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**PERFECTION OF A TRANSFER FROM A GOVERNMENTAL ENTITY -
THE MP STAR FINANCIAL CASE**

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The Ohio Supreme Court issued a troubling opinion on December 7, 2005, which held that Article 9 of the Ohio Uniform Commercial Code did not apply to the grant of a security interest in the accounts receivable of a borrower owing from governments, states, or governmental units. The case, *MP Star Financial, Inc. v. Cleveland State Univ.*, 107 Ohio St. 3d 176 (2005), involved a typical factoring arrangement. An employment service, Metro Temps, as assignor, transferred accounts receivable to MP Star, as assignee, and MP Star acquired an interest in payment obligations owed by account debtors on the accounts. Metro Temps provided employment services to Cleveland State University, and created an account receivable by billing the university. Metro Temps transferred the Cleveland State accounts receivable to MP Star pursuant to the factoring relationship.

Although Cleveland State was notified of the assignment, Cleveland State continued to pay Metro Temps instead of MP Star. MP Star filed an action against Cleveland State, arguing that the university violated the terms of the assignment. The Ohio Supreme Court looked to Ohio Revised Code (“ORC”) Section 1309.109(D)(14), which is a non-uniform provision of Revised Article 9, to hold that Chapter 1309 of the ORC (analogous to Article 9 of the UCC) (a) did not apply to any transfers of a government, state, or governmental unit and (b) that the granting of a security interest in a government account receivable was a “transfer.”

Unfortunately, this decision means that any security interest obtained from a federal, state or local governmental unit, whether the Bureau of Workers Compensation, Medicare, Medicaid, the Department of Defense, or any other governmental entity is, under Ohio law, outside the scope of Article 9. Consequently, obtaining a security agreement and filing a UCC-1 financing statement against a vendor who provides goods or services to governmental entities is not sufficient to perfect a security interest in those accounts receivable.

Under pre-UCC common law in Ohio, a lender obtained an interest in an account receivable by notifying the account debtor of the interest prior to any other assignor and by giving consideration (such as a loan). Although this process sounds simple, there are several issues to consider. For example, secured parties should determine whether they have notified the governmental unit of the assignment, and, if they have not, who is the proper person at the governmental unit to be notified about those accounts receivable. The secured party should also verify that the notification has been received and acknowledged by the governmental unit.

Another disconcerting aspect of the *MP Star* case is that MP Star apparently *did* notify Cleveland State that the accounts receivable had been assigned. Although both the common law and the UCC recognize that there are other ways to “perfect” an interest that does not fall under the UCC, the Ohio Supreme Court did not even address the issue of “perfection” outside of the UCC when rendering its decision. It is certainly difficult to believe that the Supreme Court intended to prevent any and all ability to “perfect” a security interest in accounts receivable generated by a government account debtor, but the lack of discussion on this issue is disturbing nonetheless.