objected to debtor's post-petition use of cash collateral. Between the filing of the cash collateral motion and the hearing, the debtor made several payments to a supplier. When the court denied the debtor's motion to use cash collateral, the secured party sought to recover the payments from the supplier. The court agreed with the supplier's argument that it was a transferee of cash and took the payments free of the security interest, under § 9-332, but held that the security interest had been perfected while the funds were in the debtor's deposit account, and the secured party could thus recover the post-petition transfers under the Bankruptcy Code. No control agreement was necessary to perfect, because the funds in the deposit account were proceeds of the original collateral.

In *In re Cumberland Molded Products, LLC*, 431 B.R. 718 (6th Cir. BAP 2010), a Chapter 7 trustee brought an adversary proceeding to avoid a bank's security interest in funds disbursed from the debtor's checking account, including proceeds of accounts receivable deposited in the checking account. The funds were disbursed by the bank post-petition, honoring a check payable to the trustee. The Bankruptcy Appellate Panel held that the trustee could not avoid the bank's security interest, which was properly perfected prior to the petition date, pursuant to her powers as a judicial lien creditor. Under Tennessee's uniform version of § 9-332(b) (which generally eliminates security interests in funds transferred from deposit accounts), the trustee was not a "transferee" but simply received property that was already property of debtor's estate. The bank did not lose or waive its secured claim when it honored the postpetition check made payable to trustee.

Monitor inventory collateral carefully.

In an action by purchasers of a used truck against an auto auction house, which the seller defended by claiming that an owner of a used car dealership breached an inventory financing agreement with the auction house by selling the used truck to a secured dealership without informing the auction house of the sale or repaying the auction house for the truck, the court, applying Indiana law, held that the second dealership and the purchaser of the truck from that dealership were buyers in ordinary course of business, because they had no knowledge that the sale of the truck violated the auction house's rights. *Indianapolis Car Exchange, Inc. v. Alderson,* 910 N.E.2d 802 (Ind. App. 2009). For a buyer to take free of a security interest created by the seller, the buyer may have knowledge that the security interest exists but may not have knowledge that the sale violates the rights of another person. Here, the second used car dealership had no knowledge of the details of the first used car dealership's financial arrangements, even though it understood that the auction house financially backed that dealership in some fashion. This was true even though the sale took place at another auction after the first auction ended, because it was the first used car dealership's subsequent failure to pay the auction house, not the sale of the truck, that violated the auction house's rights.

What about sales of non-inventory collateral?

The court in *Metropolitan Bank & Trust Co. v. Desert Valley Financial LLC*, 359 Fed. Appx. 764 (9th Cir. 2009), applying California law, held that another bank's knowledge of a creditor's security interest was not attributable to a bank that sought to establish a defense under § 9-308(a). The bank needed to prove that, without its own actual knowledge of a creditor's security interest, it gave new value for mobile home loan contracts and took possession of the contracts in the ordinary course of its business.

A bank holding a first-in-time filing against the accounts receivable of a Chapter 11 debtor, and thus a senior security interest, had not authorized the sale of the account receivables free of its security interest, held the Third Circuit, applying New Jersey law. *In re Jersey Tractor Trailer Training Inc.*, 580 F.3d 147 (3d Cir. 2009). After the bank perfected its security interest, the debtor made an agreement with a factoring company to sell the rights to its accounts receivable in return for a 61.5% up-front payment of the amount due on the particular account receivable. The factoring company filed a UCC-1 statement describing its lien on all the debtor's present and after-acquired accounts receivable. The court found no merit in the factoring company's contention that because the security agreement accompanying the loan did not expressly prohibit the sale of collateral, the bank waived its security interest. The debtor's sale of its accounts receivable thus ran afoul of the security agreement. The court was receptive to the factoring company's alternative argument that the bank, in its course of dealing, implicitly waived its security interest, in that the bank had knowledge of the factoring agreement and had approved of the agreement to the extent that it surrendered its security interest in the accounts receivable. However, even assuming that knowledge, there was a substantial difference between the bank's knowing of the sale of the accounts receivable and its authorizing the sale "free of its security interest." Consistent with § 9-315(a)(1), the court looked for evidence that the bank implicitly authorized the sale of the accounts receivable free and clear of its security interest. In so doing, the court hewed to the theory underlying § 9-315(a)(1) that a security interest would be

meaningless if the secured party could not reach the collateral in the hands of a third party when the debtor disposed of it without authorization. Because § 9-315(a)(1) does not require a secured party to act to preserve its security interest, inaction alone could not lead to a finding of implied authorization. Acts of implied authorization must unequivocally demonstrate an intent to waive the security interest.

Movement of collateral to a new state:

In *In re Owen*, 2009 WL 2145705 (Bankr. D. Idaho 2009), a preference-avoidance action involving a security interest in a motor vehicle, the court held that a creditor's security interest was still perfected when debtors filed their bankruptcy petition after their move to a different state. §§ 9-303 and 9-316 provide for the continued perfection of goods previously titled in one state after they become covered by a certificate of title in another state. At the time that the debtors moved to Idaho, the vehicle was subject to a perfected security interest in favor of the creditor under California law. That interest and its effective date were reflected on the electronic California title, and the parties agreed that the creditor was perfected under California law. The debtors applied for an Idaho certificate of title. The vehicle became covered in Idaho when an application and fees were tendered to the Idaho authorities. The creditor's security interest did not become unperfected upon the vehicle becoming covered by the Idaho certificate of title.

Other Article 9 Perfection and Priority Issues

Lender's security interest in accounts receivable was superior to state's tax liens

A lender's perfected security interest in borrowers' accounts receivable was superior to tax liens that were subsequently filed by the state against some of the same accounts, held the court, applying Mississippi law, in *Nabers v. Morgan*, 2011 WL 359069 (S.D. Miss. 2011). Accordingly, the state was required to turn over to the receiver for the borrowers any proceeds from the accounts that it had collected pursuant to distress warrants that were issued to the account debtors. Article 9 gave the first security interest to be perfected priority over any subsequently perfected security interests, and there was no authority for treating the tax liens differently than any other perfected security interest. Because the lender's security interest was perfected nearly four years before the tax lien was filed, the lender had priority.

Just saying it doesn't make it so.

The debtor in a bankruptcy in the Southern District of Florida had signed a security agreement including the representation or warranty that the security interest was perfected. *In re W.B. Care Center*, LLC, 419 B.R. 62 (Bank. S.D. Fla. 2009). However, the court ruled that, although the parties may say whatever they wish to in an agreement between the two of them, such representations or warranties cannot change the public notice requirements for perfection.

Beware of delay in perfection of security interest in titled vehicle.

Under Tennessee law, a creditor's security interest in a motor vehicle was held perfected

when the lien application (with appropriate paperwork and fee) was submitted to the clerk, even though the initial certificate of title was lost and a replacement certificate with a lien notation was not issued until almost two years after the application had been submitted. *Fitzpatrick v. Toyota Motor Credit Corp. (In re Hartline)*, 2009 WL 2971762 (Bankr. E.D. Tenn. 2009). This was not a case, however, where the lien had been released and then a new certificate of title was issued, but merely a replacement of the original title. The trustee's reliance on *Still v. First Tenn. Bank, NA.*, 900 S.W.2d 282 (Tenn. 1995), was misplaced, because that decision had been was subsequently overruled by amendments to the certificate of title statute. But see *Brock v. Branch Banking & Trust Co. (In re Johnson)*, 380 B.R. 455 (BAP 6th Cir. 2007) (applying Kentucky law, the purchase money security interest not "perfected" on date that county clerk received title lien statement, application for certificate of title and required filing fee); *Fidelity Financial Services, Inc. v. Fink*, 522 U.S. 211, 118 S. Ct. 651, 139 L. Ed. 2d 571 (1998) (holding perfection after 20-day grace period allowed in preference definition, § 547(e), could be avoided as preferential, even if state law allows longer period in which perfection could "relate back"); *Hepner v. AmeriCredit Financial Services, Inc. (In re Baker)*, 338 B.R. 470 (Bankr. D. Colo. 2005).

How not to deal with a senior lender:

In *In re Nat. Gas Distributors, LLC*, 2009 WL 1954836 (Bankr. E.D.N.C. 2009), a bankruptcy trustee sought a determination of the extent, validity, and relative priority of the claims of a supplier of natural gas and a bank with respect to an account receivable. The court applied North Carolina law to decide that a direction to pay, which provided that a debtor agreed to direct to the supplier all payments which it was entitled to receive from a buyer, created at most a security interest in the receivable and, because it was entered after the bank's security interest in accounts receivable was perfected, that security interest was subordinate to the bank's claim. In addition, the supplier failed to perfect its security interest in the receivable and, although the bank's lien was on record, failed to negotiate a subordination agreement with the bank. Because the supplier's security interest was unperfected on the petition date, both the trustee's and the supplier's interest were subordinate to the properly perfected security interest held by the bank.

A bank's security interest in a Chapter 7 debtor's assets had priority as to all indebtedness of the debtor to the bank over that of another secured creditor, held a Connecticut court in *In re Lombardo's Ravioli Kitchen, Inc.*, 2009 WL 3257492 (Bankr. D. Conn. 2009). The bank, as the first to file, had priority as to any security interests it then had, or subsequently obtained, in the collateral. Loans were made in both 2006 and 2007. The bank's security agreements included after-acquired property clauses that were not limited to future advances arising out of the 2006 loans. The priority of the bank's security interest was determined from the date of its original UCC-1 filing in 2006, regardless of the dates on which the advances were actually made. § 9-322(a)(1). A secured party takes subject to all advances (past and future) secured by a competing security interest having priority.

Security Interests in Unusual Collateral:

The UCC did not override the conclusion that a 2001 general indemnity agreement and a 2004 financing agreement could not have assigned a construction company's tort claims against a bank officer and a bank because the construction company's tort claims were not filed until 2007. *Conerly Corporation v. Regions Bank*, 2009 WL 3447264 (E.D. La. 2009)). Under Louisiana law, a tort claim may be assigned only after it has been filed by the tort victim. The construction company asserted that it relied on alleged representations that the bank would pay for all work done on a development. The bank argued that the construction company lacked standing because it had assigned its contract claims to a bonding company. The court recognized a potential distinction between the assignment of personal injury tort claims and commercial tort claims but said that that distinction "[went] nowhere" in this case. Louisiana has not adopted the UCC definition of commercial tort claim, suggesting that commercial tort claims were treated no differently than all other tort claims. However, even if the Louisiana UCC did treat commercial torts separately, this would not change the result in this case. Official Comment 5(g) to § 9-102 clarifies that "[a]lthough security interests in commercial tort claims are within its scope, this Article [9] does not override other applicable law restricting the assignability of a tort claim."

An equipment lessor's security interest, perfected in January, had priority over a construction company's interest as a lien creditor, which attached in May, held the court in *Metro Construction Co., LLC v. Sim Attractions, LLC*, 2009 WL 1605558 (Tenn. App. 2009). This dispute revolved around a race car simulator installed by the construction company in a retail leasehold, which was rented to and abandoned by the lessee. Generally (subject to exceptions not present here), Tennessee adheres to the "first to file or perfect" rule to determine priority. A perfected security interest takes priority over a subsequent lien creditor. The construction company did not become a lien creditor before the equipment lessor perfected its security interest or before the conditions specified in § 9-203(b)(3) were met.

Fixtures and Accessions:

A group of debtors' mortgage lenders had a valid and perfected security interest in the debtors' fixtures attached to encumbered real property under Hawaii law. *In re Hawaiian Telcom Communications, Inc.*, 2009 WL 2575663 (Bankr. D. Haw. 2009). The amended mortgage specifically included fixtures affixed to or located on the encumbered real property as collateral subject to security interests in favor of the collateral agent. The amended mortgage was properly recorded in the Hawai'i Bureau of Conveyances and was therefore a valid fixture filing.

When a bank perfected its interest in trucks via certificate of title notations, the court ruled that it gained a priority interest in the collateral over any party, including a creditor who took 186 tires, rims, and a related amount of lug nuts from trucks on the debtor's property, who may have had a perfected interest in accessions alone. *1st Source Bank v. Best-One Tire of Crossville, Inc.*, 2009 WL 2170167 (E.D. Tenn. 2009). A security interest in an accession is subordinate to a security interest in the whole that is perfected by compliance with the requirements of a certificate-of-title statute. Here, the tires, rims, and lugs nuts constituted accessions because they were physically united with the trucks in such a manner that their identity was not lost. Because the bank held an attached security interest in the accessions, the

notation on the trucks' certificates of title established the bank's first priority in the collateral over any claims to the collateral that the creditor might assert (assuming that it held a perfected interest).

Documenting Purchase-Money Security Interests:

In *In re Johnson*, 2009 WL 962193 (Bankr. E.D.N.C. 2009), the court applied North Carolina law in deciding that a business equipment finance provider held a purchase-money security interest in a log feller buncher. The debtor did not dispute that he executed a note, bill of sale, or other documents. The debtor also failed to provide any contradictory documentary evidence that a seller sold him the equipment prior to the execution of the agreements with the finance provider. The amount of the bill of sale was consistent with the terms of the note. The debtor testified that he was making one payment to the seller for three pieces of equipment, thus resulting in a pro-rata amount being distributed to each of the three lenders at the time the debtor executed the financing documents.

How not to terminate a UCC filing:

The court in *In re S.J. Cox Enterprises, Inc.*, 2009 WL 939573 (Bankr. E.D. Ky. 2009), held that a bank employee's unauthorized termination of a UCC-1 financing statement filed by another bank to perfect its blanket security interest in equipment of a debtor was wrongful. Under Kentucky's §§ 9-509, 9-511, and 9-513, the only party authorized to file a termination statement is the secured party of record and the employee's bank was not the secured party of record on this financing statement.

Other Article 9 Remedies Issues

Borrower's ownership interest in deposit account was not divested

In *Davis Forestry Products, Inc. v. Downeast Power Co., LLC*, 2011 ME 10, 2011 WL 82179 (Me. 2011), the court, applying Maine law, held that a lender's purchase at an auction, conducted after a borrower defaulted on its loan obligations, of the collateral securing the loan and the lender's subsequent sale of the collateral to one of its subsidiaries did not divest the borrower of its ownership interest in a deposit account that was part of the collateral. Thus the purchase and sale did not prevent a third party that obtained a default judgment against the borrower in an unrelated contract action from attaching the account as a lien creditor. The self-help remedies provided by Article 9 to the holder of a security interest in a deposit account required the secured party to perfect its interest by obtaining control of the account, and neither the lender nor its subsidiary ever obtained control of the borrower's deposit account.

Election of Remedies; Administrative Remedies:

A creditor was entitled to reduce its claim to judgment and foreclose upon the equipment simultaneously, held the court, applying Connecticut law, in *General Electric Capital Corp. v. John Carlo, Inc.*, 2010 WL 3937313 (E.D. Mich. 2010). The security agreement provided that

"[a]fter default, [the creditor] shall have all of the rights and remedies of a Secured Party under the Uniform Commercial Code, and under any other applicable law." The security agreement further provided that, upon default, the creditor has the right to sell, lease, or otherwise dispose of the collateral. The agreement also expressly stated that the creditor's "rights and remedies under this Agreement or otherwise arising are cumulative and may be exercise singularly or concurrently." The U.C.C. contains similar language. Under U.C.C. § 9-601(a)[Rev], a "secured party: (1) May reduce a claim to judgment, foreclose or otherwise enforce the claim [or] security interest ... by any available judicial procedure." U.C.C. § 9-601(c) provides that "[t]he rights under subsections (a) and (b) are cumulative and, except as may otherwise be prohibited under other law in a consumer transaction, may be exercised simultaneously." The statutory and contractual language was clear. The creditor could foreclose upon the collateral (which it had) and seek a judgment simultaneously, as long as it was acting in good faith. When it disposes of the collateral, it must credit the amount received against the amount of the judgment.

In *Okefenokee Aircraft, Inc. v. PrimeSouth Bank*, 2009 WL 724113 (Ga. App. 2009), it was held that a secured creditor (a bank) could retain the debtors' collateral (an airplane), while seeking an independent action for money judgment on a promissory note. The debtors did not file a counterclaim or otherwise present evidence that the bank's handling or disposition of the airplane was commercially unreasonable beyond asserting that the bank's act of repossessing and not disposing of the collateral itself gave rise to a factual issue as to the reasonableness of its conduct. The law authorized the bank to repossess and retain the collateral while at the same time seeking a money judgment for the full amount of the outstanding debt. The UCC expressly states that the rights and remedies of a secured creditor are cumulative and may be exercised simultaneously. The questions of whether the bank acted in a commercially reasonable manner, and whether the debtors would owe the bank a deficiency judgment if the bank disposed of the collateral, were not before the court. The only issue was whether the bank was entitled to a money judgment in the full amount of the indebtedness of the note, which received an affirmative answer.

Similarly, in *SunTrust Equipment Finance & Leasing Corp. v. A&E Salvage, Inc.*, 2009 WL 3584333 (E.D. Tenn. 2009), a lender repossessed its collateral and then sued a corporate borrower and its guarantors on a loan. The guarantors argued that the bank had elected its remedy upon repossession, but the court held that the lender was free to pursue the collateral and the guarantors at the same time.

In an action by secured parties against a state university system, which was an account debtor, alleging that it violated § 9-406(a) by making a check payable to the debtor only and by mailing the check to the debtor instead of the secured parties, a court in Maryland affirmed a dismissal of the secured parties' complaint. *University System of Maryland v. Mooney,* 407 Md. 390, 966 A.2d 418 (2009). The secured parties were required to exhaust their administrative remedies against the state before invoking judicial remedies.

Breach of Peace:

A reasonable factfinder could conclude that a breach of the peace occurred, held the court, applying Ohio law, in *Ford Motor Credit Co. v. Ryan*, 2010 WL 3783156 (Ohio Ct. App.

10th Dist. Franklin County 2010). A repossession of a vehicle occurred over the debtor's objection. On January 12, 2006, at approximately 8:15 a.m., the debtor was dressing when his wife told him that someone with a tow truck was in their carport. He went out to the carport and found an agent of the repossessor hooking the vehicle to his tow truck. The debtor told the agent to stop, unhook the vehicle, and leave the premises because he was trespassing. He then reached down to unhook the vehicle, and the agent grabbed his hands, pushed him, and began screaming at him. According to the debtor, the agent screamed that, "I'm going to make your neighbors know about what you're doing[;] you rich bastard, I got you." At that point, the debtor began pushing back and yelling. He eventually backed away, and the agent towed the vehicle away.

Notice of Sale:

Under Indiana law, a notice that informed a guarantor that a creditor intended to sell an excavator through a public Internet auction Web site satisfied the location requirement in § 9-613(1)(e). *Moore v. Wells Fargo*, 903 N.E.2d 525 (Ind. App. 2009). Although the notice listed the date and Web address for the auction and the physical address of the auction company. The auction had no physical location and was not a situs in the traditional sense. However, the court held that the Web address and the physical address of the auction company adequately apprised the guarantor where the auction would be held, allowing him to monitor or even participate in the auction.

Commercial Reasonableness; Amount of Deficiency:

In *Center Capital Corp. v. PRA Aviation, LLC*, 2011 WL 880451 (E.D. Pa. 2011), judgment entered, 2011 WL 867516 (E.D. Pa. 2011), the court, applying Connecticut law, held that a debtor whose aircraft was repossessed and sold by a secured creditor was entitled to no greater credit against its debt than the net proceeds from the sale, despite the debtor's contention that the aircraft was worth considerably more than the sale price. The sale had previously been determined to have been commercially reasonable, thereby entitling the creditor to recover the entire deficiency from the debtor.

A seller did not establish the commercial reasonableness of its sales of industrial earthmoving equipment to third parties after the seller repossessed the equipment following the original buyer's alleged breach of the terms of a promissory note, held the court, applying Florida law, in *Southern Developers & Earthmoving, Inc. v. Caterpillar Financial Services Corp.*, 2011 WL 637332 (Fla. Dist. Ct. App. 2d Dist. 2011). Thus the seller was not entitled to a deficiency judgment against the buyer. The seller did not submit the purchase contract for any of the pieces of the repossessed equipment or any information to establish the sale price obtained for any single piece. The seller, which sold the repossessed equipment at a private sale and an Internet auction, did not submit any evidence to support its implied assertion that the prices obtained through those means were higher than it could have obtained by selling the equipment through other means. Further, the seller did not submit any evidence regarding how contracts for the sale of used industrial earthmoving equipment were customarily reached within the industry and whether private sales and Internet auctions were commonly used.

In *Center Capital Corp. v. PRA Aviation, LLC*, 2011 WL 442107 (E.D. Pa. 2011), the

court, applying Connecticut law, held that a secured lender's sale of a repossessed aircraft after the original buyer and its guarantor defaulted on the loan for the purchase was commercially reasonable. The aircraft was sold by a reputable broker in a manner consistent with standard industry practice. The broker aggressively marketed the aircraft for a few months, rejected two low bids, and sold the aircraft for the best offer that it received.

In *SLT Dealer Group, LTD. v. AmeriCredit Financial Services, Inc.*, 2011 WL 662717 (Tex. App. Houston 1st Dist. 2011), the court, applying Texas law, held that an automobile-financing company that allegedly allowed a vehicle to be sold pursuant to a mechanic's lien and allegedly failed to obtain any value for the vehicle, which was the subject of a retail installment contract that the company had purchased from an automobile dealer under a separate contract between them, was not bound by Article 2's provision that every aspect of a disposition of collateral must be commercially reasonable. An unrelated third party placed the mechanic's lien on the vehicle to secure the cost of repairs, and the company did not possess or dispose of the vehicle. The duty of commercial reasonableness did not apply to a creditor that did not possess or dispose of collateral.

Absent opinion evidence, a bank failed to prove the fair and reasonable value of the debtors' car at the time of the repossession or of the sale, and as a consequence, it failed to prove that the value of the car at the time of the sale was less than the remaining debt owed by the debtors under the loan, held the court, applying Georgia law. The bank's collection manager's affidavit and the accompanying documents showed only the sale price of the collateral. Thus they were insufficient to establish the fair and reasonable value of the collateral. Although the record contained two documents appraising the car, neither of those appraisals contained the sworn opinion testimony of a witness who stated the basis for his or her opinion or who opined that the appraised value of the car was its "fair and reasonable" value in that particular market at the time of either the repossession or of the sale. *Versey v. Citizens Trust Bank*, 2010 WL 4009662 (Ga. Ct. App. 2010).

In *John Deere Construction & Forestry Company v. Mark Merritt Construction, Inc.*, 297 Ga. App. 743, 678 S.E.2d 183 (2009), the court ruled that a creditor met its burden of showing the value of construction equipment at the time of its repossession by submitting an affidavit that the sales prices were fair and reasonable based on the affiant's experience obtained in working for the creditor in various capacities and his review of files that stated the price of such equipment by year, make, and model; the then-existing condition of the equipment; and his knowledge of published resale values for similar used equipment. There was no evidence of any change in the condition of the collateral between the time of its repossession and sale or that the witness giving an opinion on value had not examined the repossessed equipment, but even if he had not personally inspected it, such a witness can base his opinion on hearsay so long as he has had an opportunity to form a correct opinion.

A secured party may purchase collateral at a public auction. Thus, it was held in *Commercial Credit Group, Inc. v. Falcon Equipment, LLC of Jax*, 2010 WL 144101 (W.D.N.C. 2010), a diversity action arising out of a series of loans that a commercial equipment finance company made to a limited liability company and a corporation that dealt in heavy equipment machinery for the purchase of construction equipment, that the finance company's purchase of

the repossessed collateral by bidding on it and buying it at a public auction was commercially reasonable under Delaware law. The debtors asserted that it was not commercially reasonable because the finance company did not prove the value of the collateral at the time of repossession. A low price suggests that a court should scrutinize carefully all aspects of a disposition, but the debtors here had not offered proof that the price obtained was low. Moreover, they benefited from receiving credit against the amount owed under the note; if the finance company had not bid at the public auction, the repossessed collateral would have sold for less, and the debtors would have received less credit.

A creditor was not barred from recovering a deficiency judgment from a guarantor even if the creditor's failure to give notice of the disposition of collateral was commercially unreasonable, because Maryland has adopted Article 9's "rebuttable presumption" rule. *CapitalSource Finance, LLC v. Delco Oil, Inc.*, 608 F. Supp. 2d 655 (D. Md. 2009). The creditor sued a petroleum products distributor for breach of a loan agreement and the distributor's president and sole shareholder for breach of a guaranty agreement. While a commercially reasonable disposition of collateral was required, a commercially unreasonable sale would not necessarily result in an absolute bar to a deficiency judgment. Under the rebuttable presumption rule, the debtor or obligor was to be credited with the greater of the actual proceeds of the disposition or the proceeds that would have been realized had the secured party complied with the relevant provision. If a deficiency remained, the secured party was entitled to recover it. The rebuttable presumption rule represents a fair accommodation between the legitimate interests of the debtor and the residual interests of even a creditor whose actions had not necessarily been commercially reasonable and is, therefore, the preferred approach.

In *Key Equipment Finance, Inc. v. Hawkins*, 2009 Me. 117, 985 A.2d 1139 (Me. 2009), an action by an equipment financer seeking to recover a deficiency from a personal guarantor, the court applied New York law to hold that the sale was commercially reasonable per se pursuant to § 9-627(c)(l), because the guarantor had an opportunity to participate in the disposition of the equipment. The bankruptcy court's sale order was approved as part of a judicial proceeding, in which the guarantor was involved, including the equipment sale, as a corporate officer, not as an individual party, and his potential liability stemmed from his personal guarantee. He argued, therefore, that he did not have an opportunity to participate in the disposition of the equipment. However, he had an opportunity to participate as an individual in the disposition of the equipment. The court also concluded that the sale order was sufficiently complete so as to satisfy the requirement that all sale terms be set and pass through a "judicial filter."

Where a creditor that repossessed and sold an inoperable recycler at a public auction sought a deficiency judgment against a debtor for $128,168 plus interest and attorney's fees, the auction price of $100,000 was not a sufficient valuation of the collateral. *Commercial Credit Group, Inc. v. Barber*, 682 S.E.2d 760 (N.C. App. 2009). The court acknowledged that the fact that a greater amount could have been obtained by a disposition occurring at a different time or in a different method from that selected by the creditor was not of itself sufficient to preclude the creditor from establishing that the disposition was made in a commercially reasonable manner. However, while § 9-627(a) hindered second-guessing the creditor subsequent to a sale of collateral, it did not give him unbridled discretion. The court identified three factors to consider:

(1) the price reflected by price handbooks; (2) the fair market value of the collateral; and (3) the price received on a second resale. Because the creditor offered no evidence of the price as reflected by price handbooks or fair market value, the court was left with the debtor's purchase price, $225,000, and the recycler's second resale price, $190,000, to gauge commercial reasonableness. Even assuming that the creditor's estimated $65,000 engine repair cost was accurate, those repairs were apparently not a factor in the creditor's private sale where the recycler sold for $190,000. The gross disparity between the second resale private price and the creditor's winning bid, combined with commercially unreasonable advertising methods, demonstrated that the auction price was not reasonable.

In *Lyon Financial Services, Inc. v. Oxford Maxillofacial Surgery, Inc.*, 2009 WL 2170999 (D. Minn. 2009), the court, applying Minnesota law, found that a finance lessor of medical laser equipment had not provided sufficient evidence to establish the commercial reasonableness of the sale of the laser as a matter of law. There remained a genuine issue of material fact as to whether the finance lessor had reasonably mitigated its damages. The laser was sold for 6% of its original value, whereas similar lasers had been offered for sale at significantly higher prices. The low price suggested that the court should scrutinize carefully all aspects of a disposition. The finance lessor offered the laser for sale to the highest bidder. Prior to the offering, it asked the lessee, a facial surgery practice, by letter, whether the lessee knew some other business that might be interested in the laser or if the lessee had any suggestions to help the lessor obtain the maximum price. It did not sell the laser in a "recognized market" because a recognized market is one where prices are not subject to individual negotiation. It did not provide the court with information indicating the current market price at the time of sale or that the private sale was in conformity with reasonable commercial practices among dealers of medical equipment. Given this lack of information, the court could not conclude that the sale was commercially reasonable. That the finance lessor followed its usual resale practices did not, in and of itself, render the sale commercially reasonable, and the fact that it requested resale assistance from the lessee and a guarantor did not absolve it of its duty to mitigate damages.

In *Textron Financial Corp. v. Lentine Marine Inc.*, 630 F. Supp. 2d 1352 (S.D. Fla. 2009), the court ruled that a secured party that financed a marine dealer's acquisition of new inventory did not meet its burden to prove commercial reasonableness or fair market value. The secured party recovered a portion of the cost of 66 items of a marine dealer's inventory either by selling them back to their manufacturers or by reselling them through other local dealers. An affidavit by the secured party's vice-president stated that 28 of the items were sold back to the manufacturers pursuant to contractual agreements for more than retail market prices; however, it provided no facts about these contracts or about how such contracts were generally formulated in the marine retail business, nor any evidence, aside from the opinion of its vice-president, that the prices it had obtained were higher than retail market prices. Although the finance company submitted affidavits from representatives of two local marine dealers stating that, based on their experience, the prices reflected fair market value, the affidavits lacked specific factual information that would permit the court to find that the sales conformed to reasonable commercial practices among marine dealers, that every aspect of them was commercially reasonable or that the prices represented fair market value.

An assignee of a lessor of tanning equipment was not entitled to a deficiency judgment against a guarantor because the assignee did not meet its burden to show that, if it had complied with the notice provisions, the amount of proceeds from such a disposition would have been less than the amount of its secured obligation. *C&J Leasing Corp. v. Beasley Investments, Inc.*, 767 N.W.2d 420 (Iowa App. 2009). The court noted that the adoption of Article 9 resolved the ambiguities in former § 9-507(1) regarding the effect of a secured creditor's noncompliance with the statute upon the creditor's claim to a deficiency judgment, by explicitly adopting the "rebuttable presumption" rule. It rejected the guarantor's assertion that the absolute-bar rule was still good law in Iowa. The guarantor testified, however, that had he been given proper notice, he would have cured the default and there would be no deficiency. The assignee neither presented evidence to contradict that evidence, showed what a complying disposition would have yielded, showed what the tanning equipment's fair market value would be nor submitted any appraisal as to its fair market value. It simply opined that the price received for it was commercially reasonable. The guarantor was not, required by the court to show that the price obtained for the equipment fell significantly below the range of prices a complying disposition would have brought because the disposition was to a person related to a secondary obligor.

Punitive damages for retaliatory repossession were appropriate under the unusual circumstances in *Scott v. Houston*, 2010 WL 680984 (Tenn. Ct. App. 2010). The individual debtor's employer ran a gambling ring and financed the employee's purchase of a car through an affiliate. When she cooperated with the state in criminal prosecution against the employer, the affiliate repossessed and foreclosed on her car, even though she had paid all the principal and interest, arguing that she had not paid late fees (which had not been charged), and demanded that she pay off a relative's car loan too.

Regions Bank v. Trailer Source, 2010 WL 2074590 (Tenn. Ct. App. 2010) is a complicated decision dealing with the obligation to conduct a commercially reasonable sale of collateral. The court held that (1) the obligation benefits an unperfected junior secured party, even though the junior secured party would not be entitled to notice of sale under § 9-611, and (2) the commercial reasonableness requirement in § 9-610 applied to the senior secured party, even though the collateral was actually sold by the debtor and was never in the secured party's possession. The court noted that the test was not whether the collateral was in the secured party's possession, but whether the secured party was in control of the sale. In this case, under several "unique" factors, the senior lender had "leveraged" its position to control the sale and obtain the proceeds. The court made a point of saying, however, that the rule might be different in the case of a simple release of a lien upon sale by a debtor, and finally ruled that the bank's approval of the sale, arranged by the debtor, was not commercially unreasonable.

Secured Party as Purchaser:

In *Sky Technologies LLC v. SAP* AG, 576 F.3d 1374 (Fed. Cir. 2009, cert. denied 2010), a patent-infringement action, a secured party was held to have obtained title to the patents because it foreclosed on the patents-in-suit in conformity with the Massachusetts UCC and the security agreement. The secured party disposed of the collateral through a public auction and purchased the collateral at the same auction. Therefore, the court held, consistent with §§ 9-610 and 9-617, the secured party received all of the owner's rights in the collateral, making it the

titleholder of the patents-in-suit after foreclosure and when it assigned the patents-in-suit to a third party, the assignee became vested with all rights, title, and interest in the patents. The chain of title had not been broken from the owner to the assignee, giving it standing to bring the patent infringement suit.

Secured parties, assignees and third-party obligors:

In *Summit Financial Resources LP v. Kathy's General Store, Inc.*, 2010 WL 1816685 (D. Kan. 2010), Kathy's was a combination service station and retailer. Kathy's regularly purchased motor fuel from a supplier, and pre-paid the supplier by depositing credit card proceeds into the supplier's bank account, generally resulting in a credit balance in favor of Kathy's. When the supplier delivered fuel, it would generate an invoice and offset against the store's credit balance. A factor purchased the supplier's accounts receivable, notified Kathy's and, pursuant to § 9-406, instructed Kathy's to make all payments to the factor. The supplier told Kathy's to ignore the notice, and Kathy's continued depositing credit card proceeds into the supplier's account under the existing pre-payment procedure. The factor sued Kathy's to recover the payments. The court found that Kathy's was not an "account debtor" subject to § 9-406, because it had not incurred any monetary obligation to the supplier. Because Kathy's had prepaid for all fuel delivered, the Supplier never had a right to payment that could be assigned to the factor.

The interests of an assignee of an account derives from the assignor-debtor. Thus, in *Ta Chong Bank Ltd. v. Hitachi High Techs. Am., Inc.*, 610 F.3d 1063 (9th Cir. 2010), the assignee had no right to collect directly from an account debtor after the assignor's claim against account debtor had been discharged in bankruptcy.

In *Regions Bank v. Wyndham Hotel Mgmt. Inc.*, 2010 WL 908753 (M.D. Tenn. 2010), a property owner entered into a Hotel Management Agreement ("HMA"), which provided for an operator to manage its property and for exclusive venue in Illinois. The HMA also granted a security interest from the owner to a bank to secure a loan. This security interest was acknowledged by the operator in a Subordination, Nondisturbance and Attornment Agreement among the owner, the operator and the bank. After the project failed, a dispute arose between the bank and the hotel operator as to their respective obligations regarding the property, and the bank sued in federal court in Tennessee. The hotel operator sought dismissal in reliance on the forum selection clause contained in the HMA, to which the bank was not a party. The court dismissed the bank's action, on the basis that a non-signatory to a forum selection clause in a contract may be bound if the non-signatory is so "closely related" to the dispute that it is "foreseeable" that the non-party will be bound by the clause.

Mortgage Issues

Mortgage partially securing rental property subject to modification.

The court discusses the split of authority on modification of a mortgage securing in part the debtor's residence and in part rental property. Rejecting a bright-line rule in favor of totality-of-circumstances, the court looked to the substance of the bargain at the time of the mortgage

transaction, and where the mortgage documents did not require the debtor to occupy the property as a residence, the "predominate character" of the transaction was a commercial loan, permitting the mortgage to be stripped down under § 1322(b)(2). *In re Zaldivar*, 441 B.R. 389 (Bankr. S.D. Fla. 2011).

Security interest in "easements" did not destroy anti-modification protection.

A mortgage including "all improvements. . ., and all easements" was protected from modification by § 1322(b)(2), concluding that under California law an easement is an interest in real property and not a personal property interest. *In re Lopez*, 2010 WL 4875884 (Bankr. N.D. Cal. Nov. 24, 2010) (slip opinion).

Plan must provide that wholly unsecured lien is retained until full payment of discharge.

The court concluded that "allowed secured claim" as used in § 1325(a)(5) must be interpreted the same way as the Supreme Court did for purposes of § 506(d) in *Dewsnup v. Timm*, 502 U.S. 410, 416, 112 S.Ct. 773, 116 L.Ed.2d 903 (1992). In order for § 1322(b)(2) and § 1325(a)(5) "to be sensibly read. . ., the 'secured claim' referenced in § 1322 relates to § 506(a), which focuses on the term 'secured;' and the 'allowed secured claim' referenced in § 1325 is similar to that of § 506(d), which focuses on the term 'allowed' as utilized under § 502. . . Thus, a claim must receive the treatment required under § 1325(a)(5) if it has been allowed under § 502 and is 'secured by a lien with recourse to underlying collateral.' *Dewsnup*, 502 U.S. at 415, 112 S.Ct. 773." Because the mortgage creditor had filed a proof of claim, to which no objection was filed, the claim was allowed under § 502, and the allowed secured claim must conform to § 1325(a)(5)'s requirement that the lien be retrained until the debtor either made full payment or received a discharge. The plan must contain such language, but the wholly unsecured lien may be avoided "upon receipt of a discharge at the completion of the plan." *In re Woolsey*, 438 B.R. 432 (Bankr. D. Utah 2010). See also *In re Trujillo*, 2010 WL 4669095 (Bankr. M.D. Fla. Nov. 10, 2010) (slip opinion) (Debtor ineligible for discharge was unable to strip down mortgage permanently.). Contrast *In re Hill*, 440 B.R. 176 (Bankr. S.D. Cal. 2010) (concluding that § 1325(a)(5)'s lien retention doesn't apply to wholly unsecured mortgages stripped off in plan; debt is unsecured; whether debtor is entitled to discharge or not, wholly unsecured mortgage can be stripped and lien avoided.).

Loan subject to modification could not be paid for longer term than plan.

Although a loan was not protected by § 1322(b)(2) from modification, it may not be crammed down and also paid over a period extending beyond the plan's term. A modified mortgage must be paid within the life of the plan. *In re Valdes*, 2010 WL 3956814 (Bankr. S.D. Fla. Oct. 4, 2010) (slip opinion).

Debtors not entitled to discharge may not satisfy in rem lien on home for less than 100%.

Construing § 1325(a)(5)(B)(i)'s lien retention, debtors ineligible for Chapter 13 discharge because of recent Chapter 7 discharge could not confirm a plan providing for less payment of the underlying in rem debt than nonbankruptcy law would require. The plan proposed to pay $15,000 in return for release of an in rem lien, but the prior Chapter 7 discharge did not strip the lien to its actual value; rather, the in rem lien survived the discharge. The bank "would be entitled under nonbankruptcy law to enforce its in rem judgment against whatever value exists in the residence after completion of the plan and closing of the case." The debtors may propose a plan paying the § 506(a) current value, but the plan may not require release of the lien without paying the full in rem claim. "Because the lien release provision of the plan violates the Bank's right to retain its lien under § 1325(a)(5)(B)(i)(I) until the debt to the Bank is paid or the lien is otherwise extinguished under nonbankruptcy law, the plan should not have been confirmed." *Bank of the Prairie v. Picht (In re Picht)*, 428 B.R. 885 (BAP 10th Cir. 2010).

Mortgage may be modified when it only required debtor's residency for one year.

A mortgage requiring that the debtor use the condominium as a residence for at least one year was not protected from modification, when the debtor had ceased using it as his residence before filing bankruptcy. The anti-modification protection was limited "to, at most, one year (and arguably was not entitled to anti-modification protection at all)." *In re Roemer*, 421 B.R. 23 (Bankr. D.D.C. 2009).

Real property tax purchaser bound by plan's interest rate.

Although the plan provided for an interest rate on property taxes less than would be required under § 511, the plan was not ambiguous and clearly provided the treatment of secured claims, and the plan provided for a Till formula rate, plus 1.5% risk factor. The creditor was bound by the plan's interest rate, when the creditor did not object to confirmation. "The filing of a proof of claim which sets forth an interest rate that is different than that provided by the plan does not trump the rate set forth in the plan absent a timely-file objection to the plan." The proof of claim was not treated as a constructive objection to confirmation. *In re McLemore*, 426 B.R. 728 (Bankr. S.D. Ohio 2010).

Section 1325(b) doesn't apply to postconfirmation modification.

Citing and discussing authority on both sides of the issue, the bankruptcy court concluded that "the only relevant requirements for approval of a [debtor's] motion to modify [a confirmed plan] are set out in § 1325(a)," and § 1325(b) doesn't apply. The trustee had objected to the debtor's motion to modify to reduce monthly payments and reduce the plan term from 60 to 36 months. The debtor had lost income and separated from her husband, and the court found three reasons why § 1325(b) doesn't come into play: (1) § 1325(b)'s language provides it applies only when a party objects to confirmation, and there is only one confirmation—a modification is not a separate confirmation; (2) § 1329 includes § 1325(a) requirements in a postconfirmation modification consideration, but it does not mention § 1325(b); and (3) there is no absurd result

from not applying § 1325(b) to such modifications—here the court stressed that good faith remains a factor to protect from abusive modifications. *In re Davis*, 439 B.R. 863 (Bankr. N.D. Ill. 2010). Contrast *In re King*, 439 B.R. 129 (Bankr. S.D. Ill. 2010) (holding that § 1329(b) does apply to a post-confirmation modification).

Amendment of state statute giving constructive notice applied to all mortgages, whenever recorded.

When the Indiana General Assembly amended its recording statute in 2007 to allow recorded mortgages that contained technical defects to give constructive notice as if they were properly recorded, the legislature intended that amendment to apply to all recorded mortgages, regardless of when they were recorded, as indicated by another amendment in 2008. *Miller v, LaSalle Bank, N.A.*, 595 F.3d 782 (7th Cir. 2010).

Fifth Circuit deals blow to class actions.

Taking a direct appeal from the bankruptcy court, the Fifth Circuit vacated class action certification in Chapter 13 cases where debtors had sued Wells Fargo for charging and/or collecting unauthorized and unreasonable postpetition fees and costs. The disputed charges included attorney fees, recording fees, notification fees, title fees, document fees and property inspection fees. The bankruptcy court certified a class only for the Southern District of Texas, but the Fifth Circuit held that, although the bankruptcy court had jurisdiction to certify a class action, the certification did not satisfy Rule 23(b)(3)'s predominance and superiority requirements nor Rule 23(b)(2)'s injunctive or declaratory standards. "Plaintiff's claims here fail under the predominance and superiority inquiries because individual issues for each class member, particularly with respect to damages, override class concerns when we consider how the case must be tried." The court noted that there was disagreement among bankruptcy courts on the "scope of the requirement under § 506(b) and Rule 2016 for lenders to obtain court approval before assessing contractually allowed fees." The circumstances of fees charged by Wells Fargo vary from debtor to debtor, requiring "an individual assessment of the claims. . . .The differing circumstances of the debtors render the reasonableness of the individual charges a fact-specific inquiry rather than a class-oriented decision. . . .Finally, the rulings of different bankruptcy judges during their cases may affect the computation of allowable charges by Wells Fargo." *Wilborn v. Wells Fargo Bank, N.A. (In re Wilborn)*, 609 F.3d 748 (5th Cir. 2010).

Sanction for Rule 9011 violation reduced.

The First Circuit reduced the monetary sanction against Ameriquest from $250,000 to $5,000, when the sanction was for the mortgage servicer filing documents stating that it was the holder of the note, but it was not. Although the mortgage servicer had a history of questionable practices in bankruptcy, the incorrect filings were not intentional and provided no advantage to Ameriquest. The sanction was limited to actions occurring in the present case, rather than for a pattern in all cases. *Ameriquest Mortgage Co. v. Nosek (In re Nosek)*, 609 F.3d 6 (1st Cir. 2010).

Section 1322(e) applied to undersecured creditor to allow fees and expenses.

An undersecured mortgage creditor is entitled to payment of its fees, expenses and escrow advances that are permitted under the note, mortgage and applicable nonbankruptcy law, with the Sixth Circuit applying the plain language of § 1322(e), which includes "notwithstanding. . .section 506(b)." *Deutsche Bank National Trust Co. v. Tucker*, 621 F.3d 460 (6th Cir. 2010).

Creditor didn't violate Rule 9011 by filing proof of claim without documentation.

In an unusual decision involving whether the appeal was moot, the Sixth Circuit approved a procedure used by B-Line's purchase of claims and filing its proof of claim without copies of original documents to support the debt. The bankruptcy court had threatened sanctions but did not impose any, with the BAP holding that the appeal was moot since no monetary sanctions were imposed. The majority of the Circuit panel held that the appeal was not moot and then held that B-Line acted reasonably when it relied on the warranties of the selling creditor that the debt was supported by legal and valid obligation of the debtor, and B-Line would not be subject to Rule 9011(b) sanctions for its proof of claim practice. *B-Line, LLC v. Wingeter (In re Wingerter),* 594 F.3d 931 (6th Cir. 2010).

Proof of claim errors don't supply FDCPA cause of action.

Adding to the bankruptcy courts holding that errors in the filing of proofs of claim don't support Fair Debt Collection Practices Act violations, the Second Circuit held that the creditor's inflation of its proof of claim did not form a basis for a claim under the FDCPA. In a putative class action, debtors had sued Roundup Funding, LLC and its attorneys for filing inflated proofs of claim, and the district court had granted the defendants' dismissal motion. The Second Circuit commented that "[t]he FDCPA is designed to protect defenseless debtors and to give them remedies against abuse by creditors. There is no need to protect debtors who are already under the protection of the bankruptcy court, and there is no need to supplement the remedies afforded by bankruptcy itself." The Circuit vacated an award of attorney fees to the defendants, because the question of law had been undecided in the Second Circuit prior to this opinion, but noted that the debtors were "careless" in pursuing the district court action; as a result, the Circuit court awarded reasonable costs of the appeal in favor of the defendants. *Simmons v. Roundup Funding, LLC,* 622 F.3d 93 (2d Cir. 2010). *See also Kline v. Mortgage Elec. Security System,* 2010 WL 3786584 (S.D. Ohio, Sept. 28, 2010) (slip opinion) (holding that actions under FDCPA, TILA and Ohio's Consumer Sales Protection Act were pre-empted by Bankruptcy Code, when debtor's causes of action arose from creditor's filing of proof of claim); *In re McMillen,* 440 B.R. 907 (Bankr. N.D. Ga. 2010) (filing duplicative proof of claim not abusive collection practice actionable under FDCPA, applying rationale of *Simmons v. Roundup Funding, LLC*).

Class certified for injunctive relief only.

Applying *Wilborn v. Wells Fargo Bank, N.A. (In re Wilborn)*, 609 F.3d 748 (5th Cir. 2010), class was not certified for damage issues, under Fed. R. Civ. P. 23(b)(3), when

"individualized issues begin to predominate as the Court must consider the harm suffered by each class member on a case-by-case basis," but the class was certified under Fed. R. Civ. P. 23(b)(2) for injunctive relief. Issue involved Countrywide Home Loans's fee collection practices in bankruptcy cases. *Rodriguez v. Countrywide Home Loans, Inc. (In re Rodriguez)*, 432 B.R. 671 (Bankr. S.D. Tex. 2010).

Mortgage securing property partially rental is subject to modification.

Reviewing reported authority, the court adopted the position that the date of the mortgage transaction controls for § 1322(b)(2) purposes. Here, the evidence established that at the time of the mortgage, the debtors lived on one portion of the property but rented the other portion (the two portions had different addresses). The property had never been solely the debtors' principal residence within the meaning of § 1322(b)(2), having always included some income-producing rental property. During the closing process on the mortgage, the lender became aware of the two parcels and their different status, but the loan was closed. The debtors could modify the unprotected mortgage. *In re Moore*, 2010 WL 4791833 (Bankr. N.D.N.Y. Nov. 18, 2010) (slip opinion).

Class action certification denied for lack of typicality and lack of adequacy of representation.

Class certification in a proceeding involving non-disclosure of postpetition fees and expenses by a mortgage creditor was denied, with the court finding that the typicality requirement of Rule 23(a)(3) was not satisfied, and debtors' counsel failed to prove adequacy of counsel; while prior class experience of the attorney was argued, there was no evidence to support it. Moreover, the particular debtors did not establish adequacy as class representatives. There was also expert testimony in the hearing concerning lack of uniformity in procedures concerning disclosure of postpetition fees and expenses. *Sandlin v. Ameriquest Mortgage Co., Inc. (In re Sandlin)*, 2010 WL 4260030 (Bankr. N.D. Ala. Oct. 21, 2010) (slip opinion).

Mortgage provisions not appropriately included in plan.

In an analysis of eight paragraphs of mortgage provisions that the debtor proposed to include in a plan, the court found some inappropriate and some inconsistent with the Bankruptcy Code. Provisions that restate §§ 1322(b)(2) and (5) curing and hypothetically deeming the mortgage current are unnecessary, and if they don't accurately restate the Code, those provisions are inconsistent with the Code. Requiring the mortgage creditor to perform an annual escrow analysis was consistent with RESPA, but going beyond the creditor's duties of RESPA is inappropriate - the debtor has available remedies under RESPA, adversary proceeding or contested matter if the debtor needs information from the creditor during the case. A provision suggesting that plan payment shortfalls would be suffered by non-mortgage creditors violates Code provisions for other secured and adequate protection creditors. Requiring the creditor to file notice with the court before making protective advances, such as for taxes and insurance, was inappropriate, if it resulted in taking away the secured creditor's rights under the contract. Under Eleventh Circuit authority, a secured creditor is not required to file a proof of claim to preserve its security interest in property of the bankruptcy estate, and requiring the filing of an

annual notice of postpetition fees and costs is tantamount to a proof of claim. A provision that a discharge is a determination that all pre- and postpetition defaults have been cured and that the mortgage is current is an improper expansion of the discharge resulting in Chapter 13—such declaratory relief would require an adversary proceeding. Allowing each debtor to formulate plan provisions for mortgage creditors would encourage non-uniformity. The court noted that proposed amended Bankruptcy Rule 3001 and new Rule 3002.1 address many of the concerns that this debtor expressed, and adoption of those Rules would foster uniformity in practice. The opinion quotes the debtor's proposed eight provisions, as well as the "best practices" encouraged by the NACTT and other organizations. *In re Carlton*, 437 B.R. 412 (Bankr. N.D. Ala. 2010).

See Appendices C and D for the text of the proposed amendments to Rule 3001 and new Rule 3002.1, as approved by the Supreme Court April 20, 2011.

Mortgage creditor did not violate § 362(a)(3) by posting of charges.

Posting of postpetition charges and mailing a default notice did not violate the automatic stay, when there was no actual collection activity. Postpetition bookkeeping entries do not violate § 362(a)(3). *Guevara v. Wells Fargo Bank, N.A. (In re Guevara)*, 2010 WL 4102274 (Bankr. S.D. Tex. Oct. 12, 2010) (slip opinion).

Debtor ineligible for discharge may strip wholly unsecured junior mortgage, unless bad faith is found.

Although debtors who were ineligible for discharge may strip off a wholly unsecured junior mortgage, if the only reason for filing Chapter 13 is to strip off the lien that was not avoidable in a prior Chapter 7 case, the Chapter 13 filing would be in bad faith. *In re Tran*, 431 B.R. 230 (Bankr. N.D. Cal. 2010).

Violation of due on sale clause, enforceable under state law, would be impermissible modification of mortgage.

Due on sale clauses in mortgages are enforceable under Texas law. To allow the debtor to retain property in violation of such a clause would be an impermissible mortgage modification, in violation of § 1322(b)(2). *In re Mullin*, 433 B.R. 1 (Bankr. S.D. Tex. 2010).

Modified mortgage must be paid within plan term.

When the debtor proposed to modify a nonresidential mortgage, splitting the claim into secured and unsecured portions, and lowering the interest rate, under § 1322(d) the debtor must pay the modified mortgage in full within the 5-year plan life. A modified mortgage may not be reamortized over a longer term. *In re Russell*, 2010 WL 2671496 (Bankr. E.D. Va. June 30, 2010) (slip opinion).

Stripping of prior wholly unsecured mortgage does not move third mortgage into secured position.

When the wholly unsecured second mortgage was stripped, that action did not move the third mortgage into a secured position, with the court holding that the wholly unsecured third mortgage was void under § 506(d) as a matter of law, since no value existed to support it. *In re Rosas*, 2010 WL 1610123 (Bankr. N.D. Cal. Apr. 20, 2010) (slip opinion).

Stripping wholly unsecured junior mortgage requires adversary proceeding.

Acknowledging a split of authority, the court held that an adversary proceeding is required under Rule 7001(2) to avoid a wholly unsecured mortgage. The creditor may waive that requirement by failure to object to the debtor's avoidance motion, but in the face of objection, the debtor must file an adversary proceeding. *In re Ginther*, 427 B.R. 450 (Bankr. N.D. Ill. 2010).

Local rule requires mortgage creditor to itemize postpetition charges.

Court's local rule 3002 requires mortgage creditor to provide itemized statement of unpaid postpetition charges within 28 days of the debtor's demand. Notwithstanding this rule putting burden on debtor, proposed plan provision requiring creditor to give annual notice of charges during pendency of case is confirmed, as not "too great a burden" for creditor. *In re Teran*, 2010 WL 1655892 (Bankr. E.D. Wis. Apr. 23, 2010) (slip opinion).

Debtor ineligible for discharge cannot strip wholly-unsecured junior mortgage.

In *In re Fenn*, 428 B.R. 494 (Bankr. N.D. Ill. 2010), a junior mortgagee objected to confirmation of debtors' proposed Chapter 13 plan, as improperly providing for strip-off of its lien, in a case filed by debtors who had recently received a Chapter 7 discharge and were statutorily ineligible for discharge in their current Chapter 13 case. The Bankruptcy Court held that the secured claim of the junior mortgagee, whose lien was wholly unsupported by any equity in the property over and above amount of the senior mortgage debt, could be valued at zero for plan confirmation purposes. Any strip-off of a junior mortgage lien cannot occur before the earlier of the payment of the junior mortgage debt in full or the discharge of Chapter 13 debtors, something which, in case of debtors who had recently received a Chapter 7 discharge and were statutorily ineligible for discharge in their current Chapter 13 case, could not occur. Accord *In re Gerardin*, 2011 WL 672050 (Bankr. S.D. Fla. Feb. 9, 2011) (en banc)

Only allowed secured claims are protected by § 1325.

In *In re Frazier*, 2011 WL 96836 (Bankr. E.D. Cal. Jan. 10, 2011), Chapter 13 debtors in another "Chapter 20" case moved to value a creditor's secured claim and the creditor objected to confirmation of debtors' proposed plan. The Bankruptcy Court held that granting or denying of a Chapter 13 discharge is not a basis for the court to deny a motion to value creditor's secured claim. However, the value of the creditor's secured claim was $0.00, precluding its assertion of

rights under provision of plan confirmation statute addressing treatment of secured claims. The court concluded that the plan was proposed in good faith and could be confirmed.

Homeowners' association's lien is subject to stripping.

If the value of property is not sufficient to support lien of homeowners' association, it is subject to being stripped, with the association treated as unsecured. If the association is secured, the debtor's plan proposal to surrender the property would satisfy the secured claim under § 1325(a)(5)(C). *In re Heflin*, 2010 WL 1417776 (Bankr. E.D. Va. Apr. 1, 2010) (slip opinion)

Plan provisions don't violate § 1322(b)(2) or RESPA.

On appeal from plans containing terms that regulate duties of mortgage creditors in Chapter 13, the BAP held that it could not "ban" the local plan forms that had been approved by bankruptcy judges in the Central District of California. The plan terms requiring creditors to provide monthly statements, to give the debtors mortgage payment information upon reasonable written notice, to give the debtor, debtor's attorney and trustee notice of payment increases, did not violate § 1322(b)(2)'s anti-modification. The plan terms did not violate RESPA requirements, nor did RESPA preempt the plan provisions. An appendix to the opinion contains the plan language at issue. *In re Herrera*, 422 B.R. 698 (BAP 9th Cir. 2010).

Reverse mortgage is subject to curing under § 1322(c)(2).

Finding no distinction under the Code concerning reverse mortgages, the court held that a reverse mortgage on the debtor's residence was capable of being cured under § 1322(c)(2), especially when the contract provided for reinstatement after default. *In re Boudreaux*, 2010 WL 724355 (Bankr. E.D. La. Feb. 24, 2010) (slip opinion).

Fraud on court discussed.

Examining prior authorities for factors to find fraud on the court, the bankruptcy court found that a cause of action was stated when the debtor's complaint alleged that the mortgage creditor had a practice of filing false affidavits in support of stay relief motions, and that such a practice, if proven, would be fraud on the court. Among the relevant factors for such a cause of action were "(1) large numbers of motions for relief from the automatic stay are filed; (2) there is only a short period of time to dispose of these motions; (3) there is a huge economic disparity between the resources available to the parties; (4) the subject matter is critical to the debtor's survival; (5) these matters are only rarely litigated to a final order after a hearing on evidence." *In re Woodruff*, 2010 WL 386209 (Bankr. M.D. Ala. Jan. 27, 2010) (slip opinion).

Other Claims Issues

Many other issues involving claims have appeared in cases arising in the recent financial unpleasantness. The following are selected decisions with implications for creditors.

A debtor's compulsory counterclaims can be "non-core."

Counterclaims asserted by a debtor against a creditor in bankruptcy cases are core proceedings under §157(b)(2)(C), which provides "that counterclaims by the estate against persons filing claims against the estate" are core. However, the Ninth Circuit in *Marshall v. Stern (In re Marshall)*, 600 F. 3d 1037 (9th Cir. 2010), cert granted, 131 S. Ct. 63 (2010), held that a state-based counterclaim was non-core. Under the "closely related to" test adopted in Marshall, even compulsory counterclaims must also have common elements and factual proof requirements with the creditor's claim in order to be "core," if they lack a basis for core status under §157(b)(2)(B) or (D) through (N). An Arizona bankruptcy court decision subsequently interpreted Marshall to require only that the claims arise out of the same transaction. *In re Gorilla Companies LLC*, 429 B.R. 308 (Bankr. D. Ariz. 2010).

Claim may now "arise" in the Third Circuit, even if it has not fully "accrued."

The Court of Appeals for the Third Circuit was the only court of appeals to hold that the claim must be fully accrued under applicable law before it arises. The principal case on this point was *Matter of M. Frenville Co., Inc.*, 744 F.2d 332 (3d Cir. 1984) and it was widely criticized and has now been overruled. *Frenville* was sharply criticized by courts and commentators alike. The Third Circuit has now overruled *Frenville* in an environmental case. *Jeld-Wen, Inc.v. Gordon Van Brunt (In re Grossman's Inc.)*, 607 F.3d 114 (3d Cir. 2010). In *Grossman's*, the successor-in-interest to reorganized Chapter 11 debtors brought an adversary proceeding to enjoin prosecution of asbestos-related injury and breach of warranty claims against it, as well as for determination that its liability on these claims had been discharged. Sitting en banc, the Third Circuit held that, for purposes of the Bankruptcy Code, a "claim" arises when an individual is exposed prepetition to a product or other conduct giving rise to an injury, which underlies a "right to payment" under the Code, expressly overruling *Frenville*, so the claimants' tort claims arose prepetition, when the debtors' product allegedly exposed the claimant to asbestos, even though her injury manifested itself postpetition. The Court left open the question of whether the discharge of the claimants' tort claims would comport with due process and remanded that issue for decision by the district court.

Objector must come forward with proof to rebut.

When the debtor fails to come forward with evidence to rebut, the prima facie validity of the proof of claim prevails. *In re Stewart*, 2010 WL 1258213 (9th Cir. Apr. 1, 2010) (unpublished).

Equitable estoppel applied to proof of claim in first case.

Wells Fargo Bank filed a proof of claim in the first Chapter 13 case, but its proof of claim in the second case was inconsistent, with the court applying judicial estoppel to the first proof of claim, preventing Wells Fargo from asserting charges that could have been included in the first claim. Estoppel did not apply to any charges accruing after the first proof of claim was filed, but arrearages and charges that could have been include in the prior claim were barred. *In re Oparaji*, 2010 WL 5462456 (Bankr. S.D. Tex. Dec. 29, 2010) (slip opinion). The opinion reviews the requirements for applying judicial estoppel: the two proofs of claim were clearly inconsistent; the court had accepted the first proof of claim when it approved a plan modification based on that claim's arrearages; and Wells Fargo's "inconsistency was not inadvertent." The fact that the first case was dismissed did not prevent application of judicial estoppels. Section 349 restores property rights but "does not erase all history. . . .[N]othing in § 349 prevents the invocation of judicial estoppels with respect to positions taken in a dismissed bankruptcy."

Debtor's schedules included debt, overcoming technical failures by assignee.

When the Chapter 13 debtor scheduled the original creditor, a pending state court suit and the creditor's attorney, the admissions of the debt overcame the debtor's objections to the proof of claim filed by an assignee. Although the proof of claim did not technically comply with Rules 3001(c) and (f), and even if the proof of claim lacked prima facie validity, the objection did not state grounds for disallowance under § 502(b). In the face of the sworn statements in schedule F and statement of financial affairs, the court questioned a debtor's good faith and "counsel's judgment as guided by Rule 9011." *In re Willis*, 2010 WL 5463066 (Bankr. N.D. Ga. Dec. 26, 2010).

Assignee unable to rely of Bankruptcy Rule to support prima facie validity.

The Chapter 13 debtors objected to a proof of claim filed by the assignee of credit card debt, based on lack of documentation to support the validity and amount of the debt, as well as the assignee's status. Discussing the issues that typically arise in contests concerning proofs of claims filed by assignees, the court held that to satisfy Rule 3001(c) and enjoy prima facie validity, a proof of claim filed by an assignee must have an attached "written assignment or set forth a summary of the assignment," and this proof of claim had neither. The court then discussed conflicting authority on whether there are ways, other than compliance with Rule 3001, to obtain prima facie validity, concluding "that compliance with Rule 3001(f) is not the sole vehicle for a proof of claim to achieve prima facie status." The issue is whether the "non-conforming" proof of claim shifts the burden of production to the objecting party, on which a case-by-case determination is required, considering, for example, the debtor's schedules and whether the debt is listed in the same approximate amount as the proof of claim. Although these debtors' schedules did include this debt in an amount correlating to the proof of claim, there was nothing in the record to support the assignee status of the claimant, and the proof of claim was disallowed. *In re O'Brien*, 440 B.R. 654 (Bankr. E.D. Pa. 2010).

Mortgage note not properly endorsed to transferee and not in transferee's possession did not support proof of claim.

Defects in the assignment and transfer of a mortgage note made the note unenforceable under New Jersey's UCC, and the debtor's objection to the proof of claim was sustained. The opinion discusses "holder" and "nonholder," both "in possession" and "not in possession." *In re Kemp*, 2010 WL 4777625 (Bankr. D.N.J. Nov. 16, 2010) (slip opinion).

Arbitration denied in dispute over amount of claim.

The creditor's motion to compel arbitration was denied, when the dispute involved the amount of the proof of claim, with the court holding that an inherent conflict existed between enforcing the parties' arbitration agreement and the remedies and purposes of the Bankruptcy Code. *Yarbrough v. Green Tree Servicing, LLC (In re Yarbrough)*, 2010 WL 3885046 (Bankr. M.D. Ala. Sept. 29, 2010) (slip opinion). See also *Rushing v. Green Tree Servicing, LLC (In re Rushing)*, 2010 WL 3943962 (Bankr. E.D. Tex. Oct. 6, 2010) (slip opinion) (discussing arbitration in an adversary proceeding and not compelling it when the dispute involved automatic stay violations and damages).

Relation-back doctrine discussed.

When the second mortgage creditor filed a fully-secured proof of claim that was relied on by the debtors and other creditors, the creditor's attempt to file an unsecured claim, following the first mortgage foreclosure, was denied. The creditor waited over a year after the claims bar date and confirmation, and the court held that the new claim was untimely and did not relate back to the original secured claim. *In re George*, 426 B.R. 895 (Bankr. M.D. Fla. 2010).

State fails to support objection to proof of claim filed on its behalf by debtor.

When the State of Michigan failed to file a timely proof of claim for prepetition taxes, the debtor filed a timely claim on behalf of the State under § 501(c). The State objected, but "[d]isallowance of a proof of claim filed by a debtor under § 501(c) of the Bankruptcy Code depends solely on whether one of the nine enumerated grounds for disallowance under § 502(b) can be shown by the objecting party." The debtor's 2008 taxes, although not finally payable until April 15, 2009, were nevertheless prepetition taxes, with the court adopting the view that § 1305(a)(1)'s phrase "becomes payable" does not define a claim. When the debtors had earned their 2008 income before filing bankruptcy and had self-assessed their 2008 state income taxes by filing their State return before bankruptcy, there was a prepetition debtor/creditor relationship between the debtors and State. The court rejected the State's argument that the taxes were postpetition and that the debtors were not authorized to file a claim on its behalf under § 1305. *In re Senczyszyn*, 426 B.R. 250 (Bankr. E.D. Mich. 2010).

A review of documentation issues on assigned claims.

The bankruptcy court provided a review of other judicial authority on the standing of assignee creditors to file proofs of claim and the extent to which documentation of the claim is

required under Rule 3001 and for prima facie validity. The opinion contains a review of documentation for both assigned credit card and mortgage debts, concluding that although lack of documentation is not a stated reason for disallowance under § 502(b), when there is inadequate documentation, the proof of claim may be insufficient to permit the objecting party to concede its validity. The court concluded that when a claim lacks sufficient documentation, the debtor or other party may demand additional documentation, and the claimant has an obligation to provide it within two weeks; if not provided, the debtor or trustee may then file an objection to the claim. *In re Minbatiwalla*, 424 B.R. 104, (Bankr. S.D.N.Y. 2010).

Burden of proof on § 507(a)(1) claims.

Discussing the difference in priority claims under §§ 507(a)(1)(A) and (B), when the state department of family services did not prove that its assigned claims was for the purpose of collection or how much was owed to the state directly, it failed to prove that its claim was entitled to full payment priority under § 507(a)(1)(A), permitting the § 507(a)(1)(B) claim to be paid less than 100% in a Chapter 13 plan under § 1322(a)(4). Notwithstanding § 1322(a)(4), the unpaid amount of the claim was still excepted from discharge. *In re Penaran*, 424 B.R. 868 (Bankr. D. Kan. 2010). See also *In re Sosa*, 2010 WL 318484 (Bankr. E.D. Va. Jan. 21, 2010) (slip opinion) (discussing adequate notice to governmental agency of how its § 507(a)(1) claim would be treated); *In re Wheeler*, 2010 WL 503112 (Bankr. N.D. Ala. Feb. 5, 2010) (slip opinion) (discussing nondischargeability of § 507(a)(1)(B) claims paid less than 100%).

Remedies for violation of Rule 9037.

One court held that the proper remedy for the creditor's violation of Rule 9037 was striking the proof of claim and prohibiting access to it, while allowing the creditor to file an amended proof of claim that complied with the Rule's prohibition against personal identifying information. Code § 502(b) does not include violation of Rule 9037 as grounds for disallowance. *In re Chubb*, 426 B.R. 695, 2010 WL 931863 (Bankr. E.D. Mich. 2010). Another court found that debtors stated a cause of action for violation of the tort of invasion of privacy under Mississippi's common law in an adversary proceeding about the creditor's violation of Rule 9037, and whether or not the debtors have a private right of action under that Rule, the court may use § 105(a) to remedy the violation. *In re McKenzie*, 2010 WL 917262 (Bankr. S.D. Miss. Mar. 10, 2010) (slip opinion).

Debtor failed to establish harm to support violation of Rule 9037.

The debtor must demonstrate standing to pursue an adversary proceeding alleging that a creditor filed its proof of claim containing personal identifier information in violation of Rule 9037, but the debtor did not plead any harm. The debtor had not had personal information accessed by a third party and his identity had not been stolen. Pleading the creditor's disrespect for the court's orders and Bankruptcy Rules did not give the debtor standing. Neither § 105(a) nor Gramm-Leach-Bliley Act grants a private right of action for violation of Rule 9037. *Davis v. Eagle Legacy Credit Union (In re Davis)*, 430 B.R. 902 (Bankr. D. Colo. 2010).

Creditor's failure to update proof of claim required reference to U.S. Attorney.

Rejecting the argument that Rule 9011 doesn't apply to a proof of claim, the bankruptcy court held that a mortgage creditor's continued advocation of an erroneous claim to the detriment of other creditors, and the creditor's failure to timely amend the claim, required reference to the United States Attorney to determine if there was a violation of 18 U.S.C. § 152(4), and the court sua sponte initiated a hearing as to whether the creditor should be sanctioned under Rule 9011(c)(1)(B). *Hannon v. Countrywide Home Loans, Inc. (In re Hannon)*, 2009 WL 5103305 (Bankr. M.D. Pa. Dec. 18, 2009) (slip opinion).

Claim filed by fax too late.

A proof of claim filed by fax 43 minutes after a deadline was too late when an order required the filing of the original proof of claim by the deadline. The fax was not an original, and Rule 5005(c) didn't apply, since it only gave the court discretion when the document was delivered to the incorrect person. *In re marchFIRST,* 573 F.3d 414 (7th Cir. 2009).

Claims bar date reset upon reinstatement of dismissed case.

Acknowledging that "Rule 9006(b) (3) appears to unambiguously preclude any equitable discretion on the part of a bankruptcy court to extend or toll [the Rule 3002(c)] deadlines," the court applied rationale from its Fifth Circuit authority under Rules 4004 and 4007, to "nullify original case deadlines and recalculate them when there has been the extenuating circumstance of disruption of a case....This court holds that *where a case is disrupted*, such as through a stay or dismissal, and a proof of claim deadline runs prior to the reinstatement of the case, a court has the power to nullify the original proof of claim deadline and recalculate it." *In re Gulley*, 400 B.R. 529 (Bankr. N.D. Tex. 2009) (citing *Coston v. Bank of Malvern*, 987 F.2d 1096 (5th Cir. 1992) (approving nullification and resetting of deadlines under Rules 4004 and 4007) and *State Bank & Trust, N.A. v. Dunlap (In re Dunlap)*, 217 F.3d 311 (5th Cir. 2000) (approving resetting of § 341 meeting and resulting Rule 4007 deadline when case was dismissed in error).

Creditors may have standing to object to other creditor's claims.

The Chapter 7 debtor typically lacks standing to object to creditors' claims, but creditors have a pecuniary interest, giving standing to object as parties in interest, if there either is no trustee appointed or the trustee refuses to act. *In re Ulz,* 401 B.R. 321 (Bankr. N.D. Ill. 2009).

Creditor not required to file another proof of claim after conversion.

Creditors filing timely proofs of claim in Chapter 7 case are not required to refile those claims after the case is converted to Chapter 13. The debtor sought disallowance of claims not filed in the Chapter 13 case, but, although a new claims bar date was set by the clerk upon conversion, requiring the filing of new claims would be "nothing but redundancy." The bankruptcy rules don't address this issue. *Jasinski v. Monongalia General Hospital, et al. (In re Jasinski),* 406 B.R. 653 (Bankr. W.D. Pa. 2009).

Secured creditor's right to credit bid may be trumped by cramdown.

The Third Circuit has held that a secured creditor's right to credit bid may be trumped by the cramdown provisions of section 1129 in confirming a liquidating plan. In *In re Philadelphia Newspapers, LLC*, 599 F.3d 298 (3d Cir. 2010), Chapter 11 debtors in possession moved for approval of bid procedures for an auction sale of the debtors' assets as part of a liquidating Chapter 11 plan. The Bankruptcy Court denied the motion but, on appeal, the District Court and the Court of Appeals held that section 1129(b) permitted the debtors to satisfy the lenders' liens against assets of the bankruptcy estate by conducting a sale of collateral free and clear of liens and providing secured lenders with "indubitable equivalent" of their secured claims, and the "indubitable equivalent" subsection unambiguously excluded lenders' right to credit bid at asset sale.

Lender Liability Issues

Upstream mortgages and guarantees challenged as fraudulent and preferential transfers.

In 2009, the Bankruptcy Court in the TOUSA homebuilder bankruptcy in the Southern District of Florida issued a fraudulent transfer opinion that received attention in both bankruptcy and lending circles. *Committee of Unsecured Creditors of Tousa, Inc. v. Citicorp North America, Inc. (In re TOUSA, Inc.)*, 422 B.R. 783 (Bankr. S.D. Fla. 2009). The Court avoided the "upstream" liens from subsidiaries to a parent company's secured lenders as fraudulent transfers. The bankruptcy judge was critical of the valuation experts' opinions, focusing especially on their (contingent) fees as well as other aspects of their testimony. The Bankruptcy Court also ruled in sweeping language that the "savings clauses" in the loan documents (which provide that the obligations and liens are deemed to be reduced to the extent necessary to prevent the insolvency of each obligor) were not effective to save the lenders. In the Court's view, such clauses violate various sections of the Bankruptcy Code, and "are, in short, entirely too cute to be enforced." In a harsh reversal of the Bankruptcy Court's decision, the District Court held that a transaction in which subsidiaries encumbered all of their assets to secure a loan that enabled their parent company to pay its debt was not a fraudulent conveyance as to the parties paid with the loan proceeds. *3V Capital Master Fund Ltd. v. Committee (In re TOUSA, Inc.)*, 2011 WL 522008 (S.D. Fla. 2011). The District Court held that "reasonably equivalent value," as a part of the defense to the fraudulent transfer claim, could consist of indirect, intangible benefits (e.g., when the loan strengthens the corporate group as a whole). The District Court also strongly disapproved of the Bankruptcy Judge's findings and conclusions that were based on those submitted by a party and adopted "practically verbatim" by the trial court. The opinion cited 5th and 11th Cir. authority and quoted a Supreme Court opinion to the effect that the practice has been "denounced." The Court used this as a basis for "relaxing" the "clearly erroneous" standard of review of the factual question of value.

Another attempt to avoid a security interest as a fraudulent transfer.

In *In re Propex, Inc.*, 415 B.R. 321 (Bankr. E.D. Tenn. 2009), a committee of unsecured creditors sought to avoid a loan amendment that allegedly imposed unrealistic covenants. The committee also asserted a claim for "deepening insolvency" and alleged that reperfection of a security interest was a fraudulent conveyance and that the lender's security agreement did not extend to environmental permits. The bankruptcy court dismissed the fraudulent conveyance and deepening insolvency claims (holding that Tennessee would not recognize a claim for deepening insolvency), but held that the debtor had no underlying interest in the environmental permits to which the lender's security interest could attach.

Mortgage loan on luxury second-home project left the project "too thinly capitalized to survive" and was subordinated.

Another interesting set of facts suggesting that "lender liability" practice is back can be found in *Credit Suisse v. Committee (In re Yellowstone Mountain Club, LLC)*, 2009 WL 3094930 (Bankr. D. Mont. 2009). In that case, the Bankruptcy Court subordinated for purposes of distribution the claim of a secured creditor, under 11 U.S.C. § 510(c). The Bankruptcy Court analyzed the transaction's structure, especially looking at the fees charges, and found that the lender had offered owners of a luxury second-home development an opportunity to take profits up front by mortgaging the project "to the hilt" and would lend "the money on a non-recourse basis, earn a substantial fee, and sell off most of the credit to loan participants." The owners took most of the loan proceeds out of the development as a dividend, leaving the development "saddled with enormous debt" and bearing "all the risk of loss." According to the opinion, the creditor left the project "too thinly capitalized to survive" and its "actions in the case were so far overreaching and self-serving that they shocked the conscience of the Court" and left the project "doomed to failure once [it] received their loans."

Motion for stay relief, based on defective affidavit of default, was fraud on court

On the U.S. trustee's motion for sanctions against Option One Mortgage, Fidelity National Foreclosure Services, known as Lender Processing Services (LPS) and the attorney for the creditor, the Bankruptcy Court for the Eastern District of Louisiana found that a motion for stay relief filed by Option One had been based on a defective affidavit of default and concluded that it was a fraud on the court, with sanctions awarded against the attorney and liability for sanctions determined as to LPS, with an evidentiary hearing to be held on specific sanctions. *In re Wilson*, 2011 WL 1337240 (Bankr. E.D. La., April 7, 2011) (slip copy). The opinion sets forth in detail the history of this case and several others involving the same servicer, constituting the pieces of "the puzzle of loan administration" and leading to Bankruptcy Judge Magner's decision to impose sanctions.

Appendix A

NCCUSL's Proposed Changes to Address Perfection Issues with Individual Debtor

(Deletions in code and commentary stricken through. New material in code and commentary underlined. Brackets indicate language to be addressed in legislative action.)

New 9-502(c)(3)(B):

the record sufficiently provides the name of a debtor who is an individual if it provides the individual name of the debtor or the surname and first personal name of the debtor, even if the debtor is an individual to whom Section 9-503(a)(4) applies

New 9-503(a):

(a) **[Sufficiency of debtor's name.]** A financing statement sufficiently provides the name of the debtor:

(1) except as otherwise provided in paragraph (3), if the debtor is a registered organization or the collateral is held in a trust that is a registered organization, only if the financing statement provides the name ~~of the debtor indicated~~ that is stated to be the registered organization's name on the public organic record ~~of~~ most recently filed with or issued or enacted by the ~~debtor's~~ registered organization's jurisdiction of organization which ~~shows the debtor to have been organized~~ purports to state, amend, or restate the registered organization's name;

(2) subject to subsection (f), if the ~~debtor is a decedent's estate~~ collateral is being administered by the personal representative of a decedent, only if the financing statement provides, as the name of the debtor, the name of the decedent and, in a separate part of the financing statement, indicates that the ~~debtor is an estate~~ collateral is being administered by a personal representative;

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

~~(A) provides the name 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 settlors; and~~

~~(B) indicates, in the debtor's name or otherwise, that the debtor is a trust or is a trustee acting with respect to property held in trust;~~

collateral is held in a trust that is not a registered organization, only if the financing statement:

(A) provides, as the name of the debtor:

(i) if the organic record of the trust specifies a name for the trust, the name so specified; or

(ii) if the organic record of the trust does not specify a name for the trust, the name of the settlor or testator; and

(B) in a separate part of the financing statement:

(i) if the name is provided in accordance with subparagraph (A)(i), indicates that the collateral is held in a trust; or

(ii) if the name is provided in accordance with subparagraph (A)(ii), provides additional information sufficient to distinguish the trust from other trusts having one or more of the same settlors or the same testator and indicates that the collateral is held in a trust, unless the additional information so indicates;

[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 it 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 it provides the individual name of the debtor or the surname and first personal name of the debtor; and

~~(4)~~ (6) in other cases:

(A) if the debtor has a name, only if it provides the ~~individual or~~ organizational name of the debtor; and

(B) if the debtor does not have a name, only if it provides the names of the partners, members, associates, or other persons comprising the debtor, in a manner that each name provided would be sufficient if the person named were the debtor.

[Alternative B]

(4) if the debtor is an individual, only if:

(A) it provides the individual name of the debtor;

(B) it provides the surname and first personal name of the debtor; or

(C) subject to subsection (g), it provides the name of the individual which is indicated on a [driver's license] that this State has issued to the individual and which has not expired; and

~~(4)~~ (5) in other cases:

(A) if the debtor has a name, only if it provides the ~~individual or~~ organizational name of the debtor; and

(B) if the debtor does not have a name, only if it provides the names of the partners, members, associates, or other persons comprising the debtor, in a manner that each name provided would be sufficient if the person named were the debtor.

Legislative Notes:

1. This Act contains two alternative sets of amendments relating to the names of individual debtors. A State should enact the same Alternative, A or B, for both subsections (a) and (i) of Section 9-503. A State that enacts Alternative A of the amendments to this section should also enact the amendments to Section 9-502.

2. Both Alternatives refer, in part, to the name as shown on a debtor's driver's license. The Legislature should be aware that, in some States, certain characters that may be used by the State's department of motor vehicles (or similar agency) in the name on a driver's license may not be accepted by the State's central or local UCC filing offices under current regulations or internal protocols. This may occur because of technological limitations of the filing offices or merely as a result of inconsistent procedures. Similar issues may exist for field sizes as well. In these situations, perfection of a security interest granted by a debtor with such a driver's license may be impossible under Alternative A of the amendments and the utility of Alternative B, under which the name on the driver's license is one of the names that is sufficient, may be reduced. Accordingly, the State may wish to determine if one or more of these issues exist in this State and, if so, to make certain that such issues have been resolved. A successful resolution might be accomplished by statute, agency regulation, or technological change effectuated before or as part of the enactment of this Act.

3. Regardless of which Alternative is enacted, in States in which in which a single agency issues driver's licenses and non-driver identification cards as an alternative to a driver's license, such that at any given time an individual may hold either a driver's license or an identification card but not both, the State should replace each use of the term "driver's license" with a phrase meaning "driver's license or identification card" but containing the analogous terms used in the enacting State. In other States, the State should replace the term "driver's license" with the analogous term used in the enacting State.

COMMENT:

d. Individuals. This Article provides alternative approaches towards the requirement for providing the name of a debtor who is an individual.

Alternative A. Alternative A distinguishes between two groups of individual debtors. For debtors holding an unexpired driver's license issued by the State where the financing statement is filed (ordinarily the State where the debtor maintains the debtor's principal residence),

Alternative A requires that a financing statement provide the name indicated on the license. When a debtor does not hold an unexpired driver's license issued by the relevant State, the requirement can be satisfied in either of two ways. A financing statement is sufficient if it provides the "individual name" of the debtor. Alternatively, a financing statement is sufficient if it provides the debtor's surname (i.e., family name) and first personal name (i.e., first name other than the surname).

Alternative B. Alternative B provides three ways in which a financing statement may sufficiently provide the name of an individual who is a debtor. The "individual name" of the debtor is sufficient, as is the debtor's surname and first personal name. If the individual holds an unexpired driver's license issued by the State where the financing statement is filed (ordinarily the State of the debtor's principal residence), the name indicated on the driver's license also is sufficient.

Name indicated on the driver's license. A financing statement does not "provide the name of the individual which is indicated" on the debtor's driver's license unless the name it provides is the same as the name indicated on the license. This is the case even if the name indicated on the debtor's driver's license contains an error.

> **Example 1:** Debtor, an individual whose principal residence is in Illinois, grants a security interest to SP in certain business equipment. SP files a financing statement with the Illinois filing office. The financing statement provides the name appearing on Debtor's Illinois driver's license, "Joseph Allan Jones." Regardless of which Alternative is in effect in Illinois, this filing would be sufficient under Illinois' Section 9-503(a), even if Debtor's correct middle name is Alan, not Allan.
>
> A filing against "Joseph A. Jones" or "Joseph Jones" would not "provide the name of the individual which is indicated" on the debtor's driver's license. However, these filings might be sufficient if Alternative A is in effect in Illinois and Jones has no current (i.e., unexpired) Illinois driver's license, or if Illinois has enacted Alternative B.

Determining the name that should be provided on the financing statement must not be done mechanically. The order in which the components of an individual's name appear on a driver's license differs among the States. Had the debtor in Example 1 obtained a driver's license from a different State, the license might have indicated the name as "Jones Joseph Allan." Regardless of the order on the driver's license, the debtor's surname must be provided in the part of the financing statement designated for the surname.

Alternatives A and B both refer to a license issued by "this State." Perfection of a security interest by filing ordinarily is determined by the law of the jurisdiction in which the debtor is located. See Section 9-301(1). (Exceptions to the general rule are found in Section 9-301(3) and (4), concerning fixture filings, timber to be cut, and as-extracted collateral.) A debtor who is an individual ordinarily is located at the individual's principal residence. See Section 9-307(b). (An exception appears in Section 9-307(c).) Thus, a given State's Section 9-503 ordinarily will apply during any period when the debtor's principal residence is located in that State, even if during that time the debtor holds or acquires a driver's license from another State.

When a debtor's principal residence changes, the location of the debtor under Section 9-307 also changes and perfection by filing ordinarily will be governed by the law of the debtor's new location. As a consequence of the application of that State's Section 9-316, a security interest that is perfected by filing under the law of the debtor's former location will remain perfected for four months after the relocation, and thereafter if the secured party perfects under the law of the debtor's new location. Likewise, a financing statement filed in the former location may be effective to perfect a security interest that attaches after the debtor relocates. See Section 9-316(h).

Example 2: Debtor, an individual whose principal residence is in Illinois, grants a security interest to SP in certain business equipment. SP files a financing statement in Illinois that provides the name indicated on Debtor's Illinois driver's license. On January 1, Debtor relocates to Indiana. Upon the relocation, the law governing perfection of the security interest changes from the law of Illinois to the law of Indiana.

Under Indiana's Section 9-316, however, a security interest perfected by the Illinois filing remains perfected, normally for four months. If SP does not file in Indiana before the four-month period expires, then the security interest will become unperfected and will be deemed never to have been perfected as against a purchaser of the collateral for value. In addition, under Indiana's Section 9-316, the Illinois financing statement normally would remain effective to perfect a security interest in collateral acquired by Debtor within the four months after the relocation to Indiana.

Individual name of the debtor. Article 9 does not determine the "individual name" of a debtor. Nor does it determine which element or elements in a debtor's name constitute the surname. In some cases, determining the "individual name" of a debtor may be difficult, as may determining the debtor's surname. This is because in the case of individuals, unlike registered organizations, there is no public organic record to which reference can be made and from which the name and its components can be definitively determined.

Names can take many forms in the United States. For example, whereas a surname is often colloquially referred to as a "last name," the sequence in which the elements of a name are presented is not determinative. In some cultures, the surname appears first, while in others it may appear in a location that is neither first nor last. In addition, some surnames are composed of multiple elements that, taken together, constitute a single surname. These elements may or may not be separated by a space or connected by a hyphen, "i," or "y." In other instances, some or all of the same elements may not be part of the surname. In some cases, a debtor's entire name might be composed of only a single element.

In disputes as to whether a financing statement sufficiently provides the "individual name" a debtor, a court should refer to any non-UCC law concerning names. However, case law about names may have developed in contexts that implicate policies different from those of Article 9. A court considering an individual's name for purposes of determining the sufficiency of a financing statement is not necessarily bound by cases that were decided in other contexts and for other purposes.

Individuals are asked to provide their names on official documents such as tax returns and bankruptcy petitions. An individual may provide a particular name on an official document in response to instructions relating to the document rather than because the individual actually uses the name. Accordingly, a court should not assume that the name an individual provides on an official document necessarily constitutes the "individual name" for purposes of the sufficiency of the debtor's name on a financing statement. Likewise, a court should not assume that the name as presented on an individual's birth certificate is necessarily the individual's current name.

In applying non-UCC law for purposes of determining the sufficiency of a debtor's name on a financing statement, a court should give effect to the instruction in Section 1-103(a)(1) that the UCC "must be liberally construed and applied to promote its underlying purposes and policies," which include simplifying and clarifying the law governing commercial transactions. Thus, determination of a debtor's name in the context of the Article 9 filing system must take into account the needs of both filers and searchers. Filers need a simple and predictable system in which they can have a reasonable degree of confidence that, without undue burden, they can determine a name that will be sufficient so as to permit their financing statements to be effective. Likewise, searchers need a simple and predictable system in which they can have a reasonable degree of confidence that, without undue burden, they will discover all financing statements pertaining to the debtor in question. The court also should take into account the purpose of the UCC to make the law uniform among the various jurisdictions. See Section 1-103(a)(3).

Of course, once an individual debtor's name has been determined to be sufficient for purposes of Section 9-503, a financing statement that provides a variation of that name, such as a "nickname" that does not constitute the debtor's name, does not sufficiently provide the name of the debtor under this section. Cf. Section 9-503(c) (a financing statement providing only a debtor's trade name is not sufficient).

If there is any doubt about an individual debtor's name, a secured party may choose to file one or more financing statements that provide a number of possible names for the debtor and a searcher may similarly choose to search under a number of possible names.

Note that, even if the name provided in an initial financing statement is correct, the filing office nevertheless must reject the financing statement if it does not identify an individual debtor's ~~last name~~ surname (e.g., if it is not clear whether the debtor's ~~name~~ surname is Perry ~~Mason~~ or Mason ~~Perry~~). See Section 9-516(b)(3)(C).

Appendix B

Chart of Article 9 Perfection Methods

TYPE OF COLLATERAL	NATURE OF SECURITY INTEREST		
	Secured Party (or Buyer) ...		Proceeds and Supporting Obligations
	Receives or Retains to Secure an Obligation	Receives in Sale	
Account	file		
Health-Care-Insurance Receivable	file (automatic if to provider)		
Chattel Paper	file, mark or possess		
Electronic Chattel Paper	file or control		
Payment Intangible	file	automatic	
Promissory Note	file or possess		automatic (but perfection in proceeds may lapse after 20 days)
Other Instrument			
Beneficial Interest in Estate	automatic		
Negotiable Document of Title	file on document or possess		
Non-Negotiable Document of Title	file on goods, notify bailee or issue in SP's name		
Money	possess		
Deposit Account	control (automatic if to depositary bank)	not Article 9 transactions	
Letter-of-Credit Right	control		
General Intangible (Except Sale of Payment Intangible)	file ...		
Commercial Tort Claim			
Patent	(in U.S.P.T.O. or U.S.C.O. if registered patent, trademark or copyright?)		
Trademark			
Copyright			
Beneficial Interest in Trust			
Software Not Embedded in Goods			
Fixture	(locally if "fixture filing," as-extracted collateral or timber to be cut)		
As-Extracted Collateral			
Timber to be Cut			
Investment Property	file, register, deliver or control (possess if certificated and register if registered) (bailee acknowledge in writing) (automatic control if broker or intermediary)		
Inventory	file or possess (only by title if titled, non-inventory goods) (with FAA if aircraft) (automatic if PMSI in non-titled consumer goods)		
Equipment			
Crops			
Aircraft			
Consumer Goods			
Farm Products			
Embedded Software	perfect in the goods		

Appendix C

Proposed Amendment to Rule 3001(c)
(As Adopted by Supreme Court April 26, 2011)

(c) SUPPORTING INFORMATION.

(1) *Claim Based on a Writing.* When a claim, or an interest in property of the debtor securing the claim, is based on a writing, the original or a duplicate shall be filed with the proof of claim. If the writing has been lost or destroyed, a statement of the circumstances of the loss or destruction shall be filed with the claim.

(2) *Additional Requirements in an Individual Debtor Case; Sanctions for Failure to Comply.* In a case in which the debtor is an individual:

(A) If, in addition to its principal amount, a claim includes interest, fees, expenses, or other charges incurred before the petition was filed, an itemized statement of the interest, fees, expenses, or charges shall be filed with the proof of claim.

(B) If a security interest is claimed in the debtor's property, a statement of the amount necessary to cure any default as of the date of the petition shall be filed with the proof of claim.

(C) If a security interest is claimed in property that is the debtor's principal residence, the attachment prescribed by the appropriate Official Form shall be filed with the proof of claim. If an escrow account has been established in connection with the claim, an escrow account statement prepared as of the date the petition was filed and in a form consistent with applicable nonbankruptcy law shall be filed with the attachment to the proof of claim.

(D) If the holder of a claim fails to provide any information required by this subdivision (c), the court may, after notice and hearing, take either of both of the following actions:

(i) preclude the holder from presenting the omitted information, in any form, as evidence in any contested matter or adversary proceeding in the case, unless the court determines that the failure was substantially justified or is harmless.

(ii) award other appropriate relief, including reasonable expenses and attorney's fees caused by the failure.

Appendix D

Proposed New Rule 3002.1
(As Adopted by Supreme Court April 26, 2011)

RULE 3002.1. NOTICE RELATING TO CLAIMS SECURED BY SECURITY INTEREST IN THE DEBTOR'S PRINCIPAL RESIDENCE

(a) IN GENERAL: This Rule applies in a chapter 13 case to claims that are (1) secured by a security interest in the debtor's principal residence, and (2) provided for under § 1322(b)(5) of the Code in the debtor's plan.

(b) NOTICE OF PAYMENT CHANGES. The holder of the claim shall file and serve on the debtor, debtor's counsel, and the trustee a notice of any change in the payment amount, including any change that results from an interest rate or escrow account adjustment, no later than 21 days before a payment in the new amount is due.

(c) NOTICE OF FEES, EXPENSES, AND CHARGES. The holder of the claim shall file and serve on the debtor, debtor's counsel, and the trustee a notice itemizing all fees, expenses, or charges (1) that were incurred in connection with the claim after the bankruptcy case was filed, and (2) that the holder asserts are recoverable against the debtor or against the debtor's principal residence. The notice shall be served within 180 days after the date on which the fees, expenses or charges are incurred.

(d) FORM AND CONTENT. A notice filed and served under subdivision (b) or (c) of this rule shall be prepared as prescribed by the appropriate Official Form, and filed as a supplement to the holder's proof of claim. The notice is not subject to Rule 3001(f).

(e) DETERMINATION OF FES, EXPENSES, OR CHARGES. On motion of the debtor or trustee filed within one year after service of a notice under subdivision (c) of this rule, the court shall, after notice and hearing, determine whether payment of any claimed fee, expense, or charge is required by the underlying agreement and applicable nonbankruptcy law to cure a default or maintain payments in accordance with § 1322(b)(5) of the Code.

(f) NOTICE OF FINAL CURE PAYMENT. Within 30 days after the debtor completes all payments under the plan, the trustee shall file and serve on the holder of the claim, the debtor, and debtor's counsel a notice stating that the debtor has paid in full the amount required to cure any default on the claim. The notice shall also inform the holder of its obligation to file and serve a response under subdivision (g). If the debtor contends that final cure payment has been made and all plan payments have been completed, and the trustee does not timely file and serve the notice required by this subdivision, the debtor may file and serve the notice.

(g) RESPONSE TO NOTICE OF FINAL CURE PAYMENT. Within 21 days after service of the notice under subdivision (f) of this rule, the holder shall file and serve on the

debtor, debtor's counsel, and the trustee a statement indicating (1) whether it agrees that the debtor has paid in full the amount required to cure the default on the claim, and (2) whether the debtor is otherwise current on all payments consistent with § 1322(b)(5) of the Code. The statement shall itemize the required cure or postpetition amounts, if any, that the holder contends remain unpaid as of the date of the statement. The statement shall be filed as a supplement to the holder's proof of claim and is not subject to Rule 3001(f).

(h) DETERMINATION OF FINAL CURE AND PAYMENT. On motion of the debtor or trustee filed within 21 days after service of the statement under subdivision (g) of this rule, the court shall, after notice and hearing, determine whether the debtor has cured the default and paid all required postpetition amounts.

(i) FAILURE TO NOTIFY. If the holder of a claim fails to provide any information as required by subdivision (b), (c), or (g) of this rule, the court may, after notice and hearing, take either or both of the following actions:

(1) preclude the holder from presenting the omitted information, in any form, as evidence in any contested matter or adversary proceeding in the case, unless the court determines that the failure was substantially justified or is harmless; or

(2) award other appropriate relief, including reasonable expenses and attorney's fees caused by the failure.