

NCLC REPORTS

Consumer Credit and Usury Edition

Volume 27
January/February 2009

Developments and Ideas For the Practice of Consumer Law

Special Issue on Bank Insolvencies: Bars to Jurisdiction and to Claims and Defenses

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Bank Insolvency: Navigating Potential Bars to Jurisdiction and to Certain Claims and Defenses

Twenty-five banks failed in 2008 alone, including IndyMac Bank and Washington Mutual Bank, the two largest failures in history. Of these, twenty-one closed just since July. In contrast, twenty-seven banks closed between 2000 and 2008.¹

Once the Federal Deposit Insurance Corporation (FDIC) takes over a bank, two critical questions arise for those homeowners who have or have had contractual or other relationships with the institution: Must consumers exhaust the FDIC administrative claims process to preserve their right to seek court review of claims and defenses? And do consumer claims and defenses to lender or servicer wrongdoing survive special protections available to the FDIC? In other words, homeowners face two separate and distinct legal issues:

- Subject matter jurisdiction of the court to entertain a consumer's suit and
- If the court has jurisdiction, special defenses to the homeowner's causes of action that the FDIC can raise.

The Legal Landscape

As a result of the dramatic bank failures of the Great Depression of the 1930s, the federal government created the FDIC. In doing so, Congress sought to promote stability and confidence in the banking system, to insure deposits, and to keep open the channels of trade and commerce. As another wave of bank failures hit the country in the 1980s, Congress overhauled the legal regime governing failed banks and the authority of federal receivers over those entities when it passed the Financial Institutions Reform, Recovery

¹ For a chart of bank failures, see National Consumer Law Center's website: www.consumerlaw.org/issues/financial_distress/content/failed_bank. This chart includes the bar dates for filing claims and links to the FDIC website for more information about each bank.

and Enforcement Act (FIRREA).² One of the goals of FIRREA "is to enable the receiver to efficiently determine creditors' claims and preserve assets of the failed institution without being burdened by complex and costly litigation."³

Today, the U.S. banking system faces another enormous crisis, this time triggered by the faulty mortgage loans it made or purchased over the last several years. Once again, the law triggered by bank failures stirs.

When a bank closes, a special administrative regime governs the resolution of issues raised by the failure, including the payment of depositors, general creditors and others, and the sale of the bank's assets and liabilities. The FDIC acts as the failed bank's receiver when it intends to liquidate the institution, take control of its assets and liabilities, and close the bank's affairs.⁴

Within a reasonable time following its appointment as a receiver, the FDIC may repudiate contracts and leases made by the failed bank that it believes are burdensome.⁵ The statute also creates a claims process that bank "creditors" must utilize to seek payment from the bank's assets or the FDIC insurance fund to cover some or all of their losses.⁶ Finally, the law grants the FDIC potential safeguards against certain claims and defenses raised by consumers who entered into loans with the bank prior to its failure.

The article will first address the claims procedure and related jurisdictional concerns and then discuss what causes of action and/or defenses survive the special FDIC shields against liability issues. *CAUTION: The research performed for this article was not exhaustive due to the sheer volume of cases. Practitioners should take care to review relevant authority in your jurisdiction.*

The Administrative Claims Process, Stays, Exhaustion, and the Jurisdictional Bar

The provisions relating to the FDIC administrative claims procedure appear in 12 U.S.C. § 1821(d). Once the FDIC assumes a receivership role over a failed bank, it must mail a notice to "creditors" shown on the institution's books or of which it becomes aware, advising them to present claims with proof to the receiver by a date specified in the notice (no less than 90 days from the date the notice is also published).⁷

² Pub. L. No. 101-73, 103 Stat. 183 (1989) (appearing in scattered sections of the United States Code).

³ National Union Fire Ins. Co. v. City Sav. Bank, F.S.B., 28 F.3d 376, 388 (3d Cir. 1994).

⁴ Patricia A. McCoy, Banking Law Manual §§ 15.03, 1504 (Lexis Pub. 2004) (detailed description of the powers and duties of the FDIC in its receiver role).

⁵ 12 U.S.C. § 1821(e). See also McCoy, *supra* note 4, at § 16.03.

⁶ 12 U.S.C. § 1821(d)(3).

⁷ 12 U.S.C. §§ 1821(d)(3)(B)(i), 1821(d)(3)(C). All statutory citations are to 12 U.S.C., unless otherwise noted. The courts apply varying definitions of "creditor" in this context. Compare National Union Fire Ins. Co., 28 F.3d at

The FDIC has 180 days to decide whether to allow or disallow each claim.⁸

Statutes of limitations are tolled by filing the claim, if a suit had not been initiated before the bank closed.⁹ Moreover, the filing of a claim does not prejudice the right of the claimant to continue any action filed before the appointment of the receiver.¹⁰ Thus, the FDIC's determination of a timely claim should be treated as a non-binding adjudication.¹¹

If a claim is not filed by the original bar date, the FDIC will disallow it. That decision generally is not reviewable.¹² For potential claimants who did not receive notice from the FDIC, the statute permits late filing as long as a claim is filed in time to permit payment.¹³

Cases filed before the bank failure will be stayed as to *all* parties for up to 90 days, upon the request of the receiver.¹⁴ Upon the FDIC's request, some courts also have issued stays up to an additional 180 days to coincide with the claim determination timeframe.¹⁵ This extended stay is discretionary.¹⁶ Practitioners may wish to argue that it should not apply to non-bank third parties since the causes of action against those parties are not "assets" of the failed bank subject to the receivership or are not claims relating to the acts or omissions of the failed institution or the FDIC.¹⁷

Claimants may seek judicial review of the agency's decision on the claim by requesting an administrative review or filing suit within 60 days after the end of the 180-day period or from the date of disallowance.¹⁸ If the claimant then initiates a lawsuit, the case must be filed in the federal district

387–388 (applying Bankruptcy Code definitions to find that a creditor's claim is any affirmative action asserting a right to payment, a broad definition) *with* Bolduc v. Beal Bank, SSB, 994 F. Supp. 82, 90–91 (D.N.H. 1992) (holding that a mortgagor is a debtor of a failed bank, not a creditor; finding that the mortgagors received no notice from the FDIC regarding the claims process and were not barred from filing an affirmative case in the defensive posture of stopping a foreclosure in a non-judicial foreclosure state; applying due process standards and ruling that since they received no notice to file a claim, they cannot be prevented from raising defenses in their action to stop the foreclosure sale) *and* Scott v. RTC (*In re* Scott), 157 B.R. 297, 310–312 (Bankr. W.D. Tex. 1993), *vacated due to settlement*, 162 B.R. 1004 (W.D. Tex. 1994) (ruling that a debtor of the failed bank is not a "creditor" since § 1821(d)(3)(B) refers to those entities that extended credit to the bank, not those who owe the bank). This disagreement among the courts has important consequences because the jurisdictional bar in § 1821(d)(13)(D) may not apply at all if the homeowner is not a "creditor." *See also* discussion in notes 21 and 22, *infra*.

⁸ 12 U.S.C. § 1821(d)(5)(A).

⁹ 12 U.S.C. § 1821(d)(5)(F).

¹⁰ *Id.*

¹¹ 12 U.S.C. §§ 1821(d)(5)(F)(ii) (no prejudice to continue a pending case), 1821(d)(6) (permitting judicial review or an administrative appeal of claims after the 180-day period passes or after disallowance). *See also* Rosa v. RTC, 938 F.2d 383, 397 (3d Cir. 1991).

¹² 12 U.S.C. § 1821(d)(5)(C).

¹³ 12 U.S.C. §§ 1821(d)(3)(C)(ii); 1821(d)(5)(C)(ii).

¹⁴ 12 U.S.C. § 1821(d)(12).

¹⁵ *See, e.g.*, Marquis v. FDIC, 965 F.2d 1148, 1154–1155 (1st Cir. 1992) (holding that the 90-day stay provision in the Act does not prevent the court from ordering a longer stay; ruling against the FDIC's position that the case should, instead, be dismissed; finding that the FDIC must show good cause for extending the 90-day stay but suggesting that courts would likely grant the extended stay in the majority of cases). *But see* Marc Development, Inc. v. FDIC, 992 F.2d 1503, 1507 (10th Cir. 1993) (holding that courts may *not* extend the 90-day stay because the statute does not authorize it), *vacated due to settlement*, 12 F.3d 948 (10th Cir. 1993).

¹⁶ Marquis, 965 F.2d at 1154–1155.

¹⁷ *See* 12 U.S.C. § 1821(d)(13)(D). The requirement that the mandatory 90-day stay apply to all parties should not apply to all parties in the case if a court is inclined to grant an extended stay. This is so because § 1821(d)(12) only applies to the mandatory stay.

¹⁸ 12 U.S.C. § 1821(d)(6)(A).

court for the district within which the depository institution's principal place of business is located or the United States District Court for the District of Columbia.¹⁹ Alternatively, the claimant may continue any pending case that had been stayed during the FDIC's review of a claim.²⁰

Section 1821(d) includes a jurisdictional bar. Except as provided elsewhere in section 1821(d) (i.e., the claims procedure), no court shall have jurisdiction over: "i) any claim or action for payment from, or any action seeking a determination of rights with respect to, the assets of any depository institution for which the Corporation has been appointed a receiver, including assets which the Corporation may acquire from itself as such receiver; or ii) any claim relating to any act or omission of such institution or the Corporation as receiver." Courts consistently hold that this provision requires exhaustion of the administrative claim process.²¹

Courts have struggled with constitutional due process problems that arise when judicial review of a cause of action is denied in certain circumstances. Examples of these instances include: 1) where the claim arises against the FDIC itself as receiver after the claims filing date has passed; 2) where the FDIC never notified a known creditor, thereby preventing it from filing a timely claim; and 3) where the FDIC was not aware of the potential creditor and never sent notice. Applying the jurisdictional bar to prevent a party from raising a claim affirmatively or defensively if the administrative process does not apply to that particular type of case²² or the party did not receive notice from the FDIC before the bar date²³ should be a violation of due process.

Practice Q & A

Q. Should homeowners file claims with the FDIC if they receive notice of the bar date from the FDIC?

A. Yes, or the claim likely is forever barred, even if the homeowner filed suit before the bank failure.

¹⁹ *Id.*

²⁰ 12 U.S.C. § 1821(d)(6)(A)(ii).

²¹ *See, e.g.*, Village of Oakwood, 539 F.3d at 385–385 (citing decisions from the D.C., 1st, 3d, 4th, 5th, and 8th Circuits). Differences among the circuits have arisen on the issue of whether the jurisdictional bar applies to the same or a larger set of claims as those which are subject to the administrative process. *See National Union Fire Ins. Co.*, 28 F.3d at 385–386, n.8 (holding that the jurisdictional bar in § 1821(d)(13)(D) covers a broader group of cases than those that must go through the administrative process and addressing certain constitutional issues triggered by this analysis; citing cases that hold the opposite—that the set of cases under each of these provisions is co-extensive).

²² *See, e.g.* Rosa, 938 F.2d at 394–395 (beneficiaries of failed bank's ERISA plan seeking to prevent the RTC's termination of the plan not governed by the claims procedure and not barred).

²³ *See, e.g.*, National Union Fire Ins. Co., 28 F.3d at 388–390 (due process is satisfied where the insurance company's declaratory judgment action based upon its rescission of the policy is barred even though it had no notice of the bar date and the claims process may not have applied to its case but where it could raise rescission as an affirmative defense if the RTC sued to enforce the policy; counterclaims barred); FDIC v. DiStefano, 839 F. Supp. 110 (D.R.I. 1993) (interpreting §§ 1821(d)(3)(C)(ii) and 1821(d)(5)(C)(ii) to require the FDIC to send a claims notice to newly discovered claimants and permitting time to file an administrative claim, thus avoiding a constitutional problem; recoupment claims up to the amount sought not barred); Bolduc v. Beal Bank, SSB, 994 F. Supp. 82, 90–91 (D.N.H. 1992) (characterizing an affirmative case to stop a foreclosure as defensive and holding defenses of ECOA, TILA, undue influence, and invalid endorsement not barred).

Q. Should homeowners file claims with the FDIC if they have *not* received notice of the bar date from the FDIC?

A. If the homeowner has an attorney and is aware of the bank's closure, the more prudent course of action is to notify the FDIC of any causes of action against the bank. The agency should send a letter within 30 days of "discovery" with a bar date and a claim form.²⁴ The homeowner then can file a timely claim. If the homeowner was unrepresented during the receivership period and did not file a claim (because, of course, she did not receive notice from the FDIC), defenses to a subsequent foreclosure or a suit on the debt should be preserved. Affirmative claims should survive as well if there is no other forum available to obtain the relief sought. (See discussion of the due process concerns above.)

Q. If the assignee purchased the loan *before* the bank failure, does the jurisdictional bar apply to claims based upon the bank's behavior?

A. The answer to this should be no. Arguably, the administrative process does not apply to claims involving assets that were not owned by the bank at the time it failed.²⁵ In this instance, it is extremely unlikely that the FDIC would send the homeowner a notice of the right to file a claim. Without such a notice, there should be no bar. On the other hand, the bar also applies to "any claim relating to any act or omission of such institution."²⁶ This provision may capture affirmative causes of action raised against the assignee that are based upon the bank's behavior.²⁷

Q. Must the homeowner use the FDIC claim form or can a letter suffice?

A. There is nothing in the statute that mandates that a particular form be used (and there are no regulations).²⁸ However, a recent case held that letters sent to the FDIC by counsel did not constitute a claim as they did not "contain enough identifying information on the nature of the claim to constitute a proper administrative claim under FIRREA."²⁹ Important to the court was the fact that the named plaintiff received notice from the FDIC and a copy of a claim form but failed to use it.

Q. What is the FDIC's position on class claims?

²⁴ 12 U.S.C. § 1821(d)(3)(C)(ii). There is an argument that the claims process is rendered inadequate by the lack of a reasonable time limit on the FDIC's ability to require a potential claimant to submit to the claims process. See *Coit Independence Joint Venture v. FSLIC*, 489 U.S. 561 (1989) (no obligation to exhaust where there is no time limit for the disposition of claims). The FDIC process does not suffer from this defect since the FDIC must review a claim within 180 days. However, if the FDIC can send a claim form and new bar date at any time, even after distribution of assets to other creditors, in order to coerce a claimant to enter into unfair settlements, the exhaustion requirement should not apply. under the *Coit* rationale. *Id.* at 586-87. Thanks to Michael Malakoff and Erin Brady for bringing *Coit* to our attention.

²⁵ 12 U.S.C. §§ 1821(d)(2) (powers of the receiver involve liquidating the bank and selling its assets), 1821(d)(3)(B) (notice goes to "creditors" of the failed bank).

²⁶ 12 U.S.C. § 1821(d)(13)(D)(ii).

²⁷ The resolution of this discussion may depend on whether your court sides with the decisions holding that the bar in § 1821(d)(13)(D) covers the same claims that are subject to the administrative procedure or with the courts finding that § 1821(d)(13)(D) reaches a broader universe of causes of action than those subject to the claims process. See discussion in note 21, *supra*.

²⁸ 12 U.S.C. § 1821(d)(3)(B) says only that creditors must present their claims with proof.

²⁹ *Yang v. Home Loan Funding, Inc.* 2009 WL 179689 at *5 (E.D. Cal. Jan. 23, 2009).

A. According to the FDIC, if a class action is pending against a bank on the date of its failure, counsel for the class must file a claim for each named plaintiff or risk the later dismissal of those claims for failure to exhaust the administrative process. The FDIC suggests that putative class members must file claims as well (a near impossibility, unless they are sent individual notices).³⁰

However, section 1821(d) and due process concerns weigh against the FDIC's position for several reasons. First, once the FDIC is aware of "creditors" of the bank, it "shall" send notice within 30 days of discovery of their names and addresses.³¹ The FDIC itself likely can determine the names and addresses by reviewing the class definition and the failed bank's records related to those class members. In addition, if a claimant files a claim after the bar date, the claim cannot be disallowed on that basis if the claimant did not receive notice of the appointment of the receiver in time to file timely and if payment of the claim is still possible.³² Finally, the exhaustion requirement only applies if the procedures elsewhere in section 1821(d) are followed.³³ A due process issue arises if putative class members do not receive notice, do not file claims, and the FDIC later seeks dismissal of the class claims on the ground that the class members failed to exhaust the claims process. The constitutional cases discussed earlier should be reviewed to attack the FDIC's position.³⁴

One court implicitly approved of the procedure outlined in the FDIC's letter, although its validity apparently was not challenged.³⁵ Despite the fact that the letter discourages the filing of class claims, practitioners nevertheless may choose to file both separate claims for the named plaintiffs and a class claim. If the latter is disallowed, the FDIC should be in a much weaker position if it challenges the class claims once the litigation proceeds.

What Claims or Defenses Survive FDIC Receivership?

Assuming that jurisdiction is not a problem, whether a claim or defense survives the FDIC receivership depends on a number of factors: 1) whether the bank actually failed; 2) for claims and defenses arising from the loan origination, whether the bank owned the mortgage and note at the time it closed; 3) for claims and defenses arising out of the bank's servicing activities, whether the bank serviced the mortgage

³⁰ Claire L. McGuire, Senior Counsel at the FDIC, stated in a letter to NCLC dated September 2, 2008: "Each claimant against a failed bank must file an individual proof of claim. A representative may file a claim on behalf of a claimant so long as he or she submits a written power of attorney along with the claim. Proof of each claim must be filed in order for the FDIC to evaluate the claim. Thus, each member of a class in a class action lawsuit must file an individual claim that meets these requirements." This letter is available at: www.consumerlaw.org/issues/financial_distress/failed_banks.shtml.

³¹ 12 U.S.C. § 1821(d)(3)(C)(ii).

³² 12 U.S.C. § 1821(d)(5)(C)(ii).

³³ 12 U.S.C. § 1821(d)(13)(D) ("except as otherwise provided in this section"). See also *National Union Fire Ins. Co.*, 28 F.3d at 385-386 (stating that § 1821(d)(13)(D) "is not viewed in isolation, but with reference to the administrative claims procedure of FIRREA set out in § 1821(d)(3), (d)(5) and (d)(6)").

³⁴ See note 23, *supra*, cases cited therein and any subsequent history. See also *Rosa v. RTC*, 938 F.2d 383, 396-397 (3d Cir. 1991). None of these cases struggled with this exact issue.

³⁵ *Yang v. Home Loan Funding, Inc.* 2009 WL 179689 at *5-6 (E.D. Cal. Jan. 23, 2009).

account at the time it failed; and 4) whether the cause of action is of a type that survives the FDIC receivership.

Did the Bank Actually Fail?

This is the first question to ask if it appears that the FDIC was involved in a bank's business. The Federal Deposit Insurance Act (FDIA) gives the FDIC "open" bank powers to assist banks to stay solvent or to negotiate reorganizations or sales of the bank and its assets and liabilities.³⁶ The FDIC used this authority in 2008 to orchestrate the sale of Wachovia Bank, N.A. and to avoid placing the bank in receivership.³⁷ The most reliable way to determine if the bank went into the FDIC receivership is to check the FDIC Failed Bank List³⁸ and the NCLC Failed Bank Chart.³⁹

If the bank did not fail, as in the case of Wachovia Bank, then the issues discussed below do not arise.⁴⁰ Homeowner claims and defenses against the bank will not be affected by the law surrounding bank failures, though the private purchase and sale agreements between the companies involved may affect these issues.⁴¹

Did the Bank Own the Mortgage and Note at the Time It Failed?

This question is critical to claims and defenses arising from the loan origination. In recent years, mortgage lenders, including banks, sold most of their loan portfolios into the secondary market, often via securitization arrangements. As a result, many mortgage loans would *not* be assets acquired by the FDIC when it became the receiver of the bank that originated the loan.

The statutory provision that frees the FDIC from certain claims and defenses that the homeowner may wish to raise is codified at 12 U.S.C. § 1823(e). It applies to any "agreement which tends to diminish or defeat the interest of the [FDIC] in any asset acquired by it under this section" (emphasis added). When the FDIC did not acquire the asset at issue, the few courts addressing this situation hold that section 1823(e) does not affect claims or defenses to bank behavior.⁴² These cases are listed below.

³⁶ 12 U.S.C. § 1823(c).

³⁷ FDIC Press Release, Citigroup Inc. to Acquire Banking Operations of Wachovia (Sept. 29, 2008), available at www.fdic.gov/news/news/press/2008/pr08088.html (Wells Fargo out-bid Citigroup, though the sale may be disputed).

³⁸ Go to www.fdic.gov/bank/individual/failed/banklist.html.

³⁹ www.consumerlaw.org/issues/financial_distress/content/failed_banks/failed_banks.pdf.

⁴⁰ E-mail from David Wall, Senior Legal Counsel, FDIC (Oct. 6, 2008) (on file at NCLC).

⁴¹ These Purchase and Assumption Agreements are available at NCLC's website, www.consumerlaw.org/issues/financial_distress/failed_banks.shtml.

⁴² 12 U.S.C. § 1823(e)(1) states in full:

No agreement which tends to diminish or defeat the interest of the Corporation in any asset acquired by it under this section or section 1821 of this title, either as security for a loan or by purchase or as receiver of any insured depository institution, shall be valid against the Corporation unless such agreement—(A) is in writing, (B) was executed by the depository institution and any person claiming an adverse interest thereunder, including the obligor, contemporaneously with the acquisition of the asset by the depository institution, (C) was approved by the board of directors of the depository institution or its loan committee, which approval shall be reflected in the minutes of said board or committee, and (D) has been, continuously, from the time of its execution, an official record of the depository institution.

Joslin v. Shareholder Services Group, 948 F. Supp. 627 (S.D. Tex. 1996) (where stock certificates could not be legally pledged as security for a loan note held by a bank that later failed, the FDIC never acquired the asset (the security interest in the stock certificates) and a subsequent purchaser of a promissory note could not enforce the security agreement).

Integon Life Ins. Corp. v. Southmark Heritage Retirement Corp., 813 F. Supp. 783 (N.D. Ala. 1992) (suit to quiet title; parcels of land sold before the savings and loan bank failed were not assets of the receivership, so § 1823(e) did not apply).

Alaska Southern Partners v. Prosser, 972 P.2d 161 (Alaska 1999) (loan satisfied before the bank failure could not be an asset subject to the FDIC receivership and was not enforceable by a subsequent buyer).

Joslin v. Bengal Chef, Inc., 715 So. 2d 1266 (La. Ct. App. 1997) (guarantors on loan note owed to a bank who could prove that they were released from their guarantees before the bank failed were not liable to the successor of the FDIC; since the FDIC could not enforce the guarantee, neither could the purchaser).

Applying these rulings to the mortgage loan context, if the bank did not own the mortgage loan at the time it closed, then the consumer should be free to raise those claims and defenses against the current holder. This conclusion is good news for homeowners and their advocates. ONE CAVEAT: Must the homeowner nevertheless exhaust the FDIC claims process when the case against the current holder is grounded in "any act or omission of such institution"?⁴³ The answer ought to be no, unless the FDIC sends the homeowner notice of her right to file a claim with a bar date. Otherwise, due process concerns arise, as noted above.

Did the Bank Service the Loan at the Time It Closed?

If the homeowner's complaint against the bank arose from its behavior while servicing the loan, this question takes on significance. If the bank committed servicing abuses and then sold its servicing rights (an asset) before it failed, the FDIC has no right to that asset upon the bank's closure. Hence, the homeowner can raise bank servicing abuses against the mortgage holder for whom the bank serviced the loan under agency or joint liability theories, if applicable, with the caveats mentioned in the previous section of this article. In addition, the holder's own actions and a new servicer's culpability for its own actions are not affected by the bank insolvency.

How about the scenario where the bank was still servicing the loan at the time it closed? Since the servicing rights are a receivership asset, the injured homeowner must file a claim with the FDIC, upon notice from the FDIC. The homeowner also may file a lawsuit against the mortgage holder, if she can establish separate, independent grounds of liability other than the mortgage holder's derivative liability for the acts of the servicer.

Does the Homeowner's Cause of Action Survive the FDIC Receivership?

Two separate sources provide special defenses to the federal agencies responsible for insuring banks and thrifts. First, there is the "D'Oench doctrine," first articulated by the Su-

⁴³ 12 U.S.C. § 1821(d)(13)(D)(ii).

preme Court in the 1942 case *D'Oench, Dubme & Co. v. FDIC*, which prevents borrowers from asserting "secret side agreements" with bank officers as a defense against obligations being administered by the FDIC.⁴⁴ Second, there is a special statute, 12 U.S.C. § 1823(e), sometimes imprecisely referred to as a statutory codification of *D'Oench*.⁴⁵

There are dozens of cases holding that certain claims and defenses survive an FDIC receivership because the doctrines in *D'Oench, Dubme* or section 1823(e) do not apply or for other reasons. Those cases are listed in NCLC's *Cost of Credit* at § 10.7.8. Practitioners should carefully review these decisions as the courts are not always consistent. One important question is whether an entity (the assignee) that purchases loans from the FDIC stands in the same protected shoes. The courts are split with the majority in favor.⁴⁶

The causes of action that survive include:

- Breach of fiduciary duty;
- Fraud in the factum;
- Negligent representation;
- Claims based on the actions of the FDIC itself;
- State consumer fraud (UDAP) claims;
- Breach of duty of good faith and fair dealing;
- Breach of contract;
- Truth in Lending rescission;
- ECOA;
- Statute of limitations;
- Negligent infliction of emotional distress;
- Release;
- Equitable defenses such as laches;
- Failure of consideration;
- Economic duress;
- Wrongful acceleration and unreasonable sale at foreclosure; and
- Defense based on alleged alteration of documents.

This is a partial listing and NCLC's *Cost of Credit* § 10.7.8 (3d ed. 2005 and 2008 Supp.) should be consulted.

New Case Law on Claims That Survive Bank Insolvency

The following cases dealing with claims that survive bank insolvency are too recent to appear in NCLC's 2008 Supplement to *Cost of Credit* (3d ed. 2005), and will be added to a new Fourth Edition to be released later this summer.

Fraud in the Factum

Fraud in the factum, which is deemed to render an instrument entirely void *ab initio*, is defined as "the sort of fraud that procures a party's signature to an instrument without knowledge of its true nature or contents." *Langley v. FDIC*, 484 U.S. 86 (1987). It is to be distinguished from fraud in the inducement, which is not an exception to *D'Oench*. *But cf. Bank of New Glarus v. Swartwood*, 297 Wis. 2d 458, 725 N.E.2d 944 (Wis. Ct. App. 2006) (promissory note executed with loan amounts left blank does not support fraud in the factum exception to *D'Oench*, especially where loan

⁴⁴ 315 U.S. 447 (1942).

⁴⁵ Most courts have held that a flexible "super holder in due course" or "federal holder in due course" doctrine no longer exists. See NCLC, *The Cost of Credit*: § 10.7 (3d ed. 2005 & 2008 Supp.).

⁴⁶ See discussion in NCLC's *Cost of Credit* § 10.7.6.2 (3d ed. 2005 & 2008 Supp.).

documents included warning printed in bold below signature line stating: "Do not sign this if it contains blank spaces."⁴⁷

Good Faith and Fair Dealing

Connecticut Bank & Trust Co v. Lee, 1992 WL 228093 (Conn. Super. Ct. Sept. 8, 1992) (unpublished) (special defense of breach of good faith and fair dealing does not implicate *D'Oench*, as defense is not based upon unrecorded side agreement but is derived from the note itself).⁴⁸

Failure of Consideration and Fraud

DIC v. O'Flahaven, 857 F. Supp. 154 (D.N.H. 1994) (failure of consideration defense based upon non-disbursement of funds is not barred because fact of whether or not funds were disbursed should be contained in bank records); *Cinco Enterprises, Inc. v. Benso*, 995 P.2d 1080 (Okla. 1999) (state law defense of failure of consideration available to avoid liability on certain notes; no secret agreement barring defense under either *D'Oench* or § 1823(e)); *Bank of New Glarus v. Swartwood*, 297 Wis. 2d 458, 725 N.E.2d 944 (Wis. Ct. App. 2006) (*D'Oench* does not bar a failure of consideration defense based upon non-disbursement of funds).⁴⁹

Economic Duress

Desmond v. FDIC, 798 F. Supp. 829 (D. Mass. 1992) (refusing to dismiss duress categorically as a viable claim; stating that while claim or defense of duress will not always survive, it does so in this case because duress relating to lawyer's conflict of interest was "external" and therefore peripheral to agreement and did not involve any side agreement); *Thistlethwaite v. FDIC (In re Pernie Bailey Drilling Co.)*, 111 B.R. 565 (Bankr. W.D. La. 1990) (economic duress defense is not barred by § 1823(e) because defense goes to underlying validity of agreement and is not barred by *D'Oench* because "[o]ne who executes an instrument under duress may not lend himself to a scheme or arrangement likely to mislead banking authorities"). *Cf. RTC v. Ruggiero*, 756 F. Supp. 1092 (N.D. Ill. 1991) (suggesting that defense of economic duress negates "requisite contract-formative intent" so as to render an agreement void and thus unreachable by *D'Oench*, but finding it unnecessary to address question of whether defense is covered since standard of legal duress was not satisfied), *aff'd*, 977 F.2d 309 (7th Cir. 1992). *But see Bell & Murphy & Assocs., Inc. v. Interfirst Bank Gateway*, 894 F.2d 750 (5th Cir. 1990); *RTC v. A.W. Assocs., Inc.*, 869 F. Supp. 1503 (D. Kan. 1994) (economic duress, even if proven, would only render agreement voidable and not void, so *D'Oench* doctrine applies); *FDIC v. Betancourt*, 865 F. Supp. 1035 (S.D.N.Y. 1994); *First City, Texas-Beaumont, N.A. v. Treece*, 848 F. Supp. 727 (E.D. Tex. 1994); *Federal Sav. & Loan Ins. Corp. v. Maio*, 736 F. Supp. 1039 (N.D. Cal. 1989).⁵⁰

Wrongful Acceleration and Unreasonable Sale at Foreclosure

Cf. Communication Systems, Inc. v. Ironwood Corp., 930 F. Supp. 1162 (S.D. Tex. 1996) (because acceleration clause in note is not "agreement" within meaning of *D'Oench* or § 1823(e) it is admissible to show when assignee's cause of action accrued).

⁴⁷ NCLC's *Cost of Credit* Ch. 7, note 705 (3d ed. 2005 and 2008 Supp.).

⁴⁸ *Id.* at note 709.

⁴⁹ *Id.* at note 710.

⁵⁰ *Id.* at note 711.

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But see FDIC v. Bathgate, 27 F.3d 850 (3d Cir. 1994) (wrongful acceleration defense barred where it depends upon allegations relating to an unrecorded agreement).⁵¹

Equal Credit Opportunity Act

FDIC v. Piccolo, 1994 WL 32488 (Conn. Super. Ct. June 28, 1994) (ECOA counterclaim survives based upon *CMF Virginia Land, L.P. v. Brinson*, 806 F. Supp. 90 (E.D. Va. 1992) and upon fact that counterclaim is supported by signature and thus not premised upon unwritten agreement). *Cf. Cadle Co. v. Newhouse*, 300 A.D.2d 526, 756 N.Y.S.2d 48 (2002) (*D'Oench* inapplicable as ECOA claim involved guaranty executed two years prior to subject loan).⁵²

Defense Based on Alleged Alteration of Documents

Cf. FDIC v. Kagan, 871 F. Supp. 1522 (D. Mass. 1995) (material alteration of guaranty performed without knowledge or authorization forms basis of allowable fraud in the factum defense); *Haines Pipeline Constr., Inc. v. Exline Gas Systems, Inc.*, 921 P.2d 955 (Okla. Civ. App. 1996) (alteration defense based not upon an "agreement" but upon acts performed without debtor-president's consent that exonerated him from liability, according to state law, on an altered guaranty; therefore, § 1823(e) does not apply). *But see FDIC v. Gilbert*, 9 F.3d 393 (5th Cir. 1993) ("alteration of a document, standing alone, does not preclude" doctrine of estoppel; here, alteration in the form of changes to repayment provisions initiated by parties could not be asserted as a defense to the note).⁵³

New NCLC Web Pages: Bank Failures, Lender Bankruptcies, and Crisis-Driven Loan Modification Programs

NCLC recently added extensive information to its website related to bank failures, lender bankruptcies, and crisis-driven

loan modifications. Go to www.consumerlaw.org and click on "Lenders in Financial Distress." This brings you to a choice of the following three topics:

Failed Bank Pages

The "Failed Banks" pages include a Failed Bank Chart that lists the date of closure and the claims bar date. Click on the bank name and obtain more details from the FDIC website. Articles by NCLC staff and others are also posted here. This page also includes all the Purchase and Assumption Agreements available from the FDIC. When the FDIC orchestrates a sale of one bank to another before the troubled bank fails (as in the Wachovia to Wells Fargo deal) or sells some or all of a failed bank's assets and liabilities (as has been the case for most of the banks closed since 2008), the parties enter into a P&A agreement. Important provisions in this document address which assets and liabilities are transferred, which remain with the FDIC, and whether borrower claims and/or defenses are explicitly waived. Until recently, the FDIC website only included the WAMU P&A. Others are now available on this page as a result of a NCLC FOIA request sent to the FDIC.

Lender Bankruptcy Pages

The Lender Bankruptcy pages focus on chapter 11 lender and servicer bankruptcies. Judges' orders pertaining to claim bar dates, transfer of assets, confirmation of plan, as well as voluntary petitions and chapter 11 plans are included on these pages.

Loan Modification Site

Within the last year, several loan modification and refinancing programs have emerged in an effort to minimize the number of foreclosures. NCLC created a Loan Modification site to provide a more comprehensive understanding of what the industry and government are doing to combat the rising tide of foreclosures. This site includes a chart that summarizes the industry and government sponsored loan modification programs and contains links to relevant source documents.

⁵¹ *Id.* at note 713.

⁵² *Id.* at note 722.

⁵³ *Id.* at note 732.