

Insights

Seventh Circuit Confirms that under Illinois law, Reference in Financing Statement to Parties' Security Agreement is Sufficient to Perfect Secured Creditor's Lien on Debtor's Collateral Described in Security Agreement

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In *In re IBO Equipment, LLC*, No. 18-3291 (7th Cir. Sept. 11, 2019), the United States Court of Appeals for the Seventh Circuit held that under Illinois' enactment of Revised Article 9 of the Uniform Commercial Code ("UCC"), "the UCC allows a financing statement to indicate collateral by reference to the description in the underlying security agreement." Because Revised Article 9 as enacted in other states – including Indiana – largely mirrors that of Illinois, *IBO Equipment* is noteworthy beyond Illinois.

In *IBO Equipment*, the debtor signed a financing statement with the secured lender which described, in detail, twenty-six listed categories of collateral, such as accounts, cash, equipment, instruments, goods, inventory, and all proceeds of any assets. The secured lender then timely filed a UCC financing statement with the Illinois Secretary of State purporting to cover "[a]ll Collateral described in First Amended and Restated Security Agreement dated March 9, 2015 between Debtor and Secured Party." Thereafter, the debtor defaulted and filed a chapter 7 liquidation petition for relief under the United States Bankruptcy Code. The debtor's chapter 7 trustee sought to set aside the secured lender's security interest in the debtor's assets, on the grounds that the description in the UCC financing statement – specifically, the reference back to the parties' security agreement, which was *not* filed with the Illinois Secretary of State – was insufficient under Illinois law to perfect the secured lender's security interest in the debtor's collateral. The bankruptcy court agreed with the chapter 7 trustee, and by agreement the parties pursued a direct interlocutory appeal to the Court of Appeals.

Reversing the bankruptcy court, the 7th Circuit held that under Illinois law, the financing statement's reference to the parties' security agreement, for the description of collateral, was sufficient to perfect the secured lender's security interest in the debtor's collateral - even when the security agreement is not attached as an exhibit to the financing statement. Specifically, the court noted that Illinois UCC §502 requires that a financing statement must "indicate" the collateral covered by the financing statement, that Illinois UCC §504 provides that "[a] financing statement sufficiently indicates the collateral that it covers if the financing statement provides: (1) a description of the collateral pursuant to Section 9-108; or (2) an indication that the financing statement covers all assets or all



personal property”, and Illinois UCC 9-108 provides six ways to describe collateral, including by “any other method”, so long as the identity of the collateral is “objectively determinable.” (Apparently the lender in *IBO Equipment* chose not to avail itself of Section 504’s safe harbor financing statement collateral descriptions of “all assets” or “all personal property”, and instead pursued a description of collateral as permitted under Section 9-108.) Accordingly and based upon its interpretation of these provisions of Illinois’ Revised Article 9, the 7th Circuit held that “[t]he plain and ordinary meaning of Illinois’s revised version of the UCC allows a financing statement to indicate collateral by reference to the description in the underlying security agreement.” Note that Indiana’s UCC provisions mirror those at issue in *IBO Equipment*.

Takeaways: how a secured lender describes the collateral covered by its security interest in its UCC financing statement is critically important at the loan documentation stage, as noncompliant descriptions later may be tested – and found wanting – in the crucible of the bankruptcy court. Moreover, using UCC Section 504’s “safe harbor” for financing statement collateral descriptions of “all assets” or “all personal property” may avoid litigation of the sort faced by the lender in *IBO Equipment*.

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