The Lender's Source

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New Power of Attorney Act Now in Effect

Georgia's new Uniform Power of Attorney Act took effect on July 1, 2017. The Act imposes a handful of changes that will affect how financial institutions deal with customers seeking to utilize powers of attorney.

It is important to understand that while the new Act does apply to a broad range of powers of attorney, many powers of attorney will not be subject to the Act—particularly in the months following the first effective date of the Act. More specifically, the Act does not apply to any power of attorney that was signed prior to July 1, 2017. These powers of attorney will continue to be governed by prior law. Further, the Act does not apply to "transaction specific" powers of attorney, a vague term intended to include powers granted only for purposes of a single transaction, such as a real estate closing. Finally, the Act only applies to powers of attorney featuring an individual as principal (the *principal* being the person who grants the agent power to act). A power of attorney issued by a corporation or other entity is not governed by the Act.

When dealing with powers of attorney that do fall within the parameters of the Act, institutions should take special note of a few features of the Act. First, if the power of attorney is signed in Georgia, it must be signed by the principal and attested by both a notary public and a separate additional witness. For powers of attorney signed in another state but presented in Georgia, signature requirements are governed by the laws of the state where the power was signed. Thus, while the institution must insist on a notary and witness attestation for covered powers signed within Georgia, these features may not be required for powers signed in other states.

One of the more prominent features of the Act is that it imposes an obligation on third parties to accept certain powers of attorney within a defined time period after receiving the document. If the power of attorney is governed by the Act, and is in the form set forth in the Act or otherwise "substantially reflects" the language in the form, the institution or other third party has seven business days from receipt to either accept the power of attorney or demand one of three types of additional documentation: a factual certification from the agent as to any fact concerning the power; an opinion from an attorney as to any legal matter concerning the power; or an English translation, if the power of attorney is written in other than English. So long as they are requested within the seven-day deadline, these documents must be provided at cost of the principal. Once provided, the institution has five business days to accept the power.

Importantly, if the institution or other third party either fails to accept the power or request additional documentation within the seven-day deadline, or fails to accept the power within five business days after additional documentation is provided, the third party can be charged with attorney fees incurred by the principal or agent in a court proceeding to enforce or validate the power.

The Act does give valuable protection to third parties. A party that accepts a power of attorney in good faith is entitled to presume that it is genuine, valid, and still in effect unless the party actually knows otherwise. Importantly, knowledge is not imputed to all employees of an institution: the relevant issue is only whether the actual employee accepting the power knows it to be invalid. Further, a party that requests one of the three document types discussed above is entitled to rely on the contents of the documents as correct without further investigation. Thus, legal representations from the attorney, and factual representations from the agent, can provide important protection to an institution relying on a power of attorney.

The relatively short deadlines imposed by the Act do require prompt action on the part of the institution. It must act quickly to assess whether the power is governed by the Act, whether acceptance is required, and what additional documentation should be requested. It is crucial that institutions have sufficient procedures implemented to accommodate the new features of the Act.

New Court Guidance on Divining *Perpetual Language* in Security Deeds

In the August 10th decision of *Mike's Furniture Barn v. Smith*, the Court of Appeals of Georgia provided valuable new insight into when dragnet clauses and similar features of a security deed will suffice as valid "perpetual language" extending the lifespan of a deed to secure debt.

One may recall that in the 2015 decision of *Stearns Bank v. Smith*, the Court had used a flexible interpretation of perpetual language requirements, holding that a dragnet clause together with a provision referencing a revolving line of credit could serve as an affirmative statement of intent to create a perpetual security interest as required to provide a minimum 20-year lifespan for a security deed. The new *Mike's Furniture Barn* decision from the same court clarifies that a dragnet clause alone, without additional terms such as a revolving credit line provision, does not suffice as perpetual language affecting a deed's lifespan.

The security deed at issue was given by the debtor to secure an extension of credit by Mike's. For reasons not stated, the deed was granted to the president of Mike's, rather than to the entity. The deed featured a maturity date of September 30, 2005, and purported to secure a described note, all renewals and extensions of the note, and any other indebtedness then or thereafter owing by the debtor.

The debtor failed to repay the loan, yet the creditor took no action to foreclose for more than seven years after default. In 2016, Mike's foreclosed on the property and purchased at foreclosure. The debtor sued Mike's seeking to have the foreclosure set aside on the basis that the deed had expired prior to foreclosure. The debtor was successful in the trial court, and Mike's appealed.

The Court of Appeals held the foreclosure was invalid for two reasons. First, the security deed was granted to the president of Mike's, yet the entity attempted to foreclose in its own name. Without an assignment of record to the entity, only the president himself had capacity to foreclose. More importantly, the foreclosure was void because the deed had expired once seven years lapsed from the 2005 maturity date stated in the deed.

Mike's argued, in reliance on the *Stearns Bank* decision, that the deed was valid for 20 years because the dragnet clause in the deed was perpetual language giving a minimum 20-year lifespan. The Court disagreed, holding the dragnet clause was not a sufficient statement of intent to create a perpetual security interest. The Court acknowledged that in *Stearns* the Court had relied on a dragnet clause, in part, as a valid affirmative statement of intent. Yet, the Court explained, the dragnet clause alone had not been decisive. It only met the threshold when viewed together with terms in the deed to the extent that the secured debt was a revolving line of credit. Per the Court, a revolving line of credit is "by definition, an indefinite and perpetual arrangement."

The deed relied on by Mike's did not describe a revolving credit arrangement. Instead, it referenced a closed-end debt with a fixed maturity date. In these circumstances, a dragnet clause could create only ambiguity as to whether a fixed and definite, as compared to indefinite, interest was intended. As a blanket matter, an ambiguity could not reach the level of a clear, affirmative statement as required for perpetual language.

The Court's holding is not favorable to lenders, but it does at least reimpose some surety after the *Stearns* decision: a dragnet clause alone is not likely effective *perpetual language* if the deed describes a fixed-term debt.

Court Preserves Borrower's Claims in Mix-Up After Redemption from Default

The recent Court of Appeals decision of *Roberts v. JP Morgan Chase Bank* provides an example of the liabilities secured lenders may face if they fail to properly recognize a debtor's post-default rights under a security deed.

In June of 2009, the borrower obtained a first-priority residential mortgage loan from Chase. The security deed granted to Chase allowed for acceleration upon default but provided the borrower a right of reinstatement in the event certain past-due sums were paid within a stated period after default. Importantly, the deed noted that if the borrower's reinstatement rights were properly exercised, the loan arrangement would "remain fully effective as if no acceleration had occurred."

In October of 2009, the borrower obtained a second-priority home equity line of credit from Associated Credit Union. The security deed given by the borrower provided that in the event of default by borrower, or in the event an action was commenced that could materially affect the credit union's interest in the collateral, the credit union could disburse such sums as were necessary to protect its interests and add all disbursed sums to the borrower's outstanding loan balance.

The borrower defaulted on both loans in 2013, with Chase thereafter instituting foreclosure proceedings. Chase notified the borrower of the pending foreclosure and of his right to stop the foreclosure and reinstate the loan by paying a designated amount by the applicable deadline. The borrower paid the required past-due sums three days prior to the deadline. A Chase representative issued a receipt for the funds and required the borrower to sign a "reinstatement agreement" noting that strict compliance under the loan was thereafter required.

Four days after the borrower's reinstatement, the credit union tendered to Chase the full balance of the Chase loan—exceeding $260,000. Chase accepted the full payment and terminated the loan. The credit union added this advance to the balance owing on the borrower's line of credit, with the result that the borrower's overall monthly payments on his mortgage debts increased by more than $1,200. The borrower repeatedly contacted Chase to request reinstatement of the loan. Though he was assured the loan would be reinstated, Chase never did so.

The borrower thereafter sued both Chase and the credit union, alleging breach of contract and infliction of emotional distress by both creditors, and fraud by Chase. The trial court dismissed all claims on the basis that they were facially insufficient to allow recovery. The borrower appealed.

On appeal, the Court of Appeals held that most of the claims had been improperly dismissed, and should have been preserved for litigation. Specifically, the trial court had been correct in dismissing the claim for infliction of emotional distress as the borrower had not alleged any physical impact to him, or any humiliation, embarrassment, or other severe distress as was required to support such a claim. The other claims should not have been dismissed.

With respect to the breach of contract claims, the Court noted that Chase's security deed mandated that the loan would be treated as if no acceleration had occurred in the event the borrower exercised his reinstatement rights. Yet, Chase had accepted full payment from a competing creditor and had closed the loan despite the borrower's wishes. As to the credit union, its deed only allowed for expenses to be disbursed and added to the credit line where "necessary" to protect the lender's interest. Yet, at the time the credit union disbursed the Chase payoff, the borrower had already reinstated the Chase loan and stopped foreclosure. As such, both breach of contract claims could continue.

The fraud claim against Chase was allowed to continue in light of the borrower's allegations that Chase had represented that the loan was initially reinstated, and later represented that the loan would be reopened and reinstated following the credit union's payment. However, the borrower would be required to point to specific statements made by Chase's employees to support the claims.

While this Court decision may not serve as new guidance on unique legal principles, it should serve as a caution that lenders must strictly recognize a borrower's rights, and limitations on the lender's own rights, in pursuing remedies under a security instrument. Unpermitted actions taken in hopes of maximizing recovery can leave the creditor mired in litigation and facing sizeable liability.

Understanding the UCC-1: Errors in Debtor Names, and the Importance of Search Logic

The Uniform Commercial Code's filing and priority system relies on UCC-1 financing statements that are filed, indexed, and searchable according to name of the debtor. For this reason, the UCC imposes specific rules for determining the appropriate names for use. For example, if a debtor is an individual with a valid in-state driver's license, the name used in the UCC-1 must exactly match the name on the license. If a debtor is a corporation, the name used must exactly match the name shown on the debtor's articles of incorporation.

Even a small variance in name may be a breach of UCC name requirements. However, not every breach will cause a financing statement to be ineffective. An error will only render a financing statement ineffective if the error causes the financing statement to be "seriously misleading." A financing statement is seriously misleading if a search of the appropriate index using the debtor's correct name, under the indexing office's standard search methodology, would not disclose the financing statement. In other words, to be effective the financing statement must show up in the results of a standard search using the debtor's correct name.

Determining whether an error is seriously misleading involves more than counting the number of incorrect characters, or examining similarity of appearance or sound. The indexing office's search logic is determinative. In Georgia, the indexing office is the Georgia Superior Court Clerks' Cooperative Authority (GSCCCA). Under its search methodology, most non-alphanumeric characters (such as commas, hyphens, and apostrophes) are either removed or replaced with spaces. So, for example, assume a debtor's correct name is "Pilcher's Laundry, LLC." If a UCC-1 were filed using the name "Pilchers Laundry LLC" the name would be incorrect but not seriously misleading. The apostrophe and comma would be disregarded in this example.

The GSCCCA search logic also features a defined set of approximately 50 "noise words" that may or may not be ignored, depending on whether the debtor is an individual or entity and whether the noise word is used first, last, or otherwise in the name. Summarily, the list of noise words includes abbreviations and words that are often inconsistently used, and provide little unique identifying information regarding the debtor. Prominent examples include: *company*, *inc.*, *incorporated*, *LLC*, *the*, *associates*, *corp.*, and *limited*.

Whether a noise word is ignored often depends on whether it is used first or last in the name. Most noise words are not ignored if used as the first word in a name. As an example, in the name "Company Textiles Incorporated" the words *company* and *incorporated* are both noise words. *Company* will not be ignored, as it is first in the name. In contrast, *incorporated* will be ignored. So, a UCC-1 featuring the name "Company Textiles" would not be seriously misleading. If the example were changed to the name of "Incorporated Textiles Company" the word *company* would be ignored, but *incorporated* would not. As a useful rule, for entity debtors the word *the* is ignored whether first or last in the name.

With the exception of spelling errors in ignored noise words, GSCCCA search methodology (as with most other offices' methodologies) is not tolerant of spelling errors. The basic concept is that after the name is "normalized" by ignoring, replacing, or removing characters and noise words as discussed above, a search will disclose the name only if the normalized name exactly matches the search terms or begins with an exact match of the search terms. Thus, a spelling error in a word that is not ignored in normalization will usually render the error seriously misleading. For example, assume a debtor's correct name is "Robert Chaney's Landscaping, LLC." A creditor files a UCC-1 featuring the debtor name "Robert Cheney's Landscaping, LLC." On filing, the name is normalized in the index as *Robert Cheneys Landscaping*. If a searcher uses the correct name of Robert Chaney's Landscaping, LLC (which would be normalized to *Robert Chaneys Landscaping*) the UCC-1 will not be disclosed because of the secured creditor's misspelling of the word *Chaney*.

As may be suspected from the above discussion, determining whether a name error is seriously misleading, thus rendering a financing statement ineffective to perfect, is a fact-specific process that largely depends on the indexing office's search logic. Parties should not lightly jump to conclusions about the effects of a name error without considering search logic and, more practically, conducting a standard search under the correct name to determine whether the erroneous UCC-1 is disclosed.

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