NORTH DAKOTA BANKERS ASSOCIATION

LEGAL UPDATE

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EMPLOYMENT LAW

Beware of Firing Employees During a FMLA Leave *[5TH CIR]

An employer terminated the plaintiff (employee) while he was on leave under the Family and Medical Leave Act (FMLA) and the employee filed suit. The employee suffered from epilepsy and glaucoma. In addition, his wife was seriously ill, suffering from advanced stage cancer. The employer was aware of employee's medical conditions because he had been an employee for many years. The employee received the first poor performance review of his career just months before his termination, and shortly after was given a "final warning" by his superior. This led to a substantial conflict, which resulted in the employee being escorted from the workplace. The human resources department instructed the employee to apply for disability coverage and family medical leave. The employee was on FMLA granted leave when he was notified that his job was terminated. The employer cited his previous poor performance review as the reason for the employee's termination. The employee alleged the employer violated the FMLA by discriminatory termination, and (2) interference with his right of reinstatement. The federal district court granted the employer's Rule 12(b)(6) motion to dismiss the complaint, and the employee appealed.

In HESTER v. BELL-TEXTRON INC., 11 F.4th 301 (5th Cir. 2021), the court held that the district court had erred in granting the employer's 12(b)(6) motion to dismiss because the employee had alleged a prima facie discrimination claim. To allege an FMLA discrimination claim, an employee must establish "temporal proximity" between the FMLA leave and the termination of his employment. The employee does not have to establish that the protected activity was the only cause of his termination, but rather only that the leave and the termination were not "completely unrelated." The employee's pleading established "temporal proximity," by showing that his termination occurred during his FMLA leave. The court ultimately held that granting the l 2(b)(6) motion had been erroneous. Discussing the employee's reinstatement interference claim, the court concluded that the FMLA does not impose a strict liability standard requiring employers to reinstate employees following their FMLA leave. Denying reinstatement is appropriate when an employee's right to restored employment is extinguished for legitimate reasons unrelated to his efforts to secure FMLA. An employee must allege the employer denied a benefit to which the employee was entitled under the FMLA, and here the employee had done so: the employee had alleged he was terminated solely because of his FMLA leave. Additionally, the court reasoned that the fact that the termination occurred during the employee's FMLA leave was relevant. Because the employer had instructed the employee to apply for FMLA, this indicated that before the employee's leave, his right to restored employment was still intact. Thus, the district court had erred in dismissing the employee's reinstatement interference claim, and the Fifth Circuit Court of Appeals reversed and remanded the case. By Riley Caraway rcaraway@ttu.edu

Court Dismisses ADA Claims Against Employer [5TH CIR]

An employee filed two separate charges with the Equal Employment Opportunity Commission (EEOC) against her employer after she sustained injuries during a mandatory work training. A doctor cleared the employee to return to work with the restrictions that she should not use stairs or walk excessively. When the employee attempted to return to training, the employee was unable to attend because the facility lacked an elevator. The employee also alleged that she had been denied the request to continue the required training on a lower level. The employee completed training on a later date, after the medical restrictions had been lifted. The employee filed a first charge of discrimination with the EEOC against the employer for failure to reasonably accommodate her disability. About a month later, the employer fired the employee for absences and tardiness without notification. In response to the termination, the employee filed a second charge of discrimination with the EEOC. This time, the employee alleged that she was fired due to discrimination based on race and disability along with retaliation for bringing the first charge she had asserted. The employee was issued a right-to-sue letter on both charges. She then proceeded in court under the Americans with Disabilities Act, and also alleged racial discrimination and a hostile work environment. The district court dismissed her complaint.

In JENNINGS v. WATSON, 11 F.4th 335 (5th Cir. 2021), the court affirmed the judgment of the district court, which had granted the employer's motion for summary judgment. The court reasoned that to file a suit in federal court under the ADA, all administrative remedies before the EEOC must have been exhausted. The court found that the employee exhausted the remedies regarding the first claims for failed accommodations and disability discrimination. However, the court found that the employee had failed to exhaust her remedies with respect to the second claims alleging a hostile work environment and racial discrimination. Even though the former employee had exhausted her administrative remedies regarding her disability, she could not prevail on her ADA claim. To show that an employer has failed to accommodate an employee's disability, three things must be shown: (1) the employee has a disability (2) the employer knew of the disability, and (3) the employer failed to reasonably accommodate the disability. Here, the court concluded that the employee did not state a claim that the employer had failed to reasonable accommodate her disability because the employer had offered the employee time off and later training. Moreover, the employer's failure to provide training on a lower level did not necessarily indicate that it had failed to reasonably provide accommodations for her disability. The court distinguished between what reasonable accommodations entails and what the employee had argued should be a reasonable accommodation. Also, the court determined that the employee did not have a disability at the time she was terminated. Overall, the court granted the employer's motion for summary judgment. By Avery Bertagna abertagn@ttu.edu

An Employer's Changing Explanations for an Adverse Employment Action Can Provide Evidence of Pretext for Discriminatory Animus [1ST CIR]

An employee of a medical equipment company was sent to a medical clinic to secure a signature on a certificate for a patient that the company still serviced. The employee had also been asked to attempt to repair the deteriorated relationship with the clinic. When the employee entered the clinic, the staff advised him that the clinic no longer used the company's services. When the employee explained that the company was still servicing one of the clinic's patients and needed a signature for insurance purposes, the owner of the clinic reiterated that it was not using the company's services anymore. At this point, the employee asked if he could meet with the physician. In response to this request, the clinic owner confronted the employee face to face and yelled at him to leave. After leaving the clinic and informing his supervisor what had occurred, the employee decided to call the clinic owner in another attempt to repair the relationship, but the owner became upset and hung up. After this interaction, the clinic owner complained to the company supervisor and allegedly gave a racial description of the employee. Initially, the company supervisor was unaware of the repeated phone calls and refrained from firing the employee. However, the employee was eventually fired after the clinic owner threatened legal and media action against the company. After this termination, the employee filed suit against his former employer for racial discrimination and retaliation under 42 U.S.C. § 1981 and the Maine Human Rights Act (MHRA). The company moved for summary judgment. The employee opposed the motion and submitted several documents produced during the discovery stage. However, the court granted the company's request to strike some of these documents from the summary judgement record as inadmissible unauthenticated evidence. Next, the district court analyzed the employee's racial discrimination claims under § 1981 and held that the employee failed to provide any admissible evidence showing that the company's reason for termination was based on race.

In JOSEPH v. LINCARE, INC., 989 F.3D 147 (1st Cir. 2021), the appeals court reversed and remanded the district court's ruling granting summary judgment for the company. First the court considered whether the documents excluded by the district court were authentic. Under Fed. R. Evid. 90l(b)," [a] document can be authenticated by a witness who wrote it, signed it, used it, or saw others do so." During a deposition, the authenticity of one document was established by one of the company's supervisors. The remaining documents acquired during discovery contained company logos, letterhead, and handwritten notes relating to the incident.

Because the company did not suggest the documents were not authentic and the company produced the documents during discovery, the court ruled that the documents were authentic and should not have been excluded from the record. Next, the court analyzed the burden-shifting test for opposing summary judgment. The employee was found to have met the initial burden of being in a protected class and of having faced an adverse employment action. After the company then met its burden of articulating a legitimate reason for employment termination, the burden shifted back to the employee to produce evidence that created a genuine issue of fact regarding a discriminatory motive behind his termination. The court accepted the employee's argument that the company's changing explanations for the adverse employment action could provide evidence of discriminatory animus. In short, the court found that the termination could possibly not be based on the proffered non-discriminatory reasons and that there was a genuine issue for the trier of fact. By Kyle Jones, jon60507@ttu.edu

FRAUDULENT TRANSFERS

*Even Though Debtor Did Not Receive Reasonably Equivalent Value, Transfer Could Not Be Avoided [BANKR ND TX]

An entity was a veneer manufacturer that was put up for sale in early 2014 and was acquired by the within a few months thereafter. Following a series of economic woes over the next two years, the debtor found itself in an economic bind and sought relief under the Chapter 11 of the Bankruptcy Code. Some creditors brought fraudulent transfer complaints against another creditor.

Debtor's Chapter 11 cases were converted to Chapter 7 and the trustee that was appointed amended the complaint to include additional defendants. The trustee asserted that a particular creditor-defendant had violated the fraudulent transfer laws of Texas because it had received a transfer from the debtor without giving reasonably equivalent value in exchange at a time when the debtor was insolvent, undercapitalized, or unable to pay its debts when they became due. The trustee also sought to avoid the transfer under § 548(a)(l) of the Bankruptcy Code.

In YAQUINTO v. THOMPSON ST. CAPITAL PARTNER (IN RE STONE PANELS, INC.), Case No. 16-32856, Adv. Pro. No. 16-03143, 2021 WL 4436166 (Bankr. N.D. T.X. Sept. 27, 2021) (opinion not yet released for publication), the court held that while it was clear that the debtor did not receive an exchange of equivalent value, the plaintiff failed to meet the burdens of proof required by Bankruptcy Code § 548(a)(l) and the Texas fraudulent transfer law. Firstly, the debtor must have been insolvent when the transfer was made or have become insolvent as a result of the transfer. Here, the trustee was not able to provide evidence of insolvency, while the creditor provided credible testimony showing the debtor's solvency at the time of the transfer. Alternately, the debtor had to have been engaged, or on the verge of engaging, in a transaction that would have left it with an "unreasonably small" amount of capital. Indeed, although the trustee was able to prove that the debtor did lose capital following the transfer, the loses had occurred because of the debtor's hiring decisions and unforeseen changes in customer demands, which could not have reasonably been foreseen at the time of the transfer. Thirdly, the trustee could have proved that debtor had or had acquired debts that it lacked the ability to pay as they become due. Here, the trustee could not prove that the debtor took on debts that it lacked the ability to repay. By contrast, the defendant demonstrated that it had carefully studied the debtor's past performance as well as the performance of similar businesses and would not have been able to predict the debtor's debts being unsurmountable based on its study of the debtor. Accordingly, the court ruled in favor of the defendant because the trustee failed to meet his burden of proof. By Alexander Chamales achamale@ttu.edu

Fraudulent Transfer Claims Against Secured Creditor Survive Motions to Dismiss [BKR KS]

The creditor extended credit to an affiliated group of health care providers that had been assembled by one individual. Not long after, the creditor also extended credit to the non-health care related debtors that had ties to the affiliated group through the individual responsible for assembling the companies. These two separate loans to the debtors were secured by real property. Later, one of the members within the affiliated group sought an additional loan. This loan was backed partially through cross guaranties of the debtors. Later, the debtors filed Chapter 11 petitions and scheduled the debts in ways that differed from a secured creditor's proofs of claim in aggregate amounts and with respect to the amounts that were secured. These proofs of claim had been filed before the conversion of the Chapter 11 cases to a Chapter 7 cases. The court entered an order granting post petition financing. The creditor had agreed to this order, which allowed for time to investigate aspects of the creditor's liens and claims. Eventually, the creditor was sued by the Chapter 7 trustee and the creditor moved to dismiss the complaint. Among other claims, the trustee asserted that the guaranties had been fraudulent transfers.

In OFFICIAL COMM. OF UNSECURED CREDITORS OF PINNACLE REG'L HOSP., INC. V. GREAT WESTERN BANK, Case No. 20 -20219, Adv. No. 20-06025, 2021 WL 666327, 2021 Bankr. LEXIS 361 (Bankr. D. Kan. Feb. 17, 2021), the creditor attempted to dismiss these counts for lack of standing of the Chapter 7 trustee, arguing that there were no unsecured creditors who could benefit from the trustee's suit. The court, however, opted to not dismiss on that ground because it reasoned that the argument was premature: the deadline to file claims had not yet passed. Two other fraudulent transfer counts of the complaint alleged the debtors were insolvent, and the creditor sought to have these counts dismissed. The court choose not to dismiss these counts because it reasoned the trustee's allegations of insolvency were sufficient. In addition, the creditor also attempted to dismiss these same counts for a lack of "triggering creditors," which is needed for a claim of fraudulent transfer. The creditor argued that, for the trustee to assert a claim under 11 U.S.C. § 544, there must be a current creditor of the debtor whose claim had arisen at the time of the allegedly wrongful transfer. The court agreed, holding that these claims were deficient because the trustee could not name specific creditors. Nevertheless, the court allowed the Chapter 7 trustee to file an amended complaint, as requested. Finally, the creditor sought to dismiss these same claims for the lack of unsecured creditors that could benefit from avoidance. The court disagreed because the purpose of avoidance actions is not only for the benefit of unsecured creditors. Therefore, the court ultimately denied most of the creditor's motions to dismiss and allowed the trustee to amend the complaint. By Avery Bertagna abertagn@ttu.edu

SECURITY INTEREST

Creditor's Arguable Bad Faith Did Not Render Security Interest Invalid as a Fraudulent [6TH CIR]

The debtor finance company entered into a revolving loan agreement with the creditor in 2002 ("the 2002 agreement") and created and perfected a security interest in all the debtor's assets. Unknown to the creditor at that time, the debtor was involved in a Ponzi scheme in which its owners used the revolver money as a front. Despite realizing the scheme existed in 2003, the creditor both renewed and extended the loan agreement in 2004 ("the 2004 agreement"). With its knowledge of the debtor's criminal activity in mind, the creditor waived contractual provisions in the 2004 agreement that would have required audits of the debtor's financial condition. Following the termination of the debtor-creditor relationship, the debtor's Ponzi scheme came to light and forced the debtor into involuntary bankruptcy. Subsequently, the debtor's bankruptcy trustee sought to avoid payments to the creditor as fraudulent transfers under Ohio's Uniform Fraudulent Transfer Act (OUFTA), arguing that the creditor had acted in bad faith by renewing the loan after learning of the Ponzi scheme, thus invalidating the 2002 agreement under the OUFTA. Thus, the trustee argued, the court should avoid the "new" obligations created by the 2004 agreement.

In BASH v. TEXTRON FIN. CORP. (IN RE FAIR FIN. CORP.), No. 20-3351, 2021 Fed. App. 0216 (6th Cir. Sept. 10, 2021), the court considered whether a party's subsequent actions, arguably made in bad faith, undermine its previously perfected security interest so that any payments made in connection with that security interest constitute fraudulent transfers under Ohio law. To resolve the issue, the court first considered several statutory definitions. OUFTA renders fraudulent, transfers made "[w]ith actual intent to hinder, delay, or defraud any creditor of the debtor." These transfers are avoidable by a trustee. However, a voidable "transfer" under the statute excludes a transfer of those assets already encumbered by a valid lien. For purposes of OUFTA, a "valid lien" is a lien that is "effective against the holder of a judicial lien subsequently obtained." Because this definition measures validity in reference to a dispute of two security interests, here the creditor's interest in the 2002 agreement and the-hypothetical subsequently obtained judicial lien of the bankruptcy trustee, Article 9 of the UCC governed the statutorily created priority dispute. Under Article 9, a perfected security interest prevails over any conflicting and unperfected security interest. Here, the creditor held a perfected 2002 security interest. Applying a hypothetical "judicial lien subsequently obtained" to the analysis, the 2002 security interest would prevail in a priority dispute. However, the trustee also argued that the obligation of good faith under the UCC called for reordering these priorities. Although the court agreed that lack of good faith could impact the enforceability of a senior priority interest, such reordering requires bad faith within a relationship between at least two competing creditors. Because the OUFTA test requires ranking the priority interest of a security interest against a hypothetical subsequent judicial lien, no competing-creditor relationship existed for any such subordination to exist under the UCC. Therefore, the court held that a perfected interest under OUFTA is by definition a "valid lien," and thus the creditor's 2002 security interest constituted a valid lien unavoidable as a fraudulent transfer. By Brooke Allen brooke.n.allen@ttu.edu

Security Interest Invalid Because Debtor Had No Rights in the Collateral [SD]

A borrower represented to a bank that he had purchased cattle known as "Group 21," which were listed as collateral for that year's operating loan. The bank performed a UCC search before approving the loan and found no other party had filed a financing statement against the borrower's cattle. The bank advanced the borrower a loan for the year with 1,860 head of cattle listed as collateral, including the "Group 21" cattle. Two months later, a bank officer performed an inspection and noticed that the number of cattle appeared to be inadequate. The officer ordered a full count to be performed the next day, but before the count took place, the borrower called the officer and admitted that he did not own the number of cattle he had represented that he owned, and that the reports had been falsified. In fact, there were 855 head of cattle at the feedlot compared to the 1,860 head of cattle the debtor had claimed to have owned, and of those 855, the borrower only owned approximately 285 head of cattle. The "Group 21" cattle consisted of cattle owned by the borrower's uncle.

The owner and borrower had agreed that the borrower would feed the cattle to finish, and in return, would receive $0.70 per pound of the weight the cattle gained. After the material misrepresentation was uncovered, the bank filed a declaratory judgment action claiming it had a security interest in the cattle owned by the uncle, because the borrower had apparent ownership of the cattle, the bank had exercised reasonable care to determine the number of cattle at the borrower's feedlot, and the owner had failed to file a UCC caretaker statement or otherwise give notice to the bank as to who was the actual owner of the cattle. The owner moved for summary judgment, asserting that the relationship between the owner and borrower was that of a bailment and mere possession of the cattle by the borrower was insufficient for the bank's security interest to have attached. The court denied summary judgment to the owner of the cattle and found that the owner had allowed the borrower to appear to be the owner of the cattle because he had taken no actions to protect his interests in the cattle. However, the court determined that the bank could have conducted a more thorough inspection of the feedlot. The court therefore held that the owner was not estopped from asserting that the borrower had no rights in the owner's cattle and therefore, the bank had no security interest in those cattle. The bank appealed.

In FIRST DAKOTA NATIONAL BANK v. GREGG, 965 N.W.2d 69, 2021 S.D. 53 (S.D. 2021), the court affirmed the lower court's conclusion that the bank could not claim a security interest in the cattle not owned by the borrower. First, the court explained that if the owner of collateral allows another to appear to be the owner, and a third party is led to deal with the apparent owner as if he was the actual owner, then the owner is estopped from asserting that the apparent owner lacked rights in the collateral. However, the court explained, if the creditor failed make reasonable efforts to determine ownership of the collateral or "could have reasonably discovered" that another entity owned the property, then an estoppel claim will not stand. The court found that the actions of taking the cattle to the borrower's lot and failing to file a UCC filing were not enough to establish that the uncle had allowed the nephew to appear to be the owner of the cattle. The court also stated there was no evidence that the owner had given the borrower any interest in the cattle other than mere possession of the cattle. Relying on prior case law, the court affirmed that mere possession of collateral is insufficient to enable a security interest to attach. Further, the court also found that the uncle had taken steps to show ownership by branding the cattle on the left hip with his exclusive brand and tagging each left ear with orange ear tags. The court concluded it was the borrower's fraudulent actions and misrepresentations that caused the mistake, and not the conduct of the rightful owner, that had given the bank the perception that all the cattle at the feedlot were owned by the borrower. Additionally, the court held that even though the lower court had erred in concluding that the owner allowed the borrower to appear to be the owner of the cattle, it had come to the correct conclusion when it focused on whether the bank could have reasonably discovered proper ownership of the cattle before making the loan, so there was no need to reverse the lower court's decision. By Lauren Ottmers lauren.ottmers@ttu.edu Edited by Carlos Gracia

BANKRUPTCY

For Subchapter V Eligibility, Business Debts Need Not Be Related to the Debtor's Current Business [BANKR MD NC]

The debtor was the sole owner of a corporation that provided information transport ("IT") consulting services. The corporation ceased operations and liquidated all its assets. After closing the corporation, the debtor worked as a solo IT consultant, working for two different entities as an independent contractor. The debtor filed for Chapter 11 relief, electing to proceed under subchapter V of Chapter 11. Post bankruptcy, the debtor had to file a report on the status of her bankruptcy. Upon filing the report, the bankruptcy administrator (BA) objected to the debtor's subchapter V election. During the hearing on the objection, debtor was required to prove that more than 50% of her debts arose from her previous commercial or business activities in order to be eligible for subchapter V. The hearing ended with a dispute over the classification of two categories of debt. The first category related to the debt regarding her former personal residence that had been reneting but that she was not renting to others at the time of the bankruptcy. Before the bankruptcy case, she had refinanced that house and at the time of her bankruptcy, still owed money on that mortgage and on loans she had taken out to repairs damage caused by her last tenants. The BA's primary argument regarding this category of debt was that mortgage debts should not be considered "commercial or business" activities because the mortgage had originally been taken out for personal reasons. The second category related to a Small Business Administration (SBA) loan, for which the debtor testified she was not personally liable. Later she filed a declaration stating she was, in fact, liable on that SBA loan. The BA objected to the declaration because the SBA note stated the borrower on the SBA loan had been the debtor's former corporation and she had signed that loan in her capacity as the president of the corporation.

In IN RE BLUE, 630 B.R. 179 (Bankr. M.D.N.C. 2021), the court held that the debtor had been engaged in commercial and business activities on the date of her petition, and therefore was qualified to be a subchapter V debtor. In order to claim subchapter V relief, the debtor must be engaged in business or commercial activities as of the petition date. The debtor's activities as an independent contractor fulfilled the requirement and the majority of her debts arose from commercial or business activities. In determining the debtor was eligible for subchapter V, the court reasoned that the plain language of the statute did not require that the debtor's business debts be related to her current business activities. A significant amount of the debt arose from the operation of the debtor's former corporation, which had ceased operations before she began her work as an independent contractor. As for the mortgage on the rental property, the court agreed with the BA that the mortgage did not arise from commercial or business activities, but the loans she had taken out to renovate the property after the tenant had damaged the property did arise from commercial or business activities. As to the SBA loan, the court held that the debtor had failed to establish that the loan was her personal obligation. The note clearly indicated that the debtor signed in her representative capacity as the president of her corporation, rendering her not individually liable for the loan. Nonetheless, she met the requirement that 50% of her total debt related to business activities. For these reasons, the court held that debtor was eligible to continue her case under subchapter V. By Jessica Longoria jessica.longoria@ttu.edu

BANKING REGULATION

Potential Electronic Funds Transfer Act (EFTA) Violation for Unclear Overdraft Fee Terms in the Opt-In Agreement [D Conn]

Plaintiff brought a class action against the bank relating to an opt-in agreement pertaining to overdraft fees. Regulation E promulgated under the EFTA requires that banks attain some form of consent before charging overdraft fees. Without an agreement the bank has two options: (1) cover the overdraft for the account but do not charge the account holder a fee, or (2) decline to cover the overdraft. An overdraft occurs when the account balance drops below zero, and this balance can be either the "actual" or the "available" balance. In the bank's opt-in agreement at issue here, the fundamentals of an overdraft agreement were explained, but there was no mention of whether the "actual" balance or the "available" balance was used to determine if the customer's account was in overdraft. The plaintiff and others had been charged overdraft fees by the bank based upon the "available" balance. The plaintiff contended that the opt-in agreement failed to clearly state what balance would be used, but the description suggested that an "actual" balance would be used to determine if the customer's account was in overdraft. The plaintiff argued that the agreement was confusing and inaccurate, and therefore did not comply with the Electronic Funds Transfer Act (EFTA). If the agreement were found to be "materially false," then it might also be a a violation of the Connecticut Unfair Trade Practices Act (CUTPA). The plaintiff was seeking damages as a remedy for these misleading agreements and for the overdraft fees that had been charged. The bank moved to dismiss the action for failure to state a claim under which relief can be granted.

In ADAMS v. LIBERTY BANK, 2021 WL 3726007, 2021 U.S. Dist. LEXIS 158616 (D. Conn. August 23, 2021) (opinion not yet released for publication), the court denied the bank's motion to dismiss. First, the bank argued that other documents presented to the debtor at the time the account was opened provided information specifying that the "available balance" would be used to determine if the customer's account was in overdraft. Second, the bank also argued it was immune from EFT A liability because the language used in the opt-in agreement was similar enough to a CFPB model notice. Lastly, the bank contended that the debtor had failed to state an EFTA claim because the claim was "nothing more than a breach-of-contract claim." The court, however, relied primarily on the language of the opt-in agreement because it was the agreement to which the complaint referred. For the court to consider any other documents, the defendant had to show that the documents had been received by the plaintiff. Even with the extra evidence, however, the court reasoned that the Regulation E claims were still viable because Regulation E requires the disclosures be in a "notice in writing... segregated from all other information." In addition, the court found that the bank had failed to properly disclose overdraft fees because of the inaccurate nature of the opt-in agreement. While the bank had used a model form in drafting the opt-in agreement, the agreement lacked clarity and thus failed to satisfy the second requirement for immunity. In addition, the CUPTA claim survived a motion to dismiss. Viable EFTA claims do not always result in a CUPTA claim, the court explained, but in this case the court reasoned the claim arose independently of the EFTA claim. Therefore, the court also denied the bank's motion to dismiss the CUPTA claim. By Avery Bertagna abertagn@ttu.edu

MORTGAGES

*The Power of “No Waiver” Provisions Regarding Disputes Between Debtors and Lenders [SD TX]

Husband and wife (the homeowners) borrowed money to purchase a home. The homeowners properly executed the note and deed of trust, which granted a mortgage on the property to the lender. However, the initial note and deed of trust had erroneously misspelled the wife’s name, but both the note and deed of trust (“loan” or “loan agreement”) had been corrected. The homeowners eventually became late on payments, but the lender nonetheless accepted the late payments. The note required that if the homeowners failed to make timely payments, the lender reserved the right to accelerate the maturity date of the loan and to foreclose on the property. Eventually, the lender commenced foreclosure proceedings and gave notice to homeowners pursuant to Texas Rule of Civil Procedure 736. The homeowners filed suit, arguing that by virtue of the lender’s “custom and practice” of accepting late payments on the note, the lender had waived the right to accelerate the debt. Additionally, the homeowners argued that the deed of trust had not been properly conveyed to the lender. The lender responded almost four years later by pointing to the loan agreement, which contained a “no waiver” prov1s1on, providing that the lender’s acceptance oflate payments did not waive its right to accelerate or foreclose on the property. The lender moved for summary judgment on the homeowners’ claim against it as well its own counterclaim for breach of contract and foreclosure. Instead of addressing the lender’s motion, the homeowners responded by arguing that the lender’s causes of actions had accrued more than four years before the lender filed its counterclaim, and its claim was therefore barred by the applicable statute of limitations.

In MARTINEZ v. WELLS FARGO BANK, N.A. AS TR. FOR PARK PLACE SEC., INC., ASSET-BACKED PASS THROUGH CERTIFICATES SERIES 2004-MCWl, No. 7:20 CV 104, 2021 WL 2764857, 2021 U.S. Dist. LEXIS 126798 (S.D. Tex. April 15, 2021) (opinion not yet released for publication), the court granted the lender’s motion for summary judgment. The court noted that the homeowners never disputed whether the loan agreement was valid, nor had they argued the validity of the “no waiver” provision. Additionally, the lender had properly notified homeowners of their default and of its intent to foreclose on the mortgaged property. The court determined that the lender had shown its right to foreclose under Texas Property Code § 51.002, establishing that: (1) a debt exists, in the form of the amounts owed, (2) the debt is secured by a home equity lien, (3) the homeowners were in default under the loan, and (4) the homeowners received notice of default and intent to accelerate. As for the homeowners’ argument, relying on Texas Civil Practice and Remedy Code § l 6.004(a)(3) (breach of contract claims be filed “no later than 4 years after the day the cause of action accrues”) and 16.035(a)-(b) (four-year limitation also applying to foreclosure of real property), the homeowners argued that the date the lender’s claim began was at the time of the 2010 notice of default and intent to accelerate. The court concluded that an uncontested “savings” provision that, provided for in Texas Civil Practice & Remedy Code § 16.069, allowed for a counterclaim, even though if it were a separate action it would have been untimely on the date the party had been required to answer the homeowner’s complaint. Furthermore, the court also noted that the lender had never been served, meaning that its answer was never “required” within the meaning of the savings provision and its counterclaims were timely under that provision. By Victor Perez victor.perez@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.

To contact Tracy Kennedy, NDBA General Counsel, call 701.772.8111 or email at tracy@ndba.com.