

August 2011 Update: Two Recent Georgia Banking Decisions Hold Important Lessons for Lenders

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The Georgia Court of Appeals recently issued two opinions pertinent to the day-to-day operations of Georgia lenders. The following summaries of the opinions warrant review and consideration in order to avoid a number of potential pitfalls.

- I. ***The failure to present competent evidence as to the “regularity” of a non-judicial foreclosure sale will result in the Superior Court refusing to confirm the sale.***

Summary

In what appears to be a marked reaction to the record number of property foreclosures and bank closures in the state in recent years, on June 23, 2011, the Georgia Court of Appeals barred what was previously a common practice of banks in confirming foreclosure sales. In *Franklin v. First Georgia Banking Company*, First Georgia Banking Company (“FGBC”) attempted to confirm three non-judicial foreclosure sales. The Court of Appeals held that FGBC presented proper evidence as to notice of sales under power and as to the true market value of the subject properties. FGBC’s evidence as to the regularity (*i.e.*, the occurrence and outcome) of the foreclosure sales, however, was deemed insufficient because FGBC failed to present first-hand testimony or other evidence from an actual witness to the sales. The statements of FGBC’s attorney as to the occurrence and outcome of the foreclosure sales were deemed insufficient to carry FGBC’s burden because the attorney did not actually witness the sales.

Pertinent Law

Under O.C.G.A. § 44-14-161 (the “Foreclosure Statute”),¹ within 30 days of a non-judicial foreclosure under power of sale, a lender is required to initiate proceedings to have the

¹ The Foreclosure Statute provides that:

Superior Court confirm and approve the sale of the subject property. During a required evidentiary hearing, the lender must present testimony or other admissible evidence establishing: (i) the true market value of the subject property; (ii) that the debtor received adequate notice of the evidentiary hearing; (iii) that the foreclosure sale was properly advertised; and (iv) the regularity (*i.e.*, the occurrence and outcome) of the sale. The failure to present evidence establishing any of the foregoing will result in the Superior Court's refusal to confirm and approve the sale and will likely result in the Superior Court ordering the resale of the property.

Background

On February 1, 2010, FGBC filed an application (the "Confirmation Proceeding") for the confirmation of three January 5, 2010, foreclosure sales. In conjunction with the Confirmation Proceeding, FGBC filed a report for confirmation of sale (the "Report") wherein FGBC stated that: (i) the debtor defaulted on its loans with FGBC; (ii) the debtor signed deeds to secure debt on the three properties serving as collateral (the "Collateral") for the loans; (iii) FGBC foreclosed on the Collateral pursuant to power of sale provisions in the deeds to secure debt; (iv) FGBC auctioned the Collateral; and (v) the Collateral sold for the stated amounts.²

During an evidentiary hearing, the debtor was unwilling to stipulate as to FGBC's satisfaction of the requirements of the Foreclosure Statute. FGBC introduced the publisher's affidavits and copies of the pertinent notice of sale under power publications as evidence of the proper advertisement of the Collateral. FGBC introduced expert testimony from real estate appraisers as to the true market value of the Collateral. FGBC's only evidence as to the regularity of the sale of the Collateral, however, was: (i) the Report; and (ii) statements from its attorney as to the results of the sale of the Collateral. The Superior Court confirmed the foreclosure sales despite the debtor's assertion that FGBC failed to introduce proper evidence as to the regularity of the sale. The debtor appealed.

(a) When any real estate is sold on foreclosure, without legal process, and under powers contained in security deeds, mortgages, or other lien contracts and at the sale the real estate does not bring the amount of the debt secured by the deed, mortgage, or contract, no action may be taken to obtain a deficiency judgment unless the person instituting the foreclosure proceedings shall, within 30 days after the sale, report the sale to the judge of the superior court of the county in which the land is located for confirmation and approval and shall obtain an order of confirmation and approval thereon.

(b) The court shall require evidence to show the true market value of the property sold under the powers and shall not confirm the sale unless it is satisfied that the property so sold brought its true market value on such foreclosure sale.

(c) The court shall direct that a notice of the hearing shall be given to the debtor at least five days prior thereto; and at the hearing the court shall also pass upon the legality of the notice, advertisement, and regularity of the sale. The court may order a resale of the property for good cause shown.

² While not germane to the Court of Appeals' analysis, the three parcels which comprised the Collateral sold for \$170,000.00, \$48,000.00, and \$300,000.00.

The Court of Appeals determined that FGBC failed to introduce competent evidence as to the occurrence and outcome (*i.e.*, the regularity) of the sale of the Collateral. The Court of Appeals determined that FGBC's failure to properly introduce evidence or testimony from a witness to the sale made it impossible for the Superior Court to determine that the sale was conducted with regularity under the Foreclosure Statute. Although FGBC's attorney proffered that the Collateral sold for stated amounts, the attorney's statements (normally considered competent evidence) were inadmissible hearsay because there was no evidence that the attorney actually witnessed the sale. Based on FGBC's failure to introduce competent evidence as to the regularity of the sale, the Court of Appeals reversed the confirmation of the sale of the Collateral.

Pitfall to Be Avoided

The failure to properly introduce testimony or evidence as to all aspects of a non-judicial foreclosure under power of sale (including testimony or other evidence from a witness to the foreclosure sale) will result in the trial court refusing to confirm the foreclosure sale.

- II. *When appraising multiple parcels for purposes of sale on foreclosure, the appraiser should either make a market value determination with respect to each individual parcel or (at a minimum) the appraisal must set forth a mechanism by which the market value of each individual parcel may be determined.***

Summary

On June 21, 2011, the Georgia Court of Appeals decided *Battle Properties, Inc. v. Branch Banking and Trust Company*. The Court held that Branch Banking and Trust Company ("BB&T") properly demonstrated (through a discounted cash flow valuation method) the true market value of two parcels of collateral upon which BB&T foreclosed under a power of sale. The Court of Appeals: (i) noted that the Foreclosure Statute does not provide for any specific method of property valuation; (ii) held that the trial court was permitted to determine that BB&T's discounted cash flow valuation model (which considered the depressed market conditions in the area) was more accurate than the debtor's proffered sales comparison valuation model; and (iii) determined that, although BB&T's appraisal did not specifically provide the true market value for each individual parcel, the appraisal and appraiser's testimony provided the methodology by which the true market value of the individual parcels could be determined.

Pertinent Law

Under the Foreclosure Statute,³ the lender must present evidence establishing the true market value of the subject property. The failure to present evidence establishing the true

³ The pertinent section of the Foreclosure Statute provides that:

... (b) The court shall require evidence to show the true market value of the property sold under the powers and shall not confirm the sale unless it is satisfied that the property so sold brought its true market value on such foreclosure sale....

market value of the subject property will result in the Superior Court's refusal to confirm and approve the sale of the subject property and will likely result in the Superior Court ordering the resale of the property.

Background

On September 30, 2008, BB&T filed a Confirmation Proceeding for the confirmation of the \$576,000 sale of two parcels (consisting of 24 townhome lots) of collateral.⁴ During an evidentiary hearing, BB&T and the debtor presented opposing expert witness valuation testimony.

In valuing the two parcels at \$575,000, BB&T's valuation expert utilized a discounted cash flow valuation model that took into account the depressed market conditions in the area.⁵ The debtor's valuation expert utilized the sales comparison valuation model in valuing the two parcels at \$816,000.⁶ The debtor's valuation expert, however, admittedly: (i) relied on the sale of two single-family home lots as alleged comparative sales for the townhome lots; (ii) used a non-arm's length negotiation as an alleged comparative sale; and (iii) utilized alleged comparative sales wherein the sale prices were agreed to prior to the 2008 national real estate collapse.

The Superior Court found BB&T's appraisal and expert testimony to be more accurate than the debtor's valuation and affirmed the sale of the two parcels. The debtor appealed, arguing that BB&T failed to demonstrate true market value under the Foreclosure Statute because BB&T allegedly failed to value the collateral as two separate and independent parcels.

The Court of Appeals determined that although BB&T's appraisal did not specifically provide a separate true market value for each of the two parcels, the appraisal and the testimony of BB&T's valuation expert provided the methodology by which the value of each parcel could be obtained. The Court of Appeals also took note of the fact that both BB&T's and the debtor's appraisal experts opined that the value of the parcels would not change if they were sold separately rather than as part of a bulk transaction.

Pitfall to Be Avoided

In foreclosing on multiples parcels, the failure to obtain separate appraisals for each parcel, or a single appraisal that assigns separate market values to each individual parcel, opens the door for debtors to argue that the lender failed to introduce evidence as to the true market value of each independent parcel.

⁴ Parcel 1 contained eight townhome lots and Parcel 2 contained 16 townhome lots.

⁵ BB&T's valuation expert determined the true market value for the parcels by multiplying \$23,958 (his valuation per lot) by 24 lots (the total number of lots in both parcels) to reach a total of roughly \$575,000.

⁶ The debtor's valuation expert valued each of the 24 lots at \$34,000.

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