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Evidence of Side Agreement Between Lender and Borrower Not Admissible to Show Modification of Loan Agreement

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ute's consideration exception, N.Y. Gen. Oblig. Law 9-103(2)(b) (McKinney 1988). Under the consideration exception, if Biomass gave Larini permission to ride a snowmobile along the access road in exchange for some form of consideration, Biomass would be liable to Larini for his injuries. The Larinis urged the court to accept an "indirect consideration" theory as a basis for applying the exception. Under such a theory, the Larinis argued that since Larini was a potential purchaser of a lot in the subdivision, Biomass anticipated receiving consideration from him.

The court refused to apply the consideration exception to the Larinis, noting that no New York court had ever found any form of indirect consideration sufficient to satisfy the exception. In addition to consideration, the exception expressly required the injured party to demonstrate that he had permission to use the landowner's recreational property. Larini admitted that he did not have express or even implied permission to enter the property without a real estate agent or a Biomass representative or to ride a snowmobile on the property. Therefore, the court noted that even if it adopted the "indirect consideration" theory, the Larinis' argument would fail.

Willful Or Malicious Conduct Exception

The Larinis then alleged that Biomass was liable under the willful or malicious conduct exception, N.Y. Gen. Oblig. Law § 9-103(2)(a) (McKinney 1988), due to its failure to erect guardrails and warnings around the drop-off leading to the drainage ditch and stream bed. The exception imposed liability upon the landowner for willful or malicious failure to guard or warn against a dangerous condition. The court rejected this argument as well. The Larinis failed to prove that Biomass intentionally and unreasonably failed to issue warnings regarding an obvious risk. The court noted that the road on which Larini travelled posed no danger to those who used it for its usual and ordinary purpose; Biomass could not reasonably be required to mark off-road obstacles.

Common Law Liability

Finally, the Larinis argued that the common law liability of a landlord applied in this case. The Larinis argued that Biomass was liable under the reasonable care standard because Biomass could have reasonably expected the public to enter the property and to sustain injury because of the nature of the hidden drop-off.

The court rejected the Larinis' application of the common law duty of reasonable care. The court noted that in situations covered by the recreational use statute, the statute's standard of willful or malicious conduct constituted the single standard applicable.

Finding no genuine issue of material fact with respect to the Larinis' claim, the court affirmed the district court's grant of summary judgment in favor of Biomass.

Rosemary G. Milew

Evidence of Side Agreement Between Lender and Borrower Not Admissible To Show Modification of Loan Agreement

In *Hall v. Federal Deposit Ins. Corp.*, 920 F.2d 334 (6th Cir. 1990), the Sixth Circuit Court of Appeals held that the *D'Oench* doctrine barred an action by a borrower against a failed savings and loan association for breach of a loan agreement. The *D'Oench* doctrine protected the Federal Deposit Insurance Corporation (the "FDIC") by excluding evidence of secret agreements modifying loan agreements made between the failed lending institution and its former customers.

Background

R. Vance Burkey and M.D. Kelly ("Burkey and Kelly") owned B & K Enterprises, Inc. ("B & K"), a corporation which constructed a motel in Knoxville, Tennessee. In order to finance the motel's construction, Burkey and Kelly obtained a $1,000,000 loan from United American Bank of Knoxville ("UAB"); UAB took a first priority lien in the motel units. B & K subsequently defaulted on the UAB loan and advertised the units for sale. Lillian H. Hall and William L. Hall ("the Halls") and Brenda C. Gibson and Wallace G. Gibson ("the Gibsons") answered the advertisement. Burkey and Kelly, the Halls, and the Gibsons formed the Jackson, Tennessee Motel Partnership ("the partnership") and agreed to obtain another loan to pay off the UAB debt and move the motel to Jackson, Tennessee.

In January 1983, the Halls and the Gibsons entered into a loan agreement with Commerce Federal Savings and Loan Association, Inc. ("Commerce") which provided that Commerce would lend them $1.85 million in exchange for a first priority security interest in the motel units. Burkey and Kelly served as guarantors on the loan.

The partnership allegedly believed UAB would also be involved in the new loan with Commerce. Commerce and UAB had agreed that UAB would participate in the Commerce loan, a fact confirmed in a letter signed by the two lenders. However, the two lenders had not entered a formal participation agreement at the time the partnership closed the loan with Commerce. The loan agreement between the partnership and Commerce stated that Commerce would not be obligated to fund more than $750,000 if UAB failed to participate in the loan agreement. At the closing with Commerce, the partnership signed a security agreement which gave Commerce a security interest in all personal property and gave Commerce an interest in the motel land through execution of a deed of trust in favor of Commerce. Commerce then disbursed $200,000.00 to the partnership as a first draw on the loan.

In February 1983, Commerce refused to fund the loan further because the partnership had failed to give Commerce a first priority lien on the units, in accordance with the loan agreement. The partnership stopped construction on the motel. Unpaid subcontractors

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Side Agreement

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sued the partnership and obtained liens on the motel property.

Shortly thereafter, the Commissioner of Banking for the State of Tennessee closed UAB. The FDIC was appointed as the receiver. UAB retained its first priority security interest in the units until September 1985, when the FDIC subordinated the UAB security interest to Jackson National Bank ("Jackson"). In October 1985, the partnership obtained a loan from Jackson to complete the motel and to pay outstanding debts, including the balance owed to Commerce. In August 1986, Commerce was also placed in receivership.

In April 1987, the partnership sued Commerce for breach of the loan agreement. The partnership claimed that Commerce failed to fund fully the $1.85 million loan. In August 1988, the Federal Savings and Loan Insurance Corporation (the "FSLIC") became the receiver for Commerce. Security Trust Federal Savings and Loan Association ("Security Trust") acquired most of Commerce's assets and liabilities from the FSLIC. The assignment agreement, signed in conjunction with the acquisition agreement, expressly stated that the FSLIC, and not Security Trust, would assume any liability resulting from the partnership's lawsuit.

District Court Proceedings

The district court granted Security Trust's motion to dismiss it as a party because the assignment expressly exempted Security Trust from any liability in the partnership's lawsuit. The court concluded that FSLIC was the real party in interest.

The district court also granted summary judgment to the FSLIC, concluding that the partnership's suit was barred by *D'Oench, Duhme & Co. v. Federal Deposit Insurance Corporation,* 315 U.S. 447, 62 S.Ct. 676 (1942), which precluded a party from using any secret agreements which may misrepresent a bank's assets to banking authorities as a defense to fulfilling a financial obligation to a bank. The partnership argued that Commerce's $200,000 initial disbursement at the closing demonstrated that the partnership had satisfactorily complied with the terms of their agreement with Commerce; through this payment, Commerce allegedly waived the loan agreement provision requiring the partnership to give Commerce a first priority lien in the motel units. The lower court allowed the FSLIC to invoke *D'Oench* as a defense to admission of any side agreement between the partnership and Commerce which might alter the terms of the original loan agreement. Subsequently, the court found that even if Commerce waived the priority condition in the loan agreement, Commerce's records did not reflect the waiver, nor did the FSLIC demonstrate that it knew of Commerce's waiver. Because an unwritten waiver would deceive banking authorities, the district court held that *D'Oench* was a complete defense to the partnership's breach of contract claim.

The Sixth Circuit Affirms

The U.S. Court of Appeals for the Sixth Circuit first addressed whether Security Trust was properly dismissed as a defendant. The partnership argued that because it did not agree to release Security Trust from liability, Security Trust could not assign this liability to the FSLIC. The court found that the FSLIC acted within its statutory authority under § 1729(f)(2)(A) in assuming liability from the partnership's lawsuit. 12 U.S.C. § 1729(f)(2)(A) (1989). In addition, the acquisition agreement provided that Security Trust would acquire "substantially all" of Commerce's assets and liabilities, thus permitting Security Trust to select which assets and liabilities it would acquire. Therefore, the court of appeals held that the district court properly dismissed Security Trust as a defendant.

The Sixth Circuit then considered whether the district court properly granted summary judgment in favor of the FSLIC. The *D'Oench* doctrine protected the FDIC and the FSLIC from misrepresentations regarding the assets of federally insured banks by excluding any evidence of secret agreements that tend to deceive banking authorities. The court noted that the *D'Oench* doctrine had been only partially codified at 12 U.S.C. § 1823(e) (1989). According to the court, section 1823(e) provided that "no agreement that tends to diminish the FDIC's interest in an asset acquired from an insolvent bank is valid unless the agreement is in writing, was executed by the bank and the obligor, was approved by the bank's board of directors, and has been made a part of the bank's official records." *Hall,* 920 F.2d at 338.

The partnership claimed that the language of § 1823(e) restricted the *D'Oench* doctrine to cases where the FDIC or the FSLIC had acquired an interest in an asset. The partnership argued, because they paid back the $200,000 initial disbursement before Commerce fell into receivership, Commerce did not own any "asset" when the FSLIC assumed Commerce's assets and liabilities; thus, the doctrine did not apply to the partnership's claim.

The Sixth Circuit disagreed, noting that the *D'Oench* doctrine was broader than § 1823(e). The court admitted that in most of the cases applying the *D'Oench* doctrine, the FDIC did have an interest in an asset because the FDIC was attempting to collect on a note it had acquired. In addition, the court stated that the *D'Oench* doctrine was designed to allow banking authorities to determine the specific value of bank assets and liabilities; to further its purpose, the doctrine applied even if the FDIC did not have an interest in an asset.

The court, however, found that Commerce did have an interest in an asset. Although the partnership paid off the $200,000 obligation, this amount represented only a fraction of the total amount of the loan agreement. The court determined that when the FSLIC was appointed receiver of Commerce, the FSLIC gained an interest in all of Commerce's outstanding obligations, including the partnership's outstanding loan agreement. Both the partnership and Commerce

possessed a continuing interest in the entire amount of the loan agreement. The court noted that in the absence of such a continuing interest, the partnership would not have a valid contract claim. The FSLIC, therefore, had standing to assert the *D'Oench* defense.

Finally, the court concluded that the *D'Oench* doctrine also applied in suits brought by and against the FSLIC. The court noted that if the doctrine did not apply, a borrower could circumvent the policy behind the doctrine by asserting the claim as a counterclaim rather than as an affirmative defense. In the present case, the loan agreement did not incorporate a release by UAB of its priority or evidence of a formal participation agreement between UAB and Commerce. The court held that because the partnership's breach of contract action depended on a side agreement not included in the written agreement between the parties, the action must be dismissed.

Dissent

In his dissenting opinion, Judge Jones claimed that the *D'Oench* doctrine applied only if the FDIC or the FSLIC acquired an interest in an asset from a failed bank. Because the partnership had repaid the $200,000 initial disbursement, Judge Jones asserted that the FDIC did not acquire an interest in an asset. Therefore, he concluded that the FSLIC could not use the *D'Oench* doctrine to bar the partnership's suit.

Suzi Guemmer

Federal Bankruptcy Code Does Not Preempt State and Local Utility Termination Procedures

In ***Robinson v. Michigan Consolidated Gas Co., Inc.,*** 918 F.2d 579 (6th Cir. 1990), the United States Court of Appeals for the Sixth Circuit held that federal bankruptcy law does not preempt state or local laws governing utility termination procedures. Further, the court held that Michigan law barred a claim of liability for utility termination against the bankruptcy trustee because the trustee had acted pursuant to a court order.

Background

Five tenants (the "tenants") resided in an apartment building in Detroit managed by Woodward East Management and Rental Company ("Woodward"). As a result of Woodward's failure to pay its gas bills, Michigan Consolidated Gas Co. ("MichCon"), discontinued gas service to the building's heating facility and, with other creditors, then filed a Chapter 7 involuntary bankruptcy petition against Woodward.

The bankruptcy court appointed David Allard ("Allard") as interim trustee to operate Woodward's business and directed the tenants to pay their rent to him. The court ordered Allard to arrange with MichCon for gas service to the building's heating facility and to pay for the service from the building's rental income. The order entitled MichCon to terminate service for nonpayment after a five day notice to the court and interested parties. Six months later, MichCon filed notice that it would terminate service to the building, as Allard was delinquent in his payments to MichCon; MichCon then in fact discontinued service. MichCon had not notified any of the tenants prior to the termination, although it served notice on Woodward and its creditors.

The tenants then filed a complaint in Wayne County Circuit Court against Allard and MichCon, alleging violations of state and local law governing termination of utility service. Specifically, the tenants first alleged that MichCon discontinued service without providing proper notice as required by the Detroit Code. Detroit Code §§ 56-4-1-56-4-35. In addition, the tenants asserted that Allard was responsible for the termination, and by failing to pay for the gas he violated city and state laws. The tenants asked the court to order Allard to provide heat and hot water and to pay future gas bills. Further, the tenants sought an injunction requiring MichCon to restore gas service for heat and hot water and preventing MichCon from terminating service, except as provided under the city ordinance. The circuit court refused to act on the case while it was pending in the bankruptcy court.

Allard and MichCon removed the case to the United States District Court for the Eastern District of Michigan and moved for summary judgment. The tenants moved to amend their complaint in order to assert additional state and municipal claims against Allard and also to remand. The district court granted Allard and MichCon their motions for summary judgment and deemed moot the tenants' motions to remand and to amend. The tenants appealed.

Sixth Circuit Opinion

After finding that the district court had proper jurisdiction in this case, the Sixth Circuit reviewed the law of preemption. In granting summary judgment for MichCon, the district court had held that the utility termination provisions of the federal bankruptcy statute, 11 U.S.C. § 366(b) (1989), preempted the Detroit Code provisions, Detroit Code §§ 56-4-21-56-4-35, because the local procedures frustrated the effectiveness of the federal bankruptcy law. First, MichCon contended that the federal law explicitly preempted state and local laws. Second, even in the absence of express preemption, MichCon asserted, the federal law implicitly preempted the state and local laws because the federal courts have exclusive jurisdiction over debtors' property under the jurisdiction statute of the Bankruptcy Code, 28 U.S.C. § 1334 (1989).

The Sixth Circuit, however, found neither argument persuasive. The court found that a federal law would preempt a state law under certain circumstances which included those where there was a clear expression of congressional intent to preempt state law or an actual conflict between federal and state law.

The Detroit Code directed a utility not only to notify tenants of a proposed discontinuation of ser-

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