



Court Refuses to Admit Uncertified Copies of UCC Records into Evidence

By Paul Hodnefield, Associate General Counsel for Corporation Service Company

In exchange for gaining the benefits of a UCC security interest, Article 9 places the burden of proof on the secured party to demonstrate compliance with all statutory perfection requirements. A secured party may do everything necessary to perfect its security interest yet find enforcement of its rights frustrated if it cannot offer sufficient evidence of compliance with Article 9. A recent case, *Community Shores Bank v. Babbitt's Sports Center, LLC.*, 2012 Mich. App. LEXIS 1528 (Mich. Ct. App. Aug. 2, 2012), demonstrates the risks a secured party faces if it fails to satisfy the burden of proof.

Community Shores Bank (the "Bank") held a security interest in all the assets of a business called Grow's Marine, Inc. The owner of Grow's Marine was a businessman named Rick Sly ("Sly").

In 2007, Sly formed a new entity, BMC Acquisition Company, LLC ("BMC"), to purchase a business called Boston Motors. Sly asked the Bank to finance the acquisition. The Bank agreed on the condition that the loan would also be secured by all the assets purchased in the acquisition, plus all the assets of Grow's Marine. The Bank claimed that it had perfected its security interests in Grow's Marine and BMC by filing financing statements with the Michigan Secretary of State.

The loans to Grow's Marine and BMC went into default early in 2008. At that point, Sly decided to sell the assets of BMC to Babbitt's Sports Center ("Babbitt's"). Sly and his attorney represented to Babbitt's that all the assets of BMC were free and clear of any liens. Babbitt's then purchased the assets of BMC. The Bank, however, was not paid from proceeds of the sale. Consequently, the Bank filed an action against Babbitt's alleging three counts: 1) conversion; 2) a claim under UCC Article 9; and 3) equitable estoppel.

At trial, the Bank attempted to introduce uncertified copies of its financing statements into evidence. The Bank's manager testified that the photocopies were of the financing statements that the Bank filed with the Secretary of State to perfect its security interest. The manager also testified that he did not actually prepare the UCC records, but supervised those who did.

Babbitt's objected to the introduction of the financing statements as evidence. Babbitt's argued that no one from the Secretary of State's office had testified that they were properly filed at the time it purchased the assets from BMC. Moreover, the documents were not originals and the Bank's manager neither prepared them himself nor confirmed with the Secretary of State that the documents were filed.

The trial court found that uncertified copies did not comply with the Michigan Rules of Evidence for admissibility of self-authenticating records. Moreover, the Bank failed to establish that compliant certified copies could not be obtained through due diligence. Therefore, the court ruled that the UCC copies were inadmissible as evidence.

Because the Bank could not prove it was entitled to any UCC remedies, the court ruled in favor of Babbitt's. The Bank disagreed with the decision and filed an appeal.



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The Michigan Court of Appeals reviewed the case and affirmed the trial court's decision. Without admissible evidence, the appeals court ruled that the Bank failed to prove it had perfected its security interest.

The important thing to take away from this case is that the secured party bears the burden of providing that it complied with all the Article 9 requirements for perfection of a security interest. If the secured party cannot document its compliance through admissible evidence, the courts generally will not enforce the security interest.

The burden of proof applies not just to perfection. A secured party that claims a purchase-money security interest must demonstrate when the debtor received possession of the collateral to prove that it filed a financing statement within the applicable time limit. Likewise, if the collateral consists of inventory or livestock, the secured party must provide evidence that it complied with the statutory notice requirements before the debtor received possession of the collateral.

The best practice for a secured party is to thoroughly document every step of the transaction. That includes obtaining proof of delivery for any notices, confirming when the debtor actually received collateral and maintaining records of any UCC filings or searches. If documentation is needed in court, the secured party should obtain certified copies of filed UCC records because they are generally admissible without further authentication.

The secured party alone is responsible for proving its compliance with Article 9 to the satisfaction of the court. Failure to provide sufficient evidence of compliance may limit the secured party's ability to enforce its security interest.

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