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How to Hold Your Liquor (License)

Perfecting and Enforcing Liquor License Liens

A liquor license can be an extremely valuable asset of a business. In states that allow for liens to be attached to a liquor license, creditors lending to entities or individuals that control liquor licenses should take steps to attain a security interest in the license in the event the debtor fails to make payments on the loan or otherwise defaults. A liquor license is a legal authorization to serve alcohol and is therefore not easily defined collateral. Accordingly, perfecting and executing a lien on a liquor license is often a complicated and difficult exercise.

When creditors seek to secure an obligation with a liquor license as collateral, the threshold inquiry is whether the state in which the license was issued allows for a lien to attach to such liquor license. Liquor license laws vary greatly among the states, largely depending on whether the state characterizes the license as property or privilege. For example, a liquor license may be granted as collateral in Pennsylvania, as it characterizes liquor licenses as *property* between a licensee and a third-party creditor and as a *privilege* between a licensee and the liquor control board.¹ Accordingly, lenders may attach a lien on the liquor license because it is considered property in that state.² On the other hand, New Jersey prohibits liens on liquor licenses, specifically stating that a liquor license shall not be deemed property.³

Most states are divided into two liquor license constructs: quota and non-quota. In a non-quota state, liquor licenses hold little to no value because there are no limits on the number of licenses issued; therefore, licenses are plentiful and easily attainable by businesses.⁴ In these states, creditors would have little to gain by placing liens on liquor licenses. Moreover, as in New Jersey, creditors are sometimes prohibited from granting a security interest or allowing the attachment of a lien on a license altogether.⁵

Quota states place population-based caps on the number of liquor licenses available in each county

or municipality, which forces businesses to look for a license on the secondary market, thereby driving up the value. Liquor licenses in quota states are regularly interpreted as property and could have substantial value in areas with maxed-out quotas. States permitting liens on a liquor license include Florida, Massachusetts, Michigan, Montana, New Mexico, Pennsylvania and South Dakota.⁶

Properly Perfecting a Liquor License

In order for creditors to have a legal right to take possession of a liquor license in the event of a default, they must comply with the governing state's version of Article 9 of the Uniform Commercial Code (UCC) covering secured transactions.⁷ Attaining a lien on a liquor license under the UCC in states that recognize liquor licenses as property is accomplished by properly attaching and perfecting a security interest in the liquor license.⁸

To attach a security interest in the liquor license: (1) the value must be given for the security interest by the secured creditor; (2) the debtor must have rights in the collateral (in this instance, the liquor license) or the power to transfer rights in the collateral; and (3) the debtor must grant a security interest in the collateral to the debtor.⁹ The grant of a security interest is typically contained in a security agreement or other written document, and most lenders/lessors rely on an executed security agreement to ensure proper attachment.¹⁰

Once a security interest is attached through a security agreement, creditors must perfect the security interest. A secured party perfects a security interest to have priority over other parties in the event that the borrower defaults or becomes insolvent.¹¹ Pursuant to UCC § 9-301, while collateral is located in a jurisdiction, the local law of that jurisdiction governs perfection, the effect of perfection or nonperfection, and the priority of a security interest in collateral.¹²

States recognizing liquor licenses as property provide for different perfection methods. Several



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1 See 47 Pa. Stat. Ann. § 4-468(d); see also *In re B & M Hosp. LLC*, 584 B.R. 88, 92 (Bankr. E.D. Pa. 2018) (holding that between debtor/licensee and third party, liquor license constituted property under Pennsylvania law, in which security interest could be granted).

2 *Id.*

3 N.J. Stat. Ann. § 33:1-26 ("Under no circumstances, however, shall a license, or rights thereunder, be deemed property, subject to inheritance, sale, pledge, lien, levy, attachment, execution, seizure for debts, or any other transfer or disposition whatsoever, except for payment of taxes, fees, interest and penalties imposed by any State tax law.").

4 See, e.g., City of Baltimore Liquor License Bd., "Application Process," available at lib.baltimorecity.gov/application-process (unless otherwise specified, all links in this article were last visited on April 25, 2023).

5 See N.J. Stat. Ann. § 33:1-26; IC § 7.1-3-1-2, interpreted by *Matter of Eagles Nest Inc.*, 57 B.R. 337, 341 (Bankr. N.D. Ind. 1986); Cal. Bus. & Prof. Code § 24076.

6 See 34 Fla. Stat. Ann. §§ 561.32-561.35; 20 Mass. Gen. Law ch. 138, § 23; *Brown v. Yousif*, 445 Mich. 222, 232 (1994); Mont. Code Ann. § 16-4-404(8); N.M. Stat. Ann. § 60-6A-19; 47 Pa. Stat. Ann. § 4-468; S.D.C.L. § 35-10-18.

7 U.C.C. § 9-201.

8 U.C.C. §§ 9-203, 9-308.

9 U.C.C. § 9-203(b).

10 U.C.C. § 9-102(74) ("Security agreement" means agreement that creates or provides for security interest).

11 U.C.C. § 9-308.

12 U.C.C. § 9-301.

quota states will accept general UCC-1 financing statements to perfect a security interest in a liquor license,¹³ while other states require specific forms to be filed in order to properly perfect the lien.¹⁴ The UCC determines the priority of a creditor's claim to the collateral, and for secured lenders, the UCC priority rules are set forth in § 9-322.¹⁵ Priority with respect to a liquor license lien is typically based on the time of filing but, as previously stated, the jurisdiction whose law covers whether perfection has occurred also governs priority.¹⁶

The UCC requires the description of the property in the security agreement and UCC-1 financing statement to "[r]easonably identify" the collateral subject to the lien.¹⁷ For most collateral, examples of reasonable identification are a description that identifies the collateral by specific listing, category, collateral type, quantity, formula or any other method if the collateral's identity is objectively determinable.¹⁸ The official comment to UCC § 9-108 provides that while an "all assets" or "all personal property" description for purposes of a security agreement is not sufficient, under § 9-504, a UCC-1 financing statement sufficiently indicates the collateral if it "covers all assets or all personal property."¹⁹

With respect to liquor licenses, courts have looked to security agreements for identification purposes when the UCC-1 financing statement failed to properly identify the liquor license. However, many courts have held that a specific reference to the liquor license identification number is required to be included on the UCC-1 financing statement in order to properly perfect a security interest in the liquor license.²⁰

Despite the UCC's relatively relaxed description requirements for financing statements, the best practice for secured lenders seeking to perfect a security interest in a liquor license is to specifically describe such license in both the security agreement and the UCC-1 financing statement. This practice provides lenders with additional security in the event that there are issues with either document and removes any doubt with respect to the priority of one creditor over another based on a more specific description of the liquor license in the security agreement and/or UCC-1 financing statement. If the liquor license number is unknown at closing, creditors should require the debtor to execute an amendment to the security agreement once the borrower receives such information.

It is also important that creditors confirm the liquor license lien procedures with local counsel due to the variation in the process among states. For example, in Pennsylvania, although a creditor may perfect a security interest in a liquor license by filing a UCC-1 financing statement pursuant to the

Pennsylvania UCC, the Pennsylvania Liquor Control Board (PLCB) will not recognize a third party's security interest unless such third party goes through a number of procedural steps with the PLCB.²¹ Similarly, in Massachusetts, UCC-1 filings afford creditors a security interest, but secured lenders also must gain approval by the local licensing authority and the Alcoholic Beverage Control Commission.²² In addition, a pledge of a license to secure a lease is not permitted under Massachusetts law.²³ In Florida, a lender must record the lien with the Division of Alcoholic Beverages and Tobacco using that department's specific form within 90 days of the creation of the lien.²⁴ Other states may have similar restrictions on liquor licenses, which must be researched to ensure proper perfection.

Creditors should be aware of the varying state procedures and requirements necessary to properly attach and perfect a security interest in a liquor license, assuming that the state even allows for such liens.

Execution Issues

Invariably, issues are likely to arise when lenders attempt to execute on a liquor license after the debtor files for bankruptcy or defaults under a security agreement. Common issues include the following: (1) the active license converting to a "safekeeping" status or otherwise expiring under the state law and local procedure; (2) the UCC-1 financing statement lapses; or (3) the parties fail to comply with applicable state laws and procedures when executing against the liquor license.

Some quota states impose "safekeeping" status on liquor licenses under certain circumstances, which sometimes proves to be problematic for creditors. In Pennsylvania, a liquor license may change status from "active" to "safekeeping" when a licensed establishment closes for a consecutive period of time, regardless of the reason, and the PLCB deactivates the license and holds the license in safekeeping while the establishment is closed.²⁵ When a license is in safekeeping for an extended time period, it will either be (1) reinstated by actions of the current licensee; (2) sold to another party; or (3) extinguished if the quota in that state's county or municipality is greater than permitted by the state. Accordingly, "to have a license reissued from safekeeping, [a]n application for return of the license shall be filed by the licensee," which includes additional fees.²⁶ If the license is reinstated by the debtor, a creditor that maintains a perfected interest in the license may pay necessary fees and taxes to execute on the

13 See 47 P.S. § 4-468(b); "Information Regarding Third-Party Claims Upon a Liquor License," Pa. Liquor Control Bd. (April 27, 2017), available at lcb.pa.gov/Legal/Documents/Information%20Regarding%20Third%20Party%20Claims%20Upon%20A%20Liquor%20License.pdf (hereinafter referred to as the "PLCB Guidance on Third-Party Claims").

14 See Fla. Stat. Ann. § 561.32.

15 *Id.*

16 See U.C.C. § 9-301.

17 See U.C.C. § 9-108(a) ("[A] description of personal or real property is sufficient, whether or not it is specific, if it reasonably identifies what is described."); U.C.C. § 9-203(b)(3)(a).

18 U.C.C. § 9-108(b).

19 U.C.C. § 9-108, cmt. 2.

20 See, e.g., *In re B & M Hosp. LLC*, 584 B.R. 88, 96 (Bankr. E.D. Pa. 2018) (citing 13 Pa. C.S.A. § 9-101 cmt. 4(h); 13 Pa. C.S.A. § 9-108, cmt. 2); see also *In re Ciprian Ltd.*, 473 B.R. 669, 675 (Bankr. W.D. Pa. 2012) (generic description such as "general intangibles" was broad enough to give creditor security interest in debtor's liquor license); *In re TSAWD Holdings Inc.*, 565 B.R. 292, 303 (Bankr. D. Del. 2017) (description "all assets of debtor" in security agreement was sufficient to identify disputed goods in question).

21 See PLCB Guidance on Third-Party Claims.

22 *Hillbilly Ranch Inc. v. Kahn (In re Wible)*, 42 B.R. 622 (Bankr. D. Mass. 1984)).

23 M.G.L. c. 138, § 23.

24 Fla. Stat. Ann. §§ 561.32, 561.65.

25 47 P.S. § 4-474.1; 40 Pa. Code § 7.31.

26 See 40 Pa. Code § 7.31(e).

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license.²⁷ If the license expires or is obtained by another party through a quota-vacancy auction, the creditor will lose the security interest in the liquor license completely.²⁸

Secured creditors may also face issues in executing a liquor license lien when the secured lender allows the financing statement to lapse. Such time periods depend on the type of collateral and the jurisdiction,²⁹ and most financing statements are effective for a period of five years.³⁰ A UCC-1 that is not continued before lapsing will cease to be effective, costing the secured party their perfected status and perhaps their priority position to collect. Once a financing statement has lapsed, it cannot be revived; consequently, a lapse will likely result in the loss of priority of the security interest on the liquor license.³¹

Finally, execution on a liquor license is made much more difficult due to the strict filing requirements that must be met to attach and perfect a security interest in a liquor license. In addition to closely adhering to the state-specific procedures in order to attain an enforceable lien on a liquor license, the UCC-1 financing statement must also be carefully prepared

and properly filed. If a UCC-1 financing statement contains seriously misleading errors or omissions, it may result in the following: (1) a refusal by the filing office to accept the financing statement; (2) a subordination of the secured party's interest in favor of another creditor; or (3) possible avoidance of the security interest altogether.³²

Conclusion

Properly perfecting a lien on a liquor license may afford creditors significant collateral and security when providing financing to certain debtors. Creditors should be aware of the varying state procedures and requirements necessary to properly attach and perfect a security interest in a liquor license, assuming that the state even allows for such liens. Creditors should always contact local counsel to confirm the correct process and procedure necessary to ensure that they have a valid and enforceable lien on their liquor license collateral. Moreover, creditors must perform proper and consistent due diligence with respect to their liquor license liens to avoid potential execution issues in the event of a debtor's default or insolvency. **abi**

²⁷ *In re Kanoff*, 408 B.R. 53, 56 (Bankr. M.D. Pa. 2009) (creditor paid fees to PLCB to attain license).

²⁸ PLCB Guidance on Third-Party Claims, p. 2.

²⁹ See, e.g., U.C.C. § 9-515.

³⁰ U.C.C. § 9-515(a).

³¹ U.C.C. § 9-515(c).

³² U.C.C. §§ 9-506(a), 9-338 (issues include error in debtor(s) name(s); post-filing changes in collateral, which required updates; or issues with taxes or filing fees associated with UCC-1 filing).

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