The Lender's Source

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Court Rules That Bank Properly Refused to Honor Cashier's Check After Garnishment

In the recent Court of Appeals of Georgia decision of *Burrowes v. Bank of America*, the court held a bank acted properly in stopping payment of a cashier's check payable to a garnished accountholder and in paying the amount of the check into court.

Customer Burrowes was subject to a sizeable judgment in favor of a third party, yet had approximately $88,000 on deposit at Bank of America. On the morning of February 6, 2015 the judgment creditor arranged for a garnishment suit to be served on the bank at its Decatur office. A few hours later, before the bank had processed the garnishment, Burrowes appeared at the bank's Peachtree Battle branch and attempted to withdraw $77,100 from his account. The bank employees at the branch were unaware of the garnishment. Because the branch had insufficient cash on hand, Burrowes was given $10,000 in cash and a cashier's check, payable to Burrowes, for the remainder.

Almost two hours later, the bank's legal processing department placed a freeze on Burrowes' account and placed a stop payment order on the cashier's check. The bank asked Burrowes to return the check, but he instead unsuccessfully attempted to deposit the check at a different bank a few days later. Bank of America paid the entire $88,000 balance of Burrowes' deposit account into court with its garnishment answer. Burrowes then sued the bank for wrongful dishonor of the cashier's check. His claims were dismissed at the trial level, and he appealed the dismissal.

The Court of Appeals upheld the trial court's dismissal, holding that the bank did not wrongfully dishonor the cashier's check because the bank was legally barred from honoring the check. In Georgia, garnishment reaches all of the garnished customer's money and property in possession or control of the bank at the time the garnishment is served. When a cashier's check is issued, the effect is a debit from the purchasing customer's account and a corresponding deposit into the issuing bank's own account. At that time, the amount of the check is considered legally assigned to the payee designated on the check. Thus, although issuance of the cashier's check had the effect of removing the funds from Burrowes' account, the funds remained subject to garnishment because Burrowes, as payee, was the legal assignee (owner) of the funds.

As funds belonging to Burrowes, the bank was required by garnishment law to pay the cashier's check balance into court rather than releasing it to Burrowes. In other words, by reason of the garnishment, the bank was prohibited by law from honoring the check. A bank cannot be liable for wrongful dishonor where payment of the subject check is prohibited by law. Therefore, Burrowes' claims against the bank were properly dismissed.

Timber Cutter Held Liable to Secured Lender for Value of Trees Removed, But Not for Diminution in Value of Underlying Land

The March 2017 Court of Appeals decision of *RedCedar, LLC v. CML-GA Social Circle, LLC* applied Georgia's timber conversion laws to a dispute between a secured lender and a company that performed timber cutting services at request of the timber purchaser.

The lender at issue held a recorded security deed covering a tract of 463 acres. Without the lender's knowledge, the property owner sold certain standing timber on the property to Georgia Timber, LLC. Georgia Timber then hired RedCedar, LLC to cut and haul the purchased timber. RedCedar was paid only for cutting and hauling services, and neither bought nor sold any of the timber.

When the lender discovered the clear cut timber harvest, it sued the property owner, Georgia Timber, and RedCedar, claiming each was liable for the amount by which the tract's value had decreased. RedCedar argued that it could not be liable to the lender, as it had no interest in the underlying property and had neither bought nor sold any of the trees at issue. RedCedar claimed it was only acting as the agent of Georgia Timber (the timber purchaser), and thus all liability should rest with Georgia Timber. The trial court disagreed, awarding judgment against RedCedar for only the value of the trees harvested. RedCedar and the lender appealed.

On appeal, the Court of Appeals held that the plain language of Georgia's timber conversion statute resolved all arguments in issue. The statute provides that any person who buys, sells, cuts, or removes timber from property in which a lender holds a recorded security deed, without written consent of the lender, is liable to the lender for the value of the trees removed. Liability is not limited solely to the seller and purchaser, as RedCedar had argued. It attaches even to those who, like RedCedar, merely *cut* or *remove* timber from property at the request of a buyer or seller of timber. The trial court had thus correctly ruled that RedCedar was liable to the lender for timber conversion.

The plain language of the statute also showed that the lender was incorrect in arguing that it was entitled to recover for diminution in value to the underlying land as a result of the harvest. The statute only creates liability for the value of the trees removed, and not for any other resulting damage to the property. Thus, even though the clear cut harvest may have caused the tract's value to decrease in an amount greater than the value of the trees harvested, the lender could only recover from RedCedar for the value of the trees.

Court Confirms Broad Reach of FIRREA Administrative Exhaustion Protections

In the March 16, 2017 decision of *Douglas County v. Hamilton State Bank*, the Court of Appeals of Georgia held that FIRREA's administrative exhaustion requirements apply to all claims based on pre-receivership actions of a failed bank—even claims arising from liabilities assumed by the purchasing bank from the FDIC as receiver.

In explanation, the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 ("FIRREA") authorizes the FDIC, when acting as receiver for a failed bank, to conduct a claims administration process whereby most claims against the failed bank are reviewed, either accepted or rejected, and, to the extent funds are available, paid by the FDIC with little or no intervention of the courts. To assure the FDIC has control over the process, FIRREA provides that no court of law has the ability to entertain the following types of claims unless the claims have first been submitted to the FDIC administration process: (i) claims that seek payment from, or assert rights with respect to, assets of the failed bank; and (ii) claims relating to any act of the failed bank or the FDIC as receiver.

The facts presented in the *Douglas County* decision were that Douglas County Bank, as surety, issued several performance bonds in favor of the county relating to various real estate developments. When the developers failed to complete the projects, the county issued demand to Douglas County Bank, as surety, for payment of the sums necessary to complete the projects. The bank refused to pay. Some months later, the bank was closed and the FDIC appointed as the bank's receiver.

Hamilton State Bank entered into a Purchase and Assumption agreement with the FDIC whereby Hamilton purchased and assumed various assets and liabilities of Douglas County Bank, specifically including all standby letters of credit. Thereafter, the county demanded that Hamilton make payment under the performance bonds formerly issued by Douglas County Bank. When Hamilton did not comply, the county filed a lawsuit against Hamilton. At Hamilton's request, the court dismissed the lawsuit on the basis that the county had not submitted the claims to the FDIC's administration process. The court reasoned the bonds were failed bank "assets" acquired by Hamilton, and thus FIRREA's administrative exhaustion requirement applied.

The county appealed the court's decision, arguing that the bonds were *liabilities* rather than *assets*, and further that Hamilton's assumption of the bonds removed the bond claims from FIRREA exhaustion requirements. Addressing the arguments, the court of appeals agreed the bonds were in fact liabilities rather than assets, and thus exhaustion requirements were not invoked on the basis the claims related to former "assets" of the failed bank. The court also agreed that Hamilton had assumed the bond liabilities, as the bonds were in fact *standby letters of credit* expressly assumed under Hamilton's agreement with the FDIC. Nonetheless, FIRREA exhaustion requirements did apply to the claims.

The court noted that FIRREA imposes exhaustion requirements on two categories of claims: claims that are *either* (i) related to assets of the failed bank, or (ii) related to an act or omission of the failed bank. Determining the bonds were *liabilities* rather than *assets* only removed the claims from the first category, not the second. The court held the second category to be broad, covering "any claim relating to any act or omission of a failed bank placed in receivership." According to the court, the county's claims arose from the failed bank's issuance and failure to honor the performance bonds. Thus, the claims fell within the second category and administrative exhaustion was required.

Importantly, the court held that Hamilton's undisputed assumption of the bonds did not affect whether the county's bond claims fell within the second category of claims discussed above. FIRREA's statutory language imposing the exhaustion requirements does not feature any exception for liabilities expressly assumed by a purchasing bank; if the claim relates to pre-receivership acts of the failed bank, exhaustion requirements apply. The court held that it could not ignore the plain language of the law by judicially creating an exception, despite the fact that the result seemed harsh or unfair to the county. Creating an exception for assumed liabilities would require an act of the legislature, and not of the court. Thus, the county's lawsuit against Hamilton was properly dismissed on the basis that the county failed to first submit its claims to the FDIC's administration process.

Understanding the UCC-1: When Must Maturity Dates be Included?

The general rule is that a UCC-1 financing statement remains valid until the earlier of the date on which a valid termination statement is filed or five years from the date the financing statement was filed. Further, in almost all cases, the secured party is not required to include the maturity date of the secured debt in the financing statement. But the *general rule* has an exception, and *almost all cases* is only almost the same as *all cases.*

Georgia's version of the Uniform Commercial Code is different than that of most states in that for a small segment of consumer loans, a maturity date must be included in the financing statement. More specifically, where the original amount of the loan is $5,000 or less and the collateral described in the financing statement is consumer goods, the secured party must affirmatively state the loan's maturity date in the financing statement. For these loans, the financing statement will lapse at the earlier of (i) five years from the date the financing statement was filed, or (ii) the 20th day after the maturity date indicated in the financing statement.

In other words, a maturity date is only required for small loans secured by consumer goods. As a reminder, *consumer goods* are goods that are either bought or used primarily for personal, family, or household purposes. So if the collateral is only used for business purposes (e.g., a copier in a medical office) Georgia's maturity date requirement would not apply. The effect of these special provisions is to cause financing statements related to small consumer loans to lapse automatically after the loan term even where the secured party fails to promptly file a termination statement. It is important to note these provisions cannot *extend* the life of a financing statement; in the event the maturity date is more than five years from filing, lapse will still occur at expiration of the five year period.

Most loans made by a bank will be unaffected by Georgia's peculiar maturity date requirements. For those unaffected loans, the lender has no foreseeable benefit to be gained by including any maturity date. The practice would only increase likelihood of conflict among loan documents, and necessitate filing of an amendment each time the loan is renewed or the loan term extended.

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