

THE LOUISIANA LENDER LETTER

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SANCTIONS ASSESSED AGAINST LENDER AND COUNSEL— MAKE SURE SWORN STATEMENTS ARE ACCURATE AND DO NOT SERVE AS FACT WITNESS FOR CLIENT

In *In Re Osborne*, 375 B.R. 216 (Bankr. M.D. La 2007), the Bankruptcy Court Judge for the Middle District of Louisiana, Douglas Dodd, sanctioned a mortgage lender and its counsel \$46,976.72 for using a false affidavit to obtain relief from the automatic stay. The Court had entered a Consent Order providing that the lender could obtain relief from the automatic stay by filing an affidavit that the Chapter 13 debtor failed to make the required monthly mortgage payments. The lender then filed an *ex parte* motion seeking relief from the automatic stay with an affidavit by lender's counsel declaring that the debtor failed to make the payments required by the Consent Order. The Court granted the motion and entered an order lifting the stay.

However, the debtor was not in default at the time the lender filed its *ex parte* motion and its counsel signed the affidavit. According to the Court, lender's counsel had "absolutely no personal knowledge" of the debtor's default. The Court held that counsel's conduct in obtaining relief from the stay without a sound factual basis warranted sanctions under 28 U.S.C. § 1927. Section 1927 authorizes courts to sanction lawyers who unreasonably and vexatiously multiply court proceedings. Additionally, the Court held that the lender and its counsel willfully abused the bankruptcy process and sanctions were appropriate under 28 U.S.C. § 105, which empowers bankruptcy courts to sanction both parties and counsel who willfully abuse the judicial process. In so holding, the court warned that attorneys should not serve as fact witnesses for their clients, even regarding uncomplicated matters, including alleged defaults under Chapter 13 adequate protection orders.

FEDERAL COURT HOLDING REITERATES LENDERS PROTECTION IN FLOOD ZONE DETERMINATION

In *Duong v. Allstate Ins. Co.*, 499 F. Supp. 2d 700 (E.D. La. 2007), a borrower sued its home lender after his home was damaged by Hurricane Katrina flood waters for negligently performing a flood zone determination. The court held that no federal cause of action exists against a home lender for failure to make a proper flood zone determination as required by the National Flood Insurance Act ("NFIA"), 42 U.S.C. § 4012(a). Additionally, the court held that the mortgagor failed to state a claim under Louisiana law against the home lender for negligent misrepresentation, since a lender has no duty to share a flood zone determination with the borrower. The court explained a flood zone determination is undertaken for the benefit of the lender, not the borrower.

CREDITORS BEWARE: CHAPTER 11 PLAN MUST PRESERVE LIENS

The Fifth Circuit has now made clear that lenders should not rely on the adage that "liens pass through bankruptcy unaffected." In *In Re Ahern Enterprises, Inc.*, 507 F.3d 817 (5th Cir. 2007), a creditor held a judicial lien on the debtor's property. The Bankruptcy Court confirmed a plan which preserved the bank's conventional lien on the property but did not mention the judicial creditor's lien. The Fifth Circuit joined the Fourth, Seventh, Eighth, and Tenth Circuits and held that 11 U.S.C. § 1141(c) provides that confirmation of the Chapter 11 plan "voids liens not preserved by the plan, provided that the plan dealt with the property to which they attach and the lien holder participates in the reorganization." The Fifth Circuit determined that the judgment creditor could have objected and asserted its position that the judicial lien was preserved by appealing the order confirming the reorganization plan. Since the judgment creditor participated without objection in the reorganization and the confirmed plan dealt with the property subject to the lien without preserving it, the judgment creditor's lien was voided upon confirmation of the Chapter 11 plan. This case illustrates the importance of secured creditors making certain that their mortgages, liens, and security interests are recognized and preserved in the debtor's Chapter 11 plan.

LENDER LOSES SECURITY INTEREST WHEN COLLATERAL CROSSES STATE LINES

In *First Nat. Bank of Picayune v. Pearl River Fabricators, Inc.*, No. 2006-CC-2195, 2007 WL 3407401, at *1 (La. November 16, 2007), the Louisiana Supreme Court held that the failure of a secured party to timely re-perfect its security interest within a year after the transfer to a person located in another jurisdiction, as required by La Rev. Stat. Ann. § 10:9-316, resulted in the security interest becoming unperfected. In this case, a Mississippi borrower obtained a \$200,000 loan from a Mississippi bank. To secure the loan, the borrower executed a security agreement in favor of the bank, identifying the collateral. The bank then filed and recorded a UCC-1 financing statement in Mississippi adequately describing the property subject to its security interest. Although the security agreement between the borrower and the bank prevented the borrower from transferring the collateral without prior written consent of the bank, the borrower sold the collateral to an Indiana company without the bank's consent. The Indiana company then sold the collateral to a company located in Louisiana, and the Indiana company filed a UCC-1 financing statement identifying it as the secured party. After the collateral was physically moved from Mississippi to Louisiana, the Mississippi bank filed a Louisiana UCC-1 financing statement more than a year after the transfer of the collateral from the Indiana company to the Louisiana company. After the Mississippi borrower defaulted on its obligation to the Mississippi bank, the bank filed its petition for executory process and sequestration in Louisiana. The Louisiana company that bought the collateral sought to dissolve the writ. After conflicting rulings by the district and appellate courts, the Louisiana Supreme Court held that the bank failed to re-perfect its security interest prior to the lapse of the one-year period after the transfer of the collateral to a buyer located in another jurisdiction as required under La. Rev. Stat. Ann. § 10:9-316. Pursuant to La. Rev. Stat. Ann. § 10:9-316(b), the bank's failure to timely re-perfect its security interest in the collateral in Louisiana prior to the lapse of its security interest resulted in its security interest becoming unperfected and deemed to have been never perfected against the Louisiana company, a purchaser of the collateral for value. Additionally, the Court held that the buyer's constructive notice of the bank's security interest when purchasing the collateral did not prevent the lapse of the security interest as a result of the bank's failure to re-perfect its interest in Louisiana.

ATTORNEY'S FEES OUTRANK MORTGAGEE'S INTEREST

In *Irons v. U.S. Bank, Inc.*, 2007-0570, (La. App. 4 Cir. 8/14/07); 966 So. 2d 646, the Louisiana Court of Appeal for the Fourth Circuit held that a law firm's privilege for its contingency fee was superior to a mortgagee's interest as an additional loss payee under insurance policies. As a result of Hurricane Katrina, several homeowners who suffered damages to their residences were dissatisfied with the amount of the initial settlements from their insurance companies. The homeowners retained legal counsel to pursue their claims for additional amounts. The homeowners entered into contingency fee contracts with a law firm who managed to successfully obtain increased recoveries from the insurers. The mortgage holder of each homeowner's residence was an additional loss payee on each of the insurance policies. The settlement checks were made payable to the homeowner, the mortgage holder, and the law firm. The law firm requested that the mortgage holder endorse the checks so that it may deposit the settlement amounts into its client escrow account before disbursing the funds. After the mortgage holder refused to endorse the checks, the law firm commenced a concursus proceeding in order to determine each party's entitlement to the disputed funds. The trial court granted a summary judgment against the mortgage holder determining that the law firm's privilege was superior to the mortgage holder's interest as an additional loss payee under the insurance policies. The Court of Appeal for the Fourth Circuit affirmed, relying on La. Rev. Stat. Ann. § 37:218(A) to find that a law firm's privilege for its contingency fee is superior to the mortgagee's interest as additional loss payee under the insurance policies.

SEVENTH CIRCUIT HOLDS THAT YIELD MAINTENANCE PREPAYMENT PREMIUM ENFORCEABLE

In *River East Plaza, L.L.C. v. The Variable Annuity Life Insurance Company*, 498 F.3d 718 (7th Cir. 2007), the U.S. Court of Appeals for the Seventh Circuit held that a "Treasury-flat" yield maintenance prepayment premium in a commercial note is enforceable under Illinois law. In *River East*, the borrower sought a mortgage loan to finance the purchase and development of a retail store. The lender required that the note include a yield maintenance prepayment clause, which would ensure that a prepayment did not deprive the lender of the bargained for yield over the life of the loan.

Several years after the loan closed, the borrower sought to prepay the loan but disputed the enforceability of the prepayment premium. Eventually, the borrower paid the premium under protest and then brought suit against the lender. In upholding the enforceability of the yield maintenance premium, the Seventh Circuit found that the prepayment clause was an agreed upon alternative form of performance under the contract and not a disguised penalty. The Court noted that, under Illinois law, the lender could have expressly precluded the borrower from any prepayment on the loan. Instead, the lender accommodated the borrowers with the option to prepay the loan subject to the borrowers paying the required yield maintenance prepayment premium.

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Our bankruptcy and loan restructuring attorneys are particularly experienced in large, complex bankruptcies and in the representation of secured and unsecured creditors, lessors, lessees, debtors, and others. Our diversified client base includes the entire spectrum of competing interests in this field: financial institutions, developers, service companies, wholesalers, and many other types of businesses, as well as individuals. We represent lenders on a regular basis and have defended numerous lender liability claims in connection with this representation. Our representation of banks and other financial institutions in this area is well-known and highly respected.

ABOUT LEMLE & KELLEHER, L.L.P.

Lemle & Kelleher is one of the oldest major law firms in Louisiana, tracing its origins to the late 19th century when New Orleans was experiencing a boom as the shipping and commercial center of the South. Building on that genesis, we have diversified and expanded our capabilities for more than 100 years to meet the growing needs of our clients regionally and nationally. Today, Lemle & Kelleher offers responsive, innovative, and experienced legal representation covering a broad range of practice areas. For more information please visit www.lemle.com.



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