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In Brief

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The Kentucky Bankers Association and Morgan & Pottinger Lead Passage of House Bill 264

The Kentucky Bankers Association and M&P recently collaborated in drafting House Bill 264, which was signed into law by Gov. Beshear on April 13, 2010, and will be effective on July 15, 2010. The bill, which consisted of various statutory amendments, addressed several issues currently troubling Kentucky banks. It is expected to provide much-needed clarity in important lending areas and strengthen the legal position of banks in a variety of ways.

KRS §382.270—Curing the Acknowledgment of Mortgages

HB 264 addressed a growing problem involving the acknowledgement of deeds and mortgages. Prior to HB 264, KRS §382.270 stated that in order for a mortgage or deed to be valid against a bona fide purchaser, the deed or mortgage must be properly acknowledged or proved by law. While there was an exception built in to the statute for mortgages and deeds recorded prior to July 12, 2006, any mortgages and deeds recorded after July 12, 2006, that were not properly acknowledged were consistently avoided by bankruptcy trustees on the grounds that they failed to provide constructive notice to a bona fide purchaser for value. Consequently, creditors with otherwise valid mortgages were losing large sums of money based on what most would consider a clerical error.

HB 264 provides that any mortgage or deed lodged of record, with or without a proper acknowledgment, constitutes sufficient notice to a purchaser for valid consideration and, thus, a bankruptcy trustee as well. The amendment to KRS §382.270 should ease the concerns of banks across Kentucky. As long as the mortgage is lodged of record, no bankruptcy trustee or bona fide purchaser can avoid it based on a defective acknowledgement.

KRS §382.430—Clerical Errors or Omissions of County of Residence

KRS §382.430 previously required mortgages to list the county and state of residence and the post office address of the person or corporation holding the property. This requirement sometimes led to clerical errors and omissions that endangered banks' security. HB 264 amends KRS §382.430 to read that a mortgage or other lien instrument must include the address of the person or the principal place of business of a corporation in order to have a valid lien on the property, removing any requirements regarding the necessity to include the county of residence in the mortgagee's address. This amendment protects Kentucky banks who have omitted the county of residence in their loan documents—a small mistake but one that could have great consequences under the prior statue.

KRS §425.126—Clarifying Execution on Securities

HB 264 also modernized KRS §425.126 by bringing it in line with current UCC Article 8. It now includes uncertificated securities within the realm of interests subject to garnishment and attachment. Company stock is now often issued as an uncertificated security held by a securities intermediary, nominee or agent. As the securities themselves have changed in form, the law needed to follow in making such interests attachable.

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HB 264 further addresses this issue by setting forth the requirements for attaching or garnishing an interest in uncertificated securities. In order to attach, garnish or otherwise execute on a security, certificated or otherwise, one must include the name of the issuer, the class or series of the security, or both, the number of shares or other units of interest represented by the security, the name of the debtor and the name of the person, if different from the debtor, having an account on the books of the securities intermediary or issuer.

To attach, garnish or otherwise execute on an option or right to acquire a security, the order must include the name of the issuer, the class or series of the security in which the option or right to acquire exists, the name of the debtor and the name of the person, if different from the debtor, having an account on the books of the securities intermediary or issuer in which such option or right is shown.

To attach, garnish or otherwise execute on a security entitlement, other than an option or right to acquire a security, the order must include the name of the debtor and the name of the person, if different from the debtor, having an account on the books of the securities intermediary or issuer in which the security entitlement is shown.

It is important to note that the new amendments require strict compliance and any failure to set forth all of the elements fails to bind or give notice to the securities intermediary, issuer, nominee or agent having an interest in the security, option to acquire the security or security entitlement. The new requirements provide clarity for securities intermediaries that hold uncertificated securities in the name of judgment debtors as well as banks attempting to execute on these securities.

KRS §427.150—Limiting Exempt Property

Collecting on a judgment has always been a troublesome area for banks, especially when faced with a debtor claiming various exemptions under the Federal Bankruptcy Code. HB 264 amends KRS §427.150 by limiting the exemptions a debtor may claim in an individual retirement account or annuity, deferred compensation account, tax sheltered annuity, simplified employee pension, profit-sharing, stock bonus or other retirement plan described in the Internal Revenue Code of 1986, or Section 408 or 408A of the Internal Revenue Code.

These exemptions do not apply if the contribution occurs within 120 days: (1) before the debtor files for bankruptcy if the exemption is being applied in a federal bankruptcy proceeding or (2) before the earlier of the entry of the judgment or other ruling against the debtor or the issuance of the levy, attachment, garnishment, or other execution or order against which this exemption is being applied, if this exemption is being applied in other than a federal bankruptcy proceeding. The new amendments are a significant step in preventing debtors from hiding and claiming funds as exempt that would otherwise be available to creditors for repayment of a debt.

KRS §427.170—Limiting Federal Bankruptcy Exemptions to Federal Bankruptcy

HB 264, codifying MPM Financial Group, Inc. v. Morton, 289 S.W.3d 193 (Ky. 2009), amends KRS §427.170 to limit the exemptions that an individual domiciled in Kentucky may claim under the Federal Bankruptcy Code to cases filed in bankruptcy court. In MPM Financial, the debtor attempted to extend such exemptions to his "estate" without filing for bankruptcy. The new statute limits the federal bankruptcy exemptions to only those individuals that have filed for bankruptcy. It expressly prevents the application of such exemptions outside of bankruptcy court.

KRS §355.9-518—Banks and Article 9 Correction Statements

A consistent concern of banks since the enactment of Revised Article 9 has been the ability of third parties to terminate or otherwise amend a bank's financing statement on file with the Kentucky Secretary of State without proper bank authorization. HB 264 addresses this concern by amending KRS §355.9-518 to allow banks to file a correction statement that will directly affect the effectiveness of any termination statement or other amendment filed by a third party that purports to affect, adversely or otherwise, a bank's perfection of its security interest.

In order to comply with the new requirements, the correction statement must include: (1) a written statement of an officer of the bank filing the correction statement, which (a) identifies the record to which the correction statement relates by the file number, (b) indicates that it is a correction statement, (c) provides the basis for the belief that the record is inaccurate and (d) indicates the manner in which the person believes the record should be amended to cure any inaccuracy; (2) the officer's title and information identifying how the party filing the correction statement qualifies as a bank; (3) the officer's written statement must be duly acknowledged before a notary public; and (4) the record to which the correction statement relates was originally filed by or refers to a record filed by the bank filing the correction statement.

Timothy A. Schenk

Did you know?

New amendments to Article 9 are on their way. M&P's John McGarvey reports that the drafting committee on which he served has offered its product to the American Law Institute and the Uniform Law Commission for approval at their 2010 meetings. We expect the amendments to be offered to the legislatures this fall; however, the effective date may be delayed until 2013 to assure uniformity.

The focus of the amendments is on providing certainty in the area of debtor names, particularly individuals, and guidance on the perfection of security interests when debtors relocate to another jurisdiction. The Official Comments are also being amended to illustrate how to use the model forms of notice of disposition when the disposition will be through an Internet sale.

For more information, please contact John McGarvey.

2010 Kentucky General Assembly—Legislative Session Overview

While Gov. Beshear may consider the General Assembly's failure to enact a budget for the next biennium to be the defining moment of the 2010 legislative session, many bills were still considered and passed. In the 2010 session, 232 Senate bills and 601 House bills were introduced. Of these, 44 Senate bills and 118 House bills were enacted into law. Under Section 55 of the Kentucky Constitution, the general effective date of 2010 legislation is 90 days after adjournment, or July 15, 2010. Certain bills may have provisions accelerating or delaying this effective date.

Of the many bills enacted, M&P believes the following 12 bills will be of the most direct interest to our financial institution and lender clients:

SB 76—Adopting the Uniform Prudent Management of Institutional Funds Act.

SB 117—The Kentucky Department of Financial Institution's regulatory amendments bill.

This 25-page bill addresses numerous subjects, including: (i) a new statute expressly prohibiting non-banks from using "bank" and related terms in their names or advertising; (ii) requiring a finding that the public convenience and advantage will be served before an application for a new bank or trust company is approved and increasing the minimum initial capital stock from $2.5 million to $5.0 million; (iii) prohibiting a bank's capital stock from being reduced to less than $2.5 million; (iv) setting a 1 year holding period (may be increased by the DFI) for non-real estate assets received by a bank as liquidation of collateral; (v) allowing the DFI to approve the use of different names for certain bank branches; (vi) clarifying that a bank may both establish "or acquire" new branch offices; (vii) providing that the consolidation of two or more branches into a single location in the same vicinity or neighborhood is not a branch closure requiring a 90-day advance notice to the DFI; (viii) for lending limit calculations, requiring any negative balance of a bank's undivided profits account to be deducted when computing the total capital stock and surplus; (ix) exempting from lending limit restrictions loans secured by a segregated deposit account in the lending bank in which a perfected security interest is held; (x) eliminating the requirement for an advisory bank board after a bank merger; (xi) setting specific fee caps for guardians and conservators; and (xii) eliminating the requirement of KRS §286.3-420 of the publication of a bank's financial statement after a bank examination.

SB 130—Omnibus revisions to state securities laws.

SB 150—Omnibus business entity law revisions.

SB 151—Creating the Kentucky Business Entity Filing Act (effective January 1, 2011) amending how Kentucky business entities file documents with the Kentucky Secretary of State.

SB 152—Omnibus business entity law revisions.

HB 171—Revision to the requirements for including in deeds an "in-care-of" address for subsequent ad valorem tax bills.

HB 188—Replacing the common law "Rule Against Perpetuities" with a statutory regulation and various other amendments involving trusts and estates.

HB 264—Omnibus bill relating to financial institutions

This bill is more thoroughly addressed in this newsletter; however, the bill does effect the following: (i) notices to mortgagees of delinquent property taxes; (ii) collateral for local school fund deposits; (iii) defective acknowledgements in deeds and mortgages; (iv) addresses of mortgagees in mortgages; (v) garnishing uncertificated securities; (vi) clarifying that bankruptcy exemptions only apply in a bankruptcy proceeding; (vii) confirming a financial institution's right to file a correction statement for Uniform Commercial Code filings.

HB 298—Omnibus revision of the process of collecting ad valorem property taxes.

This bill has an emergency effective date and became law on April 7, 2010.

HB 391—Omnibus revision of the law governing condominiums.

This bill has a delayed effective date of January 1, 2011.

HB 454—New lien rights of utilities against retail business ratepayers for unpaid services.

We will be happy to discuss with our clients in more detail these bills or any other bills that may be of interest.

Numerous bills were introduced, but not passed, that would have effected financial institutions—both positively and negatively. For example, House Bill 465 would have required a mortgagee creditor to register vacant properties once foreclosure proceedings began and would have imposed maintenance responsibilities on the mortgagee. Real estate appraisal management companies would have been regulated by Senate Bill 66. District courts would have been granted jurisdiction to hear disputes over motor vehicles titles by Senate Bill 120. The actual jurisdictional limits of small claims and district court would have been increased by House Bill 103 and House Bill 365. The formal steps for the notarization of a document would have been changed by House Bill 471. Deeds would have had to include a Property Valuation Administration tract number if House Bill 567 had passed. Deferred deposit transactions and the business of debt purchasing would have been regulated by House Bill 381 and House Bill 245, respectively. A two-year statute of limitations for wrongful termination and wrongful discharge employment claims would have been established by House Bill 369.

Finally, we would also point out that House Bill 415 makes texting, instant messaging, or emailing while driving a crime (with courtesy warnings until January 1, 2011). In addition to a genuine concern for our clients' safety, we would also warn employers that accidents caused by their employees' sending or reading business-related-text messages while driving poses vicarious liability risks to the employer.

M. Thurman Senn

M&P is pleased to announce:

Mindy Sunderland and Emily Cowles have been named Shareholders to the firm. Eric Jensen and Molly Rose have been named Members to the firm.

Morgan McGarvey, formerly the Special Assistant Attorney General for the Commonwealth of Kentucky, has joined the firm as an associate attorney. McGarvey is a 2007 graduate of the University of Kentucky, College of Law where he was on the Kentucky Law Journal, National Moot Court Team and President of the Student Bar Association. He obtained his bachelor's degree from the University of Missouri. McGarvey's practice will be concentrated in the area of commercial litigation. McGarvey is located in M&P's Louisville office and can be reached at 502-572-7073 or jmm@morganandpottinger.com.

In other news:

Trak America, one of the nation's largest collection/debt buying companies, named M&P as its Large Market Firm of the Year.

Brad Salyer has been admitted to practice in Tennessee and Indiana.

Morgan McGarvey was accepted to the 2010 Class of Leadership Kentucky.

Mindy Sunderland, Taylor Hamilton, Tim Schenk, John Majors, Morgan McGarvey and Brad Salyer participated as volunteer attorneys for the Credit Abuse Resistance Education Program.

John McGarvey has been appointed to Greater Louisville Inc.'s Tax Reform Task Force.

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