



"Advertising Material"

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## FACING THE ISSUES®

LEGAL BRIEFS FROM THE ATTORNEYS OF MACKALL, CROUNSE & MOORE, PLC

### Creditors' Corner

#### **Creditor Loses Priority Because of Failure to Observe Reasonable Commercial Standards in Searching for Debtor's Incorrect Name**

Priority is always critical because the first Lender in line gets paid in full before competing Lenders get anything. Obviously you need to use the Debtor's correct name. But Courts are also not kind to lenders who fail to make a diligent search of incorrect names. In the case of *In re Jersey Tractor Trailer Training, Inc.*, 2007 Bankr.Lexis 3365 (D.N.J. 2007) the secured party failed to sustain priority because it failed to observe reasonable commercial standards in conducting a UCC search on the incorrect Debtor name. Lenders should be aware that UCC retrieval systems work through a set of rules called "search logic." There are two broad categories of "search logic:" 1) State Standard Search Logic ("SSL") and 2) Name Variation Search Logic ("NVSL"). Lenders should be aware that SSL produces very narrow results which should probably only be used to verify the correct name of the Debtor. The goal of commercially reasonable due diligence is to identify all of the facts that may affect the transaction. NVSL either matches the first characters of the name or looks for keywords. If the filing office does not offer this logic the Lender may have to use a commercial firm to do the search. The Lender should obtain copies of all disclosed records and then must properly evaluate the results. Taking these steps will avoid the result of losing priority.

#### **Mortgage Foreclosure Tax Issues**

Foreclosure can result in unexpected tax consequences. First and foremost lenders should advise borrowers in writing that: "Lender has provided no tax advice to Borrower. Borrower represents to Lender that Borrower has sought and obtained all appropriate tax advice with regard to this transaction." Lenders should also be aware there are two major categories of tax consequence when a foreclosure occurs: 1) Gain or loss on the transfer when the foreclosure is effective, and 2) Cancellation of Debt Income when the debt discharged exceeds the fair market value of the property the borrower gives up. There are special calculation rules which also apply, but Lenders should be aware that the Borrower is not out of the woods just by voluntarily giving property back to the Lender. Bankruptcy, "short-sales," restructures, like kind exchanges and other resolutions of debt have varying tax consequences some of which may impact the lender when the asset is finally liquidated. Follow the Practice Pointer we offer above.

#### **Bankruptcy Fundamentals for the Financial Service Industry: A Handbook for Non-Lawyers**

Once again, Mackall, Crouse & Moore, PLC, has sponsored a short handbook on bankruptcy fundamentals. This handbook covers not only general topics such as the automatic stay, but also answers commonly asked questions. Look for your copy of this handbook to arrive in the next couple of weeks.

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If you have any questions, please call one of the following in our MCM Creditors' Remedies group:

**Timothy D. Moratzka**

(612) 305-1456

[tdm@mcmlaw.com](mailto:tdm@mcmlaw.com)**Robert S. Lee**

(612) 305-1448

[rsl@mcmlaw.com](mailto:rsl@mcmlaw.com)**Stacy A. Woods**

(612) 305-1409

[saw@mcmlaw.com](mailto:saw@mcmlaw.com)**Andrew P. Moratzka**

(612) 305-1418

[apm@mcmlaw.com](mailto:apm@mcmlaw.com)**Allen E. Christy, Jr.**

(612) 305-1490

[aec@mcmlaw.com](mailto:aec@mcmlaw.com)**Patrick C. Summers**

(612) 305-1473

[pcs@mcmlaw.com](mailto:pcs@mcmlaw.com)**Matthew A. Anderson**

(612) 305-1401

[maa@mcmlaw.com](mailto:maa@mcmlaw.com)**Mychal A. Bruggeman**

(612) 305-1478

[mab@mcmlaw.com](mailto:mab@mcmlaw.com)

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1400 AT&amp;T Tower • 901 Marquette Avenue • Minneapolis, MN 55402

Telephone: 612.305.1400 • Fax: 612.305.1414

E-mail: [info@mcmlaw.com](mailto:info@mcmlaw.com) • Web: [www.mcmlaw.com](http://www.mcmlaw.com)