NORTH DAKOTA BANKERS ASSOCIATION

LEGAL UPDATE

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BANKRUPTCY

Let's Get to the Core of Bankruptcy and District Courts' Core Jurisdiction [5TH CIR]

Multiple groups of lessors filed class action suits against an energy corporation (the debtor) for underpaying natural gas royalties. Before the parties could settle, the debtor filed for voluntary Chapter 11 relief. As per the reorganization plan (the plan), interested parties had to file a proof of claim to receive monetary compensation on their prepetition claims. Out of the 23,000 lessors that were part of the class action suits, only 161 filed a timely proof of claim. After initiating bankruptcy proceedings, the debtor settled its prepetition class action suits and moved to get preliminary approval for the settlements from the bankruptcy court. Notably, all 23,000 leaseholders would receive compensation, even though almost all did not file a proof of claim. The lessors that filed proof of claims opposed the motion claiming the bankruptcy court did not have jurisdiction to approve the settlement. The court concluded they had 'core' jurisdiction over the settlements because: (1) approving the settlement was in the debtor's best interest, and (2) since at least some lessors filed a proof of claim, it bootstrapped all others into the court's power. The court overruled the lessors' objection, and upon appeal, the district court affirmed the bankruptcy court's decision. The lessors appealed to the Fifth Circuit.

In RDNJ Trowbridge v. Chesapeake Energy Corp. (In Re Chesapeake Energy Corp.), 70 F.4th 273 (5th Cir. 2023), the appellate court explained that once a bankruptcy court approves a Chapter 11 reorganization plan, their jurisdiction is limited to certain matters that fall within their core responsibilities such as the implementation or execution of the plan or, interpreting the terms of the plan. Outside of those duties, their jurisdiction ceases to exist. The court held that since almost all of the lessors failed to file in a timely manner and because the plan specifically excluded them from making any claims after the claims bar date, allowing the settlement would completely disregard the reorganization process created by the plan. The assertion that 161 lessors preserved the rights of the 23,000 would "not fly." The court also examined allowing the settlements via post-confirmation bankruptcy jurisdiction. To have jurisdiction, a bankruptcy court must pass a three-factor test outlined by Craig's Stores. First, does the issue "principally deal with post confirmation relations?" In this case, they did not because the settlements came before the bankruptcy, meaning this factor was against jurisdiction. Second, was there "antagonism or [a] claim pending between the parties as of the date of the reorganization?" Here, there were antagonistic relations at the date of reorganization. However, they did not survive bankruptcy proceedings because almost all the class members did not file a proof of claim and could not pursue monetary recovery. Finally, are there any "facts or laws deriving from the reorganization or the plan necessary to the claim?" Nothing in the plan was contingent on the decision of the class action lawsuits. The rulings in those cases would not affect the "implementation or execution of the plan." Thus, the court held that the bankruptcy court had no jurisdiction to decide the settlements. By Ehsan Ali ehali@ttu.edu. Edited By Joshua Shetler joshua.shetler@ttu.edu and Ashley Boyce ashboyce@ttu.edu.

Creditors Failed to Establish Bad Faith and "Cause" to Dismiss Debtor's Chapter 13 Case [BKR ED MI]

This bankruptcy case arose from a separate probate litigation in which the debtor filed for Chapter 13 Bankruptcy with a case pending. Subsequently, the co-trustees of a property trust (the creditors) filed a motion for relief from stay to continue with their litigation against the debtor that was pending in Arizona state court. The bankruptcy court granted the motion because, in the court's view, it found that debtor responsible for impermissibly forum shopping. The debtor filed this bankruptcy case soon after the Arizona Probate Court ruled against the debtor on several issues in a decision granting partial summary judgment for the creditors. Only five days after the court granted the relief from

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stay, the creditors filed a motion to dismiss the bankruptcy case under Bankruptcy Code § 1307(c). The creditors cited the debtor's alleged forum shopping to support the assertion that the debtor filed the case in bad faith.

In In re Cattron, 648 B.R. 191 (Bankr. E.D. Mich. 2023), the bankruptcy court held that the debtor did not act in bad faith and denied the creditors' motion to dismiss. The court went through several steps in coming to its conclusion. First, in considering all the circumstances, the court reviewed the twelve Alt factors to determine whether the debtor's plan had been proposed in good faith. However, the court emphasized that it must keep in mind that other conceivable factors outside of the non-exhaustive list of Alt factors could be relevant when analyzing a particular debtor's good faith. Second, the court found that since the debtor owed at least nine additional creditors money, the debtor still had a legitimate reason to file for bankruptcy beyond shopping for a more favorable forum. The court stated that the stay relief obviated the need to dismiss the bankruptcy case and remedy the forum shopping problem. Next, the court held that the creditors failed to demonstrate how they would be prejudiced by proceeding with the debtor's bankruptcy case. The court also attributed the effect of the pending probate court matter in the debtor's favor through reasoning that the indefiniteness provided sufficient justification for the inaccuracies and incompleteness which the creditors alleged. After consideration of the twelve Alt factors, the court found that the creditor did not show that the debtor filed this bankruptcy case in bad faith. Lastly, the court found that the debtor's filing of this Chapter 13 Bankruptcy was not done in bad faith and that there was no "cause" to dismiss this case under 1307(c). Nor was there any valid basis to grant the creditors' request for an award of any monetary sanctions, such as attorney fees and costs. Accordingly, the court denied the creditors' motion in its entirety. By Rodger Advincula radvincu@ttu.edu Edited By Elija Benzvi elbenzvi@ttu.edu and Riley Carwayrcaray@ttu.edu.

Preliminary Injunctions in Consideration of Chapter 1l [BKR ND IL]

This case involved an LLC (the debtor) and a high-end car dealership (the tenant), both wholly owned by two brothers (the shareholders). Around fifteen years ago, the debtor borrowed two million dollars from a bank and provided real property as collateral. This property is the same one out of which the tenant operated. Notably, the only source of income for the debtor was the tenant's rent, which covered the mortgage payments that the debtor owed the bank. When the tenant later became unable to pay rent, the mortgage fell into default, and the bank sought to foreclose its mortgage on the property. The debtor later filed for bankruptcy under Chapter 11 and sought a preliminary injunction to halt efforts by the bank in enforcing a deficiency judgment against the shareholders and the tenant.

In 1600 Hick Rd. LLC v. EH Nat'l Bank (In Re 1600 Hicks Rd. LLC), 649 B.R. 172 (Bankr. N.D. Ill. 2023), The U.S. Bankruptcy Court granted the debtor's requested preliminary injunction. The court noted that the fate of the tenant and the debtor were linked. If the court declined to enter the injunction, the rent available to fund the debtor's reorganization would be in jeopardy. If this were the case, the real property would not be available for the tenant to run and operate. The court also recognized Chapter 11's primary concern of allowing debtors to reorganize and restructure their debts in order to revive their businesses. Entering the requested preliminary injunction would pause the collection of the deficiency judgment while the debtor started reorganizing, benefiting all parties and promoting an overall settlement. Without the injunction, the debtor could suffer irreparable harm by failing to collect rent, resulting in a failed Chapter 11 reorganization. Finally, the court noted that the bank would delay collecting their debt, but this would only be the case until the confirmation hearing, similar to any creditor involved in a Chapter 11 case. By Destiny Pemberton depember@ttu.edu.

Unsurprisingly, A Lack of Evidence Regarding Fraud and Misrepresentation Prevents the Non-Discharge of Debt [BKR D CO]

The debtor filed for bankruptcy which discharged the majority of her debts. However, the creditor moved to prevent the discharge of two liabilities due to alleged fraud. The creditor sued the debtor as an individual who also owned part of a company with whom the creditor had done business. Both the creditor and debtor worked in real estate, specifically, the repair and subsequent sale of homes. The creditor issued two loans, an earnest money, loan (loan 1), and an additional loan (loan 2), both intended for a specific property (property 1). The creditor wired loan 1 to the debtor's business partner (partner) without obtaining a loan application from either the debtor, or the partner, reviewing financials of the individual debtor or the shared company, and without first obtaining a signed promissory note or other documentation. After sending the money, the creditor sent a promissory note to the debtor and the partner which they signed a few days later. A mortgage deed on property1 supposedly secured the note, but the debtor did not yet own the property. The creditor disbursed loan 2 to the company's bank account after the debtor (through the company he shared with her partner) had secured a contract on property 1. Once again, the creditor did not review any financials or obtain a signed note before wiring the funds, The

creditor sent a not after the funds had disbursed, but neither the company, the debtor, nor her partner signed the note. This note also purported to be secured by a mortgage deed on property 1. Later, the company terminated the contract for property 1 and the company went under contract for a new property (property 2). Instead of calling the funds due, the creditor allowed the funds to be contributed to property 2. However, the creditor did not update the documentation. The debtor, her partner, and their company failed. to restore property 2 and ultimately filed for bankruptcy. The creditor then claimed the two loans should not be discharged due to misrepresentations, false pretenses, and fraud under 11 U.S.C. § 523(a)(2)(A).

In Together Real Estate Holdings, LLC v. Roberts (In re Roberts), No. 21-16000, 2023 WL 2565721, 2023 Bankr. LEXIS 705 (Ban.kr. D. Co. Mar. 17, 2023) (opinion not yet released for publication), the court held that the debtor's obligations to the creditor did, not qualify for nondischargability because the creditor did not prove any misrepresentations, false pretenses, or fraud on the debtor's part. The court explained that a two-part test must be conducted to determine if a debt will not be dischargeable. First, the debt must be shown to be valid. Second, the debt must have been obtained by misrepresentation, false pretenses, or fraud according to 11 U.S.C. § 523. If these two parts cannot be met, the debt must be discharged. The court reasoned that loan 1 was dischargeable because the creditor did not show any fraud by the debtor. The court explained that the creditor's failure to obtain any guarantees from the debtor negated any claim that the debtor may have entered into the contract with the intention of cheating the creditor. Further, the creditor knew prior to sending any money that the debtor did not own the land secured by the note. Thus, the creditor could not claim it was falsely led into making the loan on the property. Next, the court found loan 2 to be dischargeable as the creditor failed to meet the first prong of the test. The debt could not be established as valid against the debtor because the creditor issued the note to the debtor's company not the debtor in her personal capacity and the note claimed to be secured by a property in which the company had no ownership. The creditor alternatively argued the debtor was liable for loan 2 because she guaranteed the loan, but the court ignored this contention because the debtor refused to sign the proposed draft guaranty. By Maycee Redfearn maredfea@ttu.edu. Edited By Melissa Hightower mehighto@ttu.edu.

CONTRACTS

Big Bite out of Big Apple: Bank Pays Depositors Settlement Agreement and Attorney's Fees [SD NY]

Depositors brought a suit against the bank for allegedly unauthorized transfers from the depositors' accounts. The bank requested a settlement conference scheduled with the depositors, stating it would rather resolve the matter prior to further litigation. The depositors refused unless the bank was willing to provide core documentation, asking the court to vacate the settlement referral. Eventually the depositors and the bank came to an agreement, which included payment to depositors for reasonable attorneys' fees and costs to be determined by the court. Depositors and their attorneys, prior to the settlement agreement, created a contingency arrangement which stipulated their attorney's firm would receive a third of any recovery up to the amount allegedly stolen from their account, and forty percent of any recovery greater than that amount. Depositors filed a motion to the court after the settlement agreement seeking an order fixing the amount to be awarded for their attorney's fees and costs. The bank claimed because of the contingency agreement the depositors had made with their attorneys, the fee award should be greatly reduced. The court, however, denied this contention. The court awarded attorneys' fees and cost, separate from the settlement award.

In White v. Apple Bank for Sav., No. 1:22- CV-04481 (SDA), 2023 WL 2242498, 2023 U.S. Dist. LEXIS 32296 (S.D.N.Y. Feb. 27, 2023) (opinion not yet released for publication), the district court held that parties may agree by contract to permit recovery of attorney's fees and that the settlement agreement demonstrated the bank would pay the depositors' reasonable attorneys' fees and costs. The bank attempted to draw a distinction that the contingency arrangement should greatly reduce the fee award, which was met with rejection by the court. The court reasoned that the fee award and the contingency agreement the depositors had with their attorneys were two different matters. The contingency agreement only stipulated that the attorneys would receive one third of any recovery up to the amount allegedly stolen from the depositors and up to forty percent of any recovery greater than that amount. The attorneys' fees on the other hand were to be paid regardless of the outcome of the case, as they were not part of the contingency arrangement. The court further supported its idea stating, an award for attorneys' fees to be paid by the other party does not define the fee the plaintiff must pay his attorney according to their fee arrangement. This means the depositors attorneys' fees could be larger than the amount awarded to the depositors. Therefore, the bank could not reduce the amount awarded for reasonable attorney fees and costs based on the

contingency agreement the depositors had arranged with their counsel. By Samuel Banks Samuel.banks@ttu.edu. Edited By Melissa Hightower mehighto@ttu.edu and Peter Benson pebenson@ttu.edu.

No Contractual Duty of Notice or Good Faith if the Accused Party is a Beneficiary, But Not a Party to the Contract [BKR D CT]

Two debtors experienced massive pasta sales and, to increase production of pasta, secured a loan from the lenders to pay the construction company to build a state-of-the-art facility. The debtors and the lenders executed a credit agreement to this effect, and a mortgage on the debtors' properties secured the loan. However, due to the loss of a $30 million dollar contract and COVID-19, the debtors defaulted both on their loan and in paying the construction company. The construction company executed a mechanics lien for the debt owed. One of the debtors and the construction company executed a consent agreement which subordinated the mechanics lien to the lenders' mortgage. The debtors entered into bankruptcy under Chapter 11. The construction company sued the lenders to establish its priority in the proceeds from the judicial sale of the debtors' properties. In cross motions for summary judgment, the parties disputed whether the lenders were required to give the construction company notice of the debtors' default on the loan. The construction company contended that the subordination of the mechanic's lien was unenforceable without this notice. In contrast, the lenders argued that the mechanics lien was invalid because the construction company did not give notice that the debtors defaulted under the construction contract.

In Dennis Eng'g Grp., LLC v. People's United Bank, NA (In re Old CP, Inc.), No. 21-20111 (JJT), 2023 WL 108132, 2023 Bankr. LEXIS 4 (Bankr. D. Conn. Jan. 4, 2023) (unpublished opinion), supplemented, No. 21-20111 (JJT), 2023 WL 2333276, 2023 Bankr. LEXIS 546 (Bankr. D. Conn. Mar. 2, 2023) (unpublished opinion), the bankruptcy court found that the lenders were not parties to the consent agreement subordinating the construction company's mechanics lien to the lender's mortgage. Therefore, the consent agreement failed to bind the lenders. Even if the lenders were bound by it, the court found that a plain reading of the credit agreement showed it did not require the lenders to give notice of default to the construction company. The court made clear that a non-party to a contract cannot be bound by it. In addition, the court rejected the construction company's claim that the lenders breached a duty of good faith and fair dealing because no such obligation could exist absent a contract. Further, the court rejected the construction company's claim that the lenders committed fraud, explaining there was no misrepresentation because the credit agreement made clear the lenders did not need to give notice. After dispensing with a standing issue, the court granted summary judgment in the lenders' favor on the validity of the subordination agreement because the construction company did not contest it. In a later supplemental opinion, the bankruptcy court granted summary judgment in the 1enders' favor on the validity of the mechanic's lien. By Wyatt Macfarlane wmacfarl@ttu.edu. Edited By Melissa Hightower mehighto@ttu.edu and Peter Benson pebenson@ttu.edu.

CONSUMER FINANCIAL PROTECTION BUREAU (CFPB)

Yes, CFPB, You Have to Play by the Rules, Too! [11TH CIR]

The Consumer Financial Protection Bureau (the agency) investigated the unlawful practices of debt collection and discovered that several service companies assisted debt collectors in fraudulent collection efforts. The service providers allegedly gave "substantial assistance" by providing telephone payment processing services to the debt collectors. The agency filed a claim against service providers for violating the Consumer Financial Protection Act and the Fair Debt Collection Practices Act. The agency alleges that the service providers knew or should have known of the fraud being committed through their platforms. The claim was brought before the United States District Court for the Northern District of Georgia, however, the case did not move past the pre-trial process. The agency consistently obstructed the service provider's efforts to conduct a meaningful deposition by asserting numerous work-product protections and instructing the deposition witness to read exorbitant amounts of pages from memory aids to answer questions. Despite warnings from the district court, the agency employed the same tactics in the subsequent depositions. The service providers moved the court to grant sanctions and strike the claims against them for the agency's improper· discovery practices.

In Consumer Fin. Prot. Bureau v. Brown, 69 F.4th 1321 (11th Cir. 2023),· the 11th Circuit upheld the district court's hefty sanctions against the agency. The court rebuked the discovery abuses of the agency and "staunchly disagree[d]" with arguments that the service providers were not prejudiced by their tactics. The lengthy record of the agency's obstructionist behavior spoke for itself. The agency's tactics undermined the purpose of discovery and relegated the process to mere document production. The court reasoned that while dismissal may be a severe sanction, the district court retained the discretion to dismiss a complaint where the party's conduct amounts to flagrant disregard and willful disobedience of the court's discovery orders. The court

issued a final scathing remark that the agency "does not have the power to decide which discovery rules it will abide by and which it will ignore." The court found the agency's conduct sufficient to impose the severest of sanctions and affirmed the district court's decision to dismiss the claims against the service providers. By Hayden Mariott hayden.mariott@ttu.edu. Edited By Elijah Benzvi elbenzvi@ttu.edu and Riley Caraway rcaraway@ttu.edu.

FAIR CREDIT REPORTING ACT (FCRA)

Apparently, a Not So Fair Act: The Fair Credit Reporting Act's Timing and Reasonable Investigations [11TH CIR]

An employee of the consumer fraudulently opened a credit card in the consumer's name with the bank. For this card, the employee set up the account so that the consumer was the owner, and the employee was an authorized user. For three years, the employee ran up payments on the card from the consumer's business account without any knowledge of the consumer. The consumer discovered the fraud and alerted the bank. Meanwhile, the employee pled guilty to several crimes arising out of the incident. The bank conducted a fraud investigation but found that, since bank accounts owned by the consumer had paid for the card, the consumer had given the employee apparent authority to use the card. Thus, the bank concluded the consumer was liable for the charges despite the employee's fraud. Over the course of two and a half years, the consumer filed several disputes with credit reporting agencies who alerted the bank of the disputes. Under the Fair Credit Reporting Act (FRCA), the bank, as a furnisher, had the duty to conduct a reasonable investigation upon receiving each dispute. Each time, the bank investigated and reaffirmed its finding that the consumer was liable for the charges. The consumer filed suit under the FRCA asserting that the bank had conducted unreasonable investigations of her disputes. The bank moved to dismiss the suit for violating the two-year statute of limitations, but the district court denied that motion. The bank and the consumer then cross-motioned for summary judgement. The district court granted the bank's motion and denied the consumer's motion. The consumer appealed.

In Milgram v. Chase Bank USA, N.A., 72 F.4th 1212 (11th Cir. 2023), the appellate court affirmed the district court's grant of summary judgment in favor of the bank. First, the court held the consumer's suit was within the statute of limitations because an unreasonable investigation, not the underlying dispute, triggers the FRCA's time limitation. In other words, each time a consumer files a dispute, the FRCA requires the furnisher to conduct a new investigation, and because any investigation can be unreasonable, a separate statute of limitations runs for each investigation. Second, the court held the consumer had failed to prove the bank's investigation was unreasonable because the bank's apparent authority argument persuaded the court. To establish apparent authority, a litigant must show: (1) a representation by the purported principal, (2) reliance on that representation by a third party, and (3) a change in position by the third party in reliance on the representation. Because the consumer's bank accounts had consistently paid off the credit card, and because the employee was an authorized user on the card, the court found the bank had reasonably determined that the consumer had vested the employee with apparent authority. In reliance on that determination, the bank "paid money to third-party vendors" thus satisfying the third and final element of apparent authority. The court ruled the bank's awareness of the employee's criminal convictions was immaterial to the apparent authority analysis the bank's knowledge of the convictions "proved only that [the employee] lacked actual authority." Ultimately, the court concluded the consumer failed to show a genuine dispute of material fact whether the bank's investigation was unreasonable as a matter of law. By Marcus Braymer mbraymer@ttu.edu Edited By Elijah Benzvi elbenzvi@ttu.edu and Peter Benson pebenson@ttu.edu.

ELECTRONIC FUND TRANSFER ACT (EFTA)

*Banking on Blame: Legal Clashes Between Businesses and Banks [ND TX]

An entity imported and sold groceries. The account held by the entity at a primary bank was hacked and a considerable amount of funds was wired to a secondary bank. The primary bank froze the entity's account and asked the secondary bank to do the same. The secondary bank failed to place a hold on the funds stolen from the entity's account. Subsequently, the hacker transferred the money out of the secondary bank. In response to the incident, the entity filed suit against both banks in hope of recovering its funds. The entity asserted common law claims for negligence and breach of contract against both banks. Additionally , the entity asserted an Article 4A claim against the primary bank and an Electronic Fund Transfers Act (EFTA) claim against the secondary bank. The banks moved to dismiss the claims filed by the entity under Federal Rule of Civil Procedure f2(b)(6). The court examined the entity's claims in light of the banks' motions.

In Grainmarket, LLC v. PNC Bank, N.A., No. 3:22 CV-2419-X, 2023 WL 4162278, 2023 U.S. Dist. LEXIS 1108588 (N.D.T.X. June 23, 2023) (opinion not yet released for publication), the court ruled to dismiss with prejudice the common law claims against both banks and the EFTA claim against the secondary bank. The court also ruled to dismiss, without prejudice, the Article 4A claim against the primary bank. The court stated that

the Texas Business and Commerce Code § 4A supersedes the common law, making the entity's claims based on common law entirely ineffective. The entity's EFTA claim was also entirely ineffective because the EFTA applies to personal bank accounts, not business bank accounts. Lastly, the court found the entity's claim against the primary bank to be conclusory and lacking in plausibility and thus failed to meet the requirements of l 2(b)(6). For these reasons, the court granted the banks' motions for dismiss. By Emily Robins rob32267@ttu.edu. Edited By Joshua Shetler joshua.shetler@ttu.edu and Ashley Boyce ashboyce@ttu.edu.

Cryptocurrencies are "Funds" within Meaning of EFTA as Crypto Class Action Survives Motion to Dismiss (Although Not Unscathed) [SD NY]

Users of a cryptocurrency exchange took issue with the exchange's two-factor authentication process ("2FA"). failing to deter unauthorized log-in attempts effectively. The process which was mandatory upon creating an account, required a user to verify-their identity through a unique code sent to a separate device of their choosing. The user would then type the code into the log-in page, giving the user access to their account. This security measure was intended to ward off intruders who had access to a user's email and/or password, as the account can only be accessed by an individual who also had access to the verification device. Current and former users brought a putative class action against the cryptocurrency exchange and its former CEO, alleging that the exchange failed to implement 2FA correctly, which then allowed intruders to gain access to user accounts by adding a new verification device with only the user's email address and password. The users further allege that the exchange misrepresented the scope of their security features by stating their compliance with the Payment Card Industry Security Standards Council and claims of year-round security monitoring. As a result of the exchange's failures, the users lost their cryptocurrency savings and personal and financial information stored in their accounts. Thus, the users asserted nine causes of action, including one federal claim of an alleged violation of the Electronic Fund Transfer Act ("EFTA") and eight state claims, including deceptive business practices, breach of contract, breach of express and implied warranty, negligence, gross negligence, unjust enrichment, negligence per se, and negligent misrepresentation. The exchange moved to dismiss all nine for failure to state a claim.

In Rider v. Uphold HQ Inc., No. 22cv1602 (DLC), 2023 WL 2163208, 2023 U.S. Dist. LEXIS 29617 (S.D.N.Y. Feb. 22, 2023) (opinion not yet released for publication), the district court denied the motion to dismiss the users' EFTA claim and part of the negligence per se claim pertaining to the EFTA violation. The court labeled the exchange as a financial institution under the EFTA, as it held an account belonging to a consumer, enabling users "to transfer, purchase, trade, hold, and sell various cryptocurrencies on its platform." The court acknowledged that the EFTA does not define "funds" explicitly and turned to Black's Law Dictionary, where it found that the nature of cryptocurrency's liquidity properly constituted "funds." Therefore, the court reasoned that the exchange's behavior was subject to the EFTA's applicable language towards the transfer of funds. The court dismissed the alleged deceptive business practices and breach of contract as conclusory and found no plausible linkage between the exchange and the users' claims. Further, the court dismissed the breach of express and implied warranty claim because such a claim is only valid for the sale of goods and held that the service aspect of the exchange predominated its alleged sale of cryptocurrency. Lastly, the court held the users' negligence, gross negligence, unjust enrichment, and negligent misrepresentation claims were duplicative due to the users' lack of identification of the exchange's violation of a legal duty independent of the contract. Accordingly, the court dismissed all state claims, dismissed the negligence per se claim in part, and denied the exchange's motion to dismiss the federal EFTA claim. By Jesse Castella cas72899@ttu.edu. Edited By Elijah Benzvi elbenzvi@ttu.edu and Riley Caraway rcaraway@ttu.edu.

Customer Failed to Timely Notify and Bring Claims for Unauthorized ATM Withdrawals [ED NY]

The customer, proceeding pro se, alleged that the broker's employee made several unauthorized withdrawals from the customer's bank accounts between June 2019 and 2021. The customer transferred a significant amount of severance pay in three separate installments from his brokerage account to his account at the bank. After this transfer, the broker's employee began stealing the customer's money through regular withdrawals from the same ATM multiple times a day. The customer opened two new accounts with the bank and transferred his money over from his original account. Allegedly, the broker's employee also stole from the new accounts by making withdrawals from an ATM multiple times a day. The customer contacted law enforcement but never notified the bank of the fraudulent withdrawals.

In Zarate v. Chase Bank, No. 22-CV-1178, 2023 WL 5956334, 2023 U.S. Dist. LEXIS 162612 (E.D.N.Y. Sept. 13, 2023) (opinion not yet released for publication), the court held that the customer's claims were timebarred under the Electronic Funds Transfer Act (EFTA) and Deposit Account Agreement (DAA). Under the EFTA, a customer must allege that (1) the relevant accounts "were demand deposit, savings deposit, or other asset accounts established primarily for personal, family, or

household purposes;" and (2) "the unauthorized electronic fund transfer was initiated through an electronic terminal, telephone, computer, or magnetic tape for the purpose of ordering, instructing, or authorizing a financial institution to debit or credit a consumer's account." Additionally, the customer must: 1) notify the bank within 60 days of an unauthorized transfer to the bank and 2) bring an EFTA claim within one year of the violation. Each individual transfer triggers its own one-year limitations period. The court concluded that because the customer brought this action more than two and a half years after the first allegedly unauthorized withdrawal, the customer's claim as to any unauthorized transfers during the 60-day notice period was barred by the EFTA's one-year statute of limitations. Further, the DAA included a statute of limitations provision and required a customer bringing an action against the bank to file the lawsuit "within two years after the cause of action arises, unless federal or state law or an applicable agreement provides for a shorter time." Accordingly, the court barred the customer from asserting a breach of contract claim under the DAA. Therefore, the court dismissed the complaint in part with prejudice and in part without prejudice, allowing the customer 30 days to amend his complaint. By Jace Brown jace.brown@ttu.edu. Edited By Elijah Benzvi elbenzvi@ttu.edu and Riley Caraway rcaraway@ttu.edu.

LENDING

Investor's Bad Faith and a Principal's Unfair Dealings [BKR SD TX]

A partnership created and operated an investment fund to finance a natural gas company (the debtor) owned and operated by the partnership. To invest in the fund, investors signed a contract acknowledging that a specific principal of the partnership (the "gent) had the power to act as an agent for the fund. Years later, both the partnership and the debtor became insolvent. The partnership sold all the debtor's assets, and the debtor filed for bankruptcy. The money from the asset's sale was supposed to pay the debtor's secured creditors; instead, the agent took $125 billion from the sale and funneled it as profits to the fund instead of paying the creditors. Upon discovering the fraudulent act, the debtor's bankruptcy trustee sued the fund investors seeking to recover the $125 billion. The investors maintained an affirmative defense of good faith, claiming they lacked knowledge of the agent's actions and did not consent to the agent's fraudulent dealings. The trustee moved for partial summary judgment, asking the court to deny the investors' good faith defense.

In Schmidt v. Nordlicht (In re Black Elk Energy Offshore Operations, LLC), 649 B.R. 249 (Bankr. S.D. Tex. 2023), the court explained that the determination as to whether the investors maintained good faith hinged on whether they were on inquiry notice. If they were on inquiry notice, the investors could riot maintain their affirmative defense of good faith. An agency inquiry notice determination consists of three elements: (1) whether the principal was the investor's agent; (2) whether, through agency, the principal imputed his knowledge to the investors; and (3) whether that knowledge would put the investors on notice. The court held that all three elements were satisfied: (1) the principal was the investor's agent because of the contract the investors signed; (2) basic agency law creates a legal fiction where the investors knew of their agent's actions, even if, in reality, they had no idea, as is the case here; and (3) this knowledge of the transfers initiated by the agent would have put the investors on inquiry notice, and by not beginning their inquiry, the investors maintained their imputed knowledge.

In their defense, the investors claimed that the agent acted adverse to the investor's interests and exceeded the scope of his authority. If either claim were proven true, it would stop imputing the agent's knowledge to the investors. In response, the court denied both arguments because the agent acted in the investors' best interest in funneling money to the fund and that the agent did not exceed his authority because his crimes were foreseeable given his job duties. All this intact, the investors could not maintain their good faith defense, and the court granted partial summary judgment. By Reagan Moser remoser@ttu.edu. Edited By Joshua Shetler joshua.shetler@ttu.edu and Ashley Boyce ashboyce@ttu.edu.

A Borrower Unsuccessfully Attempted to Hold a Lender Responsible for Defaulted Loans [WY]

The borrower was a longtime owner and operator of a cattle ranching operation in Wyoming. Amid rebuilding the operation following financial trouble, the borrower accumulated unpaid bills. To pay the bills, the borrower had applied for an agricultural loan from the lender, offering cattle as collateral. The lender originally denied her loan application due to the unpredictability of the cattle market. The borrower applied again and offered a house as additional collateral. The lender accepted her application and provided the borrower two loans to utilize to operate and grow her cattle ranch. Upon the lender's approval, the borrower acquired additional loans that she also used in the course of her ranching operation. The borrower's business ultimately failed, and she consequently defaulted on her loans. The lender foreclosed on the cattle that the borrower had pledged as collateral. The borrower filed suit against the lender alleging negligent lending and advising, breach of good faith and fair dealing, and breach of fiduciary duty. The lender filed a counterclaim alleging breach of contract and moved for summary judgment. The district court granted the lender's summary judgment motion and entered judgment in favor of the lender. The borrower appealed.

In Wilcox v. Sec. State Bank, 523 P.3d 277 (Wyo. 2023), the Supreme Court of Wyoming affirmed the district court and declined to recognize negligent lending or negligent advising as causes of action because they had not previously been recognized by the court. The court determined that the recognition of a negligent advising claim would result in the imposition of a non-contractual duty on the lender when advising clients. The Wyoming Banker's Association urged the court not to recognize the cause of action because of the negative effects that it would have on lenders and borrowers. Further, the court affirmed the district court's decision to grant summary judgment in favor of the lender on the good faith and fair dealing claim because the borrower failed to identify conduct or contractual text which would have indicated there was an "interference or failure to cooperate" by the lender. Although the court has recognized that a "lender can incur additional duties by conduct that creates a special or fiduciary relationship," the borrower failed to establish the extraordinary circumstances required to impose a fiduciary duty on the lender. Because the borrower clearly admitted that she owed the lender money and was not able to establish "any clear and definite promise" to loan her additional money, the court also affirmed the district court's determination that equitable defenses did not preclude the district court from granting summary judgment on the lender's breach of contract counterclaim'. By Megan Goracke mgoracke@ttu.edu. Edited By Melissa Hightower mehighto@ttu.edu and Peter Bensen pebenson@ttu.edu.

Do Not Offer Collateral on Your Sister's Loans [VT]

The debtor pledged his Merrill Lynch investment account as collateral to the bank who offered a business loan to his sister: The same day, the debtor signed a Commercial Pledge Agreement that defined the collateral as all the debtor's property "in the possession of, or subject to the control of" the bank or "in the possession of, or subject to the control of" a third party that reported to the bank. Additionally, the debtor signed a "Control Agreement and Acknowledge of Pledge and Security Interest" addressed to Merrill Lynch that stated he granted a security interest to the bank and asked Merrill Lynch to acknowledge this. Merrill Lynch never signed the control agreement. Despite this, the bank funded the loan to the debtor's sister. Subsequently, the sister defaulted on the loan, and the bank filed a complaint against her and the debtor. It also sought a preliminary injunction against the debtor to turn over the investment account to the bank. The trial court granted the injunction but instructed the debtor to set aside the money from the account "as security for the asserted debt." The debtor transferred the money to an escrow account controlled by his attorney. The debtor moved for summary judgement against the bank. The trial court granted summary judgement, holding that because the bank never possessed or controlled the investment account "as required by the plain language of the pledge agreement" due to the unsigned control agreement, the collateral never existed, and a security interest never attached under Article 9 of the Vermont Uniform Commercial Code (UCC). The bank appealed.

ln Berkshire Bank v. Kelly, 296 A.3d 742 (Vt. 2023), the Supreme Court of Vermont affirmed the judgement of the trial court, holding that the bank did not have a valid security interest in the investment account. The court concluded that the pledge agreement, written by the bank, unambiguously required the bank to have "possession of or control of" the debtor's account to create an enforceable security interest. Article 9 of the Vermont UCC provides that a secured interest in collateral attaches once it becomes enforceable against the debtor. This happens when value has been given at least one of four evidentiary conditions are satisfied, and the debtor has rights in the collateral or the power to transfer those rights to a third party. The bank gave value by making the loan and the debtor had rights to the Merrill Lynch account, but because the account was never in "possession of or subject to the control of" the bank, the court looked to the terms of the security agreement to establish the parties' intent. Under the plain language of the security agreement, collateralization was dependent on the bank's possession or control of the Merrill Lynch investment account. Because the bank never possessed or controlled the account, and because Merrill Lynch never signed the pledge agreement, the security interest never attached. The court stated the bank essentially did this to itself by including the condition of possession or control into the description of collateral. Additionally, the court held that the bank did not have possession of the collateral when the money was put into an escrow account because the debtor's attorney was not an agent of the bank and was, instead, an agent of the debtor. Thus, the trial court correctly granted summary judgement in favor of the debtor. By Hailey Kuykendall hkuykend@ttu.edu. Edited By Melissa Hightower mehighto@ttu.edu and Peter Benson pebenson@ttu.edu.

PIERCING THE CORPORATE VEIL

Conversion and the Corporate Veil: Can a Trustee Pierce the Corporate Veil When the Debtor Has Converted their Bankruptcy Filing? [BKR ED MI]

The creditor issued to the debtor's business a line of credit in the amount of $1,500,000 for the purpose of funding pawn loans offered by their shop. The debtor's trust, his mother and her trust guaranteed the line of credit. The trust held the debtor's ownership interest in the shop. The creditor perfected its security interest in the debtor's assets. The debtor's business began to experience financial issues and started borrowing funds from a

third party, unknown to the creditor. This arrangement between the debtor's business and the third party shifted when the two parties signed an Asset Purchase Agreement (APA), which allowed the debtor to assign loan assets without the consent of another party. Soon after, the debtor's business defaulted on their line of credit with the creditor, who proceeded to sue the debtor's business and its guarantors. In response, the debtor filed an individual Chapter 13 Bankruptcy. The debtor did not list the third party as a creditor, because the debtor did not guaranty the APA individually. Later, the Chapter 13 Bankruptcy converted to a Chapter 7 Bankruptcy, which revoked the debtor's trust and turned control of the debtor's business over to the trustee. Pursuant to its perfected security interest, the creditor received liquid funds from the debtor. The trustee subsequently sued in an attempt to "pierce the corporate veil," and to treat assets transferred by the debtor's business as assets part of the debtor's estate under an alter ego theory. Additionally, the trustee raised a conversion claim against the third party for conversion of the creditor's property.

In Evangelista v. Silver (In re Silver), 647 B.R. 897 (Bankr. E.D. Mich. 2022), the United States Bankruptcy Court for the Eastern District of Michigan held that the trustee could not "pierce the corporate veil" in order to treat assets transferred from the debtor's pawn shop as part of the debtor's estate and that an alter ego claim could not be asserted against the singular shareholder of a company. Citing 11 U.S.C.S. § 544 and Mich. Comp. Laws § 566.34, the court reasoned ownership of the assets could not be consolidated under a piercing the corporate veil theory because the debtor neither had "a transferred interest in the property" nor could defraud himself in any legal sense. Michigan law decides the alter ego theory, which states "that veil piercing does not transform the alter ego's property into the property of the debtor, but rather simply allows a creditor to pursue the alter ego under a vicarious liability theory." Additionally, the court held the third party liable for conversion of the debtor's collateral because the creditor had a valid security interest in the collateral which the court classified as chattel paper. Citing Mich. Comp. Law. § 440.9330(2), the court explained that, because the third party did take possession of the debtor's loan in the ordinary course of business, the creditor's interest in the collateral had priority over that of the third party. The court systematically dispensed with the thirdparty's other arguments that the conversion claim should fail. By Oleg Perry operry@ttu.edu. Edited By Melissa Hightower mehighto@ttu.edu and Peter Benson pebenson@ttu.edu.

SECURITY INTERESTS

Caught Between a Rock and a Debtor's Place [SD NY]

A New York limited liability corporation (the debtor) borrowed a large sum of money to purchase a diagnostic imaging business. In order to secure the loan, the debtor and four guarantors pledged collateral; notably, one of the four guarantors acted as the sole representative for all the guarantors and signed on their behalf. Within a month, the borrower properly perfected the security interest. Two years later, the debtor failed to make payments for three consecutive months, and the lender filed suit seeking the pledged collateral; however, one of the supposed guarantors claimed they did not, in fact, sign anything guaranteeing the loan and denied giving authority to the signing guarantor. After some time for discovery, the disputed guarantor produced evidence contrary to the facts supplied by the debtor, showing that they had not authorized the signing guarantor to act as their representative. The lender moved for summary judgment on the breach of contract, foreclosure of security interest, and breach of guaranties claims.

In Bank of Am., N.A. v. Third Ave. Imaging LLC, No. 21-CV-0520 l (VB), 2023 WL 3818549, 2023 U.S. Dist. LEXIS 97568 (S.D.N.Y June 5, 2023) (opinion not yet released for publication), the court granted summary judgment on the breach of contract claim and summary judgment in part on the foreclosure of security interest claim and breach of guaranties claims. New York law for breach of contract states there must be four elements met to show a breach. First is an agreement, which was clear upon the facts that the borrower had contracted with the lender. Second is performance by the lender, which the facts showed the lender provided adequately. Third is a breach by the borrower, this being indicated clearly by the lack of payment by the borrower for three months. The last required element is damages, which the lender showed as the entirety of the unpaid loan and any interest on it. Breach of contract elements satisfied; the court granted summary judgment on the breach of contract claim. However, the court granted summary judgment in part on the remaining claims. The claims as to the disputed guarantor were denied because the evidence clearly showed a reasonable jury could conclude that the disputed guarantor did not authorize any collateral pledge. For the other guarantors, the court granted the claims because the borrower properly perfected their security interest. By Blaine Kaplani bkaplani@ttu.edu. Edited By Joshua Shetler joshua.shetler@ttu.edu and Ashley Boyce ashboyce@ttu.edu.

Cross Your T(s), Dot Your I(s), and File Security Interest Notices in the State of Title [BKR D KS]

The creditor obtained a security interest in a vehicle with a California title owned by the debtor. The creditor filed a notice of security interest in Kansas, the resident state of the debtor. Later, the debtor declared bankruptcy under Chapter 7, and the creditor attempted to retain its security interest in the vehicle. The Chapter 7 trustee (the trustee) filed an adversary proceeding against the creditor, attempting to avoid the security interest under 11 U.S.C. § 544(a)(l), which gives the trustee power to "avoid any security interest that would be voidable by a creditor who obtained a judicial lien on the petition date." The rights of the aforementioned creditor are determined via state law. The trustee subsequently filed a motion for summary judgment on their claim.

In Hamilton v. Glob. Lending Servs., LLC (In Re Williams), Nos. 22-06041, 21-21115, 2023 Bankr. LEXIS 1194 (Bankr. D. Kan. Apr. 28, 2023) (opinion not yet released for publication), the Bankruptcy Court ruled in favor of the trustee, granting the motion for summary judgment to avoid the creditor's secured interest in the vehicle. Citing Kansas statute, the court determined the local law of the title state controls. The title state of the vehicle being California, § 6301 of the California Vehicle Code (the CVC) ultimately "governs perfection, the effect of perfection..., and the priority of security interests in this dispute." The CVC dictates that the creditor must record their vehicle security interest in California to perfect it. Because the creditor recorded the interest in Kansas and not California, it went unperfected. Finally, the California Commercial Code dictates that an "unperfected security interest is subordinate to the rights of a [trustee]." Giving the trustee power to avoid the creditor's security interest on behalf of the bankruptcy estate. By Brendan Carter brendanc@ttu.edu. Edited By Joshua Shetler joshua.shetler@ttu.edu and Ashley Boyce ashboyce@ttu.edu.

SUMMARY JUDGMENT

Motions for Summary Judgment for Matters of Fraudulent Intent of a Debtor [BKR WD OK]

The debtor's business obtained two loans from the bank, personally guaranteed by the debtor and secured by a first priority security interest in the business's inventory, accounts, general intangibles, and equipment. The bank alleged that the debtor (1) represented that the bank would hold a first priority security interest on the business's collateral (after the debtor used the loans obtained to pay off all outstanding loans owed to another bank (the creditor) and (2) provided personal financial statements that failed to disclose pre-existing liabilities to the creditor. As a result of the fraudulent disclosures, the bank could only secure a lower-priority lien on the business's collateral. During the debtor's bankruptcy proceedings, the bank filed an adversary proceeding claiming the debtor could not discharge the bank's loans because the debtor obtained them on false pretenses. The debtor filed a motion for summary judgment (the motion) in which he sought an order dismissing the bank's complaint. In the motion, the debtor asserted that his debt was dischargeable. Moreover, the debtor denied that he committed fraud to obtain the loan and asserted that he made no financial misrepresentations. The bank failed to file a response to the debtor's motion.

In First Nat'l Bank & Tr. Co. Weatherford v. Hobbs (In Re Hobbs), No. 22-10330-JDL, 2023 WL 368932, 2023 Bankr. LEXIS 1396 (Bankr. W.D. Okla. May 26, 2023) (opinion not yet released for publication), the court denied the debtor's motion. The. court explained that the Bankruptcy Code provides that a debtor may not be discharged from any debt if the debtor obtained that debt via intentional use of a written statement that falsely represents the debtor's financial situation to a creditor. Here, the debtor failed to demonstrate that he was legally entitled to summary judgment because he only provided conclusory opinions in his motion. Further, the court clarified that for issues of intent-in this case fraudulent intent-- summary judgment is generally not a sufficient resolution as it involves questions regarding a party's intent or state of mind which are issues best left for a fact finder. While the debtor provided statements denying fraudulent intent as evidence to support his motion, the court clarified that these statements were not equivalent to affidavits, and it could not consider them when ruling for summary judgment. By Kristin Meurer krrneurer@ttu.edu. Edited by Joshua Shetler, joshua.shetler@ttu.edu and 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.