



Preserving Perfection After Your Debtor Enters Bankruptcy: Filing a Continuation Statement May Not Be Necessary, But Do it Anyway

October 12, 2018

Bridget Hart (973) 849-9013

In a recent opinion, a Maryland bankruptcy court judge indirectly reminds us of a simple message to be shared with our clients who hold perfected liens on assets of a debtor who enters bankruptcy: file your continuation statement and save on legal fees.

Filing a financing statement is one way to perfect a creditor's security interest in a debtor's assets. Such financing statements consist of a legal form that a creditor files, generally with the office of the state's secretary of state, which serves to give notice to other potential creditors of that interest in certain property.

Pursuant to the Uniform Commercial Code, a filed financing statement is effective for a period of five years after the date of filing. Within six months of the expiration of a financing statement, a creditor should file a continuation statement to retain its interest in the debtor's property.

In *Firsttrust Bank v. Industrial Bank (In re Essex Construction)*, 17-00156 (Bankr. D. Md. Sept. 25, 2018) there were two secured creditors of the Chapter 11 debtor, each providing loans to the debtor secured by pre-petition perfected security interests in all of the debtor's assets.

The senior creditor failed (post-petition) to file a continuation statement in the debtor's assets prior to the five-year expiration period that *would* have allowed its pre-petition lien to lapse during the pendency of the bankruptcy.

However, the Maryland judge's ruling found that no continuation statement was needed in this instance because of the well-established "freeze rule," which holds that valid liens existing at the time of the commencement of bankruptcy proceedings are preserved – or "frozen."

Consistent with the "freeze rule," the judge in *Essex Construction* found that liens perfected on the date of filing will not expire at the end of five years, as they would outside bankruptcy, without the filing of a continuation statement.

Therefore, the junior creditor could not step into the shoes of the senior creditor for purposes of taking proceeds from the liquidation of the debtor's assets.

So, why file a continuation statement anyway?

There's no penalty for filing the continuation statement. While unnecessary, it is easy to complete.

Because the two banks in *Essex Construction* agreed on all the facts, only a question of law and the matter was decided on a motion for summary judgment remained. The judgment repeated well-established law and made no new law. The expense of getting the judgment was incurred nonetheless.

The bottom line: avoid the expense of becoming the subject of a bankruptcy court decision, law review case-note or a "client alert" and file your continuation statement.

Please note that this is a general overview of developments in the law, and does not constitute legal advice. Nothing herein creates an attorney-client relationship between the sender and recipient. If you have questions regarding these provisions, or any other aspect of employment law, please contact Michael H. Traison at (312) 860-4230 or mtraison@cullenanddykman.com

Practices

- Banking and Financial Services

Industries

- Financial Institutions

Attorneys

- Michael H. Traison