

Cullen and Dykman Successfully Dismissed a Cross-Claim Made Against One of its Lending Clients

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Cullen and Dykman successfully dismissed a cross-claim made against one of its lending clients (the “Lender”) by a party (the “Competing Party”) asserting a security interest senior to the Lender in a substantial bank account, paving the way for the Lender to obtain possession of the funds in the account in partial satisfaction of a significant judgment debt owed by the debtor/account-holder.

Both the Lender and the Competing Party were named as defendants in an interpleader action brought by the depository bank on the grounds that they (and possibly others) asserted competing claims to the funds in the deposit account. Each of the Lender and the Competing Party filed cross-claims against the other asserting priority to the funds in the account, and the Lender successfully moved to dismiss the cross-claim against it.

In its cross-claim, the Competing Party asserted that prior to the time that the Lender levied on the depository account, it perfected a security interest in the funds by exercising “control” over the account. In dismissing the cross-claims against the Lender, the Court found that the Competing Party failed to satisfy the requirements of perfecting a security interest in a deposit account under the Uniform Commercial Code (the “UCC”). Under section 9-104(a) of the UCC, in order to obtain control of a deposit account, one of three scenarios must be met: (a) the secured party (here, the Competing Party) is the bank with which the deposit account is maintained; (b) the debtor, secured party and the depository bank have agreed in an authenticated record (i.e., a control agreement) that the depository bank will comply with instructions originated by the secured party directing disposition of funds in the deposit account without further consent by the debtor; or (c) the secured party becomes the bank’s customer with respect to the account. In ruling on the motion to dismiss, the Court found that: (1) the Competing Party was not the depository bank; (2) there was no control agreement among the necessary parties that the Competing Party would have control over the account (and the evidence the Competing Party submitted in support of that contention—only signed by one party—actually provided that three different parties, of which they were only one, needed to consent to disbursements from the account); and (3) the Competing Party did not assume the identity of the accountholder.

With this ruling, the Lender can seek possession of the funds in a further pleading to the Court. This decision serves as a good reminder that a security interest in a deposit account cannot be perfected by simply filing a UCC-1 financing statement. Instead, valid assertion of control over the account must be made by executing a

proper control agreement signed by all appropriate parties (unless of course the secured party is the depository bank or somehow takes ownership of the account). Without that, an otherwise secured party may be out of luck in reaching a deposit account.

About Cullen and Dykman's Bankruptcy and Creditors' Rights Practice

Cullen and Dykman's Bankruptcy and Creditors' Rights practice offers clients a unique perspective into the issues involved in complex bankruptcy proceedings in a wide range of industries. We have represented secured creditors, debtors, unsecured creditors' committees, and individual unsecured creditors in Chapter 11 cases filed throughout the country, and we are skilled in resolving issues among various constituencies in complex Chapter 11 proceedings. We also have significant experience in out-of-court workouts, restructurings and bankruptcy litigation, and we have secured favorable results for our clients in complex bankruptcy cases throughout the country.

About Cullen and Dykman

Cullen and Dykman (www.cullenllp.com) has been providing legal services to institutional clients since 1850. The firm represents a wide range of clients, including banks and other financial institutions, energy, telecommunications and water companies, construction companies, insurers, educational institutions, religious organizations, and not-for-profits. With over 190 attorneys in seven offices located throughout the Northeast and MidAtlantic regions, Cullen and Dykman is strategically positioned to meet the changing needs and demands of our clients.

Practices

- Bankruptcy and Creditors' Rights

Attorneys

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