NORTH DAKOTA BANKERS ASSOCIATION

LEGAL UPDATE

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BANKING REGULATION

Claim for RESPA Violation Survives Summary Judgment [6TH CIR]

Cynthia Hurst (mortgagor) obtained a loan to finance her house from Caliber Home Loans (mortgagee). When the mortgagor had to file for a loan modification, the mortgagee required she fill out a loan-modification application. The mortgagor filled out her application, but upon receiving the submission the mortgagee sent a letter informing the mortgagor she was missing documents. Back-and-forth continued until the mortgagee informed the mortgagor the application was complete. However, the mortgagee realized it was missing more information and sent another letter to the mortgagor to supply the missing documents. The two parties communicated via letters and phone calls, but ultimately the mortgagor failed to supply the documents by the deadline. The mortgagor states the mortgagee provided misleading and conflicting information as to the necessary documents. Because the documents were not provided the mortgagee informed the mortgagor the loan modification was incomplete and could not be processed. The mortgagee eventually filed a foreclosure action. The mortgagor filed suit alleging violations of the Real Estate Settlement Procedures Act of 1974 of Regulation X. The mortgagor had three claims relevant on appeal. First, she claimed the mortgagee violated the "dual tracking" provision. Second, she claimed the mortgagee failed to exercise reasonable diligence. Third, she claimed the mortgagee failed to provide adequate notice of the information needed to complete its review. The district court granted summary judgment for the mortgagee on all claims.

In Hurst v. Caliber Home Loans, Inc., 44 F.4th 418 (6th Cir. 2022), the court examined three main issues. First, the court examined whether the mortgagee violated Regulation X's prohibition on "dual tracking". Dual tracking prevents a servicer from initiating a foreclosure while a complete loan-modification application is pending. Although the mortgagee informed the mortgagor the application was complete, it gave the mortgagor a reasonable deadline in compliance with Regulation X by informing the mortgagor it needed additional required documents. Because the mortgagee, upon expiration of the deadline, had informed the mortgagor the application was incomplete, the mortgagor was no longer protected under the dual-tracking prohibition. Secondly, the court looked at whether the mortgagee exercised reasonable diligence in obtaining documents and other information necessary to complete the mortgagor's loanmodification application. The "reasonable diligence" requirement may be violated if the mortgagee repeatedly requests documents it already possesses and also if the mortgagee does not promptly request the additional information or a corrected version of a previously submitted document. The mortgagor states it was provided with misleading and conflicting information about a tax return transcript and also that the mortgagee was not diligent in communicating about the alleged required bank statement submissions, and then the mortgagee was contradicting in stating it was not actually required. The court held that the district court did not consider whether there was a lack of reasonable diligence under regulation guidance, and only focused on whether the requested documents were already in the mortgagee's possession. The analysis was too narrow, and it was vacated and remanded for further proceedings. Finally, the circuit court examined whether the mortgagee communicated and provided adequate notice of the information needed, explaining that notice needs to be given to the mortgagor in writing. The court held that the notice requirement was met here because the mortgagee acknowledged receipt of the mortgagor's application and any additional information needed in writing. Accordingly, the district court's decision was affirmed in part and vacated in part. By Shelbi Stogdill sstogdil@ttu.edu

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BANKRUPTCY

Debtor's Proposed Chapter 11 Plan Impermissibly Modifies Secured Creditor's Rights and Therefore Case Dismissed [D NM]

The creditor filed a motion to convert or dismiss the Chapter 11 case. Granting of the motion would either convert the case from a chapter 11 case to a chapter 7 case, or dismiss the case, if the movant proved cause. The party requesting conversion or dismissal has the burden of establishing cause by a preponderance of the evidence. The creditor argued that under 11 U.S.C. § 1112(b) the case should either be converted or dismissed, alleging the debtor had acted in bad faith and failed to file an acceptable plan within a reasonable time after commencement of the chapter 11 case. In relation to the bad faith allegation, the evidence reflected that the debtor has filed for bankruptcy seven times in the past eleven years. Additionally, the creditor also contended that the debtor's chapter 11 plan violated the anti-modification prohibition in § 1123(b)(5). Under that provision, unless the affected creditor consents, a plan may not modify the rights of a holder of a claim secured only by the debtor's principal residence. Whether the anti-modification provision requires a chapter 11 debtor to pay all pre-confirmation arrearages on a claim secured only by the debtor's principal residence in full by the plan effective date or permits a cure of arrearages in installments after plan confirmation depends on whether the claim is deemed unimpaired under § 1124(2) if installment payments are to be made under the reorganization plan.

In In re Jacobs, 644 B.R. 883 (Bankr. D. N.M. October 14, 2022), the court, reading § 1123(6)(5) in conjunction with § 1124(2), held the former requires a chapter 11 debtor to pay all pre-confirmation arrearages on a claim secured only by the debtor's principal residence in full, and satisfy § 1124(2)'s other requirements to "unimpair" a claim by the reorganization plan's effective date. In order to avoid the dismissal or conversion upon a showing of cause, the debtor must in response, establish there is a reasonable likelihood that a plan will be confirmed within a reasonable period of time. The debtor can "unimpair" a creditor by "curing" any defaults and place the impaired creditor back into its original position. The "cure" under § 1124(2) must occur, in full and before or on the effective date to resolve the impairment. The court stated that the debtor's bankruptcy case in particular illustrates why the cure must occur before or on the effective date for the plan to not affect the antimodification requirement. Here, the debtor had made no payments during the time this case has been pending. The debtor's final proposed plan would be insufficient to even cover the interest the debtor owed the secured creditor. Accordingly, the court found cause under § 1112(6) to convert or dismiss the debtor's chapter 11 case. Moreover, the debtor was unable to show any "unusual circumstances" that would qualify as an exception to mandatory dismissal or conversion. During closing arguments, the secured lender requested dismissal of the case and the court agreed that a dismissal would be in the best interest of the parties. The court did not have to address the bad faith allegation because the creditor satisfied its burden in showing cause in the debtor's inability to effectuate a plan that did not modify the home mortgage. By Ty Koether tkoether@ttu.edu.

Debtor's Bankruptcy Plan Could Not be Confirmed When Secured Creditor Would Not Be Paid Default Interest [BKR EDPA]

Debtor, a closely held entity, owns leases, and manages residential real property in Lewisberry, PA. At the outset of this bankruptcy case, the Debtor owned thirty properties. The debtor defaulted on its payment obligation to the secured creditor. The parties conducted negotiations on two forbearance agreements but were unable to agree on an ongoing arrangement for future servicing of the loan, leading the debtor to seek relief under Chapter 11 bankruptcy. In seeking to reorganize, the debtor sought confirmation of a creative chapter 11 plan, which would supposedly cure the existing default on the creditor's loan and leave the creditor unimpaired. The debtor claimed that its proposed treatment of the creditor's claims satisfied the requirements of the Bankruptcy Code and therefore, the plan is confirmable. The creditor asserted that the debtor's reorganization plan was legally flawed because it did not propose to pay the secured creditor default interest as provided for in its contract.

In In re Lewisberry Partners, LLC, No. 21-10327 ELF, 2022 Bankr. LEXIS 1836 (Bankr. E.D. Pa. 2022), the court held that the creditor was entitled to default interest under 11 U.S.C. § 1123(d). The Bankruptcy Code does not create a federal bankruptcy right to modify a creditor's contractual right to collect default interest otherwise collectible under the creditor's loan contract. Moreover, the creditor was not estopped from asserting its claim for default interest on debtor's failure to meet its payment obligation as the debtor offered no evidence of reliance. Additionally, the debtor had presented no evidence supporting its assertion that it could fund payment of the amount necessary to cure the default.

Consequently, the court determined that the debtor lacked the funding necessary to effectuate its bankruptcy plan; thus, it could not be confirmed. The court sustained the creditor's objection to confirmation and denied the confirmation of the bankruptcy plan. By Elijah Benzvi elbenzvi@ttu.edu.

GENERAL BANKING

Bank Loses Summary Judgment Motion on a Duress Claim [AR APP]

Debtors, husband and wife, owned and operated trucking companies and entered into an agreement with the wife's father. The agreement stated that the father would purchase eight refrigerated trailers to lease back to the company. In October 2014, the parties entered into a loan agreement with lender, using the eight trailers and two previously owned trailers as collateral. Eventually, the debtors refinanced the 2014 loan and agreed with the father to relinquish ownership of the eight trailers. Using the eight trailers as collateral, the debtors obtained another loan, Loan 627. An assistant at the bank allegedly agreed to perform the necessary steps to transfer title from the father to the lenders and to perfect the bank's security interest in the eight trailers. In May 2016, the debtors entered into another loan agreement, using their house as collateral. At some point, the debtor's father repossessed the trailers, causing financial issues with the debtors' business. They contacted the bank and spoke to both the assistant and the president. During their conversation with the president, he allegedly threatened the debtors with criminal charges if they did not immediately offer their home as collateral. In response to this threat, the debtors entered into a new loan (Loan 925), agreement that would refinance Loan 627 and 739. The debtors defaulted on Loan 925 in March 2018, Loan 739 in May 2018, and Loan 126, which the bank later acquired, in July 2018. The bank filed a complaint for foreclosure. The debtors then crossclaimed, alleging negligence in failing to secure the title transfer and asserted duress as an affirmative defense. The bank contended that a duress defense could not be available for Loan 739 because no evidence existed to prove that the bank threatened the debtors to take their home in relation to Loan 729.

In Levitt v. Today's Bank, No. CV-21-464, 2022 Ark. App. LEXIS 359; 2022 WL 4361845 (Ark. Ct. App. Div. 4 Sep. 21, 2022) (opinion not yet released for publication), the court held that there existed genuine issues of material fact as to whether the debtors experienced duress when they took out their loans, relying on Cox v. McLaughlin, 315 Ark. 338, 867 S.W.2d 460 (1993). The court laid out the elements of duress as an affirmative defense to nullify an existing contract. Cox stated that a party must show: "(1) that he or she involuntarily accepted the terms of the opposing party; (2) that the circumstances permitted no other alternative; and (3) the circumstances resulted from coercive acts by the opposing party. Additionally, the duress must be shown to be as a result of the other party's wrongful and oppressive conduct rather than the debtor's own necessity. The bank's contention that the debtors did not experience duress in the initial loan was cut short by the debtor's report of threats by the bank to foreclose. Therefore, the court determined that a genuine issue of material fact existed as to whether the bank had engaged in duress in connection with the loan agreements. By Sabrina Urso sabrina.urso@ttu.edu.

LENDING

Fifth Circuit Holds CFPB Payday Lending Rule Unconstitutional [5th CIR]

In 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act created the Consumer Financial Protection Bureau (the "CFPB"). The legislation was designed to somewhat insulate the bureau from the political intervention by Congress in two ways. First, the Director of the CFPB could only be dismissed for cause. Second, the CFPB is an independent regulatory agency within the Federal Reserve System and receive its funding from the Federal Reserve Bank. Under the law, the Director of the CFPB can seek up to 12% of the annual funds the Federal Reserve Bank received. The Federal Reserve Bank, in turn gets its funds not from Congress but rather from money paid by the banks that are members of the Federal Reserve, as well as from money it makes on its investments and loans.

In 2020, the Supreme Court held that the limitation on removal of the Director of the CFPB was unconstitutional, distinguishing that position from situations in which it had previously held that such a limitation on removal was in fact constitutional. Seila Law, LLC v. Com. Fin. Prot. Bureau. 140 S. Ct. 2183, 207 L. Ed. 2d 494 (2020). Similarly, in Collins v. Yellin, 141 S. Ct. 1761, 210 L. Ed. 2d 432 (2021), the Supreme Court held that the limitation on removal of the head of the Federal Housing Finance Agency, which is headed by a single officer, was unconstitutional. However, in both cases, the Supreme Court declined to hold that as a result of the limitations on removal, the actions taken by the CFPB or the Federal Housing Finance Agency were invalid.

Perhaps encouraged by Seila Law and Collins, the appellants, sued, challenging the CFPB's Payday Lending Rule. Among other arguments, the appellants contended that the actions of the CFPB were unconstitutional because the bureau is improperly funded. The Appropriations Clause provides "[n]o money shall be drawn from the Treasury, but in Consequence of Appropriations made by Law, and a regular Statement and Account of the receipts and Expenditures of all public Money shall be published from time to time." U.S. Const. art. I, § 9, cl. 7. The district court held that the manner of the funding did not invalidate the payday lending rule, and the collection agency appealed to the Fifth Circuit Court of Appeals.

In Cmty. Fin. Servs. Ass'n of Am. v. Cons. Fin. Prot. Bureau, 5l F.4th 616 (5th Cir. 2022), the Fifth Circuit Court of Appeals followed in the footsteps of the Seila Law and Collins decisions and took a giant extra step: it help that the manner in which the CPB obtains its funding is unconstitutional because it violates the Appropriations Clause because the funds to rule the CFPB come not through annualCongressional Appropriations but rather from the Federal Reserve Bank. Unlike in the Seila Law and Collins, however, the Fifth Circuit Court of Appeals ruled that, because the funding of the CFPB violated the appropriations clause, its acts were invalid. It recognized that Seila and Collins required that the unconstitutional aspect of the funding had to "inflict harm." Here, the circuit court concluded that it did, concluding that "there is a linear nexus between the inform provision 9 the Bureau's funding mechanism) and the challenged action (promulgation of the rule).... [W]ithout its unconstitutional funding the Bureau lacked any other means to promulgate the rule." The CFPB has filed for certiorari before the Supreme Court. By the editors.

SECURITY INTERESTS

Bank's Security Interest Invalid Because Debtors Did Not Have Rights in the Collateral. [WD KY]

Debtors operated a farm for more than twenty years. During the operation, each of the two debtors individually acquired farm equipment for use in their unincorporated partnership. To finance their farming operation, the debtors took out several loans collectively and individually secured by the farm equipment. Later, the debtors encountered financial difficulty. There were multiple liens on each of the debtors' equipment, and some of the obligations secured by those liens were in default. Consequently, the debtors formed a new partnership to take out a loan from the bank, which the debtors used to pay off the other creditors. The debtors secured the bank's loan with the partnership's farm equipment. Eventually, the debtors filed Chapter 12 petitions for bankruptcy. That court held that the bank had only an unsecured interest because the debtors never transferred their individually owned farm equipment to the partnership. The bank appealed the order, challenging its unsecured status while conceding that its interest was junior to that of all other secured creditors.

In Peoples Bank of Marion v. Nutrien Ag Sols., Inc., No. 1:2 l-CV-149-BJB, 2022 WL 4588418, 2022 U.S. Dist. LEXIS 177310 (W.D. Ky. Sept. 29, 2022), this court held that the debtors' farm equipment was not property of the partnership because the debtors purchased it separately and did not document any transfer of title. Because the partnership did not own title to the equipment, it could not offer it as collateral to secure the bank's loan. First, the court examined whether the debtors transferred their farm equipment before or after the partnership took out the loan from the bank. Kentucky follows Article 9 of the Uniform Commercial Code. The UCC requires a lender seeking a security interest to attach the agreement to collateral and then perfect that interest by filing a financing statement with the Kentucky Secretary of State. Further, a security interest only attaches if the debtor has an interest in the pledged collateral. The bank put into evidence several agreements that qualified as security agreements in the farm equipment; but, if the debtors' partnership owned no such collateral, the security interest was not attached through those referenced agreements. Second, the court assessed whether the debtors intended to transfer the equipment to the partnership before taking out the loan. The weight of the evidence supported the conclusion that the debtors entered into several agreements with the bank listing the farm equipment as their separate, individual property. Therefore, the court concluded that the bank's claimed security interest failed to attach and affirmed the bankruptcy court's ruling. By Elijah Benzvi elbenzvi@ttu.edu.

Security Interest Perfected When Automatic Bankruptcy Stay in Effect is Null and Void [FLA APP]

The debtors lived in a home on 160 acres of land; the house and land were subject to a mortgage held by a local bank. The mortgage granted the local bank a security interest in the land and all after-acquired fixtures or permanent improvements. Unfortunately, the debtors defaulted on their mortgage, and the local bank began foreclosing on both the home and the land. Shortly after foreclosure proceedings began, the debtors purchased a doublewide mobile home. They permanently

installed it-so that the mobile home became a fixture subject to the mortgage's after acquired property clause---on the 160 acres subject to foreclosure. The debtors financed their new doublewide with the help of a national mortgage lender (the creditor), who took a security interest in the home but did not perfect the security interest. One month after purchasing the doublewide, the debtors filed for Chapter 7 bankruptcy. The creditor perfected its security interest shortly after the debtors filed for bankruptcy. On appeal, the issue was whether the creditor's security interest in the doublewide was superior to the after-acquired property clause in the mortgage that created a mortgage on the fixture, the doublewide mobile home.

In Echo River Sanctuary, LLC v. 21st Mortg. Corp., No. 1D21-1940, 2022 WL 4229367, 2022 Fla. App. LEXIS 6246 (Fla. App. Sept. 22, 2022) (opinion not yet released for publication), the court held that a mortgage's after-acquired property clause claiming an interest in a mobile home is superior to a creditor's unperfected security interest on the mobile home. The court explained that once a debtor files a bankruptcy petition, creditors can no longer "create, perfect, or enforce" any security interest against the property of the bankruptcy estate. Here, the creditor perfected their security interest after the bankruptcy case was filed, automatically creating the stay of creditor actions, rendering the perfection null and void. Had the creditors timely perfected their lien, their claim would have prevailed over the mortgage's after-acquired property clause, regardless of the mobile home's status as a fixture. By Joshua Shetler joshua.shetler@ttu.edu.

Tracy Kennedy
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Role of NDBA General Counsel

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