

Focus on Finance

In the last year due diligence has increasingly become a focus of many involved in financial transactions. Those institutions that understood how the various public records fit the due diligence picture and didn't cut corners fared well, while some institutions that engaged in a philosophy of limited documentation have been adversely effected by the economic downturn.

CLAS Information Services has spoken to many clients and during these conversations we discovered that while some clients understood how public information fit into the due diligence puzzle, others had a very limited or inaccurate view of the documents they were using on a daily basis.

In the next several issues we will discuss public records as a due diligence tool. We will attempt to educate, inform and explain how documents share common

bonds that can provide you a more complete picture of a potential borrower. We hope that arming you with this information will help you mitigate risk in your operations.

In this issue we examine certificates of status / good standing in an attempt to sort out fact from fiction.

We will review online corporate systems and the dangers associated when relying on these systems to determine debtor names.

Not involved in finance? We have plenty of information for you as well! In addition to our "News from the Jurisdiction" feature we discuss Twitter and the closure of the Fresno Branch office of the Secretary of State.

Judy

Judy Kahler
President &
CEO



Finance Issue

Not in finance? Check the table of Contents.

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Good Standing Certificates - Red Flags Abound

A good standing certificate is a document that certifies a business entity has met the filing requirements to incorporate/organize in a state and is authorized to conduct business. It generally implies that the business entity has filed articles of incorporation / organization or qualification documents (at a minimum) and paid a filing fee. It also indicates that the business entity has met the state's requirements to be recognized in the state as a corporation, LLC, etc.

A good standing certificate does not prove that a company is a valid business. Why? A newly formed company that has not approved any minutes, or filed any lists of the officers and directors is a 'legal' company in the sense that they have met the minimum filing requirement under the law and paid the filing fee. This company can obtain a good standing certificate even though they have never transacted business.

The issue with this is that a market exists for corporations that are called "shell" or "shelf" companies. These are business organizations that have been formed and put on the "shelf" waiting for someone to purchase them. At some point annual reports might be filed and suddenly the company has a very attractive formation date. Purchasing "shell" companies gives the appearance of being in existence for several

years, but these companies are hollow and have had no officers, directors or shareholders until they were purchased. A good standing alone will not provide evidence of a legitimate business activities.

A danger exists in using a good standing certificate to validate a debtor's name. Why? A good standing certificate and the name of a debtor as it appears in the public record could be very different. A good standing certificate provides the name of the business organization as it appears in the corporate filing offices computer. As discussed in the next article "*when Is a Debtor's Name, Not a Debtor's Name*" on page 3, amendments to the Uniform Commercial Code passed in many states have clarified that only the articles of incorporation and amendments should be relied upon to determine the debtor's name.

Some clients feel that if they obtain a good standing certificate they need not worry about the entity that they are doing business with as they have obviously met all state obligations. This is also untrue.

There are several states where a corporation can appear in good standing literally one day only to be revoked, suspended (or other terms used to indicate a businesses authority to transact business has been terminated) the next. In Nevada, for example, a good standing ordered on December 31st can offer little assurance as to what the next day brings as annual reports are due on January 1st. Corporations that have not filed their annual reports are suspended the following

day with no grace period. In California the state is rather inconsistent when it comes to annual report filings. Although some companies can go for more than a year without filing, others are caught and suspended suddenly. If you are not verifying that requirements such as current Statement of Information (California's annual report) is on file, you may find the status of the corporation has suddenly changed.

"Your borrower could suddenly become suspended or revoked for failure to pay taxes."

The most worrisome of all can be the pitfalls surrounding the payment of taxes and good standing. A corporation could be in compliance with their annual reports, while failing to file tax returns and pay taxes. In several states the tax department shares the power to suspend (or void) a business entity with the Secretary of State or filing office. If you are not checking to make sure that the corporation is in good standing at both the tax authority and the filing office for business entities, your borrower could suddenly become suspended or revoked for failure to pay taxes.

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When Is a Debtor's Name Not the Debtor's Name?

It is still surprising that eight years after the passage of Revised Article 9, the question of the 'legal name' of a debtor is still a topic of discussion. Although most thought that the passage of Revised Article 9 would streamline the process, it has had the opposite effect.

The issue of 'the legal name of a debtor' arose from the first day of enactment of Revised Article 9. Secured parties or their attorneys had to interpret the phrase 'name as it appears in the public record.' Some secured parties interpreted this to be the articles of incorporation/organization and any amendments, while others felt the phrase referred to any

search system the corporate division made public.

The legal question of what constitutes an organizational name continues to be up for debate, but it is a rapidly changing area of the Uniform Commercial Code. If you are not using the organizational documents to determine debtor name, be prepared for changes.

In the last 18 months the issue of debtor name has been gaining momentum. Several states have enacted amendments to the commercial code to add language to specify that the 'public record' only refers to the name as it appears in the organizational documents and any amendments filed. These laws create a safe haven for filers that utilize the organizational documents to determine debtor name. These laws also have an effect on individual names and what documents should be relied upon in determining the debtor name for an individual. However, in this article we will only focus on organizational names.

made it a practice in these old systems to abbreviate common words because of system limitations or to save on storage space.

As technology improved and costs on storage decreased, the practice continued either because legacy systems limited what could be entered, or because it was departmental policy. This resulted in two separate names that could possibly be located and argued as the

meant to make it easier for secured parties to locate similarly named debtors and to prevent lawsuits, it has in fact had the opposite effect.

This issue of two different names in the public record is intensified when you consider that the 'standard search logic' that a state uses is generally inflexible and unforgiving when it comes to name variations. Differences as minor as spaces, punctuation or abbreviations



legal name of the debtor. Although the differences in the two names could be minor, depending on the state these minor differences could affect what is located using the standard search logic.

The standard search logic is the litmus test to determine whether or not a debtor name is seriously misleading. If a debtor name locates a filing, the name is not seriously misleading (even if the name contains minor errors and omissions). If the name is not located using the standard search logic of the state, then the name is seriously misleading. Although this name test was

can have detrimental effects.

This issue with legal names is of such a concern that the PEB (Permanent Editorial Board) for the Uniform Commercial Code is expected to issue a series of recommendations this year for amendments that states should enact regarding the legal name of an entity. As this is a rapidly changing area of law, anyone who files UCCs should carefully monitor changes to the Commercial Code in all states in which they have filings and be prepared to file amendments and change policies for determining debtor names. •

Are You Locating Federal Tax Liens On Your Official Search?

UCC SEARCH REPORT

Debtor Name Searched: ABC Company A Delaware LLC

0802112008 12/15/2008 Internal Revenue Service

Department of the

Fresno

08045520

Department of

08045520

Department of

Fresno, CA 93888

0802112008 12/15/2008 Bank of Money

833 N. 2nd Street

Are You Sure?

The IRS often files under names that may not be located on the official search. Find out why this should concern you, and what we can do to help!

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Why did this become an issue in the first place?

Corporate divisions within the state filing office never anticipated that their information would be utilized for the Uniform Commercial Code. Therefore, the groundwork for debtor names issues was created years ago when computer systems were as big as houses and memory and storage capacity for these behemoths was expensive. If you think back, you will realize that there is nothing in the Corporations Code that specified that names be entered into an electronic database in any specific manner. In fact, many states

Secretary of State Closes Fresno Branch Office

Since the court has ruled that the constitutional offices must also observe the furloughs the Secretary of State of California was left with the task of shaving 2,200 hours of staff time per month.

The first cut was announced on May 1, when the Secretary of State California announced that they would be closing their Fresno Branch Office effective May 29, 2009.

As the budget crisis continues to develop, changes are

happening at an unprecedented pace.

You can subscribe to CLAS BULLETIN for critical announcements. Visit our web page at www.clasinfo.com and click on SUBSCRIBE.

You can also follow us on twitter.com for up-to-the-minute updates on changes that are occurring. Not familiar with Twitter? See the story on the next page, *'Tweet, Tweet, Twitter!'* to learn about micro-blogging and why you should be doing it. •



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GOOD STANDING - Cont'd From Page 1

Things to remember:

- Do not rely on the good standing certificate for the name of your debtor if you are filing a UCC.
- If you are checking good standing in a state where the tax authority has the power to suspend or void, request that the Tax Department also be checked for status.
- Verify that annual reports are current, and when the next annual report is due, to avoid changes in status.
- Obtain copies of annual reports to ensure that officers and directors have been named for the company, or use the CLAS Corpcheck report.

In this article we focused solely on the good standing certificates and touched briefly on taxes, annual reports and filing due dates. In future articles we will look at other public documents and the relationship they share to due diligence. •

Tweet, Tweet, Twitter™ ...

News You Need 140 Characters At a Time

CLAS is an information resource to you, our clients, and we know that you rely on us to keep you advised as to what is happening in the information field. The challenge is that although we receive many pieces of information daily, it is not possible to send emails about all of them without overwhelming your in box!

Twitter, on the other hand delivers SMALL bite-sized bits of news in less than 140 characters (about the length of this sentence you just read.) This length is generally enough to convey an idea without taking more of your time than is absolutely necessary. Best of all, Twitter updates can be received and viewed on your handheld, an RSS feed, via email, your twitter page or sent to your social networking account (Facebook).

What's in it for me?
Twitter gives you the ability stay informed

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Tweets are text-based posts of up to 140 characters in length. The tweets are displayed on the user's profile page and delivered to other users who have subscribed to them (known as followers). Senders can restrict delivery to those in their circle of friends or, by default, allow anybody to access them.

What's the Catch?

Nothing. You can unsubscribe at any time. However, once you use Twitter and discover how you can stay in the loop in 10-20 seconds a day, you will wonder how you ever got by without it. •

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without information overload. Our Twitter page is never filled with useless information. We only post information that affects your business. Topics in our most recent postings include:

- Delays at the State
- Annual Report Due Dates
- State Office Closures
- State Holidays
- Jurisdiction Fee Increases
- State Announcements

You choose the distribution method that works best for you, with Twitter.Com!

View our page at twitter.com/clasinfo and click Follow CLASINFO if you would like to twitter!

Not yet on Twitter? See why The New York Times calls Twitter "one of the fastest-growing phenomena on the Internet." TIME Magazine says, "Twitter is on its way to becoming the next killer app," and Newsweek noted that "Suddenly, it seems as though all the world's a-twitter."

What is Twitter?

Twitter is a free micro-blogging service that enables users to send and read other users' updates known as 'tweets.'

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News From Jurisdictions

CALIFORNIA

The Secretary of State's office adopted regulations on May 14, 2009 that (1) provide guidelines to assist the public in selecting a business entity name prior to reserving the name or filing documents with the Secretary of State; (2) provide the public with more certainty that a proposed business entity name will meet statutory standards; and (3) assist Secretary of State staff in determining if a proposed business entity name is acceptable, ensuring more consistency in the application of the statutory standards. Information containing the text of the regulations can be found at:

<http://www.sos.ca.gov/business/be/forms/regulations-business-entity-names-text-05142009-final.pdf>

LOS ANGELES COUNTY

Los Angeles county has increased the fee for recording real estate instruments by \$1 effective April 27, 2009.

DELAWARE

Due to changes in Delaware Corporate Law 2009 is the first year corporations will be 'Voided' for failure to file an annual report. All Delaware corporations that have not filed an annual report by March 1, 2009, and are therefore subsequently voided will be required to pay all taxes, penalties, interest and file ALL annual reports that were due at the time they were declared void. •

Previously in the state of Delaware when a good standing certificate was requested,

We welcome your comments, feedback or suggestions. Please contact edward@clasinfo.com for submissions, story ideas, or other comments.

CLAS Information Services would include the printout from the state verifying the authentication number.

Based on client comments we have instituted a change to our procedures to omit this additional piece of paper.

Clients can confirm the validity of any document issued by the Department of Corporations by accessing the following link:
<http://www.corp.delaware.gov/authver.shtml>

We always welcome clients' comments regarding changes that would result in better service so please contact us if there is something we can do to make working with us easier.

KENTUCKY

Original signatures are no longer required for corporate filings; however, original supporting documentation for entities qualifying in the state continues to be required. Contact your customer service representative for more information.

MARYLAND

The state of Maryland requires a business entity withdrawing from the state to appoint a registered agent for service of process for a period of one year. CLAS Information Services, through our affiliation with National Registered Agents, can arrange this service for you in the state of Maryland. Please contact your customer service representative for more information.

TEXAS

Texas has announced that they will no longer send notices when it is time to file the Texas Public Information Form (which is required to be filed annually), nor will business organizations receive necessary tax forms for filing automatically.

Texas has also changed tax codes so that all business entities now create a tax liability, unless the business organization is designated as 'tax exempt.' Limited Partnerships, Limited Liability Partnerships, etc., are now required to file an Annual Franchise Tax Report and Public Information Reports annually (previously these entities had no annual filing requirement.)

VIRGINIA

Virginia has enacted changes to UCC Article 9 that become effective July 1, 2009. The changes clarify what debtor name should be used if the debtor is an individual. The secured creditor creates a safe harbor "if the financing statement provides the individual's name shown on the individual's driver's license or identification card issued by the individual's state of residence."

Remember that failure to provide the correct name can result in a seriously misleading financing statement.

Changes similar to this one have already been enacted in the states of Texas and Tennessee. Many other states have similar measures under consideration.

Secured parties should ensure that any financing statements in the state of Virginia filed against individuals contain the name of the individual as reflected on these documents or risk having seriously misleading financing statements of record.