NORTH DAKOTA BANKERS ASSOCIATION

LEGAL UPDATE

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APPEALS

Bankruptcy Appeals: Who Has Standing? [5th CIR]

A party in interest in a complex bankruptcy matter objected to professional fees paid to five organizations as ordered by the bankruptcy court. The bankruptcy court dismissed this objection, taking issue with the timing and merits of the objection, and approved the fee applications. The party in interest appealed to the district court. The district court dismissed the appeal for lack of appellate standing. The party in interest appealed to the Fifth Circuit, making four arguments to support its appellate standing: (1) it passes the "person aggrieved" test, which requires an appellant to show it was affected pecuniarily, directly, and adversely by the bankruptcy order at issue because it (a) also served as a defendant in a related, pending adversary proceeding and (b) had an administrative claim in the bankruptcy proceeding; (2) even if it did not pass the test, the "person aggrieved" standard was no longer valid following Lexmark Int'l, Inc. v. Static Control Components, Inc., 572 U.S. 118 (2014); (3) the "person aggrieved" test is not strictly limited to a showing of pecuniarily harm; and (4) related cases have allowed appellate standing.

In NexPoint Advisors, L.P. v. Pachulski Stang Ziehl & Jones, L.L.P. (In Re Highland Cap. Mgmt. L.P.), 74 F.4th 361 (5th Cir. 2023), the United States Court of Appeals for the Fifth Circuit addressed each of the four arguments above, ultimately affirming the district court. The court affirmed the "person aggrieved" test, a higher standard than traditional standing, to determine standing in bankruptcy matters. The court reasoned that this higher standard is necessary to prevent overwhelming the court system with bankruptcy cases involving many parties and overlapping interests. The court found that the party in interest could not be considered a "person aggrieved" because (a) its involvement in the related, pending adversary proceeding did not demonstrate a direct and adverse pecuniary harm and (b) its administrative claim had been disallowed by the bankruptcy court. The Fifth Circuit further explained that it had continually reaffirmed the "person aggrieved" standard in numerous cases post-Lexmark, maintaining that the standard is good and valid law. The court also found that the party in interest failed to raise his third argument in the district court and, as such, forfeited the right to raise it on appeal. Finally, the court held that the cases provided by the party in interest were irrelevant because they did not involve bankruptcy.

By Kristin Meurer krmeurer@ttu.edu
Edited By Joshua Shetler joshua.shetler@ttu.edu
Edited By Peter Benson pebenson@ttu.edu

BANKING REGULATION

Bank Whistleblower Retaliation Suit Dismissed in Part [ND GA]

On December 12, 2017, a former vice president (the employee) of a large multinational bank filed a claim with the Securities and Exchange Commission ("SEC") that alleged that the bank had been intentionally deceiving and misleading its patrons about its compliance with Payment Card Industry ("PCI") standards. The purpose of the PCI is to ensure that sensitive customer data is managed safely. Both the bank and its parent company would handle and transfer this sensitive data between each other, but in reality, only the parent company was compliant with PCI standards. The bank itself was not. The employee knew this fact well and alleged that the bank and its parent company did also. The employee claimed that after he addressed this issue during a meeting, the bank took no action. The employee then began to save critical emails regarding this on his personal account to keep as evidence of the bank's fraudulent actions for a future claim that would be made with the SEC.

Five months later, the bank's human resources department learned of the employee's practice of saving these emails. The employee was told to destroy all emails saved onto his personal account and certify that he had done so. The employee refused and was terminated the next day, causing him to file a claim with the SEC and thus sue the bank, its parent company, and other associated parties (the "defendants") for retaliation against

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a whistleblower under the (1) Sarbanes-Oxley Act ("SOX"), (2) Consumer Financial Protection Act ("CFPA"), and (3) the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"). The defendants subsequently moved to dismiss the case, alleging that (1) the employee failed to exhaust remedies to the other associated parties under the SOX or CFPA; (2) the employee failed to make a report to the SEC before his termination; (3) the other associated parties did not employ the employee; (4) the employee failed to show that the other parties knew of any protected conduct or took a negative employment action; (5) the employee failed to show that the defendants were "covered persons" or "service providers" under the CFPA or that the employee engaged in any activity protected by it; and (6) the employee failed to demonstrate vicarious or successor liability as to the other associated parties. In response, the defendants filed a motion to dismiss based on six arguments.

In Slawin v. Bank of Am. Merch. Servs., 491 F. Supp. 3d 1334 (S.D. Ga. 2020), the court analyzed the defendants' six arguments. First, the court ruled that the employee did not name the bank's parent company and the other associated parties in his SOX and CFPA complaint and, therefore, did not exhaust all remedies as to them. The court subsequently dismissed counts (1) and (2) of the employee's complaint against them. Second, the court ruled that the employee could not be a whistleblower under DoddFrank because he made his claim with the SEC only after his employment was terminated. The court, therefore, dismissed count (3) of the employee's complaint to all parties. The court then noted that these rulings resolved all claims against the bank's parent company and the other associated parties and, therefore, removed them from the suit. Because of this, the court did not address sections (3), (4), and (6) of their argument. Lastly, the court addressed section (5) of the argument as it pertained to the bank, finding that the bank was a "service provider" under the CFPA because it provided payment processing services to other companies and consumers. The court additionally found that the employee's actions plausibly constituted a protected activity under the SOX and CFPA. The court, therefore, denied the bank's motion to dismiss count (2) of the employee's complaint against it.

By Caleb Shetler Caleb.A.Shetler@ttu.edu
Edited By Joshua Shetler joshua.shetler@ttu.edu
Edited By Avery Bertagna abertagna@ttu.edu

Clarification of a Federal Reserve Rule Does Not Restart the Statute of Limitations [8TH CIR]

The Durbin Amendment to the Dodd-Frank Wall Street Reform and Consumer Protection Act authorized the Board of Governors of the Federal Reserve System (the Board) to regulate the transaction fees merchants pay to credit card issuers. In 2011, the Board issued Regulation II, establishing maximum transaction fees. In response to a D.C. Court of Appeals ruling, the Board published a clarification of Regulation II in 2015. Here, two North Dakota associations representing merchants (the merchants) sued the Board and alleged that Regulation II violated the Administrative Procedure Act (APA) by being arbitrary and capricious. The district court dismissed the claim, holding that the statute of limitations had run on a claim against Regulation II, and that because the clarification of the regulation did not constitute final agency action, it did not renew the statute of limitations. The merchants appealed.

In N.D. Retail Ass'n v. Bd. of Governors of the Fed. Reserve. Sys., 55 F.4th 634 (8th Cir. 2022), cert. granted sub nom. Corner Post, Inc. v. Bd. of Governors, FRS, No. 22-1008, 2023 WL 6319653 (U.S. Sept. 29, 2023), the Eighth Circuit Court of Appeals held the statute of limitations had run to challenge Regulation II. First, the clarification was not final agency action, and thus did not restart the clock for challenging Regulation II. Under the APA, once the Board takes final agency action a six-year statute of limitations begins to run. For agency action to be final, it (1) cannot be temporary or interlocutory and must be a "consummation" of the decisionmaking process, and (2) the action must have legal consequences that cause concrete actual injury to the claimant. Here, the clarification was not a final action because it did not change Regulation II or cause a new injury; rather, it explained the existing rule. Second, the court refused to entertain the merchant's assertion of the "reopening doctrine" because it only existed in the D.C. Court of Appeals, and the Supreme Court has never adopted it. Third, the statute of limitations on a "facial" challenge to agency action, rather than an "as applied" challenge, begins tolling when the regulation is published. Here, this was a facial challenge, and thus, the limitation had long since run. Fourth, the merchants failed to bring an equitable tolling claim because they did not show that they had diligently pursued their rights.

By Wyatt Macfarlane wmacfarl@ttu.edu
Edited By Joshua Shetler joshua.shetler@ttu.edu
Edited By Avery Bertagna abertagn@ttu.edu

BANKRUPTCY

Challenges to Dischargeability of Debts: Timing and Equitable Tolling [3RD CIR]

The debtor defaulted on weekly payments owed to the creditor as a part of a settlement; the creditor then obtained a judgment in New York state court against the debtor. The debtor filed for Chapter 7 bankruptcy, listing, among other debts, the judgment amount in full. Following the creditors' meeting, the bankruptcy trustee reported that there were no assets for bankruptcy distribution and that creditors should not file a proof of claim unless assets became available. No creditors

in the case filed motions to oppose the dischargeability of the debt, the bankruptcy court granted the debtor's discharge, and the bankruptcy case was closed. After more than five years, the creditor moved to reopen the bankruptcy case, alleging the debtor had fraudulently transferred assets before he filed his bankruptcy petition, to a company currently operated by the debtor. Those assets, the creditor claimed, should have been part of the bankruptcy estate. The creditor challenged the dischargeability of its debts under 11 U.S.C. § 523, claiming that the debtor's fraud rendered the debt owed to the creditor non-dischargeable. Furthermore, the creditor argued that even if its debt were dischargeable, discharge obtained through fraud must be revoked under 11 U.S.C. § 727(d)(l). The bankruptcy court, relying on In Re New Century TRS Holdings, Inc., No. 07-10416 (BLS), 2021 Bankr. LEXIS 2826, 2021 WL 4767942 (Bankr. D. Del. Oct. 12, 2021) denied the creditor's motion to reopen, reasoning that (1) the challenges as to the dischargeability were not only untimely, but 'time-barred" and (2) the creditor had a sufficient alternative to seek relief in state court against the debtor and the newly discovered company (which the creditor had already sought). The creditor argued on appeal that the bankruptcy court had discretion to reopen the case despite time limits because the bankruptcy rules governing timing for its claims allowed for equitable tolling.

In In Re Delloso, 72 F. 4th 532 (3d Cir. 2023), the Court of Appeals for the Third Circuit held that the bankruptcy court properly denied the creditor's motion to reopen the case. The court stated that the Bankruptcy Code provisions on which the creditor's claim relied (11 U.S.C. §§ 350, 523, and 727) were subject to the time limitations of Fed. R. Bankr. P. 4007(c). Even considering that under Fed. R. Bankr. P. 9006(b)(3) bankruptcy courts generally have the power to enlarge these time limitations, the court found that such enlargements were limited to the conditions set out in the plain text of Rule 4007(c). The court held that the text of Bankruptcy Rules 4007(c) and 9006(b) clearly precluded exceptions to the time limit for challenges to the dischargeability of a debt regardless of equitable tolling.

By Kristin Meurer krmeurer@ttu.edu
Edited By Melissa Hightower mehighto@ttu.edu
Edited By Riley Caraway rcaraway@ttu.edu

FORECLOSURE

No "Vapor Money" Loophole [TX APP]

A mortgagor signed a promissory note to obtain a loan. The terms of the promissory note required the mortgagor to pay a monthly installment, and in the event of a default, the note contained an acceleration clause to recoup the balance remaining on the loan. The mortgagor defaulted on the promissory note by failing to make monthly payments. After the mortgagor failed to cure the issue, the mortgagee filed suit for breach of the promissory note and accelerated all payments. The mortgagor responded to the mortgagee's motion for summary judgment by denying that he "operates under the laws of the Republic" and challenged the mortgagee's ability to lend money rather than credit. The trial court granted the mortgagee's summary judgment and awarded the mortgagee the remaining balance of the promissory note. Appearing pro se, the mortgagor appealed on the basis that the mortgagee's evidence of the note was insufficient, the contract was ultra vires for a national bank, and the trial court should have issued a RICO subpoena.

In Maldonado v. Yellowfin Loan Servicing Corp., No. 14-22-00522-CV, 2023 WL 5124767, 2023 Tex. App. LEXIS 6022 (Tex. Ct. App. Aug. 10, 2023) (opinion not yet released for publication), the court held that the mortgagee established the required elements to recover on the note and rejected the issues raised on appeal by the mortgagor. The mortgagor claimed on appeal that the loan had been "vapor money," a theory from the "sovereign citizen" movement. The mortgagor asserted that the loan he received was invalid because it involved the creation of credit instead of the transfer of lawful money. The court rejected the "vapor money" theory, holding that there is no basis in law for this claim, and other courts repeatedly have dismissed the theory. Furthermore, the mortgagor did not provide evidence for his ultra vires claim, and nothing exists in the record to show the mortgagee was a government agency or a national bank. The court dismissed the final claim, stating that the allegation of failure to issue a RICO subpoena was "wholly without merit." In short, the court concluded that the "vapor money" theory could not be used to avoid paying the loan, the mortgagee had met its burden and was entitled to recover the remaining balance.

By Hayden Mariott hayden.mariott@ttu.edu
Edited By Joshua Shetler joshua.shetler@ttu.edu
Edited By Ashley Boyce ashboyce@ttu.edu

A Mistaken Foreclosure Creates a Challenging Legal Fight [OK]

The loan servicer filed several foreclosure actions against the borrower during the first ten years of her mortgage, but the borrower always renegotiated her payments and avoided foreclosure. During a time when the borrower was late on her payment, the servicer of her loan changed. The new servicer notified the borrower that she was past due and sent a foreclosure notice. The borrower, however, again modified the agreement with the new servicer. A year later, the borrower defaulted again, but the borrower entered into a deed in lieu of foreclosure (DIL) with the servicer. Later, the servicer went to sell the property, and during this process its law firm "prepared an assignment of mortgage from the original lender." The servicer could not locate

the original lender, and "believing it had the right to do so," the servicer canceled the DIL and started the foreclosure process. The servicer's bank filed a foreclosure petition against the borrower, and the borrower counter-sued both the bank and the servicer on several causes of action for wrongfully terminating her DIL. Upon learning of its error, the bank dismissed the foreclosure without prejudice and recorded another DIL, but the borrower continued her counterclaims. In relevant part, the borrower's counterclaims included wrongful foreclosure, Category II punitive damages, an Oklahoma Consumer Protection Act (OCPA) claim, and a Fair Debt Collection Practices Act (FDCPA) claim. At trial, the jury decided in the borrower's favor on all issues, and the bank and servicer moved for a directed verdict on multiple different grounds. The trial court granted the motion against the borrower on her Category II punitive damages claim, but denied the motion in all other respects and awarded the borrower attorney's fees against the servicer. All three parties appealed. The court of appeals held for the bank and servicer on every appellate issue. The borrower appealed to the state supreme court.

In U.S. Bank Nat'l Ass'n v. Hill, No. 118680, 2023 WL 5923637, 2023 Okla. LEXIS 92 (Okla. Sept. 12, 2023) (opinion not yet released for publication), the court reversed in part and affirmed in part the judgment of the trial court after addressing six different issues. First, the court found that the borrower was not entitled to a new trial solely on the-issue of Category II damages and dismissed that portion of her appeal. The court based its reasoning on the fact the borrower had already accepted damages under the trial court's judgment and the fact no precedent supported the borrower's argument. Thus, she forfeited her right to have a new trial on the damages claim by having accepted the trial court's judgment. Second, the court considered whether the bank was liable for wrongful foreclosure. The court analogized a wrongful foreclosure claim to a malicious prosecution claim, and one of the elements of malicious prosecution requires "the action [to have] been terminated in the proponent's favor." Because the bank dismissed its action without prejudice before trial, the court found that the bank's actions did not satisfy this element of malicious prosecution. Thus, the court held for the bank on the wrongful foreclosure claim. Third, the court held for the servicer on the OCPA claim because the servicer qualified for the Act's safe harbor provision because the Consumer Financial Protection Bureau, a federal agency, regulated the servicer's conduct. Fourth, the court assessed the FDCPA claim against the servicer. Although the servicer contended it was not a debt collector under the Act, the court disagreed and held for the borrower, explaining the issue turned on the definition of the term default. Because the FDCPA does not define that term, the court looked at the terms of the original note and found sufficient evidence in the record that allowed the jury to conclude the borrower was in default. Fifth, the servicer argued that the borrower received a double recovery. The court disagreed because the trial court awarded Category I punitive damages for tort claims based on the servicer's failure to honor the DIL whereas the borrower based her recovery under the FDCPA on the servicer's collection efforts, a separate wrong from the tort claims. Thus, the borrower did not double recover because the two theories of recovery were predicated on different injuries. Sixth, the court remanded the attorney's fees' issue to the trial court in light of its holding on the OCPA claim.

By Marcus Braymer mbraymer@ttu.edu
Edited By Joshua Shetler joshua.shetler@ttu.edu
Edited By Peter Benson pebenson@ttu.edu

Promissory Estoppel May Shield Homeowners from Improper Foreclosure Proceedings [OK APP]

The bank sought summary judgment on a claim to compel foreclosure following the mortgagors' default. However, the mortgagors alleged that a former bank representative informed them that, under federal law, they had to default on the then current note for a modification to the terms of the note. In reliance on this advice, the mortgagors defaulted, and the bank petitioned for foreclosure. While these proceedings were ongoing, the bank sold the mortgage to another entity (the mortgagee) who took over the foreclosure proceedings. The mortgagee declined knowledge of the existing modification agreement and offered the mortgagors a new "assumption plan." The mortgagors followed up, but the mortgagee offered no response. Next, the mortgagee filed for summary judgment, which received no ruling, as the mortgagee attempted to work out a modification deal with the mortgagors. The mortgagors filled out many applications that the mortgagee claimed were either lost due to changes in asset managers or were incomplete, without affording an explanation. On one such occasion, the mortgagors had reached an agreement through a letter from the mortgagee's then asset manager that offered a 40-year fixed rate mortgage if the mortgagors completed the "trial period plan" which consisted of three "good faith" payments. After the mortgagors had made the payments, the mortgagee informed the mortgagors that it had hired a new asset manager and that the mortgagors would have to restart the loan modification process. The mortgagee again filed for summary judgment arguing that even if it violated federal mortgage modification program terms, its actions created no viable defense to the foreclosure. The district court granted summary judgment, and the mortgagors appealed.

In Bayview Loan Servicing, LLC v. Baxter, 530 P.3d 89 (Okla. Civ. App. 2023), the court agreed with the lower court that the mortgagors could not argue the mortgagee failed to follow the requirements of federal mortgage modification programs.

The court reached this conclusion because those programs "do not grant [mortgagors] a personal right to a modification." However, the court refused to extend this reasoning to prevent a mortgagor from possessing enforceable rights under a state law claim when a mortgagee had promised a modification. The mortgagee presented the mortgagors an offer, and the mortgagors accepted the offer and performed. Under state law, this created private contractual or quasicontractual rights between the parties sufficient to establish a promissory estoppel claim. Because such a showing of promissory estoppel gave rise to a state-law right to a modification, the court held the mortgagors could argue the promissory estoppel issue as a viable defense to foreclosure, the proceedings of which "are equitable in nature." The court explained this rule applied regardless of whether the mortgagee's or the bank's actions had violated federal law. The appellate court vacated the district court's grant of summary judgment and remanded.

By Jesse Castella cas72899@ttu.edu
Edited By Joshua Shetler joshua.shetler@ttu.edu
Edited By Peter Benson pebenson@ttu.edu

REAL ESTATE SETTLEMENT PROCEDURE ACT (RESPA)

Surviving a Motion to Dismiss for RESPA and FDCPA Claims [2D CIR]

Two borrowers sued their mortgage loan servicer (the servicer) under the Real Estate Settlement Procedure Act (RESPA). Two primary documents governed the borrower's loan: (1) a modification agreement and (2) a forbearance agreement. The servicer began servicing the loan after both were in place. The borrowers alleged two main violations of the servicer in their second amended complaint. First, the servicer failed to conduct a reasonable investigation into their account in order to correct it. RESPA requires that mortgage loan servicers conduct a reasonable investigation and respond to a borrower's "qualified written request" (QWR) in a timely manner. The borrowers sent the servicer a QWR, and the servicer responded that it found the borrower's account to be correct. The borrowers alleged that had the servicer conducted a reasonable investigation it would have found that the forbearance agreement terminated the modification agreement. Second, the borrowers alleged claims under the Fair Debt Collection Practice Act (FDCPA), arguing that the servicer was a debt collector because it had begun servicing the loan post-execution of the forbearance agreement, which existed because the borrowers had been in default of the loan governed by the modification agreement. After the borrowers filed their second amended complaint, the servicer moved to dismiss for failure to state a claim.

In Joseph v. Ocwen Fin. Corp., No. 22-1042, 2023 WL 3635077, 2023 U.S. App. LEXIS 12899, (2d Cir. May 25, 2023) (unpublished opinion), the Second Circuit upheld the dismissal of borrowers' second amended complaint for failure to state a claim in accordance with Fed. R. Civ. P.12(b)(6). The court dismissed the borrowers' first claim, alleging the loan servicer violated RESPA requirements, for two reasons. First, the "reasonable investigation" that the borrowers claimed the servicer failed to conduct was not actionable under RESPA. Second, the Second Circuit concluded that even if the claim were actionable, the borrowers failed to plausibly allege that a reasonable investigation had not been conducted. The borrowers' second and third claims, which relied on provisions of FDCPA, were dismissed for failure to state a claim for relief. The Second Circuit noted that a distinction must be made between those collecting on a defaulted debt and those who are seeking collection on a debt owed the FDCPA only governs the former. The borrowers' debt was not in default because they were up to date on payments as provided by the forbearance agreement; therefore, the borrowers failed to plausibly allege that the servicer was a debt collector under the FDCPA.

By Kristin Meurer krmeurer@ttu.edu
Edited By Melissa Hightower mehighto@ttu.edu
Edited By Ashley Boyce ashboyce@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.