

# community BANKER

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Welcome to the latest issue of the COMMUNITY BANKER.

The Community Banker is prepared by attorneys at Olson & Burns P.C. to provide information pertaining to legal developments affecting the field of banking. In order to accomplish this objective, we welcome any comments our readers have regarding the content and format of this publication. Please address your comments to:

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The attorneys at Olson & Burns represent a wide range of clients in the financial and commercial areas. Our attorneys represent more than 30 banks throughout North Dakota.

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## **HOLY TECHNICALITY, BATMAN! IT MAY BE SERIOUSLY MISLEADING!**

1944 Beach Boulevard, LLC v. Live Oak Banking Company (In re: NRP Lease Holdings, LLC), Case No. 21-11742 (11th Cir. Dec. 10, 2021).

Occasionally, an out-of-state case catches our attention because it contains a lesson for us here in the great state of North Dakota. This time it's in Florida, where a secured party financing statement (apparently? technically?) identified the debtor incorrectly.

### **BACKGROUND**

Live Oak Banking Company made two loans totaling \$3,000,000 to 1944 Beach Boulevard, LLC and its affiliates, securing the loans with a blanket lien on all personal property of the debtor and its affiliates. Live Oak filed two UCC-1 financing statements with the proper Florida registration office; each financing statement identified the debtor as "1944 Beach Blvd., LLC." Unfortunately, the articles of organization filed with the Florida Secretary of State showed the *legal* name of the debtor to be "1944 Beach Boulevard, LLC" – Boulevard spelled out. Also unfortunately, Beach Boulevard and its affiliates filed a Chapter 11 bankruptcy in December 2019 with the loans unpaid. The issue in the bankruptcy case became 1) whether abbreviating "Boulevard" as "Blvd." is "seriously misleading" so as to make the financing statements ineffective and Live Oak an unperfected secured creditor, or 2) is Live Oak protected by the safe harbor rule of UCC 9-506 which says that *if* the financing statement with the incorrect name appears when a search is performed using the correct legal name and the filing office's standard search logic, the financing statement is *not* seriously misleading (and the secured party is secured).

### **THE LAW**

The fundamental idea and purpose of UCC Article 9 is that if a secured party/lender follows the rules, it should be protected against all third parties who might challenge its security interest or the priority of the security interest in non-real estate collateral securing a loan. The secured party/lender party has the responsibility to use the correct legal name of the debtor granting the security interest on the financing statement. The entity's legal name is found on the formation document that the entity files with its home state to create the entity (*e.g.*, Articles of Incorporation/Partnership/Organization/Formation). The formation document (or the most recent amendments to that document) is the *only* document that discloses the legal name of the entity, and the financing statement should use the exact name on that document in its financing statement.

**Name of debtor and secured party.** If the debtor is a registered entity such as a corporation, limited liability company, etc., UCC § 9-503(a) directs that the debtor's name appear on the UCC financing statement as the name appears on the "public organic record" most recently filed. In English, that is the name filed with the office of the Secretary of State. Florida's statute enacting UCC § 9-503(a) is identical to NDCC § 41-09-74(1)(a), North Dakota's enactment of UCC § 9-503(a).

**Effect of errors or omissions.** UCC § 9-506(b) states that "a financing statement that fails sufficiently to provide the name of the debtor in accordance with Section 9-503(a) is seriously misleading." An incorrect debtor's name on the financing statement can affect whether the UCC filing is found by a third party using the state's standard search logic. Florida's statute enacting UCC § 9-506(b) is identical to NDCC § 41-09-77(2), North Dakota's enactment of UCC § 9-506(b).



**Safe Harbor Rule.** Happily, all is not lost under UCC § 9-506(c). Even if there are minor errors or omissions in the financing statement, the secured party may still have a valid filing in the Safe Harbor. The financing statement is not “seriously misleading” (and ineffective) if a search of the debtor’s name using the filing office’s standard search logic discloses the filed financing statement, even with minor errors. Florida’s statute enacting UCC § 9-506(c) is identical to NDCC § 41-09-77(3), North Dakota’s enactment of UCC § 9-506(c).

### WHAT HAPPENED

Beach Boulevard filed an adversary action against Live Oak in the bankruptcy proceeding alleging that the abbreviation of “Blvd.” was seriously misleading because a search under its correct legal name did not reveal the existence of Live Oak’s liens, meaning that Live Oak’s security interest was unperfected. Because this was a bankruptcy court, Beach Boulevard argued that it could use its power as a hypothetical lien creditor to avoid Live Oak’s lien. Live Oak argued that its abbreviation of “Blvd.” was a minor error and that its perfection was saved by the safe harbor rule. It pointed out that its financing statement did appear in the search results if a party searching had navigated to the “previous” page of results. The search displayed 20 results at a time, and the searcher can navigate to the previous or next page to see additional results. A record of Live Oak’s filing appeared on the previous page; had the software displayed 40 results per page, Live Oak’s UCC would have appeared on the initial page.

The bankruptcy court granted Live Oak’s motion for summary judgment, finding that had a perfected security interest despite the defect in the financing statement because Live Oak’s financing statement appeared in the search, although *not* on the first page of the search results. The district court affirmed the bankruptcy court; Beach Boulevard appealed. The 11<sup>th</sup> Circuit Court of appeals noted that in Florida, a financing statement that does not list the debtor’s correct name is, under the statute, “seriously misleading” and therefore ineffective to perfect the creditor’s security interest. It also noted that there is no dispute that Live Oak’s financing statements did not list Beach Boulevard’s correct name, *but* Florida law provides a safe harbor for defective financing statements. Whether Live Oak perfected its security interest depends upon whether its financing statements fall within that statutory safe harbor.

As luck would have it, two bankruptcy court decisions in Florida with similar facts had reached differing results regarding the safe harbor provision. One court held that the search was *limited* to the initial page of 20 names even though clicking “Next” would have shown the UCC filings in question. In other words, if the UCC filing doesn’t appear on the *first page* of search results, it’s seriously misleading and ineffective. The searcher isn’t obligated to click and search any more.

The other case found a perfected security interest where the financing statement appeared when the “Previous” button was clicked - a financing statement bearing an incorrect name of the debtor is effective as long as it is within a reasonable number of pages from the initial page of 20 names. In other words, the website tells you to view additional search results by clicking previous or next tabs, so the searcher should search more as long as it’s within a reasonable number of pages from the first page.

The court concluded that the appeal depended upon the meaning of “search” in the statutory phrase “a search of the records...using the filing office’s standard search logic.” Was the search fulfilled by only the first page with 20 listings or must other pages be reviewed? Finding uncertainty in lower courts’ interpretation of the safe harbor provisions, the 11<sup>th</sup> Circuit certified three related questions to the Florida Supreme Court: Is the search limited to

or otherwise satisfied by the initial page of 20 names displayed to the user of the Florida Secured Transaction Registry's search function? If not, must the user check all names in the database, using the command tabs? Are there any limits to how many pages the user must go through using command tabs? The Florida Supreme Court will answer these questions for the 11<sup>th</sup> Circuit, which will then use those answers to decide whether Live Oak is perfected or not.

### **WHY WE ARE INTERESTED IN THIS CASE**

North Dakota's search logic is most likely not the same as Florida's search logic. Or like Minnesota's search logic. The final result in the this case may not matter anywhere else if no other state uses similar search logic; too, interpretation of the word "search" may differ from state to state, as the search logic employed varies widely. That's not the point to this article – this case caught our legal eye because it's a good lesson on avoiding a very expensive and time-consuming court battle. Every state maintains a database with its Secretary of State or its equivalent giving the current correct legal name of entities qualified to do business in the state. Errors and omissions can be avoided by diligently checking that database *before* filing any UCC-1 and then inserting the name *exactly* as shown in its organizational documents.

The secured party bears the burden to identify the correct legal name of the debtor; the searcher is no longer obligated to search under multiple name variations. If the financing statement lists the entity name as it appears on the public organic record, your bank should not end up in court arguing about whether an error in the name is "minor" or "seriously misleading." Don't abbreviate. Don't leave out commas, or put commas in if they aren't in the organizational paperwork. Capitalize the capitalized letters and use lowercase letters where lowercase letters are used.

And finally, relevant to us here in the great state of North Dakota because it is an indication of how this issue might resolve here, be aware that the 8<sup>th</sup> Circuit Bankruptcy Appellate Panel affirmed a decision of the Bankruptcy Court which found a financing statement to be seriously misleading when a search using the jurisdiction's standard search logic of the correct legal name "EDM Corporation" failed to find a filed financing statement identifying the debtor as "EDM Corporation d/b/a/ EDM Equipment." See In re EDM Corp., 431 B.R. 459 (BAP 8th Cir. 2010).