NORTH DAKOTA BANKERS ASSOCIATION

LEGAL UPDATE

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ARBITRATION

Arbitration Compelled After Joint Account Owner Willingly Signed Arbitration Agreement as a Guardian [11TH CIR]

The joint account owner co-owned an investment account with her mother. Because of medical reasons, the mother transferred the account to the Bank involved in this litigation. The mother told the Bank that the investment account funds belonged to the joint account owner, who would continue to co-own the new account. When she transferred the account, the mother signed an agreement containing an arbitration clause. The joint account owner received no notice of the transfer until years after, after her brother had misused funds in the account and had removed the joint account owner from the account. To address her mother's declining capacity and her brother's misuse of money in the account, the joint account owner then became the legal guardian of her mother and transferred the money into a new account at the same Bank. When she transferred the money, the joint account owner signed a new deposit agreement that contained an arbitration clause. The arbitration provided it covered "any subject matter, issue or circumstance whatsoever, including, but not limited to, controversies concerning any Account, order or transaction, or the continuation, performance, interpretation or breach of this or any other agreement." The clause also covered any agreements "whether entered into or arising before, on or after the date this Account is opened." The joint account owner filed a complaint against the bank for wrongdoing, and the bank filed a successful motion to compel arbitration. The joint account holder appealed.

In FISHER v. PNC BANK, No. 21-33266, F.4th, 2022 WL 2037699, 2022 U.S. App. LEXIS 15591 (11th Cir. June 7, 2022) (opinion not yet released for publication), the joint account holder contended that the arbitration clause should not apply to her dispute with the bank. The joint account holder claimed she had signed the arbitration agreement as her mother's guardian and therefore the agreement did not apply to her personally. Additionally, she claimed that her claims against the bank for wrongdoing did not arise out of the agreement with the bank and therefore, the arbitration clause did not apply to those claims. The joint account holder never alleged, however, that her signature on the agreement was fraudulent. The court reasoned that the arbitration agreement applied because it involved "all controversies that may arise between you, us, and [the broker]." Therefore, the language demonstrated that the agreement applied to the joint account holder, despite her having signed the agreement as a guardian. Additionally, the court stated that the claims were covered by the agreement because the joint account holder sought to hold the bank accountable for alleged violations of the same agreement. The court determined that the joint account holder could not use the agreement when convenient and then try to dispute the arbitration provision at the same time. Accordingly, the court affirmed the decision of the lower court that the arbitration agreement applied to the dispute with the bank. By Avery Bertagna abertagn@ttu.edu..

BANKRUPTCY

Chapter 11 Debtor Cannot Modify Home Mortgage [B.A.P. 9th Cir.]

The debtor filed a Chapter 11 case and owed money on a home mortgage. She confirmed a reorganization plan that provided the payments on her home mortgage would be stretched out. The bank that held her mortgage appealed.

In MECHS. BANK v. GEWALT (IN RE GEWALT), BAP No. EC-21-1172-TBG, Bk. No 2:21-bk-20600-CMK, 2022 Bankr. LEXIS 284, 2022 WL 305271 (B.A.P. 9th Cir. Feb. 2, 2022), the court reversed the decision confirming the reorganization plan. First, the court dismissed the argument that the plan was equitably moot: the eggs could be unscrambled. The key factor in the court's decision, however, was that the Bankruptcy Code specifically provides that Chapter 11 individual debtors cannot modify a home mortgage. For that reason, the confirmation order confirming the plan that modified the home mortgage could not be confirmed. By the editors.

Debtor's Abandoning Collateral Did Not Make Debt Nondischargeable [BKR W.D. Tenn.]

The defendant purchased a car for approximately $13,000 and entered into an installment sales contract. The contract was assigned to the plaintiff as the lender. The defendant made some payments on the car but defaulted on the car payments and ultimately filed a Chapter 7 bankruptcy case. When the plaintiff learned of the bankruptcy case, the parties agreed to a reaffirmation of the debt remaining on the car loan. Subsequently, the defendant abandoned the car at a car dealership and purchased a new car. The plaintiff repossessed the car from the dealership and filed an adversary proceeding complaint against the defendant. The plaintiff discovered that the repossessed car was inoperable and sold the car for approximately $4,000. The defendant was served with a copy of the complaint, but the defendant never responded to the complaint. The plaintiff moved for a default judgment. Plaintiff alleged in the complaint that the deficiency balance on the defendant's car loan and the costs incurred in recovering the car was a non-dischargeable debt pursuant to 11 U.S.C. § 523(a)(4) and (a)(6).

In PACE FIN., LLC V. HERRING (IN RE HERRING), No. 20-20967, Adv, Proc. No. 20-00094, 2022 Bankr. LEXIS 1709 (Bankr. W.D. Tenn. June 14, 2022), the bankruptcy court denied the plaintiffs motion for default judgment and request for attorney's fees and held that the plaintiff failed to plausibly allege that the defendant's debt was non-dischargeable under 11 U.S.C.S. § 523(a)(4) and failed to allege an injury sufficient to warrant an exception from discharge under § 523(a)(6). The court noted that a defendant's failure respond to a complaint did not entitle the plaintiff to a default judgment as a matter of right and not all injuries are legally compensable. The court reasoned that in order to come within the discharge exception of Bankruptcy Code section 523(a)(4), the debt must have arisen from "fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny." Also, the scope of this section is solely limited to trustees who misappropriate funds held in trust, and not to those who fail to meet an obligation under a common law fiduciary relationship. The plaintiff argued that the defendant's abandonment of the car at the dealership, without notifying the plaintiff, was a breach of the defendant's fiduciary duty that resulted in the plaintiff's financial harm. However, the court reasoned that the plaintiff failed to plead facts sufficiently plausible to establish the existence of a fiduciary relationship or a trust pursuant to § 523(a)(4). On the other hand, Bankruptcy Code § 523(a)(6) excepts from discharge debts incurred for willful and malicious injury by the debtor to another entity or to the property of another entity. The plaintiff argued that the defendant had committed willful and malicious acts that resulted in a financial loss for the plaintiff and caused the plaintiff to forego its opportunity to repossess the car when it had a greater value. The court rejected this argument and reasoned that the costs incurred by the plaintiff for repossession and sale of the car were contractual fees anticipated by the parties and were not a result of the defendant's actions in abandoning the car at the dealership. The court noted that many cars remain on car lots for months without any apparent loss in value. If the debtor had surrendered the car instead of leaving it at a car dealership, the same result would have been reached. Thus, the court concluded that the plaintiff did not plausibly allege a compensable injury under § 523(a)(6). In addition, the court denied the plaintiff's request for attorney's fees and that it held an unsecured claim in the defendant's Chapter 7 bankruptcy case and are not excepted from discharge. By Love Osemwegie love.osemwegie@ttu.edu.

CONTRACT LAW

*If The Bank Throws a Rope of Opportunity, You Better Not Delay in Reaching for It [TX]

A South Carolina Bank (the Bank) was awarded a judgment against the debtor who was to repay the Bank a debt exceeding $4 million plus interest. Although the debtor attempted to settle the debt, the debtor's offers were exceedingly low. However, in an email to the debtor, the Bank's senior vice president offered to settle the debt for a payment of $2 million. The debtor did not immediately reply and accept this offer, and after a few days of no response from the debtor, the Bank reached out to another of the debtor's creditors. The Bank and the creditor negotiated an agreement whereby the creditor would take control of the Bank's judgment against the debtor and be responsible for its collection. A lawyer for the creditor emailed the debtor's counsel, informing him of his client's intent to seek the total amount owed. Upon hearing this, the debtor emailed the Bank's senior vice president, telling him of the debtor's acceptance of the farmer's offer of $2 million. The Bank responded that it no longer had the authority to settle the matter. Eventually, the creditor sued the debtor seeking the amount owed. The debtor claimed that the initial offer from the Bank was still valid when he emailed his acceptance, forming a valid contract. In contrast, the creditor claimed that under the "implied-revocation doctrine", the debtor had been made aware of the Bank's actions that were inconsistent with its previous offer, thereby terminating the Bank's $2 million offer before the debtor's acceptance.

In ANGEL v. TAUCH, 642 S.W.3d 481 (Tex. 2021), the court overturned the lower court's ruling, ruling in favor of the creditor. The court heavily relied on its previous decision in Antwine v. Reed, 145 Tex. 521, 199 S.W.2d 482,485 (Tex. 1947), which established the implied revocation doctrine. That doctrine states that an offeree's knowledge that the offeror has undertaken "some act inconsistent" with an outstanding offer is sufficient to revoke the offer and "prevent an acceptance from changing into a binding contract." The debtor argued that Antwine should not apply because that ruling dealt with real property, and the knowledge of the inconsistency came directly from the offerer. While true, the court reasoned that the implied revocation doctrine is not bound by the specific circumstances of Antwine and has broader application. The court stated revocation by inconsistent action is firmly rooted in contract law without limitation to any specific contractual context. The doctrine's touchstone is inconsistency, and that standard was met here. The Bank's action in assigning the judgment to the creditor for collection is "some act inconsistent" with the initial offer. Additionally, according to sections 42 and 43 of the Restatement of Contracts, the Bank's actions were definite actions inconsistent with entering the proposed settlement transaction. The court determined that no revocation can be effective unless the offeree knows of it, but the knowledge need only come from a "reliable" source. The court found that the creditor's letter was a sufficiently reliable source from which the Bank's inconsistent actions were made aware to the debtor. Thus, the debtor was made aware of the Bank's actions to no longer follow through on the $2 million settlement, and the settlement offer was thereby implicitly revoked. By Riley Caraway rcaraway@ttu.edu.

Whether there has been a Mutual Departure from the Terms of a Contract is a Question for the Factfinder [GA App]

Plaintiff was indebted to defendant bank (the Bank) under three promissory notes. Shortly after, the plaintiff was in default on two of the promissory notes. Defendant then sent a letter to plaintiff informing him that the Bank was accelerating the loan and the loan was now immediately due. The Bank then initiated a non-judicial foreclosure process on the plaintiff. Before the foreclosure sale, the parties signed a forbearance agreement providing that defendant would forbear from collecting under the note if the plaintiff made four payments. Plaintiff made one of the payments but made partial or no payments on the other three payments that were due. Plaintiff then met with the defendant and presented a deed to his home in lieu of foreclosure. Plaintiff claimed that he presented the deed so that defendants could give him more time to pay but that agreement was not in writing. The Bank then sent a letter informing plaintiff of his default and that it was going to record the deed on his house and take possession of it in five days. Plaintiff swore he never received the letter before the due date. The Bank recorded the letter, leading to this suit by plaintiff for breach of contract, promissory estoppel, to set aside the deed in lieu of foreclosure and conversion or trover of real property. The trial court granted summary judgement for the on Bank on all the claims and the plaintiff appealed.

In UNDERWOOD v. COLONY BANK, 869 S.E.2d 535 (Feb. 2022), the appellate court affirmed the trial court's summary judgement decision on the claims of promissory estoppel, to set aside the deed, and for conversion and trover but reversed and remanded the claim of breach of contract. The court reasoned that the arguments made by appellant that both parties thought their conduct modified the forbearance agreement was a material issue of fact. To respond to the appellee's arguments that the forbearance agreement is unenforceable because there was no consideration, the court held that there was consideration because the appellant agreed to make four payments of $25,000 to have the forbearance agreement and this was enough consideration for the contractual agreement. The court also considered the arguments made by appellant that the other party, by accepting late payments, created an issue of fact as to whether the parties deviated mutually from the forbearance agreement. The court held that if the factfinder determines that that the forbearance agreement was modified through subsequent conduct by the parties, then an issue of whether sufficient notice was given also arises. For these reasons, the court held that the grant of summary judgment was erroneous because the claims needed to be left for the jury to determine. The court thus reversed and remanded the grant of summary judgment on the claim of breach of contract but affirmed the decision of the lower court on all other claims. By Samuel Ghirmay Samuel.ghirmay@ttu.edu.

GENERAL BANKING

Because Landman's Mistake Was Mistake of Fact, Bank Liable for a Faulty Lease Extension [5TH CIR]

Three landowners owned an interest in a large farm that sat upon one of the largest natural gas fields in the country. Two related landowners (sisters) each owned a 2/6 share in the property, while the third landowner owned a 1/6 share. The sisters entered into agency agreements with the bank to manage their mineral interests. Those agreements contained a provision excusing the bank from liability in case of a "mistake in judgment." The third landowner did not sign the mineral interest management agreement. The bank's landman renegotiated a mineral lease with a third party on behalf of the landowners. Instead of entering into a lease that covered l/ l0 of the property, as was the goal, the landman extended the lease to the entire property. The third landowner also signed the mistaken lease extension. Months later, new drilling technology increased the lease values significantly, leading the landowners apparently to lose out on significant profits from their mineral interests. The three landowners sued the bank for damages arising from the landman's faulty lease extension.

In FRANKLIN v. REGIONS BANK, F.4th, No. 21-30324, 2022 WL 2128644, 2022 U.S. App. LEXIS 16402 (5th Cir. June 14th, 2022) (opinion not yet released for publication), the court upheld the decision finding that the third landowner had no agreement with the bank to manage her mineral interests; therefore, the landman did not represent this portion of the property and could not be liable to her for damages. The sisters argued that the bank was liable for the actions of the landman because the error was not a "mistake in judgment." The court reviewed legal definitions of "mistake" and "judgment" in determining whether the error could be considered a mistake in judgment. The court found that the landman made a mistake; however, there was no mistake in discretion, as the word "judgment" implies. Instead, the landman misread the lease extension and made a mistake that could have been avoided by exercising minimal care. Therefore, the court held that the bank should be liable and remanded the case for a determination of damages for the sisters. By Avery Bertagna abertagn@ttu.edu,

SECURED TRANSACTIONS

Future Advance Clauses Extend To Future Debts Despite State's Reluctance To Enforce Such Clauses [8th Cir.]

A couple purchased a condominium intending to make it their primary resident. The husband executed a consumer loan note (the "Original Note") to the Bank. The wife consented to the execution of the Original Note, but she was not a signatory. On the same day the couple executed the Original Note, they jointly granted Bank a mortgage on the condo to secure the Original Note (the "Mortgage"). Both husband and wife initialed the pages of the Mortgage and signed the final page. The Mortgage contained a future advance clause or "dragnet clause," granting the Bank a security interest in the Mortgage covering future funds that the husband might borrow, and a waiver of the couple's homestead exemption. The husband-without his wife-later borrowed money from Bank to keep his business running (the "Business Notes"). A few months later the husband filed for Chapter 7 bankruptcy, but the wife did not, and the condominium was sold. The husband and wife also initiated divorce proceedings around this time. The proceeds from the sale were deposited into escrow and the husband argued that his half of the sale proceeds were exempt from paying down the Business Notes. The bankruptcy court held that the husband's portion of the proceeds must pay down the Business Notes under the Mortgage's terms and that he could not claim a homestead exemption for those proceeds. Additionally, the Bank commenced an action against the wife in federal court, seeking her portion of the escrowed sale proceeds under the terms of the Mortgage's future advance clause. The Bank successfully moved for summary judgment and the wife appealed from that judgment.

In Sanborn Sav. Bank v. Freed, No. 21-2816, 2022 U.S. App. LEXIS 17400 (8th Cir. Mar. 15, 2022), the United States Court of Appeals for the Eighth Circuit held the dragnet clause was valid. In Iowa, a dragnet clause in a mortgage does not extend to cover future advances unless they are of the same kind or relate to the same transaction. The wife argued that the Business Notes were not of the same character as the Original Note. The mortgage between Bank and the couple provided it covered all debts from the husband to the Bank whether or not the mortgage is mentioned, or even if the debt were unrelated to the original obligation. Additionally, the court noted that the clause's broad scope and its presence on the second page of the Mortgage, in bold print under the header "SECURED DEBTS AND FUTURE ADVANCES," were important factors for its decision. In the alternative, the wife argued that the future advance clause made the Mortgage a contract of adhesion under state law. However, she could not prove that no person in his or her right sense would make the deal. The remainder of the wife's claims were dismissed as frivolous and/ or without merit and the court upheld the judgment below. By Miguel Escobar; Miguesco@ttu.edu.

Secured Creditor That Let Financing Statement Lapse Was No Longer Perfected [Bankr. D.S.C.]

The Creditor filed a motion for relief from the automatic stay to foreclose on the debtor's property. The Creditor possessed a stock certificate that indicated that he owned some shares in a corporation. The Debtor purchased the Creditor's shares of stock for $220,000 pursuant to a Stock Purchase Agreement. In exchange for the stock, the Debtor executed a promissory note for $220,000 to pay for the shares of stock in periodic installments. The documents granted the Creditor a security interest in the Debtor's stock. The note also provided that the Creditor and Debtor would file a financing statement with the secretary of state, and the Debtor would deliver stock certificates to the Creditor to keep in his possession until the note was paid in full. The Debtor, however, never delivered a stock certificate to the Creditor. However, a financing statement has been filed with the secretary of state describing the Creditor's collateral as all stock of the corporation owned by the Debtor. Debtor filed for chapter 7 bankruptcy and disclosed a 30% ownership interest in the corporation. At the time of the bankruptcy, the Debtor owed an unpaid balance of $130,000 on the note. The Creditor claimed that his security interest was perfected by his possession of a stock certificate representing the Debtor's shares in the corporation. The Creditor also claimed that the number of shares of stock sold to the Debtor represented 30% of ownership in the corporation. The Creditor further claimed that he had a security interest in the Debtor's shares generally, not just those represented by the stock certificates. The Creditor moved to lift the automatic stay in order to foreclose on the sock, but the Chapter 7 trustee of the Debtor's bankruptcy estate objected to the automatic stay relief, arguing that the Creditor did not have a perfected security interest in any collateral to secure payment of the Debtor's note.

In IN RE FLINT, CIA No. 21-00702- HB, 2022 LEXIS 1433 (Bankr. D.S.C. May 5, 2022), the bankruptcy court denied the Creditor's motion for relief from the automatic stay and held that the Creditor had not met his burden to show that the automatic stay relief was warranted. The court reasoned that the stock certificate the Creditor claimed was in his possession was never issued or delivered by the Debtor. Therefore, the Creditor's interest in the Debtor's shares did not attach by possession. The court also reasoned that while a financing agreement had been filed covering all the stock of shares owned by the Debtor in the corporation, it had expired in 2020. Therefore, any prior perfection of the security interest was no longer effective. Thus, the court held that the Creditor's claim was unsecured and any shares of the Debtor in the corporation were the property of the estate. By Love Osemwegie love.osemwegie@ttu.edu.

Bank's Security Interest and Right of Set Off Primes Garnishment [N.C. App. 2021]

A creditor of the debtor sought to garnish the debtor's bank account. The bank refused to tum over the funds, arguing that it had a prior right of setoff and security interest. The trial court disagreed and the bank appealed.

In Guy M. Turner Inc. v. KLO Acquisition, LLC, 869 S.E.2d 755 (N.C. App. 2021), the court on appeal held that the bank's right of set off and security interest primed the garnishee. The bank did not have to have exercised its right of set off to have priority. The statute on point, N.C. Gen. Stat. § 1-440.28 specifically protected the Bank as garnishee. By the editors.

SECURITIES LAW

Bank's Annual Report Statements Sufficient in Securities Fraud Action to Survive Past Pleading [SD NY]

Securities law requires a bank to maintain anti-money laundering (AML) and know-your-customer (KYC) systems both to protect the bank's reputation and to prevent bank involvement in money laundering schemes. The bank had allegedly failed to maintain effective AML and KYC practices by continuing relationships with high-risk clients despite the advice of its risk management staff. All these high-risk clients fell under the bank's wealth management business which caters only to the ultra-rich. The bank's compliance staff flagged many of these clients as high-risk because they were politically exposed persons (PEPs) or had connections to illicit enterprises. The public learned of the bank's relationships with these individuals, and the bank's stock decreased in value, harming investors. The investors sued both the· bank itself and the bank's chief executive officers (CEOs) and chief financial officers (CFOs) as control persons in a putative securities fraud class action. They claimed the bank had misled them with fraudulent statements in annual reports regarding the integrity of the AML and KYC programs. The investors relied on disclosures made by confidential witnesses (CWs) who worked in the bank's AWL and KYC programs to challenge the validity of the bank's statements in the annual reports. The bank moved to dismiss the complaint for failing to satisfy pleading standards.

In KARIMI v. DEUTSCHE BANK AG, F.3d, 22-cv-2854 (JSR), 2022 WL 2114628, 2022 U.S. Dist. LEXIS 105369 (S.D.N.Y. June 13, 2022) (opinion not yet released for publication), the court refused to grant the bank's motion to dismiss on all but one ground. The bank advanced four arguments in support of its motion. First, the bank argued the challenged statements in the annual reports were aspirational or "puffery" that were optimistic forecasts at best and "not actionable statements of falsifiable fact." The court disagreed concluding a reasonable investor could have interpreted the statements as factual. Even if conclusory and unverifiable, the bank made statements that a reasonable investor could have understood to rely on an accurate factual basis. Second, the bank raised the "truth-on-the-market" defense to argue investors already knew of the bank's AML and KYC deficiencies and therefore could not have been misled by the bank's statements to the contrary. The court concluded the pleadings stage was an inappropriate time to raise the defense due to its highly fact-specific inquiry. Moreover, the bank's generalized statements in public disclosures regarding the need to improve AML and KYC failed to address the specificity of the investor's claims. Third, the bank contended the investors had asserted mismanagement claims and not misstatement claims. If the court agreed, it would have to dismiss the complaint because mismanagement is not actionable under securities law. However, the court analyzed the statements and concluded the pleadings satisfied the standard by identifying how the bank had misrepresented its mismanagement of AML and KYC. Finally, the bank argued the investors had inadequately plead the scienter requirement regarding the CEOs and CFOs who were being sued as control persons. The court relied on circumstantial evidence raised through the CW disclosures to conclude the scienter requirement had been satisfied with respect to the CEOs but not with respect to the CFOs. Thus, the court dismissed the claims against the CFOs and allowed the litigation to otherwise proceed. By Peter Benson; pebenson@ttu.edu.

TAXATION

When You Make a Plan You Better Stick to It, Or It Will End Like This [9TH CIR]

A debtor filed for bankruptcy after defaulting on several mortgage loans for her rental properties. The Bank of NYM (the Bank) asserted secured claims based on the deeds of trust that the debtor signed. To deal with these claims, the debtor proposed a Chapter 11 plan (Plan) that would allow her to continue using the properties until adversary proceedings against the Bank's claims concluded. After losing their adversary proceedings, the debtor did not make payments to the Bank as was required under the Plan. To explain why she had not made the payments to the Bank, the debtor claimed she had received a 1099-C from the IRS, and this document indicated a substantial amount of debt was written off by a third party. Nevertheless, the Bank did not adjust its demand for this reduction. Several months passed with the debtor refusing to make payments in light of having received the I099-C, so the Bank filed a motion to convert the case to a Chapter 7. The motion was granted with the bankruptcy court finding the debtor had materially defaulted on her obligations under the Plan. For that reason, the court converted her Chapter 11 case to a Chapter 7 case. Additionally, the bankruptcy court ordered the debtor's assets which were the rent and sale proceeds of rental property, to be turned over to the Chapter 7 bankruptcy trustee. The debtor appealed both rulings.

In BARONI v. SEROR (IN RE BARONI), 36 F.4th 958 (9th Cir. 2022), the court affirmed the bankruptcy court's orders converting the debtor's bankruptcy case from Chapter 11 to Chapter 7 and ordering the debtor to tum over undistributed assets in her possession to the Chapter 7 bankruptcy estate. The court found that the conversion to Chapter 7 was proper because under 11 U.S.C. § 1112(b)(l), the moving party (the Bank) must establish that cause exists for the conversion. Here the court found that the debtor's failure to make the required payments to the Bank, as provided for in the Plan, constituted a material default, making conversion proper. The court further ruled that even if the debtor had made payments for an extended period before the default or taken other significant steps to perform under the Plan, the amount and duration of the default were so significant that there were no grounds for reversal. Regarding the second issue, under 11 U.S.C. § 1141, a Chapter 11 plan vests the bankruptcy estate's property in the debtor. However, with the conversion to Chapter 7 the court determined that unless there is an explicit plan provision regarding the distribution of assets to creditors, the assets should revest in the bankruptcy estate. The court reasoned that the assets were originally part of the Plan to repay the Bank, and to find that the assets did not revest upon conversion would go against the very intent of the Plan and run counter to it. By Riley Caraway rcaraway@ttu.edu.

IRS Form 1099-C Does Not Require Actual Discharge of Debt [3R.D CIR]

The bank obtained a substantial judgment against the debtors that the debtors failed to pay. As a result., the bank issued an IRS Form 1099-C indicating the amount of the debt discharged. The IRS obligates the bank to issue a 1099-C any time an "identifiable event" occurs, regardless of whether there is an actual discharge of indebtedness. The debtors attempted to settle the judgment, and the bank filed the l099-C to report the unpaid debt as being the debtors' income. The debtors brought this claim, alleging violation of state consumer protection laws and arguing that the form should not have been filed unless the bank truly intended to cancel the debt. The debtors believed that the 1099-C meant they no longer owed any amount to the bank. The debtors contended that the bank should rescind the 1099-C if the debt had not been canceled and that the bank's actions were unlawful.

In GERICKE v. TRUIST, No. 21- 1776, 2022 WL 2128561, 2022 U.S. App. LEXlS 1632, (3rd Cir. May 5, 2022) (opinion not released for publication), the court evaluated the requirements for the discharge of indebtedness form, which requires an identifiable event. An actual discharge of the debt is not required for the identifiable event and therefore is not required to require an entity to file a 1099-C. The court emphasized that merely filing a 1099-C does not extinguish the debtor from the debt. This is in the plain language of the IRS regulation. Finally, the court evaluated the 2016 amendments to the regulations, which discuss a 36-month rule to extinguish debt following the issuance of a 1099-C. The court stated that the IRS still does not require cancellation or discharge of debt; therefore, the amendments do not apply. Accordingly, the court ultimately upheld the dismissal of the debtors' claims. By Avery Bertagna abertagn@ttu.edu.

Tracy Kennedy
NDBA General Counsel

Role of NDBA General Counsel

NDBA's general counsel serves as the attorney for the association. Although Tracy is pleased to be able to serve as a resource for NDBA members in responding to their questions, she is providing general information, not legal advice. Banks must obtain legal advice from counsel who has been retained by the bank to represent the bank's interests in a specific matter.

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