COMMERCIAL LENDING ALERT

LENDER LIABILITY CLAIM REJECTED BY MISSOURI COURT

August 2007

Lender Liability Claims

Borrowers and guarantors often raise "lender liability" claims as a defense to suits for payment of loans. These claims typically include an assertion that the lender fraudulently induced the borrower or the guarantor to enter into a loan or a guaranty by misrepresentations such as "Don't worry, we never call guarantees." Some other lender liability claims, at their core, could be characterized as "You should never have loaned me the money because you knew I could not pay it back." These claims peaked in the early 1990's. Missouri courts joined in this trend in 1994, in a case in which the Missouri Court of Appeals upheld a judgment of in excess of $80,000,000 against a lender who refused to fund a loan commitment to a company that was never profitable and eventually ended up in bankruptcy. Anuhco v. Westinghouse Credit Corp., 883 S.W.2d 910 (Mo. App. W.D. 1994).

New Case - Facts and Outcome

A Missouri appellate court recently made it clear that at least one form of lender liability claim will not protect a borrower or guarantor against loan repayment obligations. In LPP Mortgage, LTD. v. Marcin, Inc., 224 S.W.3d.50 (MO. App. W.D. 2007), the maker and guarantors of notes (obligors) contacted the owner of the notes (who purchased them after the notes were already in default) and initiated settlement discussions. As one might expect, the owner requested extensive personal and corporate financial information from the obligors, who complied with those requests.

After a year of negotiations, the obligors offered the owner a lump-sum payment of roughly $50,000 to settle the claim, which at the time had a face value of $700,000. As expected, the owner rejected the offer and the obligors responded with an offer to pay $100,000 spread over 30 years. Four months after that offer and without any further communications between the parties, the owner published a notice of foreclosure on the real property that served as collateral for the notes.

Upon learning of the publication, the obligors contacted the owner, who decided to refrain from pursuing the foreclosure if the obligors would make a better settlement offer. Further settlement negotiations ensued which were unsuccessful, and the owner filed suit against the obligors on the notes.

In response to the suit, the obligors asserted the familiar defense of fraud based upon alleged misrepresentations by the notes holder's predecessor. Adding a new wrinkle, the obligors also filed a counterclaim for "prima facie tort." The trial court directed a verdict in favor of the owner and rejected the claim of fraud, but the court allowed the claim of prima facie tort to go to the jury, which found in favor of the obligors and awarded $700,000 in compensatory and punitive damages.

On appeal, the Missouri Court of Appeals reversed the trial court and held that, as a matter of law, the obligors did not make a case of prima facie tort that could be submitted to a jury and therefore reversed the $700,000 judgment.

Prima Facie Tort

In order to make a submissible case of prima facie tort, the claimant must establish:

- An intentional action by the defendant;
- Defendant's intent to injure the plaintiff by such action;
- Resultant injury to plaintiff; and
- An absence of or insufficient justification for defendant's act.

The appellate court held in essence that, even if the first three criteria were met, the obligors failed to establish that the owner had an absence of or insufficient justification for its act. The act complained of was the filing of a notice of foreclosure after several months of fruitless negotiation during which no reasonable settlement offer was presented. According to the appellate court:

- At the time the owner published notice of foreclosure, obligors had been in default on the notes for roughly five years;
- Under the deed of trust and under Missouri statutes, the owner had a right to pursue non-judicial foreclosure (which is commenced by filing of notice); and
- The notes provided that, upon default, the owner had the power to sell the collateral at public or private sale.

The court held that the notice of foreclosure conformed with statutory requirements and that the owner was justified to foreclose in order to protect the owner's valid business interests.

The court also held that the owner's actions before and after the publication, including requesting extensive financial information and publishing notice without first rejecting an inadequate second settlement offer, did not negate its justification for commencing foreclosure.

Lender-Friendly Missouri Courts

This decision reinforces current Missouri case law that continues to be friendly to the commercial lender by refusing claims that are used as a justification for escaping agreed-upon obligations. This approach by the Missouri courts, coupled with the state's updated no-oral-loan-agreement statute (last revised in 2004 to eliminate fraudulent inducement and similar tort claims), the enforceability in Missouri of jury trial waivers and one-way arbitration, and the purely subjective "good-faith" test (not requiring proof that good faith actions were also taken reasonably) adopted by the Missouri courts, provide commercial lenders with the prospect that their agreements, freely entered into, will be enforced by the Missouri courts as written. For that reason, to the extent there is a relationship between a lender, a lending transaction or a borrower and the state of Missouri, a lender should consider taking advantage of Missouri's lender-friendly laws and court decisions by requiring that Missouri law govern the transaction and that jurisdiction of the Missouri courts be selected if any dispute arises.

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