NORTH DAKOTA BANKERS ASSOCIATION

LEGAL UPDATE

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ARBITRATION

You Can't Have Your Cake and Eat it Too: Bank Customer Not Allowed to Sue Under Agreement's Terms and then Refuse the Agreement's Arbitration Clause [SD OH]

A bank had a Consumer Deposit Account Agreement (the "agreement") with each of its customers that outlined terms, late fees, returned deposit fees, an arbitration agreement, and more. A customer of the bank attempted to deposit two bad checks and was charged fees by the bank when the checks bounced. Using the language of the agreement, the customer argued that she should not have been fined, the bank had breached its covenant of good faith, unjustly enriched itself, and employed deceptive and unfair trade practices by charging returned deposit fees. In turn, the bank moved to enforce the arbitration clause found in the agreement, or, in the alternative, dismiss for failure to state a claim under which relief could be granted. The customer then argued that she had never received a copy of the agreement and had never agreed to it.

In **McMurray v. Huntington National Bank**, No. 2:24-cv-01481, 2025 WL 961701, 2025 U.S. Dist. LEXIS 60587 (S.D. Ohio Mar. 31, 2025) (opinion not yet released for publication), the court granted the bank's motion to compel arbitration and as such, did not need to consider the motion to dismiss. The court reasoned that if the arbitration agreement did apply, its analysis would end there. As such, the court had to determine if the three requirements to compel arbitration had been met: "(1) an enforceable written agreement to arbitrate; (2) a dispute within the scope of the arbitration agreement; and (3) a refusal to arbitrate." A.D. v. Credit One Bank, NA., 885 F.3d 1054, 1060 (7th Cir. 2018). The customer did not dispute elements two or three, so the court only had to determine whether the parties had entered into an agreement to arbitrate. The court found that the customer had, in fact, received (at multiple times) and consented to the agreement, pointing to the fact that her entire complaint arose from the terms of the very agreement that contained the arbitration clause. The court summed up its reasoning, stating "this Court finds no basis to allow [customer] to rely on the enforceability of the [agreement] for her affirmative claims while simultaneously disclaiming the enforceability of that very same contract to avoid arbitration."

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Specific Complaint of Misrepresentation of Funds Survives a Motion to Dismiss [BKR ED OK]

A debtor, along with her then-husband, obtained a loan from the lender for two of their businesses. The lender alleged that the loans were obtained based on fraud and false financial statements. The debtor, now divorced, filed for bankruptcy individually, and the lender sought to exempt the loans from discharge. Specifically, the lender pursued three causes of action, two of which were brought under 11 U.S.C. §523(a)(2) that alleged the funds were obtained under false pretenses and in reliance on false financial statements; the third cause of action was brought under 11 U.S.C. 523(a)(6) and alleged the funds were misappropriated and decreased the value of the lender's collateral. The debtor challenged the timing of the complaint and moved to dismiss for failure to state a claim under Fed. R. Civ. P. 12(b)(6).

In **Oklahoma Heritage Bank v. Van Horn (In re Van Horn)**, Nos. 24-80426-PRT, 24- 8014-PRT, 2025 WL 271281, 2025 Bankr. LEXIS 109 (Bankr. E.D. Okla. January 22, 2025) (opinion not yet released for publication), the court found that the complaint was timely filed and met the standard to overcome a failure to state a claim challenge. The court reviewed the timeline of the filing and found that an extension to file the complaint had been granted, and the complaint was filed within that extension. The court then reviewed the lender's complaint, which included very specific facts and exhibits to support its claim. For example, the complaint included 24 specific transactions in which the funds intended for the business were used for personal expenses, along with the dates, amounts, and creditors who were actually paid. Additionally, the complaint contained copies of financial statements provided to the lender that were alleged to be false. When the court viewed the complaint in the light most favorable to the lender, it found that it survived a 12(b)(6) motion to dismiss for failure to state a claim.

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CHAPTER 11 FINANCING

Good Faith Debtors Granted Bankruptcy Relief [BKR ND TX]

The debtors each voluntarily filed for Chapter 11 bankruptcy and subsequently operated and managed their businesses and properties as debtors in possession. The debtors sought to obtain postpetition financing with a credit facility (the "DIP facility"). Before consideration of the order here, the court had entered an interim order which allowed the debtors to obtain the DIP facility from the DIP Lender under the DIP Documents and made an interim amount available to the debtors. The U.S. Trustee for the Northern District of Texas then appointed an official committee of unsecured creditors (the "creditors' committee") pursuant to section 1102 of the Bankruptcy Code. The debtors filed a motion seeking entry of a formal order that, among various other things, authorized the debtors to obtain the DIP facility (in the form of a "non-amortizing priming super-priority senior secured postpetition credit facility").

In **In re Prospect Medical Holdings, Inc.**, No. 25-80002 (SGJ), 2025 WL 510458, 2025 Bankr. LEXIS 336 (Bankr. N.D. Tex. Feb. 14, 2025) (opinion not yet released for publication), the court granted the debtors' motion authorizing the DIP facility and made several other findings. The court granted the motion for postpetition financing after analyzing various aspects of the proposed financing, motion, and Chapter 11 cases. First, the court considered the evidence including several letters in support and the DIP credit agreement and related documents, as well as the arguments from the interim and final hearings, noting that all objections had been withdrawn, resolved, or overruled. Additionally, the court had determined that the motion appeared "fair and reasonable and in the best interests of the [d]ebtors and their estates, and essential for the continued operation of the [d]ebtors' businesses and the preservation of the value of the [d]ebtors' assets," and that entering into the DIP credit agreement and other documents appeared to be a sound and prudent exercise of the debtors' business judgment consistent with their fiduciary duties. Next, the court found that the postpetition financing could not be obtained from other sources or under more favorable terms than the DIP facility due to its financial condition, capital structure, and the circumstances of the Chapter 11. It also could not be obtained without granting the DIP lender liens and superpriority claims as they were "integral, critical, and essential components of the DIP [f]acility." Additionally, the court then found the DIP facility and loans were "being provided by the DIP [l]ender in 'good faith' within the meaning of section 364(e) of the [b]ankruptcy [c]ode." Finally, the court found that good cause had been shown to grant the motion and immediately enter the final order, as the final order would be in the "best interests of the [d]ebtors, their estates, their creditors, and other parties in interest." The debtors were not able continue their operations without the postpetition financing, which was necessary to allow them to pay fees and expenses in connection with the Chapter 11 cases and operational needs, and to continue business operations in order to "maintain the health and ·safety of their patients" and "relationships with customers, vendors, and suppliers." Taking the above into consideration, the court entered the final order which (1) authorized the DIP facility; (2) enforced the DIP obligations against the debtors; (3) authorized the aggregate amount of commitments detailed in the DIP credit agreement; (4) approved the DIP collateral structure, including the scope of collateral securing the DIJ> obligations; (5) granted the DIP lender "automatically and properly perfected security interests in and liens on the DIP collateral" subject to certain carve-out and permitted prior liens; (6) granted the DIP lender superpriority administrative expense claims against the debtors and its estate without the need to file a proof of claim, for all DIP obligations; (7) granted the debtors permission to use DIP financial accommodations according to the purposes and limitations described in the final order and in the DIP documents; (8) allowed the DIP lender to rely on the debtors' representations and did not impose an independent duty to monitor use of funds; (9) authorized the debtors use of the cash collateral according to the approved budget until the DIP termination declaration date; (10) granted the prepetition secured parties replacement liens on the DIP collateral, subordinate to the DIP liens, carve-out, and permitted prior liens, as adequate protection for any diminution in value; (11) authorized the debtors and the DIP lender to make any non-material changes to the DIP documents without court review and approval; (12) authorized the perfection, validity and priority of the DIP liens, the adequate protection liens, and the·FRMC lien; (13) modified the automatic stay to allow the parties to implement necessary transactions authorized by the final order and DIP documents; (14) approved provisions for cash proceeds derived from the credit or debt described in the final order; (15) required in the event the debtors receive payments or proceeds of DIP collateral before full repayment of the DIP obligations to hold those funds in trust and immediately tum them over to the DIP lender; (16) until repayment is complete, required the debtors to properly insure DIP collateral and maintain the cash management system in accordance with the DIP documents; (17) authorized the DIP lender right to credit bid all or part of its claims; (18) authorized the exercise of remedies in the event of a DIP termination event; (19) authorized the preservation of the DIP lender's rights and remedies under the DIP documents, providing that any failure to seek relief does not constitute a waiver of those rights; (20) approved the carve-out provisions; (21) provided the DIP lender with no obligation to pay professional fees; (22) approved the DIP fees and the DIP lender's professionals' fees according to the DIP documents; (23) indemnified the DIP lender; (24) provided the DIP lender does not need to file a proof of claim in Chapter 11 cases; (24) placed limitations on the debtors use of DIP funds according to the DIP documents; (25) protected the DIP lender from liability, barred marshaling, eliminated fiduciary duties or operational control over the debtors, and prevented governmental entities from recouping overpayments from cash collateral; (26) clarified that the final order does not create rights for third parties, deemed the DIP lender an additional insured and loss payee on insurance policies related to the DIP collateral; (27) made the final. order binding on the relevant parties; (28) approved the provisions for discharge, survival, and debtor necessary action; (29) clarified the final order did not affect the preexisting rights or remedies held by several companies against the debtors including one company's preexisting purchase money security interests against the debtors, and approved the provision made for monthly postpetition interest shall accrual payments.

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LENDING

Debtor's Alleged Forgery Failed After Missing Loan Payments [WI APP]

The debtors are a husband and wife collectively. In 2015, the husband and two of his business partners began negotiating the purchase of a business. They sought a loan from the bank to finance the purchase. The debtors secured the loan by granting mortgages on their personal property. As the anticipated closing date neared in July 2016, the husband and his partners pressured the bank to expedite the process to avoid business disruptions and finalize the closing. A representative of the bank delivered the necessary documents requesting they be signed and returned; some of the necessary documents required the signatures to be made in the presence of a notary. Upon being returned, the bank representative discovered the documents had not included a notarized signature, so the representative notarized the loan documents despite not witnessing the signatures. In late 20l7, the debtors began missing payments on the loan to the bank. The debtors then contacted the bank to dispute the validity of the loan documents, claiming that the signatures had been forged and that the notarization was improper. The debtors filed suit, asserting claims that included forgery, notarial misconduct, and misrepresentation. The bank counterclaimed seeking enforcement of the loan. After a twelve-day bench trial, the court concluded the loan documents were valid and enforceable and dismissed all remaining claims. The debtors appealed, challenging the finding that the loan documents had in fact been signed by him.

In Carmody v. Byline Bank, No. 2022AP1305, 2024 WL 1639513, 2024 Wisc. App. LEXIS 315 (Wis. Ct. App. Apr. 16, 2024) (unpublished opinion), the court of appeals declined to disturb the trial court's factual findings because it determined they were not clearly erroneous. In support of its conclusion, the court cited direct and circumstantial evidence showing the husband had intentionally signed the loan documents. This evidence included text messages in which the husband said he did not remember signing the documents in front of a notary. The court further noted that there was no dispute over the signature of the documentation until shortly after a missed payment. Additionally, the husband argued he was out of town at the time the documentation was signed, asserting his signature was forged. The court found the testimony persuasive that the wife never discussed the loan documents with the husband when he returned home, suggesting that he had indeed signed the loan documents himself. Additionally, the wife testified that the signature looked like that of her husband's. Although the debtors presented an expert witness who testified that the signatures had been forged, the court noted that a trier of fact is not bound by the opinions of an expert and can accept or reject the expert's testimony without the ruling being found clearly erroneous. Lastly, on appeal, the debtors challenged the trial court's grant of partial summary judgment. The court also upheld the grant of partial summary judgment, finding the debtors had failed to present admissible evidence of damages or prove that any damages were proximately caused by the bank's notarial misconduct. The proximate cause had been the husband signing the loan documentation initially. The debtors also alleged that the bank had misrepresented the business valuation; however, the court rejected this claim, noting that the debtors had participated in the negotiations and that the bank was not a party to the sale. The court explained the bank was simply the party who provided the loan, and therefore was not in a position to mislead the debtors.

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SECURITY INTERESTS

"Super Generic" Descriptions in a Security Agreement are Insufficient to Perfect a Security Interest [D UT]

The lessor and lessee entered into a lease agreement, which granted the lessee the right to use two aluminum furnaces. The lease agreement permitted the lessor to, upon default, accelerate the note, acquire a security interest in "all [of the lessor's assets," and recover interest along with all other costs, fees, and expenses associated with the breach. In addition, the owner of the lessee (the "guarantor") agreed to be a personal guarantor for all of the lessee's obligations and, as collateral, granted a security interest in all of his personal assets. Subsequently, the lessee failed to make its monthly payments and defaulted. The parties entered into an agreement that stipulated that the lessor would not "pursue contractual remedies... in exchange for [the lessee]'s commitment to make certain monthly payments." However, the lessor filed a financing statement indicating it had a security interest in all of the assets of the lessee and the guarantor. The lessee again failed to make payments and defaulted. The lessor sued both the lessee and the guarantor for (1) breach of contract, (2) breach of a covenant of good faith and fair dealing, and (3) security interest foreclosure. The lessor moved for summary judgment on its breach of contract and security interest foreclosure claims against the lessor and guarantor.

In **AVT Texas, L.P., v. Sarbali Alloys, LLC**, 756 F. Supp. 3d 1264 (D. Utah 2024), the court granted summary judgment in favor of the lessor on its breach of contract claims against both parties but denied summary judgment on the claims for security interest foreclosure. First, the court considered the breach of contract claims. The lessee and guarantor argued that summary judgment would be improper because the liquidated damages clause in the lease agreement was invalid because there was a genuine dispute of material fact on whether the clause was "a 'reasonable forecast of just compensation for the harm'... [and] whether the harm caused... was 'incapable or very difficult of accurate estimation."' However, the court dismissed this argument as "immaterial" because under Utah law, the enforceability of a liquidated damages clause can be challenged "'only by pursuing one of the general contractual remedies, such as mistake, fraud, duress, or unconscionability."' Therefore, the court found that there were no genuine issues of material fact and granted summary judgment for the breach of contract claims. Second, the court found that the lessor was not entitled to summary judgment regarding its security interest foreclosure claims. The court first noted that because the lessee and guarantor were located in Texas, Texas's law governed the perfection of the disputed security interests. Utah Code Ann. § 70A-9a-301(1). In Texas, for the lessor's security interests to be valid, "'three requirements must be satisfied: (1) there must be value given; (2) the debtor must have rights in the collateral; and (3) the debtor must have authenticated a security agreement with a description of the collateral."' Markel Ins. Co v. Origin Bankcorp, Inc., 663 F. Supp.3d 670, 677-78 (N.D. Tex. 2023). Further, the security agreement must "reasonably identify the collateral." Here, the lessor had used a "super generic" description of the collateral merely referring to "all" of the assets of the lessee and guarantor. Thus, the security interests never attached to the assets of the lessor and guarantor and were not perfected.

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A Failed Attempt to Escape a Security Interest on Farm Equipment [D NE]

The debtors executed and delivered a promissory note to the creditor, who had a perfected security interest in a planter and cultivator. The debtors then sold the planter and cultivator to a third party without informing the creditor. The third party did not make arrangements with the creditor to release the creditor's lien, and the debtors did not tum over the proceeds from the sale to the creditor. The debtor filed a Chapter 12 bankruptcy petition. The bankruptcy court granted the creditor the ability to prosecute this case to recover the property that the debtor had transferred. The creditor then sued to determine its right of possession and request the delivery to it of the planter and cultivator.

In **Stockmens Bank v. Double H P'ship**, No. 4:25CV3004, 2025 WL 470469, 2025 U.S. Dist. LEXIS 27482 (D. Neb. February 12, 2025), the court entered an order of delivery to deliver the property to the creditor. The court, using the Nebraska Uniform Commercial Code, assessed the procedures in transferring collateral when a perfected security interest exists on that collateral. According to the Nebraska Uniform Commercial Code, a security interest continues to exist unless the secured party authorized disposition free of that security interest, and a security interest attaches to any identifiable proceeds of collateral. Neb. Rev. Stat. U.C.C. § 9-315. Here, the creditor did not authorize the disposition of the property free of the security interest, so the property was still subject to the creditor's existing perfected security interest. The third party argued that there was a question of fact regarding whether that third party was a purchaser of goods in the ordinary course of business, an exception to the applicable Nebraska statute. However, the court found that the third party presented no evidence that the debtors were engaged in the business of selling this particular farm equipment. The court determined the debtors were in default on their obligations under the security agreement, and the creditor showed, by a preponderance of the evidence, that it was entitled to possession of the planter and cultivator. Conversely, the third party did not meet its burden to show why the property should not be delivered to the creditor, so the court entered an order requiring delivery of the property to the creditor.

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Be Careful Where You File: Lawyers Make a Costly Mistake by Failing to File a Financing Statement Where the Debtor is Incorporated [BAP 9TH CIR]

The debtor, a Delaware corporation, purchased broadcast companies in Nevada and New Mexico. The creditor extended the debtor four loans to purchase the companies, which were secured by the debtor's real property and personal property in New Mexico and Nevada. The creditor filed financing statements in New Mexico and Nevada but failed to do so in Delaware. Subsequently, the debtor filed for Subchapter V Chapter 11 bankruptcy and listed the creditor "as a secured creditor in both real and personal property." However, the Subchapter V trustee objected to the debtor's proof of claim for personal property, arguing that the debtor was a Delaware corporation, and the creditor must have filed a financing statement in Delaware to perfect its security interest in personal property. The debtor argued that while Delaware law governed perfection, its security interest was perfected because the financing statement was filed "in the state where the personal property was located." The bankruptcy court ruled in favor of the creditor and allowed its claim, and the trustee appealed.

In Shapiro v. Newtek Small Bus. Fin., LLC (In re Glob. One Media, Inc.), 667 B.R. 878 (B.A.P. 9th Cir. Apr. 2, 2025), the bankruptcy appellate court reversed and held that the creditor did not have a perfected security interest in the debtor's personal property. First, the court noted that under the revised UCC, the focus for filing purposes shifted "from 'location of goods' as the controlling factor to 'location of the debtor.'" 8 Quinn's UCC Commentary & Law Digest § 9-307(a)(3) (Rev. 2d ed.). Further, the debtor was undisputedly "located" in Delaware. The creditor argued that "tangible documents, goods, instruments, or money located in Nevada or New Mexico" is governed by the law in those states pursuant to 6 Del. C. § 9-301(3)(C). However, the court disagreed, stating that "where the collateral is located governs the 'effect of' perfection ... and the 'priority of' a nonpossessory security interest in collateral, that jurisdiction's law does not govern 'perfection' itself." Thus, Delaware law governs perfection, and the proper office to file a financing statement in is the Delaware Secretary of State. 6 Del. C. § 9-501(a)(2). Consequently, the creditor did not file its financing statement in Delaware, its security interest in the debtor's personal property was unperfected, and it only had an unsecured claim. Therefore, the court remanded the case to the bankruptcy court to "determine the amount of the unsecured portion of [the debtor]'s claim."

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Security Interests Don't Survive the Free Flow of Funds [OH APP]

The bank sued a merchant cash advance (the "corporation") over funds withdrawn from a commingled account. The deposit account was held by businesses owned by a bank customer, who was later convicted of a check-kiting scheme. The bank had loan agreements with several of the customer's companies, which were secured by firstpriority security interests in the companies' assets, including accounts receivable. The corporation had entered into factoring agreements with many of the customer's businesses, including the companies with accounts at the bank, purchasing future receivables in exchange for cash up front. Funds from these receivables were deposited into the customer's account at the bank, from which the corporation withdrew approximately $3.6 million. The bank sued for conversion after the customer's check kiting fraud was uncovered, arguing that the corporation unlawfully took funds in which the bank held a perfected security interest. The trial court granted summary judgment to the bank, awarded it the remaining balance of one company's loan, but denied attorneys' fees and interest. The bank appealed, and the court of appeals considered its assignment of error. The first assignment of error raised three issues: whether the loan documents adequately described accounts receivable as collateral, whether R.C. 1309.332(B) barred the bank's claim, and whether the bank had proven the elements of conversion. The second assignment of error challenged the traceability of the transferred funds, the risk of a windfall from overlapping lawsuits, and whether the damages award exceeded the bank's actual loss.

In First Fin. Bank v. Tailored Fund Cap., LLC, No. C-230626, 2024 WL 5949821, 2024 Ohio App. LEXIS 3716 (Ohio Ct. App. Oct. 16, 2024) (opinion not yet released for publication), the court interpreted Ohio Revised Code (R.C.) 1309.332(B)- which protects transferees of deposit account funds from prior security interests unless collusion has been proven- to bar the bank's claim. The court began its analysis by examining the plain language and legislative intent behind

R.C. 1309.332(B), which mirrors UCC § 9-332. The court emphasized that this provision was designed to create finality in financial transactions by ensuring that funds transferred out of deposit accounts are not subject to claw-back claims by secured parties, such as the bank in this case. The court relied on UCC commentary and case law to confirm that the statute's purpose is to protect innocent transferees and maintain the free flow of commerce. Ultimately, the court held that R.C. 1309.332(B) barred the bank's conversion claim because the corporation, as an innocent transferee, took the funds free of the bank's security interest. The court also faulted the bank for improperly shifting its theory of conversion mid-litigation in response to the transferee's statutory defense. The court adopted the majority approach, which "bars recovery for conversion" absent a "noncolluding third party." Because the bank had failed to allege collusion it therefore could not recover in this case.

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Role of NDBA General Counsel

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

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