community BANKER

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Welcome to the September/ October issue of the COMMUNITY BANKERS' ADVISOR.

The ADVISOR 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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YOU ARE ASKING

Q: North Dakota now has new UCC-1 financing statement forms that have removed the organizational fields. Can we use the old forms if we leave the organizational information out?

A: No. The UCC-1/CNS-1 Financing Statement, UCC Amendment: UCC-3/CNS-3, UCC-5/CNS-5 Overflow Sheet, the Financing Statement for Real Estate and UCC Filing/UCC-1A, and the Real Estate and UCC Filing/UCC-3A forms have been revised to remove the organizational data fields. By the time you read this, the old forms will no longer be accepted for filing. They were accepted up to August 31, 2013. As of September 1, they will no longer be accepted for filing.

For those readers near state borders, be aware that 1) Montana no longer accepts the old forms; 2) Minnesota no longer accepts the old forms; and 3) South Dakota no longer accepts the old forms. Some states, however, do accept the old forms (filing in Louisiana, anyone?). As always, contact the office of the Secretary of State in the particular jurisdiction for information on required forms or any other questions.

Q: Can a W-9 form serve as evidence of a corporate organization's official name for use on a financing statement?

A: No. If your debtor is a registered organization, or the collateral is held in a trust that is a registered organization, the financing statement must provide the name "that is stated to be the registered organization's name on the public organic record

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most recently filed with or issued or enacted by the registered organization's jurisdiction of organization which purports to state, amend, or restate the registered organization's name." N.D.C.C. § 41-09-74(1)(a). A "public organic record" is defined as a record available to the public for inspection and which is:

> (1) A record consisting of the record initially filed with or issued by a state or the United States to form or organize an organization and any record filed with or issued by the state or the United States which amends or restates the initial record;
>
> (2) An organic record of a business trust consisting of the record initially filed with a state and any record filed with the state which amends or restates the initial record, if a statute of the state governing business trusts requires that the record be filed with the state; or
>
> (3) A record consisting of legislation enacted by the legislature of a state or the congress of the United States which forms or organizes an organization, any record amending the legislation, and any record filed with or issued by the state or United States which amends or restates the name of the organization.

N.D.C.C. § 41-09-02(sss)(1), (2), & (3). Translated into plain English, this clarifies that the "public organic record" is the record filed with or issued by the Secretary of State to form an organization -- like the articles of incorporation (or limited liability company articles of organization, or limited liability partnership registration, etc.). Banks are advised to obtain certified copies of articles of incorporation or articles of organization from the Secretary of State, and see that the debtor name used on a financing statement conforms to the name in the public organic record. Please note the distinction between a state's business entity database (which is not a "public organic record") and the actual charter document for an entity. While you can look something up on the state database, it may contain abbreviations or other omissions or errors that could render a filing seriously misleading if that name or form of the name is used instead of the name actually, "officially" shown on the public organic record. When in doubt, a prudent secured party should always refer back to the charter document (or amendments thereto changing the name) for the accurate debtor name.

Q: Does it matter if the punctuation or uppercase letters are not exactly the same as on the public organic record?

A: Maybe. Use the form of the name exactly on the public organic record. Punctuation, spaces, upper/lower case, should follow exactly what is on the filing with the Secretary of State. Although N.D.A.C. § 72-01-02-11 (the administrative rule that addresses filing office search logic) states that no distinction is made between uppercase and lowercase letters and that punctuation marks and accents are disregarded, the actual statute itself requires the name on the public organic record. N.D.C.C. § 41-09-74(1)(a). Use the name *as shown on the record*; the case discussed below is an example of what can happen when it's not the same.

Texas Case Emphasizes Use of Correct Debtor Name

The dispute arose out of the financing and two sales of some equipment, an Ahern Asphalt Plant and a Kawasaki Wheel Loader. CNH Capital America LLC (CNH) financed the purchase of both pieces of equipment by Progreso Materials, Ltd (Progreso). CNH contended that one of the original buyers was Progreso Materials, Ltd.; it further claimed that Progreso had granted a security interest, which CNH had properly perfected. Ultimately, the equipment was sold to Upper Valley Materials, LLC by Progreso. Upper Valley denied that CNH properly perfected a security interest in the equipment; CNH sought a declaration that Upper Valley's interest in the equipment was subordinate to CNH's security interest and CNH sought to foreclose on the equipment. As evidence of perfection, CNH produced as an exhibit a copy of the UCC-1 Financing Statement filed with the Texas Secretary of State showing Progreso as the debtor. However, Upper Valley argued that the financing statement was seriously misleading because the "s" was left off the word "Materials" in Progreso's name. CNH did not argue that a search under Progreso's correct name -

with the "s" in the word "Materials" would have disclosed the financing statement.

The Court found that the UCC-1 Financing Statement did not perfect CNH's interest in the equipment as the filing was deemed to be seriously misleading: The correct name of the debtor was "Progreso *Materials*, Ltd.", but the debtor name on the UCC-1 was "Progreso *Material*, Ltd."

A search of the Texas Secretary of State UCC database using the state's search logic did not reveal CNH's financing statement when the missing "s" was used in the search. The Court reviewed the applicable portion of the Texas Administrative Code which sets out the standard search logic and was persuaded that the omission of the "s" from the word "Materials" would have prevented a searcher using the standard search logic from discovering the financing statement if that searcher used Progreso's *correct* name. In sum, the missing "s" made the filing seriously misleading and the financing statement would not have been disclosed in response to a search under the partnership's correct name.

Could this happen in North Dakota? We compared the Texas Administrative Code provisions for standard search logic with that of North Dakota, and while they have a number of similarities, they also differ in some respects. Texas's description of the search methodology is more detailed, but that does not mean that a missing letter doesn't matter in North Dakota. If nothing else, this case emphasizes the importance of filing under the correct debtor name - check and double-check to see that it's right before the financing statement is filed. CNH Capital Am. LLC v. Progreso Materials Ltd., 2012 U.S. Dist. LEXIS 153464, 78 U.C.C. Rep. Serv. 2d (CBC) 1007 (S.D. Tex. 2012).

Syndicated Lending - Different from Participated Loans

Overview - Syndicated loans often represent a substantial portion of the commercial and industrial loan portfolios of large banks. A syndicated loan involves two or more banks contracting with a borrower, typically a large or middle market corporation, to provide funds at specified terms under the same credit facility. The average commercial syndicated credit is in excess of $100 million. Syndicated credits differ from participation loans in that lenders in a syndication participate jointly in the origination process, as opposed to one originator selling undivided participation interests to third parties. In a syndicated deal, each financial institution receives a pro rata share of the income based on the level of participation in the credit. Additionally, one or more lenders take on the role of lead or "agent" (co-agents in the case of more than one) of the credit and assume responsibility of administering the loan for the other lenders. The agent may retain varying percentages of the credit, which is commonly referred to as the "hold level."

The syndicated market formed to meet basic needs of lenders and borrowers, specifically:

- raising large amounts of money,
- enabling geographic diversification,
- satisfying relationship banking,
- obtaining working capital quickly and efficiently,
- spreading risk for large credits amongst banks, and
- gaining attractive pricing advantages.

The syndicated loan market has grown steadily, and growth in recent years has been extraordinary as greater market discipline has lead to uniformity in pricing. In recent years syndicated lending has come to resemble a capital market, and this trend is expected to continue as secondary market liquidity for these products continues to grow. The volume of syndicated credits is currently measured in trillions of dollars, and growth is expected to continue as pricing structures continue to appeal to lenders or "investors."

In times of excess liquidity in the marketplace, spreads typically are quite narrow for investment-grade facilities, thus making it a borrower's market. This may be accompanied by an easing of the structuring and covenants. In spite of tightening margins, commercial banks are motivated to compete regarding pricing in order to retain other business.

Relaxing covenants and pricing may result in lenders relying heavily on market valuations, or so-called "enterprise values" in arriving at credit

decisions. These values are derived by applying a multiple to cash flow, which differs, by industry and other factors, to historical or projected cash flows of the borrower. This value represents the intangible business value of a company as a going concern, which often exceeds its underlying assets.

Many deals involve merger and acquisition financing. While the primary originators of the syndicated loans are commercial banks, most of the volume is sold and held by other investors.

A subset of syndicated lending is leveraged lending which refers to borrowers with an excessive level of debt and debt service compared with cash flow. By their very nature, these instruments are of higher risk.

Syndication Process - There are four phases in a loan syndication: Pre-Launch, Launch, Post-Launch, and Post-Closing.

The Pre-Launch Process - During this phase, the syndicators identify the borrower's needs and perform their initial due diligence. Industry information is gathered and analyzed, and background checks may be performed. Potential pricing and structure of the transaction takes shape. Formal credit write-ups are sent to credit officers for review and to senior members of syndication group for pricing approval. Competitive bids are sent to the borrower. The group then prepares for the launch.

An information memorandum is prepared by the agent. This memorandum is a formal and confidential document that should address all principal credit issues relating to the borrower and to the project being financed. It should, at a minimum, contain an overview of the transaction including a term sheet, an overview of the borrower's business, and quarterly and annual certified financial statements. This documents acts as both the marketing tool and as the source of information for the syndication.

The Launch Phase - The transaction is launched into the market when banks are sent the information memoranda mentioned above. Legal counsel commences to prepare the documentation. Negotiations take place between the banks and the borrower over pricing, collateral, covenants, and other terms. Often there is a bank meeting so potential participants can discuss the company's business and industry both with the lead agent and with the company.

Post-Launch Phase - Typically there is a two-week period for potential participants to evaluate the transaction and to decide whether or not to participate in the syndication. During this period, banks do their due diligence and credit approval. Often this entails running projection models, including stress tests, doing business and industry research; and presenting the transaction for the approval process once the decision is made to commit to the transaction.

After the commitment due date, participating banks receive a draft credit agreement for their comments. Depending upon the complexity of the agreement, they usually have about a week to make comments. The final credit agreement is then negotiated based on the comments and the loan would then close two to five days after the credit agreement is finalized.

Post-Closing Phase - Post-Closing, there should be ongoing dialogue with the borrower about financial/operating performance as well as quarterly credit agreement covenant compliance checks. Annually, a full credit analysis should be done as well as annual meetings of the participants for updates on financial and operating performance. Both the agent bank and the participants need to assess the loan protection level by analyzing the business risk as well as the financial risk. Each industry has particular dominant risks that must be assessed.

(Taken from the FDIC Risk Management Exam Manual - hat tip to Dawn Ystaas, American Bank Center, Minot)
