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Commercial Law

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Overview

During the past survey period, the Tenth Circuit Court of Appeals addressed a number of divergent issues in the area of commercial law. The most noteworthy decisions include a limitation on Federal Home Loan Bank Board authority, and limitation of bank liability under Article Three of the Uniform Commercial Code. As in the past, bankruptcy decisions dominated the commercial area. The cases were divided between those decided under the repealed Bankruptcy Act of 1898 and those decided under the Bankruptcy Reform Act of 1978. Where pertinent, the decisions under the repealed Act have been analyzed under the Reform Act to indicate the current status of the law. Additionally, the Tenth Circuit decisions affected other commercial areas including secured transactions, Truth in Lending, and usury. This article will discuss the majority of the reported commercial decisions of the past term, and will analyze the appellate court's most noteworthy decisions.

I. Uniform Commercial Code

A. *Negotiable Instruments*

The Tenth Circuit Court of Appeals refused to find a standard of care based on negligence implicit in section 3-405 of the Uniform Commercial Code (U.C.C. or the Code), finding the drawer of the check responsible for the loss in *Western Casualty & Surety Co. v. Citizens Bank of Las Cruces*.[1] Western Casualty & Surety Co.[2] brought suit against the Citizens Bank of Las Cruces and the Bank of New Mexico alleging that the banks failed to comply with reasonable commercial banking practices and standards in the handling of public monies. Western accepted a fraudulently procured and improperly indorsed warrant of the State of New Mexico for payment in the amount of \$395,000.[3] The district court granted summary judgment in favor of the defendant banks on all claims. The issues presented on appeal were whether the banks were entitled to the statutory defense of section 3-405 of the Code[4] and, if so, what standard of care is required by section 3-405.

The Tenth Circuit court found section 3-405[5] directly applicable. An employee of the drawer, the State of New Mexico, supplied the State with the name of a payee, the Greater Mesilla Valley Sanitation District, a ficti-

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1. 676 F.2d 1344 (10th Cir. 1982).
2. Western Casualty was subrogated to the claims of the State of New Mexico by virtue of its payment as surety on an employee blanket bond for state employees. *Id.* at 1345.
3. The warrant was presented to, accepted, and processed by Citizens Bank, and forwarded to the Bank of New Mexico, fiscal agent for the state, for payment from state funds. *Id.*
4. N.M. Stat. Ann. § 55-3-405 (1978).
5. *Id.* Section 3-405 of the U.C.C. states in pertinent part:

   (1) An indorsement by any person in the name of a named payee is effective if:
   (a) an imposter by use of the mails or otherwise has induced the maker or

tious sanitation district,[6] "intending the latter to have no . . . interest" in the instrument issued.[7] Section 3-405 places the loss on the drawer-employer who is in a position to prevent such forgeries by its employees.[8] Western Casualty argued that the banks were not entitled to the protection of section 3-405 because the indorsement was not identical to the name of the payee,[9] and section 3-405 requires indorsement "in the name of a named payee."[10] The Tenth Circuit held that the difference in spelling between the indorsement, *Greater* Mesilla Valley Sanitation District, and the name of the payee, *Grater* Mesilla Valley Sanitation District, was not significant and would not defeat the banks' protection from loss under section 3-405.[11]

Western Casualty Co. also argued that the banks acted negligently in accepting, processing, and making payment on the fraudulently procured warrant. Section 3-405 does not stipulate a requisite standard of care for banks and the New Mexico courts have not addressed the issue.[12] Judge McKay's opinion in *Western Casualty* noted that there is a split of authority on the issue of whether a bank's negligence precludes protection from loss under section 3-405.[13] Some authorities argue that a drawer should be able to proceed against a bank on a common law action for negligence under

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drawer to issue the instrument to him or his confederate in the name of the payee; or

(b) a person signing as or on behalf of a maker or drawer intends the payee to have no interest in the instrument; or

(c) an agent or employee of the maker or drawer has supplied him with the name of the payee intending the latter to have no such interest.

6. The warrant was issued to a fictitious entity, the Greater Mesilla Valley Sanitation District, which had been created by two state employees to defraud the State of money. 676 F.2d at 1345.

7. N.M. STAT. ANN. § 55-3-405(1)(c) (1978).

8. Comment 4 to § 3-405 of the U.C.C. explains the rationale for placing the loss on the drawer in such cases under § 3-405(1)(c):

> [T]he loss should fall upon the employer as a risk of his business enterprise rather than upon the subsequent holder or drawee. The reasons are that the employer is normally in a better position to prevent such forgeries by reasonable care in the selection or supervision of his employees, or, if he is not, is at least in a better position to cover the loss by fidelity insurance; and that the cost of such insurance is properly an expense of his business rather than of the business of the holder or drawee.

U.C.C. § 3-405, Comment 4 (1981). Such cases are often referred to as "padded payroll" cases.

9. The warrant was payable to the *Grater* Mesilla Valley Sanitation District, while the indorsement was in the name *Greater* Mesilla Valley Sanitation District. 676 F.2d at 1346.

10. N.M. STAT. ANN. § 55-3-405 (1978). The *Western Casualty* court noted that § 3-405 does not specify whether the payee's name and the indorsement must be identical in every respect. 676 F.2d at 1346.

Generally, an indorsement need not match the payee's name exactly. *See* U.C.C. §§ 1-201(39) & Comment 39; 3-401(2) & Comment 2; 3-203 & Comment 3 (1981).

11. Comment 1 to § 3-405 of the U.C.C. states that the instrument must bear "what purports to be a regular chain of indorsements." The *Western Casualty* court explained that the indorsement requirement is to ensure that the check presents a "normal appearance" and that the person negotiating it "can reasonably be identified as the intended payee." 676 F.2d at 1346. *See* Comment, *U.C.C. § 3-405: Of Impostors, Fictitious Payees, and Padded Payrolls*, 47 FORDHAM L. REV. 1083, 1093 (1979).

The Tenth Circuit court noted that a bank would not be protected under § 3-405 if the indorsement name were completely different from that of the payee. 676 F.2d at 1346 n.2.

12. *Id.* at 1347.

13. Much of the controversy is centered on § 3-406 and § 4-406, which allow a negligent drawer to defeat a bank's defense to a forgery by showing that the bank acted negligently. *Id.* at 1347.

Section 3-406 states that a drawer who has contributed to the making of an unauthorized section 3-405 by virtue of section 1-103,[14] which supplements the Code with general "principles of law and equity" unless "displaced by the particular provisions" of the Code.[15] In addition, jurisdictions outside the Tenth Circuit have held that negligence will bar a bank's protection under section 3-405 because of the general requirement of good faith in dealing with negotiable instruments imposed under section 1-203.[16]

The Tenth Circuit held that because Code sections 3-406 and 4-406 explicitly shift the liability for forgeries from bank customers to negligent banks,[17] "the absence of such language in section 3-405 implicitly demonstrates, in our view, an intent to displace common law negligence actions."[18] The court reasoned that the section at issue was conceived as a banker's provision that was intended to narrow the liability of banks while increasing the responsibility of their customers,[19] and that the loss should be placed on the party in the best position to prevent it—the drawer.[20] The Tenth Circuit refused to find that a bank's negligence precludes protection under section 3-405 and affirmed the summary judgment against Western Casualty.

The Tenth Circuit court's holding in *Western Casualty* obviates any obligation of good faith by banks in check forgery cases under section 3-405. Although the policy under this section of placing the burden of loss on the employer in an embezzlement type of situation is sound, such a policy should not diminish a bank's obligation to exercise due care and good faith in paying any check. The New York Supreme Court in a well-reasoned opinion, *Board of Education v. Bankers Trust Co.*,[21] held that the fact the forged indorsements were effective under section 3-405 was not determinative of the bank's liability. The court held that the drawee bank has an obligation to exercise due care and can only charge a customer's account for checks cashed in good faith. "If [the Bank] cashed these checks as a result of its own negligence, and not in good faith, it is liable . . . notwithstanding the effective-

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signature may not assert the lack of authority against a bank "who pays the instrument in good faith and in accordance with . . . reasonable commercial standards." U.C.C. § 3-406 (1981).

Under § 4-406 a customer is allowed recovery against a bank if the customer "establishes lack of ordinary care on the part of the bank in paying the item(s)." U.C.C. § 4-406(3) (1981).

14. Professors White and Summers argue that the standard of care provisions under § 3-406 and § 4-406 should be applicable to prevent a negligent bank from avoiding loss under § 3-405. J. WHITE & R. SUMMERS, HANDBOOK OF THE LAW UNDER THE UNIFORM COMMERCIAL CODE § 16-8, at 638-39 (2d ed. 1980). *See* Sun 'n Sand, Inc. v. United Bank of Cal., 21 Cal. 3d 671, 695, 582 P.2d 920, 937, 148 Cal. Rptr. 329, 346 (1978). The *Western Casualty* court noted that § 3-405 does not explicitly displace the bank's obligation to act with reasonable care, "it simply does not discuss the bank's standard of care." 676 F.2d at 1347.

15. U.C.C. § 1-103 (1981).

16. § 1-203 requires that: "Every contract or duty within this Act imposes an obligation of good faith in its performance or enforcement." The official comment to this section defines good faith as "honesty in fact."

For cases where negligence of the bank barred its use of § 3-405, see Owensboro Nat'l Bank v. Sam Crisp, 78-CA-401-MR (Ky. App. Aug. 31, 1979) (*cited in* U.C.C. DIGEST, 1982 Cum. Supp. No. 1); Board of Educ. v. Bankers Trust Co., 86 Misc. 2d 560, 383 N.Y.S.2d 508 (1976).

17. *See supra* note 13.

18. 676 F.2d at 1348.

19. *Id.* (quoting General Accident Fire & Life Assurance Corp. v. Citizens Fidelity Bank & Trust Co., 519 S.W.2d 817, 819 (Ky. Ct. App. 1975)).

20. *See* U.C.C. § 3-405, Comment 4 (1981).

21. Board of Educ. v. Bankers Trust Co., 86 Misc. 2d 560, 383 N.Y.S.2d 508, 510 (1977).

ness of the endorsements."[22]

A bank's obligation to exercise good faith in accepting, processing, and making payment on its customers' checks, albeit forged, is mandated by section 1-203 of the Code. The bank should not be able to avoid the loss under section 3-405 if it acts negligently in making payment on such a forged check.

B. *A "Lease" as a Secured Transaction*

In *In re Fashion Optical, Ltd.*[23] the Tenth Circuit, interpreting an Oklahoma statute, formulated a four-step *ad hoc* approach to determine whether a purported lease is in reality a secured transaction. The bankruptcy trustee appealed the district court's holding that a transfer of equipment from Fashion Optical, Ltd. (bankrupt) to defendant Dr. Gebetsberger was neither a fraudulent conveyance[24] nor a transfer intended as security, but was a true lease.[25]

The controversy between the trustee and Gebetsberger focused on a purported sale and leaseback of optical equipment. The bankrupt sold Gebetsberger $53,280 of new and used optical equipment for $50,000 in June 1977.[26] The used equipment was valued at $7,265 and in the bankrupt's possession before and after the alleged sale. The remaining $42,375 of equipment was new and had been ordered by the bankrupt from an optical equipment company. The bankrupt's checks in payment were returned for insufficient funds, and Gebetsberger, a business associate and friend of the bankrupt's president, intervened and purchased the equipment directly.[27] The equipment was delivered directly to the bankrupt's offices.

Approximately one week later, Gebetsberger entered into a purported leaseback agreement with the bankrupt. The lease provided for rent of $1,000 per month for sixty months, resulting in a total rental price of $60,000.[28] In addition, the agreement gave the bankrupt a five-year option to purchase the equipment for the greater of ten percent of the original cost or fair market value. Payments were made for thirteen months before Fashion Optical became insolvent.

The trustee in bankruptcy argued that the arrangement was a transfer intended as security[29] rather than a true lease, and thus subject to the filing provisions in Article Nine of the U.C.C. Gebetsberger did not perfect any security interest under the Code.[30] Therefore, the trustee would prevail if the agreement was characterized as an installment sale to the bankrupt with

22. 383 N.Y.S.2d at 511.

23. 653 F.2d 1385 (10th Cir. 1981) (*sub. nom.* Steele v. Gebetsberger).

24. This portion of the decision will not be discussed herein.

25. 653 F.2d at 1386.

26. The bill of sale was dated June 23, 1977. On June 27, 1977, Gebetsberger paid $50,000 cash for the equipment. *Id.*

27. *Id.*

28. *Id.* at 1386-87.

29. OKLA. STAT. ANN. tit. 12A, § 1-201(37) (West 1972).

30. 653 F.2d at 1388.

Gebetsberger retaining a security interest.[31]

Based on Oklahoma's definition of a security interest,[32] the Tenth Circuit adopted a four-step approach to determine whether a lease is in reality a secured transaction. First, the court held that the presence of a purchase option does not automatically preclude a finding of a true lease. Second, if a purchase option allows the lessee to become full owner by "merely paying no or nominal consideration after complying with its terms, the inquiry ends."[33] The lease will be deemed a secured transaction as a matter of law, and thus subject to the provisions of Article Nine. Third, if the option requires greater than nominal consideration for full ownership, a true lease will usually be found.[34] Fourth, the absence of a purchase option will not automatically imply a true lease. Thus, even though the lease does not permit purchase at nominal consideration, it will still be deemed a security interest if the economic realities tend to confirm "a secured transfer of ownership is afoot."[35]

The court was not, however, content to apply only the four-step approach[36] outlined above, but also considered the following factors, which under Oklahoma law tend to indicate a true lease: 1) an option price that is approximately the market value at the time of exercise of the option, 2) rental charges that compensate lessor for loss of value over the term of the lease, 3) nonexcessive rentals and an option purchase price which is not too low, and 4) facts indicating that lessee is acquiring no equity during the term of the lease.[37] The court also considered two additional factors under section 1-201(37)[38] to determine whether a security interest was intended: 1) the percentage that the option purchase price bears to list price,[39] and 2) whether the terms of the lease are such that they strongly favor exercise of

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31. OKLA. STAT. ANN. tit. 12A, § 9-301(1)(b) (West 1972). *See* Bankruptcy Act of 1898, § 70(c) (formerly 11 U.S.C. § 110(c)).

32. OKLA. STAT. ANN. tit. 12A, § 1-201(37) (West 1972) defines a security interest as:

> [A]n interest in personal property or fixtures which secures payment or performance of an obligation. . . . Whether a lease is intended as security is to be determined by the facts of each case; however, (a) the inclusion of an option to purchase does not of itself make the lease one intended for security, and (b) an agreement that upon compliance with the terms of the lease the lessee shall become or has the option to become the owner of the property for no additional consideration or for a nominal consideration does make the lease one intended for security.

33. 653 F.2d at 1388. The court cited the following cases to support this proposition: Percival Constr. Co. v. Miller & Miller Auctioneers, Inc., 532 F.2d 166, 171-72 (10th Cir. 1976), *aff'g* 387 F. Supp. 882 (W.D. Okla. 1973); Citicorp Leasing, Inc. v. Allied Inst. Distrib., Inc., 454 F. Supp. 511, 516 (W.D. Okla. 1977); Dynalectron Corp. v. Jack Richards Aircraft Co., 337 F. Supp. 659, 661 (W.D. Okla. 1972).

34. 653 F.2d at 1389. *See, e.g.*, Crest Inv. Trust, Inc. v. Atlantic Mobile Corp., 252 Md. 286, 250 A.2d 246 (1969).

35. 653 F.2d at 1389. *See, e.g., In re* Brookside Drug Store, Inc., 3 Bankr. 120 (D. Conn. 1980).

36. This approach has been used in other recent decisions to determine whether a lease was in fact a security interest. *See* Towe Farms, Inc. v. Central Iowa Prod. Credit Ass'n, 528 F. Supp. 500, 503 (S.D. Iowa 1981); *In re* Int'l Plastics, Inc., 18 Bankr. 583, 586 (D. Kan. 1982).

37. 653 F.2d at 1389. *See* Percival Const. Co. v. Miller & Miller Auctioneers, Inc., 387 F. Supp. 882, 885 (W.D. Okla. 1973), *aff'd*, 532 F.2d 166 (10th Cir. 1976).

38. OKLA. STAT. ANN. tit. 12A, § 1-201(37) (West 1972).

39. The court noted this factor is especially relevant if the option price is less than 25% of the list price. 653 F.2d at 1389.

the option at the end of the lease term.[40] The lease at issue fixed the option price in terms of fair market value to avoid the inference of a security agreement due to a low option price and favorable option terms.

The Tenth Circuit held that the absence of evidence on the equipment's fair market value and useful economic life was crucial because the facts did not otherwise indicate a security arrangement.[41] A security agreement would be inferred if the market value of the equipment was, at the time for exercise of the option, so low that the option price was nominal consideration under section 1-201(37). Also, the fact that the total rental exceeded the original cost could indicate interest payments in a financed installment sale.[42] Such an excess over original purchase price may not eliminate the finding of a true lease.[43]

The Tenth Circuit held that the inclusion of a fair market value price in an option will not automatically meet the consideration requirement of section 1-201(37), thereby indicating a true sale and lease-back agreement. If there is evidence that the option price of market value is great enough so that the lessee will be paying more than nominal consideration for the item, then a lease will be found.[44] The court remanded the case for a determination under the court's four-pronged approach of whether the purported lease in question is in reality a secured transaction. It is unclear, however, how much weight will be given to the Tenth Circuit's four-step test in light of the court's reliance on a number of additional factors in conjunction with its test. With its *Fashion Optical* opinion, the appellate court has merely added another set of factors, and not a conclusive test, for determining whether a lease is in fact a secured transaction.

II. Limitation of Federal Home Loan Bank Board Authority

In *Otero Savings & Loan Association v. Federal Home Loan Bank Board*[45] a divided Tenth Circuit Court of Appeals held that the Federal Home Loan Bank Board (Bank Board) lacks authority to impose a compensatory "penalty box" remedy in addition to a cease and desist order. The appeal arose from an order[46] of the Bank Board and the Federal Savings and Loan Insurance Corporation (FSLIC) that Otero Savings and Loan Association's (Otero) "Check-In" program violated section 1832(a) of the Federal Deposit Insurance Corporation Act.[47] The order directed Otero to close all checking

40. *Id.*

41. *Id.* at 1390. *See, e.g.*, All-States Leasing Co. v. Ochs, 42 Or. App. 319, 600 P.2d 899 (1974).

42. *See, e.g.*, National Equip. Rental, Ltd. v. Priority Elec. Corp., 435 F. Supp. 236, 239 (E.D.N.Y. 1977).

43. 653 F.2d at 1390. A lease could be found if the equipment depreciated only slightly or in fact appreciated in value over the rental period.

44. The court noted that fair market value could fall to a nominal level, especially toward the latter part of an item's useful economic life, and thereby not meet the consideration requirements of OKLA. STAT. ANN. tit. 12A, § 1-201(37) (West 1972). 653 F.2d at 1390.

45. 665 F.2d 279 (10th Cir. 1981).

46. An administrative proceeding was brought against Otero Savings & Loan Association by the Federal Savings and Loan Insurance Corporation pursuant to 12 U.S.C. § 1730(e) (Supp. IV 1980).

47. 12 U.S.C. § 1832(a) (Supp. IV 1980) (as amended by Depository Institutions Deregula-

accounts held by for-profit corporations and partnerships and to cease offering new customer "Check-In" or related automatic transfer system accounts for a period of 268 days following the effective date of the order.[48] The 268-day penalty was conceived as an equitable offset, since Otero had achieved a competitive advantage by offering "Check-In" accounts 268 days before they were legally permitted.[49] The Bank Board order was stayed pending this decision.[50] Otero argued on appeal that it had not violated section 1832[51] and that the Bank Board and FSLIC had no power to grant the type of relief encompassed by the order.

A. *Factual Background*

In April 1980, Otero, a Colorado state-chartered savings and loan association, began offering a checking account service known as the "Check-In" program.[52] The program was an automatic transfer system of withdrawal under which a customer opened two accounts, an interest-bearing savings account and a non-interest-bearing checking account. When the customer wrote a check, an amount equivalent to the check was automatically transferred from the savings account to the checking account and the check was paid.

However, section 1832[53] prohibited a savings and loan association from offering negotiable order of withdrawal (NOW) accounts before January 1, 1981.[54] NOW accounts are single accounts from which customers may write checks. Both Otero's "Check-In" accounts and NOW accounts were interest-bearing demand deposit accounts. Otero's "Check-In" accounts resulted in more than $10 million in new deposits during the first three months they were offered.[55]

Following an administrative hearing, the Bank Board issued a tempo-

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tion and Monetary Control Act of 1980, Pub. L. No. 96-221, 94 Stat. 132. This section allows all depository institutions to permit withdrawals from interest-bearing accounts, except accounts of for-profit corporations, by negotiable or transferable instruments payable to third parties only after Dec. 31, 1980.

48. 665 F.2d at 281.

49. *Id.* at 287 n.7.

50. Otero Sav. & Loan Ass'n v. Federal Reserve Bank, 665 F.2d 275 (10th Cir. 1981) (grant of preliminary injunction was proper where harm to public and associations if bank stopped processing drafts was much greater than any harm which would be felt by bank). The order granting preliminary injunctive relief appears in Otero Sav. & Loan Ass'n v. Board of Governors, 497 F. Supp. 370 (D. Colo. 1980).

51. 12 U.S.C. § 1832(a) (Supp. IV 1980). *See Otero Sav. & Loan Ass'n*, 665 F.2d at 282 n.2.

52. 665 F.2d at 281; Rocky Mountain News, June 13, 1980, at 134, col. 1.

53. 12 U.S.C. § 1832(a) (1976) provides:

> (a) No depository institution shall allow the owner of a deposit or account on which interest or dividends are paid to make withdrawals by negotiable or transferable instruments for the purpose of making transfers to third parties, except that such withdrawals may be made in the States of Massachusetts, Connecticut, Rhode Island, Maine, Vermont, and New Hampshire.

This provision was amended in 1980, *see supra* note 47.

54. *See* 665 F.2d at 282 n.2.

55. Rocky Mountain News, June 13, 1980, at 134, col. 1. Such accounts were also offered by Majestic Savings and Loan of Denver and Sun Savings and Loan Association of Golden. *Id.*

rary cease and desist order,[56] which imposed the moratorium on opening of any new Check-In-type of accounts. Otero appealed the order on the grounds that its two-account "Check-In" system was not a NOW account system and thus not illegal under section 1832. Otero also questioned the Bank Board's authority to impose the moratorium.

B. *Illegality of "Check-In" Accounts*

The Tenth Circuit appellate panel held that Otero is an insured institution within the meaning of section 1724 of the Savings and Loan Insurance Corporation Act because its accounts are insured by the FSLIC. Therefore it is a depository institution subject to section 1832(a).[57] Otero argued that section 1832(a) prohibits one-account NOW systems prior to January 1, 1981, and not its two-account automatic transfer system.[58] The majority opinion by Judge Logan states that the statutory language of section 1832(a) is broad enough to encompass both types of accounts and that the legislative history of the section indicates that Congress did not intend to differentiate between the two types of accounts.[59] Therefore, section 1832(a) applies to prohibit Otero's "Check-In," automatic transfer system type account during 1980.

C. *Bank Board's Cease and Desist Power*

Otero also contended that the Bank Board did not have the power to enforce section 1832 by a cease and desist order.[60] Otero argued that only those statutes which expressly provide for enforcement by the Bank Board or FSLIC are enforceable by cease and desist orders.[61] Section 1832 contains no express delegation of authority, and in fact, makes no provision for enforcement. A unanimous appellate panel affirmed the power of the Bank Board and FSLIC to use its cease and desist powers[62] to remedy violations of section 1832(a).

The majority opinion rejected Otero's argument that the FSLIC and Bank Board may only enforce those statutes that contain specific delegations of authority. Judge Holloway stated that the specific delegations may have

56. The order was issued pursuant to 12 U.S.C. § 1730(f)(1) (Supp. IV 1980). 665 F.2d at 289 n.9.

57. 12 U.S.C. § 1832(a) (Supp. IV 1980); *see supra* note 53. *Cf.* Wisconsin Bankers Ass'n v. Mutual Sav. & Loan Ass'n of Wis., 96 Wis. 2d 438, 291 N.W.2d 869 (1980) (state-chartered savings and loan, not insured by FSLIC, allowed to use negotiable order of withdrawal accounts under state statute).

58. 665 F.2d at 282.

59. *Id.* at 282-83. Judge McKay's concurrence discussed the legislative history in detail, however, much of the discussion is beyond the scope of this overview. *Id.* at 289-91 (McKay, J., concurring).

60. 665 F.2d at 283.

61. Otero cited the Truth-in-Lending Act, 15 U.S.C. § 1604 (1976); the Electronic Funds Transfer Act, 15 U.S.C. § 1693o(a)(2) (1976); the Debt Collection Practices Act, 15 U.S.C. § 1692l(b)(2) (1976); the Community Reinvestment Act, 12 U.S.C. §§ 2901-2905 (1976); and the Bank Secrecy Act, 31 U.S.C. § 1054(a) (1976) as examples of specific delegations of enforcement authority. 665 F.2d at 284.

62. 12 U.S.C. § 1730(e)(1) (Supp. IV 1980) permits the Bank Board or FSLIC to act where an institution has violated or is about to violate "a law, rule, or regulation."

been included only as clarification of statutes that are enforced by different agencies.[63] The Bank Board relied heavily on a Ninth Circuit Court of Appeals decision[64] holding that the Bank Board has broad authority over federal savings and loans to enforce rules and regulations, regardless of whether Congress had expressly directed the Bank Board to enforce them. In addition, the Tenth Circuit panel emphasized that the Third Circuit[65] had granted the Comptroller of the Currency[66] jurisdiction to enforce compliance with a New Jersey anti-redlining statute by national banks located in that state. The statutory language conferring cease and desist power to the Comptroller[67] is identical to the language of section 1730(e), which confers cease and desist power to the Bank Board against state savings and loan associations.[68]

The Tenth Circuit conceded that Otero, as a state-chartered institution, is not subject to the same "all-encompassing regulation 'from its cradle to its corporate grave' as are federally chartered institutions."[69] Nevertheless, the court concluded that the language of section 1730(e)(1), which refers to violations of "a law," is quite broad.[70] Thus, the appellate panel held that the FSLIC and the Bank Board have power under section 1730(e) to enforce the prohibition of section 1832[71] by use of cease and desist orders.

D. *Bank Board's Remedial Power*

Although the Tenth Circuit panel was in harmony as to the Bank Board's authority to enforce section 1832, the enforcement chosen by the Bank Board created a note of discord. A divided Tenth Circuit court[72] vacated the portions of the Bank Board order that temporarily prohibited Otero from opening any new "Check-In," NOW, or similar types of accounts and from advertising such accounts for 268 days after issuance of the order.[73]

The Bank Board and FSLIC contended that the order was properly based on section 1730(e)(1).[74] The Bank Board took the position that

63. 665 F.2d at 285.

64. Reich v. Webb, 336 F.2d 153 (9th Cir. 1964), *cert. denied*, 380 U.S. 915 (1965).

65. National State Bank v. Long, 630 F.2d 981, 988 (3d Cir. 1980) (Bank Board's authority over federal savings and loan institutions is pursuant to 12 U.S.C. § 1464 (1976)).

66. The Comptroller of the Currency regulates federal banks with cease and desist power under 12 U.S.C. § 1818(b)(1) (1976).

67. *Id.*

68. *Id.* § 1730(e).

69. 665 F.2d at 285 (citing People v. Coast Fed. Sav. & Loan Ass'n, 98 F. Supp. 311 (S.D. Cal. 1951)).

70. 665 F.2d at 286.

71. Depository Institutions Deregulation and Monetary Control Act of 1980, Pub. L. No. 96-221, 94 Stat. 132 (amending scattered sections of 12 U.S.C., including 12 U.S.C. § 1832).

72. Judge Holloway wrote the majority opinion with respect to the validity of the remedial order of the Bank Board, with which Judge McKay concurred, and Judge Logan dissented.

73. 665 F.2d at 286.

74. 12 U.S.C. § 1730(e)(1) (Supp. IV 1980) provides:

> Such order may, by provisions which may be mandatory or otherwise, require the institution or directors, officers, employees, agents, and other persons participating in the conduct of the affairs of such institution to cease and desist from the same, *and further to take affirmative action to correct the conditions resulting from any such violation or practice.*

Id. (emphasis added).

Otero's illegal "jumping of the gun" by offering "Check-In" accounts before they were legally permissible created an unfair advantage over its law-abiding competitors.[75] It was this advantage that the Bank Board's order attempted to remedy.

The Bank Board argued that its remedial powers are equivalent to those of the National Labor Relations Board (NLRB), which has power to redress unfair labor practices by ordering affirmative action to effectuate the policies of the National Labor Relations Act.[76] The Bank Board argued that if the penalty was struck down, Otero "will have succeeded in violating the law with impunity."[77] The order, in pertinent part, stated:

> Due to the length of time inherent in any cease and desist proceeding, Otero's interpretation would mean that a party could violate the existing statute, well in advance of the effective date of amendments, knowing that the cease and desist process could not be brought to bear before the arrival of the effective date. Whatever legislative purpose may have been served in delaying the effective date would, to a large extent, be thwarted.[78]

Otero, however, argued that the FSLIC and Bank Board may only prevent unlawful conduct, take affirmative action to correct conditions resulting from such conduct, and ensure that in the future the institution is law-abiding.[79] Otero contended that the moratorium was beyond the Bank Board's power to prevent illegal conduct because it would prevent Otero from engaging in lawful conduct.[80]

Judge Holloway's majority opinion, relying on legislative history,[81] agreed that the Bank Board's powers are limited. Judge Holloway argued that the Bank Board is permitted to ensure only that institutions operate in a legal, safe, and sound manner. The Board does not have "a mandate to use whatever means seem desirable" to ensure a competitive balance among financial institutions.[82]

Judge Holloway attempted to bolster this holding with several decisions that actually appear to weaken the court's limitation of the Bank Board's power. In *First National Bank of Eden v. Department of the Treasury*,[83] the Comptroller of the Currency determined that a federal bank had engaged in unsafe and unsound practices by paying excessive salaries and bonuses to its executive officers. Based on language identical to section 1730(e), the Comptroller required the bank to limit future personnel expenses and required

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75. 665 F.2d at 287.

76. National Labor Relations Act § 10(c), 29 U.S.C. § 160(c) (1976). The NLRB has authority to require a wide variety of remedies. *See, e.g.*, Virginia Elec. & Power Co. v. NLRB, 319 U.S. 533 (1943) (company union ordered to dissolve); Phelps Dodge Corp. v. NLRB, 313 U.S. 177 (1941) (company required to offer employment to certain persons).

77. 665 F.2d at 288.

78. Decision and Order at 21, *reprinted at* 665 F.2d at 289.

79. 665 F.2d at 287.

80. *Id.* Now, "Check-In," and similar types of accounts became legal after Dec. 31, 1980. 12 U.S.C. § 1832(a) (Supp. IV 1980).

81. S. REP. NO. 1482, 89th Cong., 2d Sess., *reprinted in* 1966 U.S. CODE CONG. & AD. NEWS 3532, 3538.

82. 665 F.2d at 288.

83. 568 F.2d 610 (8th Cir. 1978).

reimbursement of excess bonuses.[84] Judge Holloway's opinion explained that the *First National Bank of Eden*'s penalty "was properly directed to preventing future specified abuses and *reversing the direct, identifiable effects of the past practices* on the bank's financial soundness."[85] It is arguable, however, that the Bank Board's order in *Otero* was properly directed at preventing future abuses and "reversing the direct, identifiable effects of the past practices" of illegally offered "Check-In" accounts.

The Tenth Circuit majority also relied on *Groos National Bank v. Comptroller of the Currency*,[86] in which the Comptroller issued an order prohibiting a bank from making future advances to a controlling shareholder. The bank in *Groos* argued that there was no evidence that such dealings with the shareholder constituted unsafe and unsound banking practices. The *Groos* court upheld the order and stated that when the Comptroller finds a violation, it is within his allowable discretion to fashion relief in order to prevent future abuses of "problematic practices that have occurred in the past."[87] The Tenth Circuit explained that the Comptroller was limited to addressing future identified unlawful practices.[88] Although the Tenth Circuit court drew no distinction between "problematic" and "unlawful" practices, under *Groos* the Comptroller can address broader, problematic practices, and is not limited solely to unlawful abuses.

Judge Holloway's opinion concluded that the Bank Board's cease and desist orders were limited "even if Otero's past actions go unpunished."[89] The Tenth Circuit noted that section 1832(c)[90] permits the Bank Board to assess fines for past violations of section 1832; however, in the instant action no fine was imposed on Otero.[91]

Judge McKay concurred in the limitation of the Bank Board's remedial power and stated that he doubted that Congress had intended to grant the Bank Board authority to impose remedies except against practices which are unsafe or unsound. Judge McKay argued that gaining a competitive advantage in the market is not an unsafe or unsound practice for Otero's financial future.[92]

Judge Logan issued a strong dissent arguing that under section 1730(e)(1), the Bank Board has power to "take affirmative action *to correct the conditions resulting from any such violation or practice*."[93] Although Judge Logan conceded that the Bank Board's grant of power is narrower than that of the NLRB, he argued the Bank Board's power is sufficiently broad to support imposing the moratorium on new accounts.[94] Judge Logan's opinion used the legislative history and cases cited by the majority to lend support to his

84. *Id.* at 611.
85. 665 F.2d at 288 (emphasis added).
86. 573 F.2d 889 (5th Cir. 1978).
87. *Id.* at 897 (emphasis added).
88. *Otero*, 665 F.2d at 288.
89. *Id.* at 289.
90. 12 U.S.C. § 1832(c) (Supp. IV 1980).
91. 665 F.2d at 289 n.9.
92. *Id.* at 291-92 (McKay, J., concurring).
93. 12 U.S.C. § 1730(e)(1) (Supp. IV 1980) (emphasis added).
94. 665 F.2d at 292 (Logan, J., dissenting).

conclusion that the Bank Board had power to remedy the conditions resulting from Otero offering illegal "Check-In" accounts. Judge Logan argued that neither *Bank of Eden* nor *Groos* limit the Bank Board's power to ensure future *legal conduct* by the financial institutions.[95]

In addition, Judge Logan explained that the Bank Board could have ordered Otero to close all new accounts it had wrongfully gained, but the Board had rejected this remedy because of the inherent delays in implementing the order, the inconvenience to Otero's customers, and the danger to Otero's safety and soundness that could result from widespread withdrawals.[96] The Bank Board determined that section 1832(a) was designed by Congress to limit competitive inequality, and the effective date was intended to allow all affected associations "to reach the starting gate" at the same time.[97] Theoretically, if the Bank Board's remedy worked, Otero would be deprived of new accounts equal to those it wrongfully gained.

Judge Logan argued that the moratorium on new accounts could not be considered punitive, as the majority contended, based on the United States Supreme Court test in *Local 60, United Brotherhood of Carpenters v. NLRB*.[98] The Supreme Court considered NLRB orders to be punitive when the orders neither removed the consequences of the violation nor dissipated the effects of the prohibited action.[99] Judge Logan argued that this test was clearly applicable to the Bank Board since it is authorized to take affirmative action to correct conditions resulting from illegal, unsafe, or unsound practices. Under this Supreme Court test, the moratorium is not punitive, Judge Logan asserted, because "it will correct at least partially the effect of the violations."[100]

The well-reasoned dissent in *Otero* argues that deference should be shown to the Bank Board's order,[101] which, while attempting to remedy Otero's head start, also sought to protect Otero's safety and soundness, as well as the innocent account holders.[102] Judge Logan's opinion is strong support for the contention that the Bank Board's remedial powers extend to assessing the moratorium.

The majority opinion, which limits Bank Board authority, was weakly argued and supported, and could create adverse consequences. The limitation of the Bank Board's remedial power could be interpreted as allowing an institution to violate an existing statute, well in advance of the effective date of amendments, with impunity, due to the delays inherent in a cease and desist proceeding. Such an interpretation could thwart the legislative purpose for the amendments, and leave the Bank Board without remedy to correct the conditions resulting from such a violation.

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95. *Id.*
96. *Id.*
97. *Id.*
98. 365 U.S. 651 (1961).
99. *Id.* at 655.
100. *Otero*, 665 F.2d at 293 (Logan, J., dissenting).
101. *See, e.g.*, NLRB v. Gissell Packing Co., 395 U.S. 575, 612 n.32 (1969); Moog Indus., Inc. v. FTC, 355 U.S. 411, 413 (1958).
102. 665 F.2d at 293.

III. BANKRUPTCY

The recent case of *In re Shannon* [103] presented the Tenth Circuit Court of Appeals with the interesting question of what time limitation applies to a notice of appeal during the transition period of the Bankruptcy Reform Act of 1978 (the Reform Act).[104] The Reform Act made extensive changes in the procedures by which appeals are taken from the bankruptcy court.[105] The provisions of the Reform Act become effective on different dates throughout a transition period ending April 1, 1984, at which time the Reform Act becomes fully effective.[106] Section 248 of the Reform Act stipulates a thirty-day deadline for notice of bankruptcy appeals to the circuit courts, however, it is not effective until April 1, 1984,[107] and the Reform Act does not provide any express time for filing bankruptcy appeals to the circuit courts until that date.

In *Shannon*, the plaintiff-appellant, Marian Berg, sought review of a January 12, 1981 order of the United States Bankruptcy Court for the District of Colorado dismissing her objection to the bankruptcy discharge of Jimmie Shannon.[108] Eighteen days later, Berg filed a notice of appeal to the district court, along with a motion to extend the time for filing the notice.[109] The bankruptcy court advised the parties that, by stipulation, an appeal could be taken directly to the court of appeals. On March 10, 1981, a notice of appeal was filed in the Tenth Circuit—nearly two months after the bankruptcy order had been entered.[110]

The Tenth Circuit was concerned with the timeliness of the appeal, and therefore, its jurisdiction to consider the appeal. Under the new Bankruptcy Reform Act, both district courts and courts of appeal share original jurisdiction over appeals from the bankruptcy courts.[111] The amendments to sec-

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103. 670 F.2d 904 (10th Cir. 1982).

104. Pub. L. 95-598, 92 Stat. 2549 (1978) (codified at 11 U.S.C. and scattered sections of 15, 18, and 28 U.S.C.)

105. *Id.*

106. *See* Title IV of the Bankruptcy Reform Act, §§ 401-405, 92 Stat. 2682-85 (1978).

This statement may not be accurate following the recent United States Supreme Court decision in Northern Pipeline Constr. Co. v. Marathon Pipe Line Co., 102 S. Ct. 2858 (1982), which invalidated the broad grant of jurisdiction granted to bankruptcy courts under 28 U.S.C. § 1471(b) (1976 & Supp. IV 1980). Since § 1471 of the Act has been held unconstitutional, the Act may not become fully effective without further legislative amendment.

107. *See* § 405 and § 402 of the Reform Act, 92 Stat. 2682, 2685 (1978).

108. 670 F.2d at 905.

109. The extension of time was granted retroactively to Jan. 30, 1981. 670 F.2d at 905.

110. *Id.*

111. 28 U.S.C. § 1293 (1976) was amended under the new Act to provide:

> (a) The courts of appeals shall have jurisdiction of appeals from all final decisions of panels designated under section 160(a) of this title.
>
> (b) Notwithstanding section 1482 of this title, *a court of appeals shall have jurisdiction of an appeal from* a final judgment, order, or decree of an appellate panel created under section 160 or a District Court of the United States or from a final judgment, order, *or decree of a bankruptcy court of the United States if the parties to such appeal agree to a direct appeal to the court of appeals*.

§ 236(a) of the Reform Act, 92 Stat. 2667 (1978) (emphasis added).

In addition, 28 U.S.C. § 1334 (Supp. IV 1980) states that district courts "shall have jurisdiction of appeals from all final judgments, orders and decrees of bankruptcy courts." § 238(a) of the Reform Act, 92 Stat. 2667-68 (1978).

tions 1293 and 1334 of title 28 of the United States Code[112] make clear that the appeal filed in *Shannon* is within the circuit court's general appellate jurisdiction "so long as it was timely filed."[113]

In general, under section 2107 of title 28 of the United States Code[114] a notice of appeal to the circuit courts must be filed within thirty days after the entry of judgment. However, this section states that it specifically "shall not apply to bankruptcy matters or other proceedings under Title 11."[115] The new Reform Act amended section 2107 to make the thirty-day deadline applicable to bankruptcy appeals after April 1, 1984.[116] This congressional oversight created the dilemma in *Shannon*.

Relying on the Eighth Circuit opinion of *Andrews v. South Dakota Student Loan Assistance Corp.*,[117] the Tenth Circuit held that the thirty-day time period is currently applicable to bankruptcy appeals, and that the failure to refer specifically to section 2107 in the transition period was inadvertent.[118] The court held that the transition provisions of the Reform Act were intended by Congress to make the same jurisdiction and procedures currently applicable as if the new Reform Act were fully effective.[119] Therefore, the Tenth Circuit construed the legislative intent to make the thirty-day time limit effective as of the date the circuit courts acquired jurisdiction over direct appeals from bankruptcy decisions.[120]

The *Shannon* appeal, filed nearly two months after the bankruptcy judgment, was dismissed as untimely. The Tenth Circuit further held that because the appeal was jurisdictionally defective when filed, appellate

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112. 28 U.S.C. §§ 1293, 1334 (1976), *amended by* § 405(c)(1), (2) of the Reform Act, 92 Stat. 2685 (1978), provides, in pertinent part:

> (c)(1) During the transition period, an appeal from a judgment, order, or decree of a United States bankruptcy judge shall be—
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> . . . .
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> (B) if the parties to the appeal agree to a direct appeal to the court of appeals for such circuit, then to such court of appeals;
>
> . . . .
>
> (2) During the transition period, the jurisdiction of the district courts, the courts of appeals, and panels of bankruptcy judges to hear appeals shall be the same as the jurisdiction of such courts and panels granted under the amendments made by sections 236, 237, 238, and 241 of this Act to hear appeals from judgments, orders, and decrees of the bankruptcy courts established under section 201 of this Act.

113. 670 F.2d at 906.

114. 28 U.S.C. § 2107 (1976 & Supp. IV 1980).

115. *Id.*

116. Section 248 of the new Reform Act, 92 Stat. 2672 (1978) amended 28 U.S.C. § 2107 (1976) by striking out the sentence that makes the deadline inapplicable to bankruptcy matters.

117. 636 F.2d 233, 235-36 (8th Cir. 1980).

118. The *Shannon* court held: "We can envision no legislative purpose in making an avenue of appeal available during transition and intentionally omitting the time frame for appeal. We believe the failure to specifically refer to 28 U.S.C. § 2107 in the transition sections of the Act was inadvertent." 670 F.2d at 906. *See In re* Adamo, 619 F.2d 216, 219 (2d Cir.), *cert. denied*, 449 U.S. 843 (1980) (inadvertence in supplying effective date of other sections of the new Reform Act).

119. The court based its interpretation of legislative intent on H.R. REP. No. 595, 95th Cong., 2d Sess. 460, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 5787, 6416. *See In re* Kutner, 656 F.2d 1107 (5th Cir. 1981).

120. 670 F.2d at 907. *See* 28 U.S.C. § 1293 (1976), *amended by* § 236(a) of the Reform Act, 92 Stat. 2667 (1978).

jurisdiction never transferred from the district court.[121]

In re Callister[122] presented the Tenth Circuit court with a second issue involving appellate jurisdiction under the Reform Act over a bankruptcy court order. *Callister* was an appeal from an order of the United States Bankruptcy Court for the District of Utah,[123] which granted creditor Ingersoll-Rand Financial Corporation (IRFC) a "superpriority" and ordered the payment of interim attorney fees awarded to counsel for the debtor and the unsecured creditors' committee.[124] IRFC, which was granted a "superpriority" of $29,868, pursuant to section 507(b) of the Reform Act,[125] appealed the order to the Tenth Circuit alleging that the bankruptcy court erred in awarding interim attorney fees that would be paid in advance of its superpriority.

The *Callister* court agreed with the parties that jurisdiction is conferred on the Tenth Circuit under the new Bankruptcy Reform Act.[126] The Tenth Circuit court noted that there is some confusion regarding the applicability of certain sections of the Reform Act during the transition period;[127] however, the court relied on its holding in *In re Shannon*,[128] that the intent of the Reform Act's transition provisions "make currently effective the same jurisdiction and procedures that will apply to the bankruptcy court system when the [Reform] Act becomes fully effective."[129] Thus, section 1293(b) of title 28 will apply and confer jurisdiction to a court of appeals from a *final* judgment, order, or decree of a bankruptcy court.[130] The issue then is whether an order conferring interim attorney fees is a final order.

Interim awards of compensation, such as the attorney fees in *Callister*, are authorized pursuant to section 331 of the Reform Act.[131] Section 331 allows for repeated application to the court for reimbursement and compensation, and such awards are subject to amendment or modification during the pendency of the bankruptcy proceeding.[132] The Tenth Circuit held that

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121. 670 F.2d at 907. Because the appeal was defective when filed, mandatory dismissal under Interim Bankruptcy Rule 8007 did not become operative and appellate jurisdiction remained in the district court.

122. 673 F.2d 305 (10th Cir. 1982).

123. *In re* Callister, 15 Bankr. 521 (D. Utah 1981).

124. 673 F.2d at 306.

125. 11 U.S.C. § 507(b) (Supp. IV 1980).

126. Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (1978), codified in 28 U.S.C. § 1293(b) (Supp. IV 1980).

127. The transition period runs from Oct. 1, 1979, to Apr. 1, 1984, when the new Act becomes fully effective. 673 F.2d at 306.

128. 670 F.2d 904 (10th Cir. 1982).

129. *Id.* at 906.

130. 28 U.S.C. § 1293(b) (Supp. IV 1980) (emphasis added).

131. 11 U.S.C. § 331 (Supp. IV 1980) provides that:

> A trustee, an examiner, a debtor's attorney, or any professional person . . . may apply to the court not more than once every 120 days after an order for relief in a case under this title, or more often if the court permits, for such compensation for services rendered before the date of such an application of reimbursement of expenses incurred before such date . . . . After notice and a hearing, the court may allow and disburse to such applicant such compensation or reimbursement.

132. *Callister*, 673 F.2d at 306.

such awards are within the court's discretion,[133] and may be re-examined,[134] adjusted and ordered refunded[135] by the court during the course of the case. Since interim awards are not final adjudications on the question of compensation, the appellate panel held that they are interlocutory in nature.[136] Thus, the court concluded it was without jurisdiction under the Reform Act to review interim awards.

The Tenth Circuit Court of Appeals decided a number of divergent issues under the Bankruptcy Act of 1898 (the "Act")[137] in *In re Beery*.[138] The principal issues presented by the bankrupt, Jerome G. Beery, were: 1) whether the bankruptcy court had jurisdiction to convert his Chapter XI reorganization proceeding into a Chapter 7 bankruptcy after the Chapter XI petition was withdrawn, 2) whether bankrupt Beery was a farmer, and 3) whether the bankrupt's fifth amendment rights were infringed by the order of the district court requiring him to testify at a bankruptcy hearing. The Tenth Circuit court found against the bankrupt on all issues.

First, jurisdiction of a Chapter XI proceeding was held not to be lost by the bankruptcy court upon the voluntary withdrawal of the petition.[139] Bankruptcy Rule 11-42(a) prescribes that when a debtor files a motion to dismiss the court should "enter an order after hearing on notice dismissing the case or adjudicating him a bankrupt whichever may be in the best interest of the estate."[140] Although Beery's voluntary withdrawal of his petition was not a motion to dismiss, the court considered it as such.[141] Thus, the bankruptcy court did not lose jurisdiction, and could either dismiss the case or adjudicate Beery a bankrupt. The bankruptcy court chose to adjudicate Beery a bankrupt, but entered its order under rule 11-42(b)(1),[142] instead of rule 11-42(a)(2), with the finding of lack of prosecution. The Tenth Circuit, however, found this to be of no consequence because the "necessary finding that adjudication was in the best interest of the estate was made in any event."[143] In addition, the appellate court found that the basis of lack of prosecution under rule 11-42(b)(1) was clearly satisfied by Beery's refusal to

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133. *See In re* Solar Mfg. Corp., 190 F.2d 273 (3d Cir.), *cert. denied sub nom.* McGird v. Mintz, 342 U.S. 893 (1951).

134. *See* 2 COLLIER ON BANKRUPTCY ¶ 331.03 (L. King 15th ed. 1981).

135. *See In re* Arlan's Dept. Stores, Inc., 462 F. Supp. 1255 (S.D.N.Y. 1978), *aff'd*, 615 F.2d 925 (2d Cir. 1979) (interim award refunded to estate due to misconduct).

136. 673 F.2d at 307.

137. Bankruptcy Act of 1898, codified at 11 U.S.C. §§ 1-1200 (1976), *repealed by* Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549.

138. 680 F.2d 705 (10th Cir.) *cert. denied*, 103 S. Ct. 449 (1982).

139. 680 F.2d at 709.

140. Bankruptcy Rule 11-42(a)(2). This rule applies if the petition was filed, as here, under Rule 11-6. 680 F.2d at 709.

141. *Id.*

142. Bankruptcy Rule 11-42(b) provides:

> The court shall enter an order, after hearing on such notice as it may direct dismissing the case, or adjudicating the debtor a bankrupt if he has not been previously so adjudged, or directing that the bankruptcy case proceed, whichever may be in the best interest of the estate—
>
> (1) for want of prosecution . . . .

143. 680 F.2d at 709. The bankruptcy court based its findings on Beery's admission of his inability to pay his debts and that his liabilities exceeded his assets by more than one million dollars. *Id.* at 709-10.

sign and verify his petitions and schedules.[144] Thus, the bankruptcy judge had jurisdiction to adjudicate Beery a bankrupt and to direct the case to continue as a straight bankruptcy.[145]

The bankrupt's second contention was that he should have been considered a farmer, and therefore, could not have been adjudicated a bankrupt under section 779 of the repealed Bankruptcy Act[146] and Rule 11-42(e). The Bankruptcy Act defines a farmer as one who is personally engaged in farming or tillage of the soil, and who derives the principal portion of his income from farming.[147] Beery's appeal argued that the method used by the bankruptcy court in determining that the principal source of his income was not from farming was erroneous.[148] The bankruptcy court found that based on *gross income* Beery's principal income was from grain and commodities dealings rather than farming.[149] Beery argued, without evidentiary support, that although his grain company had a large cash flow, the profit margin was small.[150] The circuit court, however, held that gross revenues or receipts is the proper standard in determining principal source of income.[151] The court reasoned that in many instances a bankrupt may not have much income from any source.[152] The definition of farmer was clarified in section 101(17) of the Bankruptcy Reform Act of 1978.[153]

Another issue on appeal was whether Beery's fifth amendment rights were violated because of the bankruptcy court order that compelled the bankrupt to testify without a grant of immunity.[154] The Tenth Circuit found section 25(a)(10) of the repealed Bankruptcy Act to be controlling on the issue. Section 25(a)(10) states that the bankrupt shall, at the creditors' meeting and under court order, submit to an examination concerning his business and his bankruptcy. The statute provides that no testimony given by him can be offered into evidence against him in any criminal proceeding.[155]

The statute thus provides immunity against the use of testimony and evidence derived from such testimony, if the testimony was the result of a compulsory court order. Based on testimony derived from the 1977 hearing, the Tenth Circuit found that Beery was clearly ordered to submit to exami-

144. "For want of prosecution" under Rule 11-42(b)(1) includes the failure to file schedules and statements and the withdrawal and abandonment of a plan. *See* Advisory Committee Notes to Rule 11-42.

145. 680 F.2d at 710.

146. 11 U.S.C. § 779 (1976).

147. *Id.* § 1(17).

148. 680 F.2d at 713.

149. *Id.* Beery owned an enterprise known as Brownville Grain Co. that purchased grain from farmers, sold it for cash and then paid the farmers. *Id.* at 715.

150. *Id.* at 717.

151. *Id.* at 714.

152. *Id. See* 1 H. REMINGTON, BANKRUPTCY § 131 (5th ed. 1950).

153. 11 U.S.C. § 101(17) (Supp. IV 1980), defines farmer as a person who, "received more than 80 percent of such person's gross income during the taxable year of such person immediately preceding the taxable year of such person during which the case under this title concerning such person was commenced from a farming operation owned or operated by such person."

154. 680 F.2d at 718.

155. 11 U.S.C. § 25(a)(10) (1976).

nation, and thus, came within the protection of the statute.[156] Therefore, the Tenth Circuit refused to accept Beery's claim that his fifth amendment rights were infringed upon by the order requiring his testimony.[157]

Beery's constitutional privilege was protected by section 25(a)(10) for compelled testimony[158] even though Beery was not expressly granted immunity at the time his answers were compelled. The immunity was independently granted under the statute. The Tenth Circuit court held that no infringement of the bankrupt's fifth amendment rights had been demonstrated.[159]

Although not involved in the *Beery* decision, the Tenth Circuit noted that section 25(a)(10) was repealed under the Reform Act.[160] Under the Bankruptcy Reform Act, in order for a witness to be ordered to testify before a bankruptcy court over the assertion of a fifth amendment privilege, the United States Attorney must request an immunity order from the district court. The witness could be required to testify if immunity were granted. If not, the witness could claim his privilege against self-incrimination.[161]

IV. Case Digests

A. *Assignment of Unearned Insurance Premiums Under the Truth In Lending Act*

In 1980, the Tenth Circuit in *James v. Ford Motor Credit Co.*,[162] and its companion case, *Hernandez v. O'Neal Motors, Inc.*,[163] held that the assignments of unearned automobile damage insurance premiums are not security interests under the Truth In Lending Act (the Act),[164] and do not have to be disclosed by the sellers in the installment contract.[165] The plaintiff-purchasers filed a joint petition for certiorari.[166] While the petition was pending, the United States Supreme Court decided *Anderson Brothers Ford v. Valencia*[167] in accordance with the Tenth Circuit's holdings in *James* and *Hernandez* that an assignment of unearned insurance premiums does not create a security interest under the Act.

The Supreme Court subsequently vacated the Tenth Circuit's *Her-*

156. The appellate court noted that immunity under 11 U.S.C. § 25(a)(10) has not been granted to bankrupts in all bankruptcy proceedings. 680 F.2d at 719. *See, e.g.*, White v. United States, 30 F.2d 590, 592-93 (1st Cir.), *cert. denied*, 279 U.S. 872 (1929) (bankrupt had testified voluntarily).

157. 680 F.2d at 720. *See* 11 U.S.C. § 25(a)(10) (1976); 1A Collier on Bankruptcy ¶ 7.21[1] (J. Moore 14th ed. 1978).

158. The *Beery* court relied on Kastigar v. United States, 406 U.S. 441 (1972). The constitutional problem is discussed further in United States v. Beery, 678 F.2d 856 (10th Cir. 1982).

159. 680 F.2d at 720.

160. *Id.* at 720 n.18. The statute, 11 U.S.C. § 25(a)(10) (1976), was repealed by 11 U.S.C. § 344 (Supp. IV 1980).

161. 11 U.S.C. § 344 (Supp. IV 1980), which applies 18 U.S.C. §§ 6001-6005 (1976 & Supp. IV 1980) to bankruptcy proceedings.

162. 638 F.2d 147 (10th Cir. 1980), *cert. granted*, 453 U.S. 901 (1981).

163. 638 F.2d 153 (10th Cir. 1980), *vacated*, 453 U.S. 901 (1981).

164. 15 U.S.C. § 1601 (1976) as implemented under Regulation Z, 12 C.F.R. § 226 (1982).

165. For a discussion of these cases see Overview, *Commercial Law, Eighth Annual Tenth Circuit Survey*, 59 Den. L.J. 227 (1982).

166. James v. Ford Motor Credit Co., 453 U.S. 901 (1981) (cert. granted).

167. 452 U.S. 205 (1981).

nandez[168] decision insofar as it directed dismissal against the petitioners and remanded on the question of alternative bases for liability against the automobile sellers on the automobile installment contracts that were not considered by the Tenth Circuit Court of Appeals.[169] On remand, the Tenth Circuit in *Brown v. Frontier Ford, Inc.*,[170] found the Supreme Court's directive to consider the issue of alternative bases for liability "puzzling" because that issue had never been presented to the court of appeals and was raised for the first time in the plaintiff-purchasers' petition for rehearing.[171]

The Tenth Circuit deferred to the Supreme Court's holdings that "the requirement of finality is to be practically rather than technically construed."[172] The court remanded the cases back to the district court for further consideration of all issues, including alternative bases of liability, except those based on the question of whether assignments of unearned automobile insurance premiums were security interests.[173]

In the unpublished decision of *Quandelacy v. Wayne Lovelady's Frontier Ford, Inc.*,[174] the Tenth Circuit held it has become "firmly established" that an assignment of returned or unearned premiums for physical damage automobile insurance is not a security interest. Under the Truth in Lending Act, such an assignment is not required to be disclosed on the face of the automobile installment sales contract.[175] The court remanded the case to the district court with directions to dismiss. Thus, the controversy concerning disclosure under the Truth In Lending Act for assignments of unearned insurance premiums in an automobile installment contract appears to be settled in the Tenth Circuit.

B. *Postmaturity Interest Charge Not Within Usury Statute*

In *Smith Machinery, Co., Inc. v. Jenkins*[176] a promissory note that provided for a postmaturity interest rate above the statutory usury limit was held not to be within the purview of the usury statute. Jenkins, the defendant-purchaser, appealed to the Tenth Circuit court claiming that under New Mexico statutes[177] the postmaturity rate was usurious, requiring a forfeiture of

168. Nine cases involving purchaser-plaintiffs suing sellers or lenders under the Truth-in-Lending Act were consolidated with Hernandez v. O'Neal Motors, Inc., 480 F. Supp. 491 (D. N.M. 1979) including petitioners Jackson and Delores Brown, the named plaintiffs in Brown v. Frontier Ford, Inc., 666 F.2d 1291 (10th Cir. 1981) which was remanded to the Tenth Circuit during the period covered by this survey.

169. James v. Ford Motor Credit Co., 453 U.S. 901 (1981).

170. 666 F.2d 1291 (10th Cir. 1981) (the *Hernandez* case was not involved in the Supreme Court remand).

171. *Id.* at 1293.

172. Gillespie v. United States Steel Corp., 379 U.S. 148, 152-53 (1964); Cohen v. Beneficial Indus. Loan Corp., 337 U.S. 541, 545 (1949).

173. 666 F.2d at 1293.

174. No. 80-1452 (10th Cir. Nov. 16, 1981).

175. *See* Anderson Bros. Ford v. Valencia, 452 U.S. 205 (1981).

176. 654 F.2d 693 (10th Cir. 1981).

177. The New Mexico usury statute at issue is as follows:

> *Rates of Interest Allowed-Minimum Charge.*—The interest rate shall be the rate agreed to by the parties, except that [it] shall not exceed ten percent (10%) per annum computed upon unpaid balances for the actual elapsed time during which such balances. . . are unpaid where the evidence of indebtedness is secured by collateral security. . . .

the entire amount of interest charged on the note.[178]

The promissory note at issue required repayment in two annual installments. The note bore an interest rate of ten percent until maturity and a rate of twelve percent after maturity.[179] The maximum interest rate allowed by law at that time was ten percent.[180] Jenkins failed to make the first payment on the note and Smith Machinery brought an action seeking a judgment on the note and court authorization to repossess the collateral.[181] The lower court directed a verdict in favor of Smith Machinery.

The issue on appeal was whether postmaturity interest rates are covered by the usury laws of New Mexico. The Tenth Circuit court followed established case law in its holding that if the usury statute is silent, limitations on interest rates charged do not apply to postmaturity charges.[182] Such postmaturity charges are deemed penalties for nonpayment rather than charges for the use of money and are not subject to usury laws.[183] However, the appellate court noted that such charges may be considered usurious when the usury law limits interest rates that can be applied on the "detention" as well as the use of money.[184] The New Mexico statutes at issue denote consensual agreements between the parties,[185] indicating that a withholding or detention by the borrower that is not consented to by the lender is outside the purview of the usury statute.[186]

The Tenth Circuit held that the mere fact the parties agreed to a postmaturity interest rate will not make the arrangement a "forbearance" of payment subject to the usury statute.[187] The promissory note did not allow Jenkins to defer payment until after maturity. Therefore, the Tenth Circuit court held that the situation was a "detention" of money rather than a "forbearance," and was not covered by the usury statute.[188]

N.M. STAT. ANN. § 50-6-16 (1953).

178. The penalty statute for usury provides that:

> The taking, receiving, reserving or charging a rate of interest greater than that allowed by this act, when knowingly done, shall be deemed a forfeiture of the entire amount of such interest which the note, bill, or other evidence of debt carries with it or which has been agreed to be paid thereon. . . .

Id. § 50-6-18 (1953).

179. 654 F.2d at 694.

180. N.M. STAT. ANN. § 50-6-16 (1953).

181. 654 F.2d at 695.

182. *Id.* at 696.

183. *See, e.g., In re* Tastyeast, Inc., 126 F.2d 879 (3d Cir.), *cert. denied*, 316 U.S. 696 (1942); Scientific Prods. v. Cyto Medical Lab., Inc., 457 F. Supp. 1373 (D. Conn. 1978).

184. 654 F.2d at 696 (citing Ulviden v. Sorhen, 58 S.D. 444, 237 N.W. 565 (1931)).

185. N. M. STAT. ANN. § 56-8-9A (1978) specifies the scope of the usury statutes.

> [N]o person, corporation or association, directly or indirectly, shall take, reserve, receive, or charge any interest, discount, or other advantage for the loan of money or credit *or the forbearance or postponement of the right to receive money or* credit except at the rates permitted in Sections 56-8-1 through 56-8-21 NMSA 1978.

Id. (emphasis added).

186. 654 F.2d at 696.

187. *Id.*

188. *Id. See* Ferguson v. Electric Power Bd., 378 F. Supp. 787 (E.D. Tenn. 1974), *aff'd*, 511 F.2d 1403 (6th Cir. 1975).

The defendant-purchaser also argued that he had paid the debt by delivering a bill of lading for the machinery to a Smith Machinery salesman the evening before trial and, without the company's consent, had placed it with common carrier to be shipped to the company. The

C. *Sale of Repossessed Homes Excluded From Uniform Consumer Credit Code*

In *Circle v. Jim Walter Homes, Inc.*,[189] the Tenth Circuit court held that the sale of repossessed shell homes, financed at annual rates of ten percent or less, are not consumer credit sales subject to the Oklahoma Uniform Consumer Credit Code (UCCC).[190] The appeal involved consolidated class actions brought in federal court under its diversity jurisdiction against Jim Walter Corp. and its subsidiaries.[191] The members of the class were purchasers of defendant's shell homes who contended that the defendant was liable for violations of the Oklahoma UCCC because negotiable instruments were taken as evidence of the purchasers' indebtedness in the sales transactions.[192]

Jim Walter Corp. built shell homes on real properties owned by the purchaser-plaintiffs. The facts indicated that when credit sales were made, negotiable notes were used to evidence the purchasers' indebtedness and mortgages were taken on the real estate to secure the debt. In the event of default, the repossessed homes and accompanying land were sold to new buyers, often also on credit arrangements. The Oklahoma version of the UCCC states that in a consumer credit sale, the seller may not take a negotiable instrument other than a check, as evidence of the obligation of the buyer.[193] A consumer credit sale includes the sale of "goods, services, or an interest in land."[194]

The district court in Oklahoma held that the sales are not consumer sales under the Oklahoma UCCC, and are excluded as sales of an interest in land financed at ten percent or less.[195] The appellant-purchasers argued that this exclusion was inapplicable because the property was sold by a contract for deed whereby, under Oklahoma law, no equitable or legal interest passed until the buyers had fully performed.[196] In addition, the buyers argued that the original sales consisted only of the shell homes, which are "goods" under the UCCC, and would retain that characteristic even though the homes were repossessed and resold along with the underlying land.[197]

Tenth Circuit court held this insufficient proof that Smith Machinery had accepted it in payment of the debt. 654 F.2d at 697.

189. 654 F.2d 688 (10th Cir. 1981).

190. OKLA. STAT. ANN. tit. 14A, § 2-101 (West 1972).

191. 654 F.2d at 689. The res judicata effect of a foreclosure suit followed by a judicial sale was raised on appeal but will not be discussed herein.

192. Although three classes of purchasers were discussed by the trial court, only members of Class I will be discussed herein. The members of Class I were purchasers of the repossessed homes. 654 F.2d at 689-90. *See* OKLA. STAT. ANN. tit. 14A, § 2-104(2)(b) (West 1972).

193. OKLA. STAT. ANN. tit. 14A, § 2-403 (West 1972) provides that: "In a consumer credit sale or consumer lease, other than a sale or lease primarily for an agricultural purpose, *the seller or lessor may not take a negotiable instrument other than a check as evidence of the obligation of the buyer or lessee*." *Id.* (emphasis added).

194. OKLA. STAT. ANN. tit. 14A, § 2-104 (West 1972).

195. The statute, in pertinent part, excludes from the UCCC:

> *[A] sale of an interest in land if the credit service charge does not exceed ten percent (10%) per year* calculated according to the Actuarial Method on the unpaid balances of the amount financed on the assumption that the debt will be paid according to the agreed terms and will not be paid before the end of the agreed term.

OKLA. STAT. ANN. tit. 14A, § 2-104(2)(b) (West 1972) (emphasis added).

196. 654 F.2d at 690.

197. *Id.*

The Tenth Circuit panel affirmed the lower court in holding that the sales by contract for deed were excluded from the UCCC. The appellate court, relying on Tenth Circuit precedent,[198] held that "regardless of when legal title to land passes, the land is deemed to have been 'purchased' upon the execution of a binding contract for deed."[199] Oklahoma statutes are in accord with this finding.[200] In addition, the official comment to section 104 of the UCCC[201] explains that the ten percent interest rate exclusion was intended to exclude home mortgages from UCCC coverage, while retaining UCCC coverage of the higher interest rate, smaller type of real estate loans.[202]

The appellant-purchasers' argument that the shell homes were "goods" under the UCCC despite being resold with the underlying property was easily dismissed by the Tenth Circuit court based on the general property law rule that a building erected upon a tract of land becomes part of the land.[203] Thus, the sale of repossessed homes in transactions involving annual finance charges of ten percent or less are excluded from the UCCC under Oklahoma law.

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198. First Nat'l Bank & Trust Co. v. United States, 462 F.2d 908, 910 (10th Cir. 1972) (court rejected the Internal Revenue Service's argument that no "purchase" occurred until deed was delivered after full performance in contract for deed sale).

199. 654 F.2d at 690.

200. OKLA. STAT. ANN. tit. 14A, § 2-105(b) (West 1972) (sale of an interest in land includes lease with option to purchase).

201. OKLA. STAT. ANN. tit. § 2-104(2)(b) (West 1972).

202. 654 F.2d at 690.

203. *Id.* at 691. *See* Shelton v. Jones, 66 Okla. 83, 167 P. 458, 460 (1917); Mid-State Homes, Inc. v. Martin, 465 P.2d 791 (Okla. Ct. App. 1969).