

# **SOUTH CAROLINA BANKING LAW UPDATE**

*Laurie A. Becker, Esquire*

**South Carolina Bar Annual Meeting  
Corporate, Banking, and Securities Law Section CLE**

**Friday, January 25, 2002**

**SOUTH CAROLINA**  
**BANKING LAW UPDATE**  
**JANUARY 2002**

**Laurie A. Becker, Esq.**  
**Nexsen Pruet Jacobs & Pollard, LLC**  
**LBecker@NPJP.com**  
**(803) 771-8900**

The following materials provide an update on Banking Law in the State of South Carolina, and include both legislation and case law from calendar year 2001. One of the most significant pieces of legislation affecting banking and finance that was passed in the 2001 legislative session was Act 67 which embodies over 1000 pages of revisions to various articles of the South Carolina Commercial Code. Because a summary of all of the commercial code changes is beyond the scope of this update, only brief summaries of new Article 2A and revised Article 8 have been included. However, because of the importance of secured transactions to those involved in the areas of banking and finance, I have provided a more in-depth summary of Revised Article 9.

**I. 2001 SESSION LEGISLATION**

**A. Acts Passed in 2001 Session**

1. Consumer Finance Companies

2001 Act No. 44, effective May 29, 2001, amended § 34-29-140 relating to licensing of consumer finance companies to allow a licensee to impose a delinquency charge of 5 cents per dollar OR a minimum delinquency fee of \$5 on an unpaid installment delinquent for ten or more days, if such charges are agreed to in writing. The charge may be imposed only once on each delinquent installment and, if a portion of an installment is delinquent, the delinquent charge may be imposed only once on that portion of the installment that is delinquent. In addition to all other charges authorized by this Act, a licensee may charge and add to the gross amount of the promissory note a maintenance fee of \$2 for each month for the term of the loan. If the loan is prepaid, the maintenance fee must be refunded pro rata with the unexpired term of the loan. If a licensee charges any amount in excess of those charges allowed by Chapter 29 of Title 34, the loan contract is void and the licensee has no right to collect or receive any principal, interest, charge, or recompense.

2. Uniform Commercial Code

2001 Act No. 67, approved by the Governor June 11, 2001, adopts several new amendments to the South Carolina commercial code. Comprising over 1,000 pages of revisions, this Act adds chapter 2A to Title 36 so as to provide a statutory framework in the South Carolina commercial code regarding personal property leases and includes provisions for the formation,

construction, effect, performance, and default of a personal property lease contract (see Section III.A below); amends Chapter 5 of Title 36 relating to the law governing letters of credit; amends Article 8 of Title 36 relating to investment securities and financial transactions to provide a more accurate description of the realities of the securities markets, formalizes the indirect holding system, and enhances liquidity and certainty in securities transactions (See Section III.B. below); and substantially revises Article 9 of Title 36 relating to secured transactions to conform the South Carolina statutes to the federal amendments embodied by Revised Article 9 of the Uniform Commercial Code (see Section III.C. below). Revisions to Article 2A were effective June 11, 2001 while Article 5, 8, and 9 revisions became effective July 1, 2001.

## **B. Pending Legislation from 2001 Session**

### **1. Licensure of Mortgage Loan Brokers**

House Bill No. H.3360, currently pending in the Senate Labor, Commerce, and Industry Committee, proposes to amend chapter 58, Title 40, Code of Laws of South Carolina, 1976 relating to the licensure of mortgage loan brokers so as to transfer administrative control of certain mortgage loan brokers from the Department of Consumer Affairs by creating the South Carolina Mortgage Loan Brokers Board to be administered by the Department of Labor, Licensing, and Regulation; to conform Chapter 58 to the statutory, organizational, and administrative framework established for professional and occupational licensing boards; and to further provide for the licensure and regulation of individuals as mortgage loan brokers. The new Board shall (1) advise the department on matters relating to the regulation and issuance of licenses to mortgage loan brokers and on policies necessary to carry out this chapter, and (2) hear disciplinary actions against licensees as authorized under Chapter 58 and may impose penalties and sanctions pursuant to this chapter.

### **2. Postmark Prompt Payment Act**

House Bill No. H.3553 (and companion Senate Bill No. S.3) introduced February 14, 2001, and pending in both the Senate Banking and Insurance Committee and the House Labor, Commerce and Industry Committee, proposes to amend Title 34, Code of Laws of South Carolina, 1976, relating to banking, financial institutions, and money, by adding Chapter 38 so as to enact the "Postmark Prompt Payment Act." This act stipulates if any payment required to be made on or before a prescribed date is delivered after that date by the United States Postal Service to the payee, the payment is deemed to have been received by the payee on the date of the Postal Service's postmark stamped on the envelope or other cover in which the payment is mailed. This applies only with respect to a payment which is a payment on a consumer credit transaction arising under Title 34; which is a payment on a lender credit card or similar arrangement; which is a payment on a transaction arising under Chapter 29 of Title 34; or which is a payment on an agreement which is secured by a first lien or junior lien on the consumer's principal dwelling or primary residence.

3. Service Charge on Fraudulent Checks

House Bill No. H.3286, introduced January 17, 2001, is currently pending in the Senate Banking and Insurance Committee. This bill seeks to amend § 34-11-70 relating to prima facie evidence of fraudulent intent in drawing checks and service charges for drawing fraudulent checks, so as to increase the service charge on dishonored checks from \$25 to \$30. Unless the maker of the dishonored check pays the full amount of the check plus the \$30 service charge to the payee within ten days after written notice has been sent by certified mail to the address printed on the check, it will constitute prima facie evidence of fraudulent intent against the maker.

4. Fraudulent Checks and Number of Days a Check May be Held

Senate Bill No. S.4, introduced January 10, 2001 and currently pending in the Senate Banking and Insurance Committee, proposes to amend § 34-11-60 relating to drawing and uttering fraudulent checks, by increasing from ten to twenty the number of calendar days from the date the check was presented to payee that a payee may hold a check prior to depositing such check in an account of the payee with the drawer remaining liable for uttering a fraudulent check if sufficient funds are not on deposit with the bank of the drawer.

5. Consumer Identity Theft Protection Act

Senate Bill No. S.530, introduced April 3, 2001, is currently pending in the Senate Banking and Insurance Committee. This bill (companion Bill H.3847) proposes to amend Title 37, relating to the Consumer Protection Code, by adding chapter 20 entitled the "Consumer Identity Theft Protection Act." This new act would provide for the establishment by the Attorney General of a database of individuals who have been victims of identity theft, to provide an expedited court procedure for clearing the name of an identity theft victim if the victim's identity has been mistakenly associated with a record of criminal conviction, to provide strict requirements for identity and address verification by a credit card issuer, to provide for the blocking of inaccurate credit report information resulting from identity theft, and to provide that the credit agency's notice and reporting requirements conform to those of the Federal Fair Credit Reporting Act.

6. South Carolina Fair Credit Reporting Act

Senate Bill No. S.545, introduced April 4, 2001, and currently pending in the Senate Judiciary Committee, and its companion bill House Bill No. H3852 introduced March 29, 2001 and pending in the House Judiciary Committee, seek to amend Title 15, Code of Laws of South Carolina, 1976, relating to civil remedies and procedures, by adding Chapter 46 so as to enact the "South Carolina Fair Credit Reporting Act," to provide that unfair methods of reporting credit history and unfair or deceptive acts in the conduct of credit reporting are unlawful, to provide that the Federal Fair Credit Reporting Act as interpreted by the Federal Trade Commission and federal courts shall furnish guidance in construing this act, to provide penalties for willful and negligent noncompliance with the terms of this act, to provide for the jurisdiction of the state

courts to hear actions brought pursuant to this act, and to provide, with exceptions, a two-year statute of limitations to seek relief pursuant to this act.

7. Preservation of Mechanic's Liens

Senate Bill No. S.224 and similar House Bill No. H.3041, pending in the Banking and Insurance Committee and the Judiciary Committee, respectively, were introduced in January 2001 seeking to amend § 29-5-90 (while S.224 goes further and proposes to amend § 29-5-120 as well). Both bills propose to extend from 90 days to 180 days the amount of time a person who has provided labor or materials for a building or structure has to file its mechanic's lien against the property owner. If the lien is not filed within this time period, it will be dissolved. S.224 proposes to amend § 29-5-120 by extending from six months to 270 days (9 months) the time in which a suit for enforcing the lien is commenced by the person desiring to avail himself of this statute.

8. Creation of a Community Investment Account

Senate Bill No. S.607, introduced April 24, 2001 and currently pending in the Senate Finance Committee, seeks to amend the South Carolina Economic Development Act (§§ 34-43-10 *et seq.*) to add provisions relating to the creation of a Community Investment Account. This account would be controlled by the Department of Commerce ("DOC") through which taxpayers may invest funds pursuant to Chapter 43 of Title 34 and from which the DOC may make grants for the benefit of community development corporations (CDCs) and community development financial institutions (CDFIs). Taxpayers may claim as a tax credit 33% of all amounts invested in the CDCs, CDFIs, or the newly created Community Investment Account.

9. Protecting Consumers from Predatory Lenders

Senate Bill No. 122, a Senate Resolution introduced January 11, 2001, resolves to evaluate the problem of predatory lending in South Carolina by setting up a subcommittee of the Senate Banking and Insurance Committee to study the problems encountered by low income borrowers seeking home equity and mortgage loans, and to provide that the subcommittee make recommendations to the Senate regarding legislation to remedy unfair predatory lending practices in South Carolina. The subcommittee is to consist of at least five Senators appointed by the Chairman of the Senate Banking and Insurance Committee and was scheduled to report to the South Carolina Senate by January 31, 2002 regarding the findings of the subcommittee.

10. Family Privacy Protection Act

Senate Bill No. S.204, introduced January 24, 2001 and passed by the Senate March 20, 2001, is currently pending in the House Judiciary Committee. This bill seeks to amend Title 30 so as to add Chapter 2 to create the "Family Privacy Protection Act of 2001" which aims to establish state policy and procedures relating to the use and dissemination of personal information, and includes disclosure and notification requirements to be adhered to by all state entities that collect and use such personal information. The Act would prohibit a public body from selling, providing access to, or furnishing to a private person or entity personal information contained in a public record for use by that person or entity for commercial solicitation.

## 11. First Purchase Family Housing Act

Senate Bill No. S.266, introduced February 6, 2001 and pending in the Senate Banking and Insurance Committee, proposes to amend Title 34 by adding Chapter 35 entitled “The First Purchase Family Housing Act.” This amendment would allow individual taxpayers a tax deduction up to \$5,000 per year and married couples up to \$10,000 per year on amounts deposited into a first time house purchase account. The account must be set up in a trust with the trustee being a bank, building and loan association, credit union, or other financial institution that actively makes residential mortgage loans in South Carolina. The money must remain in the account for at least six months to enable the taxpayer to take the deduction; must be distributed to the taxpayer(s) within 120 months from the date of the initial contribution; and the funds comprising the account may only be invested in savings or time deposits. If the trust funds are distributed but not used to purchase a first time residence in South Carolina, the amount distributed must be added to the distributee’s gross income and taxed accordingly.

## 12. Garnishment Acts

Senate Bill No. S.154, introduced January 17, 2001 and passed by the Senate April 3, 2001, is currently pending in the House Judiciary Committee. This Bill proposes to amend Title 15 by adding Chapter 42 to enact the “South Carolina Business Debt Recovery Act of 2001.” The new chapter is designed to allow a person who has recovered a judgment against another person for recovery of a commercial debt the right of garnishment of the wages, bonuses, and commissions of the debtor. This Senate version of the garnishment act only applies to commercial debt which is any nonconsumer debt (and excludes a mortgage on such debtor’s principal residence). Notice of intent to apply for writ of garnishment must be served on the debtor and give such debtor 30 days to respond. After the 30-day period, the creditor may file a motion for writ of garnishment with the circuit court and upon the receipt of the writ, creditor must notify the employer/garnishee of the amount to be garnished each pay period – which amount shall not exceed 25% of the debtor’s disposable income on a weekly basis.

Similar to S.154, House Bill No. H.4212, introduced May 29, 2001 and referred to the House Judiciary Committee, also proposes to add a new chapter relating to garnishment. H.4212’s new chapter is entitled the “South Carolina Garnishment Act” and has a broader scope than S.154. The proposed House act does not limit garnishment to commercial debt, but merely limits the right to garnishment to debts arising under contract as opposed to tort. In addition, it would subject to garnishment additional sources of income, including wages, interest, rents, capital gains, dividends, bonuses, and commissions.

## 13. Consumer Credit Reporting

Senate Bill No. S.192, introduced January 24, 2001 and referred to the Senate Banking and Insurance Committee, seeks to amend Title 37, Chapter 1 (Consumer Protection Code) by adding § 37-1-410 which allows a consumer to notify a consumer credit reporting agency that certain information contained in the consumer’s file is inaccurate. Upon receipt of the consumer’s written dispute, the agency must reinvestigate the information within 60 days and

correct the information appearing on the consumer's report if the earlier information was inaccurate.

14. Furnishing False Credit Information

House Bill No. H.3229, introduced January 10, 2001 and referred to the House Judiciary Committee, proposes to add § 16-3-1080 to state that a person or business commits the offense of furnishing false credit information if they knowingly furnish false information about a person's creditworthiness, credit standing, or credit capacity to a credit reporting bureau. A credit reporting bureau commits the same offense if it furnishes such false information to a third party. The new statute further provides that violators must be fined not more than \$2,000 per offense.

15. Enforcing Payment of Fraudulent Checks

House Bill No. H.3317, introduced January 23, 2001 and referred to the House Judiciary Committee, amends § 34-11-60 to provide that such section does not apply to a check given to a deferred presentment service or a check cashing service. The bill also would amend Section 34-11-70 to provide that a commercial agent for collection of an obligation paid for with a fraudulent check does not have the same rights of the original payee unless the check is endorsed over to such agent for value. Finally, the bill seeks to amend § 34-39-180 (relating to regulation of deferred presentment services) and § 34-41-60 (relating to regulation of check cashing services) to provide that neither may rely on remedies in Chapter 11 of Title 34 for prosecuting and enforcing payment of a fraudulent check.

16. Unauthorized Practice of Law Consumer Protection Act

House Bill No. H.4114, introduced May 15, 2001 and referred to the House Judiciary Committee, proposes to amend Chapter 5 of Title 40 to add Article 6 entitled "Unauthorized Practice of Law Consumer Protection Act." This new article would allow attorneys to report to the Attorney General any alleged conduct that would constitute engaging in the unauthorized practice of law. The Attorney General would then have 20 days from receipt of the report to determine whether or not to proceed with criminal prosecution. If the Attorney General does not choose to prosecute, the reporting attorney may commence proceedings in the court of common pleas. Those found to have engaged in the unauthorized practice of law are subject to penalties including fines, attorneys' fees, and restitution for damages caused.

17. Collection of a Dishonored Check by a State Agency

House Bill No. H.3017, prefiled December 6, 2000 and both introduced and referred to the House Judiciary Committee January 9, 2001, proposes to amend Chapter 11 of Title 34, relating to bank deposits, by adding § 34-11-140. This new section would require state agencies to attempt to collect dishonored checks returned to them, and the collected revenues equal to the face amount of the dishonored check and a \$25 service charge may be retained and expended by the state agency with any unused amount to be deposited in the general fund at the end of the fiscal year.

18. Notice of Dishonor and Suspension of Collection Efforts

House Bill No. H.3020, prefiled December 6, 2000 and both introduced and referred to the House Judiciary Committee on January 9, 2001, proposes to amend Chapter 11 of Title 34 by adding § 34-11-115 and Chapter 5 of Title 37 by adding § 37-5-118. Section 34-11-115 requires a 30-day notice period by the holder of a dishonored check to the drawer of the check before submitting the check to a check recovery service. In addition, once the check recovery service receives notice of wrongful dishonor or bona fide dispute after it begins its collection efforts, the service must immediately halt its collection efforts. Non-compliance with this new section is punishable by a fine of not less than \$100 per occurrence. Section 37-5-118 is identical to § 34-11-115 except that it applies to a creditor who is the holder of a dishonored check.

19. Decreased Lien Period for Judgments on Real Property with Renewal Option

House Bill No. 3064, prefiled December 6, 2000 and both introduced and referred to the House Judiciary Committee on January 9, 2001, proposes to amend § 15-35-810 to reduce the lien period of real property judgments and decrees from a period of ten years to one year from the date of the final judgment or decree “unless renewed or revived for a period of five additional years as provided in § 15-39-30.” Section 15-39-20 would be amended similarly to allow the enforcement of final judgments at any time within one year after the entry of judgment and adds, “[a] final judgment may be renewed or revived for a period of five additional years as provided in § 15-39-30.” Thus, § 15-39-30’s proposed amendments reflect the option to renew or revive a final judgment or decree for a period of five years in accordance with SC Rules of Civil Procedure, and if a final judgment becomes dormant, it may be renewed or revived by an action filed in the manner provided by the SC Rules of Civil Procedure if filed within three years from the time the judgment became dormant. An action to renew or revive must be filed in the court of the county where the original judgment was obtained.

**C. Pre-Filed Bills for the 2002 Legislative Session**

The House and Senate introduced the following pre-filed bills relating to banking and/or finance in December 2001:

1. House Bills

House Bill No. H.4398, prefiled on December 5, 2001 and referred to the House Labor, Commerce, and Industry Committee, seeks to amend § 38-77-122 and § 38-77-123 to prohibit the use of creditworthiness as a factor in refusing to issue or renew an automobile insurance policy and to prohibit the use of creditworthiness in determining automobile insurance policy premium rates.

2. Senate Bills

Senate Bill No. S.790, prefiled on December 12, 2001 and referred to the Senate Judiciary Committee, proposes an amendment to (i) § 59-150-150 to prohibit the sale of lottery tickets by a retailer in the business of making consumer loans, and (ii) § 59-150-210 to add a

subsection prohibiting the sale of lottery tickets on the premises of a person or business entity that is in the business of making consumer loans of any kind.

Senate Bill No. S.798, prefiled on December 12, 2001 and referred to the Senate Banking and Insurance Committee, is the companion bill to prefiled House Bill No. H.4398.

## II. CASE LAW

### A. United States Court of Appeals (Fourth Circuit)

#### 1. Appointment of Receiver – Stay of Bankruptcy

In Gilchrist v. General Elec. Capital Corp., 262 F.3d 295 (4<sup>th</sup> Cir. 2001), the United States Court of Appeals for the Fourth Circuit found that the district court erred in giving preference to a South Carolina district court's receivership proceeding over a subsequent bankruptcy petition filed in a Georgia federal court. The district court had appointed a receiver for the assets of a South Carolina textile mill ("Spartan") at the request of the mill's major creditor ("GE") in May 2000. The district court also issued an injunction directed to "all persons" commanding them not to file any action that affects Spartan's assets. However, in June 2000 after the receivership proceeding was initiated, a group of creditors, which included employees suing for wages and benefits under the federal WARN Act, filed a bankruptcy petition in Georgia.

The district court held these 50+ Georgia creditors in contempt of its injunction and also argued that the automatic stay in bankruptcy did not apply to the South Carolina receivership proceedings under a "first-to-file" theory. The Fourth Circuit held that the mere fact that receivership commenced prior to filing of the involuntary bankruptcy petition against Spartan did not mean that the receivership proceedings were not stayed automatically upon commencement of the involuntary case in bankruptcy. In addition, the Fourth Circuit noted that the procedural requirements for liquidating a large corporation like Spartan that has thousands of creditors and property in various jurisdictions would push the receivership process to its limits and that the bankruptcy court was better equipped to deal with these circumstances.

#### 2. Truth-in-Lending Case Properly Remanded to State Court

In Hinson v. Norwest Financial South Carolina, Inc., 239 F.3d 611 (4<sup>th</sup> Cir. 2001) (unpublished), the Fourth Circuit affirmed the district court's decision to remand remaining claims of the additional joinder parties to state court after the original party settled its federal claim with the lender, Norwest. The Hinsons, the original party which brought suit in state court, alleged that Norwest failed to comply with South Carolina's truth-in-lending act by not informing the Hinsons of their right to be represented by counsel of their choosing at the closing of their loan with Norwest and by misrepresenting the interest rate and payoff amount of the loan. Norwest then removed the case to federal court based on the fact that one cause of action arose under the federal Truth in Lending Act. After the case was removed to federal court, the Hinsons amended their complaint to join seven additional parties who were also borrowers of Norwest, which additional borrowers alleged Norwest failed to comply with State law. After the Hinsons settled their claims with Norwest, only the joinder parties and their state law claims

were left to be litigated. Upon the joinder parties' motion, the district court remanded the case to State court and Norwest appealed.

The issue before the Fourth Circuit was whether the district court had the power to remand a removed case to State court after the federal claims that formed the basis for removal had been adjudicated. The Fourth Circuit affirmed the district court's decision to remand by concluding that under 28 U.S.C. § 1367(c), which authorizes a federal court to decline to exercise supplemental jurisdiction, a district court has an inherent power to remand removed state claims when the federal claims drop out of the case. Finally, the court held that the district court did not abuse its discretion in remanding the case because the federal claim had been disposed of and the State claims predominated.

### 3. Breach of Presentment Warranty Claim

In HSBC Bank USA v. F&M Bank, 246 F.3d 335 (4<sup>th</sup> Cir. 2001), a case decided under the law of Virginia, HSBC as drawee/payor bank sued F&M as warrantor for breach of its warranties of presentment. A check in the amount of \$250.00 was altered to indicate \$250,000.00 prior to being presented by F&M to HSBC. HSBC honored the check and credited the payee's account in the amount of \$250,000.00. Upon the discovery of the unauthorized alteration, HSBC recredited the account of the check's drawer, Allied Irish Bank ("AIB"), and brought suit against F&M. F&M asserted as an affirmative defense to the breach of presentment warranty claim that AIB as drawer of the check failed to exercise ordinary care in preparing the check by leaving too much space after the written and numerical portions of the check, and that such failure substantially contributed to the unauthorized alteration of the check. Under the Virginia Commercial Code, a drawer is precluded from asserting unauthorized alteration of a check as a defense if it failed to exercise ordinary care in preparing the check.

The district court found that AIB did exercise ordinary care in preparing the check and found in favor of HSBC. F&M appeals, contending that the district court's factual finding was "clearly erroneous" (F&M conceded that the factual finding by the district court must be deemed clearly erroneous in order for it to be set aside by the higher court). The Fourth Circuit affirmed the decision of the district court because it could not find that the district court's decision was clearly erroneous or implausible – noting that the district court used sound rationale to determine that the alteration could only be accomplished by abbreviating the word "thousand" and thus AIB did use ordinary care in preparing the check.

### 4. Bank Fraud; Money Laundering

In US v. Hamer, 2001 WL 589432 (4<sup>th</sup> Cir. June 1, 2001) (unpublished), the court addressed Hamer's appeal of her convictions for bank fraud, using an unauthorized access device to obtain money, goods, and services, and money laundering. Hamer, an attorney who had represented Rosslee Douglas in a civil suit, applied for and received eight credit cards in the name of Douglas, established a second telephone line at her residence under Douglas's name to effect wire transfers with Western Union using the credit cards in Douglas's name, and fraudulently obtained two mortgages on her home using Douglas's information. On several occasions, Hamer conducted wire transfers over state lines, *i.e.*, authorizing a transfer from her

home in Dillon, SC and picking up the money in Fayetteville, NC. When Douglas discovered Hamer's fraudulent use of her name, Hamer claimed Douglas had authorized her to apply for and use the credit cards in Douglas's name because Hamer was unable to obtain credit in her own name due to the failure of Douglas to pay attorneys' fees owed by her to Hamer arising from her legal representation of Douglas between December 1995 and March 1996.

Hamer alleged, *inter alia*, that the money laundering conviction was improper because the indictment failed to allege the essential elements of the offense of money laundering and that the jury instruction with respect to bank fraud was improper because it did not include an instruction on the principles of agency. The court found that Hamer's use of the fraudulently obtained credit cards together with the wire transfers did meet all of the elements of money laundering including a de minimis effect on interstate commerce and a specific intent to conceal the nature, location, source, ownership, or control of the proceeds of the unlawful activity.

With respect to the jury instructions, the court affirmed the bank fraud convictions by finding that the jury instructions were proper and Hamer was not entitled to a jury instruction on agency. The court recited the definition of agency listed in Black's Law Dictionary as a "relationship between two persons . . . where one (the agent) may act on behalf of the other (the principal) and bind the principal by words and actions." The court found that the evidence in the case did not support an inference that Hamer was acting for Douglas's benefit with the intent to bind Douglas to the obligations under the credit card applications, but instead found Hamer was acting solely for her own benefit with no intent to bind Douglas.

## **B. United States District Court/Bankruptcy Court**

### **1. Unauthorized Practice of Law – Bankruptcy Counseling**

In In re Brown, 270 B.R. 43 (D.S.C. 2001), a California lawyer and his law firm, neither of which were admitted to the South Carolina Bar or the U.S. District Court for the District of South Carolina, were found to be engaged in the unauthorized practice of law. The Browns, who were encountering economic problems, were referred by Mrs. Brown's employer to the attorney for bankruptcy counseling. The attorney and the firm undertook representation of the Browns by preparing a bankruptcy petition and a set of schedules without advising the Browns that neither were admitted to the South Carolina Bar or to practice in the South Carolina District Court. Over a year later, the attorney informed the Browns that he had not filed the petition and that he was referring the case to a South Carolina attorney. When the Browns did not receive any further communication from the California attorney or any South Carolina attorney, they sought new counsel which prepared a new bankruptcy petition and filed the current action against their former counsel.

The court found that the attorney and his firm did engage in the unauthorized practice of law because the attorney, deemed by the court to be an agent of the firm, used his specialized knowledge to offer legal advice and to draft legal documents while not being admitted to the South Carolina Bar or the appropriate court in which the case was to be brought. As further evidence of such unauthorized practice, both the attorney and the firm solicited and accepted fees from the Browns while knowing they were not authorized to assist them with their case.

## 2. Privity of Contract not Necessary for a Claim on Debtor's Estate

In re Trapp, 260 B.R. 267 (D.S.C. 2001), involved a motion by Bank of New York ("BONY"), as mortgagee, seeking to modify the automatic stay to allow it to pursue foreclosure proceedings on certain real property of Trapp (the "Debtor"), and objecting to the confirmation of the Debtor's Plan of Reorganization. BONY held a first mortgage lien on Debtor's real estate but did not have contractual privity with Debtor because the subject property was assigned by the original mortgagor to Debtor without notice to BONY. Debtor defaulted on the mortgage payments in March 2000 and the original mortgagors failed to cure the default upon their receipt of the notice of default in May 2000. The mortgage debt was then accelerated due to the default and Debtor subsequently filed for bankruptcy in November 2000. Debtor's Plan of Reorganization proposed to cure the mortgage default by recommencing monthly mortgage payments.

BONY claims that the stay should be lifted with respect to the real property that is subject to its mortgage because no debtor-creditor relationship existed between BONY and Debtor. The court disagreed, instead following the holding in the Supreme Court case of Johnson v. Home State Bank, 501 U.S. 78 (1991) which defined what constituted a "claim". The court found that BONY held a "claim" against Debtor's estate even though no privity of contract existed between the parties; therefore, a plan of reorganization could modify the rights of BONY because it was a creditor with a "claim" against a debtor's estate. Further, the court overruled BONY's Objection to Plan of Reorganization by finding that precedent existed to support the Debtor's position that a contractual acceleration of mortgage debt on a principal dwelling upon default does not end the debtor's right to cure the default in bankruptcy.

## 3. Relief from Stay to Validate a Postpetition Mortgage Recordation

In re Scott, 260 B.R. 365 (D.S.C. 2001), addressed the issue of whether to retroactively annul an automatic stay in order to validate a mortgagee's postpetition act of recording its mortgage to perfect its lien on the debtor's home. The Columbia (SC) Teachers Federal Credit Union (the "Credit Union") and Scott (the "Debtor") had signed an agreement in May 2000 whereby the Credit Union agreed to make revolving advances to the Debtor in exchange for a mortgage on Debtor's home. The Credit Union sent the mortgage for filing in May 2000 but failed to include the necessary information or remit the correct recording fees. However, the Credit Union was not notified of the problem until August 28, 2000. On August 25, 2000 the Debtor filed for bankruptcy and the Credit Union, unaware of the bankruptcy filing, properly recorded its May mortgage on September 5, 2000.

The court found that cause existed to annul the stay retroactively to allow perfection of the Credit Union's mortgage because the mortgage was originally executed and sent for filing months before the bankruptcy petition was filed, the Credit Union did not receive notice of the Debtor's petition until after the mortgage was recorded or at least in the mail to be recorded, and the Debtor did not have equity in the property subject to the mortgage thus no unsecured creditors or judgment creditors would be harmed by allowing perfection of the mortgage interest.

## **C. South Carolina Supreme Court**

### **1. Applicability of the Federal Arbitration Act in an Installment Contract**

Munoz v. Green Tree Financial Corp., 542 S.E.2d 360 (S.C. 2001), discusses the Federal Arbitration Act (“FAA”) in context of a consumer loan transaction. In this case, the Munozes commenced an action against the creditor and builder with whom they had entered into an installment contract and security agreement to finance home improvements. The Munozes claimed that they had been “grossly overcharged for materials and work performance” and that the underlying contract was an adhesion contract that contained an unconscionable arbitration clause. The creditor moved to compel arbitration pursuant to the arbitration clause in the agreement but the trial court found the arbitration clause was unconscionable and denied the motion to compel arbitration. The Court of Appeals reversed the trial court and this Court affirmed the Court of Appeals, finding that the FAA did apply because it specifically was made a part of the installment contract which stated that arbitration applies to claims “arising from or relating to this contract and the relationships which result from this contract” and that the “arbitration contract is made pursuant to a transaction in interstate commerce, and shall be governed by the Federal Arbitration Act.” The Court disagreed with the Munozes’ contention that the arbitration clause constituted an adhesion contract and thus deemed it was not unconscionable.

### **2. Architect’s Duty to Ensure General Contractors Pay Subcontractors**

Cullum Mechanical Construction, Inc. v. South Carolina Baptist Hosp., 544 S.E.2d 838 (S.C. 2001) involved the issue of whether an architect may owe a duty to ensure a general contractor pays its subcontractors. Cullum, a subcontractor, sought over \$425,000 for unpaid goods and services on a construction project, and sued the owner, general contractor, surety, and the architect. Cullum argued that the Architect owed a duty to use reasonable care in the administration of contractual provisions that were designed to ensure payment of subcontractors, specifically provisions regarding the review by Architect of the General Contractor’s payment applications and the posting by the General Contractor of a performance and payment bond. The Architect filed a motion for summary judgment which the trial court granted; however, the Court reversed and found that the trial court erred in granting Architect’s motion for summary judgment because a further inquiry into the facts of the case was desirable to clarify the application of the law. The Court stated, “Generally an architect does not have a duty to assure payment to subcontractors; however special conditions in these contract documents may have given rise to a special relationship with the subcontractors, and therefore a duty of care.”

## **D. South Carolina Court of Appeals**

### **1. Reinstatement of a Mistakenly Satisfied Mortgage**

First Palmetto Sav. Bank v. Patel, 543 S.E.2d 241 (S.C. Ct. App. 2001), involves a dispute over mortgage lien priority between two creditors. First Palmetto brought a foreclosure action against P. Patel asserting its mortgage on the property was the primary lien while a prior mortgage holder, B. Patel, asserts that its mortgage lien, which was erroneously canceled by

NBSC by its filing of a lost mortgage satisfaction, should be reinstated and have priority over First Palmetto's lien. The master in equity concluded that the attorney involved in the First Palmetto loan to P. Patel had knowledge of the facts of the prior mortgage because he had closed the former transaction with B. Patel and NBSC and had filed the subordination and collateral assignment of such mortgage. Thus, the master imputed the attorney's knowledge to First Palmetto pursuant to agency principles and canceled the mistaken mortgage satisfaction. Because this prior loan transaction occurred eight years earlier, the Court of Appeals found that the attorney could not be charged with retaining such knowledge, the knowledge could not be imputed to First Palmetto, and thus First Palmetto was an innocent party who would be prejudiced by the restoration of B. Patel's mortgage. The court stated that "a mortgage that has been mistakenly satisfied may be reinstated only where there is no third party who, without notice of the mistake, subsequently and in good faith acquires an interest in the property." Therefore, the Court of Appeals reversed the cancellation of the mortgage satisfaction and remanded the case for foreclosure with First Palmetto having first priority.

## 2. Special Referee's Conduct at a Mortgage Foreclosure Sale

Moore v. Rowe, 550 S.E.2d 877 (S.C. App., 2001) involves the novel issue of when a buyer at a judicial sale must tender his down payment. Moore, the president and sole shareholder of Fairfield Real Estate Company ("Fairfield"), was the highest bidder at the foreclosure sale of certain real estate owned by Fairfield. Contrary to the Notice of Sale, the special referee told Moore that he was required to tender his earnest money to the court within fifteen minutes of the closing of the sale. After Moore could not tender his deposit within the allotted time limit, the referee re-auctioned the property and Rowe was the successful bidder at the second sale. Moore objected to the second sale and moved to confirm the first sale. The Court agreed with Moore and found that the special referee's surprise amendment to his order of sale after the close of the bidding was invalid. The Court held that a purchaser at a foreclosure sale has until 5 o'clock p.m. on the sales date to tender the required deposit unless the order of the Court and the notice of sale specifically provide for a different payment time for the deposit.

## 3. Attorney's Fees and Costs under the Mechanic's Lien Statute

Keeney's Metal Roofing, Inc. v. Palmieri, 548 S.E.2d 900 (S.C. Ct. App. 2001) analyzes the issue of when a "prevailing party" in a mechanic's lien foreclosure suit is entitled to recover reasonable attorney's fees and costs, specifically whether fees and costs are to be awarded to a party that prevailed procedurally. When the defendants were dismissed from Keeney's action due to the posting of a surety bond, the Circuit Court disallowed the defendants to recover fees and costs finding that "neither the underlying policies of the mechanic's lien statutes nor the language of the statutes themselves contemplate or authorize awarding procedurally dismissed parties statutory attorney's fees and costs." The Court of Appeals reversed, holding that a party "may recover attorney's fees and costs as a 'prevailing party' under South Carolina Code Annotated § 29-5-20(A) even though the party obtained a dismissal from the suit via procedural rule, provided the dismissal was not due to mere technicality."

#### 4. Proper Notice of Redemption for a Tax Sale

In Johnson v. Arbabi, 2001 WL 705803 (S.C. Ct. App., June 25, 2001), Arbabi appeals the circuit court's decision to confirm title in Johnson's name for a condominium Johnson purchased at a tax sale. Dr. Arbabi and his wife, Akram Arbabi, as tenants in common, executed a contract in 1981 to purchase a condominium with title to remain in the name of their lender, ICIC, until the debt was paid in full. The Arbabis paid off the loan in 1989 or 1990 but did not record the deed for the condominium in their names until September 1991. However, in May 1991, before the new deed was recorded, the county sent a delinquent tax notice for the unpaid 1990 property taxes to ICIC instead of to the Arbabis. When the taxes remained unpaid, the property was sold to Johnson at the 1992 tax sale. In September 1992, a letter addressed jointly to Dr. and Mrs. Arbabi stated that the property had been sold and could be redeemed by paying \$2,329 by October 7, 1992. Dr. Arbabi never saw the tax notice or the notice of tax sale because in July 1992 he moved out of the couple's home due to marital difficulties. The notice was sent to the address of the home that Dr. Arbabi had vacated and Mrs. Arbabi signed for the notice without ever forwarding the same to her husband. In November 1992, Johnson was issued the tax deed and commenced an action to quiet title in 1993. The issues before the court were (i) whether the trial court erred in declaring Mrs. Arbabi to be the agent for Dr. Arbabi when she received the notice of the right to redeem, thus imputing the knowledge of the tax sale to her husband, and (ii) whether the county treasurer complied with § 12-51-120 when it mailed only one notice of the right to redeem to the Arbabis.

The Court of Appeals reversed the circuit court and held that the trial court did err in finding Mrs. Arbabi was her husband's agent because Dr. Arbabi denied authorizing his wife to act on his behalf regarding the condominium property, and a spouse is not the agent of the other by virtue of the marital relationship that exists between them. The law of implied agency is not applicable to the notice requirements of a tax sale, and because § 12-51-120 requires the notice of the right to redeem to be mailed to the owner of record or the owner's "authorized agent," the statutory procedures were not met. Because of the well-established rule in South Carolina that all proceedings leading to a tax sale must fulfill the applicable statutory requirements, the court found that a taxing authority's failure to provide a co-tenant with proper notice of redemption voids the entire sale.

#### 5. Enforcement of a Guaranty on a Promissory Note

In Crafton v. Brown, 550 S.E.2d 904 (S.C. Ct. App. 2001), Crafton brought an action to enforce a guaranty on a promissory note and then appealed the special referee's ruling on admissibility of parol evidence to alter or amend the guaranty. In 1988, Wellman and Brown presented an investment proposal for a plastic reclamation and recycling business to Crafton who consequently made several large loans to Wellman. Accordingly, Wellman signed a promissory note for \$2,395,484 in 1989 and Brown executed a guaranty for \$500,000. When the note came due in 1994, Wellman defaulted, so Crafton initiated this action to collect on Brown's guaranty. Brown seeks to prove through the admission of parol evidence that a collateral contract existed which conditioned his guaranty obligations on the loan by Crafton of an additional \$20-25,000 which Crafton never made. Crafton argued that the guaranty was unambiguous on its face and parol evidence was not admissible to vary its terms.

The Court of Appeals defined a guaranty as a “promise to answer for the payment of some debt or the performance of some duty in case of the failure of another person who is himself in the first instance, liable to such payment or performance.” Generally, when a guaranty is executed at the same time as the note, the consideration for the note functions as consideration for the guaranty. Moreover, the court found that “it is not necessary that the guarantor derive any benefit from either the principal contract or the guaranty as long as there is a benefit to the obligor or a detriment to the creditor.” The Court of Appeals held that the referee erred in admitting parol evidence to vary the terms of the guaranty because it found that the guaranty was unambiguous, that there was a meeting of the minds between the parties, and that the guaranty was supported by valid consideration.

#### 6. Issue Preservation

Langehans v. Smith, 2001 WL 1154161 (S.C. Ct. App. Sept. 24, 2001), involves an action to foreclose on a real estate mortgage. However, the court found that appellate review is negated by the failure of appellants to properly preserve the issues for appeal. In this case, three husbands executed a \$50,000 promissory note to NationsBank in 1988 together with a mortgage on certain real property jointly owned by the three men. The husbands eventually defaulted on the note and NationsBank brought suit against them in 1996 but did not seek foreclosure at that time, reserving its rights to do so at a later date. NationsBank obtained judgment against two of the husbands and shortly after the lawsuit, two of the wives paid the negotiated amount of the outstanding debt and received in exchange an assignment of the note, mortgage, and judgment lien from NationsBank. The wives then filed a foreclosure action against the husbands. The referee denied the wives’ foreclosure action, finding the assignment was without effect because the payments by the two wives extinguished the debt. The referee further found that it would be inequitable to the third husband’s creditors to allow the wives to achieve priority status through collusion with their husbands. The wives argued that the contractual assignment of the note entitled them to the notes rights and remedies which included the right to foreclosure. The Court of Appeals affirmed the order on appeal without resolving these issues because the wives failed to properly preserve such issues with respect to their rights as contractual assignees. Instead, the wives solely argued that they were equitably subrogated to the rights of NationsBank. But because the equitable subrogation argument was not raised to the trial court, even this issue was not preserved for review by the appellate court, leaving no issues that were properly reserved for appeal.

#### 7. Joint Account With Right of Survivorship

In Gibbs v. First Nat’l Bank, S.C. Lawyer’s Weekly, Oct. 26, 2001 (SC Ct. App. Oct. 18, 2001), the personal representative of a deceased’s estate alleged the Bank improperly distributed funds from a checking account to the surviving husband. The husband alleges that the checking account was a joint account with a right of survivorship and supported his allegation by admitting both his and his wife’s name appeared on the checks and the bank statements, that he had written checks on the account with his wife’s knowledge, and that he and his wife intended the account to be with right of survivorship. The Court of Appeals affirmed the order of summary judgment for the Bank, finding that the personal representative presented no evidence

that the account was not a joint account and failed to overcome the statutory presumption that the joint account was maintained with the right of survivorship.

#### 8. Insurable Interest of a Mortgagee's Servicing Agent

The novel issue of the insurable interest of a mortgagee's servicing agent arose in Jones v. Equicredit Corp., 2001 WL 1456833 (S.C. Ct. App. Nov. 19, 2001). Jones defaulted on both of the mortgages encumbering his property and had his debts discharged in bankruptcy pursuant to a 1994 bankruptcy petition. He then filed two more bankruptcy petitions to stay the foreclosure sales on his home. In 1996, fire damaged his home on the mortgaged property and the insurance proceeds were sent to the two mortgagees to pay off the mortgage debt. Equicredit, who was the servicing agent of Fannie Mae who held the second mortgage on Jones' property, claimed entitlement to the insurance proceeds to apply to Jones' remaining balance on the Fannie Mae judgment. In 1997, Jones' property was sold at a foreclosure sale to Equicredit who in turn sold it to a third party for \$12,500 (at this time, Jones' debt to Fannie Mae exceeded \$46,800). Jones instituted this action to recover the insurance proceeds that Equicredit received in 1996, alleging Equicredit did not have an insurable interest in the property after the foreclosure sale. The court found that Equicredit possessed an insurable interest separate and distinct from Fannie Mae's interest based on Equicredit's obligations and potential liability arising under its servicing agreement with Fannie Mae, and that such insurable interest would not be extinguished even if the mortgage indebtedness is satisfied.

#### 9. Priority of Mortgage Mistakenly Satisfied

In Allendale County Bank v. Cadle, 2001 WL 1597972 (S.C. Ct. App. Dec. 17, 2001) (unpublished), the Bank brought an action to establish the priority of its mortgage on real estate after it mistakenly filed a satisfaction of the mortgage. Cadle, who had four mortgages with the Bank on his property, wished to extinguish the first three mortgages and leave the fourth 1993 consolidated mortgage on file before he consummated a sale of a portion of the encumbered property to a third party. Cadle's attorney mistakenly prepared four satisfactions and thus the 1993 mortgage was marked satisfied in error. The mistake was discovered in 1997 when appellant contractors filed mechanic's liens against the property. With the intent of "reinstating" the 1993 mortgage, a "new" mortgage was executed by Cadle and recorded in December 1997.

The Bank then sought to foreclose its mortgage in 1998, asserting a first lien position over the claims of the appellant contractors as evidenced by the 1993 mortgage which was "re-recorded" in 1997. The appellant contractors allege their liens were entitled to priority over the Bank's lien. This court cited the First Palmetto case (see above) and found that the Bank's satisfaction of the 1993 mortgage was a mistake and that the contractors failed to show any detrimental reliance or prejudice resulting from the filing of the satisfaction.

### III. REVISIONS TO SOUTH CAROLINA COMMERCIAL CODE

Act No. 67, passed by the General Assembly at the end of the 2001 Legislative Session, revised several articles in Title 36 of the South Carolina Code. The new Article 2A created by Act 67 and the key revisions to Articles 8 and 9 are discussed below.

#### A. Article 2A: Personal Property Leases

South Carolina adopted the uniform version of Article 2A which is codified at S.C. Code Ann. §§ 36-2A-101 through 36-2A-532. This Article was adopted by South Carolina with some South Carolina non-uniform provisions after careful study by the South Carolina Law Institute. Article 2A addresses the personal property lease transaction which was previously addressed by a mix of common law principles, real estate law provisions, and references to Articles 2 and 9. The codification project which began in 1981 by the National Conference of Commissioners on Uniform State Laws and the American Law Institute and underwent several revisions over the years, borrowed the framework of Article 2, incorporated Article 9 concepts as applicable, and eventually produced an article specifically tailored to both consumer and business leasing of personal property. Although Article 2A borrows a lot of its provisions from Articles 2 and 9 with the appropriate changes reflecting leasing practices and technology, Article 2A has many of its own unique provisions. For example, where Article 9 only provided remedies for the secured party upon a default by a debtor, Article 2A recognizes the bilateral nature of lease obligations and thus provides remedies for both lessors and lessees. In addition, Article 2A relies on some common law tenets such as freedom to contract, allowing the parties to a lease transaction more flexibility in determining and measuring damages in the event of default.

Because there has been much dispute over whether a lease is truly a lease or whether it actually is a security interest disguised as a lease, the terms have been defined and clarified in the commercial code revisions. “Lease” as defined in Article 2A is “a transfer of the right to possession and use of goods for a term in return for consideration” but does not include a sale or the retention or creation of a security interest. S.C. Code Ann. § 36-2A-103(1)(j). A “security interest” on the other hand is defined as “an interest in personal property or fixtures which secures payment or performance of an obligation.” S.C. Code Ann. § 36-1-201(37). The definition further states that the facts of each case will determine whether a lease or security interest exists and sets forth examples of when a transaction creates a security interest.

“Finance leases” are also covered by Article 2A. Finance leases are three-party lease transactions whereby the lessor does not select, manufacture, or supply the goods but does acquire the goods or right to possess and use the goods, and then lessor enters into a lease or sublease agreement with the lessee who has typically approved of or at least received a copy of the agreement between the lessor and the supplier of the goods. S.C. Code Ann. § 36-2A-103(1)(g). The lessee in a finance lease mainly relies on the supplier of the goods for representations, covenants, and warranties with respect to the goods and is the intended beneficiary of such promises and warranties; thus, the lessor is released from most of its traditional liability. *See* S.C. Code Ann. § 36-2A-209.

Article 2A is divided into five parts: Part 1 – General Provisions; Part 2 – Formation and Construction of Lease Contract; Part 3 – Effect of Lease Contract; Part 4 – Performance of Lease Contract: Repudiated, Substituted and Excused; and Part 5 – Default. Article 2A became effective upon approval by the Governor on June 11, 2001.

## **B. Article 8: Investment Securities**

The 2000 Revision of Article 8 of the Uniform Commercial Code, adopted by South Carolina as part of Act 67, significantly changes the prior Article 8, updating provisions to better reflect the current securities industry. For example, Revised Article 8 sets out in a new Part 5 the commercial law rules for the indirect securities holding system, formalizing a pattern of securities holding that is already established nationwide. In addition, the scope of Article 8 has been broadened to include shares of stock in close corporations, rights in securities accounts, and “financial assets” as defined in the new Article 8.

Where the 2000 Revision of Article 8 has the most noticeable impact is in the secured transaction rules. The 2000 Revision moves the material relating to the creation and perfection of security interests in investment securities out of Article 8 and into Article 9. A new section in Article 9 (§ 36-9-115) sets forth the perfection methods for security interests in investment securities; however, the concept and definition of “control,” which is the preferred method of perfection of an investment security, remains in Article 8 at § 36-8-106. In summary, to perfect a security interest in an investment security, you either can file a financing statement on the investment property or obtain control as follows (noting that priority is given to the party with control over one who has merely filed a financing statement): (i) for certificated securities, the secured party must take possession of the certificate with any necessary indorsement; and (ii) for securities held through a securities intermediary, the lender may become an entitlement holder (securities are transferred to an account in lender’s name) or have the intermediary agree to act on instructions from the lender without further consent of the debtor who remains the entitlement holder. The key to control is that the secured party/lender maintain the ability to have the securities sold or transferred without any further action by the transferor/debtor.

## **C. Article 9: Secured Transactions**

In January 2000, the National Conference of Commissioners on Uniform State Laws (“NCCUSL”) and the American Law Institute (“ALI”) proposed and agreed upon a revised version of Article 9 (“Revised Article 9”) of the Uniform Commercial Code (the “UCC”). At the end of the 2001 Legislative Session, South Carolina adopted its version of Revised Article 9 (“SC Revised Article 9”) to be effective on the national effective date of July 1, 2001 (the “Effective Date”). SC Revised Article 9 is codified in S.C. Code Ann. §§ 36-9-101 through 36-9-709. SC Revised Article 9 provides a comprehensive scheme for the regulation of security interests in personal property and fixtures.

## 1. Significant Changes in Article 9<sup>1</sup>

SC Revised Article 9 includes the following key changes to Article 9: (i) requires centralized filing in the state of the debtor's location with the only local filings occurring in the real estate records for fixtures, as-extracted collateral, and timber to be cut (See § 36-9-501); (ii) recognizes additional categories of collateral and revised definitions of existing collateral categories (See § 36-9-102), which categories automatically include proceeds of such collateral (See § 36-9-203(f) and § 36-9-315); and (iii) deems choice of law rules are to be determined by the state where the debtor is located for most security interests perfected by filing (which is a significant change from prior law whereby the location of the collateral dictated the governing law). See Part 3 of SC Revised Article 9 for rules governing perfection and priority.

With respect to the central filing requirement, the new rule requires a creditor to file its financing statement as follows: (i) file in the central filing office of the state in which the debtor entity is formally registered; (ii) if the debtor entity is not registered in the state, file where the debtor entity has its chief executive office; and (iii) in the case of an individual, file in the central filing office of the state of such individual's principal residence (S.C. Code Ann. § 36-9-501(a)(2)). See S.C. Code Ann. § 36-9-307 for the rules determining the location of a debtor. The exceptions to the centralized filing requirement appear in § 36-9-501(a)(1) whereby security interests in as-extracted collateral or timber and fixtures are to be filed in the office designated for the filing of a mortgage on the related real property. South Carolina no longer requires a local filing for farm related collateral or consumer goods.

Second, SC Revised Article 9 expands the scope of current Article 9 by increasing the kinds of property in which a security interest can be taken by a creditor. For example, sales of payment intangibles and promissory notes, security interests created by governmental debtors, healthcare insurance receivables, consignments, commercial deposit accounts, and commercial tort claims are included as collateral in SC Revised Article 9. In addition, there have been changes in definitions from current Article 9 that will result in some collateral being classified differently under SC Revised Article 9. For example, collateral deemed a "general intangible" under former Article 9 may be classified as an "account" under SC Revised Article 9 (many payment rights classified as "general intangibles" under former Article 9 are reclassified as "accounts" under SC Revised Article 9).

The final significant change brought about by SC Revised Article 9 involves the choice of law rules. In SC Revised Article 9, the debtor's location, rather than the location of the collateral, dictates the law to be applied in determining the law governing perfection, effect of perfection, and a creditor's priority.

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<sup>1</sup> Much of the Article 9 information provided in this portion of the outline was included in the 2001 Banking Law Update materials presented at the 2001 SC Bar CLE. The information was based on the Model Revisions to the Uniform Commercial Code. To the extent those provisions were adopted in South Carolina, I have included the provisions and the correlating cites, and where South Carolina has adopted a non-uniform provision, I have attempted to note such differences.

## 2. Transition Rules

Part 7 of SC Revised Article 9 sets forth the transition rules and unless otherwise provided in Part 7, SC Revised Article 9 applies on and after the Effective Date to all transactions within its scope including those entered into prior to the Effective Date. S.C. Code Ann. § 36-9-702(a). As of January 1, 2002 all fifty states and the District of Columbia were scheduled to have enacted Revised Article 9.

### **a. Financing Statements**

Because SC Revised Article 9 adds new collateral categories and changes definitions for other categories, some collateral will be classified differently under SC Revised Article 9. Financial statements filed prior to the Effective Date must eventually be revised to include the new categories of collateral and to reflect the definitional changes. For financing statements filed prior to the Effective Date, a creditor does not have to immediately amend the collateral indication on the Effective Date but must do so at the time it files either a continuation statement in the ordinary course or the “in lieu initial financing statement” discussed below. Because creditors may or may not choose to amend their financing statements until they are due to lapse, searchers will face uncertainty as to whether or not the collateral descriptions include, or will subsequently be amended to include, the changes made by SC Revised Article 9. This period of uncertainty will not expire until June 30, 2006.

While creditors do not have a duty to amend their pre-Effective Date financial statements until the filing of a continuation statement in the ordinary course, it is prudent to amend your forms of financing statements now to ensure your security interest is covered under both sets of definitions. For example, a financing statement filed June 30, 2001 under former Article 9 will have a narrower scope than if you amend the statement to include the new categories of collateral from SC Revised Article 9, and it will likely have incorrect collateral indications because of definitional changes (*i.e.*, if collateral is indicated as a “general intangible” instead of the new term “account”). Also, additional collateral categories such as “instruments” which cannot be perfected by filing under former Article 9, can be perfected by filing under SC Revised Article 9.

### **b. Security Agreements**

Pre-Effective Date security agreements will be interpreted based on how the definitions and references to Article 9 are stated in such agreements. If a particular security agreement refers to the Article 9 defined terms “as they exist from time to time” or “as may be amended,” then the broader scope of SC Revised Article 9 will be deemed to be the parties’ intent on and after the Effective Date. However, if there are no references to amendments, then the Article 9 rules and definitions applicable at the time of the agreement will apply unless and until the security agreement is amended by the parties. Creditors and their advisors may want to amend their security agreements already in place to include the additional collateral categories and to refer to both the definitions of collateral “as defined in former Article 9 and as otherwise classified in SC Revised Article 9” in order to give themselves the broadest scope possible.

### c. One-Year Grace Period

If a creditor has an enforceable, perfected security interest under the laws of former Article 9 but such interest would not be enforceable or perfected under SC Revised Article 9, the creditor has one year in which to achieve enforceability and perfection pursuant to SC Revised Article 9 requirements. S.C. Code Ann. § 36-9-703(b). For example, if you perfected your security interest in instruments by taking possession of such instruments (as required under former Article 9), then you have one year in which to meet the SC Revised Article 9 requirements for perfection of instruments which is by filing a financing statement. A creditor cannot rely on its possession of the instrument to perfect its interest after the one-year grace period expires.

The one-year grace period does not apply if the security interest was perfected *by filing* under former Article 9 but which security interest would not be perfected under the new rules of SC Revised Article 9. For instance, if a SC corporation files its pre-Effective Date financing statement for its security interest in accounts in the NC Secretary of State's Office where the corporation's chief place of business is located, this would *not* perfect the security interest under SC Revised Article 9's rules, which look to a registered debtor entity's place of organization as the location for filing. In this case, the security interest remains perfected until the lapse of the financing statement in the ordinary course or June 30, 2006, whichever is sooner. At this time, the creditor would need to file an initial financing statement in lieu of a continuation statement (an "In Lieu Initial Financing Statement") in the jurisdiction and office prescribed by SC Revised Article 9, as discussed below.

### d. In Lieu Initial Financing Statements

If the original or a continued financing statement is filed in the incorrect jurisdiction and office required by SC Revised Article 9, a regular continuation statement filed upon the lapse of the original financing statement will not suffice to perfect the security interest. The secured party will need to file a new initial financing statement in the correct office and jurisdiction in lieu of the regular or "true" continuation statement B hence the name "In Lieu Initial Financing Statement." S.C. Code Ann. § 36-9-706.

To adequately serve the notice function of financing statements, the In Lieu Initial Financing Statement must specifically reference the original financing statement and the most recent continuation statement, if any, by filing office, date(s) of filing, and file numbers. The In Lieu Initial Financing Statement must also indicate that the original financing statement is still effective. S.C. Code Ann. § 36-9-706(c). The In Lieu Initial Financing Statement may be filed *at any time* on or before the scheduled lapse date B there is no need to wait until you are within the 6-month period prior to the lapse date. (Compare this to "true" continuation statements which must be filed within the 6-month period prior to the scheduled lapse date.)

**\*\*NOTE:** Regardless of whether you file a true continuation statement (if filing was in the correct jurisdiction and office as required by SC Revised Article 9) or an In Lieu Initial Financing Statement, you must amend the collateral categories and definitions per SC Revised

Article 9 at this time to reflect what is intended to be covered by the financing statement based on the meanings of the terms under SC Revised Article 9.

Finally, the information provided in all financing statements, true continuation statements, and In Lieu Initial Financing Statements, must conform to S.C. Code Ann. § 36-9-516(b). The additional information not previously required under former Article 9 includes the following: (i) whether the debtor is an individual or an organization; (ii) if the debtor is an organization, the type and jurisdiction of the organization; and (iii) the identification number issued to the organization by the jurisdiction (or if none, state “none”).

#### **e. Pre-Effective Date Filings in Local Offices**

SC Revised Article 9 requires central filing *unless* the financing statement is filed as a fixture filing or covers as-extracted collateral or timber to be cut. S.C. Code Ann. § 36-9-501. For these latter types of collateral, you will file in the local office where the real estate records are recorded. Security interests in farm-related products and consumer goods will no longer be filed in the county in which the debtor resides (or if debtor is out of state, the county where the goods are kept), and security interests in crops will no longer be filed in the county where the land is located; instead such interests will be filed at the Secretary of State’s Office.

In order to amend or continue a pre-Effective Date financing statement that was originally filed in a local office that is no longer accepting such filings under SC Revised Article 9, you follow the same procedure outlined above for an In Lieu Initial Financing Statement. It is also advisable to obtain certified copies of all local filings for your own records in the event that the local office closes up after the enactment of SC Revised Article 9.

### **3. SC Revised Article 9 Forms**

South Carolina has adopted standardized national UCC Financing Statement forms which can be accessed from the South Carolina Secretary of State’s website at [www.scsos.com/forms.htm#UCC](http://www.scsos.com/forms.htm#UCC). These forms include the UCC1 (financing statement) plus Addendum, UCC3 (amendment filing) plus Addendum, UCC11 (information request), UCC5 (correction filing), and the In Lieu Initial Financing Statement form. These forms are in Adobe’s Portable Document Format (PDF) and can be filled out on the screen and printed out by the practitioner. Because the debtor no longer has to sign the forms, this should facilitate the timely and accurate filing of UCC forms by both South Carolina and out of state secured parties and their counsel.

One final change promulgated by SC Revised Article 9 that is of particular importance to the practitioner is found in § 36-9-503 relating to the name of the debtor as indicated on a financing statement. Section 36-9-503 requires that the name of the debtor on all UCC filings be stated correctly, and if the name is incorrect the filing is deemed “seriously misleading” and will be rendered ineffective as a matter of law. S.C. Code Ann. § 36-9-506. To be sufficient, a registered debtor’s name must reflect the name indicated on the public record of the debtor’s jurisdiction of organization; for individual debtors and unregistered entity debtors, you must use the debtor’s full legal name. For individuals, it is suggested that you use the name listed on a

drivers license, birth certificate, social security card, etc. and it may be prudent to file under multiple versions of the name if there is any uncertainty. Section 36-9-503 also provides guidance for statements filed for a debtor which is a decedent's estate or a trust or trustee. Finally, note that a financing statement that only indicates a trade name of a debtor will not be sufficient.

A full summary of the changes in Article 9 as reflected by SC Revised Article 9 is beyond the scope of this update. The above mini-summary of some of the key changes in Article 9 is intended merely to provide a starting point for the practitioner involved in commercial lending transactions. Both the Official Comments and the South Carolina Reporters Comments provide invaluable information and should be consulted when navigating the requirements of, and the effects intended by, SC Revised Article 9.