

No. A05-0634

**STATE OF MINNESOTA
IN COURT OF APPEALS**

Lisa L. Bradley, Trustee for the Sally G.
Moore and Robert A. Moore Revocable Living Trust,

Appellant,

v.

First National Bank of Walker, N.A.,

Respondent.

**REPLY BRIEF OF APPELLANT
LISA L. BRADLEY**

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¹ In most cases reference in this Reply Brief to one of the uniform acts is also a reference to the corresponding Minnesota statutory provision. Where this is not the case, the context makes it apparent.

A. Factual Matters

Respondent's discussion of the facts of the case contains various statements that require correction in some instances, and clarification in others. While some of the matters alluded to by Respondent have no bearing on the issues raised in the appeal, it is still important to set the record straight.

For example, the heading appearing on page 5 of Respondent's Brief asserts that "First National's Check Processing Is Fully Automated." As noted in Appellant's Brief (at pages 7-8), Respondent's check processing software isolates "large items," *i.e.*, items in the amount of \$2,500 or greater. Thus, of the 81 checks Glenn Smith wrote to himself over a period of 25 months, at least 74 would have been identified on the "Large Item Report" that is generated on a daily basis and reviewed by a bank officer, and each of the checks was subject to actual physical inspection and inquiry by bank employees. Respondent admits that processing personnel did raise questions about some of these checks with Bank Officers, and that they were told to simply pay the items.

Respondent asserts (at page 6) that Lisa Bradley, after Sally G. Moore designated her as "successor trustee," was then "empowered to conduct transactions on behalf of the Trust." By way of clarification, it is important to understand that, under the Trust documents, a successor trustee did not actually become a trustee until Sally G. Moore died. *See generally* the Trust instruments, Respondent's Appendix at pages 78-109, especially page 102, Article V (E). Hence, Lisa Bradley was not "empowered" to do anything as a trustee until that time.

In another part of its Brief (at pages 8-10), contrary to the admonition in the rules to present the facts fairly and with complete candor, and apparently in an attempt to deflect attention from Respondent's own conduct, Respondent devotes three pages to the task of trying to establish that Lisa Bradley "ceded her responsibilities as a Trustee to Smith" (page 8). Suffice it to say that Appellant objects to and disagrees with the characterization. However, since the assertions have no connection whatsoever with the issues on appeal, Appellant's response in this Reply Brief will be limited to noting that Appellant denies that she "ceded" responsibilities to Mr. Smith and that she asserts that her actions as Trustee were appropriate.

B. UCC §3-307(b) Does Not Apply

Clearly the major point of dispute between the parties is the issue of whether Section 8 of the Uniform Fiduciaries Act (UFA) (Minn. Stat. §520.08 (2004)) controls the resolution of the case or whether UCC §3-307(b) (Minn. Stat. §336.3-307(b) (2004)) controls.

Another way of looking at that issue is to ask the following question: Prior to the enactment of the Uniform Commercial Code in Minnesota, and the associated repeal of Section 6 of the Uniform Fiduciaries Act (UFA) (Minn. Stat. §520.06) (and replacement of that section by UCC §336.3-307), would the determination of the issue be controlled by UFA Section 6 or by Section 8?

To assist in making that determination the following table compares the language of the three statutory provisions (emphasis added and party designations added):

Minn. Stat. §520.08 (UFA Section 8)	Minn. Stat. §520.06 (UFA Section 6) (repealed by UCC)	Minn. Stat. §336.3-307(b) (UCC §3-307(b))
<p>If a check is drawn upon the account of the principal [the Trust] in a bank [Respondent] by a fiduciary [Glenn Smith], . . . the bank [Respondent] is authorized to pay such check without being liable to the principal [the Trust] [absent actual knowledge or bad faith].</p>	<p>If a check . . . is drawn by a fiduciary [Glenn Smith] as such, . . . payable to the fiduciary [Glenn Smith] personally, . . . and is thereafter transferred by the fiduciary [Glenn Smith], . . . the transferee [Americana Bank or Excel Bank] is not bound to inquire whether the fiduciary [Glenn Smith] is committing a breach of his obligation as fiduciary in transferring the instrument [absent actual knowledge or bad faith].</p>	<p>If (i) an instrument is taken from a fiduciary [Glenn Smith] for payment or collection or for value, (ii) the taker [Americana Bank or Excel Bank] has knowledge of the fiduciary status of the fiduciary, and (iii) the represented person [the Trust] makes a claim to the instrument or its proceeds on the basis that the transaction of the fiduciary [Glenn Smith] is a breach of fiduciary duty, the following rules apply:</p> <p style="text-align: center;">* * *</p> <p>(3) If an instrument is issued by . . . the fiduciary [Glenn Smith] as such, and made payable to the fiduciary personally, the taker [Americana Bank or Excel Bank] does not have notice of the breach of fiduciary duty unless the taker [Americana Bank or Excel Bank] knows of the breach of fiduciary duty.</p>

When the issue is viewed in that context, it is obvious that **only Section 8 of the UFA** (Minn. Stat. §520.08) addresses the question of the liability of the payor bank (except in the limited circumstance – not present in this case – where the payor bank is

also the depository bank, *i.e.*, the first bank to take an item – *see* discussion in Appellant’s Brief at pages 21-23). The provisions of UCC §3-307(b) address the liability of the **taker**² of the check (in this case, Americana Bank or Excel Bank), not the payor bank, and do not apply in this case.

Interestingly, at the district court level Respondent premised its UCC argument solely on the assertion that Respondent Bank was the “depository bank” (see discussion in Appellant’s Brief at pages 21-23). Respondent appears to concede the error of this argument on appeal by not even discussing it (Americana Bank and Excel Bank were the depository banks). Instead, apparently by way of a fallback position, Respondent now excerpts one sentence from the official comment to UCC §3-307 to claim that Respondent is, under these facts, a “payor bank” and, therefore, UCC §3-307 controls together with the UCC statute of limitations (Respondent’s Brief at pages 16-17). This argument also fails.

UCC §3-307(b) by its own terms applies “if an instrument is taken from a fiduciary for payment or collection or for value.” Thus, where the instrument is taken from the fiduciary and the bank gives value to the payee/fiduciary (by accepting the

² Although the UCC repeatedly uses the terms “taker” and “takes,” it does not define those terms. It appears that the drafters of the UCC were satisfied to recognize the obvious: a taker is one who takes an instrument. A review of the authorities seems to validate that observation. *See generally* JAMES J. WHITE & ROBERT S. SUMMERS, UNIFORM COMMERCIAL CODE (5th ed. 2000); WILLIAM D. HAWKLAND & LARY LAWRENCE, UNIFORM COMMERCIAL CODE SERVICE (1999); LARY LAWRENCE, LAWRENCE'S ANDERSON ON THE UNIFORM COMMERCIAL CODE (3rd ed. 2000). It is noteworthy that the White and Summers treatise, in discussing the applicability of UCC §3-307, states: “In a state that has adopted the Uniform Fiduciaries’ Act, that law confers a separate course [cause?] of action on the aggrieved party.” J. WHITE & R. SUMMERS, *supra*, §16-5 at p. 599.

instrument for deposit or cashing the instrument), that bank is the “taker” of the instrument. The comment to UCC §3-307 recognizes the circumstance where the “taker” and the “payor bank” are one and the same and states that, when “an instrument is presented for payment to a *payor bank that pays the instrument by giving value to the fiduciary*” (emphasis added), this section applies. The comment does not add an additional category of “payor bank” to the statutory language; it only explains that the statutory language *may include* the circumstance where the taker is also the payor bank – not present in this case.

This principle is illustrated by the case of *Hellig Trust v. First Interstate Bank of Washington*, 93 Wash. App. 514, 969 P.2d 1082 (Wash. App. 1998). *Hellig* involved embezzlement from a trust over a period of years in which 98 percent of all transactions involved checks drawn on Interstate Bank and deposited into the trustee’s personal account at Interstate Bank. 93 Wash. App. at 516, 969 P.2d at 1083. Since terms of the comment were met (“an instrument is presented for payment to a payor bank that pays the instrument by giving value to the fiduciary”), the court held that UCC §3-307 was applicable. 93 Wash. App. at 517-18, 969 P.2d at 1084. UCC §3-307 does **not** apply in this case for that very reason – the checks were deposited at Americana Bank and Excel Bank, not at Respondent Bank.

Respondent ignores the fact that the checks (instruments) payable to the fiduciary (Glenn Smith) were *not taken* from the fiduciary by Respondent Bank for payment or collection for value. Almost all of the checks were taken from the fiduciary by Americana Bank or Excel Bank (the district court so noted in its Memorandum

accompanying its Order; A. 85). It follows that, since UCC §3-307 does not apply to the case at hand, the corresponding UCC statute of limitations is likewise not applicable.

C. The Applicability of Cases Cited by Appellant

Respondent asserts in its heading on page 17 of its Brief: “The cases cited by [Appellant] do not support her argument.” Citing *Appley v. West*, 832 F.2d 1021 (7th Cir. 1987), Respondent further asserts that *Appley* “does not even address the conflict between the Act and Code’s statutes of limitations.”

The *Appley* court states in its opinion:

In her appeal, [Appellant] argues that she sufficiently alleged a cause of action against Republic Bank for negligence amounting to bad faith . . . that is not displaced by UCC §3-419 [conversion on a forged instrument] and that it is not governed by the statute of limitations in UCC §4-406.

Id., 832 F.2d at 1030. The opinion goes on to address the applicability of the Illinois version of the Uniform Fiduciaries Act, stating (832 F.2d at 1031):

The UFA . . . allows a cause of action when the bank has actual knowledge of the fiduciary’s misappropriation of the principal’s funds or when the bank has knowledge of sufficient facts that its action in paying the checks amounts to bad faith.

The Seventh Circuit decision reversed the trial court’s summary judgment order and held that the UCC did not preempt application of the Uniform Fiduciaries Act, that the UCC did not abolish claims based on negligence where there is no specific provision in the UCC that would supercede a negligence claim, and that the shorter UCC statute of limitations was not applicable. It is difficult to understand the basis of Respondent’s assertion that *Appley* “does not even address the conflict between the Act and Code’s

statutes of limitations.”³

Respondent also asserts (Brief at pages 17-18) that the case of *Chouteau Auto Mart, Inc. v. First Bank of Missouri*, 148 S.W.3d 17 (Mo. App. 2004), *rev. denied* (Mo. Sept. 28 and Nov. 23, 2004), is not relevant to this case. *Chouteau* involved claims against a bank related to embezzled funds, assertions by the bank in that case that UCC §3-307 applied and that the statute of limitations of UCC §3-118(g) controlled, and conflicting assertions by the plaintiff that the Uniform Fiduciaries Act applied and that the general five-year statute of limitations controlled. There the Missouri Court of Appeals affirmed summary judgment in favor of the plaintiff and rejected the bank’s claim that the UCC sections controlled, holding instead that the Uniform Fiduciaries Act and the general statute of limitations applied, all of which is directly relevant to this appeal.

Notably, Respondent fails to cite any cases from any jurisdiction supporting its position that UCC §3-307 and the statute of limitations of UCC §3-118(g) apply to the exclusion of the Uniform Fiduciaries Act and the general six-year statute of limitations. Respondent is asking this Court to be the first and only court in the country to so hold, contrary to specific holdings in other states.

D. The Negligence and Breach of Contract Claims

For all the same reasons that Respondent’s arguments fail related to the UCC/UFA “conflict,” its arguments (Brief at pages 18-20) that Plaintiff’s negligence and contract

³ The Minnesota Supreme Court has held that great weight will be given to other states’ interpretations of a uniform law. *See* Appellant’s Brief at page 24.

claims have been displaced by the UCC also must fail.

This is for one fundamental reason: For all the reasons discussed above, UCC §3-307 simply does not apply to this case. It applies to “takers” of instruments. Respondent Bank is **not** a taker of the checks that Glenn Smith wrote to himself. Americana Bank and Excel Bank were takers; Respondent was not. For all the cases cited by Respondent in this section of its Brief, not one of them has analogous facts. Not one of them involves a claim against a payor bank that is not a taker of the items involved in the claim.

Accordingly, as stated in Appellant’s main Brief (at pages 24-25), since the claims of negligence and breach of contract do not “conflict with the UCC,” the UCC does not “prevent application” of those common law theories.

CONCLUSION

Respondent has built its entire argument on the foundational premise that UCC §3-307 applies to this case. At the district court level it relied on language from the official comment to that section that it applied to a “depository bank that takes the instrument for collection.” After it was demonstrated that Respondent is not a “depository bank” (the first bank to take an item), Respondent now quotes a different sentence from the comment that says the section applies to a “payor bank that pays the instruments by giving value to the fiduciary.” However, while Respondent was indeed the “payor bank,” it ignores the obvious fact that it did not pay “the instruments by giving value to the fiduciary” (Excel Bank and Americana Bank did; Respondent did not).

All the rest of Respondent’s arguments are built on that one foundation. Clearly that foundation provides no support. Respondent’s arguments must, therefore, inevitably

fall in a heap.

Section 8 of the Uniform Fiduciaries Act (Minn. Stat. §520.08 (2004)) does control, and thus the general six-year statute of limitations applies to this case. Therefore, the judgment of the district court must be reversed and the case remanded for trial.

Respectfully submitted,

July 20, 2005

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