



Banking & Debt Capital Markets

General Motors Bankruptcy Court Applies the Brakes to Unauthorized Termination Statements

Last week, the United States Bankruptcy Court for the Southern District of New York held that a UCC-3 termination statement is effective to terminate a financing statement under the Uniform Commercial Code only if the filing of the termination statement was authorized by the secured party whose security interest was terminated.¹ This decision raises the bar on the level of diligence by potential creditors to confirm that any prior liens covering their prospective collateral were effectively terminated. As stated by the Court, “the fact that a termination statement has been filed does not by itself mean that the initial statement came to an end.”

Bankruptcy Judge Robert Gerber denied a motion for partial summary judgment by the Official Committee of Unsecured Creditors of Motors Liquidation Company (formerly known as General Motors Corporation) in connection with the Chapter 11 reorganization of General Motors Corporation. The Committee sought a determination that the principal lien securing a \$1.5 billion term loan to General Motors was terminated prior to the filing of the Chapter 11 case by virtue of a UCC-3 termination statement that mistakenly listed the filing number of the financing statement relating to the security

¹ The case is *Official Comm. of Unsecured Creditors of Motors Liquidation Co. v. JPMorgan Chase Bank, N.A. (In re Motors Liquidation Co.)*, No. 09-00504 (Bankr. S.D.N.Y. March 1, 2013). The Court has certified this decision for immediate appeal to the United States Court of Appeals for the Second Circuit.

interest securing the \$1.5 billion term loan. The Court, however, found that the termination statement had not been authorized and therefore concluded that it was ineffective.²

In October 2001, General Motors entered into a \$300 million synthetic lease as the borrower, with JPMorgan as the administrative agent. In connection with this synthetic lease, UCC-1 financing statements were filed with the Delaware Secretary of State listing JPMorgan as the secured party. In November 2006, General Motors and one of its then-subsiidiaries entered into an unrelated \$1.5 billion 7-year senior secured term loan facility as borrowers, with JPMorgan as the administrative agent for this financing as well. Separate UCC-1 financing statements were filed with the Delaware Secretary of State in connection with the term loan which listed JPMorgan as the secured party.³

In September 2008, General Motors began the process to terminate the synthetic lease transaction, and requested that its outside counsel prepare the necessary documents in connection with its repayment of the outstanding amount of the synthetic lease and release of the security interest on the related properties. After the termination documentation had been distributed to and agreed by counsel for JPMorgan and General Motors, including UCC-3 termination statements, General Motors subsequently filed the UCC-3 termination statements following the repayment of the synthetic lease.⁴ One of the UCC-3 termination statements filed in connection with the repayment of the synthetic lease mistakenly listed the filing number of a UCC-1 that perfected the primary lien related to the November 2006 term loan. This error was not discovered until June 2009, shortly after the filing of the General Motors Chapter 11 case. Under the General Motors Debtor-in-Possession financing, the Court had authorized repayment of the term loan. While all parties agreed that the intent in filing the termination statements was only to terminate those UCC-1s filed in connection with the synthetic lease, the Committee asserted that the

² JPMorgan Chase Bank, N.A., the agent under the term loan facility and the defendant in the adversary proceeding, filed a cross-motion for summary judgment seeking a ruling to the opposite effect.

³ Several UCC-1 financing statements were filed in connection with the \$1.5 billion term loan, the most important of which was a single financing statement that covered the majority of the assets of General Motors.

⁴ The documentation to terminate the synthetic lease consisted of the Synthetic Lease Termination Agreement, the Synthetic Lease Closing Checklist, three UCC-3 termination statements and the Synthetic Lease Escrow Agreement.

erroneous UCC-3, although mistakenly filed, was still legally effective, rendering the \$1.5 billion term loan unperfected at the time of the bankruptcy.

In deciding against the Committee, the Court held that the filing of a termination statement must be authorized by the secured party in order to be effective. The Court examined the requirements for authorization to file a termination statement imposed by § 9-509(d), § 9-510(a) and § 9-513(d) of the UCC. The Court found that “under UCC § 9-513(d), the filing of a termination statement *generally* causes the initial financing statement to which the termination statement relates to no longer be effective. But because UCC § 9-513’s effect is ‘except as otherwise provided in [UCC §] 9-510,’ one must then look to UCC § 9-510, which requires one to look to § 9-509 to ascertain whether there has been authorization.”

The Court then turned to the law of agency to determine whether JPMorgan had authorized General Motors to file the erroneous UCC-3. The Committee argued, based upon communications between General Motors’s counsel and JPMorgan’s counsel, that JPMorgan had granted General Motors actual authority to file the UCC-3, but the Court rejected this argument and found that “neither [General Motors] nor JPMorgan intended, or believed, that their documents would affect anything [other than the termination of the liens related to the synthetic lease].” Accordingly, General Motors, the party filing the UCC-3 termination statement, did not have the authority to make the filing on behalf of JPMorgan.⁵

In ruling that the termination statement was ineffective because JPMorgan did not authorize its filing, the Court expressly disagreed with a contrary ruling from the United States District Court for the Southern District of New York, *Roswell Capital Partners LLC v. Alternative Construction Technologies*.⁶ The Court concluded that the *Roswell Capital* case was incorrectly decided in 2010 because the *Roswell*

⁵ In analyzing the narrow question addressed by the Court in this case, we do not discuss the effect of termination statements incorrectly filed by the secured party itself.

⁶ 2010 U.S. Dist. LEXIS 90695 (S.D.N.Y. Sept. 1, 2010) (holding that a termination statement filed by a borrower was effective, even if the termination statement was not authorized by the secured lender).

Capital court relied on cases decided before the 2001 revisions to Article 9 and because the *Roswell Capital* court incorrectly considered a UCC-3 not to be a “financing statement” as defined in the UCC.⁷

The Court also rejected the *Roswell Capital* court’s conclusion that a secured lender is responsible for monitoring whether a termination statement has been incorrectly filed, specifically questioning the purpose of allocating the burden to the existing lender as once the filing of a termination statement is discovered, even if unauthorized, the security interest would have already been terminated under the prior line of “dramatic and final” cases.⁸

In support of his decision, Judge Gerber cited a recent case from the Supreme Court of New York, *AEG Liquidation Trust v. Toobro N.Y. LLC*,⁹ which disagreed with *Roswell Capital* and ruled that an unauthorized termination statement could not terminate a secured party’s security interest.¹⁰ This decision was in accordance with other decisions that similarly ruled that an unauthorized filing of a UCC-3 was ineffective.¹¹

The Court’s ruling in *General Motors*, as well as the other decisions discussed above, demonstrates that potential creditors should carefully consider the extent of their diligence in connection with termination statements listed in UCC lien searches. As reaffirmed by the Court in its decision, “notice filing” is the regime under the current UCC and “Article 9 only requires information sufficient to engage in

⁷ The Second Circuit affirmed the *Roswell Capital* case, but it did not reach or rule on the question of whether an unauthorized termination statement would be effective to terminate a UCC-1. *Roswell Capital Partners LLC v. Alt. Constr. Techs.*, 436 Fed. Appx. 34 (2d Cir. 2011).

⁸ The Court was also reluctant to agree with *Roswell Capital* that the UCC provides for a right of civil remedy in the case of an unauthorized termination.

⁹ 932 N.Y.S.2d 759 (N.Y. Sup. Ct. 2011).

¹⁰ The *Roswell Capital* decision was also criticized by the Bankruptcy Appellate Panel for the Eighth Circuit, which noted that “*Roswell’s* holding appears to be contrary to the plain language of the Uniform Commercial Code.” *Lange v. Mut. of Omaha Bank (In re Negus-Sons, Inc.)*, 460 B.R. 754, 757 n.10 (B.A.P. 8th Cir. 2011) (ruling that a third party had authority to terminate a lender’s financing statements and that, alternatively, the lender’s security interest was extinguished when its loan was paid in full).

¹¹ See *Official Comm. of Unsecured Creditors v. City Nat’l Bank, N.A. (In re A.F. Evans Co.)*, 2009 Bankr. LEXIS 2473 (Bankr. N.D. Cal. July 14, 2009), *aff’d* 2011 U.S. Dist. LEXIS 51628 (N.D. Cal. May 13, 2011); *In re International Home Products, Inc.*, 2012 WL 6708431 (Bankr. D.P.R. 2012) (secured party remained perfected despite debtor’s filing of termination statement because that filing was unauthorized).

further inquiry.” Secured lenders should be aware that where the public lien search results for a borrower include a previously filed UCC-3 termination statement covering the collateral in question, further inquiry should be conducted to ascertain whether the termination statement was authorized. If the termination statement was unauthorized and thus not effective, the lender’s security interest could be junior in priority to that of the prior secured lender. A prudent potential lender should request documentation, such as a payoff letter, demonstrating that the filing of the termination statement was properly authorized to ascertain that the termination statement is, in fact, effective.

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