

Lawyers

LIABILITY UPDATE

A LIABILITY NEWS BULLETIN FROM GEORGIA LAWYERS INSURANCE COMPANY

Georgia Supreme Court Announces New Standard of Care for UCC Filings

The Georgia Supreme Court has ruled that attorneys filing a Uniform Commercial Code (UCC) financing statement on behalf of a creditor have an independent duty to renew the financing statement before it expires if they do not explicitly tell their client that the financing statement is effective for only five years. This new rule increases the potential for liability claims against lawyers engaged in a transactional practice. These lawyers should be aware of the new rule and be sure that they have safeguards in place to avoid a potential malpractice claim under this new standard.

In *Barnes v. Turner*, 2004 WL 2824213 (Ga.); 04 FCDR 3756 the Supreme Court held that an attorney filing a UCC financing statement that is covered by O.C.G.A. §11-9-515 must now either: (1) explicitly inform the client that the UCC financing statement is only effective for five years and will expire if not renewed; or (2) if the attorney does not provide this advice, he assumes a new duty to file a renewal for the financing statement independent of the duties he had to the client in the initial transaction. Importantly, the statute of limitations on this claim

does not begin to run until the time that the financing statement should have been renewed rather than from the time of the closing of the initial transaction, as was previously the law.

The case has ignited controversy among members of the Bar because the decision arguably institutes the “continuing representation rule” that has previously been rejected by Georgia courts¹. The controversy has been partially fueled by a sharp dissent by three justices in the *Barnes* opinion, warning that the decision will make it difficult for an attorney to define the limits of his representation and for legal malpractice carriers to assess potential risks.

“Because of the importance of the recent decision of Barnes v. Turner discussed in the accompanying article by Emory Palmer (especially the perceived impact on the statute of limitations for malpractice claims against lawyers), we are devoting this entire Liability Update to Emory’s article. Georgia Lawyers continues to thrive however, and I will give you an updated status report on our progress in the next issue.”



J. Littleton Glover, Jr.
Chairman of the Board

FROM
THE
CHAIRMAN

GaLawIC.com

But whatever the long term implications of the decision are, it is clear that *Barnes* creates a new rule that attorneys must abide by when representing someone in a secured transaction, or risk malpractice liability.

In *Barnes* the client was the owner of an auto parts store and approached the attorney about selling the store to some other individuals. At the closing of the sale, Barnes took back a security interest in the assets of the business to secure a note for a large portion of the purchase price. The attorney properly recorded a UCC financing statement covering the security interest, but admittedly did not inform Barnes that the UCC statement had to be renewed to prevent expiration after five years. Unbeknownst to Barnes, the purchasers of the auto parts store also later pledged the assets of the business to other lenders who properly recorded their own UCC financing statements. The Barnes UCC financing statement expired after five years because it was not renewed. When the other lenders later foreclosed on the business, Barnes learned that he was in an inferior position to the other lenders because his UCC had expired because it had not been renewed.

The ruling in *Barnes* has altered the liability landscape in Georgia.

Barnes sued his lawyer alleging legal malpractice for failing to renew the UCC financing statement or inform Barnes that this needed to be done. The lawyer moved to dismiss on grounds that the case was filed more than four years after the closing and

thus outside the four-year statute of limitations normally associated with legal malpractice claims.

The trial court granted the lawyer's motion to dismiss

ruling that any injury that occurred was the result of an act or omission by the attorney on the date of the closing and was thus barred by the statute of limitations since the lawsuit had been filed more than four years after that date. The Court of Appeals affirmed the trial court's decision holding that there was no "continuing representation rule" in Georgia and that the attorney had been retained to close the transaction and not monitor it on a continuing basis.² Thus, the four year statute of limitations applied, and the case was properly dismissed.

The Supreme Court reversed, reasoning that without advice from his lawyer that the UCC financing statement needed to be renewed, Barnes, as a layman, would not even know that such an issue might affect his

Emory L. Palmer practices with the Atlanta law firm Carr, Tabb, Pope & Freeman. His practice is focused in the areas of commercial litigation, professional liability defense and insurance coverage.



security interest. Since Barnes' lawyer did not inform him that the UCC statement was good for only five years, the lawyer assumed a duty to renew the financing statement himself and thus could be liable for Barnes' loss that could be attributed to the expiration of the financing statement. Specifically, the court held that, in the sale of a business, involving a purchase price that is to be paid over time and collateralized, the seller's attorney must prepare and file a UCC financing statement to perfect his client's security interest and:

If the financing statements require renewal before full payment is made to the seller, then the attorney has some duty regarding this renewal. Otherwise, the unpaid portion of the purchase price becomes unsecured and the seller did not receive the protection he bargained for.

In the context of *Barnes*, this meant that, by failing to inform the client of the five-year time limitation at the closing, the attorney undertook a new duty and that the statute of limitations on the claims related to this new duty did not *begin* running until the expiration of the financing statement five years later.

A sharp dissent authored by Justice Benham and joined by Justices Thompson and Hines argued that the new holding created tremendous uncertainty and lack of finality that would not only make it impossible for lawyers to assess their own potential liability, but would make malpractice insurance carriers unable to make accurate assessments of exposure, inevitably leading to higher premiums that would be passed on to clients. The dissent explained:

The majority holds the asserted failure to inform Barnes of the future need to renew the UCC statements somehow created the duty on (the attorney's) part to renew the filings without having been retained to do so. The majority thus creates new duties that could outlast not only the period of the attorney/client relationship, but even the attorney's life.

The majority went to great lengths to address the dissent, which it characterized as "hyperbole," stating that they were not holding that the attorney's failure to inform was a "continuing wrong that tolled the statute of limitations" until the expiration of the UCC statement. Rather, the majority explained that the holding means that, by failing to inform about the need to renew the UCC, the attorney undertook a *new duty* to renew his statement and that the statute of limitations began running from the alleged breach of this new duty.

Whatever view one takes of the decision, it is clear that transactional lawyers must now take steps to protect themselves when representing the seller in the sale of a business or, in any case where a UCC-1 financing statement is filed on behalf of a client. After *Barnes*, when a lawyer files a UCC statement there is a duty to renew the financing statement, unless it is made clear to the client that the attorney is not being retained for the renewal and that the client will lose the security interest if the financing statement is not renewed.

As with other situations where a duty to inform about a specific right come into play, the following practices can provide some safeguards in light of the ruling in *Barnes*:

- Create a standard-form acknowledgment, similar to the acknowledgment used for HUD-1 settlement statements, to go along with a UCC-1. At the closing, or at another appropriate time, have the UCC-1 creditor initial the financing statement and sign the acknowledgment indicating that the creditor/client has received a copy of the financing statements and understands that pursuant to Georgia law it is only effective for five years and thereafter must be renewed.
- As with any representation, have a creditor/client sign a written engagement letter explicitly setting forth what services will be provided in the course of the representation and what services will not be provided. If the attorney does not wish to be responsible for renewing the financing statement at the end of the five years, the engagement letter should state this. (Engagement letters can be a tremendous defense against malpractice claims in virtually every representation scenario).

- Create a primary and secondary calendaring system to indicate when UCC financing statements need to be renewed. Many transactional lawyers already utilize such a system for the renewal of other filings or as a part of their regular calendaring system. But remember, with UCC filings, no notice will come in the mail to remind you that the UCC is about to expire.

Of course these suggestions will not guarantee that a malpractice claim will not be brought, but are some common sense steps that can be taken to reduce this risk. The ruling in *Barnes* has altered the liability landscape in Georgia, particularly for transactional lawyers. It is unclear what other scenarios such a rule might apply to, but lawyers in this practice area should be aware that the *Barnes* case is likely to be used by plaintiffs in malpractice actions to justify

claims beyond the normal statute of limitations. With any action taken on behalf of a client where an expiration or time limit of an instrument is involved, extra care should be taken. Don't let the small headache of informing the client or filing a renewal lead to the colossal headache of defending a malpractice case.

PRACTICE SAFEGUARDS

1. **Create a standard-form acknowledgment**
2. **Have a creditor/client sign a written engagement letter**
3. **Create a primary and secondary calendaring system**

¹ See e.g., *Hunter McLean Exley & Dunn, P.C. v. Frame*, 269 Ga. 844, 849, 507 S.E. 2d 411 (1998).

² *Barnes v. Turner*, 265 Ga. App. 6, 593 S.E. 2d 9(2003).



113 Ebenezer Road
Suite 103
Fayetteville, GA 30215
770-486-3435
Fax: 770-486-3395
Toll-Free: 866-372-3435
GaLawIC.com

Call us today or visit our web site for a no obligation "QUICK QUOTE!"

GaLawIC.com

LAWYERS LIABILITY UPDATE