Professional Responsibility -- Canon 6 and the Lender's Attorney

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help find a location for the business. The court found a "substantial connection" with North Carolina on these facts. In Goldman the contract was made within the state but no representative entered. Parkland's activities in the state came about through the actions of its agent, Goldman. At first blush it appears that Goldman, by his own actions, created personal jurisdiction over Parkland. But this was done pursuant to an agreement with the foreign corporation, which was the beneficiary of the activities. And the agreement (just as the one in Byham) contemplated a continuing relationship between the parties, not just a single transaction as in Erlanger. Considering the two cases together, it is unrealistic to say that just the making of a contract within the state in Goldman takes the place of the temporary entry of a representative in Byham to supply the substantial connection. This area of the law depends heavily on a case by case analysis and does not lend itself to facile comparisons.

But it seems apparent that the North Carolina court views the place of the contract's completion as only one factor to be considered in finding a substantial connection between the contract (and thus the foreign corporation) and the state. The inference from Goldman and the other cases discussed herein seems to be that the mere fact that the contract on which the cause of action arises was made within the state is not enough by itself to sustain jurisdiction over a foreign corporation.28

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Professional Responsibility—Canon 6 and the Lender's Attorney

An ethical problem recently arose in a situation in which an attorney was employed by a lending institution to make a title search and close a secured loan. The transaction was completed and the note and deed of trust

27 Id. at 61, 143 S.E.2d at 234.
28 A holding that execution in North Carolina is alone sufficient for jurisdiction would be inconsistent with the other phrase of N.C. Gen. Stat. § 55-145(a)(1) (1965), which subjects foreign corporations to suit within the state on causes of action based on contracts "to be performed in this State." See note 9 and accompanying text supra. This has been construed to mean performance to a substantial degree. Bowman v. Curt G. Joa, Inc., 361 F.2d 706 (4th Cir. 1966); accord, Golden Belt Mfg. Co. v. Janler Plastic Mold Corp., 281 F. Supp. 368 (M.D.N.C. 1967), aff'd per curiam, 391 F.2d 266 (4th Cir. 1968). It would be anomalous for the court to allow the mere fact of execution in North Carolina, no matter how fortuitous the circumstances, to be a sufficient basis for jurisdiction while insisting that otherwise a substantial degree of performance within the state must be shown.
were assigned. After several years, the assignee of the note foreclosed on the securing deed of trust. This action prompted the borrower to request an investigation by the Consumer Protection Division of the North Carolina Attorney General's office as to possible usury. The investigation was initiated and inquiries were directed to the attorney who had handled the original transaction. Unsure of the nature of his relationship to the parties, he requested advice from the Council of the North Carolina State Bar as to what course of action he should pursue in response to the inquiries.

The answer to this request was supplied by Ethics Opinion 715, in which the Council held that the attorney was employed by the lending institution to search the title to the land which was to secure the proposed loan, and therefore he could not disclose the possibility of usurious interest rates to the borrower. The basis for the holding was that such a disclosure by the attorney would be a violation of Canon 37 of the Canons of Professional Ethics, because it would breach the "Confidences of a Client," the lending institution.

Thus the Council affirmatively held, despite some unreconciled prior language to the contrary, that the attorney who is employed by the lender to search title incident to a secured loan transaction represents the lender and not the borrower even though the usual practice is for the borrower to pay the attorney's fee. The lender's practice of using its attorney to search title and requiring that his fee be paid by the borrower has been upheld as not unethical in a series of opinions by the Council of the North Carolina State Bar. The rationale of these opinions is not given, but there are at least two alternatives. One is that only the lending institution

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3 N.C. State Bar Council, Opinions, No. 395 (1962), reported, Melott II-95, is cast in terms of "duty to the borrower." This opinion is more fully explored at notes 8-10 infra.
4 N.C. State Bar Council, Opinions, No. 370 (1962); No. 291 (1959); No. 153 (1955); No. 43 (1947), respectively reported, Melott II-85, -64, -27, -7. In these opinions the central ethical question involved the impact of Canon 6 of the Canons of Professional Ethics in the secured loan situation. Canon 6, reported, Melott VI-8, is entitled "Adverse Influences and Conflicting Interests," and states in pertinent part: "It is unprofessional to represent conflicting interests, except by express consent of all concerned given after a full disclosure of the facts."

The ABA Committee on Professional Ethics has also considered, and found no impropriety in, the identical practice. See ABA Comm. on Professional Ethics, Opinions, No. 837 (Informal).
is the client and that the attorney does not represent the borrower. If this is the position taken, then the holdings indicate that Canon 6, which proscribes representation of conflicting interests, does not apply in the secured loan situation, for that Canon contemplates representation of two interests by the same attorney. Another possible rationale for these opinions is that the attorney is representing both the lender and the borrower, but that since each has the same interest in ascertaining title to the land there is no actual conflict of interest. Under this theory Canon 6 applies but is not violated. Since none of these opinions involved an actual conflict of interest, it was unnecessary for the Council to clarify the basis of its holdings.

In Opinion 395 such a conflict was present. There the attorney searching title for a lender discovered that the proposed loan would be usurious and requested advice as to the extent of his duty to the borrower. The Council held that he had discharged his duty to the borrower by furnishing him, upon request, a disbursement sheet which disclosed on its face the usurious interest rates. By speaking in terms of duty to the borrower the Council apparently rejected the theory that the borrower is not represented. Had this theory been the basis of the prior opinion, the lender (Bank) as the client.

More recently the Council has recognized, in N.C. State Bar Council, Opinions, No. 712 (1970), reported, that the mere potential for conflict may be sufficient to find a violation of Canon 6. The Council said:

There are few situations in which a lawyer would be justified in representing in litigation multiple clients with potentially differing interests. This is so because when the interests move from being potentially differing to actually differing, the attorney is required to withdraw from employment which might well result in a hardship and burden on the client.

However, Opinion 712 deals with litigation. The Council may be reluctant to extend its reasoning to the secured loan transaction, either because it feels that there is a fundamental difference in representation during litigation and representation in the course of ordinary business affairs, or because it is willing to tolerate potential conflict in the secured loan situation since it views that potentiality as an inevitable result of a necessary method of handling the transaction.

In practical effect the duty to the borrower recognized here is more apparent than real because the disbursement sheet normally would have been furnished to the borrower as an incident of the transaction. In fact, even after it is furnished the borrower most likely remains uninformed as to the ultimate interest rate. Only extended calculation would reveal this figure, and even if the borrower made a correct determination he probably would be unaware that it is usurious.
opinions, the holding in Opinion 395 would have been that there was no duty to the borrower since no duty is owed by an attorney to one who is not his client. However, although seemingly rejecting the one alternative, the Council did not fully espouse the other. Had the basis of the prior holdings been that the attorney represents both parties, the Council would have ordered his withdrawal in the instant situation since Canon 6 precludes further representation of either party once a conflict has arisen between their separate interests. Thus the holding in Opinion 395 seems to indicate that there is a primary duty to the lender, with only a secondary duty to the borrower. Whatever it may say about the scope of this duty to the borrower, it does indicate that he is represented to some extent.

Opinion 715, without reconciling Opinion 395, denied any role for Canon 6 in this situation. Its holding that information as to usury is privileged between the lender and its attorney is clearly based on the premise that only the lender is the client. Thus, the Council found no duty of disclosure to the borrower, and, moreover, that voluntary disclosure would violate Canon 37. This holding leaves the borrower completely unprotected despite the fact that he pays the fee and as a result may well believe that his interests are represented. Such a belief would be erroneous at present but nothing in the opinions requires that the error be brought to the borrower’s attention.

However, by holding that only the lender is the client, the Council properly rejected the alternative holding that both the lender and the borrower are represented. In doing so, it avoided the application of Canon

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10 See N.C. STATE BAR COUNCIL, OPINIONS, No. 558 (1967), reported, Melott II-149. This opinion allows representation of two clients after full disclosure as long as no conflict exists or arises between them, but requires withdrawal if conflict does arise. See also N.C. STATE BAR COUNCIL, OPINIONS, No. 712 (1970), reported, N.C. BAR at 9; No. 709 (1970), reported, N.C. BAR at 11.

11 Although the ruling in Opinion 395 afforded only minimal affirmative protection, it did not preclude further action on the borrower’s behalf by the attorney; the opinion required merely that the attorney furnish a disbursement sheet upon request, but did not forbid him to do more if his conscience dictated that he must. However, under Opinion 715, even if the attorney feels morally obligated further to protect the borrower he cannot.

12 Whether borrowers routinely make this assumption is a question this writer is unprepared to answer. Informal talks with practicing attorneys and real estate brokers have revealed that on occasion borrowers have done so. One attorney commendably noted that as a matter of personal feeling he routinely makes certain that the borrower is not misled even though he is not required to do so. It is doubtful whether all attorneys feel a similar obligation. Therefore, if only one borrower is misled and thereby damaged, both he and the whole legal profession suffer. The possibility of reliance is sufficient to call for ameliorative measures, whatever the actual incidence may be.
6 and therefore did not confront the central difficulty faced in Opinion 395—the necessity of choosing among the unpalatable remedies available for a violation of that canon.\textsuperscript{13}

But was the Council justified in refusing to find that since there is a possibility of reliance the borrower is the client? In theory, the result of such a hypothetical holding would be that only the borrower would be protected in the event of actual conflict. The practical result, however, probably would be an immediate change in the handling of the secured loan transaction. Since the problem originally arose only because there was no understanding between the parties as to who was the client, if the lender were to reach an agreement with the borrower that the attorney represented only the lender, this consent by the borrower would remove the situation from the ambit of the hypothetical ruling. By obtaining such consent, the lender would easily vitiate this attempt to protect the borrower from injury occurring as a result of an actual conflict. However, as a fortuitous consequence of such an informed consent the borrower would be able to protect himself from the possibility of such conflict. After the disclosure the borrower would be aware that he was unrepresented, and, therefore, presumably cognizant of the risk that he would be running in remaining so—the risk that the loan is in any manner unfavorable to him. Thus he would be able to make a knowledgeable choice as to whether to hire his own attorney,\textsuperscript{14} or to save the additional fee and assume the risk of an unfavorable loan. Since the duties of a second attorney would be only to check the abstract of title and approve the terms of the loan, his fee should be minimal. In sum, although a holding that the borrower is the client probably would not achieve its intended result of full protection for the borrower,\textsuperscript{15} it would bring about the more practical result of insuring—because of the full disclosure and consent—that the borrower is not misled into believing that he is represented.

Thus, it might seem that it would have been preferable to find the bor-

\textsuperscript{13} These alternatives include the burdensome remedy of withdrawal, see notes 7 & 10 supra, and the anomalous principle of permitting unequal representation of conflicting interests, see N.C. STATE BAR COUNCIL, OPINIONS, No. 395 (1962), reported, Melott II-95, discussed pp. 845-46 supra.

\textsuperscript{14} Under the current practice, the borrower clearly has a right to hire an additional attorney. See, e.g., ABA Comm. on Professional Ethics, Opinions, No. 837 (INFORMAL). However, since he is not made aware that he is unprotected, he is also unaware of the possibility that he may need such an attorney. Therefore, this right is meaningless because he has no reason to know that he may need to exercise it.

\textsuperscript{15} Such full protection probably could not be achieved without the economically wasteful expedient of requiring each party to retain an attorney.
rower to be the client in order to protect him from the possibility of mistaken reliance. Such a finding would be more attractive than the present situation. Yet there may be an alternative even more appealing than this proposal. Since the protection afforded therein would be only a proximately caused consequence of such a holding, and not an *ethically required* result, the Council would be resolving an ethical problem simply by sanctioning that choice of practices which would *tend* to produce an ethical result. Ideally, the Council should *require* an ethical result, not merely structure the situation so that such a result would rationally follow.

The additional alternative would be to continue to hold that the lender is the client but to *require* that this fact be made absolutely clear to the borrower. Some sort of knowledgeable consent must be required; the borrower must be made aware that he is not the client\(^\text{18}\) even though he is paying for the attorney and is receiving incidental benefits therefrom in the form of a title search. The present holdings not only leave the borrower unprotected, but also unaware that he is unprotected; yet the nature of present practices may well mislead him into the opposite belief. The proposed warnings would insure that every borrower be able to choose whether to assume the risk of an unfavorable loan. Probably many would choose to assume that risk rather than pay the additional fee, but this infrequency is no argument against disclosure, since the burden of that disclosure is only negligible.

Perhaps an even more desirable alternative would be to require not only that this initial disclosure be made, but also that the lender pass the attorney’s fees along to the buyer in the form of a built-in cost of the loan. Including the fee in the cost of the loan would render the borrower unaware that he is paying it, thus further removing the possibility that he will be mislead into believing that he is fully represented.

In conclusion, the Ethics Opinions of the Council of the North Carolina State Bar now leave the secured-loan borrower in a deceptively unprotected position. It is strongly urged that the Council adopt at least

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\(^{18}\) *In N.C. STATE BAR COUNCIL, OPINIONS, No. 709 (1970), reported, N.C. STATE BAR at 11,* the council held that an attorney employed by an insurance company to defend its insured could also represent the insured in his counterclaim. However, the attorney was required to make a full disclosure to the insured of the effect that an exercise of the insurance company’s right to settle the suit would have on the counterclaim. The council added that if it appeared that the insurance company might desire to settle, the attorney should not represent the insured in his counterclaim.

Though not strictly analogous because it deals with the litigation situation, the opinion does lend some support to a full disclosure argument in a non-litigious context.
one of the proposed alternatives—preferably the latter—to insure that no borrower be unfairly misled.

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Uniform Commercial Code—Protection for the Purchase Money Secured Party Under Section 9-312

The basic section of the Uniform Commercial Code dealing with the problem of priorities among conflicting security interests in the same collateral is section 9-312. Subsection (4) extends special protection to purchase money security interests in collateral other than inventory by giving such an interest priority over a conflicting security interest "if the purchase money security interest is perfected at the time the debtor receives possession of the collateral or within ten days thereafter." In the recent case of Brodie Hotel Supply, Inc. v. United States, the Court of Appeals for the Ninth Circuit has unduly extended the scope of this protection.

In 1959 Brodie sold some restaurant equipment to a company that later went bankrupt. Brodie repossessed the equipment but left it in the restaurant. On June 1, 1964, Lyon took possession of the restaurant and equipment and began operating the restaurant while negotiating the price and terms under which he would purchase the equipment from Brodie. On November 2, 1964, Lyon borrowed seventeen thousand dollars from the National Bank of Alaska and gave the bank as security a chattel mortgage on the equipment. The bank assigned the mortgage to the Small Business Association (SBA), and on November 4, 1964, filed a financing statement showing the SBA as assignee. On November 12, 1964, Brodie gave to Lyon a bill of sale for the equipment, and Lyon gave Brodie a chattel mortgage on the equipment to secure the unpaid purchase price. Brodie filed a financing statement on November 23, 1964. Thus the crucial dates in the case are the following: June 1, when Lyon took possession of the equipment; November 4, when the bank filed; November 12, when the debtor-creditor relationship was entered into by Brodie and Lyon; and November 23, when Brodie filed. Subsequently, the SBA sold the equipment to satisfy its mortgage, and Brodie sued to determine

\[ \text{431 F.2d 1316 (9th Cir. 1970). The court in this case applied the Alaska version of the Code. However, for ease of discussion, the general Code provisions, rather than the Alaska enumeration thereof, will be cited.} \]

\[ \text{All of the above facts are set forth in the opinion.} \]

\[ \text{Brief for Appellant at 2, Brodie Hotel Supply, Inc. v. United States, 431 F.2d 1316 (9th Cir. 1970).} \]