NORTH DAKOTA BANKERS ASSOCIATION

LEGAL UPDATE

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# BANKRUPTCY

## The Provisions of a Confirmed Plan Bind the Debtor and Any Creditor [5th Cir.]

A grocery store went bankrupt. One of the store's creditors filed a proof of claim for $325,000, the balance on a loan it had made to the grocery. In the debtors' Chapter 11 plan, the bankruptcy court awarded the creditor the grocery store and the land on which it was located. The court assessed the value of the property at $225,000 and reduced the outstanding balance on the loan to $100,000. The couple who owned the grocery business had guaranteed the loan, so they remained liable for the remaining balance. The bankruptcy plan provided that the couple would make monthly payments toward the remaining $100,000 debt and would be entitled to a partial release of liability for the loan. The couple filed for personal bankruptcy after the store's bankruptcy case ended and the creditor again filed a proof of claim for the entire debt and accrued interest. The creditor claimed that the $225,000 credit against the loan should not apply in the debtors' personal bankruptcy because the store had not yet been transferred. The creditor further claimed that the grocery store had declined in value after the first bankruptcy. The couple objected and claimed that the creditor was bound by the provisions of the first bankruptcy plan, including the $225,000 credit and partial release of liability. The bankruptcy court disagreed with the creditor and held that the first bankruptcy plan had bound the creditor in later proceedings involving the same debt, even before the assets are transferred. The district court upheld the decision of the bankruptcy court and found that because the extent of the debtors' personal liability had been addressed by the first bankruptcy plan, res judicata barred the creditor from relitigating the issue in the debtors' second bankruptcy.

In NEW FALLS CORP. V. LAHAYE (IN RE LAHAYE), 17 F.4th 513 (5th Cir. 2021), the Fifth Circuit Court of Appeals affirmed the district court's decision and held that the creditor was bound by the provision of an LLC's confirmed bankruptcy plan, which required the creditor to accept a grocery store owned by the debtors in exchange for a fixed-value credit against the secured debt. The court also held that the creditor could not use the debtors' personal bankruptcy to relitigate the issues that had been decided in the confirmed bankruptcy plan. The court reasoned that under 11 U.S.C. § 1141(a), the provisions of a confirmed plan bind the debtor and any creditor. Also, courts have understood a confirmed bankruptcy plan to have a binding effect on subsequent proceedings involving the same debt. Thus, the provision under 11 U.S.C. § 1141(a) is a statutory bar to the re-litigation of the same issues or issues that should have been raised in the original bankruptcy plan. The court also reasoned that a bankruptcy plan can limit a creditor's claim against third-party guarantors, not by discharging the guaranty but by determining the source and value of payments to satisfy the guaranteed debt. The creditor argued that the debtors should remain personally responsible for the entire debt until the store is transferred. However, the court reasoned that after the confirmation of the first bankruptcy plan, the debtors surrendered the store and received a partial release of liability. The court noted that the confirmed plan permitted the creditor to pursue the property but nothing in the plan suggested that the debtors had to ensure that the creditor received the surrendered property. Also, any post-confirmation default in the debtors' performance would give rise to a new and separate claim against the debtors for noncompliance with the plan. The court also reasoned that while the court recognized that creditors are subjected to the risk that the debtor's assets may decrease in value before they are transferred, the court reasoned that creditors could also potentially benefit from the debtor's assets if the value increases after the confirmation order. The creditor argued that a bankruptcy plan could not bind a creditor with respect to its claims against third-party guarantors. However, the court reasoned that, based on the provision of 11 U.S.C. § 1141(a), the binding effect of a confirmed bankruptcy plan extends to third parties. Thus, the court held that the creditor was bound by the provision of the store's confirmed bankruptcy plan. By Love Osemwegie love.osemwegie@ttu.edu.

## Bank's Post-Petition Notation of Its Lien on a Vehicle's Certificate of Title is Avoidable as an Unauthorized Post Petition Transfer Under 11 U.S.C. § 549(a) [BKR D. Neb.]

The debtor purchased a vehicle less than one month before filing a Chapter 7 bankruptcy petition. The Bank of Dixon County financed the purchase in exchange for a security interest in the vehicle. However, the bank's lien was not noted on the vehicle's certificate of title until after the petition date. The Chapter 7 trustee filed a motion to avoid the bank's lien and recover all payments made by the debtor to the bank. The trustee asserted that the bank's post petition perfection of its lien was either a preferential transfer or an unauthorized post petition transfer. The bank claimed that Covid-19 restrictions prevented it from having its security interest noted on the title at an earlier date.

In OVERCASH V. BANK OF DIXON CNTY. (IN RE MATTES), No. BK21-80346-TLS, 2022 Bankr. LEXIS 1604 (Bankr. D. Neb. 2022), the bankruptcy court granted the trustee's motion for summary judgment and held that (i) the bank's post petition notation of its lien on the certificate of title was avoidable as an unauthorized post-petition transfer under 11 U.S.C. § 549(a); (ii) Neb. Rev. Stat. § 60-164(2) did not protect the bank and (iii) the lien was avoidable under 11 U.S.C. § 547. The court reasoned that the transfer occurred within 90 days before the petition date, on account of an antecedent debt, while the debtor was insolvent, and would enable the creditor to receive more than it would in a Chapter 7 liquidation. The court also reasoned that the Nebraska statute governing liens on motor vehicles, Neb. Rev. Stat.§ 60-164(2) did not change the result. This statute requires a lien to be noted on a vehicle's title certificate in order to be valid against other creditors. The statute also allows a purchase-money security interest (PMSI) in a vehicle to be perfected against the rights of judicial lien creditors and execution creditors when the lien attaches. However, if the lien is not noted on the title, the security agreement is not valid under this statute and the lien will not attach regardless of whether it is a PMSI or not. The bank argued that no post-petition transfer had been made because its security interest was a PMSI that attached and became perfected under the applicable statute. However, the court reasoned that the bank was an unsecured creditor, and its lien was avoidable. Under 11 U.S.C. § 549(a), a transfer, including a lien, may be avoided if: (1) the subject property was the property of the bankruptcy estate; (2) the property was transferred; (3) the transfer was made postpetition; and (4) the transfer was not authorized by the bankruptcy code or the bankruptcy court. The court noted that when a post-petition transfer is avoided, the trustee may recover from the transferee the value of the property transferred, in order to restore the bankruptcy estate to the position it would have been in if the transfer had not occurred. Thus, the court ordered the bank to remit to the trustee all payments made by the debtor on the vehicle, including interest. By Love Osemwegie love.osemwegie@ttu.edu.

## Only Bankruptcy Court Decides if a Judgment Can Be Discharged in Bankruptcy [BAP 7TH CIR]

The debtor and creditor divorced after a long period of marriage. The couple reconciled but did not remarry. When they separated for the second time, the wife sued the debtor for equitable relief in state court because the couple's failure to remarry foreclosed relief through divorce law. Arbitration yielded a judgment in the wife's favor. After losing on appeal to the Indiana state courts, the debtor filed for bankruptcy, claiming the money judgment of the creditor was subject to discharge in bankruptcy. The creditor filed an adversary proceeding complaint arguing the arbitrator's award had given her a property interest that was not dischargeable in bankruptcy. The bankruptcy court found for the creditor, but the district court reversed, finding for the debtor. The wife appealed.

In HARSHAW v. HARSHAW (IN RE HARSHAW), 26 F.4th 768 (B.A.P. 7th Cir. 2022), the appellate court affirmed the district court. The court reviewed three pertinent parts of the arbitration order in rendering its decision. First, that order awarded a specific monetary amount "plus post-judgment interest." The court held this language established a money judgment under Indiana precedent. It also reasoned that post-judgment interest applied only to money judgments and not to judgments creating property interests. Second, the order offered several suggestions on how the debtor could satisfy the judgment. One of these suggestions involved obtaining a Qualified Domestic Relations Order (QRDO) to oversee disbursal from the debtor's pension. The wife argued this language demonstrated the arbitrator's intent to award a property interest. Under the caselaw, an order creates a property interest if it specifies both the source of the funds to be used to satisfy the judgment and the manner and means of payment. In distinguishing prior caselaw, the court not only determined the order contained no property-division language but also held the arbitrator's suggestions merely established a list of options that left discretion to the debtor on how to pay the judgment. Although a QRDO would have created a property interest, the arbitrator did not require the debtor to obtain one. Third, the order read: "this judgment should not be dischargeable in bankruptcy." The court found this language unavailing because federal bankruptcy law, not the arbitrator, dictates whether a debt is dischargeable. In affirming the district court, the appellate court ruled the arbitration order awarded a money judgment dischargeable in bankruptcy rather than a property interest. By Peter Benson pebenson@ttu.edu.

# CONTRACT LAW

## Under Texas Law, the Court's Job in Interpreting a Written Contract is to Ascertain the Parties' Intent as Expressed in the Instrument [5th Cir.]

The parties in this case disagreed on what they had agreed to in their contract regarding where disputes are to be litigated. Both parties entered into the contract that contained a provision stating that "Any dispute arising out of or under this Agreement shall be brought before the district courts of Harris County Texas, situated in the city of Houston, unless mutually agreed otherwise this choice of forum provision shall not prevent either party from seeking injunctive relief with respect to a violation of intellectual property rights or confidentiality obligations in any appropriate jurisdiction." The plaintiff commenced suit against the defendant for misappropriation because defendant violated the agreement in developing computer programs by reverse engineering plaintiffs source code. Defendants then timely removed the action to a federal district court. Defendant moved to remand the action to state court relying on the choice of forum provision in the agreement. The district court remanded the suit to the state court, leading to the appeal by defendant.

In DYNAMIC CRM RECRUITING SOLS., L.L.C. v. UMA EDUC., INC., 31 F.4th 914 (5th Cir. 2022), the appellate court affirmed the district court's decision to remand the case to state court. The court first reviewed the district court's interpretation of the forum provision. The court considered the parties intent as expressed in the instrument by reading all parts of the contract together. Defendant's argument was that the contract's language does not indicate that Harris County district courts are the exclusive forum. The court disagreed with this argument, stating the contract uses the word "shall" in specifying where suits must be brought. This, in the court's opinion, was a mandatory word that evidenced the intent that the specified courts are the exclusive forum for actions brought. The court also held that the provision ends with "unless mutually agreed otherwise" and the parties were not in mutual agreement. The court also held that the second part of the provision doesn't help the defendant because it is not the party seeking injunctive relief. Thus, none of these exceptions were satisfied. For this reason, the appellate court affirmed the district court's decision to remand the case. By Samuel Ghirmay Samuel.ghirmay@ttu.edu.

## Option Agreements not Incorporated into Loan Files are not Enforceable and Bar Debtor's Claims for Equitable Interest [Bankr. Pa.]

Plaintiff and her husband owned their home, which was facing foreclosure. The plaintiff and defendant subsequently entered into an agreement to sell the property to the defendant and lease it back to the plaintiff and her husband for monthly payments with an option to repurchase the property. To finance the purchase, defendant secured a mortgage from Long Beach Mortgage. The defendant then refinanced the mortgage with Washington Mutual Bank, which later was acquired by JPMC from the FDIC. The defendant then defaulted on paying the mortgage, and a foreclosure judgment was entered in favor of JPMC. When JPMC acquired the note from the FDIC, there was no written agreement on file signed by Washington Mutual referencing the secret agreement made by the plaintiff agreeing to give the plaintiff and her husband an option to repurchase the property. The plaintiff filed a motion to invalidate the mortgage held by JPMC and recover title to the property. JPMC also filed a motion to dismiss for failure to state a claim upon which relief can be granted. The parties went back and forth amending their complaints and engaged in discovery. JPMC then filed an amended motion adding an affirmative defense based upon the D'Oench Duhme doctrine codified by 12 U.S.C. section 1823(e).

In (IN RE BOLGER) BOLGER v. MCCUSKER, 638 B.R. 709 (Bankr. E.D. Pa. 2022), the court granted summary judgement in favor of defendant bank based on its affirmative defense. The bankruptcy court accepted the facts as undisputed because the debtor failed to timely respond the amended motion. The court then considered the impact of the agreement in question that had been made by the plaintiff and original lender. The court concluded that under the definition of 12 U.S.C. § 1823(e) an agreement is "a condition that affects the payment of a note, including the truth of an express warranty..." The court further stated that writing, approval, and filing requirements then attach to the agreement. The reasoning behind this was that because the agreements affect the valuation of certain bank notes/loans, they have to be in writing and adequately filed in order for the FDIC to access them. As a result, the court concluded that because the agreement made between the plaintiff and original defendant affect the valuation of the mortgage note, it should have been in writing and signed by the bank financing the mortgage. As a result, plaintiff was barred from raising misrepresentation pertaining to the secret agreement. The court then examined the claims as a matter of law and granted summary judgment in favor of the defendant bank. By Samuel Ghirmay Samuel.Ghirmay@ttu.edu

# EFTA

## Banks Beware: Overdraft and Insufficient Fund Fee Terms May Not be As Unambiguous As You Think [N.D.N.Y.]

Plaintiffs filed a class action against Bank for Bank's practices including failure to comply with Federal Regulation E's Opt-In-Rule, assessing overdraft fees ("OD Fees") on Authorized, Positive, Purportedly Settle Negative Transactions ("APPSN Transactions"), assessing multiple insufficient fund fees ("NSF Fees") on electronic transactions or checks when they are reprocessed after being returned for insufficient funds, and problems with the operations of the Bank's software system meant to be used by consumers for electronic transactions, which in tum caused the consumers to incur multiple NSF fees and/or OD fees. Based on these allegations, Plaintiff asserted the following six causes of action against Bank: (l) breach of contract; (2) breach of the implied covenant of good faith and fair dealing; (3) unjust enrichment; (4) money had and received; (5) violation of the Electronic Fund Transfers Act ("EFTA" or "Regulation E"); and (6) violation of the New York General Business Law ("GBL") § 349. Thereafter, Bank filed a motion to dismiss all six claims for failure to sufficiently state claims of relief under Federal Rule of Civil Procedure ("FRCP") 12(b)(6). In response, Plaintiffs sought to amend their pleadings pursuant to FRCP 15, which permits parties to amend their pleadings when justice requires it.

In Livingston v. Trustco Bank, No. l:20-CV-1030, 2022 WL 798157 (N.D.N.Y., Mar. 16, 2022), the court denied the Bank's motion to dismiss with respect to Plaintiffs' breach of contract claims based on the allegations regarding OD fees on APPSN transactions and multiple NSF Fees on the same items while granting its motion to dismiss - with prejudice - Plaintiffs' claims for the breach of the implied covenant of good faith and fair dealing, unjust enrichment, money had and received, and the claim for violation of the EFTA. Additionally, the court dismissed Plaintiffs' claims without prejudice with respect to the breach of contract claims regarding the improper software upgrades. First, the court examined the Plaintiffs' pleadings on the OD and NSF fees on the APPSN transactions. It examined the overdraft disclosures and determined they were ambiguous because the Bank's use of the words "authorize" and "payment" conterminously. Because of this use of the terms, Plaintiffs' interpretation of the contract-that for debit card transactions there is no need for an OD fee-was reasonable, and accordingly, it denied Bank's motion to dismiss for failure to state a claim. Turning to the NSF Fees, Plaintiffs argued the last line of the Account Disclosure Notice conflicted with the Fee Schedule terms which provided the Bank could only charge a single NSF fee on a "per item" basis, rather than each time an item is presented. The use of the word "item" in both contracts made Plaintiffs' interpretation reasonable, and for that reason the Bank's motion to dismiss was denied. Second, the court examined the claims regarding the Mobile Banking Software. However, Plaintiffs' failure to reference specific account documents, or portions of the documents that the Bank allegedly breached in performing the upgrade failed the federal pleading requirements, and the claim was dismissed without prejudice. Third, the court examined the alternative breach of contract claims and dismissed them as duplicative, because neither the unjust enrichment claim-like the money had and received under New York Law-nor the claim for breach of the implied covenant of good faith and fair dealing alleged any facts that were independent of or separate from the breach of contract claim. Accordingly, the court dismissed the three claims with prejudice. Finally, the court examined the Plaintiffs' claim under Regulation E, and found that the Plaintiffs never alleged that they had entered into a Regulation E Opt-In contract, thus it could not state a claim for relief under ETFA. By Miguel Escobar; Miguesco@ttu.edu.

# EMPLOYMENT LAW

## *Employees Were Not Covered by the Highly Compensated Employee's Exception [5TH CIR]

Employees worked as field engineers to provide video camera services of wells in the oil and gas industry. While the employees were often the only representative of the employer in the field, an operations manager supervised the employees within the company. Although titled "field engineers," the employees were neither licensed as engineers nor did they have engineering degrees. The employees instead only received some on-the-job training. In their jobs, the employees took direction from a representative of the clients, called a "company man." Under the direction of the company man, the employees first assessed the clarity of the well water by dropping a coin into a sample to advise the client of the likely image quality of the videos. After doing so, the employees helped lower the camera into the well with the assistance of a wireline operator. Observing the images from a wireline truck alongside the company man and wireline operator, the employees then directed the wireline operator on the speed to descend the camera. When the camera reached the desired point, the employees explained the images to the company man and annotated the conditions into a log. The employees did not offer recommendations or solutions to issues depicted on screen.

Because the employer treated the employees as exempt from the overtime requirements of the FLSA, the employees' work hours were not precisely tracked. For this reason, the employees sued the employer for violation of the FLSA. Although the employer contended that the employees satisfied the Highly Compensated Employee (HCE) exemption, the district court held in favor of the employees. This appeal folowed.

In HOBBS v. EVO INC., 7 F.4th 241 (5th Cir. 2021), the court determined that the employees did not constitute HCEs for the purpose of the exemption for the following reasons. The FLSA requires an employer to provide overtime pay to employees who work more than forty hours per week unless an exemption applies. To qualify for the HCE exemption, the employer must show that the employee (1) receives at least $100,000 annual compensation; (2) regularly and customarily performs at least one of the exempt duties of an executive, administrative, or professional employee; and (3) has a primary duty of performing office or non-manual work. Because the employees' compensation satisfied the threshold amount, the court turned to the second requirement. A duty meets this standard if it (1) requires the employee to use independent discretion or judgment regarding "matters of significance"; or (2) is directly related to general business operations or management. For the former, an employee's decisions must not be the product of well-established standards or procedures. Although the employer first urged that the employees' decisions concerning camera setup and configuration of the equipment based on well conditions met this requirement, the employees based these decisions on guidelines provided by the employer, and deviated from these guidelines only with a manager's approval. Thus, these decisions lacked the requisite independent discretion. Next, the employer argued that the employees' interpretation or analysis of the video footage satisfied the standard because the employees based their judgments only on their on-the-job experience. However, these duties merely consisted of descriptions or interpretations of the conditions depicted on screen rather than recommendations for solutions to the conditions. Without the latter, these responsibilities could not meet the standard. Turning to the latter prong of the second HCE exemption requirement, the employer argued that the employees' duties related directly to management or general business operations because the employees performed the coin test to examine the clarity of the well fluid prior to filming. Although quality control is characterized as a qualifying duty under this prong, the test only ensured the quality of the employer's product-the images-rather than production. As explained by the court, "work that is primarily functional rather than conceptual does not meet the standard." Because the employer failed to demonstrate that the employees' duties properly met the second requirement of the HCE exemption, the court held that the employer violated the FLSA in failing to provide overtime compensation. By Brooke Allen brooke.n.allen@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.**