
Credit Union Attorney

Law Letter

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Out-of-State Bank Could Not Be Sued in North Dakota Even Though It Filed a Financing Statement There, Annually Inspected Collateral There, & Occasionally Made Loans to North Dakota Residents

In *Ensign v. Bank of Baker*, No. 2003024 (N.D. Mar. 23, 2004), the North Dakota Supreme Court held that a Montana Bank had insufficient contacts with the state of North Dakota for a trial court in North Dakota to hear a case brought against the Bank by a North Dakota resident seeking to establish the superiority of his lien over the Bank's.

Facts

The Bank of Baker was a Montana corporation with its principal place of business in Baker, Montana. It has no branches located in North Dakota. It did not solicit customers in North Dakota but occasionally

loaned money to customers who lived in North Dakota. Loans made to North Dakota customers were originated in Montana.

From August 1996 to May 1999, the Bank loaned money to Lee and Donna Lewis, a married couple, who resided in Montana and raised buffalo for slaughter on their ranch in Carter County, Montana. The Lewises secured their loans, in part, with buffalo. They executed a security agreement granting the Bank a security interest in all buffalo and "products and proceeds thereof." The Bank perfected the security interest by filing a financing statement with the Montana Secretary of State.

Gene Ensign was a farmer and rancher who operated a custom buffalo-feeding business near Scranton in Bowman County, North Dakota. Ensign was not a Bank customer.

In 2000 and 2001, the Lewises entered into contracts with Ensign to feed their buffalo. During those two years, the Lewises delivered more than 200

buffalo to Ensign's feedlot. Upon receiving the buffalo, Ensign filed with the Bowman County Recorder two agricultural supplier's liens covering the buffalo.

The Bank, upon learning that the Lewises had sent their buffalo to North Dakota, filed an additional financing statement with the North Dakota Secretary of State. Thereafter, on two occasions, the Bank sent an employee to Ensign's North Dakota feedlot to inspect its buffalo collateral.

The Lewises eventually defaulted on their loans from the Bank. In January 2002, the Lewises sold 43 buffalo for \$19,019.33. The check was made jointly payable to the Bank, Lee Lewis, Ensign, and the Farm Service Agency ("FSA"). The Bank retained possession of it. In July 2002, 40 buffalo were sold for \$18,480. The check was again made jointly payable to the Bank, Lee Lewis, Ensign, and the FSA. Ensign retained possession of the July check.

Suit Over Proceeds From Buffalo Sales

Ensign brought suit against the Bank in a North Dakota state trial court to determine his priority to the checks and to obtain a money judgment against the Bank for the face amount of the checks. The Bank moved to dismiss the complaint, arguing, among other things, that a North Dakota trial court did not have personal jurisdiction over the Bank.

Personal Jurisdiction

Under the Due Process Clause of the U.S. Constitution, a state court cannot exercise jurisdiction over a non-resident defendant unless that non-resident has sufficient contacts with the state to make it fair to require defense of the action in the state. Also, every state has a statute called a "long-arm statute" that governs when that courts within the state can exercise jurisdiction over non-resident defendants. North Dakota's long-arm statute, like that of most states, is designed to permit the exercise personal jurisdiction over non-residents to the fullest extent permitted by the federal Due Process Clause.

The question of whether a non-resident defendant has sufficient contacts with a state to make it fair to exercise personal jurisdiction over the defendant is a question of law that is decided on the facts of each individual case.

Bank's Contacts with North Dakota

In this case, the Bank maintained no place of business in North Dakota. It occasionally made loans to North Dakota residents, but did not solicit or close those loans in North Dakota. Further, this loan was not a loan made to a North Dakota resident. The Lewises were Montana residents. They merely sent a portion of the collateral securing their loans to North Dakota after the loans had been made. The Bank's only contacts with North Dakota were filing a financing statement in North Dakota after the buffalo arrived there and inspecting the buffalo annually for the two years they were there.

Trial Court Finds Sufficient Contacts

The trial court held that the Bank's contacts with North Dakota were sufficient to require the Bank to defend Ensign's suit in North Dakota. Therefore, the court denied the Bank's motion to dismiss for lack of personal jurisdiction. Ensign moved for a judgment without a trial, arguing that his agricultural supplier's lien had priority over the Bank's security interest. He sought a judgment against the Bank for the value of both the January and July 2002 checks, plus additional compensation for his care of the buffalo. The Bank made a cross-motion for summary judgment, arguing the agricultural supplier's lien was defective and Ensign was not owed anything. The trial court granted a judgment against the Bank in the amount of \$88,857.59 plus costs. The Bank appealed.

Appellate Court Reverses

On appeal, the North Dakota Supreme Court reversed the trial court's ruling that personal jurisdiction existed. The court reasoned that this case did not arise out of a loan to a North Dakota resident or a similar situation in which the Bank could be said to have purposely directed its activities toward North Dakota. Rather, the Bank's sole activities in the North Dakota

were aimed at protecting its collateral. In such situations, the Supreme Court ruled, that it would be unfair to require the Bank to come to North Dakota to defend the suit.

* * *

Bank Cannot Ignore Court Order Enjoining It from Paying a Certified Check

In *Dalessio v. Kressler*, 2004 N.Y. Slip Op. 01555 (N.Y.A.D. 2 Dept. Mar. 8, 2004), a New York appeals court held that a bank cannot ignore a court order enjoining the bank from paying a certified check.

Facts

In May 1998, Benito Dalessio wanted to marry a Jennifer Lopez. Lopez introduced Dalessio to Linda Kressler who told him that Lopez owed her certain debts that had to be paid before Lopez could marry.

Several months later, on November 9, 1998, Dalessio drew a check payable to Kressler for \$107,000 on his account at Republic National Bank of New York (hereafter "the Bank"), had the check certified by the Bank, and gave the certified check to Kressler.

Two days later, having realized that he was the victim of a fraud, Dalessio retained an attorney to help him stop payment on the certified check. The attorney drafted and filed a verified complaint naming both Kressler and the Bank as defendants. The Bank was included for the sole purpose of stopping payment on the certified check.

On November 12, 1998, a trial court issued an order temporarily restraining "Defendant, REPUBLIC NATIONAL BANK OF NEW YORK ... from transferring paying or otherwise disposing of funds in the sum of \$107,000.00 heretofore certified from"

Dalessio's account, pending a hearing and determination of permanent relief.

The next day, the temporary restraining order was personally served on the Bank's Assistant Treasurer at 11:30 A.M. The same day, the certified check was presented for payment, and the Bank paid it.

Uniform Commercial Code Provisions at Issue

Later, the court held a hearing to determine whether the Bank should be held liable for paying the certified check. There, the Bank defended payment of the certified check by arguing that Uniform Commercial Code ("UCC") § 4-303 "required it to honor payment on a certified check regardless of a subsequently received stop payment order," including a court-issued stop payment order.

The portion of UCC 4-303 relied upon by the Bank states in pertinent part: "Any ... legal process served upon ... a payor bank, whether or not effective under other rules of law to terminate, suspend, or modify the bank's right or duty to pay an item ... comes too late to so terminate, suspend, or modify such right or duty if the ... legal process is received or served ... after the bank has ... accepted or certified the item." The Bank argued that the term "legal process" included court orders enjoining payment of a certified check.

Dalessio countered that UCC § 3-603 expressly recognizes the power of courts to issue injunctions to stop payment of certified checks. Section 3-603 states in pertinent part, a bank's liability is discharged once payment is made "even though it is made with knowledge of a claim of another person to the instrument, *unless prior to such payment or satisfaction the person making the claim ... enjoins payment or satisfaction by order of a court of competent jurisdiction.*" (Emphasis supplied.)

The trial court ultimately determined that UCC §§ 4-303 and 3-603 were in conflict with one another and that the provisions of § 4-303 were controlling; therefore, a court issued injunction could not stop payment of a certified check. Dalessio appealed.

**Courts Have Authority to
Stop Payment of Certified Check**

On appeal, the New York appeals court disagreed with the trial court's conclusion regarding a court's ability to stop payment of a certified check.

The appeals court explained that the term "legal process" in UCC § 4-303 did not refer to a court order enjoining payment; rather, it referred to proceedings to secure payment of a debt, such as garnishment, attachment, and execution proceedings.

The court went on to hold that, where as here, the trial court issued an order enjoining payment of a certified check, the Bank should have complied with the order. Depending on the circumstances surrounding the non-compliance, the court held, a bank could be liable for damages and held in civil or criminal contempt for failure to obey the order.

* * *

**The Term "Prime Rate" Is Not So
Generally Understood to Mean the
Lowest Rate Available to a Bank's
Most Creditworthy Borrowers that
Failure to Disclose that Some
Borrowers Obtained Loans with
Interest Rates Below Prime Rate
Constitutes Fraud**

In *Lum v. Bank of America*, 361 F.3d 217 (3d Cir. 2004), the Third Circuit Court of Appeals affirmed the dismissal of a complaint alleging that several banks had violated the Sherman Antitrust Act, 15 U.S.C. § 1, and the Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. § 1962(c), § 1962(d) ("RICO"), by reporting to major financial publications as their "prime rate" a rate above that charged to their most creditworthy borrowers. The court concluded that the allegations stated no claim under the Sherman Act or RICO.

Facts

In April 1987, Hing and Debra Lum obtained a home equity loan from Morris County Savings Bank. The Lums' interest rate was two percentage points

above the prime rate, as reported in *The New York Times*.

In 1990 and 1991, Debra Lum received credit cards from Bank of America and Chase Manhattan Bank. Both cards had interest rates tied to the prime rate reported in the *Wall Street Journal*. Bank of America's credit card agreement defined its "prime rate" as "the base rate on corporate loans at large U.S. money center commercial banks." With respect to prime rate, the Chase Manhattan agreement stated: "For purposes of this Agreement, the Prime Rate as published in 'Money Rates' table of *The Wall Street Journal* or any other newspaper of national circulation selected by us is merely a pricing index. It is not, and should not be considered by you to represent, the lowest or the best interest rate available to a borrower at any particular bank at any given time."

The Lums' Suit

On January 14, 2000, the Lums filed a complaint in a federal district court against 12 Banks--including Morris County Savings Bank's successor in interest, Bank of America, and Chase Manhattan Bank--alleging that from April 22, 1987, to the present the Banks had formulated and carried out a fraudulent plan, scheme, and conspiracy to report as their prime rates, rates far in excess of those charged to their largest and most creditworthy customers, to effectively raise the interest rates on credit instruments tied to prime. The Lums argued that the Banks' conduct violated the Sherman Act and RICO.

The Banks moved to dismiss the Lums' complaint on the grounds that it failed to state a cause of action. The federal district court agreed with the Banks and granted a dismissal. The Lums appealed.

Appeals Court's Ruling

On appeal, the Third Circuit agreed with the district court that the Lums' allegations failed to state a cause of action under the Sherman Act or RICO, because, first, where the term "prime rate" in the Lums' loan and credit card documents was defined, it was not defined as the interest rate charged to the most creditworthy borrowers; and, second, the term "prime rate" is not so generally understood to mean the rate charged the most creditworthy borrowers as to render the Banks guilty of

fraud for reporting a higher rate as prime.

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