



Finance ADVISORY ■

NOVEMBER 19, 2014

Lenders Beware—Delaware Supreme Court States a UCC-3 Filing Is Effective Regardless of Intent

On October 17, 2014, the Delaware Supreme Court held that under the Delaware Uniform Commercial Code, the subjective intent of a secured party is irrelevant in determining the effectiveness of a UCC-3 termination statement if the secured party authorized its filing.¹

Background

General Motors (now, Motors Liquidation Company) was a debtor under a \$300 million synthetic lease transaction and a \$1.5 billion term loan facility. The agent and secured party of record was the same under both transactions.² In 2008, when the synthetic lease was due to mature, General Motors repaid the full amount of the debt and the security interests were released. However, in preparing the UCC-3 termination statements for the synthetic lease transaction, counsel for General Motors inadvertently included the filing number for the term loan UCC-1 financing statement.³ Counsel for the agent reviewed the UCC-3 termination statements but failed to identify the error. Therefore, the UCC-3 termination statement filed with the Delaware Secretary of State upon the final payoff of the synthetic lease terminated the UCC-1 financing statement for the term loan facility in addition to the UCC-1 financing statements for the synthetic lease transaction.⁴ The inadvertent filing went unnoticed until General Motors filed its petition for Chapter 11 in July 2009. As part of the bankruptcy proceedings, the agent notified the unsecured creditors committee about the mistaken filing. The unsecured creditors committee then filed an adversary proceeding with the U.S. Bankruptcy Court for the Southern District of New York seeking a determination that, despite the fact that none of the parties involved intended to terminate the term loan UCC-1 financing statement, the UCC-3 termination terminating the UCC-1 financing statement for the term loan

¹ *Official Comm. of Unsecured Creditors of Motors Liquidation Co. v. JPMorgan Chase Bank, N.A.*, No. 325, 2014 *In re Motors Liquidation*, 2014 WL 5305937 (Del. Oct. 17, 2014) at *1 (“Delaware Opinion”)

² *Official Comm. of Unsecured Creditors of Motors Liquidation Co. v. JPMorgan Chase Bank, N.A. (In re: Motors Liquidation Co.)*, 755 F.3rd 78, 79 (2nd Cir. 2014).

³ *Id.*, at 80.

⁴ *Id.*, at 81.

facility was nevertheless effective and therefore, the \$1.5 billion term loan facility was unsecured. The bankruptcy court ruled in favor of the agent, and the unsecured creditors committee appealed to the U.S. Court of Appeals for the Second Circuit. The Second Circuit then certified the limited question as to the effectiveness of the UCC-3 termination filing with the Delaware Supreme Court.⁵

Delaware Supreme Court Decision

The agent argued that a UCC-3 termination statement is ineffective “if errors in the statement resulted in the release of a security interest that the party did not subjectively intend to release.”⁶ In ruling that the UCC-3 termination statement was effective, and thus the term loan security interests were unperfected, the court looked to the plain language of Section 9-513 of the Delaware Uniform Commercial Code, which reads, “upon the filing of a termination statement with the filing office, the financing statement to which the termination statement relates ceases to be effective.”⁷ It noted that the express language of the Uniform Commercial Code contained no subjective element and therefore, as long as the secured party authorized the filing, the termination statement was effective regardless of whether the secured party understood the content of the filing or its practical effect.

The court also cited several public policy justifications supporting its conclusion. Of primary importance was the fact that the Uniform Commercial Code is designed to promote efficiency in the marketplace by “permitting parties to rely in good faith on the plain terms of authorized public filings.”⁸ A holding that would take into account a secured party’s subjective intent, the court reasoned, “would disrupt and undermine the secured lending markets” by requiring a court to determine the subjective intent underlying any public filing before other secured creditors could rely on its effectiveness.⁹

Practical Implications

This decision highlights the importance of having a strong review process in place, especially when perfection of a security interest is implicated. Agents, lenders and their counsel should closely scrutinize all aspects of the secured loan transaction documentation both at the time the loan is funded and when it is later repaid, with particular emphasis placed on the necessary UCC filings to ensure that their security interest is adequately protected. This case also highlights the importance of conducting regular UCC searches in order to confirm that security interests remain perfected during the life of any secured loan transaction.

⁵ The Second Circuit’s question assumed that the secured party “reviewed and knowingly approved the termination statement for filing.” *Delaware Opinion*, at *2. The case has been remanded to the Second Circuit to determine whether or not General Motor’s counsel was actually authorized to file the termination statement.

⁶ *Delaware Opinion*, at *2

⁷ *Del. Code Ann. tit. 6, §9-513.*

⁸ *Delaware Opinion*, at *4.

⁹ *Id.*

If you would like to receive future *Finance Advisories* electronically, please forward your contact information to finance.advisory@alston.com. Be sure to put “**subscribe**” in the subject line.

If you have any questions or would like additional information, please contact your Alston & Bird attorney or any of the following:

Kate Moseley
214.922.3434
kate.moseley@alston.com

Stacie Cargill
214.922.3449
stacie.cargill@alston.com

ALSTON & BIRD LLP

ALSTONFINANCE.COM

© ALSTON & BIRD LLP 2014

ATLANTA: One Atlantic Center ■ 1201 West Peachtree Street ■ Atlanta, Georgia, USA, 30309-3424 ■ 404.881.7000 ■ Fax: 404.881.7777
BRUSSELS: Level 20 Bastion Tower ■ Place du Champ de Mars ■ B-1050 Brussels, BE ■ +32 2 550 3700 ■ Fax: +32 2 550 3719
CHARLOTTE: Bank of America Plaza ■ 101 South Tryon Street ■ Suite 4000 ■ Charlotte, North Carolina, USA, 28280-4000 ■ 704.444.1000 ■ Fax: 704.444.1111
DALLAS: 2828 North Harwood Street ■ 18th Floor ■ Dallas, Texas, USA, 75201 ■ 214.922.3400 ■ Fax: 214.922.3899
LOS ANGELES: 333 South Hope Street ■ 16th Floor ■ Los Angeles, California, USA, 90071-3004 ■ 213.576.1000 ■ Fax: 213.576.1100
NEW YORK: 90 Park Avenue ■ 15th Floor ■ New York, New York, USA, 10016-1387 ■ 212.210.9400 ■ Fax: 212.210.9444
RESEARCH TRIANGLE: 4721 Emperor Blvd. ■ Suite 400 ■ Durham, North Carolina, USA, 27703-85802 ■ 919.862.2200 ■ Fax: 919.862.2260
SILICON VALLEY: 1950 University Avenue ■ 5th Floor ■ East Palo Alto, California, USA, 94303-2282 ■ 650.838.2000 ■ Fax: 650.838.2001
WASHINGTON, DC: The Atlantic Building ■ 950 F Street, NW ■ Washington, DC, USA, 20004-1404 ■ 202.756.3300 ■ Fax: 202.756.3333