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Reporting recent legal developments important to lending in Louisiana

By the Bankruptcy and Commercial Lending Groups of Lemle & Kelleher, L.L.P.

Claims Traders Beware

Louisiana Civil Code article 2652 offers a unique remedy to a defendant in a lawsuit where a plaintiff has sold the claim against it-- the defendant may extinguish the claim by paying the purchaser the price paid for the claim plus interest. This remedy is known as the redemption of litigious rights doctrine.

A recent Louisiana Supreme Court decision makes clear that a promissory note becomes a litigious right where a lender files suit thereon and the borrower answers and denies liability. If the lender were to assign such a note prior to judgment, the borrower would be entitled to redeem the note from the purchaser for the price paid plus interest. The Louisiana Supreme Court also indicated that the borrower's right of redemption may continue to be exercised even after the borrower emerged from bankruptcy.

In *Luk-Shop, L.L.C. v. Pinewood LaPlace Associates, L.L.C.*, 802 So. 2d 1291 (La. 2002), a lender filed suit against a borrower on a promissory note. The borrower answered the suit and denied liability on the note. The borrower then filed bankruptcy. After the bankruptcy filing and shortly before the debtor "emerged from bankruptcy," the lender assigned its claim to a purchaser. The Court did not explain whether "emerged from bankruptcy" meant that the debtor confirmed its plan or its bankruptcy case was closed.

More than a year after the borrower emerged from bankruptcy, the purchaser of the claim filed suit on the note against the borrower. The borrower claimed that it was entitled to terminate the suit by redeeming the litigious right for the amount paid by the purchaser for the note.

The Louisiana Supreme Court held that the underlying obligation, the debt, was a litigious right because it was "contested in a suit already filed." Thus, once the borrower denies liability on the note it becomes a litigious right, and the purchaser takes it subject to the borrower's right of redemption.

The Court did not address whether the bankruptcy case or bankruptcy law had any effect on the issue. What happened to the claim in the bankruptcy case? Since the purchaser of the note again filed suit on the note in state court presumably the claim was allowed. Would allowance of the claim in the bankruptcy case preclude the borrower's defense to the note and right of redemption? The implication from the *Luk-Shop* decision may be that allowance of a claim in bankruptcy does not alter a borrower's perpetuation denial of liability in a suit on the note for purposes of the litigious rights



doctrine. Claims traders should also keep in mind that an objection to a claim in a bankruptcy case will likely trigger the litigious rights doctrine.

The litigious rights doctrine does not apply to federal regulatory agencies who obtain and transfer obligations acquired from failing banking institutions according to the Louisiana Second Circuit Court of Appeal. *Peoples Homestead Federal Bank and Trust v. Laing*, 637 So.2d 604 (La.App. 2 Cir. 5/4/94). Application of the doctrine in this situation would impede the expeditious method by which federal regulators intervene in failing institutions.

Uniform Fraudulent Transfer Act Adopted...how does it compare to the revocatory action?

Louisiana has joined nearly half of the states that have enacted the Uniform Fraudulent Transfer Act. However, Louisiana's revocatory action remains in effect. What is the difference?

Effective August 15, 2003, La. R.S. 9:2790 ("UFTA") allows a creditor to avoid certain acts of a debtor in varying circumstances depending upon whether the creditor existed at the time of the transfer. Regardless of when the rights of the creditor arose, a creditor may avoid a debtor's transfer that was intended to hinder, delay, or defraud the creditor. In addition, regardless of when the rights of the creditor arose, a creditor may avoid a debtor's transfer where the debtor did not receive reasonably equivalent value if (i) the debtor's remaining assets were unreasonably small in relation to the business in which he was engaged or to be engaged, or (ii) the debtor intended to incur or believed or should have believed that he would incur debts that were beyond his ability to pay.

A creditor whose rights arose before the transfer occurred may avoid a transfer where the debtor did not receive reasonably equivalent value and the debtor was insolvent or became insolvent as a result of the transfer. In addition, an existing creditor may avoid a transfer to an "insider" if the transfer was made for an antecedent debt, the debtor was insolvent at the time, and the insider had reasonable cause to believe that the debtor was insolvent. The term "insider" includes an entity controlled by the debtor or a relative.

The UFTA action did not replace the revocatory action, Louisiana's civil law remedy for creditors facing newly insolvent debtors. The revocatory action allows a creditor to annul an act that causes or increases the insolvency of obligor. Unlike UFTA, the revocatory action only enables a creditor to annul an act of the debtor that arose after the rights of the creditor arose. Further, unlike the UFTA, the revocatory action does not allow the annulment of transfers based upon intent to defraud or of any transfers made while the debtor was solvent or that did not cause the debtor's insolvency.

If a particular transfer satisfies the standards for a revocatory action or a UFTA action, creditors should assert both actions. The "cause or increase insolvency" standard, while similar to the "reasonably equivalent value" standard, may be easier to establish.

Both the UFTA action and the revocatory action require that the creditor file the action within one year of the date that the creditor knew or should have known of the act. However, regardless of



knowledge, the revocatory action must be filed within three years from date of the act but the UFTA action may be filed within four years of the act.

Bank's right of setoff trumps garnishing creditor

In *A&B Bolt and Supply Inc. v. Standard Offshore Services, Inc.*, 858 So.2d 509 (La.App. 1 Cir. 6/27/03), a judgment creditor instituted a garnishment proceeding against the debtor's bank. The bank filed its answers to the judgment creditor's interrogatories, admitting its possession of the debtor's account but claiming the account was subject to the bank's security interest and statutory pledge for a promissory note that was in default. The Louisiana First Circuit Court of Appeal held that because the debtor had defaulted on the promissory note, the bank was entitled to utilize the provisions of La. R.S. 6:316 and apply the funds in the account towards the payment of the indebtedness on the note. Moreover, the notice requirement found in La. R.S. 6:316 did not, in the court's opinion, operate to nullify the depository bank's right to the statutory setoff remedy if such notice was not provided. The court noted that it was not bound to follow *Chrysler Credit Corporation v. Whitney National Bank*, 798 F. Supp. 1234 (E.D. La. 1992) where the court held that the bank must comply with the notice provision of La. R.S. 6:316(D) and provide the court evidence of same to avail itself of the statutory setoff remedy.

Fees in Judgment Must Be Precise

A recent decision finds that a judgment on a note that includes an award for "reasonable attorneys fees" may be reversed as imprecise. A judgment on a note should state the specific amount of the attorney and other fees due thereon.

In *Security National Partners v. Baxley*, 859 So.2d 890 (La.App. 2 Cir 10/29/03), the holder of two promissory notes obtained a judgment that included indeterminate awards (no amounts were listed) for "advanced escrow payments and late fees" and "reasonable attorneys fees". The borrower appealed the judgment on a number of bases, including that the judgment was not precise, definite and certain as required by Louisiana law. Although rejecting the borrower's other issues on appeal and holding that the lender was entitled to enforce the note, the Louisiana Second Circuit Court of Appeal did agree that the trial court's indeterminate awards for advanced escrow payments, late fees, and reasonable attorneys fees were insufficiently precise, indefinite and uncertain. According to the Court, the specific nature and amount of damages should be determinable from a judgment without reference to an extrinsic source such as pleadings or reasons for judgment.

Action for unfair collection practices recognized under state law

Debt collectors are familiar with the Fair Debt Collection Practices Act, 15 U.S.C. 1629 et seq. However, this federal act does not preclude an action under state law for coercive unreasonable acts to collect a debt.

In *Hairford v. Centurytel Inc.*, 856 So.2d 139 (La.App. 3 Cir. 10/1/03), the plaintiff was an elderly widower who received a letter from his telephone company stating that the balance due on a





woman's previous telephone number was being transferred to his account. The telephone company's records indicated that the woman had been an authorized user on the plaintiff's account and that she was the customer's wife. When the plaintiff informed the company that he was not married to the woman and not responsible for her account, it told him that he had to prove that she was not his wife, and then debited the plaintiff's bank account for her debt. Although the bank intervened and immediately reversed the charges, the plaintiff sued the telephone company for damages for mental anguish. The trial court awarded the plaintiff \$4,500.

On appeal, the Louisiana Third Circuit affirmed the trial court, holding that the telephone company's actions amounted to negligent, improper, and unreasonable tactics employed in the collection of an alleged debt. The Third Circuit explained that Louisiana recognizes a cause of action for unreasonable and intentionally coercive debt collection efforts regardless of whether the debt is justly due. "Essentially, we are called upon in this case to determine if the balance between the creditor's interest in using reasonable collection efforts and the debtor's privacy and emotional interest has been upset."

New Rules For Louisiana Notaries

Effective January 1, 2004, and pursuant to Act No. 1142, Louisiana notaries are required to place their notary identification number with their hand-printed or typewritten name under their signature on notarized documents, and to include the hand-printed or typewritten name of the witnesses under the signatures, along with the printed names of the parties. Notaries who are also attorneys can use their bar roll number in lieu of a notary identification number. After January 1, 2005, documents without a notary identification number and printed names cannot be accepted for filing by state agencies or clerks of court. Notary identification numbers will be assigned and posted on the internet.

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This publication and the information herein is not legal advice and is not intended to serve as a substitute for consultation with an attorney. Specific legal issues and concerns require the advice of an attorney.

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